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CONDITIONALITY AND SOUTH-EAST ASIAN ADJUSTMENT

Ana Marr

Working Paper 94

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Foreword

'Conditionality' is an ugly recent addition to the English language with which government officials in indebted countries have become all too familiar. In the context of this paper, conditionality refers to policy changes which an aid donor agency stipulates a government must undertake in order to obtain, or retain, access to the donor's financial support; it is an exchange of money for policy action. It arises most frequently in connection with the 'adjustment' programmes of the International Monetary Fund and World Bank but bilateral donors have made greater use of it in recent years.

This paper is a product of a research project underway in ODI, under my direction, which is examining the uses and limitations of donor conditionality as a way of bringing about improved economic policies in developing countries. It is planned to publish at least three Working Papers as outputs of this project, in addition to the main report which we hope to bring out as a book during 1997. A parallel paper dealing with Latin American experiences is currently in preparation by Ramani Gunatilaka, and an essay on the consistency of policy conditionality with the idea of national sovereignty, by Douglas Zormelo, is also nearing readiness. There may also be a country case study of Kenya.

Although they are not often thought of as 'adjusting' economies, this paper shows that most of the countries of South-East Asia have undergone adjustment programmes. The main issue addressed here is the role of donor conditionality in the design and execution of these. The countries studied are Indonesia, Malaysia, Philippines, South Korea and Thailand. Its author, Ana Marr, is a member of ODI's research staff.

The project of which this paper forms part is funded by the UK Overseas Development Administration and ODI would like to express its gratitude for this support. However, neither ODA nor any of the many people who have helped us in this project are implicated in the conclusions arrived at.

Tony Killick
July 1996

Contents

Tables

1. Introduction

This study aims to assess the importance of conditionality in the adoption of adjustment policies in a group of South-East Asian economies. For this purpose, conditionality is taken as referring to the changes in the economic policy that international financial institutions (IFIs) require of national governments in the course of adjustment. The study will concentrate mainly on the policy-related lending provided by the World Bank; wherever pertinent, IMF conditionality will also be investigated.

The countries covered are South Korea, Thailand, Indonesia, Malaysia and the Philippines. These countries are seldom thought of as 'adjusting', but in fact most of them have been extremely successful adjusters. The Philippines, as the exception in the group, illustrates the case of a country which, having been the recipient of highly conditional loans from outside agencies, failed to achieve complete success in its economic adjustment. There are therefore some relevant questions to be asked. Did outside agencies affect the policies adopted? Did they do so through conditionality or by means of influence, persuasion, financial support, etc.? What degree of responsibility should be attached to external institutions? Was the conditionality too harsh or too weak?

The study is divided into two periods. The first covers the period from the late 1950s to the late 1970s and the second, from the early 1980s to the early 1990s. Although the difference between the two periods cannot be regarded as a turning point, the 1980s saw an emphasis on the formulation and implementation of adjustment policies.

Following the oil-price shocks of the 1970s and early 1980s and the subsequent world recession, the foreign debt of these South-East Asian countries increased and their exports were severely affected. In the face of this situation, many international financial donors, in particular the World Bank, responded with fundamental changes in their aid policy, in particular the introduction of *structural adjustment lending*. Under this new regime, financial flows to developing countries were made conditional on their making changes in their economic policies.

Most of the South-East Asian economies adjusted quickly to this turn of events and achieved remarkable results; others took time to adjust and suffered the consequences of their sluggish decisions. The purpose of this paper is therefore to disentangle the factors behind the adoption, or lack of it, of these adjustment policies. It comes to the conclusion that, where adjustment policies were successfully implemented, this was the result of policies formulated by the domestic governments, and that conditionality played only a limited role in the adoption of such policies. In the cases where conditionality was most seriously attempted, adjustment policies were poorly implemented until a more favourable approach and a more committed national leader were in place.

The paper makes it clear that each country's experience of adjustment is unique and that the relationship between the stimulus of a policy-related loan and the recipient economy's response is conditioned both by donor and recipient objectives and by the political, social and economic structure of the recipient country.

The paper is organised as follows. Section 2 describes the adjustment policies formulated and implemented by the South-East Asian economies. Section 3 outlines the different factors which had an influence on the adoption of adjustment policies. The final section attempts to draw some lessons from this South-East Asian experience.

2. Adjustment in South-East Asia

Adjustment indicators

We first need to establish some criteria in order to assess the extent to which adjustment-type policies were adopted in the South-East Asian countries. Those policies' compliance with the criteria is examined within the framework of two specific periods, which describe the 'before and after' of the pursuit of a more stringent adjustment policy in each particular country.

The recommended adjustment policies which the World Bank and the IMF include in their conditional lending are well documented in the literature (see, for example, Mosley et al., 1995), and a consensus has developed on the type of policies that are conducive to economic adjustment (see Killick, 1995a; 1995b). For the purpose of this study, some of these policies are identified as follows:

Macroeconomic management

1. Reduction/avoidance of large fiscal deficits
2. Avoidance of inflationary credit
3. Establishing competitive and flexible exchange rates

Market friendliness

4. Dismantling of controls
5. Financial sector reform
6. Privatisation

Openness

7. Trade liberalisation
8. Export orientation
9. Exchange-control liberalisation

Broadly speaking, the study period (late 1950s to early 1990s) is divided into two by the events of the early 1980s. For each country, the breaking point represents the change in economic policy that the national government was obliged to put in place as a consequence of, mainly, external shocks but also of internal macro imbalances. The economic consequences of the oil-price shocks of the 1970s and the early 1980s prompted the adoption of adjustment policies in most of the South-East Asian economies. Admittedly some of them were already under considerable pressure for reform because of internal imbalances, but the drastic changes in the oil price intensified the extent of the region's economic problems. The terms of trade deteriorated, leading to a balance-of-payments deficit that impelled national governments to revise some of their economic policies. Most of the South-East Asian regimes reacted quickly to these new challenges, in some cases by sharply reversing their policies and adopting a more stringent set of economic measures.

With the exception of the Philippines, where political issues delayed the implementation of adjustment policies, these South-East Asian countries are often referred to as successful 'adjusters' rather than 'adjusting' economies. Although highly successful in adapting to new circumstances, these countries did not always apply the type of policies characterised by our criteria. Some of the strategies actually implemented led to serious macro imbalances, albeit not at Latin American levels. This section identifies the periods when the domestic economies generated macro imbalances which, in addition to external shocks, prompted the adoption of adjustment programmes.

South Korea: adjustment period 1980–93

Late 1950s to late 1970s

Despite a poor natural resource base and one of the world's highest population densities, South Korea has achieved remarkable economic performance. In the 1950s, after several attempts at autonomy, it was almost totally dependent on US foreign aid for food, fuel and other raw materials. In 1962, foreign aid financed as much as 80% of investment. This year also marked the beginning of a new strategy with the coming to power of President Park Chung Hee.

Having a small internal market and favourable relations with its trading partners, Korea under President Park sought a growth strategy that emphasised export promotion. However, in the period 1962–73, this aggressive export stance was combined with classic protection of the domestic market. Some structural and macroeconomic imbalances were generated during this period but, essentially, it was the nature of the response to the first oil price increase of 1973–4 which lay behind these imbalances. The government's response to the drastic surge in oil prices was expansionary. It stepped up aggregate demand in order to maintain the growth momentum of the 1960s. This forceful strategy was most clearly represented by the Heavy and Chemical Industries (HCI) drive, a large-scale public investment in basic chemical and heavy industries, which during 1976–8 absorbed more than 77% of all investment in manufacturing equipment (Sang-Woo Nam, 1991: 208).

This interventionist approach seems to have served its purpose of increasing industrial investment. However, the growing imbalances in the economy exerted inflationary pressures that threatened external competitiveness and economic growth. The situation was aggravated by the imposition of a fixed exchange rate following the devaluation of 1974 which weakened export growth still further. In addition, the introduction of VAT in 1977 exacerbated the already serious inflationary pressure by necessitating an across-the-board adjustment of the entire price structure. A major motivation for the new tax was the expectation that it would generate additional revenue which could be used to finance industrial plans (Haggard et al., 1994: 60).

Early 1980s

Despite a strong emphasis on growth and industrial development in the 1960s and 1970s, the imbalances caused by the Heavy and Chemical Industry drive forced the government into a sharp reversal of policy. A comprehensive stabilisation programme, launched in April 1979, proposed a severe reduction in HCI investment as well as fiscal and monetary restrictions. In October 1979, however, six months after the announcement of the programme, the second oil shock struck and President Park was assassinated. These events marked the end of almost two decades of unprecedented political stability and continuous economic growth. The GDP growth rate plummeted to 2.7% in 1980, its lowest level in two decades.

The most immediate and direct impact of the 1979–80 oil-price hike on the Korean economy was a sharp deterioration in the current account. The current account deficit, which had averaged less than US$0.5 billion during the 1976–8 period, rose sharply to US$4.15 billion (6.4% of GDP) in 1979 and to a peak of US$5.3 billion, 8.5% of GDP in 1980 (see Table 1). The sharp rise in international interest rates following the increase in oil prices, and the subsequent recession in OECD member countries, caused Korea's terms of trade to deteriorate and increased its foreign debt. Its gross long-term debt expanded by 27% in 1979 and by 19% in 1980, and its short-term debt grew by 73% in 1979 and 72% in 1980. Although official loans and IMF facilities accounted for only 22% of the rise in long-term debt in 1979, in 1980 this share jumped to 66% (Haggard et al., 1994: 56). Despite increasing concern at the growth of the foreign debt, the country was able to borrow throughout the crisis because of its proven export record (ibid.: 103).

Adjustment period 1980–93

The South Korean government began the process of adjustment with measures to stabilise the economy by reducing inflation. Later, it implemented policy reforms and restructuring of the economy.

The new policy package of January 1980 included two important adjustments: (i) a devaluation of the won by 20% to improve external competitiveness; (ii) an increase in interest rates in order to offset part of the effect of the currency

Table 1 **South Korea – macroeconomic indicators (%)**

	1980	*1981*	*1982*	*1983*	*1984*	*1985*	*1986*	*1987*	*1988*	*1989*	*1990*	*1991*	*1992*	*1993*
GDP growth[a]	–2.2	6.7	7.3	11.8	9.4	6.9	11.6	11.5	11.3	6.4	9.5	9.1	5.1	5.8
Fiscal balance/GDP[a]	–2.2	–3.3	–3.0	–1.0	–1.2	–1.2	–0.9	0.4	1.5	0.2	–0.7	–1.6	–0.5	0.6
Current account/GDP[a]	–8.5	–6.7	–3.6	–1.9	–1.5	–0.9	4.2	7.2	7.8	2.3	–0.9	–2.9	–1.3	0.3
Inflation rate[a]	28.7	21.3	7.2	3.4	2.3	2.5	2.8	3.0	7.1	5.7	8.6	9.3	6.2	4.8
Foreign debt-serv/exports[b]	19.7	21.7	22.4	21.2	21.3	27.3	26.7	32.3	14.8	11.8	10.7	7.1	7.6	9.2
Foreign debt/GDP[b]	47.9	49.3	52.3	50.8	48.4	52.5	44.3	29.8	19.9	14.9	13.9	13.6	14.4	14.4

Sources: [a] *International Financial Statistics Yearbook* (1995), [b] *World Debt Tables* (1989/90, 1991/2, 1992/3, 1994/5, 1996) devaluation by absorbing the excess liquidity. As a follow-up measure, a floating exchange-rate system based on a basket of major currencies was adopted in late February. Apart from a few exceptions, South Korea's exchange rate has remained competitive throughout the 1980s and early 1990s (Chung, 1996: 503).

The initial impact caused a surge in the rate of inflation, which peaked at 28.7% by the end of 1980. At the same time, the tight monetary policy discouraged domestic demand so severely that aggregate private investment declined by 11.5% in 1980. However, the measures ultimately brought about long-term improvements; the inflation rate dropped and the current account position reversed to a surplus between 1986 and 1989. In fact, the first half of the 1980s was a period of sharp deflation in Korea. By the late 1980s (1986–9), inflation averaged 4.7% and the current account recorded an annual surplus to average 5.4% of GDP for the period (see Table 1).

In the mid-1980s, financial, trade, and industrial reforms were initiated in order to reduce the role of government in the financial process, to provide access to foreign capital and technology, and to expose industry to greater external competition. Import tariffs were gradually reduced, a relaxation of price controls was introduced, and commercial banking regulations and supervision were liberalised. For instance, in compliance with the Tariff Act of 1984, the average tariff rate was reduced from 31.7% in 1982 to 21% in 1985 and to 7.5% by 1993 (Dailami, 1991: 399). The Bank of Korea shifted from direct credit allocation to a more market-oriented credit policy.

A large-scale privatisation scheme was introduced in the early 1980s. Although major banks and government-backed enterprises were sold to private firms, the scheme has been only partially implemented and the government continues to control some of these firms (Young-bum Park, 1993: 4, 22).

Financial decentralisation was introduced in 1981 with the privatisation of four major banks. By 1983, the government had reduced its control over day-to-day operations in all banks (Lee-Jay Cho and Yoon Hyung Kim, 1991: 610). In December 1988, the Bank of Korea and the Ministry of Finance adopted new measures to effect further financial liberalisation. As a result interest rates were deregulated in 1991, and lending rates at both the banks and non-banks had been freed by 1993 (Chung, 1996: 503).

Overall, South Korea's 1980s adjustment programme complies quite closely with the criteria listed at the beginning of this section. Faced by large macroeconomic imbalances exacerbated by the increases in oil prices, the government did not delay in embracing almost all the policies specified in our criteria. Financial, trade and industrial reforms were pursued, but the approach was gradual and sequential. Indeed, the initial stabilisation efforts laid the foundation for the subsequent industrial restructuring and trade liberalisation which in turn facilitated the liberalisation of the financial sector (see Table 2).

Table 2 Criteria of adjustment programmes – level of implementation (position by end of period)

	S. Korea 1980–93	*Indonesia 1983–92*	*Malaysia 1985–92*	*Thailand 1982–93*	*Philippines 1986–91*
Macroeconomic management					
Reduction/avoidance of large fiscal deficits	high	high	high	high	medium
Avoidance of inflationary credit	high	high	high	high	medium
Competitive and flexible exchange rate	high	high	high	high	medium
Market friendliness					
Dismantling of controls	medium	high	high	high	low
Financial sector reform	medium	high	medium	high	low
Privatisation	medium	medium	medium	medium	low
Openness					
Trade liberalisation	medium	high	medium	medium	low
Export orientation	high	high	high	high	medium
Exchange-control liberalisation	high	high	high	high	medium

Indonesia: adjustment period 1983–92

Late 1950s to late 1970s

Though endowed with a rich and diverse base of natural resources, Indonesia was one of the poorest countries in the world during the 1960s. Under President Sukarno (1949–65), attempts at state-led import substitution had failed, creating a stagnant economy with significant trade and budget deficits. In order to restore macroeconomic stability, the new regime of President Suharto put in place a stabilisation programme over the period 1967–73. Market-oriented reforms were introduced, the exchange rate was devalued and unified, imports were liberalised and foreign investment was actively encouraged. The stabilisation programme succeeded in reducing the inflation rate from its 635% peak in 1965 to 6% by 1970 (Wing et al., 1994: 30).

Like many other oil-exporting countries, Indonesia benefited from the first and second oil booms of the 1970s. Driven by oil exports, its economy grew at an average of 7% during the period 1970–81. At the same time, it became increasingly dependent on non-renewable exports – oil, liquefied natural gas, timber products, metals and minerals – which accounted for roughly 75% of the value of total exports (Thorbecke, 1992: 15).

With government revenues relying mainly on corporate taxation on oil, the surge in oil prices enabled the government to expand public expenditures. Investments in rural infrastructure, education, and health were significantly high during the 1970s. As a result, Indonesia was able to make remarkable progress in reducing poverty.

Early 1980s

Despite the impressive achievements of the previous decade, the economic policies of the early 1980s became progressively more inward-oriented, creating a substantial bias against exports and in favour of rent-seeking. The public sector expanded substantially, and the economy became highly vulnerable to external shocks as it was heavily dependent on oil revenues (for more details see Booth, 1992).

In view of the country's exposure to external factors, it is not difficult to infer that the origins of the macroeconomic disequilibrium which began to affect the economy in 1982 lay in two events. First, the slide in oil prices which reduced Indonesian oil exports from US$10.6 billion in 1981 to US$7.2 billion in 1982 (Thorbecke, 1992: 40) and second, the worldwide recession of the early 1980s which adversely influenced the demand for traditional Indonesian exports. The ratio of the current account balance to GDP – the macroeconomic indicator that best illustrates the effects of external shocks – plunged drastically from surplus in 1980 to deficit during the following two years to reach its lowest level in 1983 (see Table 3).

Adjustment period 1983–92

In response to the economic imbalances of the early 1980s, the government initiated its adjustment programme in 1983 and intensified it after the collapse of oil prices in 1986. During 1983–5, the adjustment programme was designed to achieve a current account balance and financial stability, while reducing the economy's dependence on oil revenues. Fiscal and monetary policies were tight. However, trade and industrial policies became even more inward-oriented and subject to government intervention. During the second phase of adjustment, 1986–92, the government implemented more stringent economic policies especially with regard to trade liberalisation.

How close was the adjustment programme of the 1980s to our criteria? To answer this question, we analyse these two periods of adjustment more closely and identify the difference in intensity.

Adjustment 1983–5 In order to reduce pressures on the government budget, a number of large-scale import-intensive projects were rephased in 1983, and sweeping tax reform was introduced in 1984. The government also restrained the import intensity of state enterprises' capital expenditures by imposing strict limits on the use of non-concessional trade credits. As a result of these policies, the public sector deficit began to improve immediately and, after a relapse in 1983, achieved a surplus in 1984 (see Table 3).

Targets for monetary expansion were based on maintaining low rates of inflation. A major financial reform, initiated in June 1983, removed interest-rate and credit ceilings for state bank operations, and simplified subsidised lending rates to priority sectors. The combination of cautious monetary management and austere fiscal restrictions reduced the rate of inflation significantly, from 18% in 1980 to its lowest level of 4.7% in 1985 (see Table 3).

On the external front, however, policies became more inward-oriented during this first period of adjustment. In fact, the aim of adjusting the balance of payments was effected largely through a rigorous reduction in imports rather than by promoting exports. In addition to the import-reducing fiscal policies, the 28% devaluation of the rupiah – in March 1983 – caused private sector demand to shift from imports to domestic substitutes. A proliferation of non-tariff barriers, in the form of import licences, bans, and quotas, and a complex port and customs clearance procedure, were also conducive to the compression of imports. It is estimated that in 1985 some 1,484 items were under approved-importer licence; representing about 26% of the total import value and 32% of domestic value added, excluding construction and services (Bhattacharya and Pangestu, 1993: 17).

As a result of these measures, the current account deficit declined from its peak of 7.4% in 1983 to just over 2% in 1985 (see Table 3). However, an increasing anti-export bias was caused by the distortions that non-tariff barriers imposed on the tradable-to-non-tradable price ratio. With prices of tradables set by international competition and prices of non-tradables were set by the domestic cost structure, the introduction of a quota on an imported input reduced the profitability of the tradable sector.

Adjustment 1986–92 The main feature of this period is the government's recognition of the need to deregulate trade and reduce the economy's reliance on import substitution. Although an across-the-board reduction of import tariffs was announced in March 1985, it was only in 1986 that a more comprehensive trade policy reform with a strong emphasis on export orientation was initiated.

Prompted by the collapse of oil prices in 1986, a series of steps were taken between 1986 and 1988 which led to the easing of import licensing and the promotion of exports and foreign investment. Measures to provide exporters with internationally priced inputs were announced in May 1986, and a highly efficient, corruption-free custom rebate facility for exporters was introduced; the rupiah was devalued by 31% in September 1986 and a competitive exchange rate was maintained; export restrictions were reduced in December 1987; and import licensing restrictions were lowered between 1986 and 1988. In May 1989, the government simplified the system of investment priorities and opened up new sectors to foreign markets. As a result, the current account deficit, after a surge in 1986, dropped to 1.2% in 1989 and has remained relatively low ever since (see Table 3). These policies also encouraged the expansion of non-oil exports which grew from 21% of total exports in 1983, to 61% in 1989 (Ahmed, 1991: 380, note 4).

A new set of financial measures introduced in October and December 1988 were aimed at further enhancing financial sector efficiency and developing capital markets. Other measures which followed in March 1989 and February 1991 were mainly intended to clarify rules set up in the previous reforms. The financial reform of October 1992 stipulated the end of specialised banks, and that there should be only general and people's banks. This extensive financial liberalisation has meant a growth in the overall number of banks from 61 in 1988 to 119 in 1991 and in the number of foreign banks operating in the country from 11 to 29 (Bhattacharya and Pangestu, 1993: 28). In November 1989 steps were taken to improve the performance of state enterprises, and by 1990 up to 30% of the shares of three large government cement enterprises were offered to the public. Although some privatisation has taken place, comprehensive reform has been delayed by political obstacles (Mardjana, 1992: 202–3).

These policies have helped improve the performance of most macroeconomic variables, but Indonesia's foreign debt has remained high. This burden increased considerably with the appreciation of the yen in 1986/7. The debt-service ratio rose to its highest level in 1988, and although it has declined since then, it is still above its early 1980s levels (see Table 3). However, Indonesia – unlike many highly indebted countries – has concentrated on resolving its debt problems by means of efforts to increase exports, and its foreign debt has thus not been perceived as a threat to the country's economic prospects (Ahmed and Chhibber, 1992).

Over these two periods of adjustment, Indonesia has shown remarkable flexibility. It has been able to change policies when growing inefficiencies were about to threaten the performance of the economy and has managed to achieve growth with a more equal society. In so doing, Indonesian economic policies have matched our criteria quite closely. The government's monetary and fiscal policies have been

Table 3 **Indonesia – macroeconomic indicators (%)**

	1980	*1981*	*1982*	*1983*	*1984*	*1985*	*1986*	*1987*	*1988*	*1989*	*1990*	*1991*	*1992*	*1993*
GDP growth[a]	9.9	7.9	2.2	4.2	7.0	2.5	5.9	4.9	5.8	7.5	7.2	7.0	6.5	6.5
Fiscal balance/GDP[a]	–2.3	–2.0	–1.8	–2.3	1.3	–1.0	–3.4	–0.8	–3.0	–1.9	0.4	0.4	–0.4	...
Current account/GDP[a]	4.0	–0.6	–5.6	–7.4	–2.1	–2.2	–4.9	–2.8	–1.7	–1.2	–2.8	–3.7	–2.2	–1.3
Inflation rate[a]	18.0	12.2	9.5	11.8	10.5	4.7	5.8	9.3	8.0	6.4	7.8	9.4	7.5	9.2
Foreign debt serv/exports[b]	13.9	14.1	18.1	20.1	22.3	28.8	37.3	37.0	40.2	38.0	31.5	34.0	31.6	33.8
Foreign debt/GDP[b]	28.0	25.4	27.4	36.7	38.1	40.9	55.9	73.0	63.9	61.3	64.1	65.1	66.4	58.9

Sources: [a] *International Financial Statistics Yearbook 1995*, [b] *World Debt Tables* (1989/90, 1991/2, 1992/3, 1994/5, 1996)

Table 4 **Malaysia – macroeconomic indicators (%)**

	1980	*1981*	*1982*	*1983*	*1984*	*1985*	*1986*	*1987*	*1988*	*1989*	*1990*	*1991*	*1992*	*1993*
GDP growth[a]	7.4	6.9	5.9	6.3	7.8	–1.0	1.0	5.4	8.9	9.2	9.7	8.7	7.8	8.3
Fiscal balance/GDP[a]	–6.0	–14.9	–16.1	–9.7	–6.5	–2.6	–9.2	–6.6	–0.3	–0.5	–1.3	–0.2	0.7	1.6
Current account/GDP[a]	–1.1	–9.9	–13.4	–11.6	–4.9	–1.9	–0.4	8.1	5.4	0.8	–2.0	–8.9	–3.1	–3.8
Inflation rate[a]	6.7	9.7	5.8	3.7	3.9	0.3	0.7	0.3	2.6	2.8	2.6	4.4	4.8	3.5
Foreign debt serv/exports[b]	6.3	8.2	10.7	11.6	14.2	30.4	21.8	21.2	24.8	15.1	10.3	7.7	6.6	7.8
Foreign debt/GDP[b]	28.0	38.2	52.2	62.9	60.5	69.9	84.5	77.1	56.7	45.6	39.3	39.9	36.4	38.7
Real effective exchange rate[c]	133.2	133.8	142.2	149.0	154.7	147.0	123.4	117.0	106.1	104.2	100.0	97.2	103.3	102.3

Sources: [a] *International Financial Statistics Yearbook 1995*, [b] *World Debt Tables* (1989/90, 1991/2, 1992/3, 1994/5, 1996), [c] *World Tables* (1995) conservative throughout both periods, and its determination to maintain a competitive exchange rate has never wavered. However, a loss of international competitiveness during the first 1983–5 period led to the implementation of more stringent trade policies and some structural reforms from 1986. Extensive reform of the financial sector was introduced between 1988 and 1992; however, attempts to privatise state-owned enterprises have not yet achieved a comprehensive reform (see Table 2).

Malaysia: adjustment period 1985–90

Late 1950s to late 1970s

From independence in 1957 to the late 1960s, the government pursued market-oriented policies with respect to industry but intervened to promote rural development and to provide social and physical infrastructure. Growth was stable during this period, based largely on the export of primary products, but there was little improvement in the level of absolute poverty, particularly amongst the *Bumiputera* (the ethnic Malays who constitute 58% of the total population, and other indigenous groups). In 1969, racial discontent led to riots that prompted a radical change in economic management.

To redress the inequality among ethnic groups, the government embraced the eradication of poverty as its main objective. During the 1970s, therefore, the focus of economic policy was on distributional objectives which were reflected in the New Economic Policy (NEP) initiated in 1971. In effect, this new approach meant encouraging the greater participation of Malays in modern economic activities.

An oil producer like Indonesia, Malaysia benefited from the surge in oil prices during the 1970s. Export earnings increased and provided the basis for the country's economic development which helped to finance public investments.

As commodity prices continued to rise, the government's expectations of an ever-growing economy prompted it to embark on an unprecedented fiscal expansion. It created a holding company, the Heavy Industries Corporation of Malaysia (HICOM), in November 1980 and sharply increased its investment in physical infrastructure, which was largely responsible for the high budget deficit of those years.

Early 1980s

Two events profoundly influenced the economy in the early 1980s. First, the deterioration in the terms of trade, due mainly to the decline in world trade, the fall in oil prices and the recession in the OECD countries. Second, the expansionary fiscal policy which led to the emergence of a significant debt overhang (Demery and Demery, 1992: 36–8). Over the early years of the decade, the fiscal expansion generated a massive budget deficit which more than doubled between 1980 and 1981 and peaked to 16% of GDP in 1982. As public expenditure was mainly financed by foreign borrowing, the foreign debt shot to over 50% in 1982 (see Table 4).

These imbalances were further exacerbated by the fiscal inflexibility caused by the proliferation of non-financial public enterprises (NFPEs). Between 1981 and 1985 the number of NFPEs rose from 498 to 702 (Salleh and Meyahathan, 1993: 19), and they played a significant role in channelling public-sector investment. Although the NFPEs depended on transfers from the exchequer to finance their programmes, they enjoyed operational autonomy. This combination of autonomy and access to fiscal funds is probably important in explaining the fiscal inflexibility of the early 1980s, since the NFPEs continued their investment spending when it was evident that a contractionary fiscal policy was needed (World Bank, 1989: 8).

Among the beneficiaries of this public investment were the HICOM industries. However, unlike Korea's HCI drive, which was aimed at achieving international competitiveness, the HICOM industries lost their competitiveness because of their poor management and excess capacity. This situation was aggravated by the government's exchange-rate policy during this period. The nominal exchange rate was dominated by inflows of external capital, and this upward pressure, combined with the fiscal expansion, caused a major real exchange-rate appreciation which further worsened the country's trade deficit.

The drastic drop in commodity prices created even more difficulties for the conduct of fiscal and monetary policy, together with a build-up of current account deficits and external debt. The current account deficit rose dramatically in 1982 and 1983, and the foreign debt/GDP ratio increased almost continuously between 1980 and 1986. As export revenues declined, the Malaysian economy experienced a deep recession with its GDP growth plunging from 7.8% in 1984 to its first negative ratio in decades in 1985 (see Table 4).

Adjustment period 1985–93

By the end of 1984, it was obvious that the government could not continue to accumulate foreign debt. But it was the sharp recession of 1985 that prompted it to implement a stringent programme of adjustment and liberalisation. The new emphasis on growth and efficiency was reflected in the economic programme initiated in 1985. The adjustment had two principal goals: first, to balance the national accounts, which would involve some reduction in the high level of fiscal deficit and the related external borrowing, and second, to restore competitiveness and profitability to the tradables sector, especially exports, which meant a real exchange-rate depreciation.

In order to reduce aggregate demand, a policy of fiscal restraint was combined with a more expansionary monetary stance which eased interest rates in the process. A range of reductions in fiscal spending was introduced, from development expenditures by the NFPEs to expenditures on defence, transport, irrigation, etc. The effect was immediate; by the end of 1985 the public sector deficit had fallen to less than 3%. However, domestic recession and falling petroleum prices meant lower tax revenues which generated significantly high fiscal deficits in 1986 and 1987 (see Table 4). Thereafter, the fiscal position recovered and turned into a surplus in 1992 and 1993, as a result of the privatisation of some public enterprises and a stricter fiscal policy.

On the trade front, the ringgit was allowed to depreciate against the dollar. Two major policy influences can be seen to have brought about this nominal depreciation: first, the significant fall in capital inflows, especially between 1984 and 1986, and second, the policy of a managed floating exchange rate carried out by the Central Bank since 1985. These downward movements in nominal rates, combined with moderation in domestic inflation, inevitably led to a significant real exchange-rate depreciation. As a result, competitiveness in the tradables sector was restored and the current account balance turned into a surplus between 1987 and 1989, reaching its peak in 1987 (see Table 4). After a relapse in 1991, the current account position once again improved, owing to a resurge in exports, and relatively small deficits were recorded in 1992 and 1993. An export-oriented industrialisation policy, initiated in the mid-1980s, has in fact delivered impressive returns, making Malaysia the nineteenth largest trading nation in the world by 1993 (Moore, 1996: 572).

A privatisation plan was announced in 1981 and partially implemented in the following decade. By 1992, 40 NFPEs had been taken over by the private sector and various public utilities had been privatised. However, it is far from clear that the scheme has managed to avoid the creation of private monopolies in areas such as airlines, water supply, telecommunications and electricity (Jomo, 1995: 229). The political imperative to favour the *Bumiputera* over other ethnic groups has undoubtedly been a factor in this incomplete privatisation and may still threaten the effectiveness of the programme (Salleh and Meyanathan, 1993: 23).

The New Development Policy, unveiled in 1991 as the successor to the twenty-year NEP, marked a turn away from social engineering and towards national consensus and the total eradication of poverty through rapid industrialisation and the promotion of manufacturing. Under the new policy, the sixth Five Year Plan (1991–5) emphasised financial reform (including financial deregulation) and strict monetary and fiscal controls to avoid overheating the economy (Moore, 1996: 575). Meanwhile, Malaysia continues to strive to establish itself as an attractive destination for foreign investment, promoting generous income tax allowances to 'pioneer' companies (ibid.: 572). Net inflows of foreign investment increased sharply over the period 1988–91 and stood at US$4.5 billion in 1992 and US$4.4 billion in 1993 (World Bank, 1995a: 325), the largest sources being Taiwan, Japan, South Korea, and Indonesia. Gradual deregulation of financial markets, economic and political stability, and cultural ties with other East Asian countries, have been important factors in Malaysia's success in attracting foreign direct investment.

To sum up, the adjustment phase in Malaysia has involved all the broad economic measures in our criteria. Despite expansionary budgets in the early 1980s, the main thrust of economic policy since the mid-1980s has been towards a reduction of the budget deficit engineered through privatisation programmes and cuts in public expenditure. Exchange-rate depreciation, on the other hand, has been the main instrument in achieving international competitiveness and improvements in the external accounts. However, more far-reaching structural reforms have been adopted only partially (see Table 2).

Thailand: adjustment period 1982–93

Late 1950s to late 1970s

Since the Bowring Treaty imposed by the British in 1855, Thailand has maintained a tradition of conservative fiscal and monetary policies. During the 1950s and 1960s the country established a pattern of growth dependent on import-substituting industrialisation and the expansion of agricultural production. In the 1970s, this import-substitution strategy was especially strong. Industrial policies, under the Board of Investment, favoured the development of large-scale manufacturing, with almost all the enterprises awarded privileged status producing for the home market. The share of heavy industries, as the most protected, rose from 31.9% in 1970 to 42.6% in 1979 (Christensen et al., 1993: 8).

Despite the adverse effects of the first oil shock of 1973, the government continued its investment in infrastructure financed by foreign borrowing. As a consequence, a substantial fiscal deficit had emerged by the end of 1970. However, the strategy resulted in increased growth, mainly because the prices of farm products, which constituted Thailand's major exports, also rose sharply in 1973. In fact, the composition of exports changed very little during the 1970s (Dixon, 1996: 1011).

Early 1980s

Unlike the first oil-price rise, the second oil shock of 1979 produced world commodity prices which were unfavourable to Thailand. This led to a sharp increase in the current account deficit from an average of 2.7% in the period 1970–78 to 7.6% in 1979. In addition, the closure of US bases in Thailand at the end of the Vietnam War meant that service receipts declined, exacerbating the balance-of-payments deficit still further.

The effects of these developments were magnified by the decision to keep the baht tied to the dollar during the 1960s and 1970s. This led to a rise in the real effective exchange rate in the early 1980s, despite the 8.7% nominal devaluation in 1981. Growing external and fiscal deficits pushed the inflation rate to its peak at 19.7% in 1980. To contain this, the government imposed price controls on state enterprises which, in addition to higher tariff protection and a steady appreciation of the real exchange rate, led to a misallocation of resources which contributed to the domestic imbalances of this period.

Adjustment 1982–93

The severe financial strains of the early 1980s prompted the Thai government to launch its Fifth National Economic and Social Development Plan for 1982–6. The baht was devalued by 10% against the dollar in 1981 and by 14.8% in 1984; thereafter it was pegged to a basket of major trading partners' currencies. The commercial banks' credit expansion was reduced in order to curb import demand.

Under the plan, economic policy shifted to the promotion of exports. The Board of Investment adopted foreign-exchange generation as a criterion for project approval, tariffs were drastically reduced and export-processing zones were established. The maximum tariff rate on most products was cut from 100% to 60% in 1982. However, this was offset by the imposition of tariffs on raw materials and intermediate goods in order to increase fiscal revenues (Doner and Laothamatas, 1994: 425). Foreign investment was also encouraged. During this period, Thailand evolved from a primary product exporter into an exporter of manufactured goods.

Results on the trade front were outstanding. The current account underwent a turnaround from a 7.2% (of GDP) deficit in 1983 to a surplus of 0.6% in 1986, as a result of the depreciation of the baht, the rise in the export prices of sugar, cassava, and rubber, the sharp decline in international oil prices, and the surge in the exports of manufactured products (see Table 5). However, this success in the current account position was not reflected in trade liberalisation. The complexity of the trade regime and the government's dependence on import taxes explain the delay in this regard. As noted above, despite rate reductions in 1982, the tariff structure remained broadly unchanged between 1985 and 1989. In addition, the scope of import licensing expanded from 6% of all product categories in 1982 to 8% in 1991 (GATT, 1991: 73, Table IV.11).

New incentives for foreign investment and the relocation of many industrial investments, from Japan and Taiwan in particular, have encouraged large capital inflows into the country. They increased significantly from an annual average of US$270m per year during 1980–85, to US$2.4 billion in 1990 (Christensen, 1993: 18). This high level of foreign investment largely explains the expansion of the manufacturing sector which increased its share of export earnings from 43% in 1985 to 80% in 1993 (Dixon, 1996: 1010). However, since 1990 the influx of foreign capital from Japan and the Asian NICs has stabilised, as a result of reduced outflows from these countries and the increasing costs, congestion and shortages of skilled labour in Thailand (ibid.: 1015).

During 1982–4 fiscal policy concentrated on reducing expenditure by imposing limits on public-sector wages and government borrowing. These policies failed, however, to reduce the fiscal deficit significantly; it decreased from 6.5% of GDP in 1982 to 5.3% in 1985 (see Table 5). In 1986 more substantial adjustments were implemented in both expenditure and revenue, with an increase in indirect taxation through the introduction of a value-added tax. As a consequence, the fiscal deficit fell substantially in 1987, with a continuous surplus since 1988 (see Table 5).

Irrecoverable loans by finance and securities companies brought financial crises in 1979 and 1983. As a consequence, the Bank of Thailand was given the supervisory function of intervening directly in bank affairs thereby improving the efficiency of the financial system (Doner and Unger, 1991). During the early 1990s Thailand intensified its efforts to become a regional financial centre through a programme of deregulation and institutional change. Monetary arrangements were liberalised, while the regulatory and supervisory framework of the financial sector was strengthened. Lending rates were liberalised, deposit interest rates (except for savings) were freed, and a conduit for international capital, the Bangkok International Banking Facility (BIBF), was created in March 1993 (Dixon, 1996: 1015–16).

Privatisation efforts were initiated in 1983, but no real progress was made until 1986. As of 1989, some 27 state-owned enterprises remained out of the 100 originally in operation (Doner and Laothamatas, 1994: 424). It is important to note, however, that Thailand has historically been the least interventionist country in this group of South-East Asian economies.

Overall, the Thai adjustment programme reflected a conservative fiscal and monetary policy which, in combination with a competitive exchange-rate policy, had been very successful in stabilising the economy during the first half of the 1980s. However, structural reforms took longer to be implemented. As manufactured exports boosted economic growth, the Thai government felt more

Table 5 **Thailand – macroeconomic indicators (%)**

	1980	*1981*	*1982*	*1983*	*1984*	*1985*	*1986*	*1987*	*1988*	*1989*	*1990*	*1991*	*1992*	*1993*
GDP growth[a]	4.8	5.9	5.4	5.6	5.8	4.6	5.5	9.5	13.3	12.2	11.6	8.1	7.6	7.8
Fiscal balance/GDP[a]	–5.1	–3.5	–6.5	–4.0	–3.5	–5.3	–4.3	–2.3	0.7	3.1	4.7	4.9	2.9	...
Current account/GDP[a]	–6.4	–7.4	–2.7	–7.2	–5.0	–4.0	0.6	–0.7	–2.7	–3.5	–8.5	–7.7	–5.8	...
Inflation rate[a]	19.7	12.7	5.3	3.7	0.9	2.4	1.8	2.5	3.9	5.4	5.9	5.7	4.1	3.6
Foreign debt serv/exports[b]	18.9	20.2	20.6	24.0	25.7	31.9	30.1	22.0	20.2	16.3	16.9	13.0	13.7	18.5
Foreign debt/GDP[b]	25.9	31.5	34.9	35.4	36.9	47.8	43.8	40.9	35.7	32.9	33.3	36.9	36.2	37.1

Sources: [a] *International Financial Statistics Yearbook 1995*, [b] *World Debt Tables* (1989/90, 1991/2, 1992/3, 1994/5, 1996)

Table 6 **The Philippines – macroeconomic indicators (%)**

	1980	*1981*	*1982*	*1983*	*1984*	*1985*	*1986*	*1987*	*1988*	*1989*	*1990*	*1991*	*1992*	*1993*
GDP growth[a]	5.2	2.9	3.6	1.9	–7.3	–7.3	3.4	4.3	6.8	6.2	3.0	–0.6	0.3	2.1
Fiscal balance/GDP[a]	–1.4	–4.3	–4.5	–2.0	–1.9	–2.0	–5.0	–2.5	–2.9	–2.1	–3.5	–2.1	–1.2	–1.5
Current account/GDP[a]	–5.9	–5.9	–8.6	–8.3	–4.1	–0.1	3.2	–1.3	–1.0	–3.4	–6.1	–2.3	–1.9	–6.0
Inflation rate[a]	18.2	13.1	10.2	10.0	50.3	23.1	0.8	3.8	8.8	12.2	14.1	18.7	8.9	7.6
Foreign debt serv/exports[b]	26.6	33.5	42.6	36.4	33.5	31.6	33.7	35.9	30.7	25.4	27.0	23.0	24.4	25.5
Foreign debt/GDP[b]	53.8	54.3	66.9	71.6	77.1	89.2	96.4	91.3	77.3	68.3	68.8	70.4	60.8	64.1
Real effect exchange rate[c]	140.5	145.0	150.5	126.6	125.4	137.2	107.1	98.5	95.8	102.3	100.0	98.8	109.6	106.9

Sources: [a] *International Financial Statistics Yearbook 1995*, [b] *World Debt Tables* (1989/90, 1991/2, 1992/3, 1994/5, 1996), [c] World Tables (1995) confident about the adoption of further economic reforms (see Table 2).

Philippines: partial adjustment 1986–91

Late 1950s to late 1970s

After being one of the most dynamic countries in the region in the 1950s, the Philippines gradually lost its impetus in the 1960s and 1970s. In contrast to the situation in South Korea, Filipino rural-based elites were politically positioned to resist land reform in the 1950s. The existence of these powerful groups has continued to exert a significant influence on major economic policies throughout the country's history.

From 1966 to 1986, the Marcos regime sought to retain power by developing a network of clients who, on the classic feudal model, delivered political support in return for economic benefits. Monetary and fiscal policies were highly expansionary and directed mainly to the sugar and coconut industries, which formed the principal base of political support for Marcos. The preferential loans extended to these crony firms in turn encouraged inefficient investments and financial overextension.

The bestowal of rents was also associated with classical instruments of protection – tariffs, quotas and subsidised credits – and the fostering of state-owned enterprises. Between 1972 and 1984, these enterprises expanded from 70 to 245 (Mosley, 1991: 42). This period was also characterised by the persistent recourse to foreign borrowing, which translated into high external debt and chronic balance-of-payments deficits.

In early 1970, the level of corruption, the poor economic performance, and the country's involvement in the Vietnam War, inflamed the anger of disadvantaged social groups, leading to a series of violent strikes. Marcos responded by declaring martial law in September 1972. In contrast to Pinochet's coup in Chile, Marcos did not pursue conservative economic policies. Instead, the martial law period (1973–80) saw a dramatic growth of the state, which served political as well as economic purposes. By setting up planning agencies, Marcos concentrated resources at the centre and weakened the power of local governments. Patronage and economic inefficiencies persisted. By the end of the 1970s, macroeconomic imbalances were attaining unsustainable levels. The inflation rate shot up to 17.5% in 1979 and 18.2% in 1980. The current account balance dropped to a deficit of 5.1% of GDP and 5.9% in 1979 and 1980 respectively, although the economy continued to grow.

Early 1980s

The external shocks of 1979–80 exacerbated the already severe macroeconomic imbalances. However, domestic demand continued to grow at a relatively high rate despite a deteriorating external environment, and no measures were taken to control the public sector deficits, adjust the exchange rate, and respond to the harder terms of foreign loans. Reasons for this response are intrinsically bound up with the relationship between cronyism, politics, and economic decision-making. Marcos delayed adjustment because of his need to maintain a base of support for his authoritarian regime.

The period was marked by two internal events: (i) the financial crisis of 1981, which led to a massive bailout of failing firms, many of them crony operations; and (ii) the political turmoil caused by the assassination of Benigno Aquino. The financial crisis of 1981 brought the downfall of a number of the most important industrial cronies, but at tremendous cost to the public finances and to the overall credibility of economic decision-making. As a consequence, the IMF refused to sign a stand-by credit in 1982, for only the second time since 1962 (Haggard, 1990: 237). During this year, the country's fiscal and trading situation worsened substantially. The fiscal deficit rose significantly between 1980 and 1982, and the current account of the balance of payments deteriorated to a record deficit of 8.6% of GDP in 1982 (see Table 6). At the same time, the non-crony private sector began to emerge as a new source of opposition.

In August 1983, the opposition leader Benigno Aquino was assassinated. Foreign credit became tighter and capital flight accelerated. In October, the peso was devalued by 21.4% and tariffs were increased. However, trade deficits persisted and a 90-day moratorium on external payments was declared, revealing a foreign debt crisis. Inflation emerged as a serious problem. By the end of 1983, the macroeconomic imbalances were critical, but the Central Bank concealed the extent of the crisis by manipulating the country's balance-of-payment accounts; foreign-exchange reserves were overstated by US$600m, and the foreign debt was understated by around US$2,000m (Hodgkinson, 1996: 911).

Despite pressures for economic change, the Marcos administration resisted a policy of stabilisation in view of the crucial elections of May 1984. However, after the election, under rising international pressure, the government was forced to introduce a draconian stabilisation programme which resulted in a severe recession. GDP fell by 7.3% for two consecutive years, 1984 and 1985. The peso was allowed to float and exchange controls, introduced in the 1983 crisis period, were eliminated; monetary policy was extremely tight. Although inflation was reduced from 50.3% in 1984 to 23.1% in 1985, further reforms were delayed because of the continuing power of the cronies in the agriculture sector. By the end of 1985, the economy exhibited its worst recession and public demonstrations mounted.

Partial adjustment 1986–91

In February 1986, Ferdinand Marcos was ousted from power and replaced by Corazon Aquino. The new government brought back to positions of power many representatives of the old estate-owning aristocracy who had been pushed aside under Marcos. Human rights lawyers and industrialists also became members of the administration.

In May 1986, the Philippines Institute of Development Studies, the Planning Ministry and the University of the Philippines jointly produced *Economic Recovery and Long-term Growth* (the Yellow Book) which served as the basis for the government's Development Plan for 1987–92. This document incorporated the following elements:

(i) a more open trade regime, with an exchange rate determined on the free market
(ii) reform of government financial institutions, and a limitation of the central bank's involvement in development finance
(iii) elimination of government intervention in the labour market (including minimum wages) and a move to local-level wage bargaining
(iv) a substantial extension of land reform
(v) limitation of debt-service payments to what the government could afford to pay (Mosley, 1991: 55)

Restrictive fiscal and monetary policies were implemented and some monopolies were dismantled. The initial result was an economic recovery with GDP growing at an annual average of 5.8% between 1987 and 1989 and inflation down to a phenomenal 0.8% in 1986 and 3.8% in 1987. Privatisation and trade liberalisation policies were not fully implemented, however, owing, primarily, to the revival of the Marcos cronies and the restoration of a powerful oligarchy in the business sector. According to a World Bank report, the average nominal tariff rate in the manufacturing sector was 31.8% in 1982; it decreased slightly to 28% in 1985 but it was still 28% in 1988. In 1989, the effective rate of protection of the manufacturing sector reached 55.5% (World Bank, 1990: 53). The privatisation process, on the other hand, was unable to change the oligopolistic structure that had prevailed during the Marcos regime, because most public assets remained in the hands of the cronies or were acquired by the business elite (Morisawa, 1993: 49–52).

A series of natural disasters, the loss of confidence in the political regime following the coup attempt in December 1989 and the Gulf crisis of 1990 weakened still further the fragile recovery, and by September 1990 the economic programme was substantially off-track (Balisacan, 1995: 39). In January and February 1991, the government drew up a stabilisation programme incorporating serious efforts to improve the fiscal imbalance and control the money supply. However, a crippling electricity shortage and several coup attempts offset these economic measures and the economy plummeted into recession in 1991 (see Table 6).

With the benefit of hindsight, the Aquino administration appears to have put more effort into blocking former Marcos lieutenants from regaining power than into lifting the country from its desperate economic plight. The economic policies implemented proved too limited to meet our structural adjustment criteria (see Table 2). In June 1992, the Philippines experienced its first peaceful democratic transition of power to President Ramos. The following January, Ramos launched his 'Philippines 2000' programme, which aimed to bring the Philippines to the level of a newly-industrialising country by the end of the century via a greater reliance on market forces (Malaluan, 1994: 39). A cornerstone of Ramos' reform programme is the desire to maintain investor and aid donor confidence. Measures were implemented to dismantle inefficient monopolies and improve the power supply. By the end of 1993 GDP growth had recovered to 2.1% (see Table 6). Other structural reforms were implemented during the Ramos administration, including the removal of almost all foreign-exchange controls and a continuation of the privatisation process (Hodgkinson, 1996: 912). However, problems remain, such as the survival of the landowning oligarchy, the lack of an entrepreneurial middle class and the doubtful support for the market-oriented technocrats (Malaluan, 1994: 48).

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As we have seen in this section, each country has a unique way of reacting to changing circumstances. The weight of political vis-à-vis purely economic influences seems to be the crucial factor in the *timing* of adjustment policies. In contrast to the rest of the region, the depth of the crisis and the unwillingness to adjust in the Philippines were largely the result of political factors. Instead of emerging from a period of macroeconomic crisis to one of adjustment in the early 1980s, the Philippines remained in a state of continuous crisis until the replacement of Marcos by the Aquino regime. Why did South Korea, Indonesia, Malaysia, and Thailand react so promptly in the implementation of adjustment policies? Why did the Philippines fail to do so? To what extent did outside agencies have an influence on these decisions? In the following section we deal with these and some other issues.

3. The role of conditionality in the adoption of adjustment policies

The presence of international financial institutions (IFIs) in South-East Asia has been diverse and their degree of influence on the decision-making of these countries has changed over the years. By considering each country individually, this section attempts to explain the extent of the IFIs' and other donors' influence on the adoption of these governments' adjustment policies, primarily those undertaken during the 1980s and described in the previous section.

South Korea

South Korean policy-making has been under the influence of the United States since the 1950s, though the relationship has often been strained. US investment in military support during and after the Korean War enabled the country to release larger amounts of finance for economic development than would otherwise have been the case, and US advisers used their leverage as the major donor to push for reforms on interest rates, inflation, the exchange rate and tariffs. The US also sponsored Korea's membership of the GATT, the IMF and the World Bank and helped guarantee its international creditworthiness (Kim and Leipziger, 1993: 39). Indeed, it has been suggested that Korea has at times participated in standby agreements with the IMF more to assure the lending and investing community of its creditworthiness than for the sake of the financial input involved (Carter, 1970). In addition, since 1963 Korea has had a technocratic civil service based on the Japanese model.

Major economic and institutional reforms took place under the regime of President Park Chung Hee (1961–79), who justified his military takeover from the Chang administration on the grounds of its economic inefficiency. Responding to pressure both from the US and from the domestic private sector, Park devalued the currency and unified the exchange rate, crucial factors in the country's subsequent export-led growth. South Korea accepted IMF standbys in 1970 and 1971. When domestic political pressures led to its failure to comply with the conditions attached to these loans, however, the United States, while agreeing with the IMF's reservations about Korean economic policy, nonetheless stepped in to extend additional loans (Haggard et al., 1994: 31).

In a bid to gain the political support of the *chaebols* (large trading conglomerates), Park declared martial law in 1972; at the same time he increased aid for rural welfare. As noted in section 2, his ambitious plan for the development of Heavy and Chemical Industry (HCI) generated significant macroeconomic imbalances. As early as 1974 the World Bank and the government's advisory board of Korean technocrats were beginning to raise doubts about its effectiveness (ibid.: 41), but Park stuck to the plan in the name of national security. With the recovery of the global and local economy in 1975 it became easier to maintain the plan's momentum, but within two or three years inflation had begun to rise and internal pressures were again felt, resulting in electoral setbacks. Faced with economic and political difficulties Park had recourse to the advice of the technocrats, who again came to prominence in the administration.

In 1978, in consultation with the technocrats, Park asked the Economic and Scientific Council, the Bank of Korea and the Korean Development Institute to put forward measures to address the country's economic problems. He then charged the Economic Planning Board (EPB) with the task of designing and implementing a stabilisation programme (Sang-Woo, 1991). In this he received strong support from the Deputy Prime Minister and chief economic adviser, Hyun Hwack Shin. The Deputy PM is simultaneously minister for the EPB, a body which lies at the heart of economic policy issues, carrying out the functions of forecasting, planning, budget-making and advising the President. The indirect nature of the EPB's relation to the economy (unlike that of the Finance Ministry) gives it a certain amount of flexibility and autonomy, and under Hyun it promoted a team of stabilising and liberalising economists whose ideas were quickly accepted (Byung, 1991: 104). As noted in section 2, the comprehensive stabilisation plan launched in April 1979 was overtaken by political problems, culminating in Park's assassination in October 1979. Under the Chun government which followed (1980–86), officials undertook major structural adjustment programmes which a democratic government would have found difficult to implement (Lee-Jay Cho and Yoon Hyung Kim, 1991: 610). Highly centralised decision-making and an authoritarian political structure combined to push through the interrupted stabilisation programme. The World Bank contributed some financial support to the implementation of the reforms, but refrained from imposing severe conditions.

There was thus the political will and the administrative capacity to implement a comprehensive restructuring of the economy without undue outside pressure. The role of the World Bank in the South Korean restructuring has been called 'useful but minimal' (Westphal, 1991: 411). The two Structural Adjustment Loans (SALs) met 13% of the country's external financing needs in 1982–3 and, importantly, confirmed Korea's creditworthiness in international financial markets (Dailami, 1991: 402). However, it is likely that the reform would have been implemented in any case, though perhaps at a slower pace. The World Bank itself reported that its supervision of the reform programme was not crucial to its success (World Bank, 1991: 15).

In the 1980s South Korea received four IMF stand-by loans, two SALs worth US$250m and US$300m, and an Industry and Finance Loan (see Appendix). The

SALs were low on specific conditions; it had been clear for some time that the government was already committed to a programme of reform (Dailami, 1991: 402). Under SAL I the government agreed to defer its support for the automotive industry. In fact it continued to support it and, given its subsequent success, this condition was omitted from SAL II. In other fields (e.g. promotion of energy efficiency) South Korea surpassed the targets that had been set for it (ibid.: 400). In essence, the influence of the IFIs and the United States – the country's largest and longest-established donor – has generally been exercised by means of financial support, advice and dialogue rather than through strict conditionality.

Economic policy-making has continued essentially along the same lines into the democratic era, though democratic institutions mean that the technocrats are no longer so immune from political pressures. Liberalisation of trade and financial markets has therefore slowed somewhat, but is still on course. By 1988 South Korea had repaid all its IMF loans, and its last negotiation with the World Bank was for a five-year loan in 1985.

Indonesia

Virtually all observers are agreed that Indonesia, unlike some other developing countries, carried out its structural adjustment programme in the 1980s without pressure from IMF/World Bank conditionality (see for example, Azis, 1994). A key reason for its steady pursuit, in times of both expansion and recession, of fundamentally conservative macroeconomic policies, which reassured creditors, avoided imbalances, and removed the need for emergency loans linked to unpopular policies and imposed in an atmosphere of crisis. Certainly Indonesia paid careful attention to policy advice and recommendations from the IMF and the World Bank, but it should be noted that it had already committed itself voluntarily to policies of market liberalisation and budgetary constraint similar to those forced on other countries by the IMF as a *quid pro quo* for loans (Thorbecke, 1992: 43).

By the late 1980s Indonesia had attained a position from which it could hope to model itself on the East Asian 'tiger' economies (Cribb, 1996: 372; Hill, 1995: 775). However, as recently as 1965 it had been one of the poorest countries in the world, with inflation peaking at 635% in 1967, the year in which Suharto came to power. The independence leader Sukarno had declared martial law in 1957 and ruled thereafter through a highly authoritarian system known as 'Guided Democracy'. This involved as major players not only the army but the Indonesian Communist Party (PKI), elements of whose Marxist ideology were incorporated into the state ideology. It was ostensibly the spectre of PKI rule after Sukarno's death, along with the escalating economic crisis, which motivated Suharto's seizure of power. The immediate trigger, however, was a PKI-inspired coup attempt in September 1965, the suppression of which elevated Suharto to the status of Sukarno's chief rival for power (Wing et al., 1994: 29). Thereafter Suharto quickly built up his own power base, forming the 'New Order' coalition which pressed for policies of economic recovery and political stabilisation, and crushing the PKI through a combination of proscription, imprisonment and murder.

With Suharto's accession to power, economic reform began immediately. Working closely with the InterGovernmental Group on Indonesia (IGGI) (comprising all the country's major aid donors) and with the assistance of the IMF, Suharto's US-trained economic team, known as the 'technocrats', the 'economists', or 'the Berkeley Mafia', prepared and carried through a programme of rapid economic stabilisation. This team has been a constant feature in the administration ever since, providing valuable continuity in times of crisis (Wing et al., 1994: 29) and demonstrating to creditors and financial institutions the continuing capacity of the regime to plan and implement economic reforms successfully (Hill, 1995: 781). As free marketeers with neo-classical leanings, they have often been perceived as a force opposed to the 'engineers' or 'technicians' controlling other government departments (such as the Ministries of Trade and Industry and the Investment Co-ordinating Board), who have tended to demand expansionary economic policies – with much success during periods of oil price boom (Wing et al., 1994: 41; Robison, 1988: 32–3). While the rivalry between the two groups is real, and has produced sometimes confused and contradictory economic policies, it should be noted that

> the technocrats are not free market ideologues . . . and have not been averse to state intervention to promote other objectives besides economic efficiency. They practise neoclassical economics in the sense that they believe that some methods of intervention (especially those that are market-compatible) yield better results than others (Wing et al., 1994: 40).

By the end of the 1960s the economy had stabilised and foreign aid had been resumed, while creditors made increasing demands on the government to reopen the economy to foreign investment (demands which sat easily with the ideological bent of the 'economists' but were resisted by their rivals). With the cushion of vast oil revenues, the government was able to ignore such outside pressure, and it was not until the early 1980s, with the current account crisis and the fall in oil prices, that the 'economists' really gained the upper hand over the 'technicians'. A damning report by the World Bank in 1981, at first resented by the government as unwarranted interference in domestic affairs (Robison, 1988: 36), was finally accepted, and with support from Suharto the 'economists' were able to push ahead with their plan for voluntary implementation of contractionary fiscal and monetary policies (ibid.: 41; Thorbecke, 1992: 43). The ascendancy of the technocrats brought tangible benefits; two World Bank Trade Policy Loans in March 1987 and August 1988 (which helped finance trade reforms which were already under way, rather than being imposed), and two Private Sector Development Loans in 1989 and 1991.

World Bank policy advice and recommendations have in essence been concentrated on macroeconomic management and structural reform, in support of the government's pre-existing strategy. The credibility of the government in issues of economic policy has allowed further World Bank sectoral loans in the fields of housing, urban development and irrigation even when, with the 1986 fall in oil prices and consequent rise in external debt, commercial loans were hard to secure. This credibility, underpinned by annual World Bank reports and two SALs, persuaded the InterGovernmental Group on Indonesia to make available balance-of-payments loans and other aid totalling US$3.7 billion in the three years to 1991, enabling the government to continue its programme of deregulation and restructure its external debt, while maintaining the confidence of private investors (Sadiq, 1991: 379–80).

Policy reform was able to be pushed through, in part because, as many observers have noted, Indonesia is in effect a corporatist state in which decision-making has little to do with elected politicians or society at large (see for example, Bhattacharya and Pangestu, 1993; Wing et al., 1994). Faced with domestic and international pressure for a restoration of democracy, Suharto attempted to entrench himself in power as early as the elections of 1971, which were held under conditions designed to ensure the parliamentary dominance of the government grouping, Golkar. (Suharto/Golkar won 62% of the vote in that election, and the same percentage in the 1977 election, rising to 64% in 1982 and 73% in 1987.) Golkar is essentially an umbrella group of community organisations and trade unions, dominated by Suharto. Dissent has come from many quarters, including students demanding true democracy, and particularly from religious groups. There has also been disquiet at the cosy business relationships established between 'New Order' members and the ethnic Chinese (*cukong*) business community, culminating in the Malari riots of 1974. Despite these manifestations of dissent, the opposition forces remain disorganised and fragmented, weakened as much by their internal feuding as by government repression (Cribb, 1996: 371). Continued repression has been justified, however, on the grounds that the banned PKI remains a threat.

The weakness of political and civil institutions means that any effective government administration is in a position to force through policy, including economic reform (Azis, 1994: 397). Thus policies originating with the pragmatic, well-organised 'economist' group, once approved by the President, have tended to be implemented rapidly and efficiently. The first adjustment plan was implemented in 1983. While World Bank analysis, advice and lending continued throughout the period of the adjustment programme, there was no IMF lending during the 1980s. The first World Bank loan of US$300m was not made until 1987 and it is clear that the Indonesian response to the crisis was essentially a voluntary one, elaborated within the government and carried out without direct outside pressure (Sadiq, 1991: 378–9; Azis, 1994: 410).

The ascendancy of the technocrats was consolidated by their success in persuading the World Bank, the IMF and the IGGI to agree to their proposals for concessionary loans (Wing et al., 1994: 41). While they are not the sole influence on the President, they continue for the moment to be the most important one. Suharto's advisers have tended always to come from a small elite circle. This is in large part due to a deliberate decision on his part in the early days of his rule that, in order to stimulate prolonged economic growth, political squabbling and the promotion of disparate political and economic perspectives must be kept to a minimum.

This is not to say that policy-making proceeds free of external or internal pressures. Wing et al. (1994: 36–40) suggest seven variables which impinge on economic policy-making in the New Order administration. They are: *the institutional memory* (the memory of hyperinflation and the consequent determination to stick to conservative budgetary policies); *agrarian radicalism* (the need to improve rural conditions in order to forestall a resurgence of communism or millenarian movements); *regionalism, ethnicity and religion* (the need to assuage separatist feelings by delivering real economic benefits to Outer Islanders); *economic nationalism* (the memory of Dutch colonialism among those of Suharto's generation produces a hostility to foreign ownership of capital, and hence a sometimes less than wholehearted commitment to laissez-faire capitalism); *Pribumi-ism* (a resentment of ethnic Chinese economic power, reflected in proposals that state-sponsored enterprises should be established with *pribumi* (similar to *Bumiputera* in Malaysia) at the helm, as a counterweight to Chinese businesses); *political patronage* (the need to reward supporters of Suharto, particularly military personnel); and *the personal element* (Suharto's peasant and military background, which continues to inform much of his social and economic thinking).

Economic policy and performance are also subject to some outside political influence, much of it concerned with human rights abuses, labour conditions and the East Timor question. In 1992 Portugal successfully opposed a European Community–ASEAN economic co-operation treaty because of Indonesia's failure to conform to ILO standards on working conditions (Cribb, 1996: 375). Also in 1992 the Netherlands attempted to link aid with improvements in human rights with little success, however, Indonesia reacted angrily, dissolving the IGGI and replacing it with the Consultative Group for Indonesia, chaired by the World Bank and without Dutch representation.

Such internal and external pressures mean that the administration is forced to perform a delicate balancing act, and that the macroeconomic policies adopted fall short of what is demanded by the World Bank and the IMF. However, given the progress of the economy, the ascendancy of the technocrats, their constant dialogue with the IFIs and their conservative instincts, coupled with the political capacity of the government to push through major reform, conditionality must be considered largely unnecessary.

Malaysia

Malaysia has achieved impressive levels of growth without resorting to conditional or structural adjustment loans from the IMF and the World Bank, the only non-commercial loans it has negotiated being for particular infrastructure projects. As seen in section 2, the economy grew strongly after the adoption of the New Economic Policy in 1971, but stalled in 1981–3 in response to the worldwide recession. A two-year structural adjustment programme produced a temporary upturn in 1984, but GDP growth plunged to –1.1% in 1985 as demand and prices fell for the country's main exports – amongst them palm oil, tin, hardwoods and manufactured goods. The collapse of tin-trading on the London tin market in October 1985, which coincided with a series of financial scandals and political crises, brought home the full extent of the country's difficulties and prompted some hard decisions. Between 1985 and 1987 legislation was introduced designed to encourage foreign investment, including a relaxation of regulations on foreign equities and the freeing of credit restrictions (Moore, 1996: 571). While this reform was carried out in consultation with the World Bank and the IMF, there was no request for structural adjustment loans.

Throughout Malaysia's recent history, a major government preoccupation has been an attempt to redress the economic imbalance amongst racial groups. Inter-ethnic tension, manifested in often bloody outbreaks of rioting and looting, is a recurring feature of national life. The 1957 Constitution recognised the economic dominance of the Chinese (and, to a lesser extent, Indian) communities, and attempted to balance this by ensuring the political dominance of ethnic Malays. Serious rioting in 1969 prompted a change of tack, however, and the National Economic Policy (NEP) of 1971 sought to remove the identification of economic power with race. Thus, the government's policy of industrialisation since the second five-year plan (1971–5) has explicitly included the aim of increasing *bumiputera* participation in non-agricultural work which implies high public investment, as demonstrated in section 2.

Problems with such an expansionary approach became evident with the world recession and the consequent loss of foreign reserves. Mahathir came to power in 1981 determined to put more emphasis on growth. The limited recovery in 1983 and 1984 and the further drop in 1985 served to awaken widespread worries among Malaysians about the state of their economy, and put Mahathir in a stronger position to push through reform. The World Bank and the IMF offered a package of conditional loans to accompany their traditional recipe of structural adjustment. The Mahathir administration chose, however, not to accept the package formally, and continued with its homegrown adjustment programme (Bruton, 1994: 311), as described in section 2.

Thailand

As seen in section 2, Thailand has shown firm fiscal and monetary restraint since the late 1950s. This is in large part due to the strict macroeconomic management of a class of technocrats who have historically enjoyed substantial autonomy in policy-making. Their conservative traditions derive in some degree from the historic influence of British advisers in the Kingdom; they also dovetail neatly with the abiding fear of the Thai monarchy and bureaucracy that indebtedness to foreign powers will bring with it loss of national sovereignty and independence. Hence a law was passed in 1959 restricting budget deficits to a maximum of 20% of public expenditure, and throughout the 1970s the ratio of external public debt service was kept to a maximum of 7% of export earnings (Christensen et al., 1993: 27–8).

Despite this relatively long tradition of macroeconomic conservatism, the collapse of non-oil commodity prices in 1979–80 triggered a crisis in the Thai economic system which eventually engendered a major restructuring. In the face of substantial imbalances caused by the oil crisis, the government of General Prem (1979–88) initiated discussions with the IMF and the World Bank on an appropriate policy response. During the period 1981–93 the Thai government received three IMF standby loans, two SALs and a Distribution System and Energy Efficiency Loan (see Appendix). Crucially, these provided the necessary financial inflows to preserve Thailand's ratings on the international credit market.

The history of the implementation of the SALs reveals a low degree of conditionality. The first SAL was implemented satisfactorily. The second was prone to slippages, particularly in the area of price reforms, but – almost uniquely for any country – there was no tranching. This was due to confidence on the part of the World Bank in the government's clear commitment to reform, to the limited usefulness of tranching as a control mechanism, given the substantial 'down-payment' already in place, and to the government's reluctance to accept what was seen as undue foreign interference (Sahasakul et al., 1991: 95). The World Bank insisted on failures of compliance being addressed in the third SAL, but as growth resumed and Thailand gained access to commercial credit from the Tokyo market, the government, now in a much stronger bargaining position, abandoned negotiations and the SAL was allowed to lapse. Thailand refused further disbursement of conditional loans, even though the World Bank argued strongly against this (Dixon, 1996: 1011). Such resistance to the blunt instrument of conditionality was perhaps to be expected. Thailand's political and economic history has in fact always been characterised by an openness to outside influences, coupled with firm defence of national sovereignty and independence, and it remains a source of pride to Thais that, alone amongst the South-East Asian nations, their country did not fall under European colonialism in the nineteenth century.

In effect, according to several of Sahasakul's (1991) informants, the SALs raised Thailand's creditworthiness, acted as a catalyst to open up access to credit from other sources, and introduced new and more efficient techniques of macroeconomic management and co-ordination between departments. They also contributed financially to the implementation of adjustment policies. However, it should be stressed that they did not wholly represent measures that the Thai government had not itself formulated in previous years. It has in fact been claimed that between a third and a half of the SAL measures had been incorporated into the Fifth Economic and Social Development Plan for 1982–6 (see the interviews carried out by Sahasakul and his colleagues, 1991: 138–9), and indeed many of the measures contained in SAL I drew in some degree on Thai proposals made in connection with the Fifth Plan (Doner and Laothamatas, 1994: 421). This would suggest that the government had serious intentions to restructure the economy even before its Letter of Development Policy was submitted in February 1982 for the first SAL. Those elements of the SAL which were conditional were generally the least successfully implemented, for example a restructuring of petroleum product pricing, tariff rationalisation and price increases in water and bus services (Sahasakul et al., 1991: 100).

Moreover, before any SALs had been awarded, the government had already taken action in the direction of structural adjustment: export taxes on major agricultural exports were eliminated or lowered; the baht was devalued by 10%; power tariffs and petroleum prices rose as all subsidies were removed. While some of these measures were carried out in the context of an ongoing IMF standby, this loan, rather than imposing policy conditionality, was used by the government as a pretext for the implementation of an austerity programme. In fact, when it became clear that the economy was left dangerously exposed by the expansionary policies of the early 1980s, Cabinet changes were prompted and a group of orthodox technocrats gained power. As head of the Ministry of Finance, Sommai Hoontrakul favoured a rigorous stabilisation programme and negotiated an IMF loan as a way of justifying the need for adopting such a programme (Christensen et al., 1993: 29).

It should also be noted that, even after the period of the SALs, the government continued to implement economic reforms (Sahasakul et al., 1991: 113). It may therefore be inferred from all of the above that any conditionality involved in the acquisition of the SALs was operating at a very low level, and that the Thai government was in general following its own instincts in applying structural reforms, rather than having them forced upon it. Most of the measures associated with the SALs would have been carried out to varying extents without them, though perhaps with some delay (ibid.: 100–101).

The nature of the Thai political and administrative systems undoubtedly contributed to the governments' capacity to push through reform, at least at the macroeconomic level. The 'Revolution' of 1932 had ushered in a period of military-bureaucratic rule, characterised by patron–client relations and the rise and fall of Latin American-style military *caudillos*, which left untouched the traditional social structure. The patron–client nature of political life makes it extremely difficult to liberalise particular sectors of the economy, but allows a good deal of autonomy and flexibility to the central bureaucracy. Prem's administration, while ostensibly politically unstable, in fact saw the implementation of genuine macroeconomic reforms. Experienced and professional technocrats put together and carried through a coherent programme of stabilisation with full support from the Prime Minister, while organised opposition (for example, from the military, organised labour or farmers' groups) was limited. Where opposition did emerge, Prem was able to play off the military and the parties against each other, protecting his technocrats and ensuring the maintenance of the reforms. Power of patronage in Thailand is exercised through the holding of ministerial portfolios; elected politicians have little power to supervise the bureaucracy or influence the budget-making process, but can wield considerable influence over particular sectors of the economy. The technocrats were thus notably less successful in implementing sectoral reforms; these tended to fail when opposed by the political leaders necessary to Prem's coalition.

From 1986 onwards the Thai economy showed remarkable growth, particularly in the field of manufacturing. Investment that had previously gone to such countries as South Korea and Taiwan now began, with increasing economic stability and low labour costs, to relocate to Thailand. Surplus manufacturing capacity was directed to export production, and with the devaluation of the baht Thai exports improved their competitiveness. As exports grew, Thai entrepreneurs energetically expanded existing markets and sought out new ones. As shown in section 2, from 1986 to1991 GDP grew at 10% a year and the value of exports by 30% a year. While this growth has since slowed (GDP grew by an average of 7.7% in 1992–3), Thailand continues to experience rapid integration into regional and world markets.

The Philippines

During the Marcos regime conditionality was imposed far more extensively in the Philippines than elsewhere in South-East Asia. Nevertheless domestic factors were ultimately more important in the implementation or non-implementation of economic reforms. When Corazon Aquino came to power, her team of 'economists' naturally favoured the policies approved by the IMF and the World Bank, and conditionality was therefore superfluous (though, as demonstrated in section 2, Aquino was in fact prevented from carrying out radical economic reforms by the entrenched power of the cronies of the Marcos era and some of her own supporters). Fidel Ramos in turn came to power with a determination to implement market-oriented reforms, and has had some success, though the old oligarchy remains and there is little sign of the development of an entrepreneurial middle class in the Philippines.

The Marcos regime of 1966–86 was characterised by cronyism, patronage and 'weak authoritarianism' (Haggard, 1990). Such a political structure meant that economic decision-making was heavily influenced by powerful vested interests, and the possibility of reform was thus very limited. Almost every year since 1962, the Philippines has received loans from the IMF and the World Bank (see Appendix). Between 1973 and 1981 the World Bank provided US$2.6 billion in project loans (Bello et al., 1982: 24). Continuing balance-of-payments deficits were handled by recourse to IMF standby loans, but the IMF was generally unsuccessful in enforcing compliance with their conditions; it failed to enforce a real devaluation, which was evaded by the government's turning instead to high-cost foreign borrowing (Mosley, 1991: 48). After the declaration of martial law in 1972, the economy was managed essentially by presidential decree, and an expanding economy in the 1970s masked the inefficiency and corruption of the system.

The financial crisis of the early 1980s finally forced a reluctant partial shift on the part of the administration. The World Bank stepped in to the rescue (two SALs and six SECALs provided US$1.9 billion during the 1980s) on condition that Marcos' cronies were kept in check and the 'technocrats' were allowed to gain the ascendancy (Bello et al., 1982: 185–93). The first SAL (US$200m between 1980 and 1985) was formulated under strict World Bank supervision; however, while some of its conditions were carried through (for example, tariff rates were lowered), resistance from Marcos' political advisers to the technocrats, and generalised corruption, had the effect of weakening the adjustment efforts. In 1983, despite protests from the World Bank, the government actually reimposed a series of tariff controls (Haggard, 1990: 230).

With one eye on the elections of 1984, the administration was extremely reluctant to take tough measures with the economy and risk political fall-out; it even manipulated the figures to make the country's balance-of-payments position appear more acceptable than it was. From the moment this was disclosed in December 1983, foreign creditors and financial institutions became much more rigorous in their dealings with the government and conditionality was tightened, the IMF demanding policy change prior to disbursing funds (ibid.: 240). However, outsiders did not always manage to deal with the people closest to power. While the IFIs trusted the capabilities of the technocrats, the latter actually had much less influence within the administration than appeared from outside, often finding themselves marginalised from the policy-making process. Their presence in fact helped to legitimise a flawed system of economic management.

It was not until 1984–5 that external and domestic pressure forced the appointment of an orthodox banker, José Fernandez, as Governor of the Central Bank, and a strict monetarist programme was proposed and pushed through. While the stabilisation programme had some success, it was opposed by the Marcos clique, cronyism and patronage continued to blunt its effectiveness, and the administration continued to resist pressure for far-reaching structural adjustment.

Fernandez was retained as Central Bank Governor by the Corazon Aquino administration following Marcos' ousting in February 1986. Conditionality was again relaxed as the IFIs perceived that the new government was willing to take policy initiatives without outside pressure (Mosley, 1991: 55). All economic portfolios with the exception of the National Economic and Development Authority passed to the control of Ministers with roots in the private sector (Haggard, 1990: 246). The new attitude to economic policy contained in the so-called 'Yellow Book' reflected most of the economic policies that the IFIs had been advocating for years. Negotiations were thus far more cordial than had been the case in previous rounds; the Aquino administration's first IMF standby, for instance, was approved almost immediately after its submission (Dohner and Haggard, 1994: 68).

Furthermore, even before the new government opened negotiations with the World Bank, it had already taken important steps, such as abolishing certain agricultural monopolies and export taxes, reforming the tax system and liberalising import restrictions. The Bank therefore restricted conditionality to a few key issues, three of which had already featured in the first two SALs – trade liberalisation, tax reform and the public investment programme (Mosley, 1991: 56). Between 1985 and 1988 the World Bank acted more as a source of advice and technical aid than as an initiator of reform. Many of the reforms happened to sit comfortably with some of Aquino's key political aims, such as abolishing the privileges of certain interest groups that had been acquired under Marcos. It should also be noted that the major task of macroeconomic stabilisation had been carried out before she came to power, and that the government benefited from an early inflow of foreign aid (Dohner and Haggard, 1994: 11). During her period in office President Aquino received five SECALs (amounting to US$1.2 billion) and two IMF standbys, and the renewed credibility of the administration began to attract the return of capital that had flown overseas – anything between US$4 billion and US$12 billion in 1986–91 (FEER, 1996: 26).

Nevertheless, implementation often fell short of declared commitment. Cronyism was not completely rooted out; indeed, the privatisation programme gave the interest groups of the Marcos era a chance to revive their fortunes and lobby energetically for their own vested interests. Trade liberalisation, demanded as a condition by the World Bank, was stoutly and successfully resisted by both Filipino business elites and representatives of foreign business in the country, backed up by small manufacturers, farmers and workers who had been hit by the declining economy (Morisawa, 1993: 54–6). In addition, a crippling power shortage caused by drought badly affected the situation, and the Gulf crisis, natural disasters and coup attempts jolted the government. Political instability contributed to negative economic consequences; the credibility of the government in the eyes of foreign investors fell after the near-success of a coup attempt in December 1989, and GDP growth dropped to –0.6% in 1991.

The case of the Philippines thus shows light conditionality during much of the Marcos era. When conditionality was tightened, however, in the 1980s, it still often failed to produce the desired effect, as domestic forces conspired to blunt the effectiveness of policy reform measures and lack of compliance went unpunished. Conditionality was again light during the government of President Aquino, when reform was put forward voluntarily by the technocrats; however, domestic factors and external shocks again limited the possibilities of thoroughgoing reform. Despite private-sector support for its adjustment programme, the regime was not immune to distributional pressures, and a national consensus was rarely achieved. Under the Ramos administration progress has been achieved in structural reform and foreign investment is being successfully attracted. The agreement reached with the IMF in May 1994 is regarded by the government as an 'exit facility' (Hodgkinson, 1996: 916–17) implying that further agreements are unlikely to be necessary.

4. Conclusions

This concluding section returns to the questions posed at the outset of this study. First, have IFIs and other donors influenced the adoption of adjustment policies in South-East Asia? And second, have they done so by means of conditionality? The short answers are 'yes' to the first and 'no' to the second question. Although external agencies played a role in the economic decision-making of these countries, conditionality was largely irrelevant in bringing about their policy reforms. Of the five countries reviewed in this study, only in the case of the Philippines did the IMF eventually manage to force a government to undertake action against its will, and then only briefly in response to economic crisis. In the other countries, governments have voluntarily adopted the type of adjustment policies recommended by the IFIs. In some cases they have done so well before policy-based lending negotiations reached agreement, as in Indonesia in 1987, four years into its reform programme, or without recourse to the IFIs lending as in Malaysia.

When *structural adjustment loans* coincided with the initiation of an economic adjustment programme, they came with low levels of conditionality. Moreover, compliance with these few conditions has been high only when the government itself regarded them as beneficial. Where the recipient government has remained unconvinced of the need for policy change, IFI conditionality has been violated, invariably with impunity, as in South Korea's unwavering support for its automotive industry and Thailand's reluctance to restructure petroleum product pricing.

Conversely, the amount of apparent conditionality in the case of the Philippines was high, but for many years non-compliance went unpunished, and as the IFIs continued providing financial resources, it generated a classic case of moral hazard. Only when the Marcos administration's deceptive overstatement of the country's foreign reserves was discovered did the IMF force the government to undertake a stabilisation programme. Although successful in reducing inflation, the resulting economic overkill has been one of the causes of subsequent slippages in World Bank loan conditions. By the time the new government took power, a commitment to the adoption of an adjustment programme was in place and conditionality was lowered.

If the IFIs have not influenced the adoption of adjustment programmes by means of conditionality, as seems evident, how have they influenced the economic decision-making of these countries? The most apparent IFI impact on policy reform lies in the easing of external resource constraints through financial assistance. This has provided committed governments with the financial resources needed for carrying out policy reform. However, it has not necessarily been crucial in the adoption of economic programmes, as demonstrated by Thailand's ability to break off negotiations for conditional loans when a Tokyo credit was secured. Moreover, IFI financial support has facilitated not only policy change but also its delay, as manifested in the Philippines' chronic use of IMF credits to delay action.

IFI involvement through policy dialogue and the building of intellectual capabilities seems to have played a role in the embracing of a market-oriented philosophy amongst technocrats and members of the civil service in these South-East Asian economies. As most of them were educated in Western universities and occupied influential positions in government in the 1980s, measures conducive to 'market-friendly' policies were favoured. Close relationships/negotiations/dialogue with IFIs seem thus to have generated a convergence of objectives between domestic governments and external agencies, and hence rendered conditionality superfluous. However, long relationships do not always guarantee such an outcome, as is apparent in the relationship between the Philippines and the IMF. In any case, it is extremely difficult for an outside observer to assess the degree of influence by means of policy dialogue, since most of what was 'agreed' versus what was 'imposed' in that dialogue is basically undocumented.

Regional factors also facilitated the adoption of adjustment policies in South-East Asia. Japanese economic success, in particular, has been of significant importance in influencing neighbouring countries' selection of economic strategies, as clearly manifested in South Korea's industrial policy. As Japan relocated large industrial investments to other countries in the region, it also provided crucial financial support for the implementation of economic policies in the host countries. Once economic reform began to bear fruits in countries like South Korea, Singapore and Taiwan, other East Asians followed, revealing a kind of 'copy-cat' effect whereby neighbouring countries imitated each other's policy strategies. However, the poor implementation of adjustment policies in the Philippines, and the particular features of those adopted elsewhere in the region, demonstrate that more dominant factors were at work.

This leaves us with the more difficult task of understanding why these South-East Asian countries adopted adjustment programmes when they did. Domestic politics, culture, and history are the major factors contributing to these decisions. This paper has only scratched the surface of an intrinsically complex subject and one that must be left for further studies to reach firm conclusions. However, it seems clear that an efficient bureaucracy which is relatively immune to interest-group pressures; unequivocal support from political leaders; a broad national consensus on economic measures; and a large measure of pragmatism, are all necessary ingredients for the rapid and appropriate implementation of economic policies. If the IFIs were able to contribute to the achievement of these pre-conditions, they would largely be co-operating with governments in the adoption of suitable economic programmes. In the main, however, such factors are largely beyond their reach.

Appendix

World Bank adjustment loans 1980–94 and IMF lending 1952–94

	Loan type		*Date effective*	*Date of closure*
South Korea	IMF	Standby	Every year 1965–75	
	IMF	Standby	1977	
	IMF	Standby	Mar 1980	Mar 1982
	IMF	Standby	Feb 1981	Mar 1982
	WB	SAL I	Mar 1982	Dec 1982
	IMF	Standby	Jul 1983	Mar 1985
	WB	SAL II	Nov 1983	Dec 1984
	IMF	Standby	Jul 1985	Mar 1987
	WB	Ind & Finan Loan	Dec 1985	Sept 1990
Indonesia	IMF	Standby	1961	
	IMF	Standby	1963	
	IMF	Standby	Every year 1968–73	
	WB	Trade Policy Loan	Mar 1987	Jun 1987
	WB	2nd Trade Pol Loan	Aug 1988	Mar 1989
	WB	Private Sector Dev Loan	Sept 1989	Mar 1990
	WB	PSDL II	Jan 1991	Jul 1991
Malaysia	WB/IMF NONE			
Thailand	IMF	Standby	1978	
	IMF	Standby	Jun 1981	Mar 1983
	WB	SAL I	May 1982	Mar 1983
	IMF	Standby	Nov 1982	Dec 1983
	WB	SAL II	Jun 1983	Jan 1984
	IMF	Standby	Jun 1985	Mar 1987
	WB	Distrib Sys/Energy Eff	Apr 1993	
Philippines	IMF	Standby	Every year 1962–75 (ex. 1969)	
	IMF	Extended Fund Facility	1976	
	IMF	Standby	1979	
	IMF	Standby	Feb 1980	Dec 1981
	WB	SAL I	Nov 1980	Jun 1985
	IMF	Standby	Feb 1983	Feb 1984
	WB	SAL II	Apr 1983	Dec 1984

Philippines continued	WB	Agricult Sector Loan	Oct 1984	Dec 1986
	IMF	Standby	Oct 1986	Mar 1988
	WB	Eco Recovery Loan	Jun 1987	Dec 1989
	WB	Public Sector Loan	Nov 1988	Aug 1991
	IMF	Extended Fund Facil	May 1989	May 1992
	WB	Financial Sector Loan	Jul 1989	Dec 1991
	WB	Debt Managem Loan	Dec 1989	Jun 1991
	WB	Env & Nat Res Mgt	Oct 1991	Dec 1998
	IMF	Standby	1991	
	WB	Eco Integration Prgm	Dec 1992	
	IMF	Extended Fund Facility	1994	

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