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Economic Development in Asia and the Pacific in the 21st Century: Issues and Challenges

by
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1. Introduction

One bright spot in the global economy in recent years has been the continued healthy growth in developing countries as a whole and in those of Asia in particular. Indeed, the success achieved, especially by the countries of East and South East Asia, in terms of economic growth during the last two-and-a-half decades is quite well-known. After the introduction of economic reforms in 1978, China also started growing at breakneck speed, and has been able to maintain such growth rate for nearly two decades now. In recent years, Vietnam also joined the club of high-growth countries. Although growth rates in countries of South Asia have been much more modest compared to the countries mentioned above, they have also grown consistently. Another important development in that region in the 1990s has been the introduction of economic reforms aimed at moving towards more liberalized or deregulated market-based economic regimes.

Along with high growth, developing countries of Asia have also achieved significant structural transformation of their economies - albeit in varying degrees. The economies (with, of course, exceptions) have become much more broad-based with lower dependence than before on agriculture or primary products. Some of the economies (e.g., Hong Kong, Republic of Korea, Singapore and more recently, Malaysia) have transformed themselves from a situation of surplus labour to one of full employment (or labour shortage).

One important development in the global economy has been the increasing degree of globalization and integration. Following are some of the indicators of this process (Khan 1994):

i. Important barriers to trade that fragmented the world market in the past started coming down during the 1980s. This has included substantial dismantling, in many developing countries, of restrictions on foreign trade.
ii. Barriers to international capital movement have been substantially reduced.
iii. Expansion of free trade within certain regional blocs (for example, the European Union and North America) has led to a fuller integration of the economies belonging to these blocs. This tendency is visible in Asia also, especially in the context of ASEAN.

One of the most significant developments in the 1990s has been the successful conclusion of the Uruguay Round of multilateral trade negotiations in December 1993 which has opened up further possibilities of trade liberalization and has brightened the prospects of long term growth in world trade. Quite naturally, this will have far-reaching implications for exports from developing countries and hence on their overall economic performance.

While the success of Asia, especially of countries in East and South East Asia, has been quite remarkable in terms of achieving high rates of economic growth, questions are sometimes raised about the sustainability of such rates in the long run. Such questions may appear real especially when one looks at the slowdown in exports and overall economic growth that many of these countries experienced in 1996. Apart from this immediate concern, as we are coming to the close of the present century and are preparing to enter not just a new century but also a new millennium, one naturally wonders what might happen to a part of the world which has been a bright spot for nearly three decades. There are of course risks in making economic forecasts which normally are based on assumptions reflecting experience in the recent past; unforeseen factors may completely invalidate the projections. Despite the possibility of such unforeseen developments, economists do of course make forecasts; and there are forecasts available outlining what the growth scenario of the world economy as a whole and that of Asia will look like in the first one or two decades of the 21st century. While the present paper will take a look at some of these forecasts, it will also examine the strengths and weaknesses of Asian economies as they are revealed currently and identify the challenges they are likely to face during the next two decades or so. Indeed, rather than concentrating entirely on mere numbers, it may be more interesting and useful to analyse the challenges involved - especially from the point of view of policy making to ensure sustained economic growth.

The paper, however, starts by looking at the global trends and trends in the Asia-Pacific region (sections 2 and 3). It then presents some growth projections in Section 4. The issues and challenges for the developing economies of Asia are analysed in Section 5. The final section tries to bring out a few messages.

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2. Global Trends

In this age of economic interdependence, the past performance or future prospects of any country (or group of countries) cannot be fruitfully discussed without due consideration to the world economy. The interdependence transmits itself through a variety of channels, e.g., trade and foreign direct investment flows. Especially important is what happens to economic growth in developed/industrial countries, world trade and commodity prices, and real interest rates. These variables are largely exogenous to developing countries in the sense that they cannot exert much influence on them. On the other hand, movements in these variables affect the developing countries in various ways, e.g., through demand for their exports, and net income from such exports. Hence, in addition to domestic economic policies, prospects of economic growth in developing countries will be strongly influenced by the international economic environment.

Data on global trends in GDP growth have been presented in Table 1. Several aspects of world GDP growth are noteworthy. First, the growth of the world economy in the 1990s has been lower than in the 1980s. This, in turn, is a reflection of the decline in growth in the OECD countries. Although they have recovered from the recessionary situation in the early 1990s, the overall growth rate has remained lower than in the 1980s. Second, the experience of the developing countries has been the opposite, i.e., higher growth in the 1990s compared to the earlier decade. Third, the performance amongst developing countries has varied sharply - the countries of East Asia (including China) being the star performers, followed by those of South Asia.

Table 1: World GDP Growth, 1981-95 (annual average growth of real GDP, percentages)

	1981-90	1991-93	1994	1995
World total	3.2	1.2	2.9	2.8
OECD countries	3.1	1.2	2.9	2.4
Eastern and Central Europe	2.1	-9.0	-7.5	-0.7
Former Soviet Union	1.0	-15.5	-12.6	-4.0
Developing countries	3.3	4.6	4.6	4.9
East Asia	7.6	8.7	9.3	9.2
China	9.9	12.3	12.2	10.2
South Asia	5.7	3.2	4.7	5.5
Sub-Saharan Africa	1.7	0.6	2.2	3.8
Latin America and the Caribbean	1.7	3.2	3.9	0.9
Middle East and North Africa	0.2	3.4	0.3	2.5

Source: ILO (1996)

Table 2 provides data on growth of world trade which has been an important aspect of globalization. It is clear that in terms of volume, world trade has grown faster during the 1980s compared to the earlier decade. While the growth rate slowed down in the early 1990s, it registered sharp increases in 1994. The growth rate in 1995 also remained substantially higher than in the 1980s. A comparative analysis of Tables 1 and 2 would indicate that since 1984 the volume of world trade has grown faster than world output. The growth of exports, especially of manufactured goods, from developing countries has been particularly rapid.

Alongside the growth of world trade, flows of foreign direct investment (FDI) have also increased sharply, especially to developing countries (Table 3). For the world as a whole, the average annual flows have increased more than threefold since the early 1980s. For the developing countries, the increase has been fivefold by 1993. It should be noted, however, that these flows have not been evenly distributed across different developing regions, and have indeed been highly concentrated in a small number of countries. The other important developments that need to be noted are the growth of globally integrated production systems characterized by the rapid expansion of intrafirm trade in intermediate products and of subcontracting, licensing and franchising arrangements (ILO, 1996).

Table 2: Growth of World Trade (Goods and Services), 1974-95
(Annual averages, percentages)

	1974-83	1984-89	1990-93	1994	1995
World total					
Volume	3.1	6.4	4.6	8.7	7.9
Value	8.9	3.0	1.2	2.1	8.0
Export volume					
Industrial countries	3.9	5.9	4.2	8.1	6.9
Developing countries	-1.9	7.3	7.6	11.3	11.0
Import volume					
Industrial countries	2.8	7.9	3.1	9.2	7.1
Developing countries	7.0	3.3	9.5	8.5	11.1

Source: ILO (1996).

Table 3: Foreign Direct Investment Inflows, 1981-94
(Annual average, in billions of dollars)

	1981-85	1986-90	1991	1992	1993	1994
All countries	50.0	155.0	154.6	162.1	200.7	212.5
Developed countries	36.0	129.0	112.7	113.2	127.6	128.3
Developing countries	14.0	26.0	40.9	48.9	73.0	84.2
Africa (%)	15.3	12.0	5.6	5.0	2.6	3.8
Asia (%)	46.2	36.0	52.4	57.3	64.1	59.6
Latin America (%)	38.5	52.0	31.2	26.6	23.0	25.5

Source: ILO (1996).

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3. Trends in the Asia-Pacific Region

It has been mentioned already that while Asia outperformed other developing regions in terms of GDP growth, the performance has varied considerably within Asia. A more detailed picture of the growth performance of selected countries of the Asia and the Pacific region is presented in Table 4. Considering the decade of the eighties and the first half of the nineties, the countries that have performed consistently well are China, countries of South-East Asia except the Philippines, and the newly industrializing countries. Philippines has, of course, been able to turn around during the last two years, and now appears to be re-established firmly on a high growth path. Compared to the NICs, China and high growing South-East Asian countries, growth in South Asia has been moderate. In India, growth suffered adversely in the early 1990s in the wake of stringent stabilization measures. However, thanks to a high growth of agriculture (helped by good monsoon and rapid growth in exports), the economy achieved a growth of seven per cent in 1995-96 and nearly seven per cent in 1996-97.

Table 4: Growth of GDP in selected countries of Asia, 1980
(Annual average, percentages)

	1980-1990	1990-94	1995	1996
Bangladesh	4.3	4.2	4.4	4.7
India	5.8	3.8	7.1	6.8
Nepal	4.6	4.9	2.9	6.1
Pakistan	6.3	4.6	4.4	6.1
Sri Lanka	4.2	5.4	5.6	3.8
China	10.2	12.9	10.2	9.7
Indonesia	6.1	7.6	8.2	7.8
Malaysia	5.2	8.4	10.1	8.8
Philippines	1.0	1.6	4.8	5.5
Thailand	7.6	8.2	8.7	6.7
Vietnam	n.a.	8.0	9.5	9.5
Hong Kong	6.9	5.7	4.7	4.7
Republic of Korea	9.4	6.6	9.7	7.0
Singapore	6.4	8.3	8.8	7.0
Papua New Guinea	1.9	11.5	-2.9	2.3

Source: World Bank (1996 a).
Asian Development Bank (1997)

Table 5: Domestic Savings and Investment in Selected Countries of Asia, 1980 and 1994 (percentage of GDP)

	Gross domestic investment		Gross Domestic savings	
	1980	1994	1980	1994
Bangladesh	15	14	2	8
India	21	23	17	21
Nepal	18	21	11	12
Pakistan	18	20	7	17
Sri Lanka	34	27	11	15
China	35	42	35	44
Indonesia	24	29	37	30
Malaysia	30	39	33	37
Philippines	29	24	24	18
Thailand	29	40	23	35
Vietnam	n.a.	24	n.a.	13
Hong Kong	35	31	34	33
Republic of Korea	32	38	25	39
Singapore	46	32	38	51
Papua New Guinea	25	15	15	32

Source: World Bank(1996a).

Two countries of Asia which are currently facing macroeconomic problems are Pakistan and Thailand. While both are faced with the problem of declining exports and large current account deficits, Thailand's problem appears to be one of sustaining the high growth achieved in the 1980s and the early 1990s. Pakistan, on the other hand, is facing more serious structural problems.

As investment is a major determinant of economic growth, it is useful to look at data related to investment (presented in Table 5). These data show that the NICs and the high-growth economies of South East Asia invested a higher percentage of the GDP than the South Asian countries. One exception amongst the South-East Asian countries is Philippines, whose GDP growth has also been much lower than others. Data on domestic savings (Table 5) show that countries investing at higher rates were also saving at higher rates. Countries like China, Indonesia, Malaysia, Thailand and the NICs were saving much higher proportions of their GDP compared to the countries of South Asia.

Over and above high rates of domestic savings, the NICs and the high growth countries of South East Asia achieved greater success in attracting foreign direct investment. Data in Table 6 show this difference quite clearly.

Another strength of the NICs and the new NICs has been the high growth of exports. Not only have they exported higher proportions of their GDP, they were also able to achieve higher rates of growth of exports compared to the South Asian countries. One should, however, note a couple of more points regarding export growth. First, compared to the 1981-85 period the growth of exports doubled in South Asia and increased threefold in the new NICs during 1986-93 while the growth remained almost unchanged in the NICs. There has thus been some 'catching up' - especially by the new NICs. Second, data for 1996 rang an alarm bell in the NICs as well as in Thailand when the growth in exports showed substantial declines (Table 7). While the decline in export growth in 1996 was particularly sharp for the NICs and some of the new NICs (e.g., Malaysia and Thailand), the countries of South Asia also suffered. And when one notes the decline in GDP growth in the NICs and new NICs in 1996, the link between this and export growth becomes clear.

Table 6: Net Direct Foreign Investment in Selected Countries of Asia and the Pacific, 1981-1993 (percentage of GDP)

	1981-85	1986-93	1994
Bangladesh	0	0.02	0.26
India	0.04	0.11	0.45
Pakistan	0.23	0.55	0.69
Sri Lanka	0.82	0.78	1.35
<u>South Asia</u>	<u>0.07</u>	<u>0.17</u>	<u>0.49</u>
Indonesia	0.27	0.90	1.46
Malaysia	3.81	5.08	4.39
Thailand	0.72	1.54	0.34
<u>New NICs</u>	<u>1.12</u>	<u>1.94</u>	<u>1.69</u>
Philippines	<u>0.18</u>	<u>1.17</u>	
Hong Kong			
Republic of Korea	0.75	0.49	n.a.
Singapore	0.04	0.09	-0.35
<u>NICs</u>	7.52	10.87	n.a.
	0.95	<u>1.25</u>	
Papua New Guinea			
	4.03	3.87	0.08

Source: ILO (1996)

Apart from high rates of domestic savings and investment, and success in attracting foreign direct investment as well as in achieving high rates of export growth, a few other factors which contributed to the success of NICs and new NICs of Asia are worth noting. One such aspect is skill accumulation. Policies and supporting institutions in the NICs and some of the new NICs (especially Malaysia) led to rapid skill development along appropriate lines. And this extended beyond basic education. In the Republic of Korea, the State played a very important role in vocational training, although enterprises also contributed either by organizing in-plant training or paying a training levy. In Singapore and Malaysia the governments collaborated effectively with the private sector to provide necessary skill training. Indonesia has expanded its network of vocational training institutes, in-plant training and community training centres to supplement the government network. Thailand, in comparison, has been less conscious about the importance of investment in human capital formation, and is currently facing shortages of skilled manpower as well as difficulties in redeploying workers rendered redundant by industrial restructuring.

Another factor which contributed to the high growth of NICs (not applicable to Hong and Singapore) - and one which is not always highlighted - is the attention given to the agricultural sector. Republic of Korea started with the advantage of an egalitarian land reform which helped in equitable distribution of the benefits of agricultural growth. Countries of South East Asia invested heavily in extension services and rural infrastructure, e.g, irrigation, road and electricity. Rising productivity in agriculture released surplus labour for employment in manufacturing - thus facilitating a rapid structural transformation of the economy. Also, conditions were created for growth of a dynamic non-farm sector in rural areas.

Table 7: Export Performance of Selected Countries of Asia and the Pacific

	Annual average growth of merchandise exports					Exports of goods and non-factor services as percentage of GDP	
	1981-85	1986-93	1994	1995	1996	1980	1994
Bangladesh	7.28	11.72	6.3	37.1	11.8	6	12
India	4.48	9.19	18.4	20.9	13.0	7	12
Pakistan	4.33	11.57	-1.4	16.1	7.0	12	16
Sri Lanka	7.51	10.61	15.2	18.4	12.0	32	34
Indonesia	-0.31	14.67	9.9	13.1	8.8	33	25
Malaysia	10.52	14.72	23.1	25.9	4.0	58	90
Philippines	0.91	7.62	18.5	29.4	17.5	24	34
Thailand	8.44	20.36	22.2	24.7	0.1	24	39
Hong Kong	10.70	17.82	11.9	14.8	4.0	90	139
Rep. of Korea	14.58	10.39	15.7	31.5	4.1	34	36
Singapore	6.15	15.63	25.8	21.5	6.7	207	177
Papua New Guinea	3.18	-3.77	1.8	6.6	-15.8	43	53

Sources: ILO (1996); World Bank (1996a).

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4. Prospects of Asia and the Pacific in the Early Decades of the 21st Century

In this section, we shall first present in a summary form results from three separate projection exercises undertaken by the Wold Bank, the Japan Centre for Economic Research (JCER) and the Asian Development Bank (ADB). Based on these projections, some tentative conclusions will be drawn about prospects of economic growth in the Asia-Pacific region during the first couple of decades of the 21st century.

The World Bank forecast[2]

Following are the assumptions on which the World Bank forecast (for the period 1996-2005) is based.

i. recovery in the industrial countries will lead to modest but more steady growth rates in these countries, thus contributing to a more stable external environment for the developing countries;
ii. low inflation and real interest rates will continue:
iii. private capital flows to developing countries will continue to achieve significant growth;
iv. the current boom in world trade is expected to be followed by a decade of strong growth in trade volumes;
v. commodity prices (including that of oil) are expected to continue to decline in real terms. That, in turn, is expected to contribute to a more stable environment for commodity-reliant developing countries.

Based on the above assumptions, growth in the developing countries as a whole is projected to accelerate from 3.4 per cent during 1971-90 and 5.0 pr cent in 1991-94 to 5.3 per cent over the next ten years. The prospect for East Asia (which in the World Bank classification includes China and the South-East Asian countries) is, however, brighter - although the projected growth of 7.9 per cent per annum falls slightly short of 8.7 per cent achieved during 1991-93 (Tables 8 and 9). South Asia, on the other hand, is expected to grow at 5.4 per cent during 1996-2005 compared to 3.2 per cent and 5.7 per cent achieved during 1991-93 and 1981-90 respectively. Thus, growth in the more dynamic segment of the Asia-Pacific region is expected to slow down slightly while South Asia is expected to grow at roughly similar rates.

The forecast by the Japan Centre for Economic Research[3]

The published results of this forecast do not provide any information regarding the assumptions on which it is based. It should also be noted that this is an exercise primarily meant to forecast the prospects of growth in Japan, although it contains projections for the world as a whole, Western Europe, North America and Asia (Table 9). Unfortunately, further breakdowns by sub-regions of Asia are not available.

This exercise considers the prospect for the World as a whole as well as for Asia to be a little less bright compared to that of the World Bank. It is possible that in the assumptions behind this exercise, the slow growth of the global economy in the early nineties dominates. The point to be noted, however, is that the present exercise also forecasts a very healthy growth rate for Asia in the first decade of the twenty-first century - a rate which far exceeds that of the world as a whole or the developed world. One can also expect that if the developed countries perform better than assumed, the growth rate of Asia will be even higher.

Table 8: World Bank's GDP Forecasts 1996-2005 (Annual percentage change in real GDP)

Region	1996-97	1996-2005
World total	3.1	3.5
High income countries	2.6	2.9
OECD countries	2.6	2.8
non-OECD countries	5.6	5.5
Developing countries	4.8	5.3
East Asia (including China and South East Asia)	8.2	7.9
South Asia	5.5	5.4

Source: World Bank (1996b).

Table 9: GDP Forecasts by the Japan Centre for Economic Research 1990-2010 (Annual percentage change in real GDP)

Region	1990-2000	2000-2010
World total	2.5	2.8
Western Europe	2.0	1.9
North America	2.1	2.4
Japan	2.7	3.5
Asia	4.5	4.9

Source: Japan Centre for Economic Research (1994).

The ADB forecast[(4)]

This forecast is part of an ongoing project at the ADB, and I could have access only to some summary information on this. The assumptions on which it is based are as follows:

i. The world economy continues a healthy growth. In particular, the U.S. is assumed to grow at an annual average rate of 1.7 per cent per person - which is its average in the recent past.
ii. Government policies on the whole remain similar to those in the mid-1990s. This implies, for instance, that open economies do not return to protectionism.
iii. Savings rate obtaining currently will continue.

Based on the above assumptions, it is projected that the Asian living standards will draw much closer to those of the currently advanced countries. However the prospects are considered to differ substantially across sub-regions of the Asian continent. In Hong Kong, Singapore and the Republic of Korea where growth has been exceptionally high during the last three decades, some slowdown is likely. However, it is clearly asserted that a collapse of growth predicted by some is unlikely. China and the South-East Asian countries that began their period of high growth more recently should continue to expand at about the same pace for the foreseeable future. South Asia is well placed to accelerate its economic growth if recently introduced policy and institutional reforms continue in the right direction.

What do the forecasts indicate?

All the three forecasts mentioned above suggest that growth in the Asia-Pacific region will continue, although they differ in the degree of optimism. While the World Bank and ADB forecasts are more optimistic, the one by the JCER is somewhat cautious. They can thus be taken as two alternative scenarios, in none of which a collapse of growth in Asia is predicted. Moreover, based on the ADB forecast one can predict not only a narrowing down of gap between the developed world and the Asia-Pacific region but also a narrowing of the gap between the East Asian countries and the countries of South Asia.

How credible are the projections and what are the risks that might cause the reality to be vastly different for the projected outcomes? The quality of projections depends to a large extent on the validity of the assumptions on which they are based. In that context one could perhaps say that neither the World Bank forecasts nor the ADB forecasts made assumptions which are unrealistic. For example, growth in world trade can suffer a setback only if countries abandon their policy of opening up and return to protectionism. Also, the flow of private capital towards developing countries can be hampered only by wrong policies of governments and unforeseen political changes. Similarly, it is difficult to see how countries with high saving rates will suddenly become profligate. One would also wonder why developed countries will open themselves to the risk of high inflation and raise interest rates very substantially. On the whole, therefore, the forecasts appear to be based on fairly realistic assumptions. And these forecasts point to good prospects for Asia in the early decades of the 21st century. However one cannot afford to remain complacent in a world which has become increasingly competitive. While prospects are indeed good and there are opportunities, one should also take note of the challenges and risks that are there.

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5. Challenges, Opportunities and Risks

Growth of productivity

As mentioned earlier, the slowdown in GDP growth and export growth experienced in 1996 by the NICs and the new NICs is raising the question whether this is merely a cyclical phenomenon or is reflective of some structural malaise of these economies as a result of which they are not being able to sustain the very high growth they achieved earlier. Indeed, the pessimism implicit in the latter view has been expressed earlier also.[(5)]

'The myth of Asia's miracle', 'tired tigers', 'falling stars' are some of the expressions that have been used to describe the slowdown in growth mentioned above and the associated doubts about the long term prospects of these countries. What is the real challenge faced by them?

It has been mentioned in section 3 that one of the strengths of the fast growing countries of Asia is that they have saved and invested at high rates. But high rate of investment by itself is not enough for sustained growth; efficiency in the use of resources - both capital and labour - is of crucial importance. And the pessimistic view about the growth prospects of Asian NICs and new NICs is based on the argument that their past growth has been based on quantitative expansion in the use of capital and labour - and not on gains in efficiency.[(6)] Since this argument has given rise to a good deal of controversy, it warrants a little examination.

The concept of total factor productivity enables one to measure the efficiency with which various inputs are used in the process of production. It is usually expressed as a ratio of GDP to a composite measure of labour as well as capital. The empirical exercises can, however, produce widely varying results for the same country or region depending on how the variables are measured, the weights used, and the period of reference. One study which has fuelled the pessimistic view is that of Alwyn Young which covered 118 countries over 1970-85. One of his findings was that the growth of TFP was generally no higher in East Asia than in the rich industrial economies. Krugman (1994) used Young's study to argue that East Asia's growth had largely been achieved through heavy investment and large scale transfer of surplus labour from agriculture to industry, rather than from productivity improvements.

Other economists are, however, critical of Krugman's arguments as well as Young's results. One problem is that TFP growth is estimated a residual - i.e., the part which cannot be explained by increases in capital and labour. It is therefore subject to serious measurement problems - which is one reason for the differences in results produced by various studies.

For example, a recent report by the Union Bank of Switzerland (quoted in The Economist, 1 March 1997), undertook a similar exercise for the period 1970-90, and produced very different results. In this study, five East Asian countries (Hong Kong, Republic of Korea, Singapore, Thailand and Taiwan, China) ranked in the top 12 countries (out of 104) for average TFP growth. In all these cases, productivity was roughly as important as investment in explaining growth. In a study of the ASEAN countries (by Michael Sarel of the IMF and reported in The Economist, 1 March 1997), productivity growth was found to be quite high. For Malaysia, Singapore and Thailand, this study found annual TFP growth to be 2-2.5 per cent during 1978-96, compared with only 0.3 per cent in USA. Moreover, TFP growth increased in most ASEAN countries between the 1980s and the 1990s.

A World Bank study (World Bank, 1993a) found that there is considerable regional difference in TFP growth. While the TFP growth in developing countries was lower than in high-income countries during 1960-91 (0.3 per cent compared to 1.4 per cent), the TFP growth in East Asia was significantly higher than in other developing regions. And during the 1970s and the 1980s, it was double that of high-income economies. From 0.8 per cent per year in the 1960s the figure for the East Asia region halved after the 1973 oil shock, but recovered to reach 1.7 per cent per year in the 1980s. Another world Bank study (World Bank 1993b) produced results similar to above and to the IMF study mentioned above. This also pointed to substantial differences in TFP growth within Asia - the rates being much lower or even negative in South Asia.[(7)]

The weight of evidence presented above seems to indicate that it would not be appropriate to say that economic growth in East Asia has been based entirely on quantitative expansion of the inputs of production. Moreover, the amount of capital per worker in these countries remains considerably lower than in the rich industrial countries. There is also substantial scope for improving the productivity of workers through investment in human resource development (both skill training and education).

Notwithstanding the controversies concerning the different measures of TFP, the importance of productivity growth cannot be exaggerated especially from the point of view of sustained long term growth. Indeed, as the NICs approach the developed country levels of capital per worker and educational levels, growth will tend to slow down and will tend to depend more on productivity growth. For countries at lower levels of development also it is important for at least two reasons. First, capital is scarce in many of these countries; and efficient use of capital is essential from the point of view of maximizing their growth performance from a given amount of resources. Second, with rising labour productivity, wage increases can take place without any adverse effect on the profitability of enterprises. Workers can thus benefit from the growth process.

Diversification of exports

As has been noted already, rapid growth in exports has been an important catalysing factor in the high growth achieved by the NICs and new NICs of Asia. And in an increasingly globalizing world, this is likely to remain an important factor in sustaining the growth process. As nearly two-thirds of the world's imports are accounted for by the developed countries, what happens to growth and demand in these countries is extremely important from the point of view of exports from developing countries. At the same time it should be noted that too much reliance on developed countries exposes one to the risks arising from cyclical fluctuations in demand in such countries. A second important aspect of exports is that too much reliance on a narrow range of exports also exposes a country to risks associated with fluctuations in their prices.

With respect to destination of exports, developing countries of Asia are doing better than those in other regions. While nearly 54 per cent of all developing country exports went to industrial countries in 1994, for Asian countries the figure was about 50 per cent.[(8)] This is already an improvement from the situation in 1980[(9)] - although there is scope for further increases in trade amongst developing countries. Table 10 shows more clearly the diversification in the direction of exports achieved by some countries of Asia during the period 1985-95. The NICs and the new NICs have been able to achieve notable success in this regard. In contrast, Bangladesh, Nepal, Sri Lanka and Vietnam appear to have become more dependent on industrial countries for their exports. The emergence of new labour-intensive exports, e.g., garments may have been the reason for this change in the direction of exports from these countries (with the exception of Vietnam).

Table 10: Share of Exports from Selected Asian Countries Accounted for by Developing Countries [A)]

	1985	1995
Bangladesh	14.5	8.8
India	8.9	21.9
Nepal	41.4	9.7
Pakistan	16.0	20.7
Sri Lanka	11.2	6.9
China	38.2	39.6
Indonesia	17.2	26.5
Malaysia	38.1	43.7
Philippines	19.5	25.6
Thailand	27.1	34.8
Vietnam	50.4	26.7
Hong Kong	35.6	45.6
Republic of Korea	12.9	35.3
Singapore	36.7	49.9
Papua New Guinea	9.9	19.9

Note: [a)]"Developing Countries" refer to developing member countries of the Asian Development Bank.
Source: Asian Development Bank (1997)

In terms of commodity composition of exports, all the NICs and new NICs have been able to diversify their exports considerably (Table 11). Particularly notable in this regard is the achievement by Indonesia, Hong Kong, Malaysia and Thailand. Republic of Korea has also made progress from an already low level of concentration in 1984. In South Asia, Bangladesh and Sri Lanka have made considerable progress, while Nepal and Pakistan have moved in the reverse direction. The adverse effect of export concentration can be seen from the recent experience in Pakistan resulting form decline in cotton production and export and in Nepal after the sharp decline in carpet exports. In both cases, overall economic growth suffered adversely.

Uneven distribution of the benefits of globalization and economic growth

If one looks at increases in the ratio of exports to GDP over the last two decades or so, it would appear that most countries of Asia have participated in the process of globalization. But the important question that remains is how the benefits of globalization have been distributed across countries. Take capital flows, for example. Of the total flow of FDI in 1994 (which was a little over US$44 billion) South Asia got a meagre 2.8 pr cent. While China bagged 76.3 per cent, Indonesia, Malaysia, Philippines and Thailand totalled another 18.29 per cent (see Table 12). Within South Asia, India accounted for half, but Bangladesh and Nepal received very small amounts. While a variety of factors are responsible for such vast differences in the flow of FDI, the fact is that only a small number of countries have really succeeded in attracting substantial flows of FDI. Thus, a large number of countries have not gained much benefit from the process of globalization.

Within the countries again, the various regions and groups of population have not benefited equally from the process of globalization and economic growth. In China, it is mainly the coastal provinces of the east and south-east that have been able to attract foreign capital; and these are the provinces that also achieved higher growth. In Thailand, it is mainly the Bangkok region that has benefited; the north-east has not only remained poor, but the gap in income between that region and Bangkok has widened. In Vietnam, high growth has already unleashed forces towards increased inequality between the north and the south. Globalization may thus be accentuating the regional inequalities that already existed in many countries for a variety of reasons.

Table 11: Export Concentration Index for Selected Asian Countries, 1984 and 1992

	1984	1992
Bangladesh	0.326	0.246
India	0.183	0.140
Nepal	0.237	0.519
Pakistan	0.207	0.228
Sri Lanka	0.456	0.232
China	n.a.	0.076
Indonesia	0.499	0.194
Malaysia	0.276	0.156
Philippines	0.298	0.293
Thailand	0.182	0.090
Vietnam	n.a.	0.308
Hong Kong	0.310	0.152
Republic of Korea	0.193	0.109
Singapore	0.238	0.183
Papua New Guinea	0.495	0.465

Source: World Bank (1996 a).

Table 12: Flow of Foreign Direct Investment to Developing Countries, 1994 (US$ millions)

	Amount	Percentage
All developing countries	80,120	
Asia	44,279	100.00
East Asia and Pacific	43,037	97.20
China	33,787	76.30
Indonesia	3,109	4.76
Republic of Korea	809	1.83
Malaysia	4,348	9.82
Myanmar	4	n
Papua New Guinea	4	n
Philippines	1,000	2.26
Thailand	640	1.45
Vietnam	100	0.03
South Asia	1,242	2.80
Bangladesh	11	0.02
India	620	1.40
Nepal	7	0.016
Pakistan	430	0.97
Sri Lanka	166	0.37

Note: 'n' denotes less than 0.01.
Source: World Bank (1996 b).

Human resource development

In section 3, rapid skill accumulation by the NICs and new NICs of Asia was mentioned as one of their strengths. There is, however, room for improvement in this direction. And in the countries of South Asia, a good deal needs to be done in this field. One example may help to indicate the gap between developed countries and the developing countries of Asia. In 1994, the average worker in East and South East Asia had received only seven years of education (ranging from four years in Indonesia and Thailand to nine years in the Republic of Korea). In contrast, workers in most industrial countries have at least ten years of education and often much more. Indeed, in countries like Indonesia and Thailand low level of education of workers and shortage of higher level skills and technicians is already appearing as a constraint on industrial growth. Given lower average levels of literacy in South Asian countries (except Sri Lanka and certain regions of India), the situation there must be worse.[(10)]

Apart from basic education and skills, a different type of challenge is posed by technological change that is essential to maintain competitiveness in an increasingly globalizing and competitive world. The workers will need to be retrained almost on a continuous basis so that adjustment at the enterprise level can proceed smoothly.[(11)] This will require the creation of a training culture where the workers have to be willing to undergo training to keep themselves abreast and employers prepared to invest in such training. In-plant training becomes crucially important in this context.

Opportunities

Asia has two heavy weight economies (viz., China and India) within the region itself. Both of them have huge internal markets. China, with a population of over 1 billion and phenomenal economic growth for more than a decade, has created a very large market not only for itself, but for others also. Despite controversies about the size of India's middle class, another large market has emerged in that country also. These as well as markets in other Asian countries have vast potential for further growth. In an increasingly globalizing world, markets will not remain confined to enterprises within national boundaries. Growth triangles and regional/sub-regional trading blocks are emerging (sometimes despite political differences) to take advantage of the vast potential of intra-regional trade. Both capital and labour have become highly mobile. In such a situation, neither demand nor supply can pose an effective constraint.

Economic reforms being undertaken in many countries of Asia are adding to their strength. Necessary conditions are being created for sustained growth with stability. While some of the reform measures are exposing hitherto protected industries to competition, measures of deregulation and liberalization are also creating an enabling environment for their growth. Supply constraints are being eased considerably. Overall macroeconomic policy regime is gradually becoming much more business friendly (e.g., in terms of lower rates of taxes, removal of quantitative trade restrictions) than before.

The GATT agreement, by scrapping quotas and demolishing a host of other obstacles to trade, will create opportunities for freer trade. And the benefits to Asia are potentially huge. As a region of mostly fast-growing trade-oriented economies, its gains are likely to be disproportionately high. According to one estimate (quoted in the Far Eastern Economic Review, 28 April 1994), Asia will generate well over half the new trade expected to be created by all developing countries. And within Asia, gains will be most immediate for South-East and East Asia. Expanded trade means higher income and employment.

The major source of the expected boost in trade is tariff reduction by industrial countries on a range of products produced in Asia (Chart 1). Moreover, Asia's share of world trade has already been increasing - from less than 11 per cent a decade ago, it is now roughly 15 per cent. As the region of most buoyant economic growth, Asia is sucking in investment from the rest of the world. Also, Asia is increasingly trading with and investing in itself .- thus creating a virtuous circle.

Asia accounts for more than 40 per cent of world trade in textile and clothing - one of the areas expected to benefit most from the GATT agreement. In manufacturing as a whole, Asia has already emerged as a powerhouse. In 1992, just eight East Asian nations produced 73 per cent of all developing country exports of manufactures (including textiles and clothing)[(12)] The region should naturally be able to build up further on an excellent base that exists already.

Chart 1

Expected Beneficiaries of Developing Asia from a Boost in Trade Resulting from Tariff Reduction

Product Group	% tariff reduction		Developing countries in Asia with Substantial exports of these products
	North America	Western Europe	
Textiles and clothing	15	20	Bangladesh, China, Fiji, Hong Kong, India, South Korea, Macau, Pakistan, Philippines, Sri Lanka, Tonga, Tuvalu
Metals	63	35	Papua New Guinea
Mineral products, precious metals and stones	31	22	Brunei, Fiji, India, Indonesia
Electric machinery	56	37	Malaysia, Singapore
Leather, rubber, footwear and travel goods	11	23	Cambodia, Tonga
Wood, pulp, paper and furniture	76	67	Burma, Cambodia, Indonesia, Malaysia, Solomon Islands
Fish and fish products	19	18	Fiji, Maldives, Solomon Islands
Non-electric machinery	63	61	Singapore, Tuvalu
Coffee, tea, cocoa, sugar	35	29	Fiji, Indonesia, Papua New Guinea, Singapore, Sri Lanka, Tonga
Fruits and vegetables	38	32	Burma, Philippines, Thailand, Tonga Tuvalu
Oilseeds, fats and oils	43	34	Cambodia, Indonesia, Malaysia, Papua New Guinea, Philippines, Solomon Islands
Animals and animal products	36	25	Tuvalu
Other agricultural products	49	44	Pakistan

Source: **Gatt**
Source: Far Eastern Economic Review 28 April 1994.

Risks

While Asia's economic prospects in the 21st century are indeed bright, one should not ignore the risks that face Asia. It is possible to identify two broad types of risks: one is external to the region, while the other is internal. The external risk is linked to one of the basic assumptions on which the entire optimistic scenario is based - that of increasing globalization from which Asia benefits highly and even disproportionately. Is there a risk of the global economy moving in the opposite direction, i.e., one of increasing protectionism? Although such a reversal is unlikely, an unforeseen deep economic crisis (whatever the reason may be) in the industrial countries may lead to a tendency towards nationalism and isolationism - which in turn may adversely affect growth in countries where trade is the engine of growth.

Risks internal to the region can be of various kinds. As countries grow economically, their political systems and institutions will also need to adjust accordingly. Demand for a greater degree of democratization is only likely to grow; and sustained economic growth may at some point depend to a large extent on the maturity with which political systems and institutions respond to such demand. This is relevant for most countries of the region - be it an NIC, a new NIC, an economy in transition or a less developed economy. In addition, the kind of political instability that some South Asian countries are witnessing recently can also pose serious risks.

Infrastructure - both physical and social - is of paramount importance in ensuring sustained economic growth. In some Asian countries, low level of development in this field is already acting as a bottleneck in the process of growth. There is a risk that the states may not make adequate and timely investment in infrastructure (e.g., roads, electricity, telecommunication, education and training), and growth process may stumble as a result.

In countries undertaking economic reforms with the objective of liberalizing their economies and integrating them with the global economy, one risk may be of stalling such reforms keeping them incomplete. Domestic political compulsions may prevent governments from taking hard decisions that may be essential to tackle short-term economic difficulties.

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6. Some Messages

i. The countries of Asia should capitalize on their strength and do more of what they are good at. This means a continuation of export-oriented open economy policies. In addition, efforts need to be made to diversify exports - both in terms of commodity composition and destination. Increased intra-regional trade will help achieve the latter.
ii. The above should not be taken to imply that domestic markets are not important. Indeed, in medium and large countries domestic markets can be an important source of growth - especially as incomes increase. Measures need to be undertaken to tap the potential of domestic markets.
iii. To remain competitive and to be able to maintain growth when further increases in capital per worker are not possible, improvement of productivity of both capital

and labour is extremely important. Improvement in labour productivity also makes possible wage increases without adverse effects on profitability.

iv. Investment in human resource development facilitates the growth process. While governments have the responsibility to invest in basic education, enterprises must make forward looking investment in skill training so that the workforce does not become obsolete as production processes change.

v. Investment in physical infrastructure is of utmost importance. Well-developed power supply and transport and communication network is an important factor influencing investment in industries.

vi. Reforms necessary to create an enabling environment for economic agents must not be delayed. Appropriate sequencing of economic reforms is of course important.

vii. Move towards a greater degree of democracy and appropriate democratic institutions can facilitate rather than hinder the process of economic growth.

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Endnotes

1. Deputy Director, Development Policies Department, ILO, Geneva. Views expressed in this paper do not necessarily reflect those of the ILO.

2. This section is based on World Bank (1966b).

3. For detailed results, see Japan Centre for Economic Research (1994).

4.This forecast is part of the Asian Development Bank Emerging Asia Study.

5. See, for example, Krugman (1994).

6. Ibid.

7. See, also, Mazumdar and Basu (1997) who quote a study on India showing negative TFP growth in manufacturing between 1959-60 and 1979-80.

8. These figures have been arrived at from data in World Bank (1996 b).

9. Islam (1984) showed that in 1980 industrial economies accounted for more than half the exports from all East and South East Asian countries except Singapore.

10. A caveat needs to be mentioned here. An expansion of education which is not market demand oriented can result in unemployment of the educated and thus waste of scarce resources available for human resource development. This is a common feature of several countries of Asia, especially of South Asia. It is, therefore important to sequence HRD with industrial restructuring, technological changes and changes in skill requirements. On this, see Bhagavan (1993).

11. Muqtada and Hildeman (1993) has also pointed out the importance of flexible training system to cope with rapidly changing skill requirements.

12. Far Eastern Economic Review, 28 April 1994.

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