



**Strategic Framework for the  
Accelerated Economic Recovery in Asia (AERA) Initiative**

**April 5, 1999**

**This is an internal USAID Strategy Document, and contains budget and  
procurement planning information –  
NOT to be circulated outside the US Government**

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## LIST OF ACRONYMS

|         |   |
|---------|---|
| ADB     | Asian Development Bank                                |
| AERA    | Accelerated Economic Recovery in Asia                 |
| ANE/ESA | Asia Near East Bureau/East and South Asia             |
| ANE/SEA | Asia Near East Bureau/Strategic and Economic Analysis |
| CS      | Child Survival  |
| DA      | Development Assistance                                |
| DCA     | Development Credit Authority                          |
| ESF     | Economic Support Funds                                |
| IBRD    | World Bank  |
| IFI     | international financial institution                   |
| MDB     | multilateral development bank                         |
| IMF     | International Monetary Fund                           |
| NPL     | non-performing loan                                   |
| SEC     | Securities and Exchange Commission                    |
| SME     | small and medium enterprise                           |
| US-AEP  | U.S. – Asia Environmental Partnership                 |

# Strategic Framework for the Accelerated Economic Recovery in Asia (AERA) Initiative

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## 1.0 OVERVIEW

The unexpected financial and social crisis in Asia has created an unprecedented focus on the weaknesses of the Asian economies and called into question the existing architecture of the international financial system. Addressing the root causes of the crisis has become increasingly imperative after other countries, including the United States, felt the reverberations of the Asian crisis in their own economies.

Recent analyses of the crisis, along with field inquiries, indicate that among the affected countries, Indonesia, Thailand and the Philippines demonstrate the highest levels of need for USAID assistance. In response, USAID has designed the "Accelerating Economic Recovery in Asia" (AERA) initiative to help the region, and particularly these three countries, recover from the financial crisis. The initiative will help these countries address key weaknesses in their economic, governance and social systems. These weaknesses must be resolved to restore investor and bank confidence, and revive the credit and investment flows needed to revitalize business activity that will lead to economic recovery.

Recognizing that an effective response must address both the underlying causes of the crisis and resultant social impacts, as well as take steps to ensure sustainability, the initiative will achieve its objective by:

- restarting bank and business activity;
- improving transparency and accountability in banks, businesses and governments;
- establishing more effective mechanisms that alleviate the social tensions and adverse impact associated with economic adjustments.

The Initiative's five-year relief-recovery-reform agenda will begin in FY 1999, and have a total projected budget of \$130 million. The FY 1999 budget is \$35 million, comprised of \$20 million in Development Assistance funds, \$10 million in emergency Child Survival funds, and \$5 million in Economic Support Funds. The FY 2000 budget request is \$53 million.

## 1.1 Why AERA?

AERA represents an effort that should be undertaken for a confluence of reasons: (1) US national interests in a stable and prosperous Asia are served by US leadership in response to the crisis in Asia; (2) opportunities available may be lost if timely action is not taken; (3) the comparative

advantage of USAID and its partners adds value to the donor community effort; and (4) the initiative offers flexibility and the opportunity to support regional dialogue and action.

*It Provides a Unique Opportunity to Influence Change in East Asia*

- While the US has exerted policy leadership both directly and through the international financial institutions, AERA offers the US government a proactive and more direct role in the economic and political reform processes underway in Asia. AERA is a vehicle for the US government to become substantively engaged in a once in a half-century opportunity for social and economic transformation in the Asia region.

*It Adds Value to Bilateral and Multilateral Donor Efforts*

- AERA will accelerate the recovery in Asia by addressing critical needs not yet being met by both international financial institutions (IFIs) and bilateral donor programs. For example, the International Monetary Fund (IMF), World Bank (IBRD) and the Asian Development Bank (ADB) responded quickly with significant loans to the targeted countries. The funding is directed at helping the countries meet budgetary or foreign exchange needs in return for numerous economic policy and institutional reforms. However, the countries still need considerable technical assistance and training to effectively implement many of these reforms. The AERA initiative will add value to overall donor efforts by strategically providing the needed technical assistance and training, and thus accelerate the implementation of policy, regulatory and institutional reforms.

*It Supports US National Interests*

AERA demonstrates US concern for its Asian allies, while at the same time supporting the US national interest of economic prosperity. It contributes to several foreign policy goals cited in the International Affairs Strategic Plan, including:

- opened markets to increased trade and free flow of goods, services, and capital. AERA activities should have a positive impact on US exports that declined in the targeted countries by 29 percent in the first ten months of 1998.
- increased global economic growth and stability, and
- broad-based economic growth promoted in developing and transitional economies.

*It Offers Flexibility and Supports Regional Dialogue*

- AERA offers USAID a flexible mechanism for allocating resources according to evolving country needs.

- AERA creates an opportunity for regional collaboration and the sharing of lessons and best practices across countries, the promotion of regional banking and capital markets standards, and potential efficiencies in program implementation through better coordination and economies of scale.

## **1.2 Why USAID?**

USAID has led the design of AERA, and is ideally suited by experience, expertise and contacts to implement the initiative. USAID has:

- a long and productive history working with governments and relevant NGOs in Thailand, Indonesia and the Philippines;
- expertise in providing world class technical assistance and training that can complement IFI development loans and modest technical assistance;
- extensive experience supporting civil society involvement in public sector reform;
- ongoing collaboration with, and ready access to, expertise in USG agencies (i.e. State, Treasury, SEC, Commerce, etc.) and private organizations that bring special skills and knowledge;
- solid experience working collaboratively with other donors, especially the IFIs; and
- experience developing partnerships that can sustain economic and institutional reform efforts.

Under the AERA initiative, USAID will help foster inter-sectoral partnerships within countries, partnerships between US and Asian government and private sector organizations and businesses, and regional partnerships among Asian countries. These partnerships will serve to strengthen organizational clout, promote the transfer of knowledge, and create linkages that will last beyond the end of AERA funding.

## **1.3 Why Five Years?**

At the outset of the Asian financial crisis, conventional wisdom believed it to be a rude, but brief “reality check” for the region that would resolve itself in a few months with the help of the IMF, IBRD, ADB and others. Today, the crisis is well into its second year. Now conventional wisdom believes it will take years and possibly more than a decade to restore economic growth in the region, especially in Indonesia..

The relief-recovery-reform agenda of AERA is designed to help put the targeted countries on the road to sustainable economic recovery. While the AERA initiative will demonstrate short-term results, its principal emphasis is to create and strengthen local capacity and foster regional partnerships within a five year period that can sustain continuing reform efforts. Building capacity and partnerships will take an estimated five years.

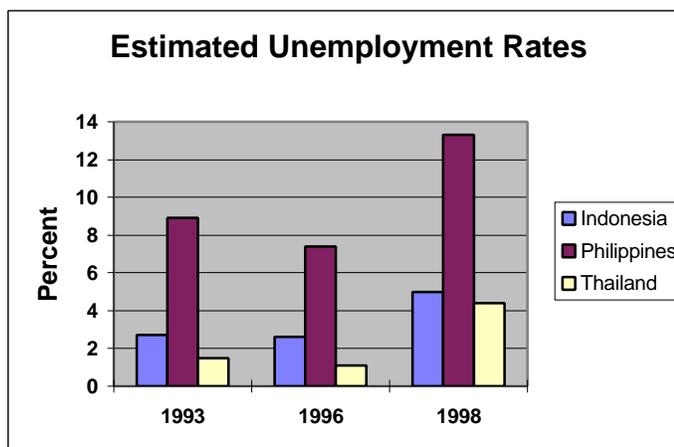
## 2.0 STATEMENT OF PROBLEM

Three decades of remarkable growth ended for the East Asian countries during the summer of 1997. The region's phenomenal growth was fueled by foreign and domestic capital that was attracted to liberalized capital and financial markets, high domestic interest rates and pegged exchange rates that seemed to offer investors the highest, and most certain rates of returns.

However, despite the large capital inflows, the financial and capital markets in East Asia remained poorly developed, regulated and supervised. Government policies intended to liberalize investment and stimulate trade combined to encourage short-term borrowing over long-term investments. By the mid-1990s, the East Asian countries had run up billions of dollars in short-term debts that vastly exceeded their levels of liquid foreign-exchange reserves.

By mid-1996, investors and lenders were becoming uneasy about their exposure in the region. They could see the quality of investments declining, export growth and earnings slowing down, and over-capacity growing in many sectors. In response, many began to scale back new investments and lending in the region. However, their prudent retreat turned into a full scale rout in mid-1997 when Thailand failed in its defense of the pegged exchange rate amid pronouncements by respected international financial experts that it faced severe financial problems and needed to take immediate and drastic measures.

Weaknesses originally identified in Thailand were soon evident elsewhere in the region. Within six months, capital flows to the region reversed by more than \$100 billion dollars, forcing companies and banks to close and putting millions of workers out of jobs, and requiring millions more to work fewer hours and for lower wages. Indonesia was the hardest hit. The economy contracted 14 percent in 1998, inflation hit 60 percent, and an estimated 30 million people were pushed into poverty (earning less than \$1.00/day). In Thailand, the economy contracted about 8 percent in 1998, and the number of unemployed went from half a million to two million as thousands of businesses went bankrupt. The Philippines was less affected, but still hurt as its economic growth stagnated and unemployment increased from 8 to 13 percent.



The social impact of the financial crisis goes well beyond stagnant growth and increased unemployment in these three countries. Reduced government revenues have forced cuts in essential public services. Health and education programs have been particularly hard hit. For example, in Indonesia and Thailand, more than 6 million students have dropped out of school, and in the Philippines, childhood vaccination programs will reach only 50 – 60 percent of the

target population. In all three targeted countries, there is now evidence of increasing crime and violence, as well as ethnic tension and stress on families, as communities and households struggle to cope with hard economic times.

While the initial financial panic in East Asia appears to have ebbed, numerous obstacles still remain in the path to positive and sustainable economic growth. All countries have massive banking and corporate debts, and a wide variety of economic governance problems. Bad debts must be written down, inappropriate financial policies must be corrected, and weak financial institutions strengthened. Equally, if not more important, the East Asian countries must also continue their transition to more accountable, transparent and democratic governance in order to compete in world markets for long-term investment capital. According to Davos Economic Forum’s annual Global Competitiveness Report, the quality of government institutions in East Asia lags behind most major developing countries. The lack of judicial independence and extensive business-related bribes were highlighted as particular problems. Although these political and institutional problems did not cause the crisis, they will be a major drag on the return to sustainable growth, and may lead to setbacks in reform.

**3.0 STRATEGIC GOAL AND OBJECTIVES**

The strategic goal of USAID, other donors and the affected countries is:

**Sustainable Economic Recovery Attained in East Asia.**

Donors and affected countries agree that achieving this goal, particularly in Indonesia, Thailand and the Philippines, depends upon restoring banks and companies to financial soundness and strengthening systems for economic governance while minimizing human suffering. Thus, economic recovery will be achieved when countries can sustain positive rates of economic growth, enjoy public and private confidence in the economy, and have in place appropriate mechanisms that can more effectively and appropriately respond to future economic crises.

Attaining economic recovery requires the revitalization of economic activity hardest hit by the crisis -- output and jobs in sectors such as manufacturing and services must be restored. For firms to rehire workers and increase output, they must have access to credit and investment capital, both domestic and foreign. Before significant credit and investment become available, however, bank and investor confidence must be restored. Because this is the key to attaining economic recovery, the principle objective of the AERA initiative is to:

**Restore Bank and Investor Confidence.**

These three elements: restoring bank and investor confidence, increasing domestic and foreign investment, and revitalizing economic activity are mutually supportive and reinforcing. For example, revival of economic activity contributes to increased confidence, which in turn, leads to further lending and investment.

Recent experience shows that no single donor or approach sufficiently addresses the range and magnitude of issues necessary to restore bank and investor confidence and restore economic activity. By working together, affected countries and donors can achieve this objective and goal.

“It is apparent that the social problems of this crisis are too big for one country to address alone”  
Prime Minister of Thailand,  
Chuan Leekpai, January 21, 1999.

To restore bank and investor confidence, the AERA initiative will support the achievement of four intermediate objectives.

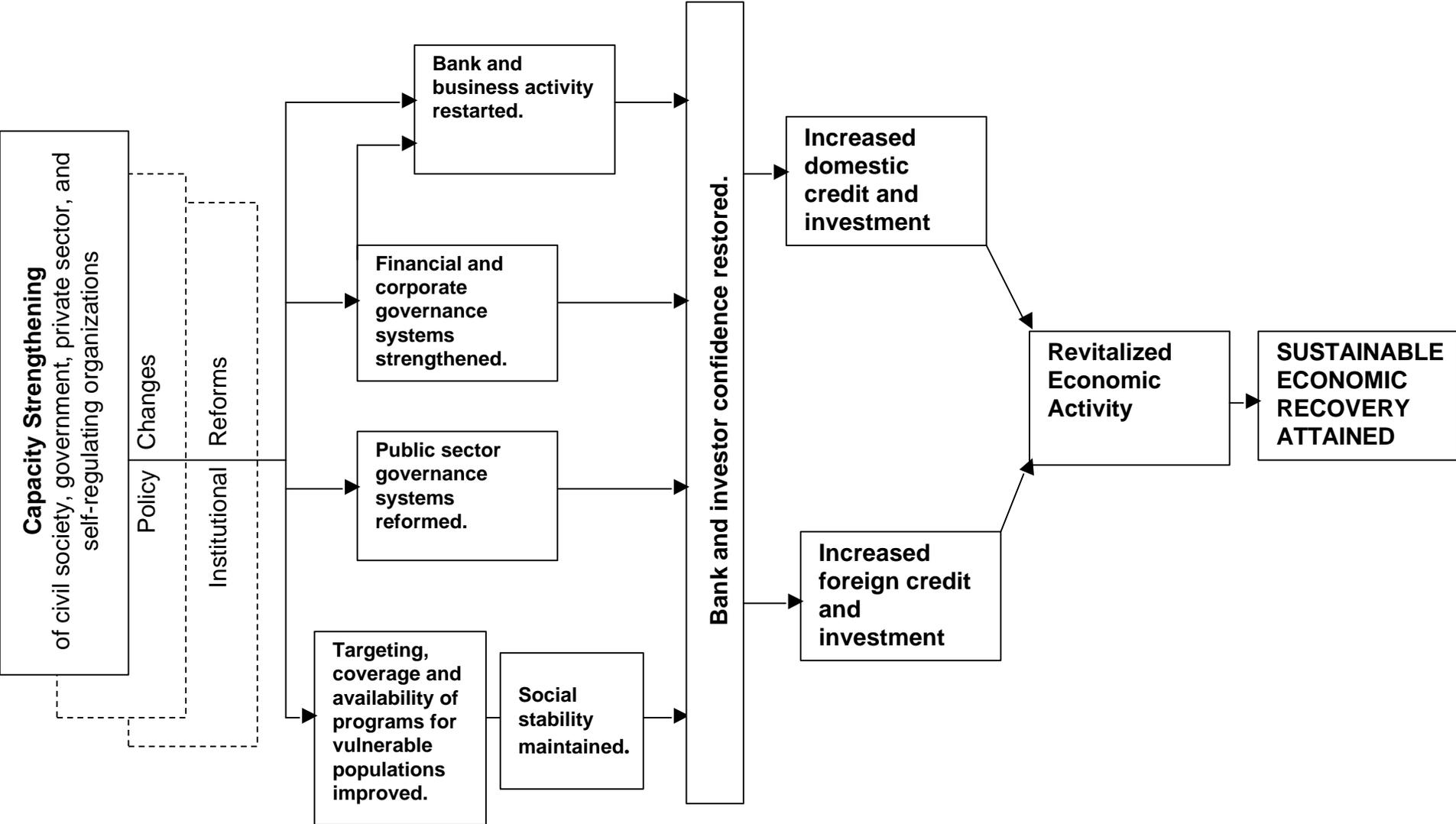
- 1. Bank and business activity restarted.**
- 2. Financial and corporate governance systems reformed and strengthened.**
- 3. Selected public sector governance systems reformed and strengthened.**
- 4. The targeting, coverage, and availability of programs for vulnerable populations improved.**

These four areas are crucial to improving the investment environment because they address the problems of stalled productive sectors, underdeveloped financial regulatory and monitoring systems, perceptions of corruption, and concerns regarding social stability, particularly in Indonesia.

AERA will concentrate its efforts on building the capacity of banks, companies, relevant business associations, government agencies and civil society organizations to implement policy and institutional reforms associated with each of these areas.

Under each of these objectives, AERA supported activities will achieve specific results that will, in combination with other donor and country efforts, contribute to the region’s economic recovery. The logic of this effort is shown in Figure 1.

Figure 1. Strategic Framework



AERA's expected results must be viewed in the context of USAID's own bilateral programs in Indonesia and the Philippines which have been re-oriented to focus on crisis response, and the overall involvement of other donor and host country institutions. The AERA initiative is specifically designed to complement ongoing IFI activities which include economic and financial adjustment, public sector reform, financial markets reform, and support for the social sectors. These IFIs also provide some grant funds for technical assistance and training. However, this assistance is generally modest in scope, specialized, and of short duration. AERA will add value to these efforts by providing long and short-term, grant funded technical assistance and training that reinforces and accelerates the implementation of IFI supported policy changes or addresses other unmet priority needs.

Thus, while each partner can rightly claim to be fully engaged in helping Asian economies work out of the financial crisis and reach a more sound footing, each recognizes that USAID has a special role to play because of its experience, access to a wide range of expertise relevant to the crisis' special needs, and its ability to finance technical assistance and training with grant funds.

### **Critical Assumptions to Achieving Success**

- The global financial system will remain sufficiently stable to support recovery in the affected countries.
- Political will among donors and affected governments will continue to support the region's recovery.
- Political stability in the three countries, particularly Indonesia, will continue.
- The countries will remain sufficiently competitive in the production of goods and services.
- USAID bilateral missions will continue to receive funding needed to fully implement approved crisis response strategies in FYs 1999 and 2000.

#### 4.0 OBJECTIVES, EXPECTED RESULTS AND ILLUSTRATIVE ACTIVITIES

The impacts of the crisis have gone far beyond the Asian financial sector. Capital flight and the closure of banks have paralyzed the financial systems in the region. Corporate access to investment and working capital has virtually disappeared, forcing thousands of companies to cut back on production or close. As a result, millions of workers have either lost their jobs or seen their wages and hours cut. The crisis also has impacted US businesses and jobs.

As described above, the AERA initiative will support selected activities organized around four ambitious intermediate objectives: restarting bank and business activity, strengthening financial governance systems, reforming selected public sector systems, and improving the targeting, coverage and availability of social programs for vulnerable populations.

The Asian economic crisis, which erupted in mid-1997 on the tail end of local currency depreciations, has been suspected of affecting U.S. trade, and ultimately the U.S. economy. Indeed, many American corporations reported lower than expected earnings and even losses, attributing these results to Asian demand contractions and domestic price suppression. *In California alone, it has been estimated that over 140,000 export related jobs have already been lost since the crisis began.* The lion's share of the blame is tied directly to the weakened buying power of the Asian community.

"Has Depreciation of Asian Currencies Affected US Trade?", 1999. ExportLinx.com

#### 4.1 Expected Result: Bank and business activity restarted.

The key to re-energizing economic activity and saving or creating jobs is to stimulate demand, investment, and production. Governments, with the assistance of the IFIs, have committed hundreds of millions of dollars to large-scale public works programs designed to provide needed infrastructure, generate productive short-term employment, and stimulate economic demand. While these projects can generate thousands of temporary jobs, they are no substitute for private sector-led growth. The AERA initiative focuses on reinvigorating the private sector by helping restore the flows of credit and capital needed for broader-based economic recovery.

One approach to restarting bank and business activity is to help domestic banks and businesses restructure and work out the billions of dollars worth of non-performing loans (NPLs). Most businesses in the region have outstanding loans that exceed their capital bases, some by several times. Helping these businesses and their respective banks restructure and reschedule these loans so that at least a percentage can be repaid will help restore investor confidence and restart business and banking activity.

Governments in all three countries have encouraged voluntary workouts of NPLs. While this approach has met with some success, the overall effort is impeded by banks' incomplete knowledge of corporate clients' financial situations, the lack of skills in restructuring and weak legal sanctions. The eventual passage of stronger bankruptcy laws will add a needed stimulus to this process, but must be accompanied by training and technical assistance to banks and

corporations. The AERA initiative will help build local capacity in corporate and bank restructuring and provide the training and technical assistance to bankers and corporate executives that is essential to the accelerated write down and repayment of NPLs.

Many small- and medium-sized enterprises (SMEs) face a different situation. These companies have traditionally served as the principal engine of economic growth in the region, employing more than 50 percent of the urban labor force and quickly adapting to changing market conditions and needs. Many SMEs are not saddled with large debts as their larger counterparts, but have lost markets and cannot access critical working capital because the finance company or bank they borrowed from is bankrupt. In Thailand and Indonesia, the government has closed virtually all finance companies and most banks in an effort to stabilize their financial sectors. The banks remaining tend to be larger and better capitalized, but have almost no tradition or experience lending to SMEs.

The AERA initiative proposes a second approach to restarting business activity - stimulating SME growth. To achieve this, the initiative will nurture bank-SME relationships by improving the banks' capacity to judge prospective SME clients and accurately assess the associated risks, and strengthening the capability of SME executives to prepare business plans and loan proposals that banks can use to assess the merits and risks of their business. The initiative also will support innovative efforts improve access to capital, technology and markets through linkages to US businesses.

Finally, in the case of Thailand and the Philippines, the banking sectors still possess considerable liquidity. While much of this liquidity is needed to meet current debt obligations, there may be an opportunity to stimulate lending of working capital to SMEs provided the risks could be reduced. One means to lower that risk is through credit guarantees. USAID will soon have authorization to implement credit guarantee programs under the Development Credit Authority. If further analysis demonstrates that banks would lend to SMEs if provided credit guarantees, USAID is prepared to design a pilot DCA guarantee program in either Thailand or the Philippines, especially if the guarantees could accelerate corporate debt restructuring. Within one to two years, Indonesia banks and businesses may also be in a position to benefit from such credit guarantees.

#### *Illustrative Activities:*

Based on the rationale described above and country-specific analyses, AERA will support the following types of activities over the next two years that represent immediate needs, and complement existing bilateral and multilateral donor programs.

AERA will provide assistance and training to improve bankers' skills in risk assessment and management and credit analysis in Indonesia as well as Thailand, and provide additional assistance in the workout of NPLs in Thailand.

To complement ongoing work to foster private debt workouts undertaken by the Indonesia mission, the initiative will also provide assistance and training to local corporations on how to restructure their debt, strengthen their ability to negotiate bank workouts for problem loans, and

facilitate debtor/creditor agreements in targeted sectors like food processing, manufacturing and services in Indonesia and Thailand.

To stimulate SME growth, the initiative will provide training to SME executives on ways to analyze and improve the profitability of their businesses, and to develop business plans and loan requests that will facilitate access to credit facilities. In Thailand the Philippines, the initiative will support pilot programs that link SMEs with export markets and potential US partners.

*Results Expected and Proposed Indicators:*

USAID expects that through its assistance and training to banks and corporations, AERA will accelerate the end of the credit crunch in the targeted countries. With AERA assistance, the proportion of NPLs to total loan portfolios will be significantly reduced over the next five years. USAID also expects that SME business activity will expand significantly over the next three years through improved access to working and investment capital, technology and markets.

Proposed indicators to measure the progress of these activities include the ratio of NPLs to total loan portfolio, the number of banks and corporations restructured or in the process of restructuring, and the level of bank lending to SMEs.

#### **4.2 Expected Result: Financial and corporate governance systems reformed.**

To restore investor confidence, the countries in the region must confront the lack of transparency and accountability in their financial and capital markets, inadequate protection of minority shareholder rights, and very weak systems for adjudicating bankruptcy that contributed to the rush to withdraw capital from the region. To date, most IFI programs have focused on strengthening policies and regulations that govern the operation and oversight of financial and capital markets. While these new policies are essential, they are not sufficient if the organizations mandated to implement the policies do not have the requisite institutional capacity or capability. Other donors, especially the IFIs, repeatedly identified this problem as one reason for the slow progress in implementing critical reforms.

“If your domestic institutions are strong, then you don’t need very strong global institutions. If domestic institutions are weak, it won’t matter how strong your global institutions are. They will not be effective.

*The more accountable and open your governance, especially as an emerging market, the less likely it is that your financial system will be exposed to surprises, the easier it will be for you to improve and adapt when it is, and the more legitimacy your government will have to share the pain when change is required.”*

Bob Hormats, Vice Chairman, Goldman Sachs International.

USAID will focus a significant portion of AERA resources to improve both bank and corporate governance. It will follow a four-pronged approach that: (1) encourages the adoption of international accounting standards by both banks and publicly listed companies; (2) strengthens the role and capacity of government regulatory agencies that oversee bank and stock market

operations; (3) bolsters the roles and operations of self regulatory organizations like stock exchanges and associations of accountants and auditors; and (4) accelerates the implementation of new/revised bankruptcy laws and improves the capability of judges to adjudicate bankruptcy cases. By centering technical assistance and training in each of these areas, and helping establish partnerships between these organizations and their counterparts in the US, AERA will complement ongoing donor efforts and accelerate the implementation of reforms that govern the operation of financial and capital markets.

*Illustrative Activities:*

In all three countries, the initiative will provide technical assistance and training to improve bank and corporate accounting and the adoption of internationally accepted accounting standards.

In Indonesia and Thailand, AERA will provide assistance and training to improve the central banks' ability to supervise the banking systems in their respective countries.

In Thailand, AERA will provide technical assistance and training to improve the SEC's operations and regulation of capital markets, and work with stock markets in all three countries to strengthen the enforcement of disclosure requirements for publicly listed companies, and more clearly specify and enforce the roles and responsibilities of corporate directors.

AERA will support the reform and implementation of key commercial laws that govern bankruptcy and foreclosure in Thailand and the Philippines, and help develop and implement systematic banking regulatory reforms, and a regulatory framework for micro-finance institutions in the Philippines.

Finally, AERA will support training programs and study tours for judges from all three countries to expose them to best practices for the speedy adjudication of bankruptcy cases, and follow up with technical assistance in how these best practices could be applied in their respective country.

*Results Expected and Proposed Indicators:*

Through its advisors and training programs, AERA will help strengthen central banks' ability to supervise and monitor banking systems in their respective countries. USAID expects that with its assistance, central banks will be better equipped to identify and intervene when banks get into trouble, and thus minimize the likelihood of future banking crises.

Through its technical assistance and training to government regulatory agencies and self-regulating organizations such as associations of accountants and auditors, stock exchanges and banking associations, banks and publicly listed companies will meet international standards for transparency and accountability within three to five years.

The training and technical assistance to improve the adjudication of bankruptcy cases is expected to have two impacts within the next two years: it will contribute to a greater number, and quicker voluntary debt work outs between banks and companies; and it will result in the

development and implementation of procedures that result in actual bankruptcy cases being adjudicated in a timely manner in the courts.

The combination of strengthened supervision of banks and stock markets, the institutional capacity of banks and firms to adhere to financial and capital market requirements for transparency and accountability, and improved protections for lenders and minority shareholders will help create an environment conducive to investment and lead to revitalized economic activity in the region.

Various qualitative and quantitative indicators may be used to measure progress in these activities. Measures of the quality of bank supervision or the improvement in disclosure requirements are two proposed indicators. In addition, USAID may measure the number of AERA-supported institutions that adopt internationally accepted accounting standards.

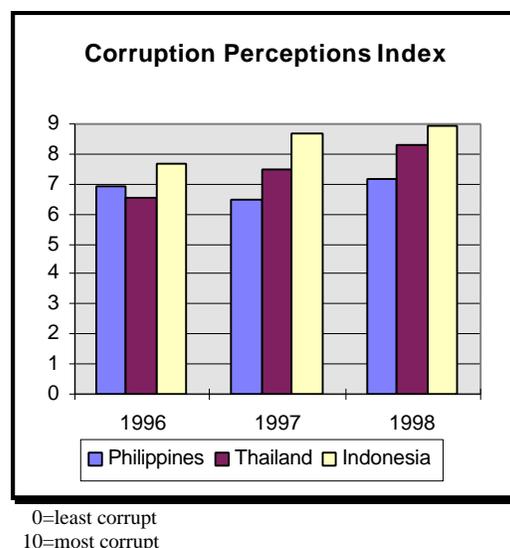
#### 4.3 Expected Result: Selected public sector governance systems reformed.

Prior to the current financial crisis, strong economic growth in the region encouraged people to overlook corruption and waste in government operations. However, foreign investors perceived a growing problem (See Figure 2). The region's economic downturn presents a unique opportunity to push reforms as tolerance for collusion, nepotism, and corruption has evaporated in tandem with economic prosperity. Today, many business and civil society groups are calling for reforms that will result in greater transparency and accountability in public and private sector affairs. Yet for the most part, these calls lack cohesion.

Past successes and failures in public sector reform have highlighted the importance of mobilizing demand for reform in tandem with providing technical assistance to government institutions. Working with government agencies responsible for activities where the need for transparency is particularly acute, such as procurement, customs, and tax collection, will help restore both domestic and foreign confidence in the economy. For lasting change, it is critical to foster public-private partnerships that can guide and sustain reform efforts. Civil society organizations can perform important analytical, advocacy, and monitoring functions to undergird reforms that limit the discretion of government officials, enhance the effectiveness of checks and balances, and professionalize the civil service.

Donors, at present, are focusing considerable attention on reforming public sector organizations - especially those that have a direct role in combating corrupt practices. Current efforts by the IBRD, ADB, and others include strengthening oversight agencies like supreme audit authorities,

Figure 2



national planning and anti-corruption institutions, and promoting the independence and capacity of judiciary bodies to prosecute corrupt acts. However, most of these programs overlook the potential role of civil society in the reform process. Thus, USAID proposes to focus part of its resources on helping to foster public-private partnerships in governance reforms. This entails working to expand and strengthen the capacity of civil society organizations to analyze, identify, support, and monitor of key public sector governance reforms while working with select government institutions to implement these reforms.

*Illustrative Activities:*

AERA activities will expand upon ongoing bilateral activities in Indonesia and the Philippines, and support new work in Thailand, to help improve the analyses and coordination of anti-corruption approaches by accountability organizations. Part of this effort will involve helping organize coalitions between civil society organizations and business associations to analyze, identify, push for and monitor specific reforms of government operations (i.e. procurement and customs). The program will also support efforts to improve the understanding of, and the quality of reporting on, reform efforts by public media by working with the press, academic institutions, and other civil society organizations.

The initiative will expose key government agencies to best practices in public sector governance from other countries, and help develop the capacity to implement such practices. To improve transparency and accountability in governments in the region, the initiative will support training and technical assistance to improve public procurement procedures and practices in Indonesia and the Philippines, support legal and regulatory reforms in Indonesia, and support efforts to professionalize the adjudication of commercial law in the Philippines.

To share lessons across the region, the initiative will support comparative analyses of country-level counter corruption reform efforts, and study travel and regional workshops to expose government and civil society representatives to best practices and to identify strategies for effectively addressing priority anti-corruption interventions.

*Results Expected and Proposed Indicators:*

Through AERA-supported activities, USAID expects to see: (1) greater transparency in specific government procedures such as procurement; (2) improved accountability of government offices and officers; and (3) a greater role for organizations and coalitions of “watchdogs” (NGOs and the media) that will maintain pressure on public institutions. These three changes will contribute to a perception of decreased corruption in the targeted countries, which will in turn promote domestic and foreign investor confidence.

To assess whether the activities contribute to more transparent and open selected government procedures, the percent of government procurements conducted under competitive procedures, for example, may be used as an indicator. In addition, a qualitative judgement of the governments’ implementation of reform agendas could be used to measure progress in these activities.

**4.4 Expected Result: Targeting, coverage and availability of programs for vulnerable populations improved.**

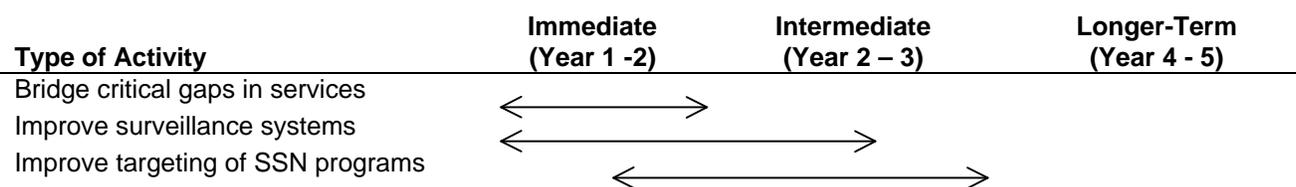
The sustained high rates of economic growth, particularly in Thailand and Indonesia, over the past twenty years resulted in higher standards of living and improvements in education and health. However, in spite of these genuine gains, the crisis has sharply highlighted major gaps and weaknesses in social systems that still exist.

Governments and donors responded to the crisis quickly, committing billions of dollars to maintain social stability and ensure the continued access to basic health and education services by those most affected. However, both governments and the donor community have expressed concern that these funds are poorly targeted, potentially wasting precious resources and missing some affected segments of society. Analyses carried out in all three countries revealed that current surveillance efforts fail to adequately inform governments and donors alike about whether investments are reaching the most affected populations. This is due to both unreliable and infrequent data and the poor linkage of data collection and analysis with targeting decisions. This information problem has hampered efforts to improve the targeting of existing resources and to develop more effective near- and longer-term social safety nets mechanisms.

In addition to this information gap, discussions with governments, USAID missions, US embassies and other donors also highlighted the need for additional resources to help bridge critical gaps in the present supply of social services, especially directed at gaps in maternal and child health care. The crisis has forced governments to trim budgets and cut programs that have long-term health and social implications in order to meet more pressing short-term needs. In response to this problem, USAID received a special allocation of \$10 million in Emergency Child Survival funds for AERA in FY 1999 to help bridge critical gaps in health and nutrition programs for children.

The AERA initiative proposes a three-tracked approach to achieve the expected result. In the short-term, it will partner with donors, NGOs, local universities and governments to improve surveillance information and its linkage to targeting decisions, and help bridge gaps in critical services. Over the longer-term, the initiative will work with other donors, governments and NGOs to design more effective and responsive longer-term social safety net mechanisms.

These activities will help address the cuts in public health expenditures that have both increased costs and reduced services provided through public health facilities. It will also help protect gains in health and nutrition made by these countries over the past decade, particularly ones that have longer-term impact on the development of human capital.





*Illustrative Activities:*

AERA will support a set of activities to build upon efforts by the missions in Indonesia and the Philippines to strengthen social programs for vulnerable populations, and to address targeted needs in Thailand.

To improve the targeting of social sector programs, AERA will provide technical assistance to strengthen epidemic or nutritional surveillance systems in the Philippines and Indonesia.

To bridge critical gaps in health and nutrition programs, AERA will: (1) fund Vitamin A supplementation and expand the Integrated Management of Childhood Illnesses (IMCI) programs in Indonesia and the Philippines; (2) support an expansion of maternal and child multi-vitamin and micronutrient supplementation programs in Indonesia; and (3) in Thailand, link with US disease research experts and the Royal Thai Government to develop and disseminate improved methods to control the spread of drug resistant malaria. This will bridge a critical gap in malaria prevention caused by a crisis-induced cuts in government funding.

In the longer term, AERA will partner with other donors, governments and NGOs to help design more effective and responsive longer-term social safety net mechanisms, such as unemployment insurance, pension programs, and targeted health and education subsidies. Specifically, AERA will work at a regional level to support analyses and dialogue both within and among countries on appropriate long-term social safety net mechanisms. This could include analyses on the estimated fiscal and employment impact of unemployment insurance, modified pension plans, health insurance and other social net mechanisms, and summaries of best practices from around the world to provide sounder, and more responsive social safety nets.

*Expected Results and Proposed Indicators:*

While its resources are limited, USAID expects that bridging gaps in health services will provide immediate relief to those most affected by the crisis. Improving the targeting of social services will translate into more effective use, and less waste, of government and donor resources. More significantly, better targeting of social services will lead to improved public perceptions of their governments' fairness in the allocation of funding for social programs. Both the immediate relief and increased perception of fairness will contribute to the maintenance of social stability, which is necessary to re-attract both foreign and domestic investors.

Furthermore, USAID expects that its support for more effective and responsive longer-term social safety net mechanisms will translate into better capability in the targeted countries to cope with future economic downturns.

Various indicators have been proposed to measure progress in improving the targeting and coverage of programs for vulnerable populations. These include: (1) service utilization or

services provided to pregnant women and children, (2) the number of policy decisions on targeting of maternal/child health programs made using information provided from surveillance systems improved by USAID assistance; and (3) vitamin A capsule coverage for children aged 6-59 months in targeted areas.

## **5.0 COMPLEMENTARITY WITH OTHER PROGRAMS**

### **5.1 Other Donor Programs**

The region's economic recovery cannot be attained through the efforts of any one donor institution working in isolation. Given the magnitude of the challenges, donors must cooperate and develop a concerted response that effectively utilizes the comparative advantage of each institution. USAID has followed this approach in designing AERA. As the crisis is now in its second year, USAID has focused the AERA design on activities where the US can mobilize particular skills that support and complement efforts already being undertaken by the wider donor community.

The IFIs have taken the lead in responding to the crisis in each of the three targeted countries. For example,

- In Thailand, the IMF committed \$4 billion as its contribution to the initial bail-out program. IBRD commitments now exceed \$700 million for economic and financial adjustment with another \$600 million in the approval process. The IBRD also has committed \$700 million for public sector reform and social investment. The ADB has approved \$500 million for a social sector program loan and \$300 million for financial markets reform.
- In Indonesia, the IMF has committed over \$11 billion in return for economic reforms. The IBRD extended a \$1 billion structural adjustment loan, and redirected approximately \$441 million of its existing loan portfolio to meet social sector needs. The ADB has a \$300 million social protection sector development loan targeted to six provinces in Indonesia, and a \$1.4 billion policy loan to support the country's financial governance reforms program.
- In the Philippines, the IBRD has committed \$600 million in new crisis response loans to complement its on-going projects and budgetary social sector support loans. The Philippines extended and augmented its existing IMF-supported program in 1997 and arranged a stand-by facility in 1998 of more than \$1 billion.

While these are significant sums, virtually all multilateral funding is directed at helping countries meet budgetary or foreign exchange needs in return for new or modified economic policies. These loans are stimulating needed changes in laws, supervisory and regulatory frameworks, the creation of new accounting and disclosure requirements, and the reduction of taxes and other economic distortions for corporations. In the social sectors, funds are being used to maintain budgetary expenditures and design improved education and health strategies. However, there exists a need for considerable technical assistance and training to support these efforts. Both the

IBRD and the ADB have extended loans and grants for technical assistance, but the amounts are relatively small in relation to the needs, less than \$40 million total for all three countries since the beginning of the crisis. In Thailand, the ADB has provided \$4.5 million in technical assistance grants while the IBRD has made available \$30 million in technical assistance loans. In Indonesia, the combined grant funds for technical assistance being provided by the IBRD and the ADB total less than \$3.0 million.

The AERA initiative brings welcomed grant-funded technical assistance and training to complement these IFI programs. For example, where the IBRD is aiding the Bank of Thailand to improve disclosure requirements and the ADB is supporting the development of policies to strengthen accounting standards, AERA will provide the technical assistance and training to accelerate the adoption of internationally accepted accounting standards by both banks and publicly listed companies. AERA also will provide assistance and training to strengthen the operation and governance of capital markets, and to help enhance the role of civil society organizations in defining and carrying out economic and social reforms. Finally, in terms of social investments, where the multilateral donors have provided loans to extend social services, AERA will support the improvement of surveillance systems and the targeting of these resources to better meet the needs of the most affected portions of society.

## **5.2 USAID's Ongoing Bilateral Programs**

The AERA initiative also complements and supports ongoing bilateral USAID programs in the Philippines (\$27.2 million in FY1999, \$39.4 million in FY2000) and Indonesia (\$75 million for FY1999 and FY2000) that have been reoriented to focus on crisis response, but are still inadequate given the magnitude of the needs.

In Indonesia, AERA complements the mission's efforts to improve governance, strengthen social safety nets, and stimulate economic recovery. For example, while the mission, in conjunction with the Department of Treasury, is providing technical support to the Indonesia Bank Restructuring Agency and the Jakarta Initiative, key organizations involved in debt workouts, it has insufficient resources to facilitate debtor/creditor agreements. The training and technical assistance to banks and corporations provided by AERA will help fill this gap. Similarly, AERA support for accounting system reform and public-private partnerships that encourage greater transparency and accountability in public and private sector operations will complement ongoing mission support for corporate law reforms. Finally, AERA will enable the mission to expand upon its ongoing social safety net response and reach additional vulnerable populations with critical health care while strengthening the use of surveillance information by government planners engaged in targeting IFI and government social safety net programs.

AERA-supported activities in the Philippines complement the mission's efforts to strengthen and deepen financial markets, improve economic governance, and create a more transparent, accountable, and responsive national government institutions. While the mission can support policy reform to improve financial services for small enterprises, it does not have the resources to provide assistance to the financial institutions directly. AERA will fill this gap through activities to improve bankers' skills in risk management and credit analysis. Likewise, bilateral activities to strengthen stock exchange self-regulation cannot address company-level needs, which will be

supported by AERA's work to develop a strong financial reporting and monitoring system for publicly listed companies. While the mission can support activities to improve the participation, accountability, and transparency of local governance institutions, it has inadequate resources to address this fully at the national level. AERA's support to reform selected public sector governance will help expand the mission's efforts at a national level. Furthermore, the mission has resources to help increase public and private sector provision of maternal and child health and family planning services, but it cannot address the need to improve monitoring and targeting of MCH services, an activity which AERA will undertake.

## **6.0 PROGRAMMATIC AND MANAGEMENT FACTORS**

### **6.1 Resource Requirements**

Based on the analyses and discussions carried out, and supplementary to existing budgets in Indonesia and the Philippines, below is a preliminary allocation of funding for FYs 1999 and 2000. Final allocations will be made each year based on work plans, needs assessments, and the prior year's performance.

**Table 1 – Estimated Budget for FYs 1999 and 2000<sup>1</sup>**  
(Figures in Millions)

| Key Results   | Thailand      |               | Indonesia     |               | Philippines  |               | Regional     |               | Total         |               |
|---|---------------|---------------|---------------|---------------|--------------|---------------|--------------|---------------|---------------|---------------|
|   | FY 99         | FY 00         | FY 99         | FY 00         | FY 99        | FY 00         | FY 99        | FY 00         | FY 99         | FY 00         |
| 1. Bank and Business Activity Restarted                             | \$4.0         | \$4.5         | \$0.5         | \$1.0         | \$1.0        | \$1.7         | \$1.0        | \$1.0         | \$6.5         | \$8.2         |
| 2. Financial/Corporate Governance Systems Strengthened              | \$3.7         | \$4.0         | \$4.5         | \$4.0         | \$2.0        | \$4.0         | \$1.0        | \$4.0         | \$11.2        | \$16.0        |
| 3. Selected Public Sector Governance Systems Strengthened           | \$1.0         | \$2.0         | \$1.5         | \$1.5         | \$1.3        | \$3.3         | \$1.0        | \$4.0         | \$4.8         | \$10.8        |
| 4. Targeting, Coverage and Availability of Social Services Improved | \$0.8         | \$2.5         | \$7.0         | \$7.0         | \$2.2        | \$3.5         | \$0.0        | \$2.5         | \$10.0        | \$15.5        |
| 5. Additional Management Costs                                      | \$0.5         | \$0.5         | \$0.5         | \$0.5         | \$0.0        | \$0.0         | \$1.5        | \$1.5         | \$2.5         | \$2.5         |
| <b>Total</b>  | <b>\$10.0</b> | <b>\$13.5</b> | <b>\$14.0</b> | <b>\$14.0</b> | <b>\$6.5</b> | <b>\$12.5</b> | <b>\$4.5</b> | <b>\$13.0</b> | <b>\$35.0</b> | <b>\$53.0</b> |

Note: The \$35 million programmed for FY 99 is composed of \$20.0 million in Development Assistance (DA), \$10.0 million in Child Survival funds, (CS) and \$5.0 million in Economic Support (ESF) funds. The \$5.0 ESF will be programmed entirely for Thailand, and the \$10 million in CS funds will finance activities to improve the targeting and coverage of key health and nutrition services.

## Outyears

In FYs 2001 and 2002, a notional budget of \$21 million per year for AERA activities has been set. This budget assumes that both Thailand and the Philippines will be on the road to economic recovery by late FY 2000. The initiative would continue to sponsor and support some bilateral activities in these two countries, but would focus most efforts on Indonesia and regional approaches and mechanisms to strengthen economic governance and social safety net responses.

## 6.2 Programming and Implementation Mechanisms

Regional and bilateral support to be provided under the AERA initiative will be delivered through a variety of bilateral, regional and global mechanisms. Listed below are some examples of the types of mechanisms that will be used to deliver assistance and services.

- In Thailand, USAID plans to build upon the US-Thai Development Partnership that it established in 1993 with the Royal Thai Government and the Kenan Institute of Private Enterprise. This partnership led to the establishment and endowment of the Kenan Institute Asia (KIASia) to support continuing development efforts after USAID closed its bilateral program. KIASia, with its board composed of Thai and US business leaders, office in

<sup>1</sup> The funding for FY 1999 could be augmented by additional funding for a special micro-enterprise initiative.

Bangkok, and past record of proactive management of development initiatives, is uniquely positioned to help lead AERA efforts in Thailand. USAID will enter into a new cooperative agreement with KIAAsia to: (1) mobilize short-term technical assistance from its partner organizations that comprise the core of the "private sector peace corps"; (2) serve as the secretariat to the program's Steering Committee that will be established to coordinate and direct activities in Thailand; and (3) provide an administrative support base for short-term expertise from other USAID sources.

- Delivery or task orders under USAID's global indefinite quantity contract (IQC) for economic development – SEGIR – for both long and short-term technical expertise in the areas of financial and capital markets reform, corporate and bank restructuring, and accounting reform.
- Buy-in to the US-Asia Environmental Partnership to access training, business development and program management support through its existing agreements and contracts.
- An Inter-Agency agreement with the Department of Treasury for technical assistance to the Bank of Thailand for on-site bank examination training and creation of a procedures manual.
- Regional cooperative agreements and leader/associate grants with US-based NGOs to support and strengthen the capability of local NGOs and business support organizations in Thailand, Indonesia and the Philippines in the areas of good governance and SME development.
- Buy-ins to existing regional and global grants and cooperative agreements in the area of population, health, and nutrition to carry out the recommended health-related social safety net activities.
- Credit guarantees under the Development Credit Authority and the Micro and Small Enterprise Development project potentially will be used to stimulate lending to micro, small and medium sized enterprises.

USAID will transfer AERA funds directly to its missions in Indonesia and the Philippines where USAID has ongoing bilateral crisis response programs. The missions will incorporate funds originally included in AERA's budget into their budgets, and where appropriate, incorporate these funds into existing agreements with their respective host governments. Missions will use the funds to carry out activities agreed upon by both USAID/ANE and the mission. To the extent possible, the missions and the Bureau will use similar global and regional mechanisms to procure services, thereby gaining economies of scale, and fostering the sharing of lessons and synergies between the countries. Incorporating AERA funds into existing agreements with host governments offers two advantages: it provides official recognition by the respective host government for activities the program will finance, and it places responsibility for activity management in the field where it can be done most effectively.

### **6.3 Program Management**

### *Regional Management:*

The ANE Bureau will form an AERA steering committee composed of representatives from the USAID offices involved in program oversight and management (ANE/SEA, US-AEP, and ANE/ESA), and as virtual members, the AERA country coordinators. This objective of this steering committee is to ensure coordination of regional activities with country programs and resolve issues with regional program performance. The ANE Bureau also will host semi-annual program reviews to inform and solicit feedback from the larger audience of US Government and private sector partner organizations regarding AERA-sponsored and supported activities.

Overall program oversight and responsibility will reside a core team composed of two people dedicated full time to AERA management. The designated program manager will chair the ANE steering committee, act as the principal liaison with field missions and the US Embassy in Thailand for the AERA initiative, and organize the annual performance reports and information for US constituencies. The core AERA management team will be supported by staff from the various offices in ANE who will have specific AERA-related work objectives. In addition to technical, financial and procurement support from within the ANE Bureau, the AERA management team will also receive program management support that will be provided through a buy-in to US-AEP.

The Bureau will also enter into specific management agreements with its bilateral missions in the Philippines and Indonesia and with the US Embassy in Bangkok for the implementation and support of AERA funded activities .

### *Country-Level Management:*

At the country level, each participating USAID mission will decide how it will manage AERA activities. Each mission will designate an AERA coordinator who will serve as the principal point person for AERA-related communications including annual performance reporting.

In Thailand, USAID will hire a US Personal Services Contractor (PSC) to serve as the AERA program manager. In addition to overseeing all activities in Thailand, this person will be responsible for keeping the US Embassy and stakeholders informed of AERA plans and activities, maintaining excellent relationships with counterpart organizations, and coordinating the program working group meetings, quarterly program reviews and annual performance reports. He/she will be supplemented with legal, financial procurement and implementation support from nearby bilateral missions (Cambodia and the Philippines) and logistical and management support from US-AEP. In addition to the PSC program manager, there will be two groups organized to assist with program oversight and coordination. One will be an AERA working group composed of the PSC program manager, a representative from the US Embassy Economics office, and key cooperators (i.e. KIAAsia). This working group will meet on an as needed basis to review implementation plans, discuss issues and assure coordination of activities. The second organization will be a Program Steering Committee that will provide overall program direction in Thailand. The Steering Committee will review the annual work plan, carry out semi-annual reviews of program activities and performance. The committee will be composed of:

- a senior USG representative (US Ambassador or designee),
- the ANE/AA or his designee,
- a senior representative from the Royal Thai Government,
- selected representatives from key partner organizations.

*Management Cost:*

While USAID expects to fund some program support with program funds, AERA program management will impact USAID's operating expense (OE) budget, both in terms of staff time and in direct travel costs. In addition to the USAID program manager in ANE and program coordinators in each of the two USAID overseas missions, successful implementation of the AERA program will require a significant level of support from offices within USAID/W and USAID missions. In particular, the ANE Bureau Assistant Administrator and Deputy Assistant Administrator for Asia will be required to participate in periodic, senior level meetings with USG, private sector and NGO representatives, and meet with key partners and counterparts in the field. Program implementation and management will also require support from the technical, legal, financial and contract management staff within three overseas missions - USAID/Philippines, USAID/Indonesia and USAID/Cambodia (for Thailand). In total, managing AERA and maintaining excellent communication with US constituencies and partners will require an estimated commitment of eight to nine person years of staff time each year from USAID.

The estimated staff time and associated operating expenses to manage the AERA initiative are summarized in the table below.

| Category                                    | ANE Bureau     | Overseas USAID | Other USAID/W | Total          |
|---|----------------|----------------|---------------|----------------|
| OE Funded Staff Time                        | 4 - 5 py/yr    | 3.5 py/yr      | 0.5 py/y      | 8 - 9 py/yr    |
| OE Travel Cost                              | \$75,000/yr    | \$25,000/yr    | \$20,000/yr   | \$120,000/yr   |
| Program Funded Management and Support Costs | \$1,500,000/yr | \$1,000,000/yr | \$0           | \$2,500,000/yr |

py = person years

#### **6.4 Performance Monitoring and Evaluation:**

Two factors require a careful monitoring and evaluation plan: (1) joint management of AERA (USAID/W for overall management and the bilateral missions in Indonesia and the Philippines and a PSC in Thailand for implementation in their respective countries), and (2) the need to monitor and report on "goal-level" data.

AERA is part of USAID's overall regional response to the Asian financial crisis. It provides the overall framework for the bilateral USAID crisis-response strategy in Indonesia and the backdrop for the forthcoming USAID strategy in the Philippines.

The first performance report for the AERA initiative will be prepared and reviewed in calendar year 2000. This report will inform decisions on the FY 2002 budget. The missions will report on results achieved by AERA funded activities or the proportion of results attributed to AERA funding in their annual performance reports using indicators and targets that will be jointly developed with USAID/W by September 1, 1999. The Thailand program manager will report to the Bureau on results achieved there. The ANE Bureau will present an overall assessment of AERA performance in a separate report that will describe the initiative's contribution to regional recovery using "goal-level" progress and trend data from non-USAID sources (e.g., the World Bank and IMF) and the concept of "plausible association," that links AERA-funded progress conceptually to general trends in the three targeted countries.

The actual schedule and mechanisms of data collection will be worked out by the missions as part of their strategic plan and by ANE.