Asians must spend more on basic infrastructure
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ASEAN nations are still hurting in the aftermath of 1997's economic crisis, writes Stephen Grenville.

The Chinese economy now bulks so large in any story of Asia that it is easy to overlook the different situation and performance of our neighbouring South-East Asian economies.

Ten years after the Asian crisis, these countries still carry its legacy. The sudden capital reversals in 1997 forced the crisis countries to dramatically reduce spending to turn their current account deficits into surpluses. Since then, even though growth has resumed at rates that don't seem far below the pre-crisis rates, the pace in countries of the Association of South-East Asian Nations [ASEAN] excluding Singapore is half that of China. These were not the V-shaped recessions we are familiar with in mature countries, where GDP gets back to its old trend-line when the cycle turns. If growth had been maintained at the pace of the two decades before the crisis, Indonesia's GDP would now be one-third higher. In Thailand it would be one-quarter higher.

Moreover these are economies exhibiting many signs of lethargy: low investment growth (3 to 4 per cent increase last year), current account surpluses and below-average inflation, with the only dynamic element being exports, driven by China's demand for raw materials and inputs for manufacturing.

Investment is running around one-third lower than before the crisis. In 1996, Malaysian private sector investment was running at 30 per cent of GDP: it is now around 10 per cent. China's dynamism (and the new kid on the block, Vietnam) have lured away some of the foreign investment which drove growth, technological transfer and productivity before the crisis.

The explanations are many. The crisis was so searing that some may have felt that slower growth was a price worth paying, and investing in low-return foreign exchange reserves was an insurance policy worth having. Many companies were in effect bankrupted and, with a flawed system of resolution, banks have been constrained in lending to corporates with questionable balance sheets. Instead, banks have preferred to lend to households for the purchase of cars and motorbikes, so the main sign of growth is the ever-worsening urban traffic. As a result of the deficiencies in governance that became painfully apparent in the crisis, more intrusive regulations have been introduced: necessary perhaps, but stultifying rule-making saps entrepreneurship. Within the bureaucracy, anti-corruption measures make officials wary of signing off on projects. Regional devolution may have been politically necessary, but puts scarce budget resources in the hands of weak administrations. Demonstrating macro-economic rectitude, in the form of near-balanced budgets, has been given a high priority, but at the cost of lost opportunities in vital public infrastructure. Before the crisis, investment in infrastructure in Indonesia was running at around 6 per cent of GDP: last year it was 2 per cent.

More recently, a new trend - perhaps a new economic paradigm - is tentatively emerging in Thailand and Indonesia. In Thailand, with the departure of the Thaksin government, the king has promoted the idea of the "sufficient" or "enough" economy - where people would not be motivated by greed for worldly goods. At the same time, the distrust of foreign investment, never far below the surface, is showing more clearly. Foreign ownership restrictions, not strictly enforced before, are now given more attention. In Indonesia a similar line of thinking goes under the rubric of the "Pancasila Economy". Policy-making based broadly on the Washington Consensus - basic reliance on the market and an open economy - survived the crisis without much question, but might be diverted by these ideas.

Eliminating some of the grosser manifestations of the globally oriented market economy has many attractions. These countries, however, still have many poor people and have pressing demands on their meagre social services. The best weapon against poverty is still growth, no matter how much we might fret about aspects of distribution. Infrastructure has run down in Indonesia and has not kept pace with demands in Thailand. Getting a larger part of GDP into the hands of government (and having this competently administered when it is) seems a high priority in countries like Indonesia, where the budget - central and regional - is less than one-fifth of GDP. Near-balanced budgets are fine in principle, but more spending on basic infrastructure (much of it commercially profitable if properly priced and managed) will cut through production bottlenecks. The parlous state of infrastructure ought to create the possibilities of beneficial partnership with the private sector, and even with the foreign private sector, provided the vexed issues of monopoly and hard to define property rights can be resolved.

For those interested in world climate change and cutting carbon emissions, there are more opportunities for high-return investments in Indonesia than in Australia (e.g., a reliable central electricity grid which would end the need for inefficient micro-generation, or effective public transport in major cities which would reduce private car use).

These countries should be running bigger budget deficits and current account deficits, funded by foreign capital inflow. It is time to slough off the legacy of the crisis and restore the policy primacy of strong growth.

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