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2 Understanding the ASEAN Development Gap

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Introduction

In the minds of ASEAN stakeholders, the ASEAN development gap is the disparity that exists between the ASEAN-6 and CLMV groups—that is between the original members of ASEAN (Singapore, Malaysia, Indonesia, Philippines and Thailand, plus Brunei Darussalam) and the latter joining members (Cambodia, Lao PDR, Myanmar and Viet Nam). The narrowing of this gap has been a focus of ASEAN since the launch of the Initiative for ASEAN Integration (IAI) at the Fourth Informal ASEAN Summit in 2000. Narrowing the development gap is a cornerstone of the equitable economic development agenda within ASEAN and forms an important part of the ASEAN Roadmap. ASEAN recognises that the gap between its member countries needs to be narrowed if it is to move forward in a more unified manner towards the achievement of an equitable ASEAN community.

Since the inception of the IAI, there has been much ambiguity over precisely how to define and measure the development gap between ASEAN countries. A rigorous and quantifiable definition and measurement of the development gap between these groups is required so that policies can be developed that directly target specific disparities. To some the gap is differences in living standards, variously defined, between ASEAN member states. To others the gap relates to differences in policies and other drivers of these differences. Reconciling these perspectives requires a shared definition of the term ‘development’, and from this shared understanding we can then measure and monitor the development gap.

This chapter provides a definition of the development gap that is consistent with current international thinking on the meaning of development. In line with the writings of Nobel Prize-winning economist Amartya Sen, and widely accepted quality of life or standard of living conceptualisations, it treats development as an end or as an outcome in which people are provided with the opportunity to exercise their reasoned agency. As such it does not define the development gap in terms of the many drivers of development in ASEAN member states, but as the quality of life outcomes that these drivers generate.
After this initial discussion, the chapter then turns to quantifying the ASEAN development gap. The previous chapter provided some initial observations of this gap, based on differences in incomes per capita among ASEAN members. This chapter provides a more thorough investigation, looking at gaps from a number of analytical perspectives and using various development achievement indicators. Data from UNDP (United Nations Development Program) Human Development Reports, including statistics on the well-known and well-used Human Development Index (HDI), are used to measure these gaps.

The chapter then turns to its third principal focus—identifying and discussing the drivers of development and their influence on the ASEAN development gap. This builds on previous analytical work on the ASEAN development gap by Brooks et al. (2010) and Menon (2012). The drivers of development identified in this chapter are those for which there is both robust theoretical and empirical support, as well as those with broad acceptance in policy circles. These drivers will differ in importance among ASEAN countries. All these drivers are important in all countries, although their relative importance to countries at varying stages of development may differ. The identified drivers include trade openness, investment in human and physical capital, governance and institutions, labour mobility and external development finance. Processes through which these drivers contribute to development and to development gaps are identified.

Defining Development

'Development' is a term that has many different meanings. It means different things to different people. To the layperson, development is often seen as the provision of physical infrastructure, such as roads and buildings. This is not unlike early notions of development held by policy makers and theorists, who saw development as a process whereby economies were modernised, progressing from a reliance on agricultural output to the industrial sector. In this conception, economic growth was largely unquestioned as the main indicator of development. An economy was thought to be experiencing development if it was sustaining economic growth and to be 'developed' if it achieved a high level of income per capita. In this view development was good, and something for all countries to aspire to. This was the popular view of development from the 1950s to the early to mid-1970s. Others, however, had a much different perspective of development. They saw it as inherently negative, involving the exploitation of vulnerable groups of people, especially those with relatively low incomes. Within this conception, development was characterised by cultural degradation, social dislocation and growing inequality.

While some still see development as a process principally involving progress and economic modernisation, most see it in a more nuanced
manner. Development, broadly speaking, is seen as multidimensional, involving achievements in universally valued quality of life outcomes. The UNDP, through its annually published *Human Development Reports*, has provided informed articulations of the notion of development consistent with this definition. It has also been arguably the most influential proponent of what might be termed a people-centred approach to development. The first *Human Development Report* was published by the UNDP in 1990 (UNDP, 1990). In this report the UNDP attempted to shift development thinking and strategies away from what was thought to be an excessive preoccupation with economic growth, and back to what it saw as core values—the UNDP advanced its concept of *human development*. The UNDP defined human development as follows:

Human development is a process of enlarging people's choices. The most critical ones are to lead a long and healthy life, to be educated and to enjoy a decent standard of living. If these essential choices are not available, many other opportunities remain inaccessible (UNDP, 1990: 10).

The UNDP was at pains to emphasise that its concept of development was broader than the achievement of economic growth and higher per capita incomes or what might be termed 'economic development'. It made the powerful point that income is not an end in its own right but a means to an end. What matters, according to the UNDP, is not so much the level of income but the uses to which it is put. The UNDP invoked the thinking of the ancient Greek philosopher Aristotle in articulating this position. Aristotle warned against judging societies by achievements in income and wealth that are sought not for themselves but desired as means to other objectives. More precisely, equating wealth with accumulated income, Aristotle's view was that 'wealth is evidently not the good we are seeking, for it is merely useful for the sake of something else' (UNDP, 1990, p. 9).

The UNDP's approach to development has strong conceptual underpinnings, being linked to the work of Amartya Sen. Sen was the winner of the 1998 Nobel Prize in Economics for his contributions to the field of welfare economics. In the late 1970s, Sen began proposing what became known as the 'capability approach'. This was in the context of how inequality should be judged, with Sen arguing the case for looking at inequalities not in variables such as income but in what he referred to as basic capabilities (Sen, 1980). Sen had long been critical of the use of income as a measure of development, because in his view the level of income or its growth was not as important as what it could be used to purchase (Sen, 1985). To this extent he is in agreement with Aristotle. Accordingly, as Alkire (2002) points out, development in Sen's capability approach is not defined as an increase in income growth, or for that matter
in terms of enhanced education or health alone, but as an expansion of capability. Capability is treated as the freedom to promote or achieve combinations of valuable functionings (Sen, 1990). Functionings, in turn, are the ‘parts of the state of person – in particular the things that he or she manages to do or be in leading a life’ (Sen, 1993: 31). The link between freedom and development was a theme Sen articulated further in subsequent writings. In his well-known work, Development as Freedom (Sen, 1999), he argued that the expansion of freedom is both a primary end and a principal means of development. More precisely, he argued that development involved the removal of the ‘unfreedoms that leave people with little choice and little opportunity of exercising their reasoned agency’ (Sen, 1999: xii). It is reference to this choice, and the view that basic capabilities include the ability to lead a long and healthy life, the ability to be knowledgeable, and the ability to have access to the resources associated with a decent standard of living that links the UNDP’s approach to the work of Sen (UNDP, 1995: 18).

The UNDP not only proposed its own definition of human development but also a measure designed to show which countries had achieved the highest levels of this development and which had achieved the lowest. This measure is the now famous HDI. The HDI provides a league table—a ranking—of countries based on the levels of human development they have each achieved. A detailed technical description of the HDI is not necessary for our current purposes, and will be provided later in Chapter Three, but it combines measures of achievement in three dimensions—longevity, knowledge and the material standard of living—into a single number. The HDI has changed since its inception in 1990 but in the original version these measures were life expectancy, adult literacy and a measure of GDP (Gross Domestic Product) per capita adjusted for differences in the cost of living between countries (UNDP, 1990). The use of a measure of income in the HDI has in some circles been contentious, seemingly being inconsistent with the UNDP’s invoking of Aristotle’s thinking regarding wealth. By way of justification, income provides security against unforeseen circumstances and can serve as a proxy for many other quality of life achievements not directly captured by indicators of health and education. Irrespective of what we might think of such justifications, along with GNI (Gross National Income) and GDP per capita, the HDI is now arguably the most widely used and reported measure of the level of development among countries.

High levels of inequality and poverty have long been associated with low levels of development. Reductions in inequality and poverty and their links to development were identified in an extremely influential work published initially in late 1969 by Dudley Seers. This writing, and the thinking on which it is based, still has considerable influence today. Seers rejected the view that development was an objective or positive concept
that, for example, described what was necessary for a country to achieve higher living standards for its citizens. Instead, he thought that development should be seen as a concept that requires us to identify the normative conditions for a universally acceptable aim, which for Seers was the ‘realization of the potential of human personality’ (Seers 1972: 6). While this realization is different to Sen’s notion of development, it is similar in that like exercising reasoned agency, it can be seen as a universally accepted aim.

Seers argued that three questions had to be addressed in considering whether realization, as he defined it, was being achieved. They were: (1) what has been happening to income poverty?; (2) what has been happening to unemployment?; and (3) what is happening to income inequality? Seers asserted that if all three of these phenomena had declined over time from high levels, then ‘beyond doubt this has been a period of development for the country concerned’ (Seers, 1969: 3). He further asserted that ‘if one or two of these central problems have been growing worse, especially if all three have, it would be strange to call the result “development” even if per capita income doubled’ (Seers, 1972: 7). On the issue of inequality, Seers argued that poverty could be reduced much more quickly if economic growth was accompanied by reduced inequality. The same by inference applies to unemployment. One can further infer that of the three questions posed by Seers, the first, concerning poverty, was the most important. This is not to imply that he considered inequality and unemployment to matter only in terms of their implications for poverty reduction. To the contrary, Seers viewed equity as an objective in its own right, arguing that inequity was objectionable on ethical grounds. It is simply to imply that what mattered most was poverty reduction. On these grounds, but also in part due to data availability, we later focus our attention on poverty reduction.

Seers’ position should not be interpreted as a rejection of per capita income as a measure of development, or as the assertion that the achievement of high income levels is not in itself development. Instead it should be interpreted as an argument for not only looking at this measure in assessing development achievements. Nor should Seers’ position be seen as inconsistent with the notion of human development as outlined above. Seers was concerned with income poverty. This poverty occurs when incomes fall below a threshold, or a poverty line. A widely used poverty line is 1.25 purchasing power parity dollars per day. The UN Millennium Development Goal of halving world poverty is based on this line. Achievement in income is a dimension of human development. A country containing large numbers of people living in income poverty will have lower levels of income per capita and as a consequence lower levels of human development than would otherwise be the case.

Looking at poverty and inequality or disparity does not confine attention to income achievements only: both can be looked at from a
multidimensional development achievement perspective. When Seers made his contributions to development thinking poverty and inequality were considered from an income perspective. Much more recent thinking looks at poverty and inequality from a multidimensional perspective. Multidimensional poverty has been the subject of much attention. Poverty is broadly defined as the lack of something of special importance (Gasper, 2007). From a multidimensional development perspective, this clearly includes, but is not limited to, income. The World Bank, for example, acknowledges that:

> although poverty has been traditionally measured in monetary terms, it has many other dimensions. Poverty is not only associated with insufficient money or consumption but also with insufficient outcomes with respect to health, nutrition, and literacy (Coudouel et al., 2002).

The concept of multidimensional poverty not only recognises that there is more to being in poverty than having a low income, but also that absence of income poverty does not guarantee the absence of other forms of poverty. Put differently, a person or country can be non-poor in terms of income but poor in terms of another development dimension. Improvements in income will not guarantee improvements in these dimensions and vice versa.

**The ASEAN Development Gap: Definition**

Defining development in terms of achievements in or levels of health, education and income has clear implications for how development gaps are defined and measured. As these achievements differ among individuals according to the country in which they live, development in this sense varies among countries. This variation may be considered as a development gap, and this is how the gap between the ASEAN-6 and CLMV countries will now be examined. The means by which development is achieved are, of course, all those factors that drive achievements in health, education, income and other valued quality of life achievements. It follows that these factors are also the drivers of development gaps. To be clear, for the purpose of this chapter and those that follow, the achievements in, or levels of, these drivers of development is not considered development per se; development is the intrinsically valued quality of life outcomes that these drivers generate.

If the gap is defined in terms of the many drivers of development this would lead to a very long list of variables that would need to be quantified and monitored. This list is likely to be very long, and the requisite data required for quantification and monitoring will not be available for many of these indicators. Nor is it likely that widespread agreement within ASEAN or elsewhere could be achieved regarding the variables that belong
on this list. Even if all requisite data are available, and agreement on the list could be obtained, monitoring would be a very difficult and time-consuming exercise and the interpretation of the monitoring results very difficult. In contrast, data on achievements in health, education and income are widely available for ASEAN countries.

But let's assume that agreement on a list of drivers of the development gap could be obtained, and that data on each of these variables were available for all ASEAN countries. Further, let's assume that the various imperatives identified in the three ASEAN Blueprints, referred to in Chapter One, can be quantified for all of these countries. While these quantifications can and probably should be used for monitoring the implementation of the Blueprints, this in itself does not provide a sufficiently strong case both to define the development gap and monitor this gap over time along these lines.

The AEC Blueprint has among its priorities the free flow of goods, services, skilled labour and investment and fairer competition among firms. To highlight our case let us assume that progress is being made against these priorities in all ASEAN countries, those in the CLMV group in particular. This progress in itself is of little value in its own right. We need to ask what the purpose of a freer flow of goods or increased competition is, and why they are of value. They are only of value if they lead to outcomes that are of intrinsic value, such as progress in quality of life dimensions. Here we need to refer back to Aristotle's position on wealth, that it is only useful for the sake of something else. This applies to most of the drivers of development outlined in this book, and also to the Blueprint priorities. We also need to ask why the Blueprints were adopted by ASEAN. This was due to a concern for differences in living standards among member states.

Of course, it could be argued that achievement in drivers that can be leveraged by policies outlined in the Blueprints ensures achievement in intrinsic quality of life outcomes, so that in monitoring the former we are, in effect, monitoring the latter. This argument is flawed as it ignores the fact that there are many other drivers that cannot themselves be driven by policy. Policies might well be implemented successfully, with increased competition, freer flows of goods, increased infrastructure investment and so on. It could also be the case that levels of infrastructure investment and the flow of goods and services between each ASEAN member is equalised. But clearly this will not ensure that living standards between ASEAN members are equalised. It does not even guarantee improvements in the quality of life and it could be very misleading to simply assume that it has increased in line with success in terms of policies aimed at driving the drivers. Given the above remarks, it follows that the case for monitoring development gaps in what might be termed high-level achievements in health, education and income is not confined to definitional convenience and data availability.
The ASEAN Development Gap: Measurement

Multidimensional Development Achievements

ASEAN HDI and income per capita data are shown in Figures 2.1 and 2.2 respectively. The data required to construct these figures, as well as Figures 2.3 to 2.6 and Table 2.1, were taken from UNDP (2012). The data in UNDP (2012) are widely used in policy and research circles and are highly accessible, being available for download from the UNDP website. In some instances missing yearly values for some countries had to be estimated, typically by linear extrapolation. Income per capita, infant mortality and adult literacy data for 2011 were not available for any countries. Each country value indicator was obtained by extrapolation using a linear time trend for the years in question, namely 2000 to 2011. The measure of income per capita shown in Table 2.1 is GNI per capita recorded in purchasing power parity dollars. GNI is preferred over the other common measure of per capita income—GDP per capita—as it includes income from abroad whereas the latter does not. Purchasing power parity data are preferred as they are adjusted to reflect differences in the costs of living between countries, which is important from a quality of life perspective. Large differences in average development achievements between the ASEAN-6 and CLMV are evident from Figures 2.1 and 2.2. Therefore concerns about the ASEAN development gap within official circles have empirical support.

There are many ways the development gap can be quantified using the HDI and GNI per capita and, of course, other development achievement measures. Different quantifications will be discussed and provided in Chapter Three. For the moment we confine ourselves to a simple but empirically and conceptually valid measure, that is the difference between average ASEAN-6 and average CLMV achievement, with the latter average being subtracted from the former.

A major consideration in selecting this measure is whether to use weighted ASEAN-6 and CLMV averages that take account of each ASEAN member’s population size. It is common, although not universally accepted in research on inter-country income inequality to weight measures using each country’s share of world population (see, for example, Milanovic, 2005, Firebaugh, 1999, McGillivray, 2010, and McGillivray and Markova, 2010). The basic rationale behind this is that countries with higher populations should have a greater impact on what is being measured. In the case of ASEAN development gaps, it would be expected to attach a higher weighting to the ASEAN-6 countries given the very large populations of Indonesia and the Philippines. This would mean that the gap, if population weights were applied, would be greater than would otherwise be the case.

In the final analysis it was decided not to apply population weights. This is on the grounds that within ASEAN policy and political circles the
concern is for gaps in development achievements between countries irrespective of their population sizes. In other words, there would still be concerns within ASEAN for the lagging development achievements of the CLMV countries, even if their populations were much smaller than they actually are.

Gaps in unweighted averages are shown in Figures 2.3 and 2.4. These averages have been calculated using data for all ASEAN member countries. In terms of human development and income per capita achievements, this gap is the vertical distance between the graph lines in Figures 2.1 and 2.2. These figures show gaps commencing in 2000, after all CLMV countries had joined ASEAN, until the latest year (2011) that data are currently available for all countries. Particularly interesting are the trends over time in the gaps in question. For example, the gap in human development has fallen by 13 per cent between 2000 and 2011; while during the same period the gap in income per capita has increased by 10 per cent. That the income gap has not reduced is consistent with the findings of the econometric investigation of Alavi and Ramadan (2008).

While it is a positive sign that the development gap between the ASEAN-6 and CLMV is converging over time, the rate of convergence and the relative distance between the two groups remains significant. The gap between these groups is emphasised by the information in Table 2.1. This table reports the number of years, based on simple linear time trends over the period 2000–2011, each country will take to converge with the highest individual ASEAN country achievement in 2011 with respect to each of the development gap indicators in question. The method used to calculate this number of years is outlined in Appendix 2.1. It follows that a gap also exists in these indicators, with the CLMV countries lagging well.

Figure 2.1 Differences in human development between ASEAN countries, 1980–2011 (Data source: UNDP, 2012)
Figure 2.2 Differences in achievements in income between ASEAN countries, 1980–2011 (Data source: UNDP, 2012)

Figure 2.3 Human development gap between CLMV and ASEAN-6 countries, 2000–2011 (Data source: UNDP, 2012)

behind their ASEAN-6 counterparts. These are the number of years to eliminate the ASEAN development gap measured using various indicators. It also reports the number of years required for each country to converge with the ASEAN-6 average for each indicator, with the exception of those countries that have already achieved these averages. These variables include achievements in health (indicated by life expectancy in years and the infant mortality rate), education (indicated by mean years of schooling and expected years of schooling), income (indicated by $PPP purchasing power
parity) and multidimensional development (indicated by the HDI). These variables are widely used in international development policy making and research circles and include those used in the current HDI (UNDP, 2011).

The information in Table 2.1 is sobering. Based on the results of the simple calculations reported, it will take the CLMV countries between 25 and 27 years to achieve the highest individual ASEAN country HDI score in 2011 based on trends in this variable since 2000. It will take them between 15 and 19 years to reach the 2011 average ASEAN-6 HDI score. For achievement in income, the equivalent numbers are between 37 and 59 years and 28 and 44 years. The estimated number of years for convergence to occur in the other indicators is typically higher, in some cases considerably so. For example, at the upper end of the scale, it is estimated that Viet Nam will take 268 years to achieve the highest individual ASEAN country achievement in expected years of schooling, and that Cambodia will take 235 to do likewise with respect to mean years of schooling.

What is also revealing from Table 2.1 is that the ASEAN-6 countries Indonesia and the Philippines will also take many years to achieve the benchmarks on which the calculations are based. In some cases they will take longer than some CLMV countries. The Philippines will take longer to achieve the 2011 average ASEAN-6 achievement in life expectancy than all the CLMV countries, and Indonesia will take longer to achieve the corresponding average for infant mortality than all of these countries except Myanmar. While this is based on estimates, it is nonetheless of policy relevance. It also points to a danger of measuring gaps using averages, which can conceal important information. We return to this issue in Chapter Three.
Table 2.1 Estimated years required for elimination of ASEAN development gap based on recent trends

<table>
<thead>
<tr>
<th>Achievement in Health</th>
<th>Achievement in Education</th>
<th>Achievement in Income</th>
<th>Achievement in Human Development</th>
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<td>Infant Mortality</td>
<td>Mean Years of Schooling</td>
<td>Expected Years of Schooling</td>
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<td>88</td>
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<tr>
<td>Viet Nam</td>
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<td>23</td>
<td>19</td>
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Data source: UNDP (2012)

Note: n/a: not applicable, as country is that with the highest or has equal to or greater than average ASEAN-6 achievement.
It should be emphasised that the calculations underlying Table 2.1 are relatively simple. They obviously take no account of growth in the highest development achievement of those countries in 2011, holding this achievement constant in all calculations. Nor do they take into account that continual achievements occur non-linearly over time, with it becoming increasing difficult to sustain rates of achievement at higher and higher levels. Both of these factors point to the estimated years required for the elimination of a development gap based on recent progress alone to be under-estimates. This points to the enormity of the task of eliminating, or at least significantly reducing, development gaps among ASEAN member countries, and the significant policy challenges ahead.

A different perspective on the ASEAN development gap is provided in Figures 2.5 and 2.6. They provide information on disparities among all countries, not just between the ASEAN-6 and CLMV groups. Disparity, or inequality, is measured using a Theil Entropy measure, which is used widely in research on inequality. This measure is outlined in Appendix 2.2. The higher the level of this measure the greater the inequality and vice versa. Disparities in human development and income achievements among the ASEAN-6 group since the mid-1980s and for the full ASEAN membership since the early 2000s are included in these figures. What is clear is that the addition of the CLMV group has made ASEAN a much more diverse group, contributing to a higher overall level of disparity. This is evident from the sharp jumps in the Theil measure from mid- to late 1990s; note that Viet Nam joined ASEAN in 1995.

![Figure 2.5 Disparity in human development among ASEAN countries, 1980–2011](image)

\[ \text{Disparity in Human Development (Theil Entropy Measure)} \]

\[ \text{ASEAN (Full Membership)} - ASEAN-6 \]
Poverty Reduction Achievements

It is unambiguous that a development gap between the ASEAN-6 and CLMV countries exists, with the latter lagging behind the former in achievements in human development and income. This is not the case if the existence of a gap is defined in terms of poverty levels. Figures 2.7 to 2.10 indicate why. Constructed using data obtained from World Bank (2012), these figures contain information on poverty levels in ASEAN-6 and CLMV countries. They are based on the two most widely used poverty measures, the number of people living below the $PPP1.25 per day poverty line and the number living below the $PPP2.00 per day poverty line. These measures are also known as poverty headcounts, as they are obtained by counting the number of people living below the chosen poverty lines.

For both measures, there are more people living in income poverty in the ASEAN-6 group than the CLMV group. So there is a development gap, defined purely in terms of income poverty, but it is subtaientially in the CLMV group's favour. As Figure 2.7 suggests, there have been significant reductions in $PPP1.25 per day poverty rates in the CLMV countries over the last 15 years. Much of this is due to the performance of Viet Nam. The rate of reduction in poverty at this level has been less impressive in the ASEAN-6 countries and has stabilised relative to the CLMV, as can be clearly seen in Figure 2.8.

Based on the most recent comprehensive country-level data at our disposal, relating to 2008, just under 66 million people in ASEAN-6 countries lived on less than $PPP1.25 per day. Almost all of these people lived in Indonesia and the Philippines. In the CLMV group, just under
20 million lived on less than $PPP1.25 per day, meaning that there were 46 million more people living in extreme income poverty in the ASEAN-6 group than in the CLMV group. Poverty data for Myanmar are not available and not, therefore, included in this comparison, nor are data for Singapore and Brunei Darussalam owing to unavailability, although this is of no consequence for the present analysis owing to there being few people living in poverty in these countries. Yet if data for Myanmar were available and included in the CLMV total this would not swing the gap in
the ASEAN-6 group's favour as the total population of this country was 47.25 million in 2008 (UNDP, 2012). For the $PPP2.00 per day line, there are 120 million more people living under this poverty line in 2008 or 2009 in the ASEAN-6 group than in the CLMV group. Data for Myanmar are also not included in this comparison owing to unavailability but if it was the case that all Myanmar citizens lived on less the $PPP2.00 per day, which is certainly not the case, then there would still be an excess 70 million more people living in poverty according to this line in ASEAN-6 than CLMV countries.

In examining poverty levels one needs not only to look at the number of people living in poverty but also at how far the incomes of the poor fall below the poverty line in question. Put differently, one needs to look at both the extent and depth of poverty. The depth of poverty is measured by the poverty gap indicator, which shows the average income shortfall from the poverty line of the population living below it. Poverty gap data based on the $PPP1.25 and $PPP2.00 poverty lines are shown in Figures 2.9 and 2.10 respectively. These data are also taken from World Bank (2012). In each of these figures the average gaps for the ASEAN-6 and CLMV countries are plotted for those countries for which poverty gap data are available. The countries for which data are not available are Myanmar, Singapore and Brunei Darussalam. What the figures reveal is that while there are more poor people in the ASEAN-6 than CLMV countries, the poor in the latter are poorer than those in the former. In 2008 the extremely poor in the CLMV countries fell on average below the $PPP1.25 poverty line by roughly twice their counterparts in the ASEAN-6 countries, by 4.9 per cent compared to 2.2 per cent. Approximately the same margin applies to the $PPP2.00 poverty line, being 18.6 per cent for the CLMV countries and 8.30 per cent for the ASEAN-6. This does not imply that the poor in the CLMV countries are on average twice as poor as those in ASEAN-6 countries, just that they are poorer. In 2008 those below the $PPP1.25 poverty line in CLMV countries were on average 4 per cent poorer than those in ASEAN-6. For the $PPP2.00 line the poorer in the former group of countries were on average 11 per cent poorer than those in the former group.

From the preceding discussion it has been established that there are many more poor people in the ASEAN-6 than in the CLMV group, but those in the former are less poor than those in the latter. So which group has the highest development achievement assessed against an income poverty criterion, and in whose favour does the development gap fall? A crude way of combining information on the number of people living in poverty and the poverty gap is simply to multiply the two indicators by each other, or to multiplicatively weight the poverty gap by the poverty headcount. Such a weighting is shown in Figures 2.11 and 2.12, for the $PPP1.25 and $PPP2.00 poverty lines respectively. It has been calculated
using the data plotted in Figures 2.7 to 2.10. It is shown that ASEAN-6 countries on average lag slightly behind the CLMV group in terms of both poverty lines.

Finally, with respect to income poverty, another way of looking at poverty is to look at what might be described as its intensity or incidence, measured by the percentage of a country’s population that lives below the chosen poverty line. This is consistent with equating a country’s development achievement with its success in minimising the proportion of
its population that live in income poverty. This information on the intensity of poverty is shown in Figures 2.13 and 2.14, for the $PPP1.25 and $PPP2.00 per day poverty lines. The data used to construct these figures has been taken from World Bank (2012) and has the same country coverage of Figures 2.7 to 2.10. The intensity of poverty is higher in the CLMV than ASEAN-6 group, although the gap has narrowed since the early 1990s. Measured using the $PPP1.25 poverty line, in 2008 it was only slightly higher in the former than the latter, being 18.6 per cent compared to 16.7 per cent.
It was noted above that poverty is multidimensional. Thus far we have focused purely on income poverty in assessing the ASEAN development gap. The UNDP provides a measure of multidimensional poverty—the Multidimensional Poverty Index (MPI). The MPI recognises three quality of life dimensions that are considered important to all people in all societies. These dimensions are health, education and material living standards. Household achievements in these dimensions are measured using ten equally weighted indicators (Alkire and Santos, 2010; UNDP, 2010). Further details of the MPI are provided in Chapter Three.
The MPI was first introduced in the *Human Development Report 2010* (UNDP, 2010) and at present the country and yearly coverage of the index is rather limited. UNDP (2011) provides MPI scores for all ASEAN countries except Brunei Darussalam, Malaysia and Singapore. Shown below in Figure 2.15 are scores for the 2000s, ranging from 2000 for Myanmar to 2008 for the Philippines. Multidimensional poverty is on average far higher—three times—in the CLMV than the three ASEAN-6 countries, Indonesia, the Philippines and Thailand (IPT). The MPI is interpreted differently to the income poverty measures discussed above, encompassing both the depth of poverty and its intensity.

**The ASEAN Development Gap: A Synthesis**

How might the material presented above be summarised and synthesised? What has been shown is that a development gap exists, with the CLMV countries lagging behind their ASEAN-6 counterparts in each of the development achievements in the health, education and income dimensions, based on all indicators considered. However, this gap has narrowed slightly over the last decade. The gap in income has increased by 10 per cent during this time though. Different messages are provided by the poverty data. There appears to be a very large development gap that favours the CLMV countries. The gap based on the number of people living below the $PPP1.25 and $2.00 per day poverty lines sees the ASEAN-6 countries lagging well behind their CLMV counterparts; the reverse is the case based on the average poverty gap where the CLMV group lags slightly behind ASEAN-6 in terms of the intensity of poverty.

*Figure 2.15 Multidimensional poverty in ASEAN countries (Data source: UNDP, 2011)*
What can we conclude from these findings? It follows that if we are to talk of an ASEAN development gap that is real and empirically robust across a variety of measures, then this applies to multidimensional development but not poverty reduction achievements. Or, put differently, the gap is only meaningful and evident if we define development in terms of the former achievements only. On these grounds, what shall follow in this chapter and the remainder of the book is a focus on the ASEAN development gap defined on the basis of overall achievements in the identified development variables.

**Drivers of the ASEAN Development Gap**

The ASEAN development gap arises from differential development achievements. Policy interventions seeking to reduce the gap must be based on an understanding of what drives it, and, in turn, which of these drivers can themselves be driven by policy interventions. Achievements in health, education and income are endogenously related. Growth in incomes is, in particular, a major driver of achievements in health and education. It does so by providing both public and private resources that can be allocated to health and education services (McGillivray, 2005). Growth alone is insufficient to guarantee broad-based achievements in health and education, but it is necessary for such achievement (Commission on Growth and Development, 2008).

What drives income growth, in large part, drives these achievements. This is true in general, but also applicable to the CLMV countries, as shown in Figures 2.16 to 2.20. These figures contain scatter plots linking achievements in $PPP GNI per capita to adult literacy, infant mortality and the HDI respectively. The first of these variables is expressed as a natural logarithm, reflecting the well-known diminishing marginal returns to the conversion of income to other quality of life dimensions. Each scatter plot contains a line of best fit, obtained from a simple regression of $PPP GNI per capita on each of the three other achievement variables. These scatter plots show the simple statistical relationship between the former and the latter variables. These relationships should be interpreted as showing a general association as the method obtained to depict them ignores a range of statistical issues such as endogeneity (in which income both drives and is driven by the other variables) and the influence of variables other than income on the health and education outcomes under consideration. They, in particular, do not and are in no way intended to show a precise, causal relationship, just a general association. This caveat noted, in each case higher achievements in income per capita are associated with higher achievements in the other four variables. Higher achievements in the case of infant mortality means a reduction in the infant mortality rate.
In what follows we first examine drivers of growth. These drivers include health and education. It follows that if we are to understand and devise policies aimed at driving growth we also need to know what drives achievements in health and education. This topic is also examined below. There is an enormous academic and policy literature on these drivers. Many drivers are identified but there is significant disagreement over some
of them. In what follows we focus on key drivers that are thought to be common to all countries that have been shown, or are widely believed to have the potential, to be important to ASEAN countries. It follows that if certain drivers are to be stimulated in efforts to reduce the ASEAN development gap there needs to be confidence that there is a real and robust link between each driver and development achievements. An objective of
understanding the ASEAN Development Gap

our examination is to provide such confidence, based not only evidence from ASEAN, where it exists, but on the experience of other countries as documented in the research literature.

Drivers of Growth

As Brooks et al. (2010) and Menon (2012) and many other studies note, the literature points to the following key drivers of growth:

1. physical capital;
2. openness to trade;
3. human capital;
4. financial sector development;
5. governance;
6. labour mobility;
7. foreign direct investment, and;
8. external development finance.

Of these drivers, it is physical capital that is the least contentious. Physical capital or infrastructure includes roads, water supply, power grids, telecommunications and water supply and sanitation systems. As Brooks et al. (2010: 7) comment, ‘no country has sustained economic growth without also keeping up an impressive rate of investment in infrastructure’. While there is some speculation about the precise empirical contribution of infrastructure investment to growth, and discussion of the contributions of
different types of infrastructure, it can be taken as a basic fact that ongoing investment in infrastructure, together with maintenance of the infrastructure stock, are keys to achieving and sustaining higher per capita income levels. This is substantiated time and time again in the research literature. Brooks et al. (2010) refer to the research of Calderón and Servén (2004) in support of the statement quoted above. This cross-country research of 100 nations covered the period 1960–2000. It found that an increase of one standard deviation of an index in infrastructure stocks would raise per capita income by an average of 2.9 percentage points per country. It is clear from the preceding comments that ongoing investments in infrastructure in CLMV countries are essential for reducing the ASEAN development gap. This issue is discussed in some detail in Chapter Four.

It is important to be clear as to what is meant by openness to trade. Trade openness refers to the actual or potential extent an economy trades with the rest of the world. As such it may be defined and measured in two broad ways. It may be defined as the extent to which an economy trades with the rest of the world, measured by the volume of its trade flows relative to the size of its domestic economy. The volume of trade relative to GDP is measured by the sum of the economy’s exports and imports as a share of its GDP. Yet an economy may still be open to international trade even if it has low trade volumes. Key here is the policy stance of the government of the country in question. An economy may be considered open to trade if the following conditions are present: if imports are able to flow freely into it owing to an absence of tariff and non-tariff barriers; if there is an absence of a black market for foreign exchange that sees the exchange rate for the country’s currency below the official rate; and if there is an absence of government monopolies in major exports and a command economic system. These specific indicators are the criteria on which the well-known Sachs and Warner (1995) measure of policy-related trade openness is based.

Openness can contribute to growth in per capita incomes in a variety of ways. Exporting to the rest of the world can allow for greater capacity utilisation and economies of scale and incentives for technological innovation and improved management efficiency due to the pressure of overseas competition, as Feder (1982), Balassa (1985) and a host of other studies have noted. Importing goods from the rest of the world can allow for the greater absorption of technological advances and for greater productive capacity. Moreover, as Edwards (1997) and others note, if the costs of technological imitation in poorer countries are lower than the costs of locally developed technological innovations, then these countries can grow faster than their richer counterparts and development gaps can be reduced more expeditiously.

There is an enormous empirical literature on the impact of trade openness on growth. Among the many studies focusing on developing countries are Balassa (1978, 1985), Dollar (1992), Edwards (1993) and
Yanikkaya (2003). Any objective and comprehensive reading of this literature would conclude that the relationship between trade openness and per capita income growth is ambiguous. This is not to imply that trade, both import and export, does not contribute to higher growth. To the contrary, there is a robust and positive empirical relationship between trade volumes relative to GDP being drivers of per capita income growth. The ambiguity is over the impact of policy regimes and trade liberalisation. While it seems that most economists and policy makers strongly favour trade liberalisation, it is not clear that removing restrictions on trade is necessarily good for growth in all circumstances. Yanikkaya (2003) actually concludes that trade restrictions, including those imposed under an import substitution regime, can under certain circumstances be beneficial for growth. These circumstances include whether production in a protected sector is relatively efficient. This is consistent with the position taken by Rodrik (1999) and cited by Yanikkaya, that just as the advantages of import substitution policies were overstated in earlier eras, the benefits of openness have often been oversold by its proponents. Such a finding should not in any way be seen as an unqualified justification for trade restriction. Such restriction can only be justified, if and only if, it can be shown that the government in question selects the right sector to protect.

There is also a large literature on the impact of openness in ASEAN countries, mostly relating to the ASEAN-6 countries. Some studies have concluded that exports have played an important role in promoting growth (see, for example, Fukuda and Toya, 1995, and Hsiao and Hsiao, 2006). Others question the direction of causation, presenting evidence that growth has caused exports but failing to find a causal link from exports to growth (Ahmad and Harnihirun, 1992, 1995). Singapore, however, seems to be the exception, with exports both causing and being caused by economic growth (Ahmad and Harnihirun, 1995). One can speculate why this might be the case, but given the experiences of many other countries there remains a strong case for seeking to promote greater trade openness and, in particular, higher levels of exports throughout ASEAN and, in particular, the CLMV group. Achieving higher levels of openness, both in terms of the levels of exports and imports relative to GDP, and in terms of policy stance, among the CLMV group will help address the ASEAN development gap. Further discussion of this issue is provided in Chapter Five.

Human capital has traditionally been defined as the stock of competencies, skills and knowledge possessed by individuals to produce economic value. As such it is associated with achievements in education and training. The definition of human capital can be extended to include the ability to produce such value, and therefore is associated with achievements in health. A person with low achievements in health will obviously be constrained in the economic value they produce.
Economists have long been aware of the importance of human capital for economic growth, with discussion of it gaining prominence in late 1950s and early 1960s from contributions such as that of Schultz (1961). That education and training is in general a key driver of growth is unchallenged, as a number of key studies have shown (see, for example, Barro, 1991, 2001; Romer, 1993). What is debated is whether all aspects and types of educational achievements drive growth. Romer (2001), analysing a sample of 100 countries for the period 1960–1995, found that growth was positively related to the average years of school attainment of adult males at the secondary and higher levels but not significantly related to years of school attainment of females at these levels or to years of primary attainment by either sex. Some studies point to investments in education having a limited short-run effect, and others have questioned the link between educational attainment and growth, including Benhabib and Spiegel (1994) and Pritchett (1997). While questions regarding short-run effects remain, later research has suggested that the doubts about educational attainment were due to the impact of unrepresentative observations in the datasets under question. As such there is now a case for disregarding this research.

What must not be disregarded is research on the drivers of health and educational achievements. These are development achievements that are of value in their own right, irrespective of their impact on growth. As such, information on these drivers is of dual benefit. Surveying the drivers of the many different types of health and education achievements is an enormous task that is beyond the scope of this chapter. But it is instructive to point to some key messages that emerge from the literature. The first is that while economic growth is a key driver, there is much more to these achievements than growth alone, with some countries achieving much higher levels of health and education than their income levels alone would predict (McGillivray, 2005). There are several other drivers of these achievements that can be stimulated by government policy. Public expenditure accompanied by the effective delivery of health and education services are the most obvious drivers. Good quality health and education systems are required, more generally. This not only relates to service delivery and funding, but also to the use of human resources, the provision of information, the quality of medical and educational products and technologies, and leadership and governance (WHO, 2007; Glewwe and Kremer, 2005). There are also important social determinants of both health and education achievement, including poverty, social exclusion and gender discrimination. As Glewwe and Kremer (2005) and many others observe, there is often a pro-rich bias in the provision of education services. The same applies to health services. Such bias is a significant constraint to higher health and education attainment in developing countries.
In 2000, the WHO ranked 190 countries on the basis of the performance of their health systems (WHO, 2000). It no longer provides such a ranking now owing to the complexity of the task, and the 2000 ranking was controversial. It is now, of course, rather dated. With these points in mind it is instructive to consider the rankings of the ASEAN countries. The CLMV countries were ranked among those with the worst performing health systems. Viet Nam’s ranking out of the 190 countries was 160. Lao PDR, Cambodia and Myanmar were ranked 165, 174 and 190 respectively. Of the ASEAN-6 countries, Singapore was ranked at position 6. The rankings of Brunei Darussalam, Thailand, Malaysia, Philippines and Indonesia were 40, 47, 48, 69 and 92 respectively. One would hope that these gaps have diminished substantially. If not, they must be seen as a major issue in addressing the ASEAN development gap, and be given very high priority in policy interventions.

The financial sector provides financial services to commercial and retail customers and consists of banks, credit unions, financiers (including microfinance providers), insurance companies, investment fund managers and all other organisations that manage money. There is a compelling case that financial sector development is an important driver of economic growth in developing countries. Zhuang et al. (2009) and Brooks et al. (2010) note that a well-functioning financial sector mobilises and pools domestic savings, enhances resource allocation by effectively transmitting information, exerts pressure to improve corporate governance, facilitates trade and diversification and the better management of risks, and promotes the exchange of goods and services. Through these impacts, financial sector development drives economic growth not only by promoting private sector expansion, but also by supporting public sector investment in physical infrastructure and enabling households to invest in human capital and smooth consumption (Zhuang et al., 2009).

There is an enormous research literature on financial sector development and growth. There have been many surveys of this literature, including Honohan (2004), DFID (2004), Levine (2004), Andrianova and Demetriades (2008) and Zhaung et al. (2009). While there was some disagreement in the early research, there is now overwhelming and robust empirical evidence that financial sector development contributes to higher economic growth. For example, building on the influential research of Goldsmith (1969), King and Levine (1993a, 1993b) find that for 80 countries over the period 1960 to 1989, financial development is positively associated with growth. Increasing financial depth (measured by the ratio of liquid liabilities to GDP) was found to be particularly important, as it increased a country’s per capita income growth rate by almost one percentage point per year. They also found that the depth of the financial sector accounts for 20 per cent of the difference in per capita income growth performance between the highest and lowest quartile of performers.
over the 30-year period from 1960 to 1989. King and Levine’s results also suggest that the level of financial depth in 1960 is a good predictor of subsequent rates of economic growth, capital accumulation and productivity growth over the next 30 years, even after controlling for income level, education, and measures of monetary, trade and fiscal policies (King and Levine 1993a, 1993b, cited in Zhuang et al., 2009). This finding is consistent with a number of other empirical studies that suggest the positive impact of financial sector deepening on economic growth appears to be greater for developing countries than for developed countries (Calderon and Liu, 2003; Jalilian and Kirkpatrick, 2005; Kumbhakar and Mavrotas, 2008; Mavrotas and Son, 2006). Zhuang et al. (2009) cite a number of studies pointing to the benefits of financial sector development in Southeast Asia.

While the evidence of the important role of financial sector development in supporting growth is reasonably clear, it is equally clear that such developments are no panacea insofar as growth is concerned. That is, in order for it to be effective in this regard it needs to be accompanied by a range of support services, including the provision of training and capacity building and assistance in accessing markets and technologies. Financial sector development and innovation will also bring risks, and as such it is important to maintain sound macroeconomic management, put in place effective regulatory and supervisory mechanisms, and carry out structural reforms in developing the financial sector (Zhuang et al., 2009). This will need to be kept in mind among ASEAN countries should financial sector development be relied upon to reduce the development gap among them. That noted, based on the wealth of evidence on the impact of financial sector development, ignoring this sector could well be at the cost of a larger development gap than would otherwise be the case.

**Governance** has long been acknowledged as an important driver of growth, increasingly so over recent decades. Often also referred or linked to institutional quality, governance is the manner in which authority is exercised in the management of a nation’s resources. The positive association between governance and institutional quality, and economic growth and income levels is very well established. Institutional quality and governance enable the enforcement of property rights and contracts that facilitate market exchange, investment and innovation, and reduce transactions costs (Acemoglu et al., 2001; Aron, 2000; North, 1990; Rodrik et al., 2002). Empirical research points to governance and institutional quality being associated with higher economic growth and income levels (Campos and Nugent, 1998; Barro, 1999; Acemoglu et al., 2001; Lee and Kim, 2009), higher levels of public and private investment (Knack and Keefer, 1995; Rodrik, 2003), higher levels of human capital (Arimah, 2004) and greater sustainability of common resource pools (Ostrom, 2005).
Accountability, transparency, rule of law, political stability, bureaucratic capability, property rights protection and contract enforcement, and control of corruption are now regarded as key and mutually reinforcing aspects of growth-enhancing institutions. ASEAN countries, in particular the CLMV group, will need to continue to strive for improvements in each of these areas if the development gap is to be reduced. Control of corruption is an area in which CLMV countries especially will have to work, based on the 2011 Transparency International Perceptions of Corruption Index. While Singapore was ranked number 6 according to this index, Viet Nam, Lao PDR, Cambodia and Myanmar were ranked number 112, 154, 164 and 180 respectively out of 182 countries (Transparency International, 2012).

Labour mobility involves the flow of people, or migration, and has emerged as a key issue in development. Two aspects of labour mobility are central to its development implications: brain drain and remittance flows.

Brain drain occurs when the source country loses skilled personnel to the host country. This can have significant adverse implications for countries where the earnings of personnel are relatively low. Skilled personnel can leave these countries seeking higher earnings abroad, leaving a skill shortage at home. The impact of brain drain for the host country need not necessarily be adverse, as Beine et al. (2001) note. This is because it can foster investments in education and training in the source country, leading to a higher average level of human capital than would otherwise be the case. Whether brain drain has an overall adverse impact on income growth depends on the relative strengths of the two impacts. There is little empirical evidence on the relative strengths of the impacts, although Beine et al. (2001) find that the beneficial impact of higher average human capital outweighs the impact of the outward flow of skilled personnel. In an interesting analysis, Mountford (1997) shows that when migration is not a certainty, a brain drain may increase both average productivity and equality in the source economy.

The impacts of remittances have been extensively researched. This is no surprise, as remittances are an important source of foreign income for developing countries, increasing dramatically in size over recent decades. Arising primarily from migration of un- or semi-skilled workers, developing country remittance receipts were US$ 0.3 billion in 1971. These receipts are expected to reach US$ 350 billion in 2011, up from US$ 320 billion in the previous year. Remittances now account for more than two and a half times the global level of Official Development Assistance (ODA), having accounted for less than 5 per cent of the level of ODA in 1971 (World Bank, 2011a, 2011b). They flow directly to households rather than governments, which can be advantageous, as they can serve as a de facto social safety net in difficult times, and can offset macroeconomic volatility.
It is not surprising, therefore, that there is a large and growing research literature on the economic impacts of remittances in developing countries. A number of empirical studies have looked at the impact of remittance inflows on the economic growth rates of these countries. Catrinescu et al. (2009), Jongwanich (2007) and Pradhan et al. (2008) find some evidence of a positive association between remittance receipts and growth while other studies find the impact varies according to a country’s educational attainment, financial market depth and quality of institutions (Giuliano and Ruiz-Arranz, 2009; World Bank, 2006; Ramirez and Sharma, 2008). Ang (2007) reports a positive and statistically significant impact of remittances on growth in the Philippines. Feeny et al. (2012) report the same finding for small island developing states (SIDS), and find that, in the absence of remittances, growth in South Pacific SIDS would have been negative for the period 1971–2010. Other studies have examined the impacts of remittance inflows on known drivers of growth. López-Córdova (2006) and Acosta et al. (2007) looked at impacts on human capital, Aggarwal et al. (2011) and Demirgüç-Kunt et al. (2011) were concerned with impacts on financial development, Chami et al. (2003) and Jackman et al. (2009) examined impacts on investment volatility, and Amuedo-Dorantes and Pozo (2004) investigated the impacts on the real exchange rate, reporting mixed evidence.

Regardless of what the impact of brain drain and remittances on growth of per capita income might be, the point remains that migration can be made to work for source countries. The potentially harmful impact of skilled labour losses owing to brain drain can be offset by the potentially positive impacts of a more highly skilled workforce and remittance flows. Ensuring a freer flow of migrants of all levels of skills among ASEAN countries, and in particular from CLMV to ASEAN-6 countries, is therefore one way to narrow the development gap.

**Foreign direct investment** (FDI) can play a crucial role in contributing to income growth in host countries. It not only augments local investment but can potentially lead to increased technology, better managerial expertise, increased research and development, and productivity and efficiency gains. It will promote higher growth in the long run if it generates improvements in technology (Solow, 1957; de Mello, 1997) or improvements in human capital (Lucas, 1988; Rebelo, 1991; Romer, 1986). Yet it is not without its critics, who argue that policies to attract FDI can distort domestic incentives and displace domestic investment, crowding out employment and the activities of domestic firms.

There is a large empirical literature on FDI and growth. Studies include Alfaro et al. (2004), Borensztein et al. (1998), Bornschier et al. (1978), Carkovic and Levine (2005), de Mello (1999), Doucouliagos et al. (2011), Lensink and Morrissey (2006), Mankiw et al. (1992) and Papanek (1973). The consensus of this literature is that the impact of FDI has been
favourable in that growth would be lower in host developing countries if it were not for FDI. This does, however, depend on a number of contingencies, with the incremental impact of FDI varying across host countries. In a meta-analysis, Doucouliagos et al. (2011) find that the impact of FDI varies across these countries according to levels of financial development, trade and human capital. A number of empirical studies point to FDI being an important driver of income growth in many of the ASEAN-6 countries. Hsiao and Hsiao (2006) point to a bidirectional relationship between FDI and growth for a sample of countries that includes Malaysia, Philippines, Singapore and Thailand. Fan and Dickie (2000) found that for Indonesia, Malaysia, Philippines, Singapore and Thailand FDI contributed between 4 and over 20 per cent of GDP during 1987 to 1997.

This research provides a compelling reason for seeking to increase FDI flows to the CLMV countries as one means of decreasing the ASEAN development gap. But it is also clear that FDI alone will not sustain higher growth rates in these countries. It should not crowd out domestic economic activity, and needs to be led to or be accompanied by higher levels of human capital, improvements in technology and financial sector development. In this context the encouragement of FDI in Cambodia, Lao PDR and Viet Nam in most sectors is a welcome development, although the downward trend in FDI to Myanmar since the early 2000s is a matter of concern (Menon and Melendez, 2011; Menon, 2012).

External development finance consists of a number of inflows including export credits, portfolio investment and official development finance. Official development finance from OECD countries, the largest providers, consists of ODA and other official finance, the latter not being sufficiently concessional to be classified as ODA. ODA is also more popularly known as foreign aid. The developmental effectiveness of foreign aid, including its impact on economic growth, is a contentious topic. Brooks et al. (2010: 21) recognise this, commenting that the 'role of official development assistance in closing development gaps has been mixed and at times controversial'.

In looking at the literature on aid and growth it is instructive to distinguish between studies published in the late 1990s and earlier. The earlier studies were largely inconclusive, either finding that aid increased, decreased or had no impact on growth or a key driver, savings. If an overall conclusion is possible from this literature it is that aid had no impact on growth in recipient countries (McGillivray et al., 2006). The late 1990s marked a significant change in the aid-growth literature, commencing with the influential study by Burnside and Dollar (2000), which concluded that aid can work if recipient governments had 'good' policies. Subsequent studies, including Burnside and Dollar, used better data, theory and empirical techniques than those that preceded them. There have been numerous comprehensive surveys of the more recent aid-growth literature, which consists of scores of studies. These surveys include Morrissey (2001),
Clemens et al. (2004), Dalgaard et al. (2004), Addison et al. (2005), McGillivray et al. (2006) and Feeny and McGillivray (2011). All point to the literature concluding that growth would have been lower in the absence of aid. The results of a number of studies suggest that growth in recipient countries would be in the vicinity of one percent points lower in the absence of aid (Feeny and McGillivray, 2011).

That the aid-growth literature surveys point to growth being lower in recipient countries in the absence of aid does not mean that there are no contrary voices emanating from empirical research circles. Doucouliagos and Paldam (2008) conducted a meta-analysis of the aid-growth literature and found that aid has failed to stimulate income growth. Mekasha and Tarp (2011) looked closely at the Doucouliagos and Paldam analysis and suggested that its results were not robust owing to a number of technical issues. Rajan and Subramanian (2008) could not find a positive association between aid and growth. This widely cited paper has been extremely influential in policy circles, and has led observers to conclude that it is evidence that aid has been ineffective in promoting growth. This is a misinterpretation of the paper’s results. Rajan and Subramanian simply could not find a link between aid and growth, which is not to say that such a link does not exist. That so many other studies have found the link suggests it does indeed exist.

The results of empirical research on aid notwithstanding, it remains the case that there is widespread disappointment with aid effectiveness, as is evident in the remarks of Brooks et al. (2010) quoted above. What are the grounds for this disappointment? It is reasonable to speculate that it stems from too lofty expectations of aid in the first place. In the early days of aid to developing countries, and in part consistent with the success of the Marshal Plan in Europe after World War Two, it was expected that aid alone would put developing countries on a path to self-sustaining growth and would eventually rid the world of poverty. That it has not, and that as global aid has increased over time so has the incidence of global poverty, is perhaps at the heart of the disappointment and the reason why so many have considered aid as a failed enterprise. It needs to be remembered, however, that aid, has, on average, over the last 40 years roughly been 1 to 1.5 per cent of recipient country GDP. At these levels one can hardly realistically say that aid has been a failure, although one might be able to argue that the aid effort, by not leading to larger amounts of aid, has been. A better question is to ask whether economic growth, and poverty incidence, would have been lower in the absence of aid. The aid-growth literature quoted above suggests the answer to this question is yes.

What does this mean for aid and the ASEAN development gap? Unfortunately, we do not have a research literature on the impact of aid on growth to ASEAN countries on which conclusions about its
effectiveness to these countries can be judged. What is also unfortunate is that the aid-growth literature does not provide a consensus on the mechanisms through which aid leads to growth. As mentioned, Burnside and Dollar (1997, 2000) argue that the impact of aid on growth is contingent on the policy regime of recipient countries. Subsequent research rejects this contingency, instead pointing to factors such as economic vulnerability, democracy and climate (McGillivray, 2003). This lack of consensus is unfortunate as guidance for policy aimed at increasing aid effectiveness is not provided.

This is not, however, to imply that such guidance does not exist. It does, in the form of the Paris Declaration principles. These principles emanated from the Paris Declaration on Aid Effectiveness, which was adopted by the international community at the 2005 Paris High Level Forum on Aid Effectiveness, hosted by the French government and organised by the OECD. Based on decades of lessons from the practice of delivering aid to developing countries, the five principles are as follows.

1 Ownership—developing countries must lead their own development policies and strategies, and manage their own development work on the ground.

2 Alignment—donors must line up their aid firmly behind the priorities outlined in developing countries’ national development strategies, they should use partner country systems, their aid must be untied and be predictable.

3 Harmonisation—donors must coordinate their development work better among themselves to avoid duplication and high transaction costs for poor countries.

4 Managing for results—all parties in the aid relationship must place more focus on the result of aid, the tangible difference it makes in poor people’s lives.

5 Mutual accountability—donors and developing countries must account more transparently to each other for their use of aid funds, and to their citizens and parliaments for the impact of their aid (OECD, 2005).

Aid to the CLMV countries that is consistent with the Paris principles will enhance its impact on growth and in turn reduce the ASEAN development gap. This does, however, require that relative to the size of their economies and populations, the CLMV countries receive larger shares of total ASEAN aid receipts than their ASEAN-6 counterparts. If we accept that aid flows are effective in promoting growth in per capita incomes and greater achievements in health and education, giving preference to the ASEAN-6 over CLMV countries will exacerbate the existing gap. This issue is explored further in Chapter Five.
Conclusion

The preceding discussion demonstrated that a real and measureable development gap exists between the CLMV countries and the ASEAN-6. The gap in human development achievement has been gradually decreasing over time, but the gap in income has increased by 10 per cent over the last decade or so. With regards to poverty, the analysis in this chapter has demonstrated that by far the largest number of poor people live in the ASEAN-6 countries, almost entirely in Indonesia and the Philippines, but that the depth of poverty and its intensity is greater in the CLMV countries. That is to say that the poor in the CLMV are poorer than the poor in the ASEAN-6. This chapter also suggested, very conservatively, how long it will take CLMV countries to reach the average development achievements of the ASEAN-6. This analysis suggested that it will be at least two decades before we see some significant convergence in most indicators, although some countries, most notably Viet Nam, will converge with ASEAN-6 much earlier and indeed convergence in some areas is already being observed.

This chapter also highlighted the various drivers of the development gap and commented on issues that should be considered when developing policy responses to narrow the gap. This analysis suggested that the impact of these drivers will be variable across countries depending on their development achievements to date and on their capacity. A clear theme running through this analysis is the importance of improving governance and institutional quality to more expeditiously narrow the gap. These issues will be discussed at length through this book.

Appendix

2.1 Estimation of Years Required for Elimination of ASEAN Development Gap Based on Recent Trends

The number of years was estimated in two steps. The first step involved fitting the following regression equation to annual development achievement data for the period 2000–2011:

\[ d_t = \alpha + \beta t + \mu_t \]

where \( d_t \) is the ASEAN country development achievement (in health, education or income) in question in period \( t \), \( t \) is time, \( \alpha \) is an intercept, \( \beta \) a regression coefficient and \( \mu_t \) is a residual. The first observation of the time variable is 2000 and the last is 2011. The equation was fitted to the data using the ordinary least squares method.

The estimate of the number of years required to eliminate the gap was obtained in the second step. This involved solving for \( n \) in the following equation:
where $d_{2011}^w$ is either the highest development achievement in question among all ASEAN countries or the average achievement in question among the ASEAN-6 group in 2011, $d$ is the achievement of the country in question in 2011, $v_d$ is the arithmetic mean of the development achievement in question during 2000–2011 and $n$ is the number of years required to eliminate the gap.

2.2 Calculation of Disparity in Development Achievements: The Theil Entropy Measure

The following Theil Entropy measure was used to quantify development disparities or inequalities among all ASEAN countries:

$$I_d = \frac{1}{j} \sum_{i=1}^{j} \ln \left( \frac{\Phi_d}{d} \right)$$

where $I_d$ is inequality in the development achievement in question, $\Phi_d$ is the arithmetic mean of the development achievement among all ASEAN countries, $j$ is the total number of ASEAN countries and $d$ is that achievement for ASEAN country $I$ and ln denotes natural logarithm.

Note

1 It must be noted that ASEAN, through the ASEANstats Division, currently compiles the same indicators used in this study, excluding the GNI per capita $\$PPP$, but as provided by the national statistical bodies.

References


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