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## SECTOR POLICIES AND ECONOMIC PERFORMANCE IN THE ASEAN REGION

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## ABSTRACT

The economic development performance of the Philippines compared to that of the other countries of ASEAN has been poor. Explanations are sought by comparisons with three other ASEAN countries: Indonesia, Malaysia, and Thailand. The disappointing Philippine performance does not appear to be due to a bias against the agriculture sector per se. A more likely explanation comes from the prolonged tendency of Philippine development policies to focus on domestic market protection rather than on gaining international market competitiveness.

A detailed comparison of the agricultural, industrial, trade and exchange rate policies practiced by the four ASEAN countries is undertaken to show that agricultural policies were similar among the four. There was a common tendency by all governments to intervene in both food and export crop markets. Each promoted often contradictory policy objectives such as low domestic consumer prices, self-sufficiency, and increased rural incomes.

While all four countries engaged in some form of import-substitution strategy, the Philippines relied most heavily on its domestic market to foster the growth of its industrial sector. Trade and exchange rate instruments were used aggressively in the Philippine case to protect the domestic market against import competition. These policies led to a high rate of resource transfer out of agriculture and into the rest of the economy in the Philippines.

Although the anti-agricultural bias is sometimes blamed for the disappointing economic performance of the Philippines, the more damaging longrun impact of the protectionist trade and exchange rate policies in the Philippines was to weaken the international competitiveness of Philippine products. Compared to other ASEAN countries, the Philippines in comparison to the other ASEAN countries, was less able to take advantage of the phenomenal post-war growth of the international economy that contributed to the high rates of economic growth in the region.

## EXECUTIVE SUMMARY

The disappointing performance of the Philippine economy, especially when compared to the more encouraging economic growth of several other ASEAN countries, begs for explanation. One widely held view is that it is the Philippine bias for industrial growth rather than agricultural growth that has held back its economic development. While this view is not without merit, the policy prescription it suggests, namely, that the Philippines should place a greater emphasis on the agricultural sector, is misleading. There is considerable evidence that the problem is not agriculture versus industry, but that slow growth has resulted from a practice of protecting domestic economic interests rather than encouraging them to become internationally competitive. This protectionist approach has not only caused resources to flow out of agriculture and into industry, but more importantly, repressed the growth of both sectors and the economy as a whole. By comparing the broad outlines of the development approaches taken by the four larger ASEAN countries (i.e., Indonesia, Malaysia, Philippines, and Thailand) through the past four decades, the impact of their specific agricultural, industrial, trade and exchange rate policies can be examined in some detail.

Statistically, the Philippine economic growth has been substantially slower than that of the other three ASEAN countries. The Philippines has had a lower rate of GNP growth, especially in the past two decades, and its average annual GNP/capita income growth from 1965-1989 has been less than half of the rate registered by the other three countries. Moreover, a decomposition of this aggregate economic growth into growth by production sectors, shows that it has been the poor performance of the industrial sector that has held the economy back.

Historically, the Philippines have tended to favor a domestically driven economic growth approach. Malaysia, the only country in this ASEAN group with a favorable legacy towards more international and market-oriented development policies, was able to maintain a high level of openness and market-orientedness despite its vigorous pursuit of income redistribution goals. Indonesia, after suffering from Sukarno's inward-looking and anti-market policies in the early 1960's, managed to avoid a prolonged commitment to heavy government intervention in the economy. Thailand, because of its historical legacy of political pragmatism, has also been able to avoid a drawn-out commitment to interventionistic policies. Unfortunately, the Philippines by succeeding somewhat with its early import-substitution industrialization strategy, has found it difficult to emerge from interventionistic development policies.

In agricultural policies, there was a common tendency, even in Malaysia, to promote political objectives by intervening in agricultural commodity markets. Intervention in the Philippine case was no more intense or extreme. However, in industrial promotion, the Philippines depended more heavily and for a longer period of time on domestic market intervention instruments, especially the undervaluation of the foreign exchange rate and the use of import restrictions.

In all four countries the price of rice, a common major crop and staple food, has been subjected to control measures. In efforts to diversify the export base as well as raise government revenues, dominant agricultural exports have also been subjected to substantial taxation in all four countries. Agricultural development policies in all countries focused on direct government

investment expenditures for rural infrastructure and technological upgrading through government agricultural research and extension programs. Of the four countries, the Malaysian government appears to have used its resources most effectively in support of agriculturally oriented development programs.

In the area of industrial protection, all countries underwent an early import-substitution phase implemented through trade protection measures. Malaysia and Thailand, however, were always reluctant to engage in widespread protection because of their perception that such policies gave undue advantage to their ethnic Chinese minority and thus aggravated the sensitive racial issues. Indonesia also held back from extending heavy protection because of its painful experience with Sukarno's trade and market control policies. The Philippines ended up with the longest and most severe form of trade protection to promote industrial development. It was first implemented through quantitative restrictions in the 1950's and then by prohibitive tariffs in the 1960's and 1970's.

The anti-trade bias of Philippine policies were made more severe by the chronic overvaluation of its domestic currency. Malaysia and Thailand, by virtue of their strong comparative advantage in agricultural exports and traditional fiscal conservatism, have enjoyed relatively stable foreign exchange rates. Indonesia, again because of the memory of their disastrous experience with Sukarno's policies, has not hesitated to adjust their foreign exchange rate periodically in response to accumulated exchange rate misalignments.

In the Philippines, however domestic currency overvaluation brought about by adverse international terms of trade changes and domestic fiscal expansionism have always been met by increased trade restrictiveness rather than timely exchange rate adjustments. The result has been a case of chronic foreign exchange overvaluation.

These historical comparisons support the view that it was the Philippines reliance on domestic market protection as opposed to gaining international competitiveness which explains the slower economic growth in the Philippines. Among the more important economic development implications suggested by these findings are the following:

1. Heavy state economic intervention represses economic growth. The quick collapse of the Indonesian economy under Sukarno is a radical case in point. The Philippine's lingering economic malaise is a milder but chronic case protectionism.

2. Liberal economic policies stimulate economic expansion. The recent case of Thailand in the latter half of the 1980's is a dramatic demonstration of this, while Malaysia's consistent impressive growth is the longterm proof of it.

3. The government can vigorously pursue political agendas without being overly intrusive of private enterprise. Malaysia's committed pursuit of economic parity for the Malays has not substantially reduced Malaysia's degree of economic openness nor its market-orientedness in the region.

4. The economic role of government is in the provision of goods and services where the private sector fails or is initially incapable of doing so. Malaysia, the least interventionistic case, also devoted substantial government expenditures on rural infrastructures and in improving the production techniques of its agricultural producers.

5. The evidence suggests that increasing trade restrictions as a way of handling foreign exchange imbalances should be avoided. It not only hides the more fundamental causes of these foreign exchange imbalances, such as fiscal and monetary mismanagements, but also negativeiy affects the economy's longterm ability to compete internationally.

The lessons from ASEAN's history of economic development supports Gillis' (1983) prescription for a successful development approach: macro liberalization with micro "dirigisme". The evidence from the ASEAN countries suggests that the best prescription for sustained growth is a relatively open economy with government activity limited to carefully selected strategic interventions.

## SECTOR POLICIES AND ECONOMIC PERFORMANCE IN THE ASEAN REGION

Drawing conclusions about agricultural policies of ASEAN countries and economic development is a difficult task.[1] It is often their similarities rather than their differences in development performance and policy approach that draws attention, especially in comparative studies. However, the striking contrast between the Philippines' poor economic performance relative to the other ASEAN countries provides a unique opportunity to examine the relationship between development policies, and the growth of the economy as a whole.

The findings of the study suggest that it was not the development bias against agriculture per se that led to poorer economic performance in the Philippines. Rather, it was the relatively anti-trade bias of Philippine development policies. A review of ASEAN development experiences shows that taxation of agriculture and subsidization of industry were not unique nor more pervasive than in the Philippine case. Furthermore, the design and objectives of policies specific to agriculture were quite similar among the four countries. Diversification of agricultural exports, as well as cheaper domestic food supplies, were commonly sought agricultural intervention objectives.

What clearly sets the Philippine development experience apart was its more pervasive and enduring structure of disincentives against external trade. Industrial protection and import substitution not only slowed the growth of agriculture in the Philippines, but even worse, it stunted the growth of the Philippine industrial sector itself. While industrial import protection made locally manufactured goods more competitive at home, it made all Philippine goods less competitive abroad. The Philippines, therefore, was not able to take good advantage of international trade as an engine of economic growth during a period when the international economy was expanding rapidly.

The first section is a statistical comparison of the economic growth of these four countries. Its purpose is to show that Philippine economic growth and structural transformation have been markedly lagging in the region. Section 2.0 compares broad development policy regimes, revealing that more liberal and outward-oriented policy regimes have generally performed better. The next section looks at agricultural policies and their effects on agricultural production incentives. It shows no clear difference between Philippine policies and policies in the other countries. Section 4.0 compares industrial protection and exchange rate policies, revealing greater bias against trade in the Philippines. The last section is a summary of findings and conclusions.

[1] ASEAN is composed of the Philippines, Brunei, Indonesia, Malaysia, Singapore, and Thailand. For comparative purposes, ASEAN will be used in the discussion to refer only to the four larger countries (i.e., excluding Singapore and Brunei).

# 1. COMPARISON OF ECONOMIC GROWTH PERFORMANCES

Table 1.1. 1989 Aggregate Characteristics

| | Population (Millions) | Area (Mil. Ha.) | GNP (Bil. US $) | Land/Capita (Hectares) | GNP/Capita (US $) |
|---|---|---|---|---|---|
| Philippines | 60.0 | 30.0 | 42.6 | 0.50 | 710 |
| Indonesia | 178.2 | 190.5 | 89.1 | 1.07 | 500 |
| Malaysia | 17.4 | 33.0 | 37.6 | 1.90 | 2,160 |
| Thailand | 55.4 | 51.3 | 67.6 | 0.93 | 1,220 |

Source: World Bank, World Development Report 1990, 1991.

The Philippines is the second most populous country in ASEAN, but only the fourth largest in terms of land size. It has the lowest land-to-capita ratio among the four countries, but its gross national product (GNP) per capita ranks third as of 1989, above that of Indonesia (Table 1.1). This aggregate measure of economic welfare, however, has been growing much faster in the other three countries. If the 1965-88 GNP per capita growth trends (Table 1.2) continue, the Philippines will have the lowest per capita income in the region by the year 2002.

Table 1.2. 1965-89 Average Annual Growth Rates (Percent)

| | Population | GNP | GNP/Capita |
|---|---|---|---|
| Philippines | 2.7 | 4.3 | 1.6 |
| Indonesia | 2.2 | 6.6 | 4.4 |
| Malaysia | 2.6 | 6.6 | 4.0 |
| Thailand | 2.5 | 6.7 | 4.2 |

Source: GNP/capita growth rates are from World Bank, World Development Report 1990; population growth rates computed from the United Nations population estimates for 1965, and World Bank estimates for 1989; GNP growth rates residually computed from GNP/capita and population growth estimates. All are real growth rates.

This lag in per capita income growth is not due only to the Philippines' higher rate of population growth but, more importantly, is caused by its slower rate of growth in economic production (e.g., GNP). In the 1950's (Table 1.3), the Philippines was actually the fastest growing economy in the region. But by the 1960's, the economies of Malaysia and Thailand were growing much faster. A decade later, even Indonesia's economy was also growing faster.

Table 1.3. GDP Annual Growth Rates (Percent)

| | 1950-60 | 1960-70 | 1970-80 | 1980-89 |
|---|---|---|---|---|
| Philippines | 6.3 | 5.1 | 6.3 | 0.7 |
| Indonesia | 5.2 | 3.9 | 7.6 | 5.3 |
| Malaysia | 2.6 | 6.5 | 7.8 | 4.9 |
| Thailand | 5.6 | 8.4 | 7.2 | 7.0 |

Source: All data, except those for 1950-60, are from the World Bank's World Development Report, 1982 and 1991. Data for 1950-60 taken from Castro, Jurado, and Mariano (1975) for the Philippines; Mangkusuwondo (1975) for Indonesia; Arudsothy (1975) for Malaysia; and the United Nation's Yearbook of National Accounts Statistics (various issues from 1955 to 1964) for Thailand. Data are all real growth rates.

The 1980's provided further indication of the Philippines' economically weak position in the region, as its economy virtually stagnated while the other three countries registered annual gross domestic product (GDP) growth rates above 4.5 percentage points.[2]

Another indication of the Philippines' poor development performance, in comparison to the three other ASEAN countries, can be seen in the trend of agriculture's share of the GDP (Table 1.4). This share usually declines as a country's per capita income increases (Chenery and Syrquin, 1977). It showed a consistent downward trend in Indonesia, Malaysia, and Thailand. However, since the 1960's, the decline in the relative share of agriculture. It appears to have stalled, if not reversed, in the Philippines. The Philippines was the first in the region to diversify its economic base and shift away from a dependency on agriculture (Tan Tat Wai, 1990). It now has the highest agricultural share of GDP in the region.[3]

[2] The Philippine economy actually shrank by a yearly average of a percentage point from 1984-87 (World Bank, 1990). It must be noted that this economic collapse was triggered by a political shock, the assassination of former Senator Benigno Aquino. However, studies of the Philippines economic policies for this period (e.g., Montes, 1987) blame longstanding structural policy defects as the root cause of this failure. Some studies prior to the assassination, like Bello (1982), had been predicting this eventual collapse based on the weaknesses of the debt-led growth strategy of the Marcos government.

[3] The Philippines has also had difficulty in substantially reducing its employment dependency on agriculture (Table 1.4). Agriculture remains the main source of employment, employing at least half of the labor force in all the countries except Malaysia.

Table 1.4. Sectoral Indicators (Percent)

| | 1950-60[a] | 1960-70 | 1970-80 | 1980-89 |
|---|---|---|---|---|
| PHILIPPINES | | | | |
| Agric. Share in GDP | 34.0 | 26[b] | 27.3 | 27.0 |
| % Labor in Agric. | 59.0[c] | 57.8[d] | 52.8 | 50.7 |
| Annual Growth of VA: | | | | |
| Agriculture | 5.1 | 4.3 | 4.9 | 2.0 |
| Manufacturing | 9.9 | 6.7 | 7.2 | 0.5 |
| Services | 7.2 | 5.2 | 5.4 | 1.2 |
| INDONESIA | | | | |
| Agric. Share in GDP | 55.6 | 56[b] | 29.3 | 24.0 |
| % Labor in Agric. | - | - | 62.0 | 56.0[e] |
| Annual Growth of VA: | | | | |
| Agriculture | 4.6 | 2.7 | 3.8 | 3.2 |
| Industry/Mfg. | 10.6 | 3.3 | 12.8 | 12.7 |
| Services/Others | 5.0 | 4.8 | 9.2 | 6.6 |
| MALAYSIA | | | | |
| Agric. Share in GDP | 40.2 | 28[b] | 29.9 | 23.9 |
| % Labor in Agric. | 58.6[f] | 55.1[g] | 47.5 | 32.8 |
| Annual Growth of VA: | | | | |
| Agriculture | 2.9 | 4.4 | 5.1 | 3.9 |
| Industry/Mfg. | 4.6 | 8.8 | 11.8 | 7.5 |
| Services/Others | 5.3 | 5.7 | 8.2 | 3.9 |
| THAILAND | | | | |
| Agric. Share in GDP | 43.3 | 32[b] | 24.5 | 19.2[b] |
| % Labor in Agric. | - | 79.8[h] | 72.0 | 69.3[i] |
| Annual Growth of VA: | | | | |
| Agriculture | 3.2 | 5.6 | 4.7 | 4.1 |
| Industry/Mfg. | 4.9 | 11.4 | 10.6 | 8.1 |
| Services/Others | 6.2 | 9.1 | 7.3 | 7.4 |

Source: Data for 1960-88, unless otherwise indicated, are from various issues of the World Bank's World Development Report, various years. The 1950's data, unless otherwise indicated, are from Castro, Jurado, and Mariano (1974) for the Philippines; Mangkusuwondo (1975) for Indonesia; and the U.N.'s Yearbook of National Accounts Statistics for Malaysia and Thailand. Data for percent of labor in agriculture in the 1970's and 1980's are from Arya (1990) and the Asian Development Bank's (ADB) Asian Development Outlook 1990. Agriculture includes crop production, livestock, and fisheries; manufacturing does not include mining or construction; services include retail and wholesale trade.

Notes:
[a] 1950's data for Indonesia are only for 1951-57; 1955-60 for Malaysia; 1951-60 for Thailand.
[b] 1965 only
[c] 1956 only
[d] 1964-66 only
[e] 1980-86 only.
[f] 1957 only (Arudsothy 1975)
[g] 1965 only (Arudsothy 1975)
[h] 1966 only (Chomchai 1974)
[i] 1980-86 only.

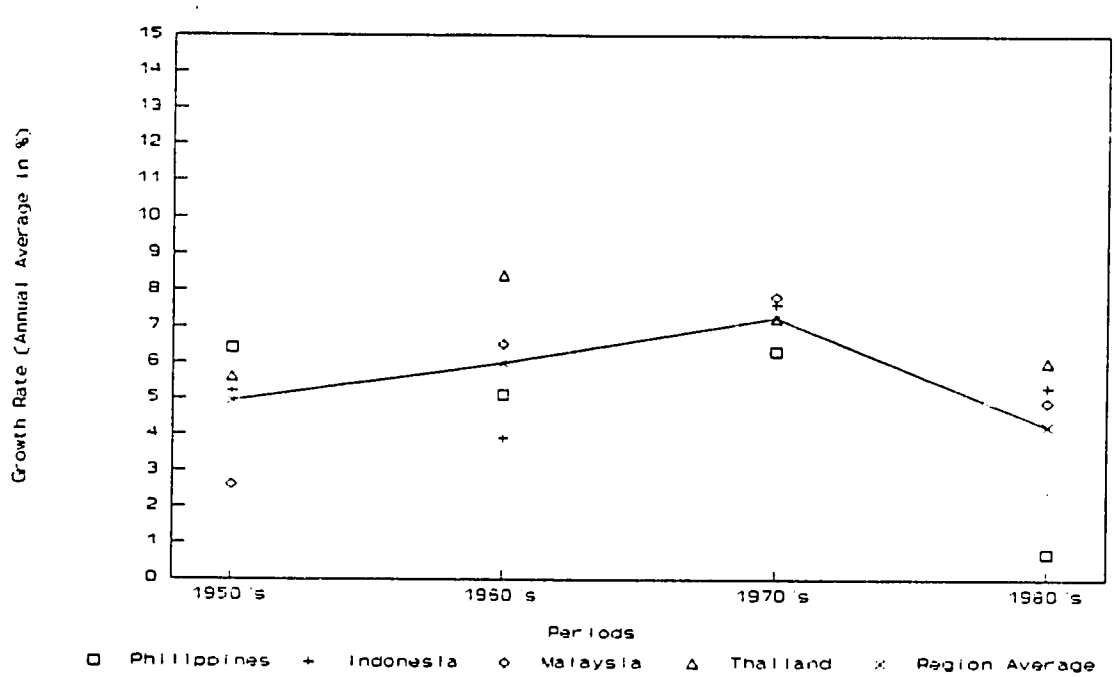


*Figure 1.1. GDP Growth*

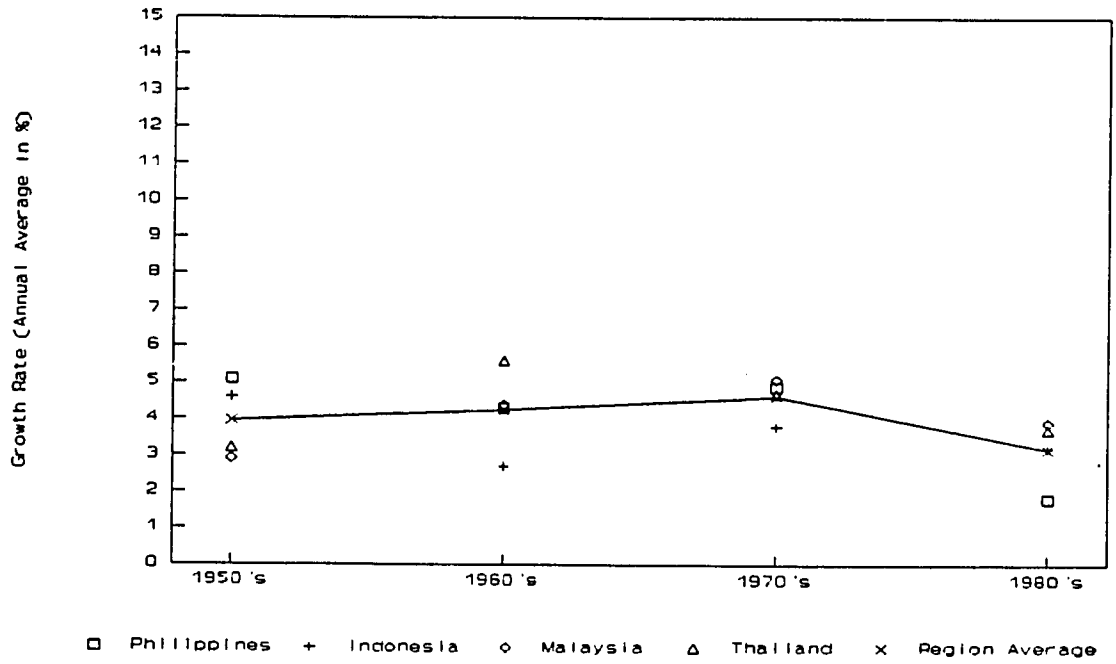


*Figure 1.2. Agricultural Value-Added Growth*

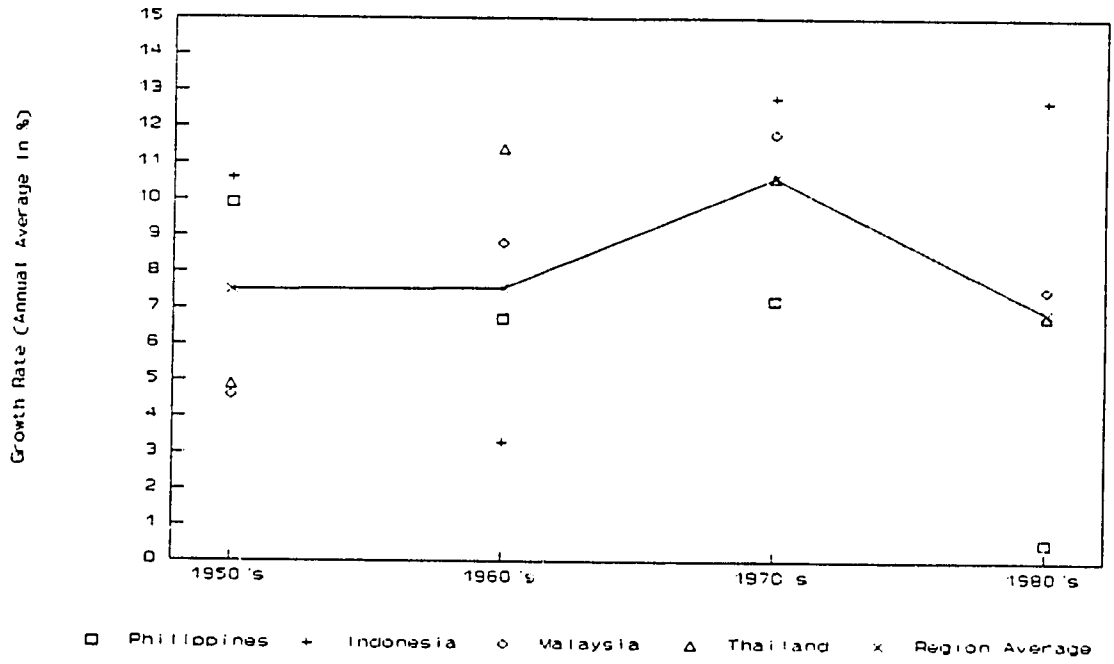


*Figure 1.3. Manufacturing Value-Added Growth*

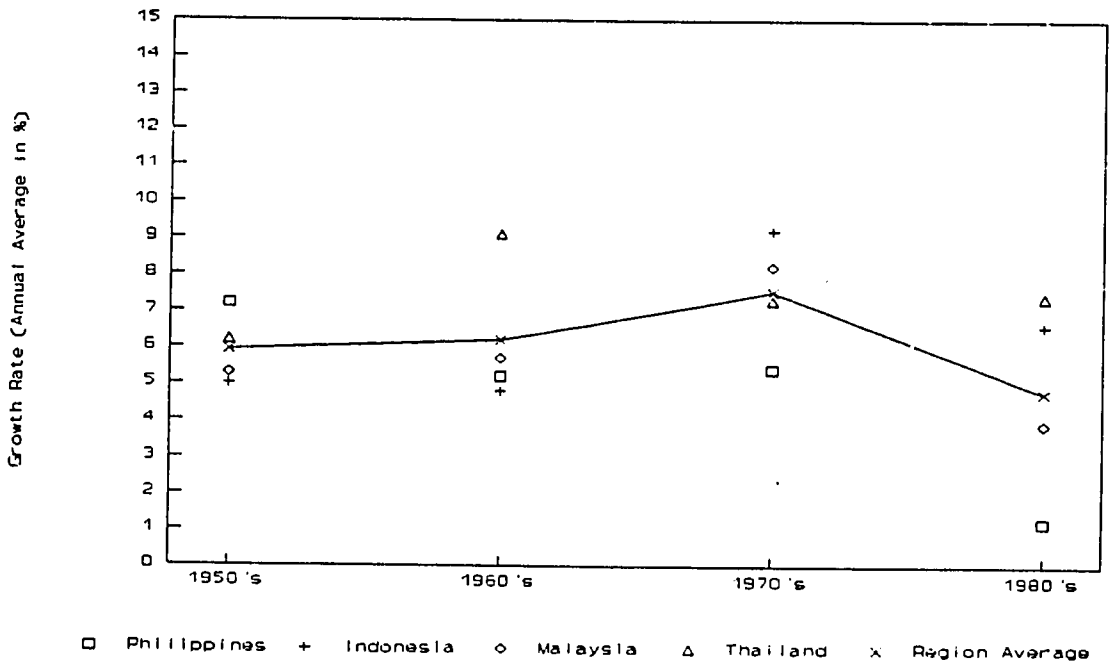


*Figure 1.4 Services Value-Added Growth*

Figure 1.1, Figure 1.2, Figure 1.3, and Figure 1.4 compare the annual growth averages of each country's GDP, agriculture's value-added, manufacturing's value-added, and services' value-added to their corresponding unweighted regional averages.[4] Regional averages show that growth rates were generally increasing until the 1980's, when the international economy's slowdown brought them back down to the level of the 1950's. The growth rates of manufacturing and services sectors accelerated their upward trend between the 1960's and the 1970's, a period when prices and demand for the region's commodity exports rose. Agriculture's growth rate, although positive, continued the pattern established in prior periods. The figures also show that the difference in GDP growth rates between Indonesia, Malaysia, and Thailand has narrowed, and all are substantially above that of the Philippines's. Agriculture's growth performance has been less variable across countries, than manufacturing and services sectors which have exhibited a good deal of variance.[5] Philippine manufacturing and services growth rates have been pulling down the regional averages since the 1970's.

The figures suggest that the Philippines' slower rate of economic growth and greater difficulty in decreasing economic dependence away from agriculture are due to the poor performance of its manufacturing sector.[6] The driving sectors of large open economies are its agricultural and industrial (e.g., manufacturing) sectors. The services sector, with little tradability, can only depend on the two other sectors for its own growth momentum. The growth of agriculture's contribution to value-added in the Philippines does not compare badly relative to its growth performance in the other countries. When the Philippine economy faltered in the mid-1980's, only the agricultural sector managed to register a positive rate of growth in production. Manufacturing, however, has fared badly relative to the regional average since the 1960's.

[4] Data for the graphs are from Table 1.4. All variables are in real terms.

[5] If Indonesia was not included in the comparison during the 1960's, a period that includes years of Sukarno's excesses, then this manufacturing performance lag would have started in the 1960's.

[6] This is an observation shared by other comparative analysis of Philippine economic development (e.g., David, 1986).

## 2. COMPARISON OF BROAD DEVELOPMENT POLICY REGIMES

The previous section established that Philippine economic growth has lagged behind that of the other countries in ASEAN. Furthermore, the breaking down of the growth of the domestic product into sectoral contributions suggests that the difficulties lie in the non-agricultural sectors.

Economic growth is generated by a nation's ability to mobilize its productive resources in response to the economic opportunities created by a mixture of exogenous events. Explaining the economic growth trends of the ASEAN countries, therefore, requires some judgment on the degree of influence caused by government policies. This section reviews the development policy regimes and economically significant events of the past four decades in each of the countries.

### 2.1. The 1950's: Decade of Economic Nationalism

In the 1950's former colonies in ASEAN began to emerge as newly independent economies. The Philippines and Indonesia had just regained their independence, while Malaysia was to be constituted as a new nation in 1957 from former British possessions in Peninsular Malaya and Borneo.[7] Thailand had long been an independent country, but was just beginning to break away from foreign economic domination that had characterized the country before and during the Second World War.[8] Economic nationalism, as the guiding principle of economic policies was therefore a widely accepted view in the region during this era.

In general, these nationalist sentiments were directed against nationals of the former colonizing countries and the local Chinese, who usually dominated the commercial sectors of the economy.[9] This nationalist perspective led to policies that were biased against private enterprise and free markets. Additionally, in countries with legacies of state monopolies and heavy state economic interventions during the colonial years, such as the Philippines and Indonesia, this economic nationalism was combined with "etatist" tendencies.[10] Malaysia was an exception, due to the influence of the more economically open and laissez-faire nature of British rule. Also,

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[7] Malaysia was formed as a federation of West and East Malaya, Sarawak, Sabah, and Singapore in 1957. Singapore would later leave the federation.

[8] British gunboat diplomacy had forced Thailand, with the Bowring Treaty of 1856, to relinquish control over its economic borders. While able to maintain political independence, Thailand was stripped of fiscal and trade autonomy by the Western mercantilist powers. See Akrasanee and Adjanant (1986).

[9] A census of businesses in the Philippines in 1948, for example, showed that 13% of businesses were owned by Americans, 23% by Chinese, and 46% by Filipinos. The ownership of the larger businesses though, were highly skewed in favor of the foreign nationals. See Zafra (1960, p. 58).

[10] Timmer (19[illegible]), for example, argues that the "dirigiste" economic philosophy of the Dutch colonial administration, embodied in the so-called "Ethical Policies" and typified by beliefs in economic dualism and the economically unresponsive peasant, had strongly conditioned the policy responses of a whole generation of Indonesian leaders after independence.

Malaysia's smoother and more gradual transition from colony to independence (i.e., no war for independence), and its ethnic factionalism diluted nationalistic sentiments.

Regarding external economic affairs, a world divided between a communist trading bloc and a capitalist international economy began to emerge from the disruptions of World War II. The capitalist international economy was strengthened by the formation of international institutions like the World Bank and the International Monetary Fund (IMF), encouraging a more multilateral pattern of trade. All four ASEAN countries belonged to the capitalist international system. Their trade patterns soon began to diversify from a heavily bilateral pattern of trade with former colonizing countries to a more multilateral pattern. Also, the Korean War gave a boost to world demand for primary commodities, improving the terms of trade for most of the region's exports.

Indonesia

During the 1950's, the biases against private enterprise in favor of state intervention found the Indonesian government progressively extending its control over the economy. According to Mangkusuwondo (1975), to fight inflation the government first attempted to control prices by taking over the foreign exchange market. When that failed, it decided to undertake imports itself and, when this also failed, took over domestic markets. This failure led the government to believe that the number of regulatory measures was still insufficient. By 1957, the country had succumbed to Sukarno's totalitarian philosophy. Under his policy of the "Guided Economy", the country became a heavily regulated economy with strong repression of private entrepreneurship. While the country was able to achieve a high annual average rate of growth in GDP (5.2 %) during the decade, mostly on the strength of its agricultural export performance in the first half, its economy began to sharply deteriorate in the late 1950's with bouts of severe inflation (Mangkusuwondo, 1975).

Malaysia

Malaysia had only a modest rate of economic growth during the 1950's (2. 6% GDP growth per year). A colony for most of the period, its economic development policy was guided by the historical British approach of commodity specialization and exploitation of comparative advantage. This policy resulted in a highly specialized and dualistic economy. The country's development and economic performance virtually relied on the export of two commodities: rubber and tin. High productivity rubber plantations existed side by side with low productivity subsistence agriculture. Even Malaysian society was highly specialized, with native Malays engaged in subsistence agriculture, Chinese labor in tin mines, Chinese entrepreneurship in local commerce, Indian labor in rubber plantations, and European capital and management in export enterprises.

By the beginning of the decade, the British colonial administration had begun efforts to correct the weaknesses of Malaysia's overspecialized economic structure. With the first formal development plan for Malaysia (1950-55), the government started to take a more active role in directing the growth and development of the economy by influencing the investment and consumption expenditures of the country in order to diversify its economy and strengthen its

domestic base. However, Arudsothy (1975) reported that only a fifth of the development budget was allocated to the rural non-estate sector, and had no employment, food production, nor industrialization objectives. Basically, the plan, which became the framework for economic policy and management for the first half of the decade, retained the laissez-faire biases of historical British policies. Public investments and expenditures concentrated on efforts to raise the productivity of the traditional sectors of rubber estates and tin mines.

The second five-year plan for the decade (1956-60), continued by the newly independent administration, did not radically change the earlier plan's development outlook. The second plan emphasized rubber replanting and large rural infrastructure to increase rubber productivity. A significant change in the plan, however, was the recognition of the government's role in developing the non-estate agricultural sector. According to Jenkins and Lai (1989), the previous colonial administration discriminated against the rubber smallholders and considered them inherently economically inefficient. Independence changed this policy bias as the government realized that, if productivity in rubber exports was to be raised in order for Malaysia to retain its comparative advantage, then rubber smallholders had to be assisted. Assistance was provided through financing for replanting, and research and farm extension services to improve smallholders' production technology. Another policy modification was in the area of land disposal, where the new government now favored smallholders in the disposal of untilled land, and assisted them in developing these lands through land resettlement schemes.

With regard to the industrial sector, the new government recognized the importance of promoting the growth of local industry. Its industrial policy followed the recommendations of the Working Party Report of 1957, which rejected the use of protective tariffs in promoting domestic industries and favored the use of tax-exemption instruments.[11]

Thailand

Nationalist economic policies and etatist policies also held sway in Thailand during the 1950's. Under the military dictatorship of Phibun Songkram (1947-57), anti-Chinese sentiments led the government to adopt policies clearly biased against private entrepreneurship. The rice export trade, with its high Chinese economic participation, was further restricted by requiring a quota rent called the rice premium in 1955. The government also established several state monopolies meant to diminish Chinese control in the economy.[12]

[11] The rejection of tariff protection is best explained by the strong views against local industry protectionism held by the foreign agency houses and Malay politicians. The former recognized that tariffs would reduce foreign trade and raise the cost of living leading to wage increases eroding the profitability of their domestic investments. The latter feared that protectionism would only benefit the Chinese at the expense of the Malays, since the former were dominant in the nation's commerce and in a better position to participate in protective rents and the expansion of local industries than the native Malays who were mostly in subsistence agriculture and rubber smallholdings (Lee Kiong Hock, 1986, p. 103).

[12] To appreciate the extent of this statistic bias during Phibun's regime, consider Akrasanee and Adjanant's (1986) report that a majority of the Thai public enterprises in 1985 were created during the Phibun era.

Despite the government's interventionist push at the time, it did not adopt a protective tariff structure to promote domestic industries due to the belief that tariff protection would only enhance the profits of local Chinese businessmen (Akrasanee and Adjanant, 1986).

The state interventions, however, had another hidden motive. According to Akrasanee and Adjanant, state monopolies were also a means of rewarding loyal friends of the ruling regime. A few favored Chinese families thus accumulated even greater wealth through alliances with Thai families in power. Ethnic nationalist objectives of these interventionist policies were actually subverted.[13]

The opportunist nature of Phibun's economic nationalism eventually discredited his regime. However, unlike Sukarno's Indonesia, economic mismanagement and government controls were not so pervasive as to cause the collapse of the market economy nor to stifle private enterprise. Moreover, the pragmatic nature of the Thai government avoided the extremes of economic ideology. The Thai economy managed to show high economic gains (5.6% annual GDP growth) during this period due to the strong performance of its agricultural exports. During the last three years of this decade, Phibun's economic policies were changed. Sarit Thanarat, who governed from 1957-63, favored the growth of private enterprise and more liberal economic policies.

Philippines

In the Philippines, the 1950's was a period of high economic growth (6.4% annual GDP growth), fueled by the expansion of import-substituting manufacturing industries. These new industries were established by an industrialization development policy founded upon a system of foreign exchange and import controls. The system of controls was instituted in response to a foreign exchange scarcity crisis that came to a head in late 1949 as a result of the Philippines' commitment to a fixed and overvalued exchange rate.[14] Exporters were required to surrender their foreign exchange earnings at the fixed overvalued rate to the Central Bank, which in turn rationed the foreign exchange in accordance with a priority list to licensed importers. The priority list determined the structure of protection, and thus, the type of import-substituting industries established. Sectors producing products at the bottom of the list received the highest degree of protection while those at the top were least protected. At the top of the priority list were those items classified as "essential": staple foods, medicine, milk, and other imported basic needs. Next were hard-to-substitute imports used as inputs in domestic production and capital goods. Import licenses and quotas were issued based on this system of prioritization.

[13] Much of the wealth remained in Chinese hands to form the foundation for large Thai-Chinese conglomerates that became prominent later in the 1970's (Siamwaila and Setboonsarng, 1989, p. 22).

[14] The Philippines-U.S. Commercial Treaty of 1946 (Bell Trade Act) severely constrained the Philippines' ability to design its own economic policies. The treaty, for example, prohibited the Philippines from placing import duties on U.S. goods, required consultations with the United States before it could change exchange rates and monetary policy. Quantitative controls, therefore, were deemed as the only workable measure to deal with the foreign exchange disequilibrium (Baldwin, 1975, pp. 39-40).

This system of controls, in effect, forced the agricultural sector (the only substantial exporter at the time) to finance the expansion of the import-substituting industries. For a time, this development strategy produced a high rate of GNP growth as the domestic manufacturing sector expanded to replace technically less-sophisticated imports and imports that required little locally unavailable input. The availability of frontier land during the earlier years of the period also allowed agriculture to expand without much reinvestment funding, thereby indirectly supporting the increasing foreign exchange requirements of the protected industries.

During this period, government agricultural policy was dominated by a policy of importing sufficient rice and corn to keep prices from rising. Land disposal and resettlement projects were also implemented allowing agricultural production to expand faster into the frontier. Agricultural exporters, clearly the most disadvantaged by the system of controls, did not initially resist the controls because they needed government financing to rehabilitate the farms that had been destroyed in the war. Furthermore, favorable terms of trade in the early half of the 1950's, especially for the sugar producers who were receiving U.S. export quotas, mitigated the taxation effects of the control system. It was only toward the end of the decade that the sugar exporters would gained enough political power to force the government to abandon the system of controls.

Another important economic policy during this period was the reservation of retail trade for Philippine nationals. This policy was aimed at excluding the local Chinese who had traditionally controlled this sector.[15] The policy, however, was easily circumvented by Chinese merchants who engaged Filipino fronts for their retail activities. Even though it failed, such a policy was consistent with the rising economic nationalism of the time. In further efforts to squeeze out foreign control of the economy, the government established a number of public enterprises in other sectors such as in transportation and utilities.

## 2.2. The 1960's: Planning and Market Orientation

The 1960's was a decade of steady expansion for the international economy. It also marked a distinct shift in economic development policy perspective in the region, from the nationalist ideology of the past decade to an acknowledgement of the positive role of private enterprise in national development. Indonesia, after a harsh experience with an extreme form of economic ideology under Sukarno, turned to more market-oriented policies under Suharto's New Order in the second half of the 1960's. At the beginning of the decade, Thailand was well on the road to looser government regulation of the private economy and launched economically sound development plans. In the Philippines, too, deregulation of the system of foreign exchange and import controls was implemented. Malaysia, a more liberal and open economy than the other ASEAN countries, took a more active role in directing its economic development through increased public investments and expenditures programs. In the region as a whole, government leaders began to recognize the legitimate role of the private sector in stimulating economic growth and development.

[15] The Retail Nationalization Act of 1954 banned foreigners, except U.S. nationals, from engaging in the retail business (Zafra, 1960, p. 62).

Indonesia

The economy of Indonesia declined rapidly under the weight of Sukarno's economic policies. Inflation skyrocketed to triple-digit rates in 1962-66, before a new government under Suharto would be able to stabilize the economy.[16] Foreign exchange reserves were down to minus $ 75 million in 1965 (Gillis, 1983, p. 12), and the Central Bank failed to honor cash letters of credit. An accurate assessment of the overall production decline is even now impossible due to the breakdown of the country's statistical network during the period.[17]

The near collapse of the economy led to the ouster of Sukarno. Disaffection with his policies prompted the new government to a changed its course. Under Suharto, economic rationality took precedence in the national development plan, and competent economists were authorized to chart the economic development of the country.[18] The new policies provided a stable and relatively more liberal environment for private enterprise. A commitment to balanced government budgets and dismantling of quantitative restrictions on the foreign exchange market marked the later years of the decade. The economic recovery that took place in response to these new policies allowed Indonesia to post a 3.9% annual GDP growth average for the decade.

Malaysia

Malaysia continued its policy in the previous period of limited government interventions in the economy. Government development efforts continued to focus on directing the flow of public expenditures and investments as its main instrument of development policy. The development plan for 1961-65 continued to emphasize the use of fiscal incentives for encouraging the growth of industry. Most government resources were still directed toward the rubber-replanting program and expansion of rural infrastructures. There was a new push for economic diversification as government allocated more resources for expansion of palm oil production in the development plan for 1966-70.

The rubber-replanting program, together with large public investments in rural infrastructure, are credited with increasing the productivity of rubber production and rural incomes of rubber smallholders during this period (Jenkins and Lai, 1989). These increases in productivity led to a high rate of growth in agricultural exports. The stable economic environment attracted foreign investments, which, coupled with increased incomes, would led to rapid growth in Malaysia's manufacturing sector. Malaysia's GDP grew at an annual average of 6.5%.

[16] Annual inflation was at 72% in 1961, and by 1966 it was at 636% (Gillis, 1983, p. 8).

[17] Production in some sectors, particularly in agriculture, continued to grow, but not by much, as farmers found ways to circumvent the pervasive web of government controls (Gillis, 1983, p. 12).

[18] Suharto's political control of Indonesia since 1966 allowed economic policy in Indonesia a continuity unmatched elsewhere. The group of economists he first engaged to stabilize the economy has continued to hold influence over current Indonesian policymaking.

Malaysia's rapid economic growth, however, increased simmering ethnic tensions, as participation in the gains from growth were uneven. Racial riots in 1969 threatened the prosperity of the country and precipitated a change of thinking regarding the role of government in economic development. Ethnic rivalries forced the government to begin a new era of economic policies into the next decade that aimed at intervening in the distribution of incomes.

Thailand

The 1960's were a decade of sustained economic prosperity in Thailand as Sarit's economic policies (1957-63) continued through the reign of Thanom Kittikachorn (1963-73). The World Bank recommendations in 1959 were heeded by the Thai government. Included in these recommendations was the fostering of longterm growth by increasing public investments, particularly in irrigation and transportation infrastructure. The latter program benefitted agriculture and allowed agricultural production to expand into the still abundant untilled lands of the country. The mild tariffs instituted during this period and the very low export taxes on most commodities except rice expanded Thailand's agricultural exports.

Formal development planning was also instituted with the First Plan for 1961-67. The plan had no explicit restrictions or guidelines with respect to foreign trade. It nevertheless reflected a policy of import substitution for spurring growth of local industries. Significant changes in industrial promotion policy occurred as tax incentives were reduced while mild tariff protection measures were instituted. Meanwhile, there was no effective promotion scheme for manufactured exports. These policies were basically carried over to the Second Plan for 1967-71. Better macro management, expanded infrastructural facilities, benefiting agriculture in particular, and the inflow of Vietnam War money from the United States have been cited as major contributing factors for Thailand's growth in the period (Siamwalla and Setboonsarng, 1979).

Philippines

The system of foreign exchange and import controls that was successful in establishing import-substituting industries in the Philippines in the 1950's was dismantled in 1961. The government extended the inward-looking development policy perspective of the country, but with a new set of policy instruments. Pressure from the sugar exporters led the government to abandon the system of foreign exchange and import controls, and to shift instead to a system of high protective tariffs. The intent of the tariffs was to protect the domestic manufacturing industries established in the earlier period of import-substitution.[19] In 1961, full decontrol was declared and the exchange rate devalued to a more realistic level. High world prices for the country's agricultural exports and the change in foreign exchange policy (which effectively reduced the rate of export taxation) led to an expansion of agricultural exports in the early half of

[19] President Macapagal's inaugural speech in 1962 revealed the intent of the government to continue with a protectionist policy for the country's import-substituting industries. He stated that by pushing for decontrol, he wished to substitute a system of protective tariffs for the inefficient system of foreign exchange and import controls of the previous regime, thereby protecting domestic industry (Macapagal, 1968, p. 21).

the 1960's. This extended to the rest of the economy, but monetization of these higher export earnings soon created inflationary pressures.

In addition, expansionary fiscal policies of the two administrations led to rising prices and renewed overvaluation of the domestic currency. Toward the end of the period, restrictions on foreign exchange and imports were again applied in order to deal with yet another developing foreign exchange crisis that would force government to change policies radically in 1971. With the election of Marcos in 1965, a new direction in agricultural policies also took hold. Marcos embarked on a policy of rice self-sufficiency by initially improving rice's domestic terms of trade. Efforts were also undertaken to increase rice productivity in the long run. Government increased the allocation of public investments and expenditures in agriculture, somewhat mitigating the anti-agricultural bias of previous development policies.[20] The economic development strategy of the 1960's could best be characterized as an extension of the inward-oriented development strategy of the prior period. By retaining protection for domestic industries, launching a food self-sufficiency program, and relying on expansionary fiscal policies to stimulate the economy, the government was clearly looking inward for sources of growth. Higher domestic inflation and a fixed exchange rate led to exchange rate overvaluation that additionally biased production incentives toward domestic markets.

### 2.3. The 1970's: Expansionist Policies

The 1970's was a period of rapid expansion of the international economy punctuated with unpredictable world events. The Yom Kippur War and the subsequent Arab oil embargo in 1973, changed the destiny of several ASEAN countries, notably Indonesia, and to a lesser extent Malaysia. Oil importing countries such as the Philippines and Thailand, on the other hand, were faced with foreign exchange management problems only slightly mitigated by the world demand boom that led to improved prices for their exported agricultural commodities. On balance, however, the general environment of rising prices for primary export commodities and the sudden availability of large sources of foreign loans created an expansionary economic environment in the region.

In retrospect, every government became overly aggressive during this period with regard to their public investment and expenditure programs. The availability of international loanable funds allowed all four countries to embark upon programs to rapidly expand their economies. Private investments rose rapidly as well, as governments channelled funds to favored sectors of the economy and also extended various tax and regulatory incentives to their domestic businesses.

In this type of expansionary international and regional economic environment, all four countries would post high rates of economic growth with rapid structural transformations. The

[20] Based on data from the Philippine Statistical Yearbook (1975) public expenditures (operating and capital) in the agriculture and natural resources sector increased in real terms by 31% in 1965-66, and by 79% in 1969-70 in comparison to expenditures in 1958-59. The share of irrigation and rural electrification in the infrastructure budget of government rose from 5.9% in 1958-59 to 7.8% in 1965-66, and 29.8% in 1969-70.

question of sustainability could be postponed as international credit and finance remained buoyant throughout. All four ASEAN countries became more outward-looking and tried to promote export activities, even in the manufacturing sector. Although easy credit stimulated growth, it also hid fundamental structural problems in the economy, which would cause severe problems in the early part of the next decade.

Indonesia

The oil price hikes were a windfall to Indonesia, a major oil exporter. Increased export earnings, however, also posed a problem as they created externally originated inflationary pressures, appreciation of the domestic currency, and ills of the Dutch disease.[21]

Indonesia was more successful in tackling the potential problems of windfall oil profits than many other oil-producing countries. For example, the government increased public expenditures in the agricultural sector, especially for rice, not only to maintain a more diversified economic base, but also to spread the benefits of the oil windfall to a larger portion of the populace. The industrial promotion programs, though import-substituting, were biased in favor of labor-intensive enterprises.

Indonesia also practiced prudent monetary and foreign exchange policies. Two major devaluations were implemented during this period to correct misalignments in the exchange rate.[22] A balanced and stable growth approach was apparent in the way Indonesia managed its economy in the fast-paced expansionary environment of the 1970's.

Indonesia had avoided serious bouts of inflation characteristic in the early 1960's and achieved high rates of growth (7.6% GDP growth annual average). It also achieved high growths in rice production, reducing its import-dependency on rice. Its manufacturing sector expanded with the promotion of import substitution in the later years of the period. Export performance was strong not only in the oil sector, but in non-oil products as well.

Malaysia

The racial riots of 1969 forced the abandonment of the hands-off tendency of Malaysia's economic policy. In 1971, the political party in power, the United Malay National Organization (UMNO), launched the New Economic Policy (NEP) which asserted the economic aspirations of native Malays for greater income parity and participation in the economy. The NEP sought to provide an economic security net for native Malays who perceived themselves as economically

[21] The "Dutch disease" refers to the economic phenomenon wherein the economy's traditional export and import-competing sectors suffer a decline because of the export boom in one commodity sector, as was observed in the squeeze placed on the Dutch economy's traditional exports because of the rapid development of its export energy sector in the 1970's (Rivera-Batiz, 1985, p. 265).

[22] The first in 1971 devalued the rupiah (Indonesian currency) by 10%; the second in 1978 by 50% (Gillis, 1983, p. 25).

disadvantaged by Malaysian Chinese.[23] While some native Malays were aided by the government's rubber-replanting program as rubber smallholders, most were in low-income subsistence agriculture, producing mainly rice. Meanwhile, the Chinese, who had largely resettled in the urban areas as a result of British efforts to deny a base for the earlier Chinese-led communist insurgency, had been able to improve their economic lot with the expansion of the domestic economy. Urbanization allowed them better access to government services such as education, and they replaced the ranks of departing British and European expatriates in business and professional groups.

The NEP acknowledged that without government intervention, economic growth would only worsen the ethnic economic gap. It called for a national effort to eradicate rural poverty and change employment and income patterns, allowing better native Malay economic representation. Attainment of NEP objectives required the government to intervene in numerous areas of the economy to assure Malay participation. Price guarantees and subsidies for rice farmers were thus strengthened.[24] The Industrial Coordination Act was passed in 1975, which increased the requirements for manufacturing licenses to include targets on equity participation and employment of native Malays. Public funds were used to buy established plantations and industrial corporations to take up the Malay reserved portion of new stock issues of existing companies. Banks were encouraged to give preference to Malay applicants with lower rates and faster loans. Public investments in rural infrastructure were accelerated, as well as public expenditures for social services in Malay-dominated areas. NEP objectives were targeted for 20 years and were vigorously pursued by the government.[25]

Other significant government in the 1970's were in the area of promoting local manufacturing industries. A new Investment Incentives Act was passed in 1968 that broadened the scope of industries qualifying for government benefits. Additional incentives promoted export-oriented industries, and thus increased use of tariffs was instituted to protect new manufacturing concerns, for example, infant industries.

While the government assumed a more activist stance in the 1970's, it would be wrong to conclude that a significant change in the management of economic activities occurred. First, the economy began as very open and liberal; second, the government carefully chose policy instruments that intruded only minimally on private initiatives and private enterprise.[26] Ariff and Hill (1985), for example, report that Malaysia maintained the lowest average tariff rates (15%) among the four ASEAN countries in the 1970's.

[23] See Mehmet (1988) for the causes of the racial riots and the NEP.

[24] In 1973, a price support scheme by the National Rice Board was made operational (Jenkins and Lai, 1989, p. 89).

[25] For more on NEP see Mehmet (1988) and Jenkins and Lai (1989, Chap. 3).

[26] See Lee Kiong Hock (1986) or Hoffman and Tan (1980) for more on Malaysian industrial promotion policies.

As an oil exporter, Malaysia's problems with the oil shocks of the 1970's were similar to those experienced in Indonesia. Malaysia managed to avoid the loss of international competitiveness in the non-oil sectors associated with the Dutch disease, with prudent fiscal management and monetary polices. Because its internal inflation rate was markedly lower than its trading partners and competitors, it actually gained in competitive strength as the Malaysian currency depreciated in real terms during the decade (Glassburner, 1984, p. 37). Its 7.8% annual average growth in GDP was the highest among the four countries.

Thailand

The economic policies of the Sarit-Thanom era, successful in a period of relatively stable and predictable international economic affairs, were no longer adequate in the 1970's. In 1973, during the same week the Arab oil embargo was imposed, the Thanom government fell and a period of political uncertainty ensued (Siamwalla and Setboonsarng, 1989, pp. 20-27). There were four other governments, none with the same unchallenged authority as the previous military regimes. A brief period of domestic rule from 1973-79 was replaced by a still shorter ultra-conservative military rule from 1976-77, which itself succumbed to a compromise government led by civilian politicians with a low profile military. This was also replaced by another coalition government in 1980.[27]

Economic policy did not suffer the same instability as the political regimes. The political players allowed economic bureaucrats some leeway in managing the economy. Due to international economic volatility and an open economy, the role of economists in macromanaging the economy would became very important in Thailand. While the country benefitted from the strong international prices for its commodity exports, the oil price shock would transmitted inflationary pressures to the domestic economy. The result was that Thailand experienced double-digit inflation for the first time.

Meanwhile, a 14% annual growth in Thailand's exports stimulated expansion of the non-agricultural sectors of its economy. Production expanded in its newly established manufacturing industries. This export-led growth caused problems for the domestic economy and induced a deteriorating balance-of-payments position, which in turn increased pressures for industrial protection. Between 1974 and 1978, average levels of nominal protection rose from 35% to 51% for products with low import competition and 25% to 36% for products with higher import competition (World Bank 1980, p. 4).

Industrial policy in the 1970's focused on export promotion with the Investment Promotion and Export Promotion Acts of 1972. These acts provided full tax exemption on imported inputs, tax rebates, and a discount facility on short term loans for exporting industries. However, a revision of tariffs in 1974 resulted in an escalation of the tariff structure that blunted the effect of the export-promotion measures.

[27] The government of Prem Tsinulanda was able to hold power from 1980-88 despite two coup attempts. See Crouch (1984).

Another policy initiative of this period, the Fourth Development Plan 1977-81, was an attempt to reduce the heavy concentration of industries in Bangkok. Additional incentives were provided for industries locating in the rural areas. Aside from this, government development policies promoted the industrial and urban sectors rather than the rural or agriculture sectors. The revisions in industrial policy throughout the period reveal attempts to push industrial incentives toward export production rather than only import-substitution. But these efforts were mostly held back by pressures to retain protection from import-competing industries established previously.

Philippines

The expansionist international environment also stimulated the Philippine economy by a debt-led development push by its government. Instead of reforming its structure of economic incentives, which was overly biased against exporting, and taking advantage of the world demand boom for primary commodities, the Philippines taxed heavily its traditional exports (sugar and coconut) by promoting monopolies in the marketing and exporting of these commodities. The Philippines also relied on infusions of foreign loan proceeds to fuel its economic growth. From 1971 to 1983, the country would accumulate a $25 billion debt as it increased public investments and expenditures (National Statistical Coordination Board, 1987). The oil price shocks of the decade were no doubt a major contributing factor in the country's debt problems, but the policy of relying on foreign debt to correct balance-of-payments deficits aggravated the situation. The reliance on foreign debt added to the overvaluation of the exchange rate, further discouraging exports.

The availability of foreign loans allowed the government to embark on numerous government-initiated development projects. It also gave the government substantial power to influence the direction of domestic investments and production. Urban and rural infrastructure projects were built with borrowed funds, the food self-sufficiency program was accelerated, and financial incentives for new industries were made available. An attempt to balance sectoral incentives was made by promoting exports. Fiscal and tax exemption incentives were extended to encourage non-traditional export production. Investment codes were modified to encourage foreign investors to set up operations in the country. Special export-processing zones, exempted from the normal tariff and trade restrictions, were established. In addition, the government promoted the monopolization of coconut and sugar exports under the justification of improving export terms of trade, and modernizing production technologies in these sectors. All these measures served to strengthen the hand of government in the private economy.

Toward the end of the 1970's, an ambitious industrialization investment program was mapped out, aimed at establishing a capital-intensive industrial base in the 1980's. Implementation of this program, however, was put on hold as international financial markets became tight in the early 1980's. Nevertheless, these plans provide an indication of the sort of inward-looking policy perspective that has pervaded Philippine policymaking, leading it to ignore basic principles of economic efficiency such as factor endowments and comparative advantage.

Heavy involvement of the government in the private economy not only caused allocative inefficiencies, but also provided opportunities for gross economic abuse. Economic decisions

were no longer guided by private or social profitability but by political considerations. Unprofitable enterprises were subsidized so long as government could borrow. Critics of the Marcos regime referred to this system as "cronyism", a system of rent-seeking that allowed the Marcos family and friends to reap great wealth while leaving the country heavily indebted. This system also nurtured inefficient import-substituting domestic industries, so long as they retained political connections to the Marcos regime. The protectionist policy perspective of the previous two periods was essentially retained, thus prolonging inefficient domestic industries.

The massive inflows of foreign debt allowed the Philippines to post high economic rates of growth in the 1970's, although not as high as its ASEAN neighbors, by attaining a high investment-to-GNP ratio. The productivity of investments, however, quickly deteriorated as the incremental-capital-to-output-ratio rose (Villegas, 1990). By the beginning of the 1980's, it was became clear that this pattern of economic policies was unsustainable.

### 2.4. The 1980's: Adjustment and Liberalization

The fast pace of growth in the 1970's slowed, forcing difficult adjustments in the economies of all the ASEAN countries by the mid-1980's. The Philippines was hardest because of its huge foreign debt, the weakness of its export sector, and the capital flight following Aquino's assassination in 1983. Indonesia, also heavily indebted, had oil and was in a better position to handle its external deficits. Thailand also found itself with serious balance-of-payments problems that forced it to seek structural adjustment loans. Even Malaysia faced current account and fiscal deficit problems.

Each country attempted to deal with the externally induced problems differently. But, generally, programs involved fiscal austerity, a reform of investment codes, liberalization of foreign exchange and trade policies, and greater privatization. By the second half of the decade, most of the reforms were well under way, and all countries, except the Philippines, were resuming the high growth rates of the previous decade. The Philippines, saddled by debt-servicing burdens, managed to post positive but modest growth rates by 1987.

Indonesia

The fall in oil prices in 1983, and again in 1986, was particularly painful for Indonesia, since oil was its major export. At the same time, world interest rates rose adding to the burden of servicing its large foreign debt.[28] The GDP growth rate dropped from a 6% annual average for 1980-83, to a 3% average for 1984-87. A large current account deficit of 7.6% of GDP in 1983 convinced the government to diversify exports quickly. The oil boom in the 1970's had brought substantial foreign exchange and revenues to the government, which led to an inward direction in trade policies as it tried to catch-up with other countries on the road to industrialization. Now protective trade policies were reformed with a more outward orientation to boost non-oil exports.

[28] Indonesia had a debt-service ratio of 27.8% in 1987, the highest in the region (Mangkusuwondo, 1990, p. 80).

One of the responses to the deficit problem was to adjust growth targets, thereby cutting public investments and expenditures programs. Fiscal austerity and structural adjustment reforms were evident in REPELITA IV, the development plan for 1984-89 (Hobohm, 1987). To strengthen the export sector, a 31% devaluation was made in 1987. Also, the government's revenue-raising capability was improved with tax reform. In addition, liberalization reforms in the investment and trade policies were undertaken.

A clear shift in economic policies with less regulation and more market orientation was evident during the decade. The country was able to attain an average annual GDP growth rate of 5.3% from 1980-89, and by 1990 economic growth rates had recovered.

Malaysia

Malaysia, which always had better fiscal, balance-of-payments, and foreign reserve positions than the other ASEAN countries, embarked on counter-cyclical fiscal policies to counter the worldwide slowdown of the early 1980's. It wisely abandoned this strategy in 1983, however, and focused instead on refining its relatively more open and liberal investment policies to attract more foreign investments.[29] While government public expenditures were the source of growth in 1981-82, external sector expenditures (including foreign investments in Malaysia) again became the source of growth in 1982-85. Malaysia attained the high rate of 4.9% average annual GDP growth for 1980-89.

The Fifth Malaysia Plan (1986-90) continued to emphasize the more effective aspects of previous policies, while urging the private sector to rely less on government support and protection. It included a large rural development expenditure program for infrastructures and services, and food production subsidies. Declarations of the government's intentions to lessen its role in the economy in favor of increased privatization were also incorporated in this plan (National Planning Department, 1986).

Thailand

Thailand's economic performance was strong in the second half of the decade. It was able to rebound from the recessionary environment and deficit problems of the early 1980's, and achieved double-digit annual GDP growth rates from 1986 to 1989. Liberalization reforms undertaken in the middle of the decade were the key factors for this success.

The serious balance-of-payments deficit and weakened foreign exchange reserve position early in the decade moved Thailand to seek IMF and World Bank assistance. It accepted the conditions for structural adjustment loans in 1983, and implemented economic policy reforms such as tariff reductions, removal of price controls, reform of fiscal policies, and devaluation in

[29] Despite the NEP, Malaysia was an attractive economy for foreign investors in search of alternative sites for relocating manufacturing operations from the Western industrialized countries and Japan. Its excellent infrastructure system, stable monetary and financial macro environment, and generally pro-business policies, complemented a low-cost labor economy. Malaysian authorities were successful in carefully pursuing the interventions necessary to promote NEP, without unduly interfering in private entrepreneurship (Jenkins and Lai, 1989).

1984 (Hewison, 1987). Implementation of these policy reforms was not easy as in the face of strong opposition from the protected industries that had benefitted from the import-substitution push of the prior two decades. The price rationalization moves also stirred up public outcry.[30]

The reforms, however, attracted multinational capital into Thailand that would resulted in annual GDP growth rates above 10% from 1986 to 1989. This new form of unbridled capitalism, however, had begun to damage the environment and stress Thailand's natural resources (Handley, 1991). It also bred corruption at high places as the vigorous economy would produced an uneven distribution of income growth. A military coup with widespread appeal used these issues to justify taking power in February of 1991. Economic expansion since 1986, however, had been so strong that Thailand posted a high 7.0% annual GDP growth rate average for the decade.

Philippines

The 1980's were painful for the Philippines as a huge foreign debt and political chaos resulted in negative growth of the economy from 1984-87[31] and slowed its rate of recovery since 1987. The Marcos government tried to deal with the recessionary environment at the beginning of the decade by counter-cyclical policies, which only created greater debt from 1980-83. A structural adjustment program highlighted by gradual liberalization of imports and cuts in tariff protection was adopted in 1981. The strategy apparently was to gradualize the adjustments to allow time for those negatively affected (e.g., protected industries) to adjust. The massive capital flight triggered by the Aquino assassination, however, brought the economy into a fast downward spiral as the government adopted restrictive monetary and credit policies (e.g., interest rates above 40%). The restrictive policies immediately cut the balance-of-payments deficits, mostly because of a reduction in domestic demand.

In 1986, the new government of Corazon Aquino resumed the trade liberalization program of the previous administration and removed most of the government controls on the private economy, especially the highly unpopular monopolies in sugar and coconut trading. Monetary policy continued to be restrictive, however, prompting charges that it was preventing a higher rate of recovery and growth of the economy. The economy began to grow again in 1987 and achieved a 5.6% average annual growth rate between 1987-89. The liberalization program was cautiously implemented due to resistance from the protected industries (PIDS 1988, Clarete 1989).

[30] There were two attempted military coups during the 1980's (Handley, 1991).

[31] The Asian Development Bank (ADB) reported a growth rate of -0.9% for 1984-87 (ADB, 1991).

# 3. AGRICULTURAL PROTECTION AND PRICING POLICIES

The history of development policy regimes in the region indicates several similarities in the way agriculture was treated in the four countries. There was a tendency to tax agricultural exports and protect import-competing agricultural production. The differences in protection between agricultural products influenced the allocation of resources within agriculture of relatively agriculture-specific factors, for example, land. The overall level of agricultural protection in comparison with levels of protection in other sectors of the economy, on the other hand, affected the allocation of relatively more mobile factors across sectors such as unskilled labor and capital. Protection distorted the allocation of factors and even their level of employment, with important negative implications for economic efficiency. This section reviews the agricultural product pricing policies and agricultural input-pricing policies of the ASEAN countries revealing some of the differences in the level and structure of protection they have provided to agriculture.

## 3.1. Agricultural Output Pricing Policies

Agricultural pricing policies are systematic interventions in the free market determination of agricultural commodity prices. The immediate reasons for interventions are often political, for example, protection of urban consumers or commodity lobbies. There is also a heavy fiscal motivation in these interventions, as governments in most developing countries search for the most effective (but not necessarily efficient) means of raising public revenues. To be politically viable, however, these interventions often need to be justified in the name of economic equity and overall economic desirability.

### Rice Price Policy

Rice, the staple food crop in all the ASEAN countries, is subjected to a great deal of policy intervention. A common food policy goal in all the countries has been to keep the price of

Table 3.1. Domestic/Border Price Ratio for Rice (Annual Averages)

| | 1960-69 | 1970-79 | 1980-83 |
|---|---|---|---|
| Philippines | 1.208 | 0.983 | 1.010 |
| Indonesia | 1.448 | 0.938 | 1.124 |
| Malaysia | 1.097 | 1.216 | 1.760 |
| Thailand | 0.581 | 0.616 | 0.819 |

Source: Data for Malaysia and Thailand were estimated from prices reported in Jenkins and Lai (1989), and Siamwalla and Setboonsarng (1989). Indonesian data were estimated from Dorosh (1985), while Philippine data were from Intal and Power (1990).

rice low and affordable to protect low-income domestic consumers, while providing adequate producer incentives to ensure sufficient domestic food supplies and protect farm incomes. Table 3.1 shows the average annual domestic-to-border price ratios (indicators of nominal protection rates) for rice since 1960. The direction of protection rates has varied according to the country's comparative advantage and level of per capita income. In Thailand, where it is exported, rice has been subjected to heavy equivalent taxation from combined export taxes and premiums, export quotas, and domestic rice reserve requirements (ostensibly to protect the interests of domestic consumers and raise revenues for the government). Thailand's great comparative advantage, not only in rice production but other agricultural production as well, gives the government lower problems with regard to maintaining adequate domestic food supplies and maintaining farmers' incomes. The taxation of rice is even cited as a positive influence in the diversification of Thai agricultural production and agricultural exports (Siamwalla and Setboonsarng, 1989).

In the Philippines, Indonesia, and Malaysia, where rice has been imported at times, rice imports are restricted (i.e., private imports banned) to stabilize the domestic rice price and to prevent it from dropping to the lower border price level. Their governments have also undertaken local procurement programs, domestic price subsidies, and in some instances, export subsidies to support a higher domestic rice price. These countries have sought self-sufficiency in rice as long-term rice policy goals, and have made public investments in irrigation facilities and rice production research and extension to increase rice productivity. At the same time that the three countries have sought to provide incentives for domestic rice producers, cheaper rice imports have been used to keep domestic rice prices from becoming too high in the short run. Domestic rice prices, therefore, have been generally higher than border prices in the three countries but have fluctuated less than the world price of rice. But in the 1970's, the average annual domestic rice price was lower than the border price in the Philippines and Indonesia as a result of the sharp increase in the world price of rice (i.e., Bangkok F.O.B. price) in 1973-75, and the deliberate actions of the government in the two countries to maintain a lower domestic rice price to protect consumers. In Malaysia, the same action was taken during the same period, but an increase in the guaranteed minimum price for paddy rice farmers in 1974, coupled with the fall in the world rice price since 1976, sharply raised the nominal protection of rice in that country. Hence, an annual domestic price average higher than the annual border price average has been registered in Malaysia since the 1970's.

Malaysia's domestic rice price is moving away from the world price, as indicated by the 1.76 annual average ratio from 1980-83, while the domestic rice price in the other three countries is generally moving closer to the world price. Differences in the political and economic situations among the countries account for the contrast. In the Philippines and Indonesia, where rice farmers have always been considered as politically potent because of their sheer numbers, the relatively low real household incomes counter the tendency to support higher domestic rice prices. Increases in domestic rice productivity, hence, improved comparative advantage, also decreased the pressure to protect the domestic price.

In Thailand, on the other hand, the currently low level of the world price of rice moderates the tendency of the government to maintain a high equivalent export tax rate for rice to avoid increased burdens on farm incomes. In Malaysia, however, high and increasing real

household income make a policy of price supports for the politically potent paddy farmers, in the name of food self-sufficiency and income equity, more politically sustainable.

Corn Policy

Apart from rice, few food commodities generate the same level of policy attention. Corn policy, however, is becoming more important as a result of the increased demand for livestock production coming on the heels of rising incomes and nutritional programs for improved diets in the region. Corn is important both as a cereal substitute for rice and as the major livestock and poultry production input. Increased importance of corn is the result of rising income not only within the region but also of Japan, Taiwan, South Korea, and Hong Kong. Relative to these countries, ASEAN countries (except Singapore and Brunei) have a great comparative advantage in agricultural production, creating opportunities for corn exports as well. However, ASEAN countries, except perhaps Thailand, have a lower comparative advantage in corn production compared to world corn suppliers such as the United States.

Table 3.2. Domestic/Border Price Ratios for Corn (Annual Averages)

| | 1960-64 | 1965-69 | 1970-74 | 1975-79 | 1980-82 |
|---|---|---|---|---|---|
| Philippines | 1.46 | 1.38 | 1.20 | 1.20 | 1.20 |
| Indonesia | n.a. | n.a. | 0.82 | 1.23 | 1.33 |
| Malaysia | 1.18 | 1.14 | 1.19 | 1.17 | 1.14 |
| Thailand | n.a. | 0.98[a] | 0.95 | 0.97 | 0.93[b] |

Source: Data, except for Thailand, are from David (1986, p.16). Data for Thailand were computed from Siamwalla and Setboonsarng (1989, p. 96).

[a] 1967-69 only
[b] 1980-81 only

Table 3.2 indicates the history of nominal protection for corn in the four larger ASEAN countries. As the table indicates, corn has historically enjoyed a higher protection rate than rice, due perhaps to the fact that it is less important as a food staple than rice and, therefore, less a target of food consumption policies. The gap in nominal protection, however, appears to be narrowing in all four countries, with Malaysia having reversed the protection bias in favor of rice. Corn protection rates have declined in the Philippines and Malaysia, consistent with the observation that increased demand for meat products may be increasing pressure not only to improving comparative advantage in the long run, but allow more inexpensive corn imports in the short run.

In the Philippines, where domestic corn producers have traditionally been protected by high tariffs and import quotas (Intal and Power, 1990), corn policy is under growing pressure from the conflicting interests of corn producers on one hand, and livestock producers and feedmillers on the other hand (Committee on Livestock and Feedcrops, 1988). In Indonesia,

where corn has been exported in some years and marginally imported in other years, Glassburner (1984) reported that clamors for import liberalization and rationalization of tariffs to reduce domestic food prices are on the rise. The traditional policy dilemma of keeping corn prices low to protect domestic consumers versus providing adequate price incentives to promote cereals self-sufficiency has grown to include the dilemma of keeping corn prices low to further meat and poultry food self-sufficiency versus keeping adequate price incentives for corn self-sufficiency. Malaysia, a traditional food importer, has had relatively low import tariffs, which have even further declined as corn imports have increased in the face of rising household incomes.

In Thailand, where corn has always been exported, corn policy has shifted since 1981 to one of full export liberalization after years of a policy of restricting corn exports through quotas. The taxation effect of the quota was relatively mild, especially in comparison with the effective rate of taxation for rice exports. The objective of the corn export quota was not so much to keep prices low for domestic food and feed consumption, but rather to stabilize export prices and ensure export contract performance with Japanese and Taiwanese buyers. With the diversification of its corn export markets, primarily from the increased demand for meat products from other fast-growing countries of the region, the government's intervention rationale disappeared. The propensity to intervene in exports of agricultural products to gain some improvement export performance, i.e., terms of trade gain, is prevalent in the region, especially for traditional exports, i.e., commodities with great comparative advantage. This phenomenon is discussed further in a following section.

### 3.1.1 General Pricing Policies for Agricultural Imports

Generally, agricultural and food imports have been restricted by all of the ASEAN countries, either through quotas or tariffs to protect domestic producers (at the expense of consumers) and, more importantly, to conserve foreign exchange. Agricultural tariff rates in ASEAN countries are moderate in comparison with other developing countries. Malaysia has the least restrictive agricultural trade tariff structure (Table 3.3) with an average tariff level of 9% for all agricultural products and a 77% tariff frequency ratio.[32] The Philippines has the most restrictive structure with a 28% average tariff level and a 100% frequency ratio. Thailand has a slightly higher average tariff level at 29%, but its frequency ratio is only 88%. Based on tariff restrictions alone, Indonesia appears to have a relatively liberal agricultural trade policy regime with only a 14% average tariff level and an 80% frequency ratio.

Tariff restrictions, however, do not reflect the complete impact of trade protection. Non-tariff barriers (NTB's) are widely applied to agricultural imports by all four countries. Import licensing is the most important form of non-tariff restriction, followed by import quotas or outright prohibitions, state trading, and health/sanitation regulations. The measurement of the protective effectiveness of NTB's has proved to be a difficult task so that studies of trade protection have tended to focus on the measurement of tariff protection. It is most likely, however, that NTB's provide a higher rate of protection than tariffs. A comparison of the

[32] A frequency ratio provides an indication of the pervasiveness of tariff protection within a product class by dividing the number of tariff restricted items in the product class by the total number of items in that class.

Table 3.3. Agricultural Tariff Rates in ASEAN, 1985-88 (Percent)

| | Agricultural Commodity | Average Tariff Level | Tariff Frequency |
|---|---|---|---|
| Philippines | All | 28 | 100 |
| | Food | 35 | 100 |
| | Raw Materials | 21 | 100 |
| Indonesia | All | 14 | 80 |
| | Food | 19 | 75 |
| | Raw Materials | 10 | 100 |
| Malaysia | All | 9 | 77 |
| | Food | 8 | 68 |
| | Raw Materials | 9 | 97 |
| Thailand | All | 29 | 88 |
| | Food | 36 | 86 |
| | Raw Materials | 22 | 95 |

Source: Agricultural Productivity Organization (1991, p. 2).

incidence frequency of these different forms of NTB's across countries among similar trade items, while perhaps not an accurate gauge of their equivalent degrees of protection, does provide an initial point of comparison of the pervasiveness and probable degree of protectionism from these instruments. Table 3.4 shows that the Philippines has the highest incidence of licensing, state trading, and import entry (e.g., health/sanitary) regulation restrictions. Indonesia applies import quotas and prohibitions most frequently, while Malaysia, again, is by far the least restrictive with regard to the number of NTB restrictions as well as tariffs. The overall picture projected by these tariff and non-tariff measures of protection is that the Philippines has the most restrictive agricultural trade regime, while Malaysia has the most liberal.

Another feature of agricultural trade policy in the region is the differential rates of protection and trade restrictions across product types. In general, raw materials (e.g., industrial inputs) and commodities consumed more by higher-income groups are subjected to higher import duties than those consumed primarily by low-income groups. Hence, meat and dairy products are subjected to much higher rates of import tariffs than grain products in all ASEAN countries (David, 1986). Table 3.5 lists the rates of protection for livestock and meat products in the region.

Thailand subjects the imports of agricultural food products, for example, soybeans, cotton, and palm oil, to low tariff levels (less than 10%) and minor non-tariff restrictions (Siamwalla and Setboonsarng, 1989). Malaysia also imposes low tariffs and inconsequential trade barriers on most agricultural food imports (Jenkins and Lai, 1989). In Indonesia, Glassburner (1984) reported substantial effective rates of protection for imports of corn (50%), soybeans (46%), fruits and vegetables (209%), and dairy products (21%). In the Philippines, in

Table 3.4. Frequency of Non-Tariff Restrictions, 1985-88

| | Commodity | Non-Tariff Barriers Frequency Ratios (%) | | | | |
|---|---|---|---|---|---|---|
| | | Licensing | Quotas | Prohibitions | State Trading | Entry Regulations |
| Philippines | All | 49 | 6 | 9 | 3 | 71 |
| | Food | 53 | 4 | 13 | 5 | 96 |
| | Raw Materials | 39 | 10 | - | - | 11 |
| Indonesia | All | 26 | 23 | 50 | 2 | 4 |
| | Food | 8 | 29 | 63 | 5 | 5 |
| | Raw Materials | 98 | - | - | - | - |
| Malaysia | All | - | - | 1 | - | 20 |
| | Food | - | - | 2 | - | 29 |
| | Raw Materials | - | - | - | - | - |
| Thailand | All | 35 | 1 | 24 | 1 | 20 |
| | Food | 40 | 0 | 32 | 1 | 24 |
| | Raw Materials | 23 | 1 | - | - | 7 |

Source: Agricultural Productivity Organization (1991, p. 2).

contrast, tariff rates and non-tariff restrictions have been substantial for most agricultural imports -- more than 50% average tariffs in 1978 and 40-50% averages in the 1980's as reported by Clarete (1989).

In the latter two countries, import restrictions have been intended less to protect domestic producers, but rather to conserve foreign exchange, especially during episodes of severe foreign exchange scarcity. The two countries also have suffered chronically from prolonged exchange rate overvaluations and large subsequent exchange rate devaluations as a result of inflationary episodes and aggressive expansionary policies. Increased and high rates of trade restrictions have been often associated with attempts to postpone exchange rate adjustments. In comparison, Malaysia and Thailand have had more stable and realistic currency valuations, and subsequently less restrictive import policies. The interaction of these macro policies with agricultural policies is discussed in more detail in a following section.

### 3.1.2 General Pricing Policies for Agricultural Exports

Price interventions have been applied on agricultural exports to diversify production patterns, improve foreign terms of trade, and raise government revenues. Table 3.6 shows the rates of equivalent export taxation for some export commodities in the region. As mentioned earlier, traditional export crops have been substantially taxed while newer export crops are taxed less and may be even promoted through subsidies. This export-pricing pattern reflects the

Table 3.5. Nominal Protection Rates for Livestock Products. 1960-82
(In Percent of Deviation from Border Price)

| | 1960-64 | 1965-69 | 1970-74 | 1975-79 | 1980-82 |
|---|---|---|---|---|---|
| Philippines | | | | | |
| Beef | 45 | 19 | 7 | 42 | 42 |
| Pork | n.a. | 24 | n.a. | 7 | 6 |
| Chicken | n.a. | 100 | 66 | 36 | 41 |
| Indonesia | | | | | |
| Beef | n.a. | n.a. | -46 | 26 | 37 |
| Chicken | n.a. | n.a. | n.a. | 16 | 87 |
| Malaysia | | | | | |
| Beef | 42 | 19 | 7 | 42 | 42 |
| Pork | n.a. | 24 | n.a. | 7 | 6 |
| Chicken | n.a. | 100 | 66 | 36 | 41 |
| Thailand | | | | | |
| Beef | -35 | -35 | -31 | -17 | -31 |
| Pork | 35 | 61 | 33 | -2 | n.a. |
| Chicken | -3 | 41 | 20 | -1 | n.a. |

Source: David (1986, p. 16).

intention of diversifying exports as a strategy of coping with volatile agricultural exports earnings. It also reflects the tendency to rely on a few dominant export commodities for government revenues. Such is the case for Malaysia where the rubber export tax (called a "cess") contributed a major portion of the government income, especially during the early post-colonial years.

In Malaysia, taxation of rubber used to be "dualistic" on account of the dualistic nature of its rubber industry. Prior to Malaysia's independence, the British government favored the foreign-owned rubber estate producers over the predominantly Malay rubber smallholders. Premium prices were paid to the estate producers, while discounted prices were paid to the smallholders to discourage expansion. Rubber productivity programs such as agricultural research were also aimed at benefiting the estates instead of the smallholders, even though the smallholders equally contributed to the rubber research cess assessed on rubber exports. These policies were reversed with independence and the emergence of UMNO, a political party with strong support from the rural Malay areas. Although the rubber industry continued to be taxed substantially, government programs to designed to assist the small producers increase productivity were implemented. The most effective of these programs was the rubber-replanting program is which the, government financed grower investments in new higher yielding trees. Substantial taxation of rubber exports motivated Malaysia's agriculture sector to diversify into palm oil exports, where taxes were initially relatively lower. Eventually, taxes on the new crop increased, however.

Table 3.6. Equivalent Export Tax Rates, 1960-84

| | 1960-69 | 1970-79 | 1980-84 |
|---|---|---|---|
| Philippines | | | |
| Sugar | 0.112 | 0.213 | 0.255 |
| Copra | 0.043 | 0.137 | 0.280 |
| Fruits[a] | 0.000 | 0.040 | 0.040 |
| Indonesia | | | |
| Coffee | n.a. | 0.225 | 0.310 |
| Cassava | n.a. | 0.096 | 0.050 |
| Malaysia | | | |
| Rubber | 0.074 | 0.139 | 0.118 |
| Palm Oil | 0.075 | 0.133 | 0.045 |
| Thailand | | | |
| Rice | 0.419 | 0.384 | 0.184 |
| Sugar | -1.093 | -0.491 | -0.310 |
| Rubber | 0.133 | 0.178 | 0.182 |
| Maize | 0.039 | 0.071 | 0.071 |
| Cassava | 0.000 | 0.000 | 0.000 |

[a] Bananas, pineapple and other minor fruit exports from David (1986).

Source: Philippine data from Intal and Power (1990), Indonesian data for coffee from David (1986), while for cassava estimates based on Dorosh (1985); Malaysian data from Jenkins and Lai (1989), Thailand data from Siamwalla and Setboonsarng (1989). Equivalent export tax rates reflect the effects of export taxes, quotas, and other export restrictions as revealed by the ratio of the difference of the border price from the domestic parity price over the domestic price. These rates do not indicate effects of overvalued exchange rates.

In Thailand, where rice and rubber exports were taxed substantially, sugar exports enjoyed a net subsidy. The subsidization of sugar exports in Thailand is the "step-child" of a previous policy of subsidizing domestic sugar production when sugar was imported the subsidy was aimed at achieving self-sufficiency. This further demonstrates the strong propensity of sugar producers (primarily because of the economic and political power created by the centralization of income flows through a few sugar mills) to force governments to continue supporting a relatively inefficient crop. Cassava exports were not subjected to any restrictions until 1980. Attempts were made to impose quotas such as voluntary export restrictions (VER) requirements by the European Economic Community (EEC) since 1980, but they have not been very effective (Siamwalla and Setboonsarng, 1989).

Taxation of rice exports in Thailand has taken the form of export duties and premiums, export quota rents, and rice reserves. The rice premium is an additional duty on top of the usual export tax that has served to even out the earnings of rice exporters by siphoning off some of the windfall profits caused by fluctuations in world prices. It has constituted the major portion (40% to 80% ) of the rice export taxation, and has contributed substantially to the government budget.

From the mid-1960's, however, the fiscal contribution of the export tax and premium has been declining, with 1985 being the last year when it combined to form as much as 10% of government revenues.

The reserve requirement is a requirement for exporters to sell certain quantities of rice to the government at below-market prices before the exporters are awarded shipping permits. It was used as an instrument for the government to subsidize domestic rice consumption mainly from 1973 to 1981 when rice export prices were strong. Since 1983, however, its application has been suspended in view of the weak export prices for rice. Export quotas for rice are believed by the government to control international rice terms of trade for Thailand. According to Siamwalla and Setboonsarng (1989), Thailand's Ministry of Commerce has long believed that Thailand has monopoly power in the international rice trade, and thus it has attempted to cartelize the rice export trade by fixing market shares of exporters and setting minimum export prices. However, for much of the period they studied, the quotas have rarely been restrictive enough to affect domestic price formation, and one study has even concluded that cartelization was simply a facade (Usher, 1967). It is wrong, however, to dismiss the licensing system as ineffective policy intervention. Siamwalla and Setboonsarng interpret the continued existence of the licensing system as an insurance to satisfy some government and exporter objectives. The export licensing requirement serves as a standby means by the government to discipline the traders, which it does not have to wield as long as traders operate within policy designs. Traders, on the other hand, do not see the system as counter to their interests as long as implementation is not overly restrictive. Besides, the licensing arrangement provides economic rents to established exporters.

In Indonesia, coffee, an estate crop, has been substantially taxed. Most exports such as cassava, however, have faced light direct taxation. Glassburner (1984) pointed out that exporters are faced with serious bureaucratic bottlenecks in exporting.

In the Philippines, the domestic price of sugar is actually higher than the world price. But since Philippine sugar has access to the protected U.S. sugar market, the government has been able to tax sugar exports. Taxes or levies were placed on sugar and coconut exports in pursuit of policy objectives similar to rubber in Malaysia or rice in Thailand. These rates of direct export taxation were not much higher in the Philippine case, especially when compared to export taxation of rice in Thailand. The difference, however, seemed to come from more pervasive disincentives to exporting by the agricultural sector in the Philippines, namely, the effects of the overall structure of protection and an overvalued exchange rate. Explicit export taxes are often designed to transfer part of export rents to domestic consumers and to the government, but they also influence resource allocation efficiency. However, while more explicit commodity pricing policies such as export taxation of rice in Thailand or rubber in Indonesia encouraged shifting resources away from these commodity sectors into other newly profitable agricultural exports, the Philippines' overall trade protection structure and overvalued exchange rate appeared to have prevented attractive alternative investments in agriculture or other export-oriented sectors. The resource allocation inefficiency that arose from macro pricing policies are discussed in a subsequent section.

## 3.2. Agricultural Input Pricing Policies

Increased irrigation and fertilizer use are the two most significant factors in the sustained growth of agricultural production in Asia since the mid-1960's. The percentage of irrigated areas and fertilizer usage, especially for food production, has dramatically increased in the ASEAN countries (Ahmad and Falcon, 1989). While national accounts and aggregated input-output data tend to minimize the importance of these two agricultural inputs because of their small accounting share in total costs and value-added, policies for providing these inputs to the farmers can significantly impact the agricultural performance of the countries. The governments of all four countries have intervened heavily in the provision and pricing of these agricultural inputs. Irrigation water and fertilizer-pricing policies are the two most important agricultural input-pricing policies. Net protection of value-added and thus net incentives for agricultural production depend on the structure of nominal protection between outputs and inputs -- a higher output/input price ratio increases the profitability of an agricultural activity.

### 3.2.1 Irrigation Policy

Irrigation, unlike fertilizer and pesticides, is not only non-tradable (i.e., a fully domestic good) but also a non-marketed good. Its provision and distribution are commonly implemented through government and other non-market institutions such as farmer associations. Nevertheless, the costs of providing and distributing this agricultural input are very real; not only to the farmer, but also to the society of each of the four ASEAN countries. Agricultural policy analysis must take into account the deviations in private prices and social prices, and the efficiency implications that are engendered by the structure of irrigation policies.

The two most important costs associated with providing irrigation water to the farmer are construction costs of the irrigation system and the operations and maintenance (O&M) costs. Comparative studies on irrigation policies (e.g., Taylor and Wickham, 1979) reveal that in all four countries, farmers are often fully subsidized by the government for the construction of irrigation facilities.[33] Farmers, as a matter of public policy, are expected to pay O&M costs. In general, however, the direct payments of farmers in the form of irrigation fees are much smaller than the actual costs of operating and maintaining these irrigation systems (Lazaro, Taylor, and Wickham, 1979). The provision of irrigation remains as the most significant conduit of transferring resources from other sectors of the economy to the agricultural sector in these countries.

In Indonesia, Taylor (1979) reported that farmers typically pay only for the distribution of irrigation water by a local ditch-tender from the terminal canal to farm plots, plus some costs of repair and maintenance of these terminal facilities. Taylor estimate these costs borne by the farmers to have been $9.10/ha in 1973-74, while the costs of fully maintaining the main irrigation system was estimated to be $6.75/ha. He argued, however, that farmers in Indonesia ultimately pay fully for these O&M costs through higher land tax assessments for irrigated land.

[33] Privately provided irrigation systems are usually the small private pump systems (e.g., tubewells), which form a very insignificant portion of the total irrigated area in these countries.

He further estimate that 40% of the land tax assessments go to agrarian expenditures such as irrigation maintenance.

This policy of financing irrigation costs is similar across the four countries, with Thailand and Malaysia subsidizing more than Indonesia or the Philippines. In Thailand, Duncan (1979) reported that the Thai government absorbs the costs of irrigation construction and most O&M costs. In Malaysia, the studies of Thavaraj (1979) and Jenkins and Lai (1989) indicated that the Malaysian government similarly fully subsidizes rice farmers for costs of irrigation water. In the Philippines, the situation is no different, as reported by Tagarino and Torres (1979) in their study of the Upper Pamapanga River Project. Their study indicated that farmers' payments through irrigation fees were inadequate to support the estimated $94/ha costs of annual construction and O&M of the irrigation system in 1974-75.

### 3.2.2 Fertilizer and Pesticides Policy

Policies on fertilizer and pesticides in the ASEAN countries typically revolve around two themes: the attempt to subsidize farmers for fertilizer costs to encourage increased food production, and the attempt to achieve self-sufficiency in fertilizer supplies by extending import protection to domestic fertilizer producers. These contradictory policy objectives result in wide distortions of fertilizer and pesticide prices. Not only are there wide gaps between domestic fertilizer and pesticide prices versus border prices, but also different fertilizer/pesticide prices for different crop usages. Food producers, for example, rice farmers, typically secure subsidized prices while commercial crop farmers must pay higher prices.

Table 3.7. Fertilizer and Pesticide Nominal Protection Rates (Percent)

| | Fertilizer | | Pesticides | |
|---|---|---|---|---|
| | 1970's | 1980's | 1970's | 1980's |
| Indonesia | 17 | 0 | 17 | 0 |
| Malaysia[a] | 23 | 12 | 23 | 12 |
| Thailand | 42[b] | 4 | - | 4 |
| Philippines | 31 | 34 | 17 | 31 |

[a] Malaysian data are for 1973 and 1978.
[b] For urea and ammonium phosphate in 1971-73.

Source: Indonesian data are from Pangestu and Boedino (1986); Malaysia from Lee Kiong Hock (1986); 1980 Thailand from Akrasanee and Ajanant (1986); Philippines from Tan (1986) -- all in Findlay and Garnaut (1986). Thailand data from 1971-73 from Siamwalla and Setboonsarng (1989).

The desire to be self-sufficient, in fertilizers especially, has led to significant nominal rates of protection for these inputs in various periods (Table 3.7). Prior to 1980, all four countries had significant rates of nominal protection for fertilizers and pesticides. In Thailand, for example, the high rate of protection on urea and ammonium sulfate from 1970-73 was due to the protection of the lone domestic manufacturer of nitrogen fertilizer (Siamwalla and Setboonsarng, 1989). By 1980, however, all the countries, except for the Philippines, had liberalized fertilizer and agricultural chemical imports. Thailand gave up its fertilizer self-sufficiency goal, while Indonesia by achieving comparative advantage in fertilizer production found it no longer necessary to protect domestic producers. The Philippines, however, appears to have increased its determination to be self-sufficient in fertilizer, despite failure to gain comparative advantage in fertilizer production, by slightly increasing its already high nominal protection rate from 31% to 34%.

Table 3.8. Paddy Rice to Fertilizer Price Ratios

| | Paddy Rice to NPK Ratio [a] | Paddy Rice to Urea Ratio [b] |
|---|---|---|
| Philippines | 0.27 | 0.32 |
| Indonesia | 0.66 | 1.0 |
| Malaysia | 0.69 | 0.76 |
| Thailand | 0.22 | 0.34 |

[a] 1978-1982 data from APST (1986).

[b] Indonesian data is for 1975 from Widianto (1991); Malaysia is for 1974 and computed from Jenkins and Lai (1989); Thailand is for 1974 and computed from Siamwalla and Setboonsarng (1989); Philippines is for 1974 and from APST (1986).

The impact of differences in fertilizer pricing policies on agricultural production incentives becomes clearer when looking at the differences in agricultural output/input price ratios, such as for paddy rice and fertilizer in Table 3.8. The Philippines and Thailand have much lower ratios compared to Indonesia and Malaysia. The latter two countries have strongly promoted increased domestic food production, especially rice, and have intervened not only by raising the paddy rice price over its border price, but also by subsidizing fertilizer prices to the rice farmers. Thailand's taxation of rice, in which it has a tremendous comparative advantage, accounts for the low paddy rice/fertilizer price ratio in Thailand. For the Philippines, however, the low price ratio is inconsistent with its efforts to achieve rice self-sufficiency and suggests inefficiencies due to failure in properly resolving conflicts in commodity policy objectives. Pricing policies in pesticides and other agricultural chemical inputs have generally been less important and followed trends in fertilizer policy.

# 4. INDUSTRIAL PROMOTION, TRADE, AND EXCHANGE RATE POLICIES

The historical review of development regimes in the region shows that sustained growth of the four ASEAN economies depended on how successful they were in promoting the growth of their industrial sectors. While agriculture continues to be an important economic contributor in all four countries, its share in the domestic product has generally declined in the region. This decline in agricultural importance has been abetted by a general tendency to favor industrial expansion as the principal component of development programs. The countries have engaged in some form of industrial promotion that naturally diverted the flow of investments and use of existing transferrable factors of production from the agricultural sector to the non-agricultural sector. Furthermore, exchange rate policies, capable not only of distorting allocations of resources from the agricultural sector to non-agricultural sectors but also in allocations within agriculture itself, played an important role in the development performance of the four countries.

The thrust of this section is to show that industrial promotion policies in the Philippines have relied comparatively more on import protection, which not only hurts agricultural sub-sectors that export but also retards the development and growth of export-oriented non-agricultural sectors as well. Together with a foreign exchange policy that chronically overvalued the domestic currency more than in the other three countries, the anti-trade bias of Philippine development policies led to a disappointing economic performance and depression of both rural and urban incomes.

## 4.1. Industrial Promotion and Trade Policies

Trade protection can be an important instrument in promoting industrialization, especially in the early stages of industrial development when economies of scale and infant industry disadvantages initially have to be overcome. In the more mature phase of industrial development, however, it is a potential hindrance as protected industries may fail to improve their international competitiveness and thus remain dependent on the domestic market. Obviously, such a situation restricts the growth of the industrial sector as protected industries become constrained by the growth dynamics of the domestic market instead of gaining access to the larger more dynamic international markets. Additionally, industrial trade protection retards the growth of other sectors in the economy, especially the sectors that are being discriminated against as resources become tied up in the protected sectors.

In the practice of using industrial trade protection as an instrument of industrial development, the Philippines had a head start on the other ASEAN countries. As early as the 1950's, the Philippines had embarked on an import-substitution industrialization strategy that was implemented through a system of foreign exchange rate and import controls. This created in the Philippines a highly restrictive trade regime that was only rivaled in the region by Indonesia.[34] During the same period, Thailand and Malaysia had relatively liberal trade regimes as both

[34] Indonesia had installed a highly restrictive regime not for industrial development but rather to deal with foreign exchange shortages caused by inflationary pressures originating from its failure to align government expenditures with available government revenues.

governments were reluctant to employ industrial trade protection to promote the development of domestic industries.[35] Thailand tried to pursue industrialization through state enterprises, while Malaysia opted for tax and other fiscal incentives instead. Quantitative import restrictions were not significant in either country so the degree of trade restrictiveness was fully reflected in the average level of tariff rates. For Thailand, Akrasanee and Adjanant (1986) reported that the average nominal rate of protection for 1950-59 stood at 18%, while in Malaysia, Lee Kiong Hock (1986) reported that tariff rates were less than 10% for most import items during the same period.

In the 1960's, trade protection as an instrument of industrial promotion became more widely practiced in the region. Average rates of import tariffs increased in both Thailand and Malaysia as government policy began to favor accelerating domestic industrial development through import substitution. In the Philippines, the system of foreign exchange and import quantity controls was scrapped as the principal means of protecting the already established domestic import-substituting industries, in favor of a protective tariff structure. In Indonesia, the collapse of the Sukarno government in 1966 led to changes in the trade policy regime. Trade policies became more liberalized as the new government sought to establish economic stability. Available estimates of average levels of nominal protection for the period show that the Philippines had the most restrictive regime at 75% nominal protection rate (NPR) for consumer goods, and 42% overall (Tan, 1986). Thailand, in comparison, had 30-55% NPR's for consumer goods (Akrasanee and Adjanant, 1986). Malaysia's average NPR was reported to have risen from 10% in 1963 to 16% in 1970 (Lee Kiong Hock, 1986). For Indonesia, Pangestu and Boedino (1986) reported that tariff and other import charges stood at 25% of total import values in 1969.

In the 1970's, a period of high industrial growth rates for the ASEAN countries, trade protection continued to be an important tool of industrial policy. Tariff protection rates in both Thailand and Malaysia rose significantly, while Indonesia began to embark on its own phase of import-substitution by raising tariff rates and increasing use of non-tariff forms of import restrictions. In the Philippines, the highly protective tariff rates adopted in the 1960's were little changed. Average NPR stood at 45% in 1974 in the Philippines, while it was estimated at 32% in Thailand by the end of the decade, and 22% in Malaysia in 1978.[36] In Indonesia the average NPR rose to 48% in 1975, before declining to 27% in 1980.

While increased import protection appears to have increased the entrenchment of import-substituting activities during this period, efforts to wean domestic industries away from import-substitution into production for exports, though not fully effective, also surfaced. In the Philippines, high export taxes on traditional primary exports were adopted to encourage some additional form of processing and value-added before being exported. For example, copra (dried coconut meat) exports were subjected to a 7.5% basic export tariff and an additional export

[35] As discussed in Section 2.0, this reluctance was due to the anti-Chinese sentiments in both countries and the perception that trade protection was only going to benefit the Chinese who dominated the local commerce of the two countries.

[36] Data are from the same cited sources as those in the previous period.

premium duty of 30%, while non-traditional exports were only taxed at 4% (Tan, 1986). Investment incentives to exporting industries were also extended in the Philippines, Malaysia, and Thailand to encourage more manufactured exports. Export-processing zones began to be developed to promote manufactured exports in the Philippines, Malaysia, and Thailand. However, as Tan (1986) noted, export incentives were insufficient when compared with the incentives extended through import protection in the Philippines, to significantly alter the deployment of resources from import-substitution to export production.

The 1980's became a period of significant reform in industrial promotion policies as governments in all four countries summoned the political will to push forward with trade liberalization despite strong resistance from vested interests in the import-competing local industries. In the Philippines, the number of items subject to import restrictions was drastically reduced and tariff rates significantly cut as well as narrowed. The average tariff level declined to 16% in 1988 (Baldwin, 1990), while the number of restricted imports dropped to 8% of total trade items in 1989 from 34% in 1985 (Pante and Medalla, 1990). In Thailand and Indonesia, similar trade liberalization programs were implemented in the second half of the period to make ASEAN one of the most liberal trading regions.

Throughout these periods, the structure of trade protection was similar in the four countries. A cascading pattern of protection, where manufactured goods nearest the consumer level received more protection, was evident in all four countries. Table 4.1 lists the tariff rates for 21 familiar manufactured commodity groups for the four countries in 1980. The Philippine rates already reflect the rates in the reformed Tariff Code of 1981. However, the Philippine rate was highest in 9 of the 21 commodity groups, while Thailand was highest in 5, Indonesia in 4, and Malaysia in 3 of the 21. These results indicate a persistent tendency in the Philippines to extend more protection in comparison with the other three countries, despite the reforms.

### 4.2. Exchange Rate Overvaluation

An exchange rate overvalued by excessive trade restrictions penalizes exporters and rewards import-competing domestic producers. It also encourages smuggling as high rents invite risks to bypass the official trading system. Thus, economists have often criticized the economic efficiency of protecting an overvalued exchange rate by more trade restrictions. An overvalued exchange rate that is accommodated by foreign reserve drawdowns and foreign borrowing is even worse, as it is an unsustainable policy that encourages speculative attacks on the domestic currency and prevents sound investment decisions. It also encourages the shift of resources into consumption and away from domestic investments as demand shifts more to imports, even impairing import-competing industries.

As Table 4.2 shows, the Philippines and Indonesia had the highest rates of overvaluation among the four ASEAN countries. Indonesia, however, had completely corrected its misalignment by 1980, while the Philippines continued to post high rates of overvaluation. Thailand has had a mild case of overvaluation, although a trend toward higher rates was indicated in the early 1980's. Malaysia had the lowest and most stable rates of foreign exchange alignment.

Table 4.1. Industrial Tariff Percentage Rates, 1980

| Commodity Group | Indonesia | Malaysia[a] | Thailand | Philippines |
|---|---|---|---|---|
| Food Manufactures | | | | |
| Canned Food | 66 | 20 | 60 | 9 |
| Cigarettes | 68 | 210 | 60 | 69 |
| Beverages | 64 | 23 | 45 | 51 |
| Light Industriales | | | | |
| Textile/Weaving | 52 | 15 | 61 | 44 |
| Garments | 20 | 25 | 64 | 36 |
| Leather Footwear | 49 | 40 | 60 | 11 |
| Paper Products | 55 | 20 | 29 | 39 |
| Non-metal Furniture | 15 | 20 | 52 | 7 |
| Soap/Detergents | 23 | 20 | 46 | 51 |
| Drugs/Medicines | 3 | 0 | 18 | 28 |
| Tires | 12 | 66 | 24 | 40 |
| Glass | 27 | 25 | 45 | 38 |
| Elec. Appliances | 27 | 45 | 36 | 80 |
| Bicycles/Motorbikes | 24 | 16 | 49 | 55 |
| Basic/Heavy Industriales | | | | |
| Iron and Steel | 8 | 15 | 2 | 30 |
| Industrial Chemicals | 3 | 25 | 22 | 22 |
| Cement | 5 | 10 | 11 | 0 |
| Elec. Machinery | 17 | 25 | 21 | 22 |
| Non-elec. Machinery | 13 | 20 | 15 | 22 |
| Motor Vehicles | 46 | 60 | 73 | 90 |
| Communication Equip. | 25 | 25 | 36 | 23 |

[a] 1978 data

Source: Indonesia data from Pangestu and Boedino (1986); Malaysian data from Lee Koing Hock (1986); Thailand data from Akrasanee and Adjanant (1986); and Philippine data from Tan (1986).

Exchange rate overvaluation has served not only to transfer resource allocations from export-oriented sectors to inward-oriented sectors but has also affected real transfers of income from exporters to preferred import-using sectors in the Philippines. This is because of a system of allocating the scarce foreign exchange to import-competing industries that utilize imported inputs and capital.[37] While there were substantial distortions in the pricing system caused by more direct price manipulations on some major commodities in the other ASEAN countries, the Philippines relied most on indirect means of transferring income between interest groups.

[37] The amount of income transfers that occurred because of the combined impact of commodity pricing, trade protection, and exchange rate policies were estimated for Malaysia by Jenkins and Lai (1989), for Thailand by Siamwalla and Setboonsarng (1989), and for the Philippines by Intal and Power (1990). They are presented and discussed in a following section.

Table 4.2. Exchange Rate Overvaluation in ASEAN, 1960-83 (Percent)

| | 1960 | 1965 | 1970 | 1975 | 1980 | 1983 |
|---|---|---|---|---|---|---|
| Philippines | 25.7 | 18.5 | 21.4 | 26.9 | 32.2 | 31.4 |
| Indonesia | 157.2 | 87.8 | 17.3 | 50.1 | 7.8 | -0.8 |
| Malaysia | 5.9 | 6.4 | 8.4 | 11.0 | 4.9 | 14.7 |
| Thailand | 12.5 | 9.9 | 25.2 | 19.2 | 24.2 | 25.1 |

Source: Data for Philippines from Intal and Power (1990); Indonesia from Dorosh (1985); Malaysia from Jenkins and Lai (1989); and Thailand from Siamwalla and Setboonsarng (1989). Overvaluation is defined as the percentage deviation of the actual rate over the equilibrium rate, where equilibrium rate is defined as the rate that would have prevailed in the absence of trade restrictions and deficits.

## 4.3. Net Protection and Exchange Rate Bias and their Effects on the Agricultural Sector

Extraction of the agricultural surplus to finance the development thrusts of the governments of the Philippines, Malaysia, and Thailand was crucial, especially in the earlier phases of programs for economic development in these countries. Only in Indonesia was the engine for economic growth primed by a non-agricultural sector, petroleum exports. Extraction of the agricultural surplus was accomplished through direct (e.g., agricultural export taxation) and indirect (e.g., import restrictions, foreign exchange overvaluation) policy instruments that turned the domestic terms of trade against agriculture. In the Philippines, the surplus was indirectly transferred to selected manufacturing entrepreneurs through the system of selective import and foreign exchange rate controls that lowered the price of agricultural exports, chiefly from exchange rate overvaluation, and increased the price of domestic manufactures relative to their border prices. In Malaysia and Thailand, substantial portions of the agricultural surplus were transferred to the government through more direct means, i.e., taxation of exports. These transfers of resources from the agricultural sector were effected by the combination of trade, exchange rate, and agricultural pricing policies.

Trade protection provides a means of transferring income not from consumers to producers of protected sectors, but also from producers in some unprotected sectors to producers in protected sectors. Income is transferred directly between producers through input-output production linkages. Protection requires an unprotected sector to pay higher prices for inputs it purchases from a protected sector.

Another, more subtle, means of transfer is through the sectors' competition for scarce factors of production, e.g., capital and labor. Protection forces the unprotected sector to pay higher wages and release resources for the use of the protected sectors. A comparison of net effective protection rates that takes into account the impact of misaligned exchange rates (e.g., definition of Corden, 1966) provides a net measure of these resource "pulls". However, the absence of such estimates that could be consistently compared for all four countries, prevents us

Table 4.3. Transfers out of Agriculture, Various Periods

| | Period | % of Agriculture's Gross Value-Added Transferred |
|---|---|---|
| Philippines[a] | 1951-60<br>1961-65<br>1969-74<br>1978 | 22<br>21<br>12.5<br>17 |
| Indonesia[b] | 1975 | 17 |
| Malaysia[c] | 1960-69<br>1970-79<br>1980-83 | 8<br>7<br>-4 |
| Thailand[d] | 1960-69<br>1970-79<br>1980-83 | 8<br>9<br>7 |

[a] Philippine data for 1951-65 are from Paauw (1968), while 1969-78 are from de Leon (1982).
[b] Indonesian data is from Quisumbing and Taylor (1985).
[c] Malaysian data computed from resource flow estimates by Jenkins and Lai (1989).
[d] Thai data computed from resource flow estimates by Siamwalla and Setboonsarng (1989).

from comparing the extent of misallocation of resources in the countries. Instead, estimates of the percentage of agriculture's value-added that was transferred out of agriculture into the rest of the economy because of the combined effects of non-price measures (e.g., infrastructure expenditures), direct price measures (e.g., producer price subsidies or taxation), and indirect price measures (e.g., exchange rate overvaluation) is provided (Table 4.3). While the data are from disparate sources and use different methods for calculating the income flows, they do provide some indication of the relative severity of discrimination against agriculture in the Philippines.[38] The Philippines clearly shows the highest rate of resource transfer per value-added in agriculture. Malaysia, which had lower rates of policy price distortions, not surprisingly, showed the lowest levels of transfers out of agriculture, which became inflows into this sector in the 1980's.

A breakdown of the resource flows into non-price transfers, direct price transfers, and indirect price transfers, show government providing a net transfer into agriculture primarily because of a pro-agriculture bias in public infrastructure expenditures, especially for the case of Malaysia and Thailand. Data from Jenkins and Lai (1989) for Malaysia, for example, show that government made net transfers into agriculture that were 46% to 61% of the income transferred out of agriculture by direct and indirect price means from 1960-1980. The tendency of

[38] Quisumbing and Taylor (1985) also reported resource flow estimates for Malaysia in 1971 and Thailand in 1975. Their estimates were very much higher than Jenkins and Lai's (1989) estimate for Malaysia, or Siamwalla and Setboonsarng's (1989) estimate for Thailand. The more extensive studies of the latter authors, however, make them more reliable.

government spending to compensate for the bias against agriculture from trade protection and pricing policies was similarly reported for the case of Thailand (Siamwalla and Setboonsarng, 1989) and the Philippines (Intal and Power, 1990). Indirect price mechanisms, however, were more severe and played a more significant role in the Philippines.

## 5. SUMMARY AND CONCLUSIONS

The four ASEAN countries all have a high degree of international economic participation. The continued substantial contribution of their agricultural sector to exports suggest that they have a comparative advantage in agriculture. The growth of their manufacturing sectors, especially in contributions to exports, also suggest that they are gaining comparative advantage in the production of labor-intensive manufactures. There is thus an ongoing process of transformation of agricultural comparative advantage into comparative advantage in labor-intensive manufactures. The comparison of their development experiences and their policies affecting agriculture suggests that more outward-orientedness and less reliance on trade and exchange rate interventions in promoting sectoral objectives would produce more optimal policies in this transformation process. Agricultural and manufacturing products are not homogenous products. Therefore, the process of discovering what products each sector should be producing is a complex matter that should best be left to the competitive markets. The price of food, undoubtedly, is a critical factor in keeping wages low and contribute to gaining manufacturing comparative advantage. But food prices can also be kept lower not only by appropriate production incentives but also by appropriate trading policies.

There are valid reasons for government interventions in markets. An important one is to provide a secure environment for economic activities. Tensions from socially unacceptable income distributions and wealth-endowments are too strong to be neglected by any government. The experiences of the ASEAN countries, especially Malaysia, however, point to the need for careful selection of policy intervention instruments so as not to stifle the productivity of private enterprise, which can only, ultimately, defeat the purpose of any of these interventions. Economic prosperity is the key for any successful income-improving program, a sluggish economy would have less to offer in terms of income improvements and defeat the very purpose of income-distribution programs.

The more specific conclusions apparent in this broad review of agriculture and development policies are the following:

1. Heavy state interventions in the economy are likely to repress economic growth in the long term, if not sooner. This was shown in the case of Indonesia under Sukarno and in the Philippines during Marcos' martial-law years. Thailand, which ironically has had a number of undemocratic political regimes, has been able to sustain high growth rates by allowing its economy to operate in greater freedom. Malaysia, which has had uninterrupted democratic rule since independence, engaged in economic interventions. These interventions, however, were much milder and its government was careful not to allow them to substantially distort market incentives.

2. Liberal economic policies are likely to stimulate growth in the economy. The most recent example was Thailand's phenomenal GDP growth rates from 1986-89, achieved after liberal investments and trade policies were instituted. In the Philippines, decontrol in 1961 was greeted by two years of economic expansion, largely the result of a positive agricultural export response to more liberal exchange rate policies. Unfortunately, a

protective tariff policy and the gradual overvaluation of the exchange rate due to sustained government deficit, negated these in time.

3. While the growth of industrial sectors received more attention from the governments of all four countries, the countries did not neglect their agricultural sectors. Malaysia and Indonesia have subsidized particular areas of their agricultural sectors, and have invested heavily in raising agricultural productivity. Thailand, even while enjoying a great measure of comparative advantage in agriculture, has invested substantially in irrigation and infrastructure to further improve agricultural productivity. Even the Philippines, with its rice self-sufficiency program, devoted substantial sums towards raising agricultural productivity. These policies indicate a more balanced approach to economic development.

4. Industrial protection, while perhaps necessary in the early stages of establishing domestic industries, is not an effective long-term strategy for growth. Protection limits the industrial sector's growth by limiting its market to the domestic market. The irony is that while protection makes domestic goods more competitive in the domestic market, it makes these protected goods and previously exported goods less competitive in international markets.[39]

5. The foreign exchange rate exerts a powerful influence on sectoral incentives and flow of resource between sectors, especially for the traditionally more export-oriented agriculture sector of these four economies. While episodes of severe exchange rate overvaluation were not intended to discriminate against agriculture the tendency to deal ultimately with the fiscal imbalance crisis through exchange rate rationings played a key role in repressing agricultural development, especially in the Philippines. The Philippines, in particular, had a more severe and enduring case of resorting to foreign exchange rationing instead of price adjustments when faced with these problems. This difference, ultimately, is pointed out by studies of Philippine development as the cause of the country's more disappointing development performance in the region.

6. There are valid economic reasons for the government to intervene in the economy. The provision of public goods (e.g., irrigation, roads, communication infrastructure) is a vital government function supportive of economic growth. Malaysia is a case in point, where excellent transport and communication systems have been a strong factor in its ability to attract foreign as well as domestic investments. Another area for government intervention is in environmental protection. Thailand's unbridled capitalism in the second half of the 1980's brought about pollution and other environmental degradations that threaten the quality of life in spite of economic prosperity (Handley, 1991).

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[39] Protection lessens international competitiveness in two ways. One is by the increased costs of production brought about by inefficient use of resources; the other is by its effect on the exchange rate. Protection leads to an overvalued exchange rate. Bautista (1987, p. 56) estimated that trade protection has overvalued the real exchange rate in the Philippines by as much as 156% during the period of foreign exchange and import controls (1950-61).

7. There are also valid political reasons for government to intervene in the economy. A political system is a social contract, without which no economic system can thrive. An economy can only thrive in a safe and secure environment. If that political system is threatened by some attendant results of economic growth, then the government must step in. Malaysia's pursuance of the NEP provides a good example of how vital this function is. The NEP defused the racial tensions threatening to break the country apart in the late 1960's. It did so, however, without sacrificing growth and prosperity, by carefully selecting and implementing policy instruments that were least intrusive of private enterprise.

8. Increasing trade restrictions and interventions to deal with foreign exchange problems must be avoided. External imbalances usually emanate from fiscal and monetary mismanagement as the history of the ASEAN countries illustrate. Increasing trade restrictions only lead to further production distortions that are often at odds with declared sectoral policy objectives.

In summary, the lessons from successful development policies reveal that government interventions should concentrate on providing public works and infrastructure supportive of the private sector initiative, and a macro environment conducive of free enterprise and competitive markets. Interventions with economic and political justifications should be carefully targeted and limited to specific markets. Perhaps what Gillis (1983) describes as macro liberalization with micro "dirigisme", for example, Indonesia under the New Order, is an appropriate paradigm for successful economic development policies. This recommends that the economy, on the whole, should be open and liberal, with only carefully selected areas for government interventions.

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