[Book review] "Southeast Asia's Misunderstood Miracle: Industrial Policy and Economic Development in Thailand, Malaysia and Indonesia by Jomo K.S. et al."

solid foundation for future research, for which I would like to express to the contributors of this study my fullest approval and gratitude. (Yukihito Satō)

Southeast Asia's Misunderstood Miracle: Industrial Policy and Economic Development in Thailand, Malaysia and Indonesia by Jomo K. S. et al., Boulder, Colo., Westview Press, 1997, xiv + 196 pp.

In *The East Asian Miracle: Economic Growth and Public Policy* published in 1993, the World Bank evaluated governmental roles in economic growth and analyzed their effectiveness. At about the time that this report was released, there were heated debates among researchers over the reasons for the rapid economic development that had taken place in East Asian countries in the lead up to, and during the first half of the 1990s. The point in question was whether this development could be explained wholly in terms of the traditional neoclassical school that it was achieved through market mechanisms, or whether the economic growth was the result of selective government interventions. The role of the government was frequently analyzed when examining the Northeast Asian economies, but infrequently analyzed when dealing with the Southeast Asian economies. Instead, in some quarters, Southeast Asian economic growth was ascribed to market mechanisms, with government intervention seen as having proved ineffectual.

In the book under review, the neoclassical school, with its emphasis on free market forces, has been rejected, along with arguments based on the developmentalist state. The book criticizes both schools of thought and focuses on the historical analysis of the role of governments, especially industrial policy, in the recent economic growth and industrialization of the second-tier Southeast Asian NICs. I will evaluate this approach with some rigor, and begin my review with a brief introduction to the book.

Chapter 1 summarizes the principal thrust of the World Bank report, *The East Asian Miracle*. While acknowledging considerable government intervention, especially in Japan, the Republic of Korea, and Taiwan, the report concludes that the gains from industrial policy are ambiguous. On the other hand, the report concludes that Southeast Asian NICs have achieved rapid growth and industrialization without resorting to industrial policy (Thailand), or by abandoning it (Malaysia and Indonesia). In other words, Southeast Asian governments found it difficult to acquire the capabilities needed to implement industrial policies in a disciplined way. The social and political circumstances in the Northeast Asian economic miracle are unlikely to prevail elsewhere. The report points instead to the second-tier Southeast Asian NICs' supposed record of rapid growth and industrialization without industrial policy as more desirable, alternative models for emulation. Thus, the Miracle study claims that second-tier Southeast Asian NICs have grown rapidly by relying on mar-

As the book under review was published before the currency crisis of 1997, I have refrained from commenting on the Southeast Asian economies in relation to the crisis.

ket forces and minimal but generally supportive government interventions (e.g., in the areas of primary education and infrastructure provision) without, or even despite bad industrial policy, i.e., attempting selective policy interventions to promote particular industries.

Chapter 2 outlines important differences between the Southeast Asian NICs and their Northeast Asian predecessors in terms of the different contributions of resource rents as well as the motivations and nature of government interventions which have significant implications for the growth and structural change in Southeast Asia. As far as their initial conditions are concerned, unlike the Northeast Asian counterparts, the Southeast Asian NICs have invested in agricultural expansion and rural development, but have not experienced any major agrarian reform. The Northeast Asian NICs have progressed precisely because their lack of natural resource endowments have been more than adequately compensated for their wealth of human resources which have been created by deliberate government policies. Regarding industrial policy, the much greater ethnic and cultural homogeneity of the Northeast Asian newly industrializing societies has probably rendered nationalism a far more potent force. In contrast, much state intervention in Southeast Asia has mainly been for redistributive ends, mainly at the behest of politically influential business interests and interethnic redistribution. However, in Southeast Asia the conditions for the emergence and existence of such "relatively autonomous" states have also existed. Such circumstances have made it possible for the regimes concerned to undertake industrial policy. The national and firm-level corporatism which obtains in Japan and Korea is less common in Southeast Asia. In such societies, Chinese business networks play an important role in reducing some transaction, information, and other costs as well as risks and in resolving some coordination and collective action problems not satisfactorily addressed by state intervention.

The World Bank report ascribes the rapid growth in each economy to the application of a set of common market-friendly economic policies, but it fails to analyze the dynamic changes in the developing countries which are trying to catch up with the developed countries through trade, investment, and reshaping the regional division of labor. However, in Chapter 3 the book analyzes the so-called flying geese theory, or the dynamic chain of structural conversion in which one country's economic development inspires to promote development of other countries, as seen in the East Asian nations with mutual geographical proximity. Japanese firms have thus played a key role in organizing regional networks of production, and hence in rapidly increasing intra-regional trade flows. Southeast Asian governments and firms have become increasingly selective and sophisticated in implementing industrial policies and attracting as well as regulating such investments as they endeavor to extract greater advantage from transnational economic linkages. Rapid increase in foreign direct investment in these countries since the latter half of the 1980s is explained by the sharp appreciation of the yen in 1985. In addition, this chapter outlines the characteristics of foreign direct investment from the principal source countries, such as Japan, Taiwan, and Korea.

Chapters 4 to 6 deal with the role of governments in the process of industrialization, and analyze the industrial policies of Thailand, Malaysia, and Indonesia. The World Bank report concludes that, in Thailand the maintenance of stable macroeconomic management formed the basis for achieving economic growth with minimal government-directed industrial policy. The book recognizes, in part, the adequacy of the report's analyses. In the field of macroeconomic management, four institutions—the Bank of Thailand, the Ministry of

Finance, the Bureau of the Budget, and the National Economic and Social Development Board—have coordinated their economic policies and have continued to carry on the tradition of maintaining economic stability by precluding political intervention. On the other hand, the government had no coherent policy to promote specific industrial sectors within line ministries in charge of industrial policy. In some cases, party politicians became the competent authorities for the ministries, and utilized their power for their own purposes. Industrial policy making in Thailand has been spread across at least seven agencies. As a result, poor coordination among these agencies and overlapping jurisdictions exacerbated the lack of coherence. Government policy has not been active in directing and guiding business to purse industrial growth in the same way as that of the governments of the Northeast Asian NICs. Minor policies which favored specific industries emerged due to a combination of successful lobbying by industrial groups and the preferences and biases of bureaucratic factions within line ministries.

The book under review refutes the World Bank report view when it states that Thailand's industrial development in the latter half of the 1980s cannot be explained only by the effect of coordination through pricing mechanisms. It points out that the neo-liberal's focus on rent seeking has caused them to overlook important contrary evidence of highly effective, long-standing, and large selective distortions in agricultural markets and to miss equally important examples of successful selective interventions during the period of import substitution industrialization begun in the 1960s as well as in the export promotion measures adopted in the 1980s. Another problematical point with the World Bank analysis is, according to the book, the tendency of the neo-liberal researchers to view the Thai government as not having changed at all, and to regard rent-seeking behavior as a quite natural practice. It is true that politics in Thailand is characterized by the patron-client relationship and the fragmented implementation of industrial policy. The book argues, however, that Thai politics has shifted toward liberal corporatism and more rational outcomes with the growing technical capacity of the Thai bureaucracy, and that this has led to drastic changes in the policy-making process in both individual sectors and specific industries. The business community has become stronger and more financially independent and so has become increasingly able to influence government policies rather than be controlled by the government. By the early 1980s, individual members of peak business associations were able to persuade the government to set up a public-private sector forum, the Joint Public and Private Sector Consultative Committee. Through such channels, the business community has requested many tax reforms and changes in government regulations to support their export drives and other business interests.

Malaysia also owes its economic growth to one decisive factor which has been its ability to attract export-oriented foreign direct investment into the country's education system, infrastructure, and legal system. In addition it has focused on macroeconomic stability. This is an economic developmental approach that is called by the World Bank "functional interventions." In Malaysia, the weakness of a general civil service subordinated to vested ethnic political interests has prioritized the promotion of a Malay rentier business community rather than the emergence of an efficient, deepening industrial policy. In 1970 the government announced the New Economic Policy (NEP), and has sought to create the socioeconomic conditions for national unity through massive economic redistribution programs to achieve its twin objectives of poverty eradication and the restructuring of society. In the early 1980s, there was a major push for heavy industries by the Malaysian government. The government's objectives included the development of a capital goods sector and greater linkages with the domestic economy, especially with Bumiputera enterprises. Unfortunately, most of these heavy industries faced glutted world markets and stiff international competition from the outset. Financial returns in Malaysian state-owned industry were poor or negative, but improved with better management, macroeconomic recovery, and entry into export markets. In addition, the sharp decline in Malaysia's real effective exchange rate in 1986 was accompanied by a relaxation of the guidelines imposed under the 1975 Industrial Coordination Act (ICA)—for example, the requirements for local shareholdings were relaxed—and the increased incentives under the 1986 Promotion of Investments Act. Together these made Malaysia an even more attractive place for investment. Confirmation of the mid-1980s change in policy direction came with the adoption of Vision 2020, seen to favor growth, modernization, and industrialization over the NEP's emphasis on interethnic redistribution.

This book suggest that the nature of much state intervention in Malaysia has been the target of rent-seeking behavior in the past, combined with a bureaucracy preoccupied with ethnic redistribution. However, in Vision 2020 there appears to be a greater symbiosis between large corporate groups and the government with the former appearing to have built up special relations with some of the top political leaders. Hence, state intervention, including industrial policy, in these circumstances must recognize the nature and role of the state while seeking to ensure its efficacy in achieving national economic objectives. The Malaysian government has been establishing the institutions and mechanisms for closer private-public cooperation and interaction. The World Bank report regards Malaysia's heavy industrialization efforts as a costly failure. But this ignores the fact that the design of the interventions was poor and the period over which the policy's effectiveness should be assessed should be longer when complex learning processes are involved. According to the book, market forces alone will not be enough for the promotion of industrial development, and there is a need to remedy market failure with selective government intervention.

In Indonesia, as in other Southeast Asian countries, there is conflict between ministers charged with seeking the protection of the sector under their control and economists who advocate trade liberalization. This book suggests that the economic policies that have been implemented result from the struggle between these two institutions. After General Suharto brought in military control of the government in 1965, the planning of economic policy adopted by the New Order regime was left in the hands of the Western-backed technocrats known as the Berkeley mafia. They endeavored to consolidate a base for the introduction of foreign investment and promotion of exports. Following the oil boom in 1973, soaring oil prices boosted export income and fiscal revenues. This made possible the establishment of many state-owned enterprises and the implementation of major projects. Policies intended to protect domestic industry were also reinforced. During the period of structural adjustment in the mid-1980s, however, the government implemented a deregulation package which included the lifting of restrictions on imports and foreign investment, as well as export promotion in response to decreased export levels and stagnant investment. At this juncture, however, the technocrats exerted little influence over industry-specific intervention in the form of non-tariff trade barriers until the second oil slump.

Public policy in Indonesia has been quite interventionist where the industrial sector has been concerned. This book notes, however, that the government did not specifically plan for industrial development and did not seem to have pursued a coherent industrial policy. The problem may very well be with the domestic regulatory environment that discourages domestic competition, rather than high protection. In Indonesia, industrial policy has been abused by the politically influential for their self-aggrandizement or perhaps even to further political ambitions, and the government has had close relationships with private firms that have expanded rapidly through rent appropriation thanks to interventionist policies. It is true, also, that Indonesia's dynamic comparative advantage cannot be attained solely through freely functioning markets. It is important to articulate Indonesia's long-term strategic vision and ensure that policies and institutions are in place to realize that vision. The book observes that the bureaucratic attitude in government agencies has changed significantly in the last decade in favor of greater cooperation with private business.

The last chapter, Chapter 7, summarizes lessons from industrial policy in Southeast Asia. The World Bank report concluded that, unlike the first-tier East Asian NICs, the second-tier Southeast Asian NICs failed to carry out effective intervention because their governments were not capable of establishing systems that were conducive to private-public sector cooperation. In fact, however, since the latter half of the 1980s, Southeast Asian countries have achieved rapid economic growth under such governments. This fact is in need of a consistent explanation. When a government was strongly influenced by patron-client relationships that tended to promote rent-seeking behavior, how could it achieve growth without becoming inefficient? On this point, the book notes: While some motives for state intervention may be described as rent seeking in nature, rent capture essentially involves transfers which may be considered unfair, but are not necessarily wasteful in the sense that the rent is entirely dissipated by rent-seeking behavior. This would go a long way toward structuring rents more effectively to achieve desired policy objectives besides minimizing unnecessary and undesirable rentier activity as well as rent dissipation due to rent-seeking activities. The book points out that the quality of governance would obviously also benefit from appropriate institution building as well as a capacity for flexibility in responding to new challenges.

Drawing on the commentary of the book's seven chapters, I would now like to present my own conclusions. The World Bank report provides country analyses based on their static comparative advantages. However, this approach does not offer any meaningful examination of economic growth in the Southeast Asian countries. In contrast, the book under review is of the opinion that, as stated in Chapter 3, economic growth was achieved in geographically proximal Southeast Asian countries as they were linked internationally through direct investment. I share this view. The book notes that in developing countries, selective government intervention is needed because if they relied only on market mechanisms, they would not be able to strengthen their competitiveness in areas such as technology, finance, human resource development, and infant industry protection. I also accept this analysis. I wish to emphasize, however, that just as development strategies vary to reflect different conditions in different countries, industrial policies should also be studied from a dynamic viewpoint that takes into account their history and developmental stages. The World Bank report suggests that the Southeast Asian NICs' experience of high growth with minimal industrial policy and economic liberalization is a more desirable, more feasible, and more easily emulated alternative for other developing countries than the Northeast Asian experience of rapid growth and structural change accelerated by industrial policy. This contention is open to question. The reason for this is that, as the book under review points out, even in Southeast Asian countries, sustained rapid growth cannot be achieved unless the government intervenes through the implementation of industrial policies. Moreover, the governments must be capable of effective policy implementation.

The discussion in this book includes a few points over which I have some misgivings. In order to clarify the elements of Southeast Asian economic growth, the book has focused on industrial policies intended to foster specific industries (in contrast to the World Bank report which denies the effectiveness of such industrial policies), and includes a dynamic analysis related to the developmental stages of each country. I value this approach highly, but am not convinced by its reasoning. The book views industrial policy as something that is greatly desirable for Southeast Asian countries, yet admits that rent seeking has often led to inefficiency in these countries. I believe that, before reaching such a conclusion, the book should have undertaken a detailed analysis of the decision making and operation of industrial policies. If industrial policies proved to be ineffective, then the reasons for the failure should have been investigated fully. For instance, Southeast Asian countries adopted industrial policies for the automobile industry. It is important, therefore, to compare and discuss the policies planned for local content, the domestic engine production projects and national car projects, the way these policies have been applied, and their significance. As one way of approaching this analysis, I have in mind the idea of analyzing the way different players, such as politicians, economic bureaucrats, business associations, and individual companies, exerted influence on each other during the policy-making process.

By referring to the recent achievements of the new institutional and political economy approaches, the book focuses on the role that selective government intervention, institutions, and organizations played in overcoming market failure in the course of economic growth. This viewpoint is very important, and one that I thoroughly appreciate. It should be noted, however, that the mere implementation of policies and establishment of institutions does not mean change in the industrial structure. The key factor for economic growth is the way in which companies can efficiently conduct their business under well-established policies and institutions. Further business expansion, and the resultant major changes in the economic structure, would force governments to formulate new policies and institutions. Finally, I would like to emphasize the importance of capturing the relationship between such changes in the economic structure and policies in a dynamic way. (Shigeki Higashi)