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**RESEAU D'ETUDES ET DE RECHERCHES SUR LA COHESION ET LES TERRITOIRES EN EUROPE**

# **GOVERNANCE AND GROWTH: CASE STUDY OF SELECTED COUNTRIES IN SOUTH EAST ASIA**

*Problem Analysis: The Need for Governance Indicators*

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The post WWII reconstruction period considered economic growth as a primary factor to development. Economic Indicators such as market openness, industrialization, and growth rates were the only measurement of the growth of an economy. It was not until the 1980s that many economists and social scientist started to feel that the trickle down effects of economic growth was insufficient for long term development and poverty eradication.

The role of factors previously thought of as external, such as institutions, system of governance, level of corruption etc began to gain importance in the designing and implementing a long term sustainable poverty reduction policy. In recent times, more and more scholars, including Jeffery Sachs, Amartya Sen, Joseph Stiglitz etc articulated their concerns on including a diversified range of factors to induce and measure economic development including the political system and good governance. Researchers in recent times estimate that with one-standard deviation of improvement in governance, income rise 3 fold in the long run. (The World Bank 2006)

In measuring economic growth, per capita GDP growth rate, adjusted for inflation is a widely used indicator. To acquire a realistic scenario of the society as a whole, indicators such as the Gini Index is used to measure income distribution, Human development index can be used to understand the nature of growth and the effects of GDP growth on the welfare of the population.

In terms of the quantitative measurement for governance, the indicators vary between different organizations and schools of thought-while some organisations measure the effectiveness of government functions, other measure the type of govt. or the nature of democracy. Eg., The United Nations Development Programme prefers to customise the indicators on a country to country basis, World bank conducts its research on a fixed set of indicators that range concentrates on political accountability, political stability and violence and Government Effectiveness and calculates a percentage point for each indicator in a global comparison, i.e., if a country is at 70% at Government Effectiveness, it is better than 70% of the countries of the world. Thus a higher value in this category indicates better performance. Thus, a choice of indicators differs amongst actors and organisations. The broad based normative assumption for this kind of measurement is that a democratic government will be better equipped to implement the poverty reduction as well as growth policies. Thus, the good governance factors are increasingly regarded as basic requirement for inclusive and sustainable growth and the absence of these may induce higher inequality and degradation of basic human rights.

### ***Political Governance in South East Asia***

South East Asian countries differ greatly amongst themselves in history, culture and Governance systems. At various stages of development, the political process in these countries are also varied. Generally, Electoral system dictates the choice of ruling party

although a single party contest in general elections is common in many countries including Singapore.

The South Asian nations are fast becoming strong economic forces. Countries such as Malaysia, Thailand, Singapore are becoming important not only in Asia, but also in the world and policies undertaken are being emulated by other developing countries including those of Africa and South Asia. At the same time, developing countries such as Cambodia, Laos, Vietnam and Myanmar have been growing despite the recessionary world trends.

In order to acquire a comprehensive view of the growth and governance pattern in South East Asia, 5 countries are selected for detailed examination. The countries are at different levels of social and economic progress and provide a representative picture of South East Asia. Thus the countries chosen for analysis are Thailand, Malaysia, Cambodia, Philippines and Singapore.

#### *Objective of the paper*

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The paper would therefore seek to understand the growth trends in the 5 South East Asian countries and compare the existing governance indicators with the growth indicators. The paper will try to analyse the following primary question:

***“In the context of selected countries in South East Asia, what is the relation between growth and governance?”***

#### *Suggested Methodology of the paper*

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In order to analyse the relationship between growth and the governance system, the key factors studied are;

- a) the perception of governance as surveyed by the World Bank through 1996 to 2011, to get a clear indication of the national governance in reference to the world;
- b) the current level of decentralisation to understand the efficacy of local level governance; and
- c) public private partnership (PPP);

with the assumption that a diversified and widespread indicate stable and strong governance and regulatory framework. The Indicators for Governance efficiency will therefore be analysed against the economic indicators which consist of GDP growth rate, inflation rate and trade balance rate, in order to explore whether a relationship exists between them.

The research will be conducted through desk review and will consolidate primary survey data available on

- Growth and other economic indicators to be taken from the World Bank Database
- Governance indicators from the Worldwide Governance Indicators as calculated by the World Bank

- Social development indicators such as the Human Development Index, Gini Index and Corruption Perception Index is also utilised.

The research will also review the existing literature on sustainable economic growth, governance systems and institutions in South East Asia. The research will draw particularly on information available to multilateral institutions such as United Nations, the World Bank, Institute for Democracy and Electoral Assistance and other Non- Government Organisations.

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## GOVERNANCE AND GROWTH: CASE STUDY-THAILAND

### *Section 1: Background*

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Thailand, a country of geographic and strategic importance in South East Asia region has been experiencing political turmoil since the end of World War II, but has managed to retain itself as an important business hub. However, the political scenario has been less impressive. In 2007, elections were held and constitution revised under a bloodless military coup against the then president Takhsin Sinawatra. Amidst existing turmoil and the changing political scenario, there still continues a tradition of elections and Thailand elected its first woman prime minister in 2011. Yet, the elections have not eliminated the possibility of further political instability. Thailand is the only country in the sample which has been able to avoid



European Colonisation although the country was invaded by Japan during WWII. Thailand's earlier political history is marked by military coups. Absolute monarchy in Thailand was overthrown in 1932 and constitutional monarchy was established. General election in 1988 was followed by a military coup in 1991, the 2<sup>nd</sup> in 15 years.

Thailand is also of economic significance as it is one of the rising players in the ASEAN able to host production centres for large companies because of its relatively cheaper production costs. Thailand's growth rate in 2010 was 7.8% which made it the fastest growing economy of the South East Asian region in the same year. However the growth rate in the years preceding has been moderate, and according to OECD there is a distinct downward shift in the projected GDP growth rate for 2015 where Thailand falls considerably behind the growing nations in ASEAN, including Malaysia, Indonesia and Vietnam.

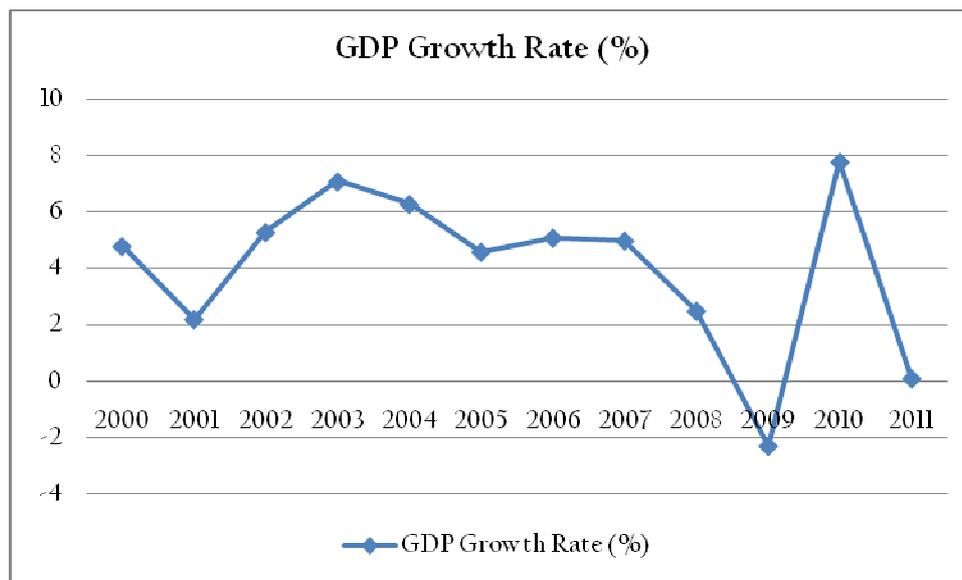
Socially, Thailand faces a major social challenge in the form of high HIV incidence. With a flourishing sex industry, Thailand has taken the lead in providing cheaper generic drugs for HIV/AIDS sufferers as well as conducting awareness campaigns. They have also been credited with a reducing the number of new infection.

In addition, the long and contentious historical relationship with neighbour Cambodia is being newly intensified on disputes regarding natural resources in the Gulf of Thailand.

## Section 2: Economic growth indicators

Thailand's 10<sup>th</sup> national economic and social development plan for the years 2007 to 2011 focused on balanced growth and sustainability which, in the 11<sup>th</sup> national plan refocuses slightly to include specific interventions on economic variables such as infrastructure and agriculture as well health, education and energy.

Traditionally measurements of economic growth takes account of the increase in GDP growth rate,, the current account balance a, inflation rate etc. As emphasised above, when comparing Thailand with many emerging countries in ASEAN Thailand's growth rate, although high in 2010, has already been revised downward in 2011 to 2.5%<sup>1</sup>, The Thailand GDP growth rate over the last decade is displayed below:



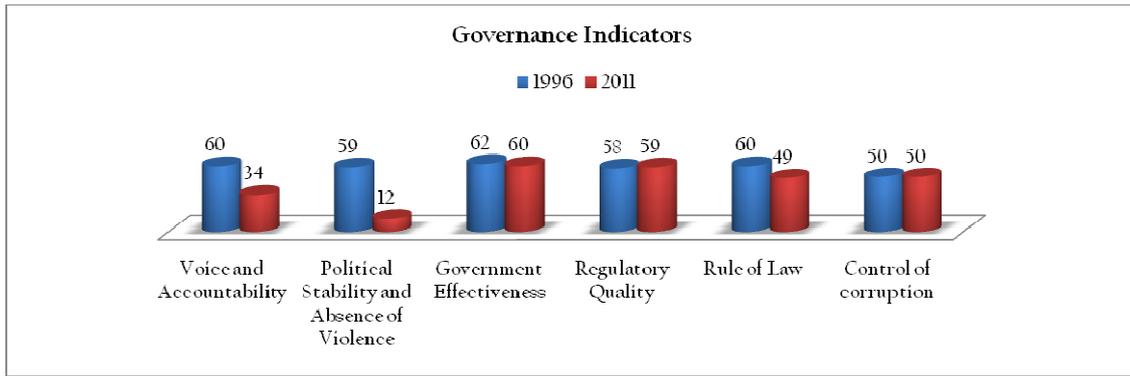
The oscillating curve shows that the growth rate in Thailand have changed frequently over the last decade. Thailand's growth has been a factor of short-term capital inflows. The inflows through bank account held by foreigners account for 23% of the total investment (Warr 2011), however, the international reserves continue to fall leading to Thailand's losing competitiveness in the world market. The falling growth rate in 2009 is attributed to the global financial crisis and Thailand's dependency on external market.

### *Section 3: Governance Indicators*

#### PERCEPTION OF GOVERNANCE

To what extent the governance system and the political instability leads to shortfall in growth can only be estimated, The World Bank Governance indicators calculations reveal some interesting trends on governance in Thailand. The chart below shows how Thailand was performed in global comparison . The details of each of the indicators are provided below:

<sup>1</sup>[http://www.keepeek.com/Digital-Asset-Management/oced/development/southeast-asian-economic-outlook-2011-12\\_9789264166882-en](http://www.keepeek.com/Digital-Asset-Management/oced/development/southeast-asian-economic-outlook-2011-12_9789264166882-en)



**Voice and accountability** has been gradually decreasing since 1996, with a fractional increase since 2006, and maybe as a result of the reoccurring military coup and regional separatist movements. In 2006 the Thai Constitution was reformed and elections were held in 2007. This might have prevented further decrease of this indicator.

The perception on **political stability and absence of violence** describes whether there is a likelihood of government destabilisation, and in this case there is a clear downward trend, especially during the second half of the decade. Whereas in 1996, Thailand stayed at around 60%, over the last decade the indicator moved down to 12%, which maybe a result of turbulent political transition over this period.

The quality in the **rule of law** is indicated by the decrease of 20% in the 15 years of data collection. Once again, Thailand experienced multiple events of political turmoil starting in 1996 when the Banharns government resigned on the face of corruption charges and multiple accusations of electoral fraud at a time when Thailand was plagued by the East Asian financial crisis. The brutal crackdown on the unrest in the southern part of Thailand during this time may also lead to degrading confidence on the rule of law.

The **effectiveness of the Government and regulatory quality** are the two indicators that have not experienced volatility in the time of the study, and may also explain why Thailand remains to be a destination for foreign investors. The first indicator describes the quality and the effectiveness of government services while the latter gives an indication of the open environment for carrying on economic activities, and thus also shows that indeed Thailand has more stable investment climate than the political history would suggest. It may be noted that in the last 15 years, there has not been a shift upward, which may be significant as competitive business environment is at the centre of Thailand's growth and it is imperative that it is able to maintain its position in the world market.

Although there has not been a clear downward trend the perception of **control of corruption** from 1996 to 2009 but it has fluctuated frequently in between. The lowest point was at 40% in 2008, which have increased steadily in 2009 most likely after reassurance of a constitutional reform. The Corruption Perception Index by Transparency International ranked Thailand at 80 in 2011 among 183 countries in the world, with a score of 3.4 in a scale of 0-10. This is a step down from the previous year where Thailand ranked 78<sup>th</sup> among 178 countries. (Li 2011)

### DECENTRALISATION IN THAILAND

The State Administration Act 1991 divides the administrative functioning into the central administration and the local administration, emphasising on local autonomy. Prior to the 1992 elections, decentralisation was a major electoral pledge and promised to bring about increased government accountability and flexibility.

Following the election, the Office of the National Decentralisation Committee was formed in order to ensure smooth transfer of services inter-governmentally. Yet, in terms of decentralisation of human resources and financial authority there have been necessarily no change in the way businesses are conducted and there exists no data on the actual progress on the decentralisation plan. Local authorities are only authorised to collect certain forms of taxes and which is again gradually declining from 11.1% in 2001 to 8.9% in 2006. In terms of recruitment, most officials are appointed centrally and are subject to the central government approval.

The slow rate of transfer of power to the local level is identified to be because of the incompetence of local level government officials, the lack of appropriate environment for intra-governmental cooperation but most importantly, the lack of legislative regulation that may guide the decentralisation process. In the absence of appropriate rules and regulations, the entire process of decentralisation becomes ineffective and incomplete. (JICA 2007)

### PUBLIC PRIVATE PARTNERSHIPS (PPP)

Public private ventures in Thailand are still largely government financed, lacking the infrastructure and legal backing necessary to promote an equal partnership between the private and public sectors. Although Thailand enjoys a steady rate of FDI flow, public investments are inadequate to provide the necessary services. The Thai government's prioritises balanced growth focusing on greater availability of public services and the fact that Thailand has experienced increased public debt emphasises the importance of greater financial involvement from the private sector.

There is an effort to build up a public private partnership framework in Thailand through the 1992 'Act Of Private Participation In The State Undertaking', but implementation is hindered by the fragmented bureaucracy. (Ashurst 2009)

The Thai government's plan on PPP is centred on the sectors of communication, transportation, logistics, electricity generation etc. In a paper on the future of PPP in Thailand, the government highlighted a number of sectors where there is private participation including power generation, telecommunication, lease development in parts contracts etc. (H.E. Mr. Chalongphob Susangarn 2007) However, these ventures constitute of providing operating service contracts to the private sector.

In spite of the effort to put a PPP framework in place, the legal backing to establish a strong foothill for effective partnership is missing; there is also lack of procedural institutionalisation which prevents the establishment of the preconditions for effective participation of the private sector in public services.

#### *Section 4: Reconciling Governance and Growth Indicators*

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The variable identified above compares the economic and the governance progress in Thailand over the last two decades. While it is clear that the Thai Government is prioritising sustainable economic growth, the political uncertainty and the unstable governments creates a barrier in enhancing infrastructure to induce further investment, especially from the private sector within the country.

The Rule of law system have not progressed over the last 15 years and it is accompanied by a transitioning and centralised government, with a level of corruption that has continued to worsen. Its fall in the CPI ranking adding further doubt to the effectiveness of the rule of law and control of corruption. Financial organisations such as Deloitte have opined that Thailand now ‘sits on a knife’s edge’ and the political instability must be reduced if growth rate is to increase.

The priority of the Thai Government is balanced growth, yet Thailand falls behind in the Human Development Index at 103 significantly below Singapore (26) and Malaysia (63), it suggests is unable to provide the facilities and services to create a sustainable development trend.

Although a direct correlation cannot be drawn without deeper analysis, it is seen that the Thailand growth pattern is extremely erratic during the recent years. The variables on perception on governance, the level of decentralisation and private sector participations shows that there is a lack of stability in the governance system, which coincides with the unstable growth trend in the country and indicates that a stable and effective governance system is likely to foster a more balanced and faster growth in the future.

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## **GOVERNANCE AND GROWTH: CASE STUDY-MALAYSIA**

### *Section 1: Background*

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Geographically and demographically one of the largest economies of South East Asia, Malaysia still has political and economic challenges to overcome and place itself as the leading player in world. Malaysia also shares some distinct geographic features with two parts of the country separated by around 640 miles by the South China Sea. It is a federation of 13 states shared by ethnic Malays (60%), Malaysians of Chinese descent (26%) and Indians and indigenous people. There is little racial integration while there have been no sustained racial conflict amongst the communities. (BBC 2011)



FIGURE 1 MAP OF MALAYSIA

Malaysia needs to constantly face the challenges of unifying and harmonising the ethnic Malays, the Chinese and the Indians. The country also faces more serious challenges politically, in ensuring participatory democracy in the face of religious differences and the ethnic wealth gap, and, environmentally, in preserving its valuable forests, considering the dependency of the Malaysian economy on its natural resources. Main export items of Malaysia includes Electronic equipment, petroleum and liquefied natural gas, chemicals, palm oil, wood and wood products, rubber, textiles (BBC 2011)

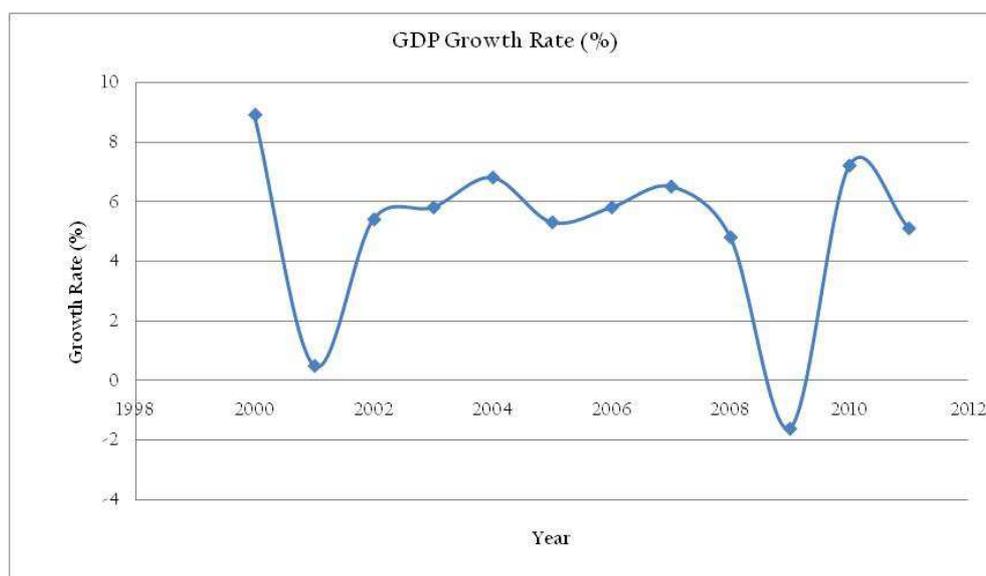
Malaysia gained independence from British colonial hold in 1957 and much of Malaysia's economic and political success to date has been attributed to leadership of Mahatir Mohammad who had been the Prime Minister from 1981 to 2003. He had been the long-term leader of the United Malays National Organization (UMNO)-led alliance, and had been able to uphold the rights of the Malays and tap into the business resources of the Chinese decent Malaysians, transforming the country into the economic powerhouse of today. Political uncertainty continued to brew following the discharge of Mr Anwar Ibrahim, the one-time supposed successor of Mahathir, from the Government. Anwar Ibrahim surfaced as the primary rival for the alliance since then. The National Front leading the alliance suffered its worst election results in 2008 and added to the political instability of the country. The arrest and the trail of leader of the opposition Anwar Ibrahim, on sexual conduct charges reflects the political tensions and the lack of adequate independence of the judiciary. Malaysia's human rights record has faced international criticism. (Datamonitor 2011). Internal security laws allow suspects to be detained without charge or trial and Malaysia following a dual

justice system (Secular and Sharia Laws) facing challenges in maintaining balance between these two.

Despite some elements of uncertainty in the political sphere, the country's economy grew at a steady rate. Amidst the global economic downturn, Malaysia faced a negative growth rate in 2009 but quickly bounced back in 2010.

### *Section 2: Economic growth indicators*

Malaysia has enjoyed a positive economic growth rate following a slump due to the Asian financial crisis in the late 1990s. Although 2009 saw the growth rate plummet to negative figures, over the last decade the GDP per capita has been increasing at a rate of approximately 616 USD a year. (Bank 2011) During the post global economic crisis phase, Malaysia recorded a growth rate of 7.2% facilitated by its strong export sector which rose by 24.2% in 2010. (Datamonitor 2011)



The New Economic Plan (NEP) advocated by the current government lays emphasis on economic growth through fostering a culture of creativity and innovation. These principles have also been outlined in 1Malaysia concept, New Economic Model and the Tenth Malaysia Plan. (The Economic Planning Unit 2010) as well as the vision 2020.

The NEP as well as the tenth Malaysia Plan 2011-2015 focuses on shifting the country to high income through focus on innovation and establishment of a knowledge infrastructure, private sector growth and fostering private consumption. The need for physical infrastructure development is also maintained, and a need for the development of Small and Medium Enterprises (SME's) for national and international trade, acquiring a high skilled labour force through higher education and training is a primary point of focus. (OECD 2011) Softer development focus also includes improvement of the tax regime. The 10th Malaysia Plan, an

expenditure plan covering 2011–15, will promote 12 national key economic areas including tourism, palm oil, and private healthcare. These initiatives are expected to have significant potential to boost overall economic growth and help transform Malaysia into a progressive nation. (Datamonitor 2011)

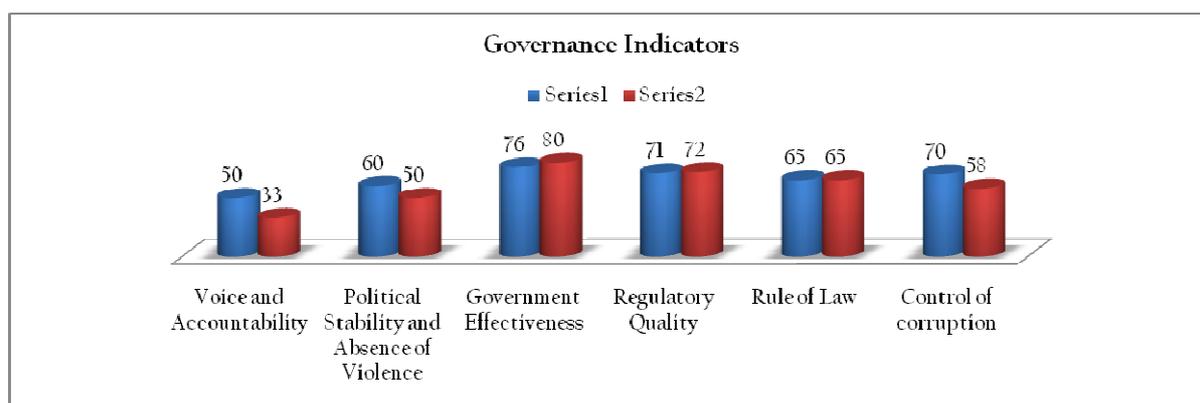
It may be noted that Malaysia, while emphasising the need for innovation and high skilled labour force, is also known for its highly protective industrialisation policy. Share of subsidies with regard to total operating expenditure has been consistently high. (OECD 2011) Protectionist policies, combined with high regulatory requirement for foreign companies due to the affirmative action for Bumiputras (ethnic Malays) restricted foreign investments in many sectors in spite of the generally favourable standing in the World Bank doing business indicators where Malaysia rose 5 steps to 18 in the world.

Thus, as the chart above reflects, being a trade dependent economy, Malaysia is invariably affected by the global economic changes, but has the strength of the domestic market to revive its growth rate. Overall Malaysia is enjoying a steady rate of the growth in its per capita GDP despite some of its political and electoral fluctuations.

### Section 3: Governance Indicators

#### PERCEPTION OF GOVERNANCE

As the above figure shows, the public perception on Governance in Malaysia, as reported by World Bank, some of the indicators have remained fairly stable over the last decade while a number of them have declined by more than 10 points. Detailed analyses of the trends are as follows:



Taking on world banks indicators on Governance, the most striking change noticed is in the **voice and accountability** indicator. Since 1996, the voice and accountability indicator have steeply declined. Starting off low at 50%, in 2011 the indicator stands at only 33%, with some minimal incline during 2005/2006 which again declines during the years leading up to 2011. This may also indicate rights to free speech and demand for political reforms ensuring that have gained a greater level of importance. In 2011, after the use of tear gas and water cannons on an electoral reform rally, a parliamentary standing committee was formed to study electoral reforms (BBC 2011). As of July 2012, a plan to review and repeal the existing

Sedition Act is undertaken (Kevin Drew 2012) Thus, given the tradition of low political dialogue, it is yet to be seen how the steps taken contributes to improving Malaysia's performance on Voice and Accountability in the future.

In comparison to the time of Mahathir Mohammad, there has been a sharp decline in the perception on **political stability and absence of violence** indicator. Dropping from 65 in 1996 to 50 in 2011, this indicator was particularly low in 1998 and 2009, at around 40%. This may correspond to the uncertainty created in the political field in Malaysia when Mahathir Mohammad had sacked his presumed successor Mr Anwar Ibrahim on charges of misconduct. 2008 was the year of election which saw a watershed result for the National Coalition followed by the arrest of Mr Anwar Ibrahim (BBC 2011). Overall the political stability indicator is highly unstable and changes closely with the dynamics between the government and the opposition parties.

**Government effectiveness** measures quality of public service and the quality of civil service and has consistently seen a stable and slowly inclining trend. From 1996 to 2011, it has risen from 76% to 80%. Although the rise in this indicator is very steady, overall, it never drops below 75% in any of the years surveyed. This indicates that despite the political turmoil, the Government institutions are stable and strong enough to carry out their regular functions and enable their citizens to continue with uninterrupted lives. In fact, Malaysia boasts one of the strongest infrastructures in Asia as well as a public transport and housing system.

Despite the government's declared commitment to encouraging private sector enterprises, there has not been a noticeable or drastic change in the **regulatory quality** indicator, which improved just 1% in the last decade. Regulatory quality measures the government's ability to formulate and implement sound policies and regulations that permit and promote private sector development. Although relatively high, this is an indicator which reflects that the decentralisation and private sector policies, as outlined in the New Economic Plan and the Tenth Malaysian plan have yet to lead to creation of an effective business environment. The existing affirmative action for the native Malays (BhumiPutras) also leads to a restricted environment for investments, especially FDIs.

Similar to regulatory quality, the **rule of law** indicator has also remained largely unchanged, with slight fluctuations between 2002 and 2005. Yet, it may be noted here, the indicator reveals that the majority of the surveyed perceive that the Malaysian government is governed by the rule of law and confidence on the government's non-interference remains the same despite the changes in the political scenario.

Dropping nearly eight percentage points from 1996 to 2011, the **control of corruption** indicator clearly reflects the lack the Government's ability in managing corruption in the country. The decline over the years has been relatively steady, and also coordinates with rising inequality in the society. The Gini Index shows a rise of 9 points from 37.9 in 2004 to 46.2 in 2009, indicating the prevalence of corruption at the highest levels of business and the government.

The ruling government has been accused of lack of transparency in public procurement in areas ranging from agriculture to defence, resulting in scandals such as the RM250 million National Feedlot Centre that failed to cut the country's beef imports and the multibillion ringgit spent on buying submarines and naval patrol boats. (The Malaysian Insider 2012)

Malaysia's comprehensive anti-corruption system, a core component of the current Prime Minister Najib's governmental and economic reform program, tries to address these criticisms through the establishment of the independent Malaysian Anti-Corruption Agency (MACC), however the ability of the MACC to function objectively and independently is yet to be seen

In addition to the indicators mentioned above, factors such as decentralisation and Private public partnership also help to provide an indication of the stability of the Government, its institutions and the maturity of its policy making abilities. A brief analysis of these factors also helps to reveal the possible sustainability of the strong growth trends as experienced in Malaysia

#### DECENTRALISATION IN MALAYSIA

Decentralisation is integrally related to efficient public service delivery, Malaysia can still be considered to be a largely centralised state that has a centrally governed public transport system and the public housing system under the Prime Ministers Department. State Governments have heavy dependence on federal funding. It is reported that a state such as Penang (Malaysia's second state) has the financial authority of RM740, which is less than the budget of its main university. In the three levels of Governments of Malaysia, in accordance with Article 111 of the federal constitution, state governments are prohibited from borrowing without federal approval. (Zohari 2012) These existing regulations are a major impediment to financial and political independence of state decision making. This also helps to re-establish the control of the federal government over the states. (Nooi May 2008)

Government weakness in monitoring of service delivery quality, the lack of state level independence has come up as sources of contention and the complaints bureau of the Prime Minister's Office had received notification of ill-mannered services. Local Governments have come under criticisms on delay and weak enforcements and the top-down centralised power structure has been attributing to the lack of improvement in efficiency. In addition, with the local government election being held and states being ruled by federal opposition parties, the problem of centralisation becomes more acute. (Sim 2012)

Steps undertaken to improve these situations have included a survey by the Administrative Modernisation and Management Planning Unit (MAMPU) on improving service delivery. At the same time, the new economic policy delineated various actions such as privatisation in order to fulfil administrative reform measures. (Hussai and Brahim 2006) However, it needs to be mentioned that decentralisation by providing a higher level of financial and political freedom to the local government does not come up to be a primary focus for the government at this point.

#### PUBLIC PRIVATE PARTNERSHIPS (PPP)

PPP has received considerable focus from the Government as a way of reducing corruption, improving transparency and financial support. (Public-Private Partnership Unit, Prime Minister Department, Malaysia 2009)

PPP arrangements is preferred to traditional arrangements, especially to facilitate start-up finances and procurement through the private sector while the Government can share costs of long-term maintenance, benefiting both the parties. (Huong 2012) Similar prospects are also outlined in the Economic Transformation Program (ETP) where the plan is to attract and channel \$444 billion in private investments (Shmavonian 2012). Steps undertaken in this regards has been the move to eliminate half of the 761 varieties of licences currently required for most business startups. (Bernama 2012)

However, PPP is mainly to be used in large infrastructure projects such as tolled roads, power plants, ports, airports and urban transportation (Huong 2012) while savings out of PPP may be utilised to fund social services project such as health, education and housing. The PPP is led by the PPP Unit under the Prime Ministers Department, however, beyond state of planning and identification of appropriate sectors, PPP in Malaysia is at an elementary level and needs further focus and discussion to be a ful-fledged government policy.

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#### *Section 4: Reconciling Governance and Growth Indicators*

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In spite of the decline in the freedom of expression and political stability indicators, more institutional factors such as the regulatory quality and Government effectiveness put Malaysia in a strong position within Asia and globally. That the government is deemed effective despite the lack of voice and accountability can explain the steady rate of growth that Malaysia has been experiencing because Malaysia has certain institutional abilities to foster economic growth.

The Governments primary focus is clearly on economic growth and the government outlines a generally comprehensive outlook on achieving growth based on innovation, entrepreneurship and high-skilled labour force. However, simultaneously, inequality is growing at a steep rate and may prove to be a barrier in achieving balanced and sustainable growth. Political opposition and civil demand for a more transparent and open government is a reality in Malaysia now and steps to address these challenges are already being undertaken. High perception of corruption might add to the existing political uncertainties and prove detrimental to achieving the economic success that Malaysia is aiming for.

Yet, amidst such criticisms the perception on the rule of law indicator shows a slow but gradual transformation to an acceptable electoral democracy. The lack of homogeneity in the Malaysian society presents a challenge and positive discriminatory policies for ethnic Malays come on the way of growth based on competition, industrialisation and innovation.

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## GOVERNANCE AND GROWTH: CASE STUDY-CAMBODIA

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### *Section 1: Background*

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Modern Cambodia is defined by its long history of conflict, both within itself and with its neighbours, as well as its dichotomised relationship with its colonial ruler and the resulting changes in its political scenario. Present day Cambodia is marked by its recent disputes and ongoing war crime trial against the Khmer Rouge, whose armed revolutionary stance destroyed the economic possibilities of the country at the time. Much of Cambodia's predicament has been caused due to its location as numerous attempts were made by the Thai and the Vietnamese to conquer the kingdom of the Khmer people.



The French protectorate in Cambodia was established in retaliation to the threats from its neighbours and had been regarded as the only way to save the kingdom at the time. Although the French rulers had maintained the traditional way of life in Cambodia, it failed to develop the country socially and this has been attributed to the later tragedies that had befallen Cambodia. The French protectorate was regarded as an euphemism, as it is widely acknowledged that the French governor generals administered Indochina as a colonial unit from Hanoi and left after the peace conference was brokered in Geneva after the WWII as they faced tremendous anti colonial movements in the region. (Tully

2005)

Reeling from the invasion ridden history of the 17<sup>th</sup> and 18<sup>th</sup> century due and the aftereffects of the French protectorate, Cambodia saw the beginning of a new dark age with the hostile undertaking of the Khmer Rouge in one of the worst genocides in history of the modern world.

The occupation of the Khmer Rouge left a long lasting scar that Cambodia is still mending, and its history during this period defines much of its existence now. The Khmer Rouge coup in 1975 forced Cambodians to move into the rural areas and subsistence farming and have executed millions during a period regarded as the darkest in Cambodia's history. Cambodia's emergence from the period is once again integrally linked to the fate of its neighbor, namely Vietnam and the US occupation in Vietnam.

Following an orchestrated peace accord in 1991, the first democratic elections in the country was held in 1993 under the strict supervision of the UNTAC (United Nations Transitional Authority in Cambodia). The elections were narrowly won by the royalist 'National United Front for an Independent, Neutral, Peaceful and Cooperative Cambodia' (FUNCINPEC), who formed a coalition government with the Cambodian People's Party (CPP). (Foreign and Commonwealth Office 2012)

This first coalition government ended in 1997 following armed clashes between the forces loyal to Hun Sen, the former Prime Minister, and Prince Ranariddh, the then Prime Minister and the former re-asserted his political dominance. (AANZFTA 2012) However, despite the

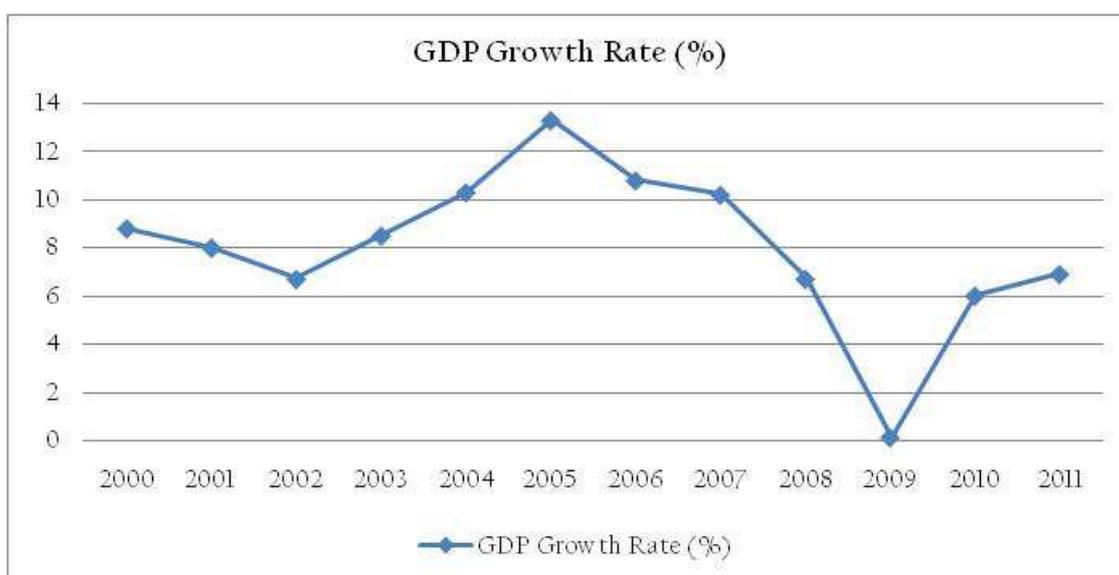
disputes within the Government, a culture of general elections in Cambodia had been established.

Known for its vast forests and rich natural resources, Cambodia's rural population drives much of their survival. Livelihood in rural areas depends on subsistence farming, logging and fishing. Cattle raising has also been a major source of asset for households. (Forum Syd 2009)

In terms of Human Development Index (HDI), Cambodia is still behind Laos and Thailand and more than 10 percentage points below the average of other countries in the Asia and Pacific, the HDI further decreases when controlling for inequality where Cambodia is .38 and rest of Asia Pacific is .528. (UNDP 2011)

### *Section 2: Economic growth indicators*

As a low income country with 30% of the population below the poverty line, much of the Cambodian national development strategy focuses on the achievement of the Millennium Development Goals. There have been some significant progress made in MDG achievement, especially in reducing under-five mortality, the prevalence of HIV/AIDS. Cambodia has also been able to decrease the number of mine casualties, a goal which was specified to Cambodia. Yet, the high level of maternal mortality is an ongoing challenge and so is the high rate of school drop-outs. (UNDP 2010) The World Bank's estimates suggest that Cambodia has achieved the Millennium Development Goal (MDG) of halving poverty by 2009. However, despite this remarkable progress, rural poverty remains a challenge, with 92 percent of the poor residing in the country side.



The Cambodian development plan, the National Strategic Development Plan (NSDP) Update (2009-2013) outlines growth, employment, equity and efficiency (Rectangular Strategy Phase II) as the primary focus of the Government and provides additional emphasis on the

achievement of the Millennium development goals. With very recent history of conflict, development plans consist of building social stabilisation and relationship within and outside, and is undertaken through the Governments ‘Triangle strategy’ focused on building peace, integrating Cambodia into the world and economic and social development.

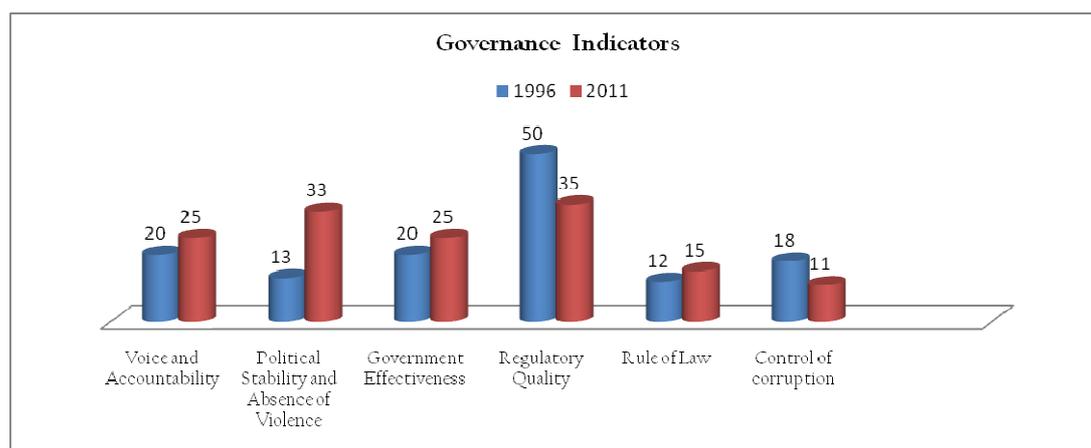
The NSDP dictates good governance as its central focus, aided by the four pillars of rectangular strategy including agricultural sector strengthening, private sector development and employment creation, human resources and physical infrastructure development.

As the chart reflects, over the last 10 years, Cambodia has been experiencing a high rate of growth averaging at around 8%. The economy took a heavy toll during the global economic downturn due to the narrow economic base dependent on garment, construction and tourism. The economic upturn in Cambodia is attributed to the flow of foreign direct investment which began in 2000, and the growth of the economy was fuelled by the expansion of garments and tourism sectors. The argument is now diversifying Cambodia’s export base to include sectors such as agribusiness, mineral and oil extraction in order to expand infrastructure and cheap energy generation. (Heder 2011) Thus, Cambodia’s management of its environmental resources, including its forests, will prove crucial in the long term development of Cambodia.

### *Section 3: Governance Indicators*

#### PERCEPTION OF GOVERNANCE

As mentioned previously, good governance is at the centre of Cambodia’s official development strategy, where the government has pledged to place special focus on public administration reform, armed forces reform, corruption and judicial reform. Yet, being a post conflict developing country with high level of poverty and inequality the Governance indicators of Cambodia provide a realistic picture of the country’s political scenario.



In Cambodia’s case, there have been some distinct ups and downs in relation to the governance indicators although it needs to be mentioned that many of components indicate that very low level of overall confidence of the Government as a whole.

**Voice and Accountability** indicator has increased 5% points since 1996, indicating very little development in this regard. 1993 saw the first internationally recognised election taking place in Cambodia, however the general election which followed in 2004 was heavily criticised by the European Union. Yet, the first multi-party local election held in 2002 has been reported to have increased the political participation of the rural citizens and has been said to have developed the legal and policy framework for local development (Gavin Tritt 2012) This is of further importance as nearly 80% of Cambodia's population live in the rural areas.

Over the last decade, the indicators may refer to the decrease in violence and increase in political stability in Cambodia. The indicator on **Political Stability and Absence of Violence** has increased around 20% points over the last decade, and marks that the country has moved a long way from the volatile days of the 80s and early 90s. The regular general elections, however disputed have been able to bring the long awaited stability into the lives of the Cambodians although there are existing tensions and conflicts in the achievement of individual and social rights.

Although political stability has increased significantly in ranking, it has not been accompanied by similar upturn of the **Government Effectiveness** Indicator. Unlike countries such as Malaysia and Singapore, Cambodia does not yet boast national housing policies (Bunnarith 2004), however, in line with its decentralisation policies, Special Operating Agencies in the Ministries of Health and Labour are established as autonomous local management units in order to improve service delivery and accountability. (OECD, SIDA, DFID, Irish Aid, Orxford Policy Management Ltd. 2011)

The **Rule of Law** indicator has also slightly increased by 3% points in the last decade, showing lack of faith in the judiciary and the institutions providing security and protection. Improvement in the rule of law situation has been a major focus of the aid agencies in Cambodia, however strong censorship is maintained with regards to the print and electronic media as well as NGO activities, which require prior approval. More importantly unapproved public demonstrations have been subject to state-level forces and leads to the restriction of free and democratic practises. At the same time, land grabbing by the powerful remains a major issue debate and dispute within all sectors of the society (Asian Legal Resource Centre 2007)

The **Control of Corruption** Indicator is the only one that has decreased further over the last 10 years. Starting off at a low level in 2006, the indicator has moved down further to 11% in 2011 displaying an absolute lack of corruption control by the Cambodian Government. In fact, in the Doing Business Survey conducted by the World Bank, corruption has been listed as the number one problem faced by the foreign investors in the country, followed by political instability.

Cambodia ranked 164 out of the 183 countries surveyed by the Transparency International Corruption Perception Index where 84% of the surveyed population has reported to paying a bribe. (Transparency International 2011) Corruption has also been acknowledged by the

Government as a major concern and has been included as a key reform agenda in the Rectangular Strategy and an Anti-Corruption Unit as well as an Anti-Corruption Law has been formed in this regard, but the success of the government initiatives is yet to be seen.

#### DECENTRALISATION IN CAMBODIA

As mentioned previously, the local elections which took place in 2009 opened new opportunities for decentralised development in Cambodia. The post-1993 period also saw a Provincial Budget Law being formulated such that the communes could enjoy a level of financial independence. Cambodia local government structure is broadly defined as communes and municipalities which are further divided into khans and districts. The smallest geographic areas in Cambodia are the villages. Yet the overall decentralisation process is administered by the Ministry of Interior whereas the financial decentralisation is conducted through a Public Finance Reform programme under the Ministry of Economy and Finance. At the same time, The Ministry of Planning leads the commune planning processes and the Ministry of Rural development leads the infrastructure development. The above mentioned provincial budget law provides limited independence in terms of tax expenditure and revenue collection and tax bases, rates and collection procedures are fixed by the centre.

Although a comprehensive decentralised law known as the Law of Administrative Management, Capital and Provinces, has been passed, to what extent the core decision making processes has been decentralised remains unclear. It is also maintained that the creation of the law has been political motivated to gain control of the local administrative bodies.

It has also been argued that decentralisation in terms empowering the local authorities might be inherently at war with the traditional communal values and culture of the Khmer society, where a hierarchal decision making system is respected. Thus, the decentralisation process needs to surpass the internally driven ideas and build a framework that 'restores mutual trust between the public and the local authorities'. (Rotha and Vannarith 2008)

#### PUBLIC PRIVATE PARTNERSHIPS (PPP)

In relation to developing economies such as that of Cambodia's, PPP may be of more importance as it may reduce the financial and operational burden on the already financially weak Government. Nevertheless, Cambodia is yet to embark on a holistic strategy to initiate public private partnership and thus a legal framework in this regard is yet to be established. Physical infrastructure has been prioritised in the NSDP and has been regarded as a core sector where development is required for the overall growth of the economy.

As of 2011, PPP in Cambodia has been implemented in sectors such as Power, Water, Solid Waste management, Airports and Railways. (ADB). The railways sector has also been listed by NSDP as a potential area where full-fledged PPP system can be developed however, no concrete strategy have been emphasised on. According to the Asian Development Bank, in addition to the ongoing PPP projects, there is a large potential in Cambodia to raise PPP funds, although a proactive government preparation and competitive funding structure is

required. Until now, there is no indication of any PPP initiation in social sectors such as health or education and ADB believes that the current PPPs are completed on an ad hoc basis rather than being visualised as part of an elaborate and comprehensive growth strategy.

#### *Section 4: Reconciling Governance and Growth Indicators*

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Largely leaving the scars of the recent genocide behind, Cambodia is slowly but deliberately progressing toward improving its economic and social condition.

In the first rectangular strategy promulgated in 2004, Cambodian Government highlights good governance as a prerequisite to sustainable growth and tries to address the same challenge again in the updated version. This is further elaborated in the updated rectangular strategy, yet in terms of Governance Indicators, the data in Cambodia clearly reflects the challenges it faces. Although, it has enjoyed a high growth rate and has been able to bounce back quickly after the 2009 global financial Cambodia still suffers from the basic lack of citizens role in the society. Decentralisation initiatives have just begun, and PPP initiatives are still at a nascent stage.

Although growth rate is high, HDI reveal that social progress or overall framework for sustainable progress is not yet built. At the same time, the share of agriculture in the GDP is increasing while the share of industry in the GDP has reduced, (Royal Government of Cambodia 2010) which is in stark contrast to the growth path of developed countries where industrialisation has been a driving force for growth. A high level of corruption presents a barrier for the creation of a sustainable investment climate and is reflected through a low ranking in the World Bank Doing Business indicator 2011 where Cambodia ranks 147.

Thus, the high growth rates of recent years are not corroborated by improvements in other indicators, including the social ones depicting a lack of overall confidence in the economy as well as the politics and casts doubt on the nature and sustainability on the type and rate of growth in the country.

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## GOVERNANCE AND GROWTH: CASE STUDY-PHILIPPINES

### *Section 1: Background*

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'While The Philippines is not a poor country but nevertheless it is a country with a lot of poor people' expresses the current European Union Country Strategy for the Philippines and gives a clear picture of the country's questionable growth pattern. Once thought of as the next rising star of Asia and rich in natural resources, Philippines have always fallen short of achieving the growth and development that would establish them as a prominent player among the ASEAN countries.

The Philippines is an archipelago of 7000 islands, however life is centred mainly around the 11 larger islands amongst them. It began its struggle for independence against the Spanish stronghold in the region since the 16<sup>th</sup> Century and this ultimately also gave rise to a long partnership with the United States who had the advantage of locating a military base in the country for some time.



Similar to many countries with multiple colonial pasts, the Philippines independence was followed by a time of instability and uncertainty. Martial law was declared for a brief period of time in 1972 by the then elected President Marcos who was ultimately ousted in 1986 through a non-violent mass revolution known as the People Power Revolution. President Aquino succeeded Marcos but was assassinated in 1983. Nevertheless, she was able to introduce a new constitution and a culture of democratic practises. However, her tenure experienced a number of attempted coups. Philippines was marked by continuing communist guerrilla campaigns and pro-independence movement in parts of the country. (British Foreign and Commonwealth Office 2012)

Thus, political disturbance was never far apart in the Philippines and each government's tenure is marked by coup attempts and revolutions where leaders

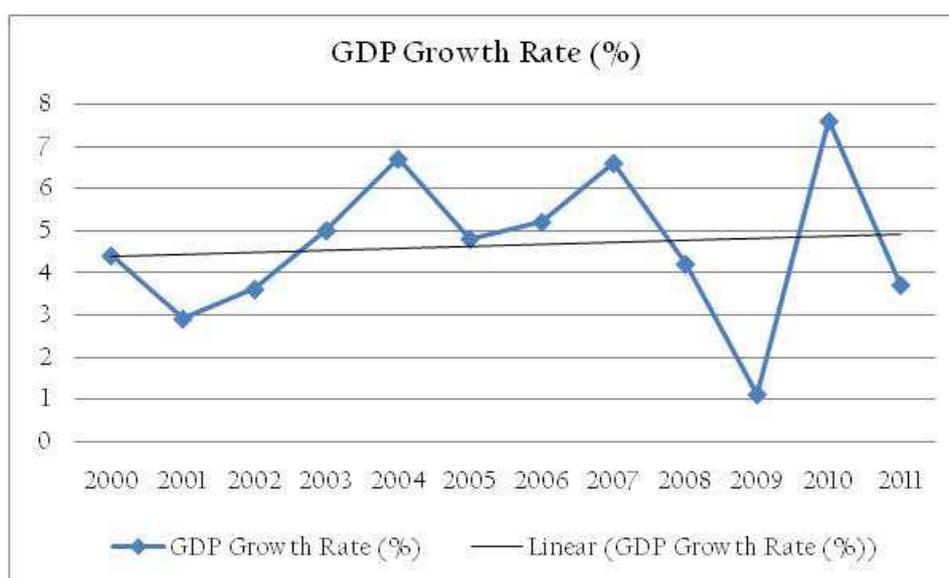
continued to garner a reputation of being incompetent and corrupted. The previous president Gloria Macapagal Arroyo is currently charged on corruption and on exerting undue influence of the judiciary as well as election fraud. She is being charged by Benigno "Noynoy" Aquino III, son of the late former President Cory Aquino, who won and the current presidency. The Current president meanwhile has also been accused of electoral fraud and the validity of the government needed to be endorsed by the supreme court. (European Commission 2006)

In addition to alleged communist guerilla campaign, a number of Islamist groups exist in the Philippines, and while the security forces have vowed to crack down on the radical Abu

Sayyaf, peace negotiations are attempted with groups such as the Moro Islamic Liberation Front as well as the pro-communist National People's Army (NPA). In general the Philippines is a largely Catholic country and a substantial challenge for the government is reducing the birth rate. It is estimated that the 2011 population of 94.8 m is likely to double in thirty years.

### *Section 2: Economic growth indicators*

The World Bank identifies the Philippines as a lower middle income country, with a current per capita income of USD 2,370 (not adjusted to purchasing power parity), over the last decade, Philippines have experienced an average growth rate of 4-5%, which even in comparison to lower income countries such as Cambodia, gives an indication of the challenges that Philippines have faced in achieving high and sustained growth.



The Philippines has experienced a slow but consistent growth in the early 2000s which came to a crushing 1% in 2009 due to the global financial crisis, an important consideration for the remittance income of the Philippine economy. However, the economy is more closely reliant on its services sector including the banking and non-banking financial services. The services sector contributes to about 43.4% of the GDP. Its rich mineral and energy sources have established it as one of the 10 largest producers of gold, copper and bromite. (PWC 2010) Yet, the Philippines, which had once been self sufficient in rice production is currently the largest importer of rice. (Mangubat 2011)

In terms of growth rate, the first quarter of 2012 however has been promising for the Philippines and indicated that the economy has the ability to absorb external shocks quickly and foreign investors are showing increasing interest in the economy, especially in the mining sector. (BBC 2012)

The Philippines Development Plan 2011-2016 recognises that the aim for the nation is to foster inclusive growth and likewise outlines measures for human development and physical

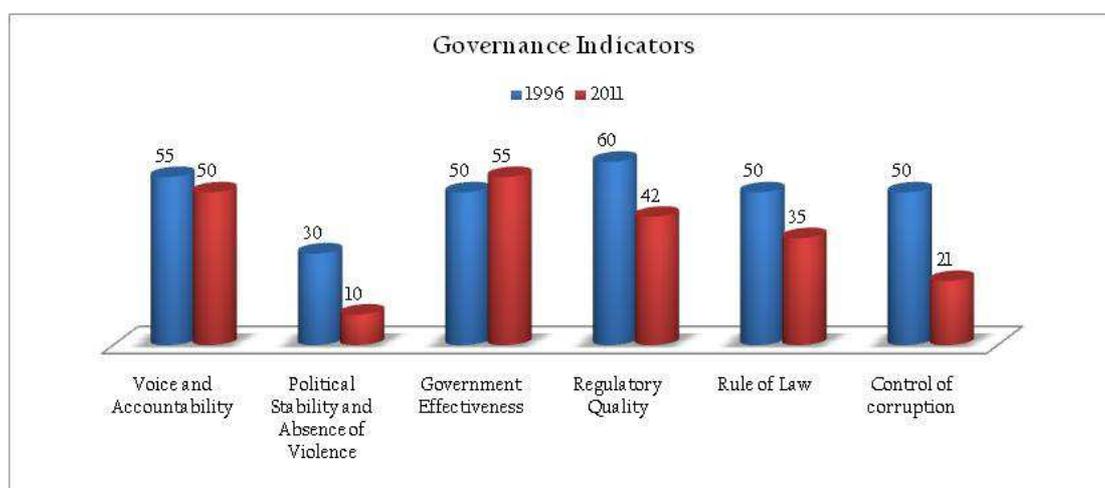
infrastructure development. Good governance is also being regarded as a pillar for successful and inclusive growth, however there is a distinct lack of focus on the specific methods of natural resources management.

In terms of investment inflows, infant industry protectionism has always been regarded as somewhat contradictory to a general open market policies favoured in Philippines. During the time of the legislation of the Board of Investment, a 60-40 Filipino-to-foreign equity rule was thought to have limited the role of FDI in developing the national industries, (Sicat 2012) and might have attributed to the non-competitiveness of the Philippine economy in reference to many ASEAN countries, namely Malaysia, Singapore and even Indonesia which ranks 46<sup>th</sup> while the Philippines rank 75<sup>th</sup> in the World Economic Forums Global Competitiveness report in 2011/2012. (Mangubat 2011)

### Section 3: Governance Indicators

#### PERCEPTION OF GOVERNANCE

The Philippines once again epitomises the downfall of an economy from a relatively well established position of governance, with all the indicators decreasing from their earlier stages, some drastically.



The **Voice and Accountability** indicator on the contrary has decreased by 5% in global comparison, indicating the current state of compromise in between the existing political leaders in the country, where amidst the widespread accusation of electoral fraud, a culture of general elections have still been established. The last general election in 2010 was accepted by the international community to be reasonably fair due to the use of new electoral technology, (ANFREL 2010) however the constant threat of coups and a brief period of emergency during 2006 reflect the lack of an existing culture of an accountable government. At the same time, much of the period included in the survey was during the authority of Joseph Estrada and Gloria Arroyo, both of whom have been nationally accused of large scale corruption marked by a gross lack of accountability to the public. The media is also known to be control by political interests and as the BBC reports, violence against media workers is

persistent. In late 2009, gunmen massacred 57 people, including 30 journalists, in a politically-motivated attack in the south. (BBC 2012)

**Political stability and absence of violence** decreased by 20 points in a period where many countries of the world were emerging from their conflict ridden status marks the constant uncertainty and a continued existence of a lack of democratic culture in the country. Following the peoples power revolution in 1986, street protests again broke out in 2001 to force the then president Joseph Estrada out of office. The presidency of Gloria Arroyo was also fraught with allegations of corruption and scandals without much improvement in the development indicators such as poverty levels. (Mangubat 2011)

**Government effectiveness** has improved 5 points in the last decade, to 50 and is the only indicator which has improved in global comparison, although marginally. Public service delivery system in Philippines still faces numerous challenges. The Government does not provide a mass transit system, and transportation generally consists of a privately run system consisting of an array of vehicles. A national health insurance system is in existence and has been incrementally increasing. The 2010 health sector reform strategy, aims for greater coverage especially amongst the poor, but currently continues to results if high levels of out of pocket payments, (World Health Organization 2011) while private sector health care remains costly. Over the last 20 years, progress has also been made in the housing policy for the poor, where a more participatory approach is being undertaken in order to ensure more efficiency in housing provision. Yet, acute housing shortage remains and supply falls short by more than one million units. (Marife Ballesteros 2010) Thus, whether or not the trend of increased government effectiveness continues it yet to be seen since the current government by Aquino has attracted criticism of having a weak government and ‘easy-going’ work ethics (Mangubat 2011)

**Regulatory quality** has decreased 18 points in the last decade amidst the numerous attempts by the government to streamline its development policies and create an environment for businesses to flourish. Over the past two years, 13 out of 20 cities in the Philippines carried out 19 regulatory reforms to make it easier to start and operate a business. However, challenges remain in simplifying the requirements and obtaining the required permits for construction. For example, obtaining a construction permit in Manila takes 169 days. (The World Bank 2010) As mentioned earlier, there is a restriction on foreign investments as well as regulatory capture which has inhibited business growth. (Government of Philippines, United States Government 2011)

**Rule of Law** has also decreased 15 points over a time period where the economy was moving through a political transition from a period of emergency to electoral democracy. Emergency rule indicates the government’s influence over the judiciary and security agencies. The period has also been marked by multiple impeachment proceedings against former heads of states and a deterioration of the overall security situation in the country.

In addition to factors such as terrorist bombings, there is consistent report of state run atrocities against the activist peasants in various parts of the country, which is particularly

relevant for an agrarian society such as the rural Philippines. The disputes have been related to tenancy and land seizures all throughout the 80s. At the same time, during 2008 an agreement with MILF rebels on the expansion of a Muslim autonomous region in the south was negotiated but the deal later on failed to materialise. (BBC 2012)

**Control of corruption** index fell 29 points during the period surveyed although Philippine's position in the corruption perception index slightly increased in 2011 from 2010. In 2011, Philippines ranked 129<sup>th</sup> among 183 countries surveyed by Transparency International. The survey, which was conducted from December 2009 to September 2011, covers two administrations, the latter part of the Arroyo administration and the early part of the Aquino administration. (Horario 2011)

The current government has won elections on the mandate of eradicating corruption; however governments after governments have been accused of corruption in various forms including catering to special interest groups. Unofficially, it is estimated that corruption costs in infrastructure projects can be up to 30% of the total cost (Angeles 1999) which indicates the vastness and pervasiveness of the corruption phenomenon in Philippines. The former Chief of the Anti-corruption unit has been voted by the government to be impeached on corruption charges (BBC 2011). Thus, despite the apparent attempts of the current government to curb corruption, steps still need to prove effectiveness in the long and short term.

#### DECENTRALISATION IN THE PHILIPPINES

The Local Government Code enacted in 1991 has been called a landmark decentralisation step for the Philippines, and it is noted that local government units have a generally greater level of flexibility and independence than many of countries considered in this report. Local government units have been entrusted are among others with, land use planning, community based forestry, solid waste management, social welfare service, local infrastructure, municipal service amongst others. Fiscal transfers through 40% internally generated taxes allocated to local government, active participation of Non-Government organization in local governance is also an innovative approach which Philippines have undertaken (Llanto 2009)

Yet, surveys to assess citizen satisfaction on public services have given mixed results of local governance performance. Understandably, a number of units have emerged as well performing, more accountable and more transparent; it is found that constraints remain in the 'key resource management systems and procedures processes, such as planning, budgeting, procurement, and financial and human resource management'. More effort is required in the abilities of the local government units to earn revenues and manage their own resources. Administrative capacity of the local government could be further improved in order to ensure the effective use of resources and reduce overlapping functions of the various local government units (ADB 2005)

#### PUBLIC PRIVATE PARTNERSHIPS (PPP)

The Philippines have been a front runner in the initiation of PPP ventures in the region. The PPP centre was established in 2010 in order to facilitate the initiatives that maybe taken. The

Economic Intelligence Unit has reported in 2011, Infrascope Study that in terms of readiness and capacity for PPP, Philippines has ranked high and can be regarded as a forerunner. Among the ASEAN countries, Philippines ranks highest in offering an ideal environment for PPP. The legal framework for PPP in the Philippines is established and a bidding process that facilitates private sector investment in this area. Projects in PPP ranges from building schools to prisons to airports, and the Government aims to solidify the PPP initiatives in the future. In 2012, 21 projects have been identified for implementation ( Manila Bulletin 2012)

The Philippines also boasts committed resource allocation for PPP through the 'PPP strategic support fund' which has recently earmarked an additional 3 billion Philippine Peso through a national budget circular. Yet, P 1.497 billion is allocated for government's priority and social economic projects. Thus, The Philippines have already somewhat progressed toward institutionalising the PPP initiatives in the country in spite of the rampant corruption allegations against the government. (Manila Bulletin 2012)

#### *Section 4: Reconciling Governance and Growth Indicators*

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In the case of the Philippines, the current policy makers and their international donors, including the European Commission, the United Nations and USAID, agree that the good governance indicators including the lack of political stability and prevalence of corruption etc, present major challenges in achieving the growth potential of the country, in spite of formulating some sound policies.

With an average growth rate of 4.65% over the last decade, the Philippines growth rate does surpass the global growth rate of 3.8% for the same period of time, but still falls short of reaching its desired rate of growth given its strong overseas labour force and rich natural resources.

The Philippines scores .644 in the Human Development Index, in the medium human development category, and ranks 112 among 187 countries, thus in terms of HDI, Philippines is still within the lower 50%. With an inequality rate of 44%, its Gini index places Philippines behind Malaysia and Thailand. (Journal Online 2011)

It is also notable that while growth failed to accelerate, the good governance indicators have largely regressed putting Philippines amongst the bottom half in institutional indicators such as rule of law and regulatory quality. Corruption has been acknowledged as the biggest challenge that the government faces currently and in the case of Philippines, the interconnectedness of the individual indicators play out.

The strong comeback after 2009 is an indication of the resilience of the Philippine economy, however, the Philippines development plan, along with all other reports on the country, reiterates that good and stable governance is an important pre-condition of inclusive growth and suspects that the economy will fail to progress further without a sustainable and people friendly growth plan, with an environment of political stability and peace.

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# GOVERNANCE AND GROWTH: CASE STUDY-SINGAPORE

## *Section 1: Background*

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With per capita GDP of USD **46,200** in 2011, Singapore has emerged as a true Asian miracle and as one of the most successful economies of not only of South East Asia but also of the world. Notoriously referred to as ‘Disneyland with death penalty’ by a Wired magazine columnist named William Gibson in the early 1990s, Singapore’s perfectly manicured streets combined with a heterogeneous population and an unusual political practise have inspired admiration and confusion simultaneously in the world. As is widely acknowledged by the authorities, Singapore has built its economic foundations on pragmatism and clear investment ideas which were significantly aided by a long stretch for unchanged policies that Singapore’s unique political culture privileges it with.

Singapore is a city-state comprising of the main island at the south of Malaysia and about 50 smaller islands around the mainland. In the post WWII period Singapore became a separate a crown colony, but continuing struggle for independence from the British led to the emergence of a self-governing system in 1959. Amidst fear of further insecurity, Singapore joined the federation of Malaysia in 1963. However, difference in economic and political opinions put an end to this alliance and Singapore emerged as a fully independent nation in 1965.

With a population of 5.3 million in an area of 660 km/sq Singapore has become the second most densely populated country of the world, however a staggering 28% of the population are foreigners, many of them low skilled labours engaged in the construction sector.



Considering the limitations that Singapore has in terms of manpower and space, Singapore has aimed to establish itself as a communication hub in the region, focusing on maintaining a sea and an air port, taking advantage of the trading outposts established by the British.

Since Singapore has only been governed by the People’ Action Party, invariably the history of the party is linked to the history of

modern Singapore. The founder and spearhead of the party Lee Kuan Yew headed the government as the Prime-Minister from 1959 to 1990 and is widely credited with transforming Singapore from a dependent and poor outpost to one of the most developed countries of the world.

Singapore ranks highly in the Human Development Index with a total score of .866, it has a high life expectancy at birth and high years of expected schooling. However, in spite of strictly enforced regulation and close monitoring of public policies, Singapore is not known to have a comprehensive social security system such as an unemployment benefit or full

health care coverage. However, social services such as health and education enjoy government subsidies.

However, the severest criticism that Singapore faces deals with the political process of the country. Being governed by a single political party, it is perceived that there is an acute absence of multiple opinions and voices in the political arena. Public policy making is highly centralised and space of discussion with the people is limited. Singapore also suffers from the limitation of being a relatively new culture with a heterogeneous population. Racial harmony is also enforced by the State through tools such as the religious harmony act.

Main exports in Singapore include manufacturing products and financial service. With a shortage of manpower and a relatively educated labour force Singapore's main focus remains knowledge based industries such as biotechnology and ICT.

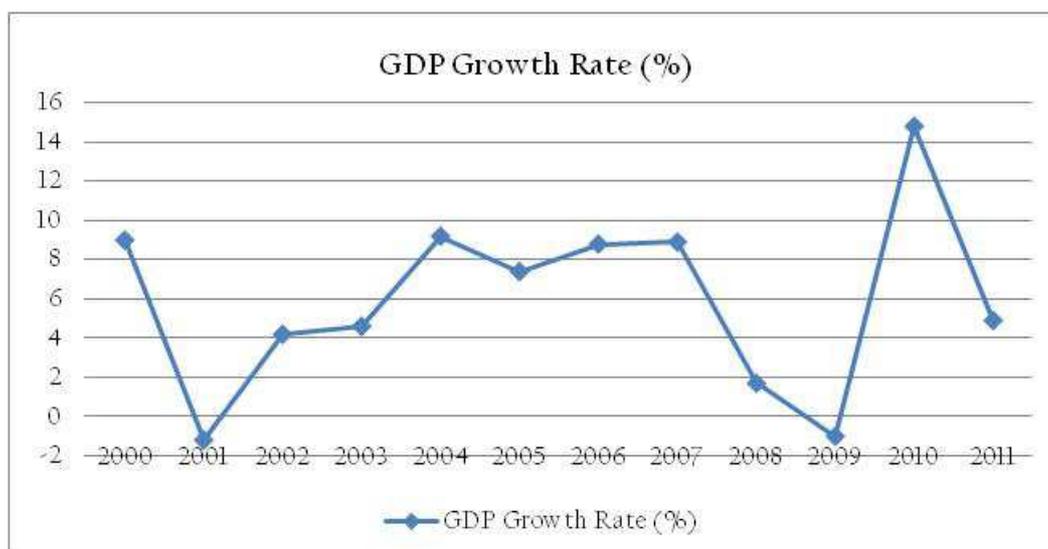
One of the main challenges to be faced by Singapore in the coming decades is the decline of its population. Total fertility rate stands at 1.16 and is gradually declining. The median age of resident workforce has increased to 41 from 38 over the last 10 years. By 2020, this is expected to be between 40 and 44. (Information Daily 2011)

### *Section 2: Economic growth indicators*

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The current economic progress in Singapore is founded on the policies undertaken as early as the 1960s, in the early days of the Peoples Action Party (PAP). Initially the government emphasised on building labour intensive industries such as textiles and assembling. Acute investment friendly policies were undertaken including tax reliefs and unlimited repatriation of profits in selected industries. (Thomas White International 2005).

In recent times, World bank ranked Singapore 1<sup>st</sup> among 183 countries in ease of doing business, and second in investors rights protection. In 2010, Singapore received more than USD 50b in Foreign Direct Investment, exceeding that of India. (Information Daily 2011) At the same time, Singapore is a highly trade dependent country with the exports accounting of 197% of GDP in 2010, and this makes Singapore vulnerable to the world economic shocks. (Datamonitor 2011), as is reflected in the falling GDP growth rate in 2009.



Singapore enjoyed an average of 5.9% growth rate over the last decade, although at negative following the financial crisis, growth rate bounced back with a staggering 14% in 2010. One of the reasons behind this progress is the incentives provided by the Government to business and innovation enterprises. The government has committed SGD 850 m in the period 2010-2014, in grants under the Enterprise Development Fund for Small and Medium Enterprises and business associations. (Information Daily 2011)

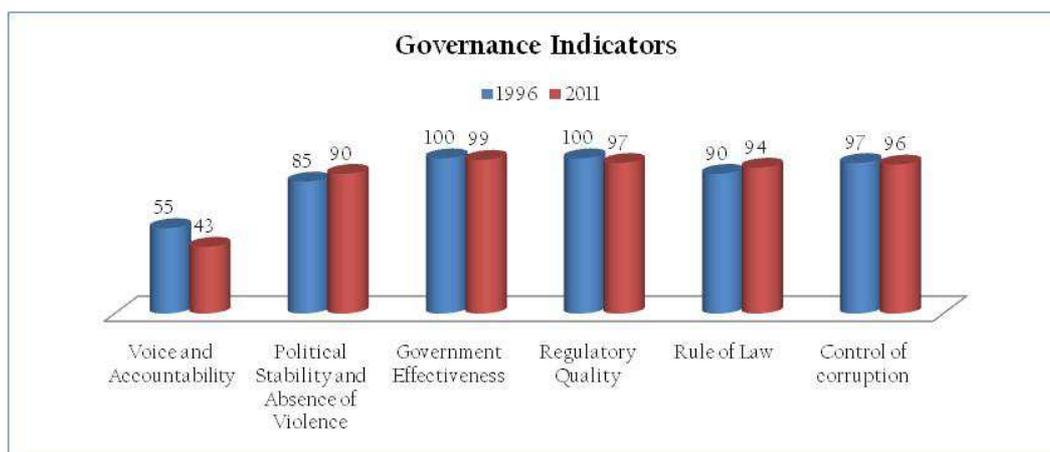
Singapore invests heavily in education and training especially in the Information Technology Sector. In 2010, SGD 4.4b was allocated for education, infrastructure and health. In a speech, the former Singapore Prime Minister has expressed the government's determination to increase productivity by 2-3% a year. In 2011, the 'National Productivity Fund' was an estimated SGD 2b. (Information Daily 2011)

Working with a budget titled 'Inclusive growth' Singapore aims to increase its real income by 30% by 2020, with per capita yearly GDP reaching USD 55,000. Yet, Singapore challenges remain in equalising income distribution and the prospect for high public expenditure which accompanies a high aging population.

### *Section 3: Governance Indicators*

#### PERCEPTION OF GOVERNANCE

The chart portrays that Singapore ranks the highest amongst the countries compared in this paper in all indicators saving Voice and Accountability, where the Philippines have achieved a higher score in the category in recent times. Yet the challenges remain that important institutional indicators such as Government effectiveness and Regulatory quality have fallen, albeit marginally, and failure to address these change may lead to heightened uncertainty in the future.



Singapore faces extreme criticism in the category of **voice and accountability**. The indicator has reached an all time low at 34% in 2006, which happened to be an election year. The election was won by Lee Hsien Loong, the son of the former Prime Minister Lee Kuan Yew founding member of the People's Action Party (PAP). While the public service is regarded as one of the best in the world, The PAPs 'absolute political dominance' in the political field presents a contrast to most democratic societies. Political pluralism is generally regarded by PAP as a obstacle to continuing sustainable governance policies of PAP and is seen as detrimental to the elemental focus of the Singapore policy makers; economic growth, security and ethnic hegemony. (Hwee 2002) The Government has also been accused of using state-run tools such as the Internal Security Act to minimise political opposition. Accusations of gerrymandering and financial incentives have also been floated. (*ibid*)

Since 2006, **Political stability and absence of violence** has improved 5 points to 90. The political competition in Singapore, though contentious, is devoid of violence. Political opponents more often face legal charges whereby their political power is controlled. (BBC 2008) Thus, in face of feeble political competition and tightly regulated law enforcement, violence in general in Singapore has been non-political and sporadic. There have been reports of gang violence in certain areas of Singapore, which were promptly addressed by the authorities. (Ng 2010)

At 99 the **Government effectiveness** indicator surpasses 99% of the countries globally. Although decreased from a full-score of 100 in 2011, Singapore steadily ranks at a full 100 on a frequent basis and has not dropped below 98 in the past 5 years. Singapore uniquely has a more efficient public sector in comparison to a relatively weak private sector and is supported by a number institutions which have been established to fulfil this requirement. Public service delivery institutions such as the Housing Development Board (HDB), the Economic Development Board (EDB) and Temasek Holdings etc., help the Government to control the prominent sectors of the economy including housing, media, transport, water, electricity, airline, banking etc. (M. S. Haque 2004) Such comprehensive public service delivery system has helped to keep Singapore at the top of government effectiveness ranking. Singapore boasts one of the best public transport systems, 85% of Singaporeans live in Public Housing and the Singapore state operates the largest public housing programme among the free market economies. (Park 1998) The Singapore state also caters for a mandatory

Provident Fund Scheme which however has been criticised for being inadequate. At the same time, with the increasing aging population the role of the Government in providing a comprehensive and sustainable coverage falls short. (Asher 2004)

**Regulatory Quality** has dropped 3 points to 97 in 2011 with a distinct downward trend starting from 2002. 2002 follows the highly publicised lawsuit against the former opposition MP Mr J.B. Jeyaretnam, who faced lawsuit and expulsion from parliament in defamation cases. This raised serious questions about the independence of the judiciary. Other criticisms of the judiciary has been the tough and quickly executed corporal punishment such as canning. The government as well as the Judiciary has been accused of blatantly disregarding human rights of the suspects or the accused in favour of overtly harsh and exemplary punishment (BBC 2012)

**Rule of Law** has increased to 94 from 90 and over the last decade has generally been above 90. This may express that there is a steady level of confidence on the conduct of the security agencies. As mentioned before, in law enforcement Singapore differs greatly from western electoral democracy. Strict Penalties have been doled out for speaking in public without permit, vandalism etc. Additionally, crimes involving recreational drugs are dealt with extreme level of seriousness and can lead to a capital punishment ruling. However, in terms of safety, Singapore ranks among the top countries with 91% of the men and 88% of the women surveyed feel safe to walk alone at night. (Gallup World 2011) This may be attributed to the prevalence of highly technological security system and an intensive anti-crime campaign throughout the country.

Singapore Government conducts its human resources management system based on meritocracy and there is no apparent accusation of the corruption in this regard. Over the last decade the perception on corruption stayed between 96 and 98 placing Singapore among the top countries in the world in **Control of Corruption**. In 2011, Singapore ranked 5<sup>th</sup> among 183 countries in the world with a score of 9.2 on a scale of 0-10. Anti-corruption measures in Singapore has been initiated even before the country emerged in its current form. An independent Corruption Practises Investigation Bureau (CPIB) was established in 1952 in order to address lingering corruption accusation in pre-independence period when Singapore was still a crown colony. The CPIB has the authority to arrest suspects and confiscate property acquired through unfair means. One of the main reasons why the civil servants in Singapore are highly paid is the intention of the government to reduce the incentive for corruption among the civil servants. (Quah 2001) Thus, the Singapore Government took a number of holistic measures in order to reduce both the demand and supply of corruptive practises.

#### DECENTRALISATION IN SINGAPORE

There is no constitutional or legal provision for local government in Singapore and neither is it deemed necessary. Localisation or decentralisation in the Singapore context needs to be viewed somewhat differently because of the size of the country. Being a city state, the Singapore government is in charge of only 5.3 million people and approximately 19 Ministries, public services such as health, transport, and education policies are nationally

controlled. Community programmes are designed and enforced by 5 development councils. It is however divided between its electoral and administrative sub-divisions. Administrative sub-divisions are mainly required for urban planning purposes. (Commonwealth Local Government Forum 2010) The main features of the Development Councils however are to coordinate with the central government in disseminating policy information and providing feedback, assisting community development and enhancing racial harmony. (M. S. Haque 2009)

#### **PUBLIC PRIVATE PARTNERSHIPS (PPP)**

Following the East Asian Financial Crisis and the SARS outbreak in the early 2000s, Singapore Government faced the prospect of budget deficit for the first time. This led to the consideration of the PPP as a ‘value for money’ financing option for Government projects. (Lam 2004) Since 2004, PPP has been initiated in Singapore in a variety of sectors mainly in infrastructure related projects. Sectors include defence, sports, water, education, environment, trade and selected projects of ICT.

PPP in Singapore is guided by the Handbook issued by the Ministry of Finance and takes precedence from PPP initiatives in the UK and Australia. Singapore wants to establish itself as the PPP ‘regional centre for excellence’ and is assisted by its sound business environment yet large scale PPP Projects are restricted by its limitation of size and population. (Ashurst 2010)

Thus, although there is considerable commitment from the Governments part, PPP is still at an early stage and no particular PPP model has been developed. Most projects are confined to designing, building and operating PPP facilities and the operations are heavily overseen and regulated by the Government.

#### ***Section 4: Reconciling Governance and Growth Indicators***

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Singapore has grown tremendously in its relatively short independent history. The Singapore model of development has become an example for developing economies to follow and replicate. This growth has been achieved at the cost of political discourse within the nation, the lack of which is compensated by high income and increased human security. In Singapore’s case strong political discourse had never been able to form and thereby any political stability was avoided.

In recent times, it is indicated that the State has become more tolerant toward differing political views. The opposition won 6 seats among 87 in the last election in 2011, the highest ever in the history of the country, however PAP remains the sole driver of policies in the country.

Despite the low level of political participation, as the governance indicators reveal, Singapore has achieved remarkable success in governance and growth simultaneously. It presents a situation where both politics and policy are geared toward increased growth and achieved an harmony in this regard. Whether the citizens have been politically active in terms of fruitful

discourse have not affected the standard of living, which is why a high level of HDI is acquired in face of rising inequality in the country.

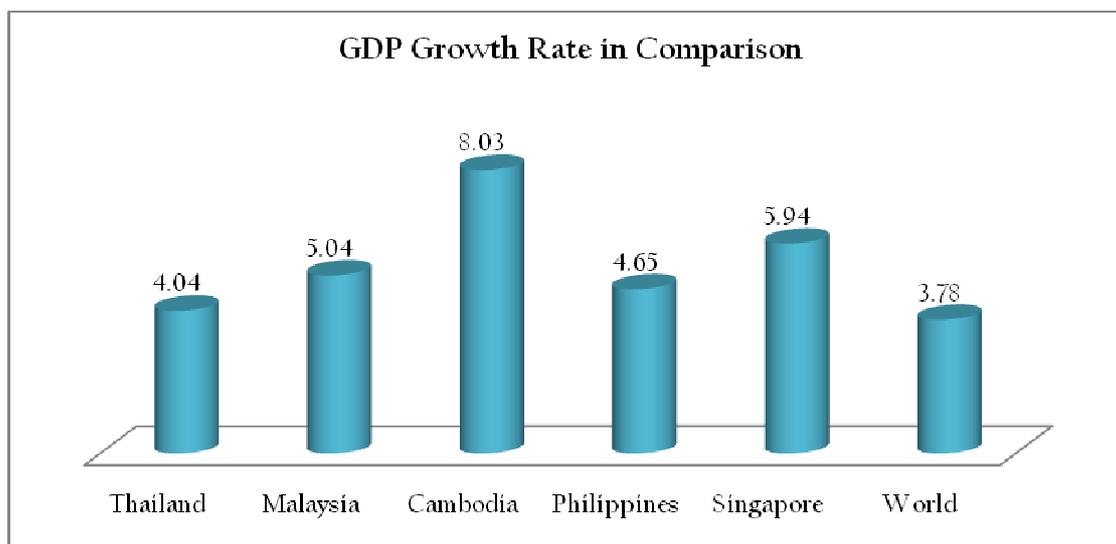
From the information presented through the indicators, it may be concluded that in a political environment which is not free and highly regulated, Singapore Government has achieved tremendous growth because of the strength of its ability to formulate and implement policies and gain trust from its citizens in its ability to deliver the necessary services.

## GOVERNANCE AND GROWTH

### POLITICAL PARTICIPATION OR GOVERNANCE INSTITUTIONS?

As advocated by scholars and development agencies alike, good governance is now considered to be a relevant factor for growth, yet the exact influence of good governance on growth is yet to be fully explored. Since there are a number of significant comparable indicators, a basic analysis may reveal whether these factors are likely to affect growth rate and how, and whether the nature of the increased growth is likely to foster further inequality or higher Human Development.

The World Bank indicators which have been considered in the paper present a comparative snapshot of the governance situation of the country in reference to rest of the world, it may be useful to acquire a similar comparison in the growth indicators as well. The chart below gives an idea of the growth rate achieved by the countries in question in comparison to the world growth rate for the period 1999-2011.



It is interesting to note that all the countries analysed have a higher growth rate when compared to the average world growth rate over the same period of time. The world as a whole has experienced an average growth rate of 3.78% per year while the lowest growth rate among the countries analysed is 4.04% and is achieved by Thailand, while Cambodia achieves the highest at 8.03%. Thus, it may be argued that while the governance indicators show that some of the countries are falling behind in comparison to the rest of the world, the rate of per-capita GDP growth has not been similarly affected thus, scoring low in governance indicators does not translate to having an corresponding lower level of growth.

Therefore in constructing a relationship between growth and governance, a number of observations may be emphasised:

*History of political participation may not translate to political stability*

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Among the five countries analysed, Thailand and Philippines have a much higher level of visible history of public protest against the government and a continuous history of changing government in the face of public discontent. This becomes extremely visible in countries such as Philippines and Thailand which have seen multiple military coups in recent times and frequent change in the government due to widespread public protests. In Malaysia, the voice and accountability indicator ranks 32 in 2009 whereas in Thailand it ranks 34 in the same year. However, for political stability the countries rank 50 and 12 respectively.

Similar comparisons can be made between Singapore and Philippines, in 2011 Philippines scored 7% higher in the voice and accountability indicator but scored 80% lower in stability. Thus, in Singapore and Malaysia, while the Governance system may be more authoritarian in comparison, it does not result in increased political violence in these countries. At the same time, a higher level of political voice did not necessarily result in the election of a satisfactory government geared toward greater economic and social development.

*Steady growth rate is generally accompanied by higher government effectiveness and regulatory quality*

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The countries after Cambodia with the highest average growth rate in the region, Singapore and Malaysia, with a growth rate of 5.94 and 5.04 respectively, have a much higher score of factors such as government effectiveness and regulatory quality. The countries both score relatively higher in these categories with score of 80 and 72 for Malaysia in Government Effectiveness and Regulatory Quality and 99 and 97 for Singapore. Thus the countries not only score high with respect to the South East Asian countries but also to the world. As shown earlier, their average growth rate is also nearly 2% higher than that of the world during the same time period.

Similar points can be raised in the cases of Philippines, which has a lower growth rate compared to Singapore and Malaysia, Philippines rank between 42 and 55 and Thailand ranks approximately 60 in these categories, although between each other Philippines has a slightly higher rate of growth most likely due to its strong natural resources base.

Cambodia on the other hand reverses this trends somewhat and achieves a high rate of growth despite a low score in the said categories. Yet, it is also noteworthy that the high rate of growth in Cambodia is not accompanied by a high score in the Human Development Indicator, in fact Cambodia scores the lowest in HDI among the countries compared. Thus, as a post-conflict nation Cambodia has achieved a high rate of growth based on its affordable labour and flourishing tourism and has been able to take advantage globalisation. However, unless the growing economy is sustained by higher living standards of the citizens, Cambodia is exposed to the risk of failing to progress from its current status.

*High rate of corruption is generally accompanied by high level of inequality*

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In the pathway to sustained growth, corruption may turn out to be extremely detrimental as it might present itself as an obstacle to the level of investment required for growth. A high level of corruption, in the case of a country like Philippines, has been a primary reason for decreased confidence on investment. A high level of corruption in conjunction with a high level of inequality is likely to indicate that the earnings from corruptions is being enjoyed by the high income earners at high levels power, this holds true in case of Philippines where multiple heads of state have been accused of corruption. Initiatives such as Public Private Partnership has been undertaken in countries such as the Philippines such that more transparency and accountability can be ensured, but a low level of investor confidence will prevent PPP to flourish in these sectors.

Among the cases studied, interestingly the countries with the highest HDI are also the countries with the lowest levels of corruption. Control of corruption is 58 and 96 in Malaysia and Singapore respectively with 2011 HDI ranking of 61 and 26 respectively among 187 countries. Although inequality in both the countries is on a rise, yet the countries currently enjoy a standard of living that not only fosters higher level of investment but also a more stable economic and political environment. Thus, considering the conclusions, it may be argued that

*For growth, Institutional factors may be more relevant than political factors*

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The countries examined in this paper show how institutional factors such as government effectiveness and regulatory quality inspire greater confidence in the business environment in the country and stimulates growth, but at the same time it is possible for low level of voice and accountability or political participation to be accompanied by a relatively strong and continuing growth rate.

This is revealed firstly in the case of Singapore and the Malaysia which not only have a relatively high growth rate but also the highest per capita GDP per year. At the same time, both countries were able recover very quickly after the external shock from the global economic slowdown. These are also the countries which garner relatively low scoring in the voice and accountability indicator but their growth rate does not seem to be deterred by it. While both the countries are showing indication of allowing increased political freedom, it is not yet the case and growth has been achieved within a restrictive political culture.

However, for these countries government effectiveness and regulatory quality achieve a relatively high score with 70-80% in Malaysia and 97-99% in Singapore. These indicators, which points more towards system and process of policy making and implementation rather than the political or electoral process of the country, reveal how focused implementation of growth policies may lead to higher growth even when implemented through largely authoritarian governments.

This is also relevant in the case of Thailand which with a 60% government effectiveness and regulatory quality score and a 12% political stability score has an average growth rate of 4.04 and foreign investments continue to flow in.

For the Philippines, the opposite is the case. Philippines has a voice and accountability score of 50, higher than both Malaysia and Singapore but scores 55 and 42 in government effectiveness and regulatory quality respectively, lower than these countries. Philippines' growth rate is also lower at 4.65% per year. In addition, with a strong labour force, extensive natural resources base, comprehensive decentralisation and PPP policies, the current growth rate in Philippines continue to fall below its potential and anticipated growth rate.

Therefore, although political voice, political stability are conducive to sustainable growth, it factors such as government effectiveness and regulatory control are likely to have a greater and more direct impact on the rate and nature of growth in a country.

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