The Economic Growth of East Asia and Latin America in Comparative Perspective

Lessons for development policy

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In the middle of the twentieth century (1950), Latin America was the most developed region outside the industrial countries, with an average level of real GDP per capita more than 2½ times that of East Asia (excluding China and Japan),[1] and around one-fourth that of the US (Table 1). At the beginning of the current century (2001), however, this relative position had been reversed: real GDP per capita of the East Asian region had more than doubled, while that of Latin America had actually declined, in relation to the United States. What can account for this big reversal of fortune? And what are some of the lessons from this experience for development policy? These are the questions that this article seeks to shed light on.

Table 1: Real GDP per capita in relation to that of the US

	1950	2001
East Asia*	0.057	0.151
East Asia (w/o China)	0.097	0.215
Latin America	0.263	0.208

Source: A. Maddison (2003)
* includes China, the four Newly Industrializing Economies (Hong Kong, Korea, Singapore and Taiwan) plus Indonesia, Malaysia, the Philippines and Thailand.

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[1] For this comparison, East Asia is defined as the four Newly Industrializing Economies (NIEs)—Hong Kong, Korea, Singapore and Taiwan—plus the ASEAN-4 (Indonesia, Malaysia, the Philippines and Thailand).

Clearly many different factors need to be considered in trying to answer these questions. And a complete answer would need to take account of differences in "initial conditions", including, for example, the impact of culture, historical traditions and the legacy of colonialism. But one way of organizing one's thinking on these issues is to consider the so-called "deep determinants" of economic development which have been given much attention in recent economic research and reflect some of the impact of initial conditions and other fundamental factors in the development process: geography (natural endowments, distance from the equator or from major markets), integration (trade and other policy reform), and institutions.

Geography, it turns out, is not a significant differentiating factor between East Asia and Latin America. Both regions contain countries that are resource-rich and resource-poor; both regions include a roughly similar portion of territory that is in the tropics; and both regions are similarly located in relation to major markets for their trade. Studies of the Inter-American Development Bank have shown that any differences of geography that do exist between the two regions account for only a minor part of the difference in economic growth between the two regions. This, then, leaves integration (or policies), and institutions, as the key determinants to consider in explaining the "big reversal" noted above.

Most of the growth divergence between the two regions occurred in the last quarter of the twentieth century. For the Latin American region as a whole, the record of economic growth was particularly weak during the 1980s and 1990s, which was a time when the region was implementing widespread economic reforms. Following the so-called "lost decade" of the 1980s when real GDP per capita fell by nearly 1 per cent in the wake of adjustments to a regional debt crisis, average real income grew by only 1.9 per cent in the 1990s (Table 2), while the open unemployment rate for the region, according to ILO data, rose to 10 per cent by the end of the decade. Real income growth was actually weaker in the second half of the 1990s than for the decade as a whole, and during the period 1998–2003, it was zero. By comparison, the growth in real GDP for East Asia was around 6 per cent a year, on average, during these same time periods. In addition, growth volatility has been significantly higher for Latin America than for East Asia since 1980. A comparison of other indicators of macroeconomic performance also shows dramatic differences between the two regions:

Table 2: Real GDP growth per capita: East Asia and Latin America

	1971–1980 (%)	1981–1990 (%)	1991–2000 (%)
East Asia*	4.8	6.1	6.8
China	4.2	7.8	9.0
Hong Kong	6.9	5.2	2.8
Korea	5.9	7.4	5.2
Singapore	6.9	5.0	4.9
Taiwan	7.6	6.5	5.5
Indonesia	5.6	3.4	2.8
Malaysia	5.0	3.2	4.5
Philippines	3.2	–0.6	0.7
Thailand	4.0	5.9	3.5
Latin America*	3.4	–0.6	1.9
Chile	1.1	1.6	4.9
Guyana	–0.6	–2.7	4.8
Dom. Rep.	4.0	–0.2	4.0
Argentina	1.2	–2.5	3.0
El Salvador	0.5	–1.3	2.8
Costa Rica	2.9	–	2.5
Panama	2.4	–0.8	2.5
Trinidad & Tobago	3.0	–4.1	2.4
Uruguay	2.5	0.1	2.4
Peru	1.1	–3.0	2.2
Mexico	3.6	–0.2	1.9
Brazil	6.0	–0.5	1.7
Bolivia	2.4	–1.8	1.5
Guatemala	2.8	–1.9	1.3
Colombia	3.1	1.6	0.8
Nicaragua	–2.6	–4.6	0.7
Honduras	1.2	–0.3	0.3
Venezuela	0.2	–1.6	–0.1
Ecuador	5.5	–0.5	–0.3
Jamaica	–1.2	2.0	–0.5
Paraguay	5.5	–	–0.7
Haiti	3.0	–2.5	–1.5
Latin American countries' simple average	1.6	–1.0	1.4

* Regional growth rates are averages for each period based on PPP weights.
Source: IMF *World Economic Outlook* database

Table 3: Comparative macroeconomic data for East Asia (EA) and Latin America (LAC)

	1971–1980		1981–1990		1991–2000	
	EA	LAC	EA	LAC	EA	LAC
Percentage change						
Real GDP per capita	4.8	3.4	6.0	–0.6	6.8	1.9
Consumer prices	10.5	32.2	6.3	337.8	5.9	45.4
Terms of Trade (std. dev.)	4.4	6.6	6.7	4.9	1.3	4.4
Private capital flows (s.d. in per cent of GDP)	...	...	4.3	5.2	4.9	5.8
As a per cent of GDP						
Gross domestic investment	29.5	23.2	31.6	20.8	34.9	21.1
Gross national savings	30.7	20.2	31.3	19.2	36.1	18.3
Broad money	37.3	23.5	56.4	32.6	100.4	36.1
Overall government deficit	–0.4	–2.1	–1.5	–3.6	–1.5	–1.8
Exports & imports (G&S)	41.2	28.3	51.8	30.2	65.9	33.2
Trade balance	–0.6	–1.6	0.3	1.8	1.7	–1.1
Foreign direct investment	0.8	0.3	1.9	0.7	3.1	3.2
Incremental capital–output ratio (ICOR)	4.1	3.8	4.0	13.9	4.3	6.2

Source: IMF *World Economic Outlook* database
Note: Data are averages for each region based on PPP country weights, except in the case of consumer price inflation, terms of trade, private capital flows and foreign direct investment which are based on equal country weights.

domestic savings and investment, trade openness and financial deepening show substantially higher values for East Asia, while the differences with respect to Latin America have been expanding over time (Table 3). A regional comparison of the incidence of extreme poverty (those living on less than US$1 a day) and income inequality also shows marked differences, with Latin America exhibiting little or no change in these measures of development from 1980 to 2000.

A comparison of the recent development experience of East Asia and Latin America highlights three factors related to the deep determinants of integration and institutions, which can account for much of the lagging economic performance of Latin America. The first is the persistent problem of macroeconomic instability in Latin America; the second is the relatively weak state of integration of Latin America into the global economy; and the third factor is the poor quality of its public institutions. Each one of these factors is discussed below.

The problem of macroeconomic instability in Latin America

Recent economic research and thinking has confirmed that macroeconomic stability is a necessary (but not sufficient) condition for sustained economic growth and development. The absence of a stable policy environment, with relatively low levels of inflation, competitive exchange rates, and positive real rates of interest, is clearly detrimental to long-run decisions for investment and growth. This principle was enshrined in the so-called "Washington Consensus" of the early 1990s and generally received wide credence among economic officials in Latin America. It has also been long a bedrock of the performance of most of the East Asian economies which, relatively early in their post-World War 2 development, established a reputation for fiscal prudence, low public debt and high domestic savings. By contrast, the record of Latin America has been far weaker in this respect, with the region traditionally plagued by fiscal instability and high inflation. Recently, however, much progress has been made in Latin America in reducing chronic inflation and improving fiscal performance, under the impetus of macroeconomic reforms to improve domestic tax systems and privatize loss-making public enterprises. But important elements of macroeconomic instability continue to exist, which discourage productive investment and growth.

Average fiscal deficits in relation to GDP were reduced significantly across the Latin American region in the 1990s, but fiscal policy in many countries continued to be pro-cyclical (exacerbating booms in the upswing, and recessions in the downturn, of the economic cycle) and to depend heavily on external financing. These characteristics intensified the growth volatility noted earlier, especially in the face of the high variability of private capital flows (so-called "sudden stops"), thus contributing to capital account crises. The data presented in Table 3 on the variability of capital flows during the last two decades suggest that it was not substantially different across the two regions. However, the East Asian region was better equipped to withstand any external shocks from unstable capital flows because of the stronger fiscal positions of its governments, low public external debt levels, and more robust export sectors. Even with the shock of the financial crisis of 1997–98, the East Asian region experienced a relatively quick recovery and has resumed a robust growth trajectory.

By contrast, Latin American governments tended to have a low tolerance

for external debt, in particular because of the high level of external public debt to exports for the region. In the case of Argentina and Brazil, for example, external public debt as a ratio to exports exceeded 300 per cent in the 1990s, reflecting the relatively small trade sectors of these economies In this connection, a recent study by the IMF concluded that public debt ratios in Latin America at the beginning of the current decade were roughly 2½ times a level that could be considered sustainable based on recent fiscal performance, whereas those for East Asia were in line with long-run sustainability.[2]

A unique counter-example in the Latin American region to the tendency noted above prior to 2000 was Chile, which has now set a high standard for fiscal policy management for emerging market economies. As a result of fiscal reforms and sound public sector management over the past three decades, Chile today maintains a small overall surplus position for central government operations and has a public debt to GDP ratio of less than 15 per cent. On this basis, the government can implement a neutral fiscal policy, on a cyclically-adjusted basis, and support central bank independence to maintain relatively low inflation. To insulate the economy from external price shocks, the government also has established a copper price stabilization fund to ensure that windfall revenues from commodity price booms are sterilized in order to sustain government expenditure (and economic activity) during periods when copper prices fall below their medium-term trend. In these conditions, it is no surprise that Chile was the only country in the region to register a sustained growth in real income per capita over the past three decades, although still below the rapid pace observed in East Asia.

In other aspects of macroeconomic policy, Latin America has not yet achieved the stability characterized by East Asian economies. One of these areas is financial system stability. During the last two decades, according to World Bank data, Latin America was subject to more systemic banking crises than any other region in the world, except for sub-Saharan Africa. Since 1980, the region has suffered 27 banking crises, with some countries, such as Argentina, experiencing a banking crisis every 5–6 years, on average.[3] In many cases, these crises were a consequence of boom–bust cycles induced by fiscal instability and "sudden stops" in private capital

[2] See chapter 3 of the IMF *World Economic Outlook* (October 2003).
[3] The problem of banking crises in Latin America was explored in *Finance and Development* (September 2004).

flows noted above, but they also reflected poor bank management, especially of state banks, and weak regulatory systems, especially at a time when governments were pursuing financial liberalization. These crises, in turn, tended to exacerbate public debt problems in the region, as the resolution of banking crises required government intervention and financial support in some cases exceeding 20 per cent of GDP.

Financial system instability over time also led to relatively low rates of financial intermediation, widespread substitution of the US dollar in domestic financial transactions, and high interest rates (with large spreads between domestic lending and deposit rates). Based on IMF statistics, real lending rates (i.e., rates for bank loans adjusted for the rate of inflation) in Brazil were more than 60 per cent, on average, during the period 1996–2000, which clearly represented a major impediment to sustained investment in that country. While this was an extreme value for the region, average real lending rates for most countries in the region were in the double-digit range during the last decade. At the same time, the flow of bank credit to the private sector in most Latin American countries was relatively low, at less than 30 per cent of GDP during the second half of the 1990s (Table 4).

Table 4: Bank credit, real lending rates and real exchange rate

	1981–1985	1986–1990	1991–1995	1996–2000
	Bank credit (as a per cent of GDP)			
Total				
East Asia	63	68	85	111
Latin America	24	47	52	28
Private sector				
East Asia	56	60	87	108
Latin America	23	27	35	28
	Real lending rate (in per cent per annum)			
East Asia	5.8	6.1	4.3	6.7
Latin America	2.4	4.4	13.4	18.2
	Real exchange rate (1990=100)			
	1980	**1985**	**1995**	**2000**
East Asia	145.6	133.8	102.9	95.8
Latin America	170.9	182.4	112.5	121.3

Source: IMF, *International Financial Statistics*

The contrast with East Asia could not be more striking. Typically in the East Asian economies, financial intermediation ratios (as measured by broad money in relation to GDP) were above 90 per cent in the 1990s, and credit flows to the private sector generally exceeded 80 per cent of GDP. While the East Asian region also has had to deal with banking problems (especially in the crisis period of 1997–98), real interest rates have not exhibited the volatility or high levels sustained in many countries of Latin America, and were typically in the single-digit range. Correspondingly, investment ratios have been much higher in East Asia than in Latin America.

Another aspect of macroeconomic instability that has differentiated the two regions relates to exchange rate behavior. Key elements of the macroeconomic reforms that Latin American governments have implemented since the mid–1980s have been a reduction in trade barriers, and a move toward more competitive exchange rates. In both these respects, Latin America has traditionally lagged behind East Asia. In addition, during the 1990s, there was a marked tendency for exchange rates, in real effective terms, to appreciate significantly in Latin America, thus reversing the course set in the previous decade. To a significant extent, this tendency resulted from the frequent use of the exchange rate as an anchor for achieving domestic price stabilization. Argentina and Brazil were prominent examples of this phenomenon in recent years, with both countries experiencing a currency crisis as a result of an extended period of currency overvaluation to support domestic price stabilization. By contrast, East Asia, with a stronger record of macroeconomic policy implementation, has maintained a greater degree of exchange rate stability and competitiveness, which has helped to promote its dynamic export sector.

Regional integration into the global economy

While Latin America has lagged behind East Asia in establishing the conditions of macroeconomic stability needed to sustain growth and development, it also fell behind East Asia in the degree of its integration into the global economy and the competitiveness of its manufactured exports. In 2000, total exports of Latin America represented only 5½ per cent of global exports, unchanged from 1980 (Table 5). By contrast, regional exports of East Asia more than doubled from 8 per cent to 20 per cent over the same

Table 5: East Asia (EA) and Latin America (LAC) in global trade

	1980 (%)	1990 (%)	2000 (%)
Share of World Exports			
EA	8.0	13.0	20.0
LAC	5.5	4.2	5.6
Share of World Imports			
EA	8.6	12.5	18.0
LAC	6.1	3.7	5.9
Ratio of Merchandise Trade to Merchandise Value-Added			
Asia	93.8	115.8	168.5
China	12.1	23.7	32.1
NIEs	216.5	259.5	365.5
Other	39.4	52.4	84.3
LAC	37.2	42.6	58.6
o/w Mexico	22.8	48.3	102.6

Source: UN Comtrade Data and IMF, *World Economic Outlook*.
Note: Asia includes Bangladesh, Pakistan (in "other") and India.

time period. East Asia has also exhibited higher levels of intra-industry trade, as measured by the ratio of merchandise trade to merchandise value-added, which reflect its growing participation, and specialization, within global production chains.

Most of East Asia's growth in intra-industry trade has been in the category of high-technology exports (e.g., electronic and ICT components), which have been the area of most rapid growth in world trade. In the case of Latin America, except for Mexico, export growth was heavily weighted toward natural resource commodities and low- and medium-technology exports. As a result, East Asia's share of global manufactured exports rose sharply to 18 per cent by 2000, compared with only 5 per cent for Latin America. Excluding Mexico, Latin America's share of global manufactured exports was only 2 per cent, a rate below that recorded in 1980 (Table 5). In a global economy where international production systems for commodities such as automobiles, electronics and garments have become increasingly fragmented across national boundaries, and trade in manufactured goods (mostly in the form of intra-firm trade) has risen to 80 per cent of total trade, East Asia has been far more successful than Latin America in benefiting from the gains of global trade patterns.

A key driver in the trade dynamics described above has been foreign direct investment (FDI) of multinational corporations. East Asia has generally been a larger destination for FDI flows than Latin America, notwithstanding the marked increase in FDI flows to the latter region in the 1990s. From 1985 to 2000, total FDI inflows to East Asia were roughly double the amount for Latin America. By the year 2000, eight of the ten largest recipients of FDI and exporters of manufactured goods (outside the industrial world) were in East Asia; the other two were Brazil and Mexico.

Whereas most FDI inflows have been channeled into the export of manufactured goods in East Asian countries, Latin America has followed a more heterogeneous pattern. During the period 1996–2000, roughly half of FDI flows to Latin America was related to mergers and acquisitions in connection with the privatization of state-owned utilities and domestic banks (Table 6). This development suggests that improvements in the infrastructure needed to sustain economic growth are likely to result in the future, which is an area in which East Asia has been well-positioned for many years. But it marks a significantly different pattern from that of East Asia, where FDI has typically been "efficiency-seeking", i.e., related to the establishment of export production capability.

A significant share of the remaining FDI flows to Latin America has been directed in the case of Southern Cone and Andean countries to the exploitation of natural resources (e.g., mining, oil and forestry), where restrictions on private and foreign participation have been lifted under the reform effort. In the Caribbean and Central America, countries such as Costa Rica and the Dominican Republic have followed the pattern of the Mexican "maquila" industry in the use of FDI to support exports to the

Table 6: Foreign direct investment inflows to East Asia and Latin America (in billions of US$)

	1990–95 (average)	1996	1997	1998	1999	2000	2000 stock
East Asia	23.0	44.7	45.1	25.4	31.7	74.3	1114.1
Latin America	22.3	52.9	74.3	82.2	109.3	94.4	613.1
o/w M&A	7.2	20.5	41.1	63.9	42.0	45.2	
Other	15.1	32.4	33.2	18.3	67.3	49.2	

Source: UNCTAD, *World Investment Report*

US market of electronic components and garments, based mainly on imported inputs and enclave production in export processing zones. However, there has been little growth in domestic value-added for these activities, other than that associated with local employment absorption. In addition, with the phase-out of the Multi-Fiber Agreement at the end of last year, many of these garment operations are facing increasing pressure from lower-cost Asian producers.

Mexico is the one case in Latin America that seems closest to the East Asian model in its export drive, with FDI supporting assembly operations ("maquiladoras"), as well as the automotive export sector which is building roots in the local economy. Mexico's entry into NAFTA has clearly been a factor in its strong export performance. Nevertheless, studies by UNCTAD have shown that labor productivity growth in its manufactured export industries has been relatively weak compared with that of East Asian countries, while domestic value added has grown at a far slower pace than export value because of an increasing reliance on imports. Notably, too, in recent years, exports from Mexico's assembly goods sector have begun to lose market share in the United States under increasing competition from China.

The differences between the two regions in the role played by FDI can be related to marked differences in their technological capability, as reflected in the quality of infrastructure, technical training of their workforce, and the use of technology. The longer history of efforts in these areas by East Asian economies has also given them first-mover advantages vis-à-vis Latin America, in that clusters of inter-connected, technologically advanced firms, supported by private-public partnerships to promote R&D activity, operate as a magnet for continued FDI inflows.

Studies of UNIDO and the World Bank have shown that Latin America has not kept pace with East Asia in the extent of its technological upgrading. The quality of infrastructure, as measured by the efficiency and extent of its transport and telecommunication networks, is inferior to that of East Asia. A recent World Bank study shows that Latin America is significantly weaker than East Asia across a range of indicators, such as transport costs, port efficiency and the depth of its road, rail and airfreight facilities.[4] Similarly, tertiary enrollments in science and engineering

[4] See Tables 2.1 and 2.2 in World Bank, *From Natural Resources to the Knowledge Economy* (2002).

Table 7: Indicators of technological capability

	1985	1998
Tertiary enrolments (per 1000 population)		
East Asia	0.38	0.54
Latin America (LAC)	0.35	0.35
Enterprise-financed R&D (US$ per capita)		
East Asia	6.6	60.3
Latin America	0.4	2.9
Royalty and license payments abroad (US$ per capita)		
East Asia	35.1	109.8
Latin America	2.6	4.7
Telephone mainlines (per 1000 population)		
East Asia	125.1	265.2
Latin America	42.9	114.7
Commercial energy use (kg of oil equivalent per capita)		
East Asia	1202.9	2621.6
Latin America	609.5	2024.1

Source: Regional averages calculated from country data provided in UNIDO, *Industrial Development Report 2002/03*

education and business expenditures on R&D, on average, are well below the regional average for East Asia. Korea, Taiwan and Singapore are among the world leaders in these areas (Table 7).

The dynamism of investment and exports in East Asia has also been enhanced by regional forces (or positive "neighborhood effects"). Intra-regional trade has been growing sharply among East Asian countries, and by the end of the last decade represented around 37 per cent of total regional trade; by contrast, intra-regional trade accounted for only around 18 per cent of total trade flows for Latin America. This phenomenon is likely to increase in East Asia with the increasing dominance of China as a major world exporter and destination for FDI flows. In some respects, its growth represents a competitive challenge to other exporters of manufactured goods in the region. However, in other respects, it is continuing a regional pattern of structural change in the product cycle that can be observed over the past 40 years, as countries at the early stages of technological development upgraded the skill and technology components of their exports, while newcomers in the region took over the production of

lower-technology exports (dynamic comparative advantage). This regional pattern can be traced back to the modern postwar development of Japan and the subsequent emergence of manufacturing industries in Korea and Taiwan which was followed by Singapore, and later by other countries in South-East Asia. No comparable regional inter-dependence can be observed in Latin America, outside of NAFTA. Recent studies have shown that the "spillover effects" from trade among growing economies can be a powerful stimulus to economic growth.[5]

The growing strength of intra-regional trade in East Asia is mirrored in the case of FDI flows, as outward flows of FDI have grown more sharply in East Asia than in Latin America. During the period 1996–2000, such flows for East Asia amounted to US$44 billion a year, or roughly double the amount for Latin America. On the assumption that most of these flows were to other countries in their respective region, such a development would enhance the forces arising from each region's interaction with the rest of the world.

The quality of public institutions

The role of institutions has been given increasing importance by development theorists as a critical factor in accounting for divergent growth patterns across countries.[6] At its broadest level, institutions can be defined as the structure of incentives that promote or impede entrepreneurial activity and productive investment. In many empirical studies, institutions are often measured by the extent to which governments are effective in promoting respect for the rule of law, contract enforcement, and the protection of property rights.

A number of institutions such as the Political Risk Services Group, the World Bank, and the World Economic Forum have developed surveys to measure over time the effectiveness of government institutions across a range of emerging market and industrial countries. These surveys typically score countries on an annual basis according to a variety of indicators, such as the control of corruption, government effectiveness or bureaucratic quality, regulatory quality, political stability and democratic accountability.

[5] These effects were explored in *Finance and Development* (September 2005).
[6] The relationship between institutions and growth was explored in chapter 3 of the IMF *World Economic Outlook* of April 2003.

These measures of government institutional capacity show clear weaknesses for Latin America in comparison with East Asia across virtually all dimensions and consistently over time (since 1985 in the case of surveys by the Political Risk Services Group). The only area where Latin America has consistently scored higher than East Asia is in relation to democratic accountability (Table 8).

In the light of these results, it is reasonable to ask what institutional elements have been important in the case of East Asia and lacking in the case of Latin America. Three elements of government institutions in the East Asian context stand out. One is the strong record of policy consistency of governments in East Asia over a long period of time. Policy credibility and political stability, along with a stable macroeconomic environment, provided an essential underpinning for the promotion of long-term investment

Table 8a: Measures of government institutional capacity for East Asia and Latin America

	East Asia	Latin America
Corruption	4.4	4.1
Law and Order	6.3	4.1
Democratic Accountability	6.0	7.8
Bureaucratic Quality	7.4	5.1
Total (March 2003)	6.0	5.3
Total 2000	6.0	5.6
Total 1995	7.0	5.3
Total 1985	5.7	4.1

Source: Political Risk Services Group (scores are based on a ranking of 0 to 10, with 10 the highest)

Table 8b: Governance indicators for East Asia and Latin America (2000)

	East Asia	Latin America
Voice and accountability	47.5	60.4
Political stability	59.4	51.2
Government effectiveness	71.3	50.4
Regulatory quality	68.5	59.4
Rule of law	65.4	51.4
Control of corruption	60.7	51.3

Source: World Bank (Governance Indicators database); scores are average country percentile rankings for each region, with 100 being the highest.

in East Asia. A second element is the strong focus on economic development as a strategic national goal. Such a strategic vision projected by national leaders has been especially characteristic of Korea, Taiwan, Singapore, Malaysia and China.

A third element of government institutions that was an important factor in the economic development of East Asia and has traditionally been lacking in Latin America is the strength and independence of government bureaucracies. In a number of East Asian governments, strong efforts were made to foster the development of a professional, merit-based civil service tradition, which was insulated from political influence, to implement government economic policy, in close consultation with business groups. To streamline decision-making, a lead government agency with strong coordinating authority was created to translate a national strategic vision of economic development into specific actions. The Economic Development Board of Singapore is a prominent example of such an institution. While Singapore has been one of the top-rated countries in the world for the quality of its public institutions, seven of the East Asian countries surveyed in the World Economic Forum's Competitiveness Report for 2004 were in the top half of countries surveyed for the soundness of their public institutions. Most of the Latin American countries were in the bottom half.

Notwithstanding the strength of government institutions in East Asia, it needs to be recognized that the Asian financial crisis of 1997–98 revealed how in certain cases close coordination between the public and private sectors gave rise to serious problems in corporate governance and regulatory forbearance. This experience showed that certain institutional arrangements that may have been effective in earlier stages of the development process needed to be adapted and transformed as market-based arrangements expanded more fully.

Despite these problems, the elements of strategic vision, policy consistency, and bureaucratic autonomy in a number of East Asian societies during their postwar development have served to compensate for the lack of well-developed market-based institutions and legal frameworks which supported economic development in the advanced countries. By the same token, these elements were not particularly prominent in Latin America's post-WW2 development. Many governments in that region provided examples of capture by special interests, or were dominated by

patron–client based political parties focused on the distribution of rents to favored elements of society. In respect of bureaucratic strength, clearly there are examples (such as Brazil, Chile and Mexico) of strong ministries of finance and independent central banks that have developed more recently in the region, but a professional civil service tradition has not generally been fostered. Often, government office-holding has been a reward for political support of the ruling political party.

In addition, government bureaucracies in Latin America have not been as sharply focused on export or FDI promotion as in the East Asian countries. For example, surveys carried out by staff of the UN Economic Commission for Latin America in the latter half of the 1990s among samples of exporters in Brazil, Chile, Colombia and Mexico portray a mixed picture of government policies supporting export development.[7] Exporters complained of difficulties in obtaining export credit insurance or long-term financing to support export activities, and a lack of transparency in government procedures (e.g., regarding the treatment of imports used in exports). Also, registration procedures were required in certain countries for new exporters which were viewed as time-consuming and cumbersome. Few countries in Latin America have been as aggressive in the promotion of foreign direct investment as in East Asia. One prominent exception has been the recent case of Costa Rica's Investment Promotion Agency (CINDE) which followed the best practice of Singapore in enticing Intel to establish a processing plant in its country.

Lessons for development policy

By comparison with East Asia, the recent economic experience of Latin America clearly shows a mixed record in terms of the results of economic reform and the benefits that the region has gained from globalization. What lessons can be drawn from this comparative experience for development policy more generally?

First, the requirement of macroeconomic stability for sustained economic growth must be viewed more broadly than an issue of maintaining low inflation and fiscal control. The soundness and stability of the financial system is an essential ingredient of the appropriate macroeconomic

[7] The results of these surveys are summarized in Melo (2001).

framework for development. Stable and competitive values for the real exchange rate and domestic real interest rates are critically important as well.

Notwithstanding past debates about the relative importance of the state and the market in the development process, it is clear that governments have a crucial role to play in supporting economic growth. The establishment of good infrastructure, support for technical training and local technology absorption, and the promotion of exports and foreign direct investment are all legitimate activities that governments should pursue in order to encourage economic development.

Third, if governments are to play a positive role in the development process, then the integrity of public institutions needs to be ensured. In many countries, this will require continued public sector reform to streamline bureaucracies and to establish independent judiciaries, tax and customs authorities, and regulatory agencies. Strong support should also be given to anti-corruption initiatives and the development of civil society organizations to strengthen oversight of government activities.

Fourth, the experience of East Asia has shown that institutions are context-specific and need to be adapted over time. In the absence of well-developed legal frameworks for property rights at the beginning of the post-WW2 development phase, other arrangements including close government–business coordination, clear policy signals, and good public administration provided the necessary institutional support for productive investment. At later stages of the development process, however, experience has shown that these arrangements needed to be supplemented by appropriate regulatory and governance structures to support an evolving market-based system.

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