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EAST ASIAN ECONOMIC RECOVERY AND STRUCTURAL REFORM

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I. INTRODUCTION

After three decades of remarkable economic growth and poverty reduction, several economies of East Asia fell into a severe recession in 1998. The economic crisis in the affected countries (Indonesia, Korea, Malaysia, the Philippines, and Thailand) has caused a serious setback in development performance, but at the same time has provided a window of opportunity to strengthen domestic economic institutions and policy frameworks through wide-ranging structural reforms. The transition economies of China and Vietnam, though less affected by the regional crisis, maintain their momentum of economic reform of the state sector and further marketization. The trade-driven smaller and poorer economies of the Pacific, Indochina, and Mongolia also continue their efforts to reduce poverty and to build institutions and capacity.

Beyond the current recovery process, post-crisis East Asia faces two broad challenges. The first is how to cope with the forces of globalization. Facing global competition, governments throughout East Asia must ensure that public policies that regulate key economic activities—such as in the financial sector, corporate governance, infrastructure, or environmental protection—are effective at creating world class frameworks. At the same time the government must manage the impact of globalization on the domestic economy. The second is how to respond to socio-economic changes, including demographic shifts, urbanization, and higher levels of education and income, and how to embrace political and societal transformation. Older, more urban, more educated, middle class populations have voiced louder demands for greater transparency and accountability of the government and for a range of public services, such as new forms of social safety net. The trend toward political and social pluralism, set in motion well before the recent economic crisis, has been reinforced by global connections—enhanced information access and increased demand for diverse lifestyles and values.

This paper addresses the questions: Is the current economic recovery process sustainable? What are the risks to sustained recovery? What are the medium-term policy issues the East Asian economies must address? Can they transform the current economic recovery process into sustained, broadly shared growth?

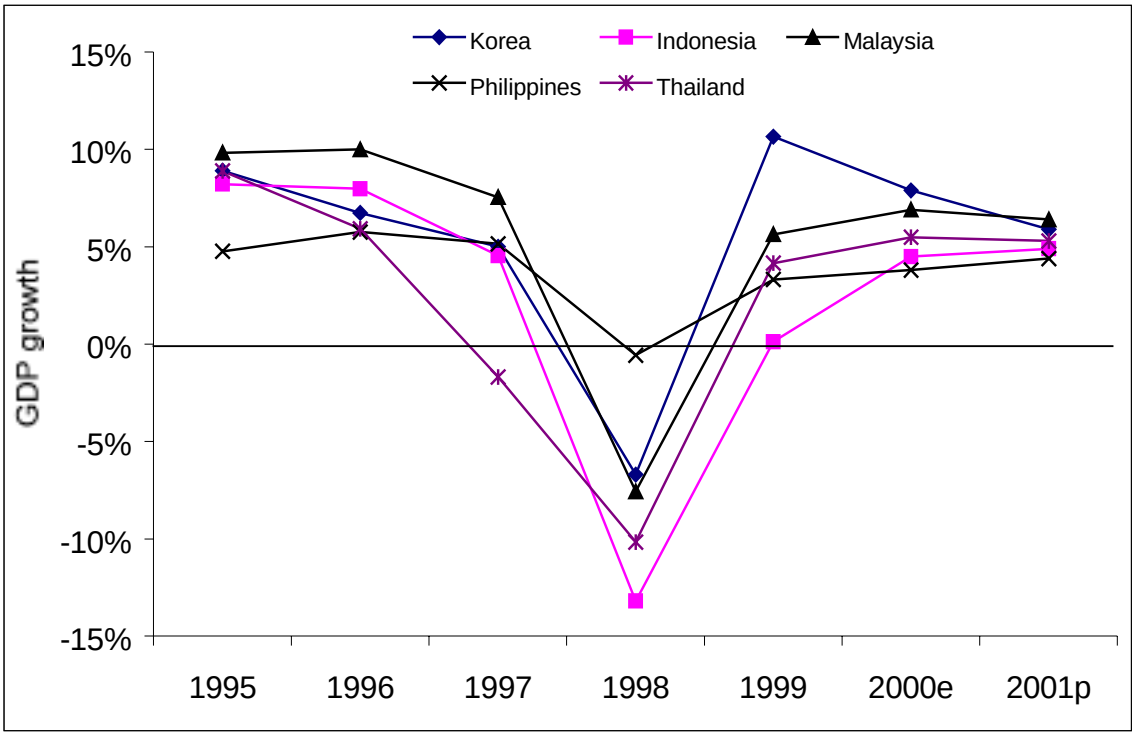
II. EAST ASIAN ECONOMIC RECOVERY

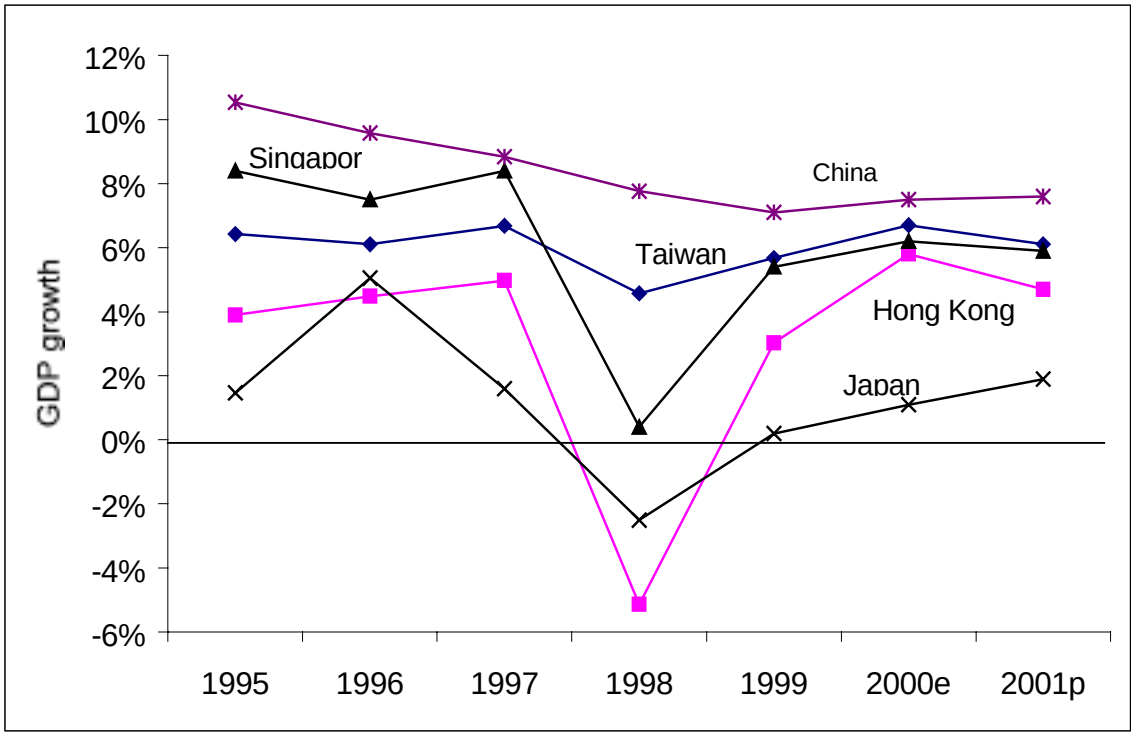
The East Asian economies have clearly emerged out of the worst of the crisis and are recovering strongly in 1999 (Figure 1). The only exception is Indonesia, but even its economy is rebounding at a projected 4-5% growth rate in 2000. Has East Asia entered the medium-term phase of sustained growth? Or is this just a temporary, cyclical rebound?

1. Sharp Economic Recovery

The worst period of output contraction ended during the first or second quarter of 1999 among the economies hit by the crisis. The economic consolidation and recovery phase has firmly begun with Korea showing the most dramatic improvements in levels of output, exports and employment. Even Indonesia, despite its political turmoil in the last two years, is showing signs of an incipient economic rebound.

Figure 1. GDP Growth Rates of the East Asian Economies





Source: International Monetary Fund; Consensus Forecast, June 2000.

Economic recovery is strong and its pace is faster than expected. After a sharp recession—with growth down 7.8 percent in 1998—growth in the five affected countries surpassed 5 percent in 1999. Korea is outpacing the other four affected countries, with growth of close to 11 percent in 1999 a projected 8 percent in 2000. At the other extreme, Indonesia faltered with barely positive growth in 1999 and its recovery process is still fragile. China and Vietnam continue to perform well, and the smaller economies also fared better in 1999 (see Appendix Table).

Foreign capital in the form of direct investments and portfolio equity investments has picked up (World Bank, 2000). After recording an outflow of US$60 billion in 1998, net private outflows of East Asia declined to US$23 billion in 1999. Though East Asia is expected to continue to experience net outflows of private capital due to large net outflows of bank loans, net foreign direct investments and net portfolio equity flows have expanded, reaching US$15 billion and US$9 billion respectively in 1999.[1]

The five affected countries began to turn around for three reasons. Financial stabilization (in the foreign exchange and financial markets) and countercyclical macroeconomic policy allowed domestic aggregate demand, and eventually personal consumption in particular, to recover. Assertive structural adjustments helped boost consumer and investor confidence. The regional recovery, supported by strong growth in the United States and Europe, bolstered external demand in a mutually reinforcing way.

The recovery process has been driven by buoyant exports, fiscal stimulus, personal consumption, and inventory re-stocking. However, fixed investment has not recovered fully, except in Korea, due to the continued presence of excess capacity in the manufacturing sectors. Falling interest rates, the easing credit conditions and the restoration of export finance facilities should help the utilization of the prevailing capacity for domestic consumption and export production. As excess capacity is reduced, fixed investment in new equipment is expected to rise, thus making the current recovery process more solid and firm.

As a result of recovery, real GDP has exceeded the pre-crisis levels in Korea, Malaysia, and Thailand, while it may take a few years for Indonesia to attain its pre-crisis level. Due to real exchange rate depreciation, however, per capita GDP measured in the US dollar is still lower than the pre-crisis levels in the affected countries. Full recovery in East Asia will mean that per capita GDP measured in the US dollar (adjusted for US inflation rates) must recover to the pre-crisis level.

2. Progress on Financial and Corporate Sector Restructuring

There is no question that the current recovery process has been supported by significant progress made in the areas of financial and corporate restructuring. Governments indeed have generally achieved much progress, albeit at a substantial fiscal cost, in initiating and sustaining the process of financial sector restructuring and rehabilitation as well as debt and operational restructuring of corporations.

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[1] Though brighter, most of these private flows have concentrated on one or two countries (Korea and China), leaving the rest of Asia behind.

Many non-viable and insolvent financial institutions have been closed or temporarily nationalized, bad loans of weak but viable financial institutions have been carved out to official (and, more recently, private) asset management companies, the capital base of several weak but viable institutions have been strengthened by public resources, and the process of rehabilitating weak institutions has been underway. In Korea and Thailand, the banking sector has been opened to foreigners to attract foreign capital, expertise and competitors.

Table 1. Institutional Arrangements for Corporate and Financial Restructuring

	Agency for Voluntary Corporate Workout	**Asset Management/Resolution Company**	**Agency for Bank Recapitalization**
INDONESIA	Jakarta Initiative Task Force (JITF)	Indonesian Bank Restructuring Authority (IBRA)	Indonesian Bank Restructuring Authority (IBRA)
KOREA	Corporate Restructuring Coordination Committee (CRCC)	Korea Asset Management Corporation (KAMCO)	Korea Deposit Insurance Corporation (KDIC)
MALAYSIA	Corporate Debt Restructuring Committee (CDRC)	Danaharta	Danamodal
THAILAND	Corporate Debt Restructuring Advisory Committee (CDRAC)	Financial Sector Restructuring Authority (FRA) and Asset Management Corporation (AMC) for nonbank finance companies	Financial Restructuring Advisory Committee (funded by the Financial Institutions Development Fund)

Source: World Bank, *Global Economic Prospects and the Developing Countries*, 2000, p. 85.

Corporate sector restructuring has been the other side of the process of financial sector resolution. The substantial overhang of bank NPLs was largely a consequence of weak performance of corporations. Several frameworks have been established to accelerate corporate sector restructuring (see Table 1). First, court-based insolvency procedures have been strengthened, including the bankruptcy, reorganization and foreclosure laws and the establishment of functioning judiciary systems. This has particularly been the case for Indonesia and Thailand which lacked effective legislative procedures. Second, formal frameworks for voluntary, out-of-court debt negotiations have been developed under the "London Approach" arrangement.[2] Once financial obligations and property rights have been clarified and agreed upon by both creditors and debtors, market-driven mechanisms should facilitate the required debt restructuring and reallocation of productive assets.[3] Finally, official asset management companies have

[2] This includes the Corporate Debt Restructuring Committee in Malaysia, the Corporate Debt Restructuring Advisory Committee in Thailand, and the Jakarta Initiative Task Force in Indonesia.

[3] Governments have also changed regulatory and tax incentives in promoting greater asset mobility, especially by encouraging corporate mergers and acquisitions, FDI, and debt-equity conversions and swaps.

been empowered to restructure distressed debts and corporations, in addition to disposing of acquired assets.

One of the consequences of financial sector restructuring is that governments have acquired not only banks but also, through asset management companies, the assets of failed institutions and the bad assets of weak but viable institutions. The state has thus become an important holder of corporate assets. In Indonesia, the government is the biggest holder of bank assets, acquiring 78 percent of banking assets, while governments of Korea, Thailand, and Malaysia respectively own 58 percent, 32, percent, and 18 percent of respective banking assets. The processes of disposing of the acquired assets or of restructuring the debts and debtor corporations have yet to take place on a large scale.

Another consequence is that the crisis has left heavy public debt with the government. Government debt has already risen to 35-50 percent of GDP in Korea, Malaysia, and Thailand, and to 90-100 percent of GDP in Indonesia and the Philippines. The growth of government debt is attributable to the initial sharp depreciation of the exchange rate (which raised the domestic currency value of government external debt), the resolutions of troubled financial institutions—purchases of NPLs, recapitalizations of weak but viable banks, and temporary nationalization of non-viable banks—and fiscal stimulus. Large government debts and debt servicing obligations may pre-empt development and social expenditures.

3. Risks to Sustainable Economic Recovery

Despite the strong V-shaped recovery, East Asia faces several risks that could hamper sustainable economic recovery. They include weak economic policies on the domestic front, external negative shocks, and potential political and social instability.

First, weak economic policies include unsound macroeconomic policy, delayed restructuring in the financial and corporate sectors, and unsustainable public sector debt. The risk in the form of unsound macroeconomic policy does not appear to be serious at this point unless public debt becomes out of control or the economies are subject to significantly large external shocks.

The greatest risk is complacency in financial and corporate sector restructuring. The financial sectors of the affected countries remain plagued by the overhang of bank NPLs and corporate debt (Table 2). Progress in NPL resolution and corporate debt restructuring is uneven—again Korea leads and Indonesia lags—but no country is near completion which may well take close to a decade to fully resolve. Temptation to slow the restructuring process exists due to the presence of vested interests and a nationalistic backlash against fire-sales of assets to foreigners. Vested interest groups are trying to slow the restructuring process in order to maintain their equity stake in, and control over, indebted corporations, which could otherwise be lost in the process of debt and operational restructuring. Domestic bank creditors may be unwilling to pursue aggressive NPL resolution because doing so would force them to realize losses, reduce capital, and thereby dilute bank ownership and control. Slow restructuring would mean that bank

NPLs and corporate debt would continue to be a large overhang, thereby choking off credit flows to the corporate sector.

Table 2. NPLs of Crisis-Affected Countries [(a)]
(percentage of total loans)

	1997	1998				1999			
	Dec.	Mar.	Jun.	Sept.	Dec.	Mar.	Jun.	Sept.	Dec.
Korea [(b)]	--	--	14.1	--	16.8	17.0	18.0	17.9	--
Malaysia [(c)]	6.0	9.1	12.6	21.3	22.6	22.7	23.4	23.6	23.9
Philippines [(d)]	4.7	7.4	8.9	11.0	10.4	13.2	13.1	13.4	12.5
Thailand [(e)]	--	--	32.7	39.7	45.0	47.0	47.4	44.4	41.1

Note: (a) For Indonesia, JP Morgan ("Asian Financial Markets"1999-Q3) provides estimates of NPLs as a percentage of total loans: 20-30 percent at end-1997; and 60-80 percent at the peak of 1998 and through 1999-Q3. (b) Figures include commercial banks, specialized and development banks, merchant banks, insurance companies, mutual saving banks, credit unions, leasing companies, securities companies, and KAMCO. (c) Figures include commercial banks, finance companies, merchant banks, and Danaharta. (d) Figures are for commercial banks. (e) Figures include commercial banks, finance companies, and the estimated amount of NPLs transferred to wholly-owned private AMCs. If the last item is to be excluded, the NPL ratio for December 1999 would be 38.5 percent.

What is clearly needed for corporate debt restructuring is to firmly establish a credible threat from the judicial/legal system. For a voluntary process of corporate restructuring to work, the alternatives to an out-of-court agreement must be made clear and credible. The case of TPI in Thailand illustrates how crucial it is to establish an effective insolvency procedure and a well-functioning judiciary system. Improvements of the functioning of courts, not just bankruptcy but the procedures of foreclosing on collateral and registering of security interest, helps protect creditor rights and provides the debtor with a credible threat to negotiate in good faith. This would contribute to resolving bank NPLs.

Rising public debt is another important policy risk that needs to be managed. Large public debt has raised debt servicing obligations and thus put pressure on development and social expenditures. In Indonesia, for example, close to half of government revenues will have to be spent for interest payment in the next several years. There is a serious risk that the public sector may not be able to meet the rising demand for development and social needs in such areas as infrastructure, health, education, and other public services. If the fiscal problem cannot be controlled, particularly in Indonesia and the Philippines, macroeconomic policy management will be difficult. With some of the social problems still ahead, governments face the complex task of managing their fiscal costs.

Second, external negative shocks can be another downside risk to the sustainability of recovery. The US economy, which has been the locomotive of East Asian recovery in the last two years, remains vulnerable to a potential abrupt decline, especially because of exuberant stock market activity, a record level of private sector financial deficits and the rising current account deficit. There are also concerns about the strength and durability of recovery in Japan. A slowdown of the US economy and a reversal of the Japanese

economic recovery can hamper the current East Asian recovery process. Another external risk arises from the recent hike in oil prices and upward pressure on the interest rate. So far, the high oil prices and rising global interest rates have not constrained the recovery process in the region but, if the high oil prices and high interest rates continue for a substantial time period, an adverse impact on growth can be non-negligible. Domestic restructuring of financial institutions and corporations would be necessary to make them more resilient to such external shocks.

Third, political instability or uncertainty poses a risk to the sustainability of the current recovery process. This is particularly the case for Indonesia which is facing rising signs of domestic political polarization and regional conflicts. The Philippines is also facing a resurgence of violence at the provincial level. The lack of evolution of political institutions in China is a potential risk to the region's economic health. Even in countries like Korea and Thailand, political and social dissatisfaction is emerging as an increasing number of people feel deprived of the benefits of economic recovery. The social impact of the economic crisis has been both severe and wide ranging, and the costs of socio-economic dislocations are still to emerge fully. Though governments have been implementing various programmes to mitigate the adverse social impact of the crisis, social distress can derail the current restructuring efforts.

An average 6 percent growth rate over the course of the next few years is possible for East Asia if there is further progress on economic policy (macro, structural, and public debt), external economic environments continue to be favorable, and political and social stability is maintained.

III. THE EAST ASIAN MIRACLE REVISITED: LESSONS FROM THE CRISIS

1. The East Asian Miracle

East Asia's achievement of spectacular economic and social gains during the Miracle years (1965-96) is beyond dispute. The Miracle economies of East Asia recorded an average growth rate of 7.5 percent per annum over the thirty year period.[4] Poverty declined, not only in breadth (the number of poor) but also in depth (severity of poverty). The number of poor living below the international poverty line of US$1 a day declined from 720 million (58 percent of total population) to 350 million (21 percent of total) during 1975-1995. Life expectancy at birth, infant mortality rates, and literacy indicators have all improved in tandem, generating real improvements in people's standards of living. East Asia succeeded in converting persistently high growth rates into improved social conditions because growth created jobs for the poor and opportunities to expand productivity. The Miracle was real and tangible.

Propelling these achievements was a high and equitable performance of economic growth. Several factors lay behind this remarkable growth performance. These included:

[4] The original Miracle economies in the World Bank's (1993) study included Japan, four Asian NIES (Hong Kong, Korea, Singapore, and Taiwan), and three ASEAN members (Indonesia, Malaysia, and Thailand). In this paper, the Miracle economies of East Asia refer to the four Asian NIES, the three ASEAN members, the Philippines, China, and Vietnam.

- Stable macroeconomic environments (low inflation, disciplined fiscal policy, and stable, competitive exchange rates);
- High savings (through positive real interest rates and effective deposit protection) and high investment in fixed assets;
- High investment in human capital through public expenditures on education;
- Limited price distortions;
- Outward-oriented trade policy and absorption of foreign technology; and
- Relatively limited biases against agriculture.

Essentially, most of East Asia's extraordinary growth was attributed to the application of a set of common, market-friendly economic policies leading to both higher accumulation and better allocation of physical and human capital. These economies not only achieved stable macroeconomic environments and superior accumulation of physical and human resources, but also were better able than many counterparts in other regions to allocate these resources to highly productive investments and to acquire and master technology. In this sense, there was nothing "miraculous" about the East Asian economies' success; each has performed these essential functions of growth better than most other developing countries.

2. Reflection on the Crisis

Following the Thai baht devaluation in July 1997 and the currency contagion throughout the region, all affected countries in East Asia plunged into a sudden, downward spiral of economic activity. The currency and financial crisis was quickly transformed into an economic and social crisis. Interactions between the force of globalization and domestic structural weaknesses were the major factors behind such rapid, startling crisis.

In retrospect, rapid growth in the pre-crisis years had spawned structural weaknesses in three dimensions:

- Large current account deficits, financed by short-term capital inflows, exposed East Asian economies to sudden reversals of capital;
- Domestic financial markets' growth and integration with global markets outpaced domestic regulation, and exposed banks to asset-liability mismatches. Inadequate regulation allowed banks to assume unhedged external debt positions and maturity mismatches that left them vulnerable to sudden currency depreciations; and
- Corporations, without alternative sources of financing, borrowed heavily from banks (domestic or foreign) to finance their rapid expansion, and in the process became highly leveraged, which exposed them to interest rate hikes and/or currency fluctuations.

It is important to note that domestic structural weaknesses explain only part of the emergence of these countries' vulnerabilities and subsequent crises. Failures in international financial markets in the boom period of the cycle, as well as during the crash, were no less pivotal; herd behavior, during both the boom and bust periods, and contagion in financial markets were another important factor behind the crisis. The East

Asian crisis revealed that the risks of financial instability in a globalizing market environment—especially for developing countries—are greater than had previously been thought.

3. Lessons from the Miracle and the Crisis

The East Asian crisis has exposed some of the structural weaknesses of the East Asian economies. These structural weaknesses were deeper than those observed in external accounts, the financial sector, and the corporate sector. They had been hidden or contained under the impressive growth performance of these economies. They were:

- The lack of urgency to manage the forces of globalization;
- The absence of good regulatory and supervisory frameworks to improve market efficiency; and
- The lack of commitment to maintain transparency and accountability of the government.

First, economic policy did not recognize fully the forces of globalization and the need to manage them. Reaping the benefits of greater integration with the world economy will require careful attention to managing risks associated with financial and trade integration. Though the international community's efforts to reduce, and respond to, global vulnerabilities are vital, each economy must manage globalization by strengthening the domestic economic system in a way resilient to shocks emanating from abroad. In an increasingly globalizing world economy, macroeconomic policy must be sound and consistent with the chosen exchange rate regime, the risk management of financial institutions and corporations must be prudent, and adequate social safety nets must be provided to protect those who are adversely and severely affected by globalization and external shocks. Policymakers should pay due attention to the right sequencing of financial sector liberalization and capital account liberalization.

Second, during the Miracle years many East Asian governments played a significant role in allocating real and financial resources to priority sectors and industries. Such a direct role of the government was already diminishing in the pre-crisis period, but the new role of government as a regulator and supervisor was not fully appreciated. Retreating from a direct, interventionist role does not imply that government should always take hands-off stance. On the contrary, the government should focus on establishing good regulatory and supervisory frameworks and institutions to govern private sector economic activity and to improve market efficiency.

Third, the importance of good governance of the public sector was not fully recognized. The public sector must improve its accountability, transparency, and efficiency, particularly in the areas of public service delivery and protection of the socially vulnerable.

IV. EAST ASIA'S MEDIUM-TERM CHALLENGES

What is needed to transform the current recovery process into a sustained and broadly shared economic expansion? The East Asian economies must concentrate on

revitalizing the private sector, streamlining the public sector, and forging a new social contract while recognizing the need to manage the forces of globalization.

1. Revitalizing the Private Sector

The East Asian economies must make persistent progress on financial and corporate sector restructuring in order to set the stage for the next sustained growth era. Together with financial sector restructuring, these economies must strengthen the financial system by requiring commercial banks to conduct prudent asset-liability management (through, for example, sufficient capital adequacy ratios and loan loss provisioning), by improving the regulatory and supervisory frameworks, and by developing capital markets, particularly those for long-term bonds. Competition from the capital markets is expected to put greater pressure on commercial banks to increase efficiency and productivity within prudent regulatory supervisory frameworks.

Together with corporate restructuring, these economies must strengthen corporate governance through improved disclosure and accounting requirements, redefining the role of the board of directors, and protection of minority shareholders. Since corporations are the mirror image of the underlying business societies and culture, improvement in corporate governance requires changes in the underlying business organization.[5] The technological developments and competition will induce such fundamental changes. Rapid developments in information technology are expected to widen the level-playing field, thus putting pressure to streamline business activities. Competition in the product, factor and capital markets is expected to impose greater discipline on the way corporations are run in these economies.

In order to enhance competitiveness, governments must create environments for the private sector to shift resources towards knowledge-based and information-intensive economic activities. In order to compete in a globalizing world economy, private firms must be able to create, acquire, use, and disseminate knowledge at low costs. Investment in human resources for a knowledge-based economy is vital to improving competitiveness in the global market.

2. Streamlining the Public Sector

Countries throughout East Asia are experiencing profound changes in governance. Even before the crisis, East Asians were becoming inclined to accept greater participation in government, greater accountability from officials, and more comprehensive social safety nets in exchange for fast-rising incomes. The cessation of growth unleashed forces of political change, leading to new governments in Indonesia, Korea, and Thailand, and creating greater demands for good governance.

[5] One of the features of the East Asian economies has been the prevalence of relationship-based businesses based on "trust." Such business organizations have played the role of lowering transactions and agency costs due to asymmetric information. In an increasingly globalizing open market environment, however, trust is not enough to sustain complex operations, and arms length relationships need to be developed.

Fiscal pressures—emanating from debt burdens and socio-economic changes—and globalization are making countries rethink the role of the state. Under pressure to do more with less, governments will have to focus on regulations that support market development, contain its negative spinoffs, and help incorporate those left behind; they may have to enlist private investment in activities that are now the sole domain of the state. Governments are also rethinking the organization of the state and according more responsibility and power to subnational governments. Finally, governments are being compelled to improve institutions of public managements—revenue and spending agencies and ministries—as well as the civil service.

Though East Asian public institutions performed critical functions relatively well in the Miracle period, the crisis has revealed some serious shortcomings in public sector performance. To increase the productivity of the public sector, governments must improve the institutions of expenditure and human resource management, civil service administration, and the service-delivery capacity.

Moving toward a higher degree of transparency and accountability may take some years, and involves many inter-related aspects of the governance regime. Attempts to improve accountability must be built into public sector management systems. For example, public expenditure monitoring and audit, along with a transparent budget process with timely reporting, are key mechanisms of oversight in the public expenditure system; and performance evaluation, merit-based promotion practice, and citizens' grievance processes are critical to ensuring the accountability of the civil service.

3. Forging a New Social Contract

In East Asia, social protection has traditionally been provided not by the government's social programmes or income transfers, but by a combination of economic growth, labor market flexibility, informal social safety nets (such as support by extended families and communities), enterprise policies (such as the provision of social services and long-term employment), and a controlled and gradual type of external liberalization. The economic crisis has shown that the economies in the region are indeed flexible in absorbing the consequences of the crises: households have protected their consumption of some critical items by drawing down on savings; informal social safety nets, provided by extended families and communities, have been quite resilient and effective in many countries; the labor market has proved flexible in securing employment, though real wages had to go down; and governments have beefed up safety net programs. What this means is that high savings, labor market flexibility, and informal safety nets must continue to be an integral part of the social safety net system.

Facing pressures from globalization, urbanization, and population aging, East Asian governments are now required to respond to heightened economic insecurity of households by ensuring that the poor and the socially vulnerable are insulated from downturns during bad times and benefit from growth during good times. With the simultaneous pace of globalization, growth in urban labor markets and the gradual aging of societies, there will likely be new demands on economic security. With growth increasingly dependent on skills and knowledge rather than on unskilled labor augmented

by capital, the risk should not be dismissed that wage gaps could widen, and the poor could be left out of the growth process. This risk underscores the important role of government, and the effects its revenue and spending policies have on incorporating low-income groups into the growth process—or leaving them by the wayside.

These pressures would force East Asian countries to move towards a more formalized social safety net society, particularly in high income countries such as Korea. Formal social safety nets are also important in China to make progress on SOE reform, which would require the state to play an important role in providing safety nets which have been traditionally provided by the SOEs in the form of housing, schooling, health care, old-age pensions, etc. It is also important to note that the provision of social safety nets is an important component of market reforms—it cushions the damage done on the most severely affected, it helps maintain the momentum of these reforms, and it avoids a backlash against the distributional and social consequences of globalization. However, it is quite unrealistic to implant top-notch OECD-type social protection systems into the East Asian countries, except for Korea which is already an OECD country. Governments should carefully examine internationally recognized best practices of social sector protection, and establish a formal safety net system in a way consistent with the evolving reality of the country, taking into account informal social safety nets based on families and communities.

Governments have to foster institutions able to respond to an aging, increasingly urban population that is likely to feel more vulnerable in a globalizing world economy. Government information systems must respond faster in times of crisis. And social safety nets have to be stronger, complementing traditional family and community support systems, and be able to expand (or contract) in line with economic conditions.

V. CONCLUDING REMARKS

Whether the East Asian economies can transform the current recovery process into a long-term growth path depends on whether they can reap the maximum benefit of globlization at the smallest cost and can provide a stable political and social environment conducive to a broadly shared economic expansion. In the short run, they must diligently pursue the restructuring and reform efforts in the financial and corporate sectors and manage the public debt and fiscal deficits.

In the medium term, these economies must focus on: revitalizing the private sector through reforming the financial sector, strengthening corporate governance, and enhancing the economic competitiveness and human resources; streamlining the public sector through improving public expenditure systems, reforming the civil service system, and making government more transparent and accountable; and forging a new social contract through achieving rapid poverty reduction and providing adequate social safety net systems.

Sustained economic growth requires total factor productivity to rise, in addition to a more educated labor force, efficient capital and technology. The reward to overcoming these medium-term challenges will be shown as higher total factor productivity and another era of stable, sustained economic growth.

Appendix Table. East Asia's Macroeconomic Performance: Real GDP Growth and CPI Inflation Rates

	Real GDP Growth Rate							*CPI Inflation Rate*						
	Actual					*Estimate*	*Projection*	*Actual*					*Projection*	
	1995	*1996*	*1997*	*1998*	*1999*	*2000*	*2001*	*1995*	*1996*	*1997*	*1998*	*1999*	*2000*	*2001*
East Asia 5														
Indonesia	8.2	8.0	4.5	-13.2	0.1	3.8	4.4	9.4	8.0	6.7	57.6	20.5	4.4	5.9
Korea	8.9	6.8	5.0	-6.7	10.7	8.3	5.9	4.5	4.9	4.5	7.5	0.8	2.5	3.1
Malaysia	9.8	10.0	7.5	-7.6	5.6	7.4	6.3	5.3	3.5	2.7	5.3	2.8	2.7	3.4
Philippines	4.8	5.8	5.1	-0.4	3.2	3.4	3.6	8.0	9.0	6.0	9.7	6.7	5.2	6.6
Thailand	8.9	5.9	-1.7	-10.2	4.2	5.3	5.1	5.8	5.9	5.5	8.0	0.3	2.3	3.1
Transition Economies														
China	10.5	9.6	8.8	7.8	7.1	7.5	7.5	16.9	8.3	2.8	-0.8	-1.4	0.8	2.0
Vietnam	9.5	9.3	8.2	4.4	4.4	5.3	4.7	16.8	5.6	3.1	8.8	4.3	7.0	9.0
Small Economies														
Cambodia	7.6	7.0	1.0	1.0	4.0	5.5	6.0	1.1	10.1	3.2	14.8	4.0	3.5	4.5
Lao PDR	7.3	6.8	6.9	4.0	4.0	4.5	5.0	19.6	13.0	27.5	91.0	128.4	n.a.	n.a.
Fiji	1.4	3.4	-1.8	-1.3	7.8	3.5	3.0	2.2	3.1	3.4	5.7	2.0	2.0	5.0
Papua New Guinea	-3.6	3.5	-4.6	2.5	3.9	4.7	4.5	17.3	11.6	3.9	13.6	14.9	14.6	5.0
Solomon Islands	7.0	0.6	-0.5	-7.0	1.0	2.0	3.0	9.6	11.8	8.1	12.3	8.3	8.0	7.0
Mongolia	6.3	2.4	4.0	3.5	3.3	4.3	4.5	56.8	49.3	36.6	9.4	7.6	n.a.	n.a.
East Asia NIEs (excl. Korea)														
Hong Kong SAR (China)	4.9	4.5	5.0	-5.1	3.0	6.7	4.4	9.1	6.3	5.8	2.8	-4.0	-1.6	1.7
Singapore	8.4	7.5	8.4	0.4	5.4	6.5	5.9	1.7	1.3	2.0	-0.3	0.1	1.6	1.9
Taiwan (China)	6.4	6.1	6.7	4.6	5.7	6.7	6.0	3.7	3.1	0.9	1.7	0.2	1.6	2.3
Japan	1.5	5.0	1.6	-2.5	0.2	1.3	1.5	-0.1	0.1	1.7	0.6	-0.3	-0.4	0.0
U.S.A.	2.9	3.6	4.2	4.3	4.1	4.9	3.2	2.8	2.9	2.3	1.5	2.2	3.1	2.6

Source: World Bank; IMF; Consensus Forecast, June 2000, for Hong Kong SAR (China), Singapore, Taiwan (China), Japan, and the USA.

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