



Asia Pacific Economic Cooperation

# OPEN ECONOMIES DELIVERING TO PEOPLE

APEC'S DECADE OF PROGRESS

A report prepared for the  
APEC Economic Leaders Meeting  
Brunei Darussalam 2000



# About this report

*Open Economies Delivering to People: APEC's Decade of Progress* has been prepared by the Australian Department of Foreign Affairs and Trade, with input from other APEC economies, for the November 2000 APEC Economic Leaders Meeting in Bandar Seri Begawan, Brunei Darussalam. It builds on an earlier report, *APEC — A Decade of Progress*, endorsed by APEC Ministers Responsible for Trade when they met in Darwin, Australia, on 6–7 June 2000.

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# Contents

<b>Highlights</b>	<b>vii</b>
<b>1 Globalisation – the APEC way</b>	<b>1</b>
APEC’s experience	1
APEC’s role in fostering openness and sustainable structural adjustment	2
<b>2 Open trade and investment policies deliver growth</b>	<b>4</b>
Openness leads to economic growth	4
Trade barriers have fallen in APEC economies ...	8
... and trade has expanded ...	11
... as has foreign direct investment	11
Liberalisation and integration have brought strong economic growth ...	13
... and are facilitating recovery from the financial crisis	14
APEC contributes to open trade and investment in the region	14
<b>3 Greater growth by getting the domestic environment right</b>	<b>20</b>
Microeconomic reform is a necessary adjunct to trade and investment liberalisation	21
Stronger institutional capacity leads to higher growth	22
APEC economies are improving their economic governance	23
Microeconomic reform strengthens APEC economies ...	25
... as all economies respond to the challenge of adjustment ...	30
... and prepare for the ‘new economy’	33
APEC’s work strengthens economic governance and supports microeconomic reform	35
<b>4 Open economies deliver social advancement</b>	<b>39</b>
Poverty is being alleviated	40
Employment is growing	42
Health is improving	42
Educational opportunities are expanding	44
Environmental challenges are being tackled	47

<b>5 APEC – maximising the benefits from increasing openness</b>	<b>52</b>
APEC is building on success ...	53
... by intensifying trade and investment liberalisation ...	54
... by strengthening domestic markets and institutions ...	55
... and by building the ‘new Asia-Pacific economy’	55
Managing change better is the challenge	56
<b>Technical notes</b>	<b>58</b>
<b>References</b>	<b>63</b>
<b>Boxes</b>	
2.1 The discipline of open trade policies	5
2.2 Key points in recent APEC statements on multilateral trade negotiations	16
3.1 Microeconomic reform in Viet Nam	29
3.2 Adjusting to liberalisation	30
3.3 Key principles of Thailand’s social safety net	32
3.4 APEC Finance Ministers and international financial reform	37
4.1 Trade and investment liberalisation promoting environmental protection	50
<b>Charts</b>	
2.1 The rewards of openness in developing economies are higher rates of growth	6
2.2 A 1 percentage point increase in openness leads to 2–3 per cent growth in income per person	7
2.3 Average tariffs in APEC economies fell between 1988 and 1998	9
2.4 Frequency of non-tariff barriers in APEC economies fell between 1995 and 1998	10
2.5 APEC trade has boomed as APEC economies have become more open	11
2.6 APEC inflows and outflows of foreign direct investment have grown rapidly	12
2.7 FDI flows to lower income APEC economies have grown particularly rapidly	12
2.8 Lower income APEC economies have prospered over the past decade	13
2.9 APEC economies are rebounding from the Asian financial crisis	14
3.1 Economies with good economic policy and strong institutional capability grew up to eight times faster between 1964 and 1993	22
3.2 Better governance helps to explain the income gap between East Asia and Africa	23

3.3	One measure shows governance is improving in APEC economies	24
3.4	APEC economies have good risk ratings	25
3.5	Policy choices affect socioeconomic development	29
3.6	Access to the internet has expanded rapidly in APEC economies	34
4.1	Indexes of human development have improved in APEC economies	39
4.2	East Asian APEC members have been alleviating poverty	40
4.3	Growth is the driving force behind poverty reduction	41
4.4	New jobs have been created	42
4.5	Infant mortality has fallen and life expectancy has risen in lower income APEC economies	43
4.6	Access to sanitation and safe water has expanded in lower income APEC economies	43
4.7	Public expenditures on health are generally growing faster than GDP	44
4.8	Education enrolment ratios have improved in APEC economies	45
4.9	Women's enrolment in education compares favourably	45
4.10	Adult literacy rates in APEC economies are high	46
4.11	Public expenditures on education are generally rising faster than GDP	46
4.12	Natural resource depletion is falling in APEC economies	48
4.13	Resource management in lower income APEC economies improved between 1984 and 1994	48
4.14	Economic prosperity need not come at the expense of the environment	49

# Highlights

## **Open trade and investment policies deliver sustainable economic growth**

- Open developing economies typically deliver growth in gross national product per person that is 5 percentage points higher than in closed economies.
- A 1 percentage point increase in the ratio of trade to gross domestic product results in a 2–3 per cent increase in gross domestic product per person.
- Tariffs on imports effectively tax exports by, among other things, driving up exchange rates, thereby making exports more expensive.
- International competition results in greater efficiency and productivity, leading to better quality and lower priced goods to the consumer.

## **Over the past decade APEC economies have achieved impressive economic growth while lowering protection**

- APEC member economies have substantially reduced both tariffs and non-tariff measures — some well beyond Uruguay Round commitments.
- APEC exports have increased by 113 per cent to over US\$2.5 trillion.
- Foreign direct investment in APEC economies has grown by 210 per cent overall, and by a staggering 475 per cent in lower income APEC economies.
- APEC real gross national product has grown by about a third overall, and by 74 per cent in lower income APEC economies.
- Despite significant population growth, gross national product per person in lower income APEC economies has grown by 61 per cent.
- The economies of APEC have generated nearly 70 per cent of global growth and as a region has consistently outperformed the rest of the world.
- Open trade and investment policies have facilitated an export-led recovery in economies affected by the Asian financial crisis.

### **APEC as a grouping has contributed to the ability of its members to achieve these impressive outcomes in a number of mutually reinforcing ways**

- APEC played a key role in the successful conclusion of the Uruguay Round and continues to secure benefits for its members by working towards a new round.
- APEC played a pivotal role in developing the WTO Information Technology Agreement.
- APEC has set an ambitious goal to achieve free and open trade in the region, and encourages its members to work towards it through a revamped Individual Action Plan system.
- APEC has facilitated regional trade through, for example, mutual recognition arrangements, the development of paperless customs procedures and the APEC Business Travel Card.
- APEC complements this liberalisation work by helping developing member economies to build their capacity to implement and enjoy the benefits of liberalisation through technical assistance.

### **Trade and investment liberalisation are not enough for sustained economic development**

- Wide-ranging domestic economic reform and strong institutions of governance are needed for economies to reap the full benefits of open market policies.
- Economies with strong institutions and open policies have grown at nearly eight times the rate of those with weak institutions and closed policies.
- Stronger institutions and more open policies accounted for about three-fifths of the 320 per cent difference in average incomes per person between East Asia and Africa.

## **APEC economies have made considerable progress in domestic economic reform and strengthening economic governance**

- APEC economies have improved their economic governance over the past decade and are now attracting lower risk ratings than comparable economies.
- APEC economies have undertaken wide-ranging microeconomic reform, including:
  - financial sector restructuring and regulation;
  - legal and judicial reform to improve the framework for contracting and enforcing debt;
  - taxation and public expenditure reform to improve incentives for private investment and to increase the efficiency of delivering social and infrastructure services; and
  - promotion of competition through deregulation and the adoption of measures to counter anticompetitive practices.
- APEC economies are adopting labour market programs to facilitate adjustment to policy change, and are extending social safety nets to protect vulnerable groups from adverse developments.

## **APEC as a grouping is supporting reform efforts through collaborative policy development and cooperation in capacity building**

- APEC Finance Ministers have established a range of initiatives to strengthen regional financial and capital markets and to support freer and stable capital flows in the region.
- APEC's 'strengthening markets' initiative is helping members in aspects of strengthening governance, implementing competition policy, enhancing the quality of economic regulation and reducing compliance costs.

## **APEC's growth over the past decade has delivered social advancement**

- UNDP's Human Development Index for lower income APEC economies improved by nearly 18 per cent.

## Highlights

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- Poverty in East Asian APEC economies fell by about a third — some 165 million people — mostly as a result of strong economic growth.
- APEC economies created about 195 million new jobs, including 174 million in lower income economies.
- In lower income APEC economies, infant mortality fell and life expectancy rose, linked to significant improvements in access to sanitation and safe water, and expanding public expenditure on health.
- APEC economies invested heavily in human capital, with improving education enrolment ratios and growing public expenditure on education.
- Environmental degradation remains a key issue in some APEC economies.
  - There is no evidence that liberalisation and economic reform cause environmental problems. Some of the worst environmental records are from closed economies.
  - But trade and investment liberalisation does not provide an automatic solution to environmental degradation; stronger environmental policies are necessary to ensure sustainable development and cleaner environments.
  - APEC economies have been significantly reducing resource depletion, improving resource management and investing in cleaner environments.

### **APEC cooperation will continue to play a critical role in building on the successes of the past decade**

- APEC can be expected to maintain support for the launch of a new WTO round and redouble unilateral liberalisation efforts to meet the Bogor goals.
- APEC is likely to intensify work on competition policy and regulatory reform and strengthen economic and corporate governance capacity.
- It will be important to ensure that the impact of new information and communication technologies permeates all sectors to sustain productivity growth and social progress.
- APEC economies will need to maintain a strong emphasis on human resource development and give increased attention to proactive structural adjustment strategies.

# 1 Globalisation – the APEC way

Around the world the process of international economic integration, often called globalisation, is raising concerns. Some people are claiming that globalisation is responsible for a host of contemporary evils, including impoverishment of the developing world, unemployment and environmental degradation. This belief has generated vocal opposition to efforts to further free up world trade and investment through the launch of another round of multilateral trade negotiations in the World Trade Organization (WTO).

But the evidence clearly demonstrates that this belief is misplaced. It is true that globalisation necessitates some adjustments that can be difficult for some in the community. However, the process of internationalising economies by opening markets to international competition and expanding international trade has consistently led to substantial improvements in economic growth and increased wealth in the economies that have adopted open economic policies. This increased wealth has translated into significant improvements in a range of social indicators. Open economic policies have led to substantial reductions in poverty, significantly increased employment, improvements in health, expanding educational opportunities and better environments.

## **APEC's experience**

### **Open economies deliver wealth and social progress ...**

APEC was founded in 1989 on a common commitment to open trade and investment and to continue domestic economic reform. Over the past decade each APEC economy has individually pursued more open economic policies. And the fruits of this policy direction are undeniable. The APEC region has consistently been the most economically dynamic part of the world. The economies of APEC generated nearly 70 per cent of global economic growth in the decade that ended in 1999, and APEC has consistently outperformed the rest of the world, even during the regional financial crisis.

APEC economies have progressively reduced tariffs and non-tariff barriers, and have been rewarded with both efficient domestic economies and dramatically expanded exports. Increasing openness to international investment has helped to

fuel the impressive growth of APEC economies; it has also helped the economies affected by the regional financial crisis to bounce back quickly.

Over the past decade the open economic policies of APEC members have created the wealth necessary to dramatically improve the standard of living of their peoples, slashing poverty by about a third in East Asian economies and generating around 195 million new jobs. This wealth has also led to significant improvements in basic indicators of health, greater access to education and higher levels of literacy. There is also evidence of greater attention being focused on improving environmental standards and resource management.

### **... but complementary actions are required to sustain the gains**

APEC member economies have recognised that reducing barriers to trade and investment alone is not sufficient to ensure that they will fully reap the benefits of internationalisation. Comprehensive economic reform to create efficient, competitive and modern economies has been an essential ingredient in their success in the international marketplace. The regional financial crisis also demonstrated that open and efficient economies must be supported by robust and effective institutions of governance. So APEC economies are now paying particular attention to improving the quality of their economic and corporate governance.

The dramatic changes in APEC member economies have not taken place without posing challenges. Increased international competitiveness requires major structural adjustment efforts to ensure that everyone shares in the wealth generated by expanding economies. Member economies have adopted a variety of structural adjustment strategies to help affected industries rise to the challenges of internationalisation, as well as instituting social safety nets to assist their people to cope with change.

## **APEC's role in fostering openness and sustainable structural adjustment**

While the achievements of APEC member economies have resulted primarily from the individual policy choices of each economy, APEC as an institution has also made a significant contribution to the ability of its members to pursue open economic policies.

- APEC has encouraged further opening of member economies through both its advocacy of multilateral liberalisation and the establishment of the Bogor goals of free and open trade in the APEC region.
- APEC has facilitated the expansion of trade in the region through practical measures to reduce impediments to trade.
- APEC has helped in the adoption of best practice solutions to a range of microeconomic reform challenges.
- APEC has promoted understanding of the policies necessary for successful capital account liberalisation and strengthening of financial markets.
- APEC has helped its members to improve their economic and corporate governance and has undertaken a range of capacity-building activities to enable its members to build strong, open and competitive economies.

APEC continues to help its member economies meet the challenges and reap the benefits of increasingly open economic policies, which will generate even greater wealth to sustain the continuing social advancement of their people.

## **2 Open trade and investment policies deliver growth**

Since APEC was formed, member economies have actively pursued the benefits of international economic integration. Tariff and non-tariff barriers to trade have been reduced, and foreign investment has been liberalised. The rapid growth of trade and foreign direct investment (FDI) facilitated by liberalisation has brought with it a significant expansion in output and income. In the ten years from 1989, APEC trade more than doubled, FDI inflows tripled, and combined real gross national product (GNP) increased by a third. It is no coincidence that good economic performance has accompanied liberalisation, since there is a strong link between openness and economic growth.

### **Openness leads to economic growth**

During the last quarter of the twentieth century the process of globalisation accelerated throughout the world, driven by an expansion of trade in goods and services and international capital flows. This acceleration has been due in part to technological change, which has been reducing the costs of international transport and communications and facilitating the internationalisation of production networks. But it is also due to the policy and institutional changes in many economies designed to increase their openness to trade and investment.

The primary reason for adopting more open trade and investment policies is to secure sustainable economic growth. How the benefits of that growth are distributed within economies is sometimes cause for criticism, but the answer never lies with shutting down growth. Open trade and investment policies contribute to growth in a number of ways.

Open investment policies facilitate access to foreign savings, which can be used to complement domestic resources to finance investment. But the more important impact of foreign investment comes through its direct and indirect impacts on productivity. Foreign investment brings with it the technology, know-how and production and management practices of other economies, which can spill over to domestic enterprises. For emerging economies, a 1 percentage point increase in foreign direct investment (measured as a proportion of gross domestic product), with other things staying the same, can lead to a 0.8 percentage point increase in

productivity (measured as income per person) (Bergsman, Broadman and Drebenstov 1999).

Open trade policies also promote efficiency and increased productivity. Open markets allow the most efficient use of trade as a process for transforming inputs of land, labour, capital and entrepreneurship into the goods and services that people want to consume or producers want to use (box 2.1). They play a central role in ensuring competitiveness and efficiency of resource allocation and in disciplining investment and production decisions.

Open markets also increase investment opportunities and, with that, access to the technology and technological know-how of others. A large proportion of foreign investment is directly linked to trading opportunities, as multinational companies seek appropriate locations for segments of their global production networks. A third of all world trade is now accounted for by intra-firm trade among multinational companies that have adopted regional and global production strategies for locating interdependent facilities in different economies.

Open markets also subject foreign and local enterprises to competitive pressures, while providing them with access to up-to-date equipment and high quality inputs, and exposure to the world's best management and production practices. The extra competition spurs innovation as producers seek to improve and

### Box 2.1 The discipline of open trade policies

The main reason for reducing barriers to international trade lies in the role that open trade policies play in ensuring competitiveness and efficient resource use, and in disciplining investment and production decisions.

This becomes apparent if international trade is thought of as a technological process for transforming locally produced goods and services into goods and services made in other economies. Trade is a way that an economy can convert the labour and capital used to make, for example, computers into, say, beef or rice or aeroplanes. It offers an alternative way of supplying the goods and services that people want to purchase besides producing them locally.

When viewed as a production technology, international trade also provides a benchmark for the efficiency of local production. If local producers can produce at the same cost in local resources and factors of production as it takes to acquire goods through trade, they are using the local resources efficiently. Conversely, if local producers can generate adequate returns only if prices are much higher than international prices, it can be presumed that they are using resources inefficiently and that those resources would generate greater benefits to the economy if they were used in other activities.

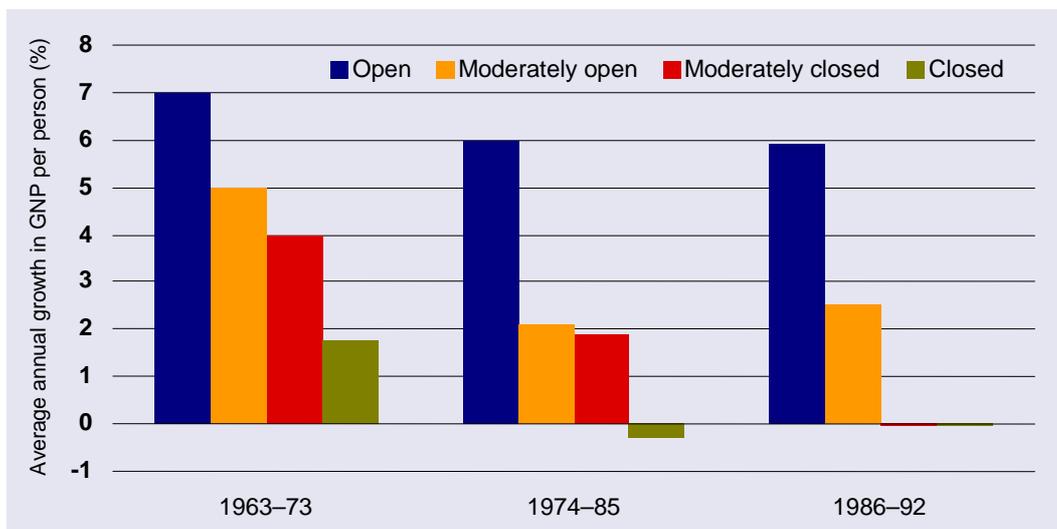
differentiate their products in the marketplace ahead of their competitors. As new products or variations to old products are introduced or made in better ways, productivity in the economy rises. Experience has shown that the principal benefits of foreign investment — the technology and productivity spillovers to the domestic economy — are maximised in an environment that promotes competition, especially from international sources of supply.

Open markets can also promote growth and efficiency by locking in good economic policies and by assisting risk management through diversification of markets and sources of supply. Open economies are typically seen as being less risky by international and domestic sources of finance, which lowers the premium that must be paid on borrowed funds, and hence the cost of investing.

The strength of the link between openness and economic growth is borne out by the relative performances of economies. As chart 2.1 shows, from 1963 to 1992, open developing economies typically achieved growth rates in GNP per person that were over 5 percentage points higher than in closed economies.

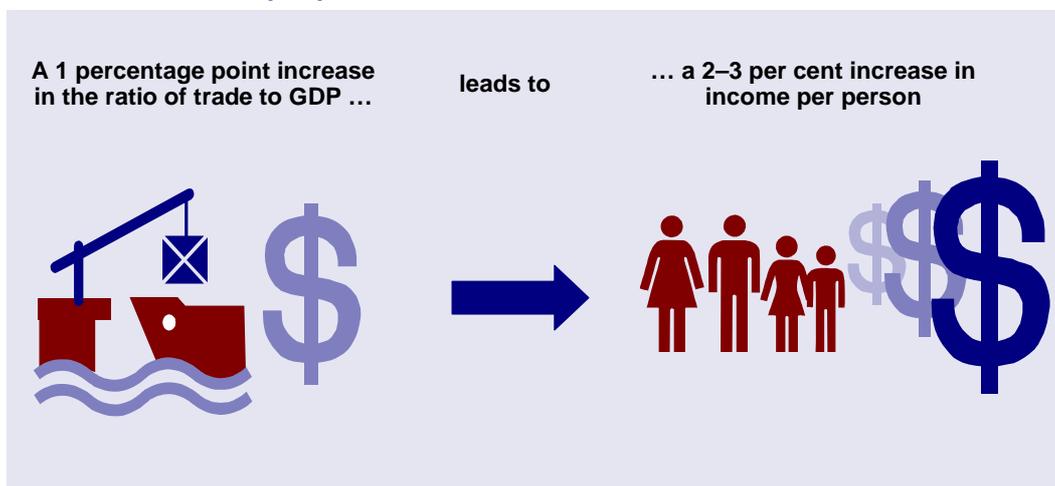
More recent research confirmed the link between open trade and economic growth. Frankel and Romer (1999) rigorously examined the interdependency between trade and growth across economies and found a strong causal link between openness, growth and income. Their results indicate that, for every 1 percentage point increase in the ratio of trade to gross domestic product (GDP), income per person is 2–3 per cent higher (chart 2.2).

Chart 2.1 **The rewards of openness in developing economies are higher rates of growth**



Data source: OECD (1999).

Chart 2.2 A 1 percentage point increase in openness leads to 2–3 per cent growth in income per person



While attention is often focused on the export dimension of an economy's openness and the gains from participation in export markets, the principal policy action typically required to increase openness is to reduce barriers to imports. One reason for this is that such barriers act as a tax on exports. So an important way to increase openness is to address the impact that import barriers have on the exchange rate and import prices.

A recent paper (Stoeckel 1999, p. 80) explained the impact that barriers to imports have on exports in the following way:

Suppose a country stopped all of its imports by imposing a prohibitive tariff (that is, an import tax). For a while exports would continue, but eventually accumulating foreign exchange without supplying any foreign exchange in return (that is, importing) would see the exchange rate appreciate, pricing exports out of foreign markets. Through the workings of the economy, the import tax ends up being in effect an export tax.

But more fundamentally, the end purpose of trade is to import, since it is imports, not exports, that are consumed or invested and contribute to national wellbeing — now or in the future. Imports, especially of capital goods and intermediate inputs, frequently embody or complement the technological improvements that trigger productivity increases. Imports of final goods expand people's choices with respect to cost, quality and variety, and expand the purchasing power of their incomes.

Economies — and their people — thus benefit most by reducing their own barriers to imports. At the same time, they gain additional benefit when other

economies reduce their trade barriers, creating new or expanded markets for their internationally competitive products. This is why multilateral trade negotiations play an important role in shaping efforts to liberalise trade. The Uruguay Round Agreement under the GATT (now WTO) produced broad-based reductions in tariffs and eased many of the most important non-tariff barriers to trade. This has been a key factor in the growth of global trade and, through that, of global incomes.

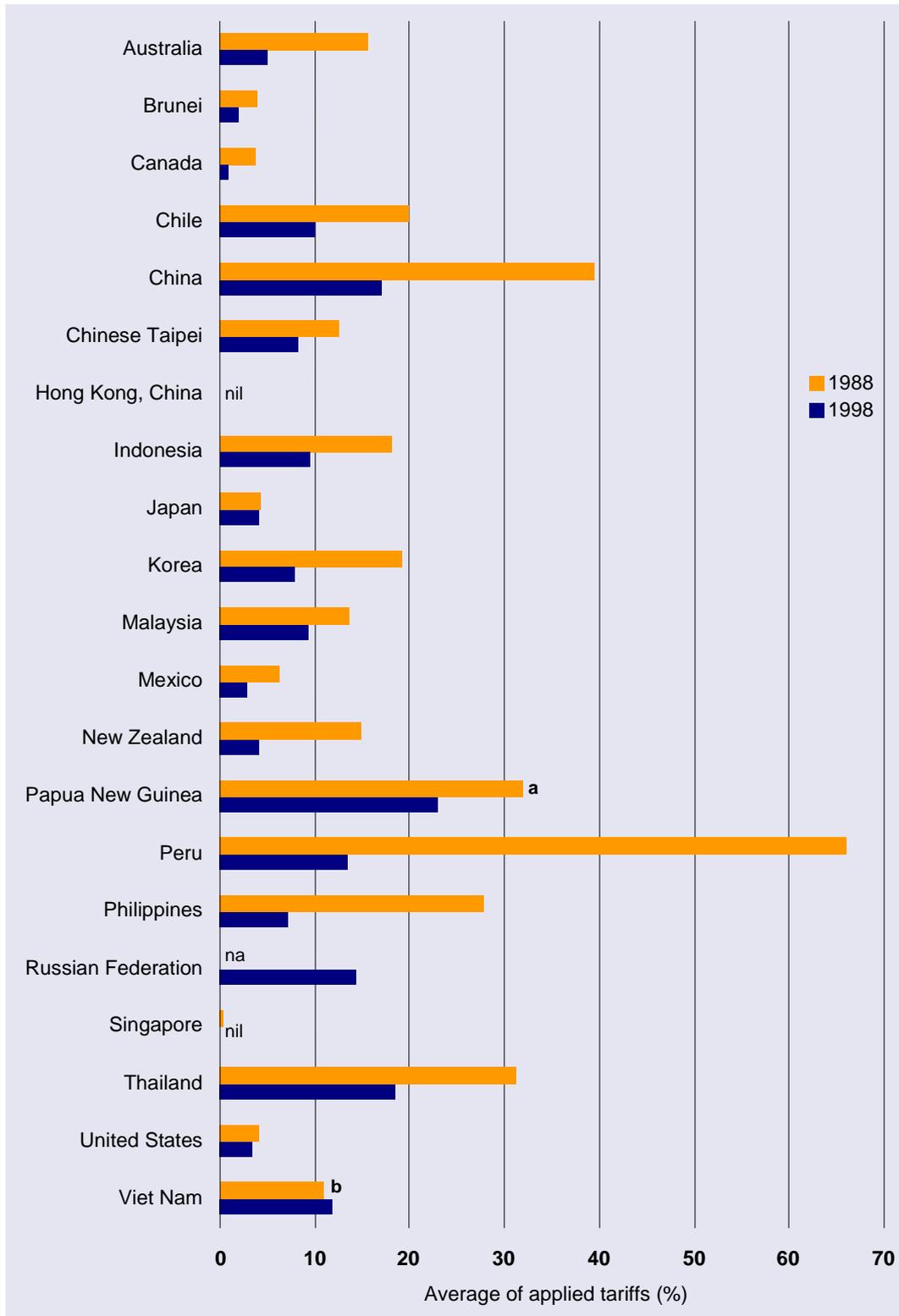
The inclusion of important trade-related and other measures affecting investment in the ambit of the multilateral system following the Uruguay Round and the establishment of the WTO has also provided a framework for removing some barriers to investment. Similarly, the agreement on trade in services has brought activities that now account for 61 per cent of world GDP into the reach of the disciplines and processes of the WTO. The WTO system also provides valuable rules and disciplines for international trade that are legally binding and subject to clear dispute settlement procedures — a particularly valuable asset for smaller economies.

### **Trade barriers have fallen in APEC economies ...**

The formation of APEC reflected an appreciation among the member economies of the gains from openness, and members have been acting on their common commitment to open trade and investment policies. All APEC economies — including new members — have been progressively reducing barriers to trade over the past decade. Most economies have substantially reduced tariffs (chart 2.3), while others have significantly reduced levels of protection by converting non-tariff distortions into tariffs. In cases where non-tariff barriers have been converted, average tariff rates may have risen, even though levels of protection (and associated distortions) have fallen.

A recent review by the Pacific Economic Cooperation Council (PECC 1999) showed that APEC members have taken significant steps to meet the Bogor declaration goals of free and open trade by 2010 for industrialised economies and 2020 for developing economies, with progress on key non-tariff measures as well as tariff reduction. That review also revealed that there has been progress in reducing the incidence and use of core non-tariff barriers (chart 2.4), although there has been some lagging in certain sectors where there are domestic sensitivities.

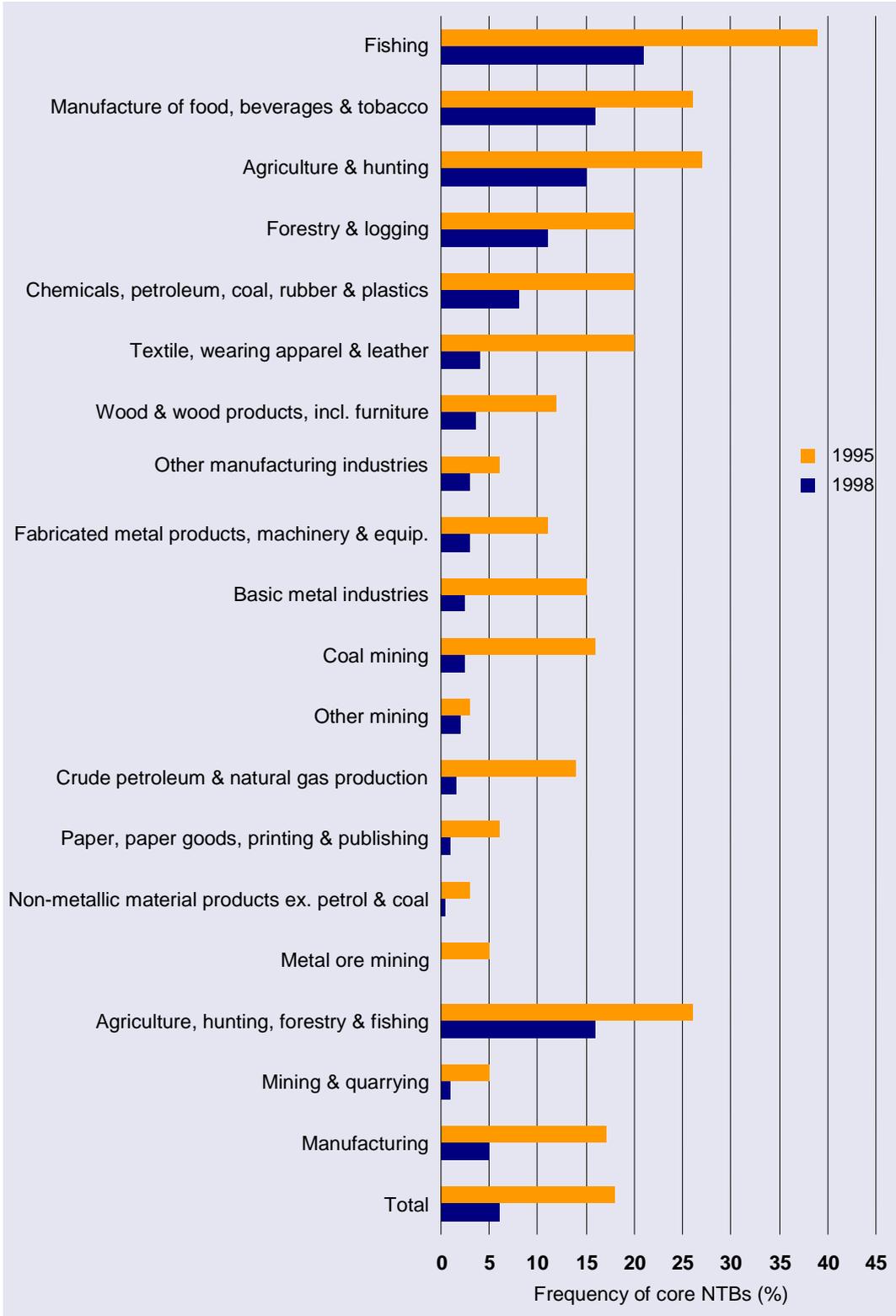
Chart 2.3 Average tariffs in APEC economies fell between 1988 and 1998



<sup>a</sup> In 1995. <sup>b</sup> In 1993. na Not available.

Data source: DFAT (1999b); see technical note 1.

Chart 2.4 Frequency of non-tariff barriers in APEC economies fell between 1995 and 1998

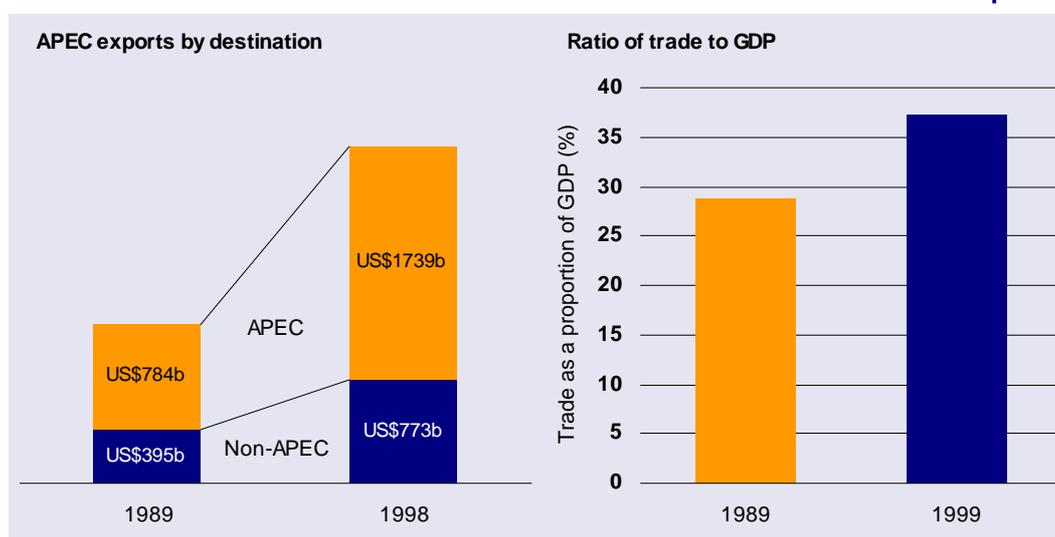


Source: PECC (1999).

### ... and trade has expanded ...

The period in which this liberalisation occurred was one of rapid expansion in trade by APEC members — both within APEC and with other economies. Between 1989 and 1998, APEC exports increased by 113 per cent to over US\$2.5 trillion. Trade between APEC and non-APEC economies almost doubled and intra-APEC trade more than doubled (chart 2.5). As a result, trade has become much more important to APEC economies. The ratio of total trade to GDP rose from 29 per cent in 1989 to 37 per cent in 1999 (chart 2.5).

Chart 2.5 APEC trade has boomed as APEC economies have become more open



Data source: DFAT (1999a); see technical note 2.

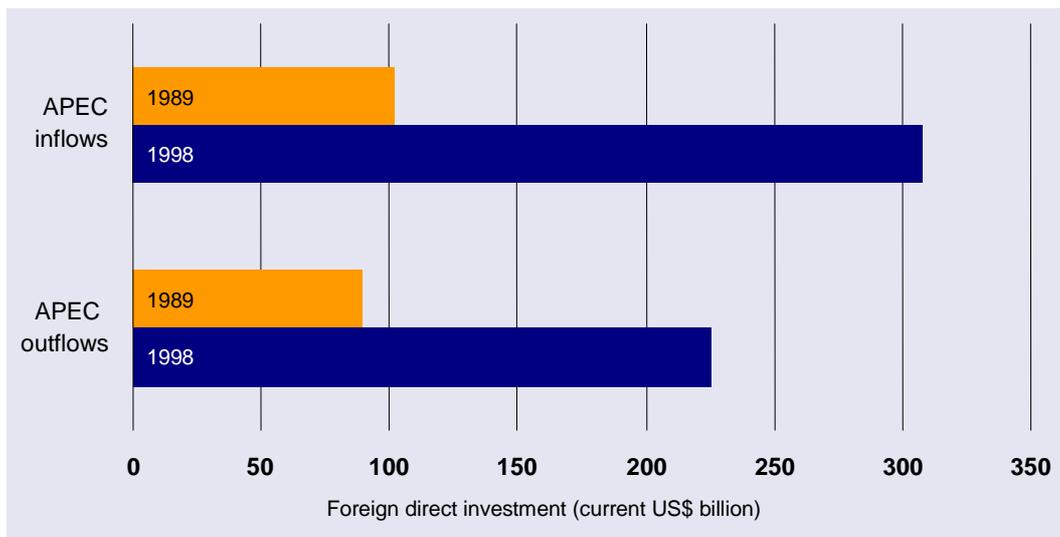
### ... as has foreign direct investment

Another dimension of the deepening economic integration of the APEC economies with the world economy is the rapid growth of FDI flows (chart 2.6).

Foreign direct investment in APEC economies grew by 210 per cent over the period 1989–98, and APEC economies now account for around a half of global FDI inflows. This expansion occurred despite the Asian financial crisis, which badly affected capital flows to several APEC members in 1997 and 1998. As well as being a major destination of foreign direct investment, APEC economies are a major source of such investment. Some US\$225 billion of world FDI flows in 1998 originated in APEC economies.

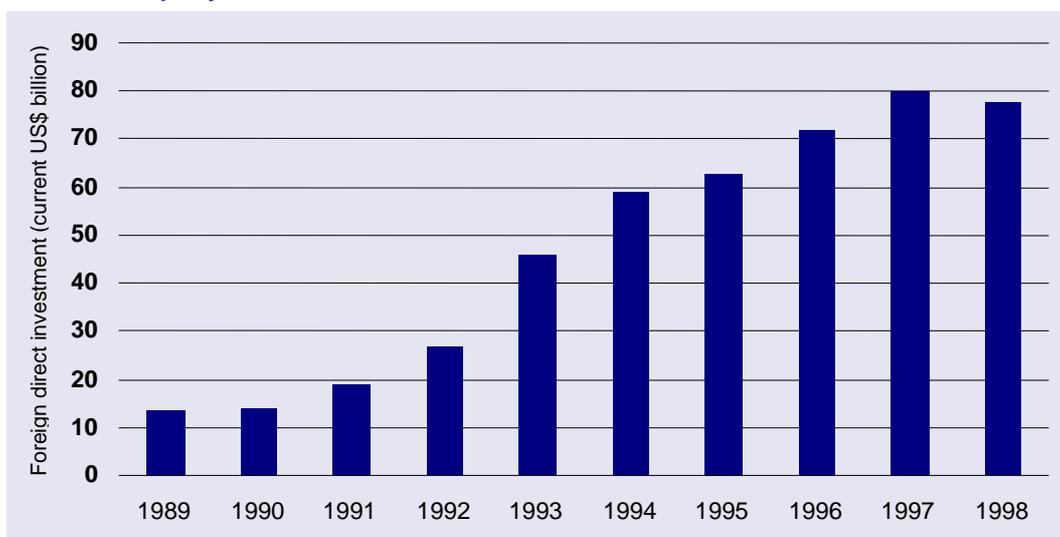
Lower income APEC economies have been particular beneficiaries, with foreign direct investment growing by a staggering 475 per cent over the period 1989–98 (chart 2.7), even though foreign direct investment did falter during the Asian financial crisis.

Chart 2.6 **APEC inflows and outflows of foreign direct investment have grown rapidly**



Data source: See technical note 3.

Chart 2.7 **FDI flows to lower income APEC economies have grown particularly rapidly**



Data source: See technical note 3.

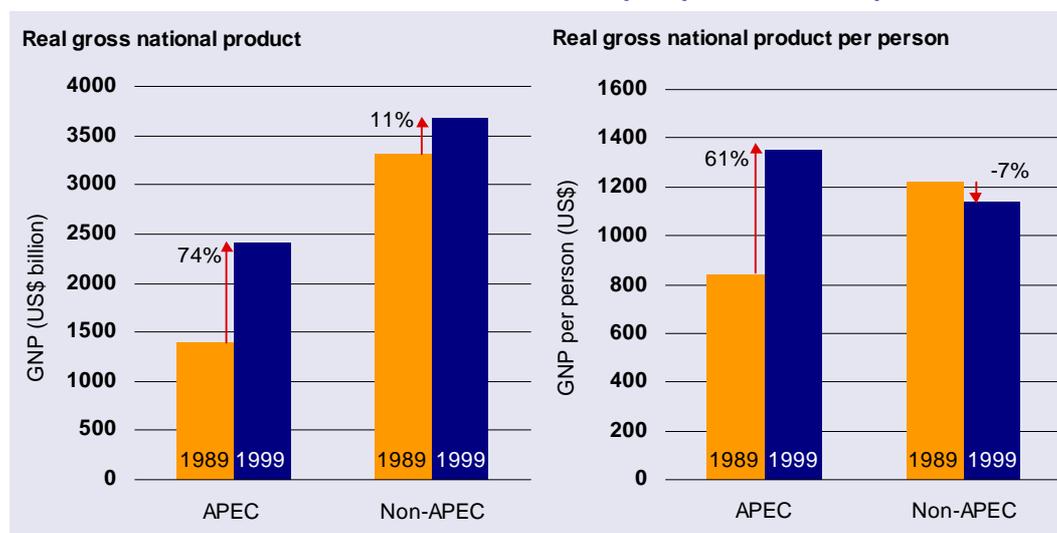
## Liberalisation and integration have brought strong economic growth ...

APEC liberalisation has been delivering the expected returns. The combined real GNP of APEC economies has grown by about a third since APEC was formed, and member economies have grown faster as a group than have non-APEC economies. Lower income APEC economies have grown by 74 per cent, much more rapidly than their counterparts elsewhere in the world (chart 2.8).

APEC economies have not only grown rapidly, but their growth has far outstripped population expansion, so that GNP per person has increased substantially (by 16 per cent for high income economies and by 61 per cent for lower income economies). So over the past decade APEC economies as a group have become much bigger and much richer on a per person basis. In this regard lower income APEC economies have done much better than their counterparts elsewhere (chart 2.8).

APEC liberalisation is expected to continue to deliver strong economic growth. A recent study (APEC 1999) estimated that commitments made by APEC economies as part of the Uruguay Round Agreement, when fully implemented, could add some US\$114 billion a year (in 1997 prices) to regional GNP by 2010. And APEC liberalisation beyond the Uruguay Round promises to deliver far greater growth. When APEC economies reach their stated goals of free and open trade and investment in the APEC region, the gains could reach US\$515 billion a year (see technical note 5).

Chart 2.8 Lower income APEC economies have prospered over the past decade

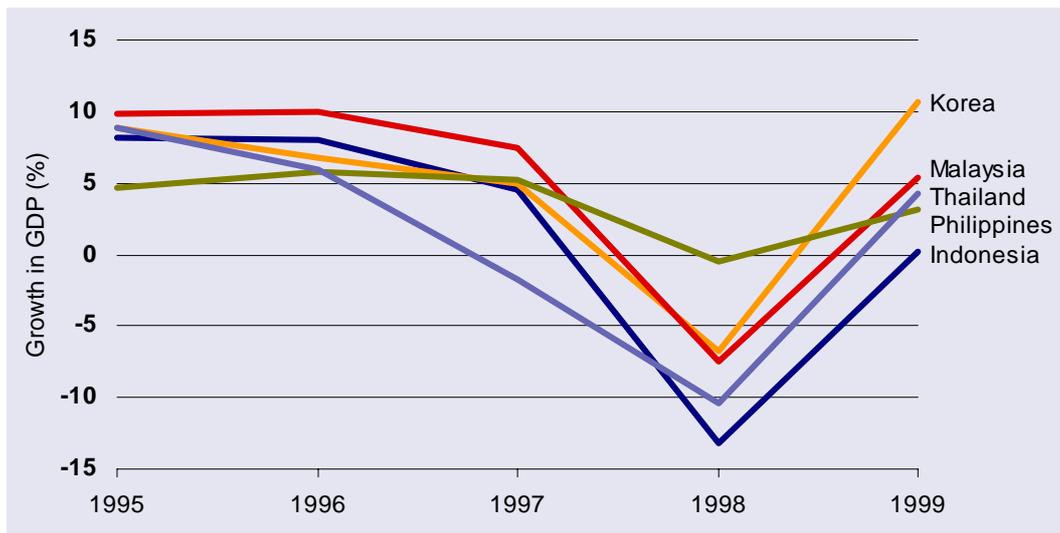


Data source: See technical note 4.

## ... and are facilitating recovery from the financial crisis

The economies most affected by the Asian financial crisis are now experiencing a strong cyclical recovery (chart 2.9). While fiscal stimulus provided the initial basis for recovery, strong improvements in the volume and value of exports, supported by real exchange rate devaluations and growth in export markets, now lie at the core of better economic performance. The firm resolve of economies not to resile from maintaining and deepening their open trade and investment policies is a key reason why rapid export-led recovery has been possible in the region.

Chart 2.9 APEC economies are rebounding from the Asian financial crisis



Data source: IMF (2000).

## APEC contributes to open trade and investment in the region

The impressive achievements recorded by APEC member economies over the past decade are principally a result of individual APEC member economies choosing, through both multilateral trade negotiations and unilateral action, to liberalise their trade and investment regimes. However, APEC as an economic grouping has made a very important contribution to the ability of its members to pursue open trade and investment policies. APEC's contribution has been manifest in several ways.

### **APEC has contributed to the multilateral trading system ...**

APEC has made a valuable contribution to the continuing health of the international trading system. When APEC was formed in 1989, the Uruguay Round negotiations were stagnating and there was concern that, if the round did not proceed expeditiously, the world economy could fragment into competing exclusionist regional trading blocs. The Joint Statement of the First APEC Ministerial Meeting, issued in Canberra on 7 November 1989, made clear the common commitment of APEC members to an open multilateral trading system and their concern to '*unblock any obstacles to a comprehensive and ambitious MTN result*'. The First APEC Economic Leaders Meeting, held at Blake Island in the United States in 1993, also played an important role in bringing the Uruguay Round to a conclusion by using the political and economic weight of the Asia-Pacific economies to that end.

APEC's founding principle is 'open regionalism' — regional cooperation that gives primacy to multilateralism and does not seek to form an exclusionist trade bloc. This means that APEC acts as a caucus or lobby group working in support of the multilateral trading system. It galvanises political support for progress at the multilateral level. Because APEC is a diverse group of developed and developing economies, and represents a large part of the global economy, its collective view is very important. Indeed, APEC strengthens the voice of the Asia Pacific in multilateral trade fora. APEC Economic Leaders expressed strong support for the launch of a new round in Seattle at their most recent meeting (in Auckland in September 1999) and suggested key features that should be included in the new round. And APEC Ministers Responsible for Trade reiterated the Auckland call for the early launch of a new round at their most recent meeting (in Darwin in June 2000) and announced some practical steps to facilitate the launch of a new round (box 2.2).

APEC also works as an incubator of ideas and a place to develop ideas and approaches to issues for use in the WTO. One example is work done in APEC on trade barriers in information technology, which formed the basis of the WTO Information Technology Agreement. Another example is work done in APEC on trade facilitation, on regulatory reform and on competition policy now being used in the WTO as it begins its work on these issues.

Another contribution from APEC to the multilateral trading system is in the area of training and capacity building. APEC has a proud tradition of helping developing APEC economies to implement and benefit from the multilateral

**Box 2.2 Key points in recent APEC statements on multilateral trade negotiations**

**APEC Economic Leaders' Declaration 'The Auckland Challenge', Auckland, 13 September 1999**

- Agreed to give the strongest possible support at Seattle to the launch of a new round.
- Agreed that the round should be comprehensive, have a balanced and sufficiently broad-based agenda, and be concluded within three years as a single package.
- Supported the abolition of agricultural export subsidies and unjustifiable export prohibitions and restrictions as part of the negotiations.
- Made a commitment not to impose new or more restrictive trade measures for the duration of the negotiations.

**Statement of the Chair, Meeting of APEC Ministers Responsible for Trade, Darwin, 7 June 2000**

- Reaffirmed their commitment to the APEC Leaders' Declaration in Auckland in order to increase momentum toward the launch of a round.
- Announced a new strategic plan to build the capacities of developing APEC economies to participate in a new round through technical assistance to help them to implement WTO agreements.
- Called for preparatory work on industrial tariffs and other related areas to begin in the WTO as part of the preparation for the new round.
- Announced an APEC-wide moratorium on the imposition of customs duties on electronic commerce transmissions until the next WTO Ministerial Conference.

trading system. A particular example relates to intellectual property rights. The announcement by APEC Ministers Responsible for Trade in Darwin, June 2000, of a strategic plan for capacity building to assist with implementing WTO agreements reinforces and consolidates this aspect of APEC's work.

All of these efforts by APEC have helped to strengthen the multilateral trading system and thereby contributed to the benefits of trade liberalisation that APEC economies have enjoyed.

**... while encouraging its members to open further ...**

While pursuing open markets through the multilateral trading system, APEC has encouraged and facilitated continuing individual trade and investment liberalisation beyond the WTO commitments.

At the second APEC Economic Leaders Meeting in Bogor, Indonesia, on 15 November 1994, the Leaders issued a Declaration of Common Resolve which included, among other things, a '*commitment to complete the achievement of our goal of free and open trade and investment in the Asia Pacific no later than the year 2020*'. Recognising the different levels of economic development among APEC member economies, the Economic Leaders agreed that industrialised economies would achieve this goal no later than 2010, and developing economies no later than 2020. These 'Bogor goals' have been the bedrock of APEC's efforts to promote individual trade and investment liberalisation by member economies.

In order to monitor progress towards these goals and to encourage a process of continuous liberalisation, APEC economies agreed to report their progress on an annual basis across 15 policy issues set down by Leaders in 1995 in the Osaka Action Agenda. These reports, known as Individual Action Plans (IAPs), have become the primary vehicle for encouraging economies to individually adopt market-opening measures. The IAP system was further enhanced by a process of peer review, in which each economy receives comments on its IAP and suggestions on how to improve its trade and investment regime from other economies. This system has been an important contributing factor supporting the liberalisation by APEC member economies beyond their Uruguay Round commitments referred to previously.

In 1999 APEC Ministers and Leaders called for the IAP system to be strengthened with a view to making IAPs more comprehensive, transparent and specific. In response, APEC economies have adopted a more rigorous IAP system, incorporating a standardised reporting format with common reporting criteria. These improved IAPs will be made available on-line over the internet from the 2001 reporting cycle, further sharpening the IAP as a mechanism to encourage unilateral and voluntary trade and investment liberalisation.

APEC economies have also sought cooperative approaches to opening their trade and investment regimes. In 1997 and 1998 APEC economies undertook some important work to identify priority sectors in which to pursue early liberalisation. The Early Voluntary Sectoral Liberalisation process identified 15 priority sectors for future liberalisation efforts and focused on four main elements — tariffs, non-tariff measures, trade facilitation and technical cooperation. The tariff elements of these 15 priority sectors were referred to the WTO for consideration as part of a future comprehensive negotiation, while the other elements are being taken forward in a variety of APEC fora. In addition, the

key APEC subfora working on trade and investment liberalisation — the Market Access Group, the Group on Services and Investment Experts Group — continue to work collaboratively to help member economies to pursue their liberalisation goals.

### **... and facilitating the implementation of market-opening policies**

An important reason why APEC has succeeded in encouraging member economies to further liberalise their trade and investment regimes is the comprehensive approach taken to liberalisation. APEC members recognised at an early stage that work on liberalisation needed to be complemented by concerted efforts to facilitate trade and investment and technical assistance to build the capacity of its members to implement open market policies. This integrated approach is one of APEC's greatest strengths.

Through a series of Collective Action Plans, APEC has substantially improved the capacities of APEC members to liberalise and to take full advantage of the trade opportunities offered by open market policies. For example, APEC has concluded mutual recognition agreements on a number of major traded goods (including the world's first such agreement for telecommunications equipment and an agreement for electrical and electronic equipment). These mutual recognition agreements have substantially reduced the cost of complying with local technical standards, and so have encouraged trade. Considerable work has also been done to streamline customs procedures, and APEC economies are leading the way in developing paperless trading — electronic lodgment and processing of customs documents — saving considerable time and money. The process of doing business has also been made easier with the introduction of the APEC Business Travel Card, effectively a pre-approved visa for approved business executives that is valid for travel to all participating APEC economies. These practical steps have made an important difference to the way business is done in the APEC region.

A key element of the Collective Action Plans has been that measures to open and facilitate trade and investment have been matched by technical assistance to ensure that all members are able to implement and therefore reap the full benefits of open markets. The work programs of all APEC fora include projects that provide technical assistance directed at achieving equitable access to the benefits of open markets. The Energy Working Group, for example, provided training for energy regulators on structural reform and organised a workshop on

environmentally sound energy infrastructure. Subfora of the Committee on Trade and Investment have also mounted training programs on topics ranging from the implementation of the harmonised system for customs classification to a workshop on public sector reform. These projects help to build the capacities of APEC member economies to implement and benefit fully from APEC trade and investment liberalisation and trade facilitation efforts.

### **3 Greater growth by getting the domestic environment right**

The link between open trade and investment policies and sustained economic growth is clear. There is mounting evidence around the world that open economies achieve higher rates of productivity growth, which in turn fuels economic growth. But there is also clear evidence — and the Asian financial crisis provides compelling lessons on this — that openness without good public and private sector governance and continued microeconomic reform will not assure sustained improvements in national prosperity. The crisis exposed the risks from not refining systems of governance and broader policy and institutional frameworks to maintain robust financial and corporate sectors and strong and responsive public sector management. And the challenges facing economies making the transition from central planning are emphasising the role of strong market institutions.

There is a strong link between governance and economic performance. Economic liberalisation must be embedded in an effective system of governance if risks are to be managed and economic and social development assured. In an increasingly integrated world there are more avenues for consumers, producers and investors to respond both positively and negatively to policy and institutional developments. Open trade and open financial and capital markets can raise the costs of poor economic governance. Loss of investor confidence due to poorly developed institutions, weak cultures of corporate governance and inappropriate systems of regulation and supervision can be transmitted rapidly into a contraction in the availability of finance in an economy, with possibly quite drastic implications for output and employment.

Most economies adopting more open trade and investment policies are also pursuing broader based microeconomic reform. Much of this reform has been targeting the remaining regulatory barriers to competition, increasing the efficiency of delivering public goods and services, reducing the distorting effects of taxation and concentrating the efforts of the public sector on those areas that only governments can deliver effectively.

## **Microeconomic reform is a necessary adjunct to trade and investment liberalisation**

Microeconomic reform has been pursued in part because of the direct benefits it can generate, but it has also been seen as a necessary adjunct to trade and investment liberalisation. There is strong evidence, for example, that the benefits of foreign investment are optimised when the policies of host economies promote competition. And reducing domestic transaction and service costs helps local enterprises to better meet international competition.

Microeconomic reform helps local enterprises to take better advantage of the opportunities created by trade and investment liberalisation. But it also serves to increase the efficiency with which the economy generates the goods and services that people want. Through such reform governments are seeking to deliver higher quality public services at a lower cost to taxpayers and with greater transparency. By removing regulatory impediments to competition and fostering better corporate governance, economies are facilitating domestic innovation, greater responsiveness to consumer needs, and a more favourable environment for investment and growth. Microeconomic reform is ultimately about ensuring that the economic system delivers the goods and services that people need at the lowest cost.

Microeconomic reform is particularly necessary if economies are to reap the benefits of the advances in information and communications technology that are transforming the global economy. The so-called ‘new economy’ and the quick access to information that it provides offer the potential for rapid increases in productivity through the adoption of new technology in developing as well as developed economies. But the domestic environment for innovation and new technology will need to adapt if this potential is to be realised and the ‘digital divide’ is to be bridged. Special emphasis will also need to be given to developing human resources if economies and their people are to effectively participate in the new economy and gain the benefits of applying information and communications technology in all areas of economic activity.

Some microeconomic reform — such as removing impediments to labour mobility, capital relocation, enterprise formation and market entry — plays an important role in facilitating adjustment to change and so complements trade and investment liberalisation. But many economies are also adopting and refining social safety nets to address the needs of people lacking the capacity to

take care of their own welfare, along with social investment programs designed to help people acquire the skills needed in a changing economy.

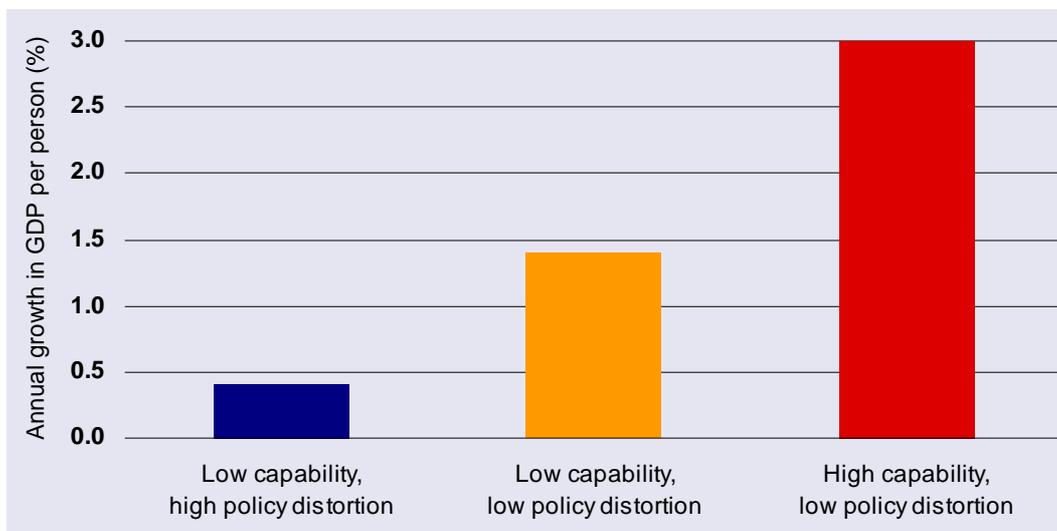
## Stronger institutional capacity leads to higher growth

Research undertaken at the World Bank (1997) shows that economies with stronger institutional capability have grown at twice the rate of those with lower capability (chart 3.1).

Of greater importance is that economies with high institutional capability as well as better policies grew at nearly eight times the rate of those with low institutional capability and a high degree of policy distortion. Good policies and more capable institutions to implement them produce better results. Inappropriate policies and weak institutions impede sustainable economic growth, poverty reduction and social development.

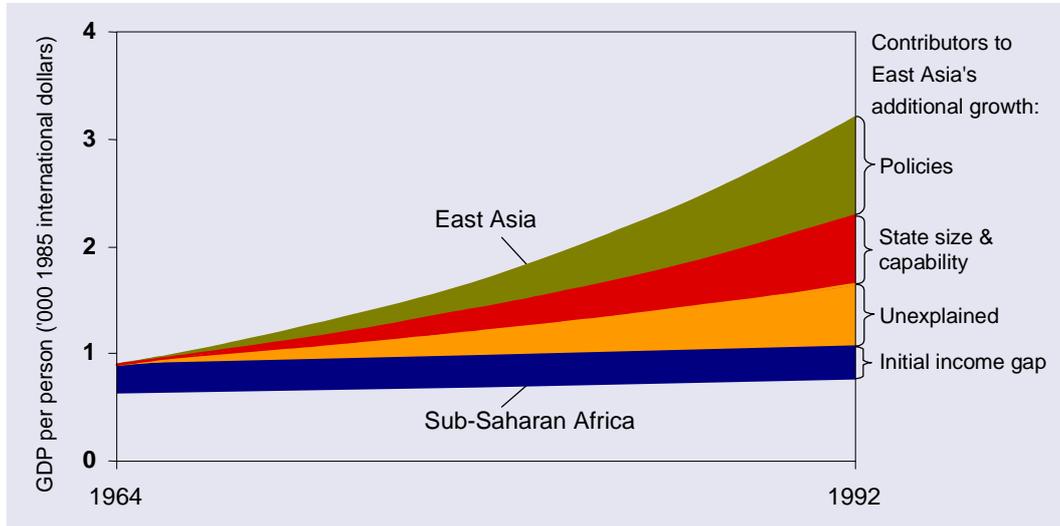
Another example of the importance of good policies and capable governments is provided by a comparison of the performance of East Asian economies and those of sub-Saharan Africa. After controlling for variables such as initial income and education, researchers found that better policies — including openness to trade and investment, the absence of price distortions, and high levels of education and investment — and better state capabilities explain the largest part of East Asia's superior economic performance from 1964 to 1992 (chart 3.2). Of the 320 per cent

Chart 3.1 **Economies with good economic policy and strong institutional capability grew up to eight times faster between 1964 and 1993**



Data source: World Bank (1997).

Chart 3.2 **Better governance helps to explain the income gap between East Asia and Africa**



Data source: World Bank (1997).

difference between the average income per person in East Asia and Africa in 1992, about two-fifths can be attributed to better policies since 1964 and over another fifth to better state capabilities (although there is a range of performance within both regions).

Good governance is not only important for economic progress; it is also essential for progress in social development. The provision of public health, infrastructure, social amenities and other public goods requires government to intervene either by directly providing the public good or service or by assigning property rights and creating a 'market' for private operators. Effective and efficient delivery of these services thus depends on the quality of governance in both the public sector and the private sector.

### **APEC economies are improving their economic governance**

APEC economies have been working hard to improve governance, especially in the aftermath of the Asian financial crisis. A survey of economic governance capacity building submitted to the 1998 Leaders Meeting as part of APEC's response to the crisis showed that economies were working to address a range of governance needs that had been exposed (CIE 1998a). Crisis-affected economies are all acting (often with the cooperation of other APEC members) to strengthen financial and corporate sector governance. This includes restructuring distressed

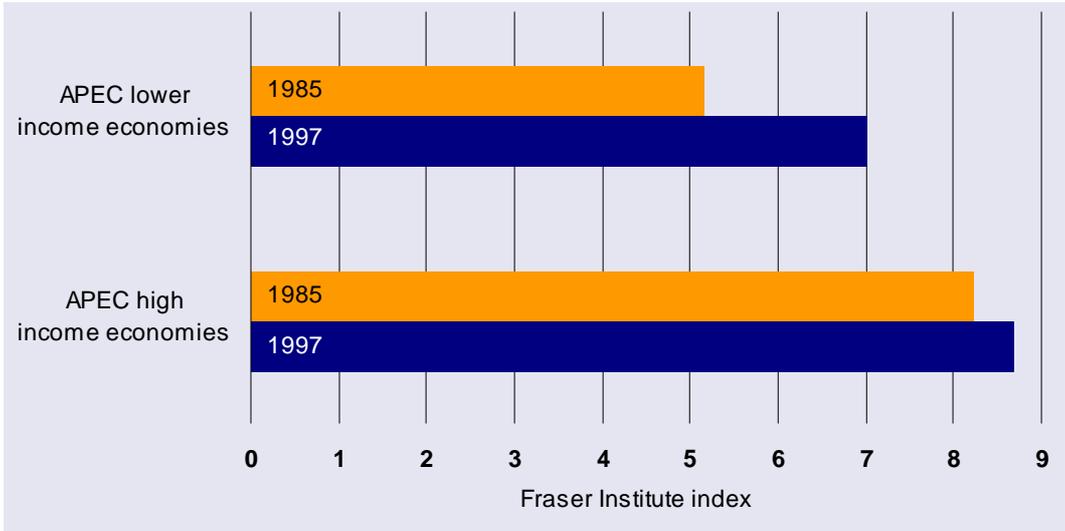
financial institutions and buttressing the institutional framework for prudential regulation and supervision, and strengthening business law and the legal and judicial systems for the enforcement of this law. Many economies are also strengthening the management of public finances and developing frameworks for privatising and commercialising state-owned business enterprises. Also linked to changes in public sector management are efforts to improve economic forecasting and the assessment of policy options, to strengthen social safety net systems and to implement public administration and civil service reform.

There are no simple measures of good governance and appropriate institutions, but some measures do reflect market and institutional judgments about the quality of governance across economies.

One well-known index, published by the Fraser Institute, placed nine APEC economies in the twenty (out of 123) highest ranked economies in 1997 (Gwartney, Lawson and Samida 2000). According to this index — which reflects aspects of government expenditure, monetary policy and price stability, access to foreign currencies, legal structures and property rights, and controls on international trade and exchange and on capital and financial markets — the ratings of APEC economies improved during the period 1985–97 (chart 3.3).

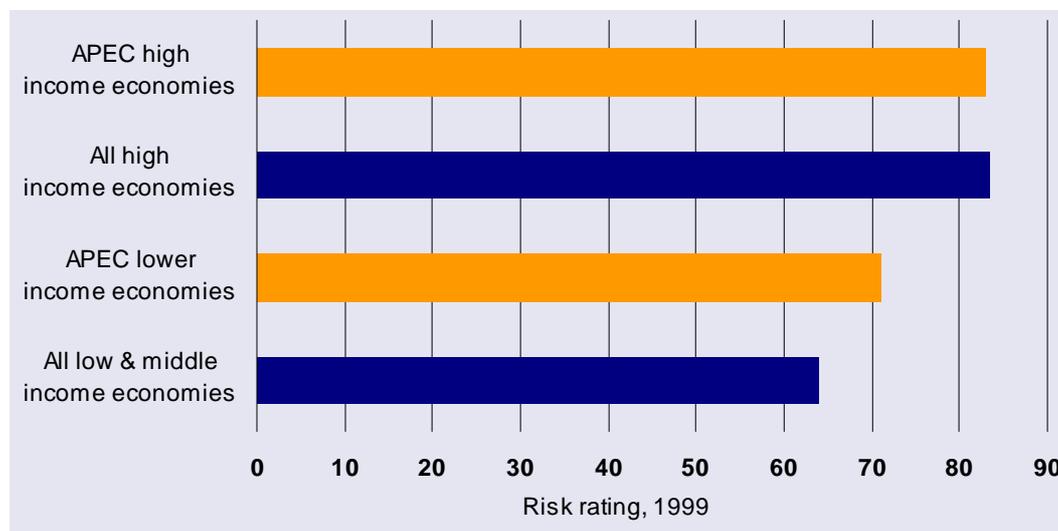
APEC economies also have good risk ratings. As chart 3.4 shows, risk ratings for these economies are low, reflecting lower expectations of default on debt — a measure of the market valuation of the quality of governance.

Chart 3.3 One measure shows governance is improving in APEC economies



Data source: See technical note 6.

Chart 3.4 APEC economies have good risk ratings



Data source: See technical note 7.

## Microeconomic reform strengthens APEC economies ...

For many APEC economies, liberalisation of trade and foreign investment has been just one part of a much broader program of microeconomic reform. The financial crises experienced by some economies have led to considerable attention being focused on the structure of financial systems and their regulation and supervision; they have also focused attention on legal and judicial frameworks surrounding the contracting and enforcement of debt and other financial transactions. Taxation and public expenditure management reforms have also been common, as economies have addressed the incentives for private investment and activity created by tax policies and their administration, and have sought more efficient ways of delivering social services and addressing market failures.

Significant reforms have occurred in the financial sectors of APEC economies affected by the Asian financial crisis. These economies were quick to establish or reinvigorate institutions to deal with the restructuring of corporate and financial sectors, including agencies for voluntary corporate debt workouts, asset resolution and bank recapitalisation. They also took steps to restructure financial systems, including closure, state takeover and government-supported mergers. Different economies have adopted different approaches to restructuring their financial sectors. For example, Thailand and Korea have employed an early closure option with weak and non-viable banks and finance companies. Malaysia, on the other

hand, has not closed any financial institutions and is relying on mergers with good banks to resolve problems with poorly performing banks. This restructuring has been accompanied by moves to strengthen the capacity of government regulatory agencies to supervise participants in the financial sector. These economies have also implemented a range of policy reforms to facilitate a market-based reallocation of assets to more productive uses (World Bank 2000c). These reforms have included policies facilitating mergers and acquisitions and encouraging foreign direct investment, bankruptcy procedures, and improved corporate governance (including better accounting standards).

Over the past two years Indonesia has tackled a number of difficult reforms of its financial and judicial system. It has amended a range of laws including the Company Law, the Anti-Monopoly Law, the Consumer Protection Law, the Bankruptcy Law and the Banking Law. Changes have been made with the aim of improving transparency and clarifying roles and obligations of parties while promoting competition. Indonesia has also established a National Law Commission to guide legal reforms and a National Commission for Good Governance, which has the task of drafting a Code of Good Corporate Governance.

Thailand has also reformed its legal framework governing the corporate sector. The Thai Government has introduced two broad initiatives:

- a stronger legal framework for the recovery of non-performing assets by improving the legal regime for insolvency; and
- a process for voluntary out-of-court settlements.

The Thai Government is also continuing to strengthen its corporate regulatory regime by improving the institutional framework for accounting and auditing practices, improving the quality and reliability of corporate financial and non-financial information, strengthening the role of boards of directors and intensifying enforcement of the regime.

A number of APEC members have reformed their systems of taxation with a view to strengthening their tax bases and reducing distortions to incentives from existing taxes. The introduction of a value-added tax has been a common reform, with Papua New Guinea, Viet Nam and Australia introducing such a consumption tax in recent years. Value-added taxes in these economies have typically replaced distorting taxes such as turnover or wholesale sales taxes, which have unpredictable effects on incentives.

Restructuring of utilities and related regulatory reform, especially of those utilities once dominated by the public sector, have been priorities for some economies, many of which have also pursued regulatory and legislative changes to facilitate greater private sector involvement in the provision of infrastructure. At the same time, close attention has often been paid to competition policies, concerned both with the regulation of anticompetitive conduct and the elimination of unwarranted legislative and regulatory constraints on competition.

The telecommunications sector has been a common area of reform in APEC economies. New Zealand, Australia and Peru, for example, have privatised state operators and opened their markets to competition. These economies have seen a rapid expansion in services, improvements in quality and reductions in price. This has had a flow-on effect to business in terms of lower costs and increased productivity. Other infrastructure such as airports and electricity has also been opened up to private participation in APEC economies. New Zealand has corporatised and, in some cases, privatised its major airports. Similarly, China and Thailand have allowed private airport development. For some economies with extensive state involvement in business, privatisation has extended beyond infrastructure. Peru, for example, has privatised state enterprises in the financial, fishing and mining sectors, and has introduced a private pension system as an alternative to the public system.

A number of APEC economies have undertaken broad-based regulatory reform aimed at reducing administrative barriers to entry into markets and compliance costs for industries. One example of competition policy and regulatory reform is Australia's National Competition Policy process of reviewing all laws and regulations that restrict competition. It has subjected large sections of federal and state government legislation to public investigation of the effects of regulatory constraints on competition, subjecting them to a strong public benefit test.

Another example is in Korea where the Regulatory Reform Committee was established to build a foundation for more fundamental, enduring and systematic regulatory reform. In its first year of operation (1998) the committee scrapped 48 per cent of the existing administrative regulations and improved a further 22 per cent (OECD 2000a).

Japan has also pursued regulatory reform based on the principles that:

- the economic arena should be deregulated, and social safety net, environmental and consumer protection regulations should be minimised to avoid over-intervention by government;

- where regulation is necessary, it should allow for maximum private initiative and efficiency;
- regulation should be stated as explicitly and simply as possible;
- regulations should be made as internationally compatible as possible; and
- the process of making regulations should be transparent.

Regulatory reform began in Mexico in 1989 as a complement to the process of trade liberalisation, which started in 1986. In the following decade, most state enterprises were sold, and entry, exit and pricing for nearly all tradable goods and services were deregulated (OECD 2000b). Framework laws covering standards, competition, foreign investment, civil and commercial judicial procedures, bankruptcy and collateral requirements were enacted or reformed, and an independent regulatory improvement commission was established.

Economies have also undertaken industrial relations and workplace reforms to increase labour market flexibility. Peru has reformed labour market legislation, and Australia has implemented wide-ranging changes in the regulations framework for labour–enterprise relations.

The scope of microeconomic reform has varied considerably across APEC economies, reflecting their diversity — historical, cultural and institutional. But there have been common themes of increasing competition and facilitating a stronger role for the private sector. Some economies have fundamentally changed their approaches to property rights. Peru, for example, introduced land rights legislation and accompanying regulations to help secure the property rights of rural landowners. In economies moving from central planning to a market orientation, reforms have been extraordinarily wide ranging (box 3.1).

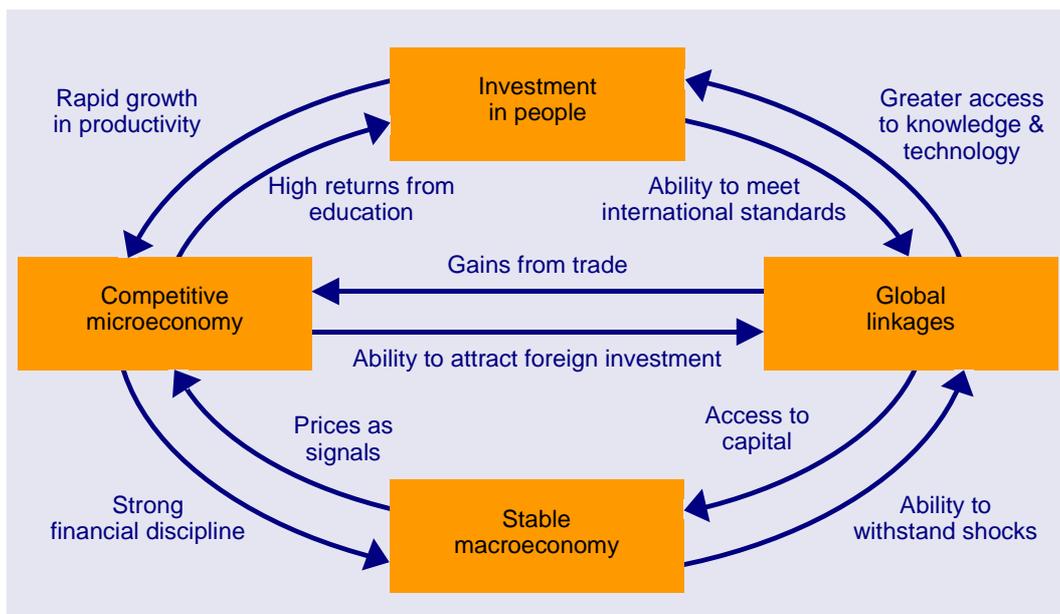
The pursuit of these reforms in APEC economies reflects a strong appreciation of the critical role that a competitive microeconomy plays in securing growth and social development. Along with a strong focus on macroeconomic stability and policies to encourage human resource development, economic integration and the pursuit of a competitive microeconomy have proven to be the main keys to socioeconomic development (chart 3.5). Microeconomic reform aimed at increasing the efficiency with which resources and factors of production are used in the economy has involved deregulation to promote competition as well as privatisation in sectors previously occupied by the public sector. But it has also involved a strengthening of the role of government in addressing market failures and in ensuring the smooth and efficient operation of the market system by securing the foundation of property rights and the rule of law.

#### Box 3.1 Microeconomic reform in Viet Nam

While all APEC economies have been implementing some microeconomic reform, those making the transition from central planning are addressing quite comprehensive policy and institutional transformations.

This is the case in Viet Nam. Its transition to a market economy has included reversing the collectivisation of agriculture by granting individuals and families long-term rights to use land, liberalising prices and removing barriers to internal trade. Steps have been taken to create a modern banking system, by splitting off the commercial banking functions of the State Bank, facilitating the establishment of new foreign and domestically owned banking entities, and developing a supervision and regulatory system. Foreign investment and international trade have been liberalised, accompanied by efforts to formalise entry to the multilateral and regional trading system and to regularise bilateral trading and investment relations. The foreign exchange market has been reformed and a market-determined exchange rate system has been adopted. Reform of the state enterprise system has been initiated and formal acceptance of the private sector has been embodied in the constitution. Steps have been taken to create a legal system for the functioning of a corporate sector. Finally, budgetary reform — the adoption of a revenue-raising system based on taxation and the adoption of a more formalised system of planning and controlling budgetary expenditure — has been part of broader reform of the public administration.

Chart 3.5 Policy choices affect socioeconomic development



Source: Based on World Bank (1991).

## **... as all economies respond to the challenge of adjustment ...**

The Asian financial crisis underscored the importance of adequate and appropriate measures to facilitate adjustment and to address the impact of economic downturns and policy change on the wellbeing of those who are poorly equipped to absorb shocks affecting their livelihoods.

The evidence shows that, except in some transition economies, the costs of adjustment to liberalisation are typically small, especially when considered relative to the benefits (see box 3.2). However, economies have found that structural adjustment measures can be useful in easing some consequences of trade liberalisation and microeconomic reform, particularly when certain sectors have long been dependent on protection from competition, or in some cases are located in regions where alternative employment opportunities are limited. Adjustment packages have included such things as notice of impending policy changes; phased changes in policy; assistance for skills development, job search and relocation; direct job creation programs and wage subsidies; and outright compensation for owners of factors of production affected by change. At the same time, continued economic reform to remove institutional and regulatory

### **Box 3.2 Adjusting to liberalisation**

While fears are frequently expressed about the adjustment costs of liberalisation — and there is no doubt that some individuals and firms can be losers — the evidence suggests that, except in some economies undergoing a rapid transition from central planning, the costs of adjustment to liberalisation are relatively small. A review of some 50 studies of trade liberalisation in developed and developing economies found that, in developing economies, manufacturing employment usually increases (or the decline is very small) one year after liberalisation. This was because (Matusz and Tarr 1999):

- developing economies typically have a comparative advantage in labour-intensive manufacturing, so trade liberalisation should favour labour;
- there are usually many interindustry shifts in activity after liberalisation, which minimises the dislocation of factors of production;
- in many industries, normal turnover exceeds dislocation from trade liberalisation so that downsizing where necessary can be accomplished without much forced unemployment; and
- in economies where small and medium-sized enterprises play a significant role, the typical dynamism of these enterprises means that there is a quick response to new opportunities.

impediments and disincentives to adjustment plays an important part in facilitating positive responses to change.

In APEC economies labour market adjustment programs form an important part of the measures for dealing with the consequences of policy change. These programs include:

- policies to match the unemployed to existing jobs
  - Australia, Chile, Chinese Taipei, Japan, the Philippines, Singapore, the United States and Hong Kong, China all have job information and job matching programs and provide job search assistance; and
  - nearly all economies provide job training and/or educational subsidies.
- policies to create new jobs
  - Indonesia, Japan, Korea, Malaysia, the Philippines, Thailand, Viet Nam and Hong Kong, China use public employment programs as a means of providing employment opportunities for retrenched workers;
  - Japan, Chinese Taipei and the Philippines provide wage subsidies and/or employment credits; and
  - Australia, Indonesia, Japan, Korea, Malaysia, the Philippines, Singapore, Chinese Taipei, Thailand, Viet Nam and Hong Kong, China are implementing a variety of initiatives to promote employment growth in the private sector, directed largely at enabling the establishment of small and medium enterprises.
- programs to provide for the needs of affected individuals
  - Most economies are implementing some kind of social safety net for individuals, including government loans, employment insurance, safety net programs and community-based programs.
- workplace programs to improve productivity, ease restructuring and enhance abilities to respond to uncertainty
  - Several economies are making efforts to institute workplace practices by, for example, improving the flow of information between affected firms and workers, improving employer–employee relations, making firms aware of alternatives to retrenchment and promoting exit policies to smooth the transition for retrenched workers.

The regional crisis brought into sharp focus the issue of social safety nets to protect vulnerable groups from adverse developments. In many lower income economies, family and community resources have been the main buffers against adversity, but governments are now moving to develop more formal safety net

**Box 3.3 Key principles of Thailand's social safety net**

Thailand's social safety net emanates from the Eighth Development Plan (1997–2001), which has an objective of establishing:

... systems of social security in which all Thai citizens are guaranteed access to basic social services, social and labour welfare, safety in life and property, safety in the workplace, and protection of civil rights. (p. 43)

This plan changed the emphasis of government planning, devolving responsibility for identifying needs and financial management and delivering services to the community level.

Thailand's social security system includes the following key principles:

- Developing social and welfare systems that support an improved quality of life:
  - streamlining the social welfare system, including linking all providers of social welfare (public sector, private sector, and non-governmental organisations) at central and local levels, reducing the public sector's role to a facilitator and supervisor rather than principal actor, and streamlining administration procedures for non-governmental organisations and community organisations;
  - establishing a standardised labour welfare system, encouraging the private sector to provide labour welfare services such as medical centres and kindergartens, and promoting the establishment of company savings and provident funds as sources of welfare for workers during their working life and in retirement;
  - expanding and improving the social insurance system to cover child support and the contingencies of aging and those working in the informal sector, computerising services such as medical and compensation payments, and developing monitoring systems to ensure that eligible businesses and employees enter the social security system.
- Improving the efficiency of labour protection, workplace safety and labour relations:
  - accelerating and extending labour protection, including eliminating exploitation of child labour, improving systems involved in setting minimum wage levels, encouraging employers to formulate pay structures that allow for wage adjustments based on skills and experience, and improving workplace safety and working environments;
  - developing labour relations, including creating a trilateral consultation system for resolving labour disputes, and educating employers and employees to give them a better understanding of labour relations.
- Preventing and suppressing crime and drug abuse to maintain social harmony, by upgrading information systems and technology for crime prevention agencies, educating families and communities on drug issues and imposing harsher penalties for drug distributors.
- Improving prevention and relief systems for public emergencies and disasters.
- Upgrading the efficiency of the justice system and the protection of civil rights.

systems. In doing this, they are addressing the need to ensure that systems are cost effective, reflect local cultures and values, and introduce minimal distortions to the operations of the labour market. Lower income economies that do not have highly developed social insurance systems are putting together packages that include some or all of the following features:

- income generation through mechanisms such as employment programs;
- maintenance of food supplies using instruments such as food subsidies, nutritional supplementation programs and food-for-work programs;
- maintenance of expenditure on basic health services;
- preservation of human capital development by maintaining or increasing real education expenditure and targeted scholarship programs; and
- provision of retraining opportunities, job search support and other assistance to the unemployed.

The principles underlying the development of the social safety net system in Thailand are described in box 3.3.

### **... and prepare for the ‘new economy’**

The other challenge prompting a strong focus on microeconomic reform is the need for economies to position themselves to take best advantage of the opportunities created by the advances in information and communications technology that are transforming the global economy. The use of information technology is producing efficiency gains and innovation at an extraordinary rate, and is facilitating their diffusion in ways that were inconceivable a decade ago. The technology is accelerating the shift in the determinants of economic success towards learning and continuous innovation. While the so-called ‘new economy’ holds the potential for higher productivity across all sectors — not just in high technology or information technology enterprises — realising this potential creates challenges requiring significant responses from governments.

APEC economies are already achieving rapid increases in access to information technology. The number of people with access to the internet has grown quickly in high and lower income economies (chart 3.6). In the APEC region, some 246 million people are estimated to have access, accounting for around 65 per cent of the total world population with access to the internet. However, penetration in lower income economies is still quite low. Although the number of users in China has grown at an average annual rate of nearly 340 per cent in the past three years, only 1.3 per cent of the population currently has access.

Making the best use of information technology, and the opportunities for greater business efficiency and enhanced access to knowledge at all levels of society, requires economies to place considerable emphasis on human resource development. It also requires efforts to increase the flexibility of labour and product markets so that resources can flow to new industries. Governments will also need to implement further reforms to promote the overall climate for electronic commerce and investment by, for example:

- establishing competitive domestic telecommunications markets, adopting policies that promote high quality cost-effective internet access, allocating the electromagnetic spectrum on a technology-neutral basis; and
- avoiding barriers to electronic trade and removing regulatory, logistical and trade barriers in key sectors affecting electronic trade, such as customs, transportation, payment systems and delivery services.

Chart 3.6 Access to the internet has expanded rapidly in APEC economies



Data source: NUA Internet Surveys, [http://www.nua.ie/surveys/how\\_many\\_online/asia.html](http://www.nua.ie/surveys/how_many_online/asia.html), Accessed 21 September 2000.

Developing economies stand to reap considerable benefits from the new technologies. This is in part because of the significant productivity gains they can realise by buying the new technologies from the economies that develop them and copying established production methods — the traditional avenue of catching up. But further than this, the internet provides free access to an enormous range of information, and e-commerce looks to be reducing the optimal size that firms must reach to operate in global as well as domestic markets, by making it easier to buy in services. And reduced communication costs also make it easier for corporations to locate production facilities in economies with lower labour costs. But taking advantage of these possibilities places a high premium on establishing more effective legal frameworks for business and the protection of property rights, developing efficient financial markets, as well as opening markets for foreign trade and investment and liberalising the telecommunications sector.

### **APEC's work strengthens economic governance and supports microeconomic reform**

The Asian financial crisis highlighted the particular value of APEC cooperation in strengthening the capacity of economies to implement liberalisation and domestic economic reform. Negative perceptions about the quality of institutional aspects of economic governance played a particular role in the chain of events surrounding the crisis. Institutional impediments to a rapid response to the crisis and to actions to quickly restore confidence were factors in the subsequent contagion.

As the former Prime Minister of Thailand, Anand Panyarachun, noted:

... in our exuberance to reap the fruits of capitalism the need for such mechanisms [the checks and balances such as transparency and accountability] was unheeded.  
(ADB 1999, p. 1)

The crisis underlined the importance of capacity building to:

- strengthen economic governance, particularly in the banking, finance, regulatory and corporate sectors;
- deal with the social impacts of the crisis on vulnerable groups;
- help economies cope with the transition to more open and competitive markets through continued microeconomic reform; and
- build capacity for further reform.

APEC economies are heavily involved in cooperation activities directed at improving economic governance in the region and at supporting structural adjustment and microeconomic reform. This involvement is occurring through APEC initiatives, extensive bilateral programs and support for the programs and activities of the international financial institutions.

The scope to broaden APEC's work in this area is recognised in work programs for coming years. The crisis demonstrated that openness (broadly defined) is a necessary, but not a sufficient, condition for growth and prosperity. Thus the pursuit of APEC liberalisation objectives must be accompanied by actions to ensure that institutions of governance evolve to match changing demands and the imperative of managing risk. It must also be accompanied by ongoing efforts to create efficient, competitive and modern economies.

APEC cooperation is currently focusing on five priority areas: strengthening markets, e-commerce and technology cooperation, entrepreneurship and the development of small and medium enterprises, education and life-long learning, and social safety nets.

APEC's work on strengthening markets is concerned with:

- promoting greater transparency in corporate and public sector governance;
- enhancing the role of competition to improve efficiency and broaden participation by enterprises;
- improving the quality of regulation and the capacity for regulators to design and implement policies for sustainable growth;
- reducing compliance costs and facilitating business growth;
- building a favourable regional and international environment for free and fair competition; and
- promoting understanding of the policies needed for freer and more stable capital flows, including sound economic policies and policies to strengthen financial markets.

A significant part of APEC's work on governance has been developed through the APEC Finance Ministers process, which accelerated work on collaborative initiatives targeting the soundness of financial systems, the quality of corporate governance, and stronger accounting and financial reporting practices (box 3.4).

Many other aspects of work within APEC have also contributed — directly and indirectly — to the objective of strengthening markets, by facilitating the

evolution of stronger governance institutions in the region and supporting microeconomic reform and structural adjustment.

APEC's framework for cooperative policy development has led, for example, to the development of principles on investment, principles to guide competition and regulatory reform, energy policy principles to guide energy policy reform, and principles for government procurement. The non-binding principles on enhancing competition and regulatory reform endorse the concepts of non-discrimination, comprehensiveness, transparency and accountability. These principles encourage members to, among other things, review regulations that impede the ability of businesses to compete on the basis of efficiency and innovation, and address anticompetitive behaviour by implementing competition

#### Box 3.4 APEC Finance Ministers and international financial reform

As part of APEC's response to the Asian financial crisis, APEC Finance Ministers established a range of collaborative initiatives to strengthen regional financial and capital markets and to support freer and stable capital flows in the Asia-Pacific region. These included:

- strengthening financial market supervision and regulation by improving domestic training of banking supervisors and securities regulators and enhancing international cooperation in such training programs and holding a series of symposiums and training programs for insurance and pension regulators;
- assessing bank supervisory regimes, through a survey of key APEC economies which identified the need for closer contacts among APEC banking supervisors;
- improving bank failure management through policy dialogue involving APEC regulatory authorities;
- reforming pension systems, through regional fora and seminars;
- improving credit rating agencies and disclosure, through workshops on best practices for domestic rating agencies and surveys of codes of conduct in rating agencies;
- developing domestic bond markets, through surveys, workshops and preparation of a compendium of best practices and guidelines;
- strengthening corporate governance, through symposiums, reports and policy dialogue relating to raising corporate standards, improving insolvency law, and strengthening accounting and financial reporting;
- promoting capital account liberalisation consistent with macroeconomic and financial stability, through work on a Voluntary Action Plan for Supporting Freer and Stable Capital Flows;
- supporting privatisation, through the establishment of the APEC Privatisation Forum;
- encouraging best practice in public sector management reform; and
- developing a set of guidelines for cost-effective social safety nets that provide a buffer for vulnerable groups in times of crisis.

policy. The principles also exhort members to provide economic and technical cooperation to help build capacity in relevant areas in developing economies. APEC has also developed a cooperation framework for strengthening economic legal infrastructure, aimed at encouraging continuing regulatory and institutional reform. The framework is concerned in particular with building the capacity and skills of the legal profession in enforcing and applying corporate law and competition policy. APEC economic and technical cooperation activities and the work of the Human Resource Development Working Group have also targeted capacity building in important areas related to governance.

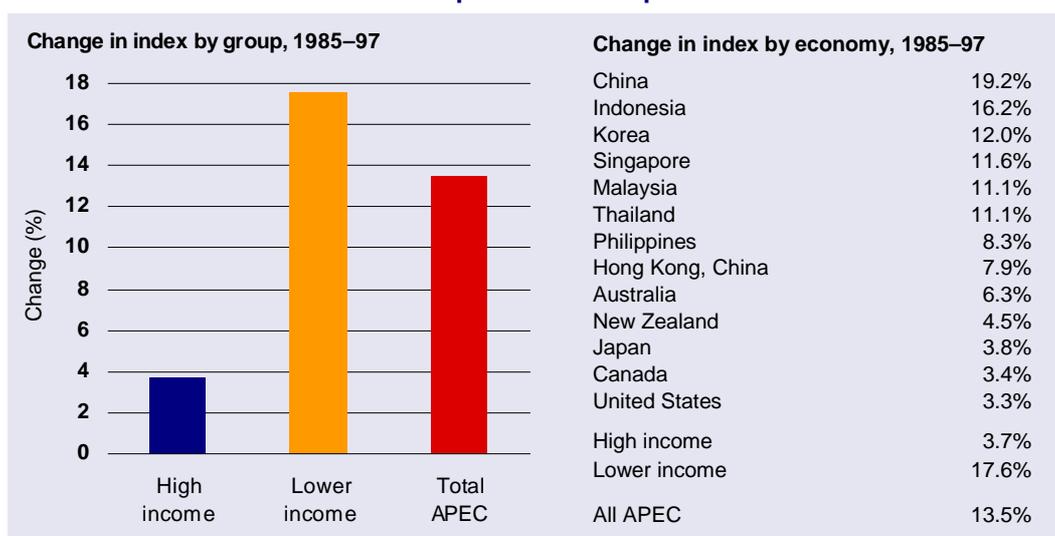
APEC is also taking a series of initiatives to facilitate effective participation in the new economy. This includes adopting principles on the interconnection of telecommunications networks and on international charging arrangements for internet services, as well as exploring issues in the preparation of electronic authentication policies. APEC has formulated a blueprint for action on electronic commerce, and members have agreed to a moratorium on customs duties on e-commerce transactions, as well as support for implementing systems of paperless trading. The Cancun Declaration of the APEC ministers responsible for telecommunications adopted a plan of action addressing issues of access to information and communications technology, human resource development, regulatory reform and liberalisation of telecommunications markets. APEC ministers responsible for education have identified strategic areas for transforming education systems to facilitate moves to become knowledge-based economies, including preparation for the use of information technology and harnessing its potential to enhance teaching and learning.

## 4 Open economies deliver social advancement

The primary reason why economies pursue open trade and investment policies is to help secure sustainable economic growth. Economic growth and increasing incomes are not the only ingredients for meeting the aspirations of an economy's people. But providing all of the other ingredients is difficult — especially in developing economies — unless strong growth is maintained. Without growth, government revenues are likely to remain stagnant, unable to support an expansion of social services and infrastructure facilities needed to improve human and physical capital. Growth may be associated with increasing income disparities, but without growth it is very hard to reduce the incidence and extent of poverty.

The pro-growth policies pursued by APEC economies are making it possible to deliver advances across the broader aspects of national development such as improved job opportunities, reduced poverty and better health and education. As chart 4.1 shows, the UNDP Human Development Index — a measure of social progress that reflects income, education and life expectancy — increased between 1985 and 1997 for all APEC economies for which data are available.

Chart 4.1 **Indexes of human development have improved in APEC economies**



Data source: See technical note 8.

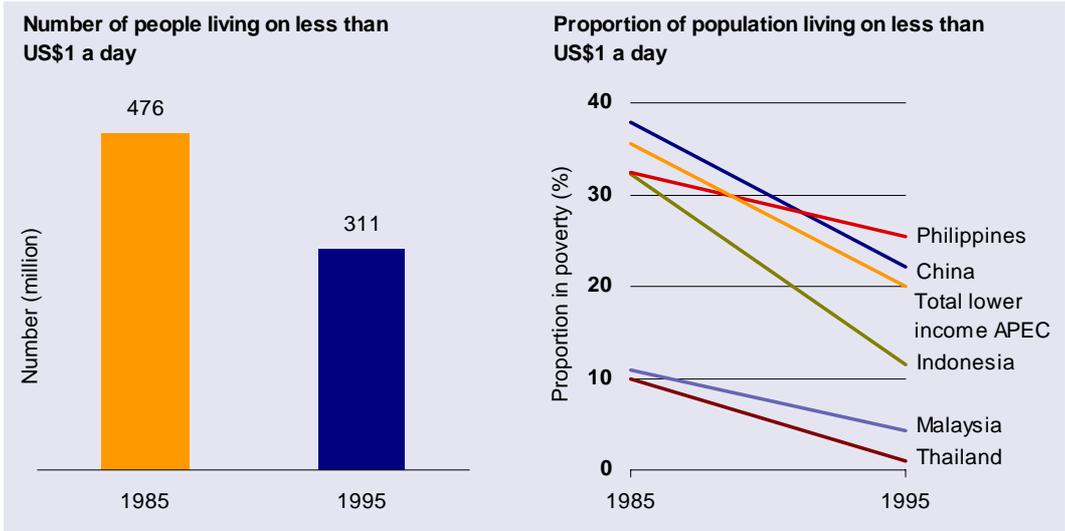
## Poverty is being alleviated

World Bank figures show that there have been large reductions in the incidence of poverty in APEC economies, particularly in East Asia. The absolute number and proportion of people living on less than the World Bank’s uniform poverty line of US\$1 a day fell sharply in East Asian APEC economies between 1985 and 1995 (chart 4. 2). The number of people living in poverty fell by about a third (around 165 million people). In Indonesia and China, the proportion of the population living in poverty fell by 65 and 41 per cent respectively.

Some new member economies, such as Viet Nam, have also achieved considerable success in reducing the incidence of poverty over the past decade according to this criterion. The measure shows, of course, changes in only one dimension of poverty. But the success of APEC economies in improving a broader range of social indicators confirms a positive story about the wellbeing of the poor, which has been affected, but far from reversed, by the recent increase in people living below the poverty line caused by the financial crisis (World Bank 2000b).

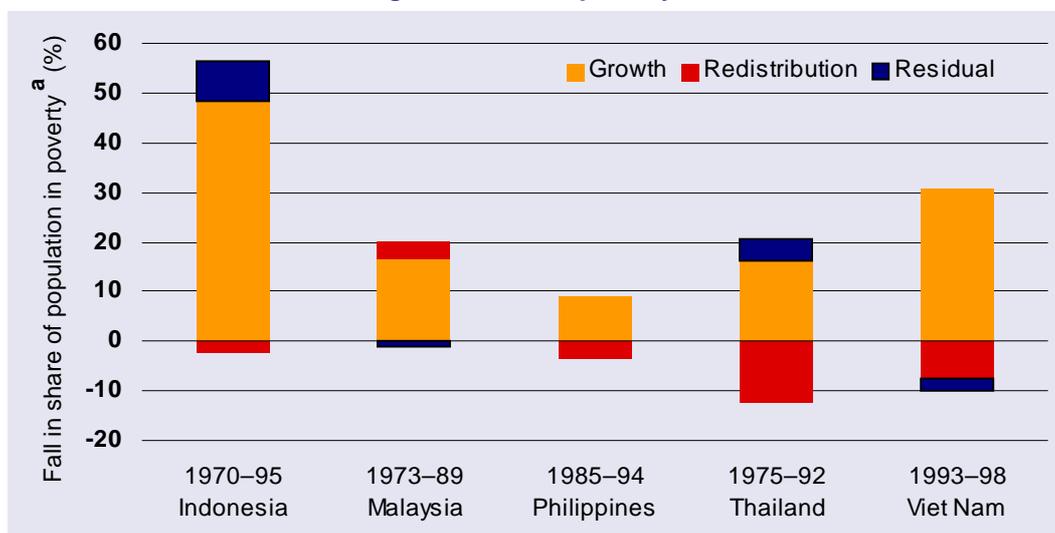
Most of this reduction in poverty is attributable to the strong growth of these economies. Chart 4.3 shows that economic growth has been the overwhelming force behind poverty reduction in many East Asian APEC economies. This

Chart 4.2 East Asian APEC members have been alleviating poverty



Data source: Ahuja et al. (1997).

Chart 4.3 Growth is the driving force behind poverty reduction



<sup>a</sup> Percentage of population living on less than US\$1 a day.

Data source: World Bank (1999b).

conforms to recent research, which shows that, contrary to some widely held views, growth is good for the poor. The evidence shows that, on average, every percentage point increase in average household consumption reduces the proportion of people living on less than US\$2 a day by about 2 per cent (World Bank 2000c).

In other words, the benefits of overall economic growth are felt quite strongly by the poorer parts of society. Economic growth has consistently led to rising consumption in the poorest fifth of the population in developing economies. World Bank analysis of growth and contraction experiences in 65 developing economies shows that, on average, growth in consumption by the poorest fifth tracked overall economic growth one-for-one in the 1980s and 1990s (World Bank 2000c).

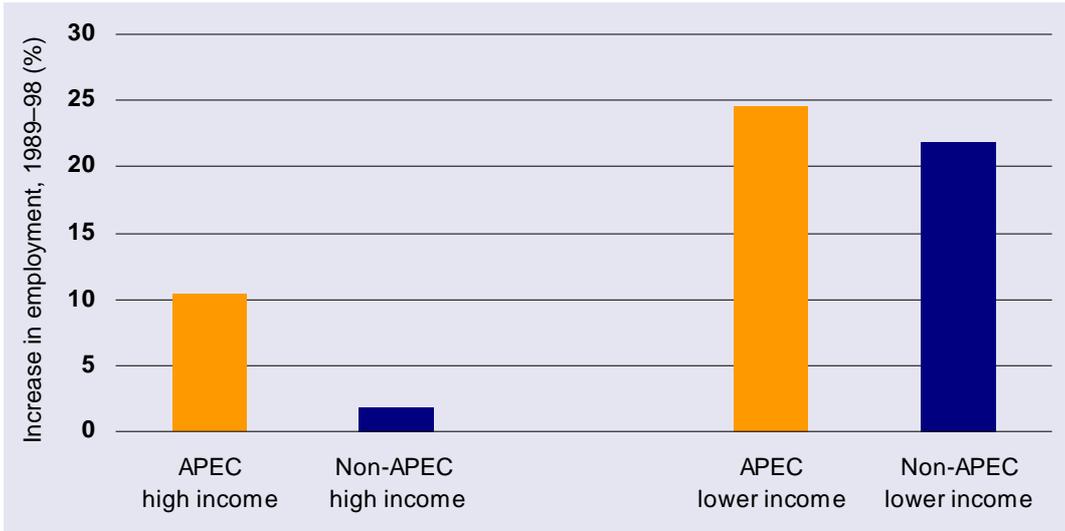
Differential economic performance across economies is leading to growing inequalities in income around the world. However, the evidence does not support the idea that economic growth necessarily increases income disparity within economies. Studies show that, on average across developing economies, growth has no systematic impact on income inequality (World Bank 2000c). The distribution of wealth delivered by growth depends partly on the overall policies pursued by individual governments.

## Employment is growing

APEC economies generated about 195 million new jobs in the period 1989–98. In this regard they considerably outperformed comparable economies in the rest of the world (chart 4.4). About 174 million of these new jobs were created in lower income economies.

Unemployment increased in crisis-affected economies in the latter part of the decade, and in response to this many economies increased the coverage and availability of programs to assist the unemployed. High income APEC economies have been achieving much better unemployment outcomes than their non-APEC counterparts. Unemployment in many high income APEC economies fell strongly in the latter part of the decade.

Chart 4.4 **New jobs have been created**



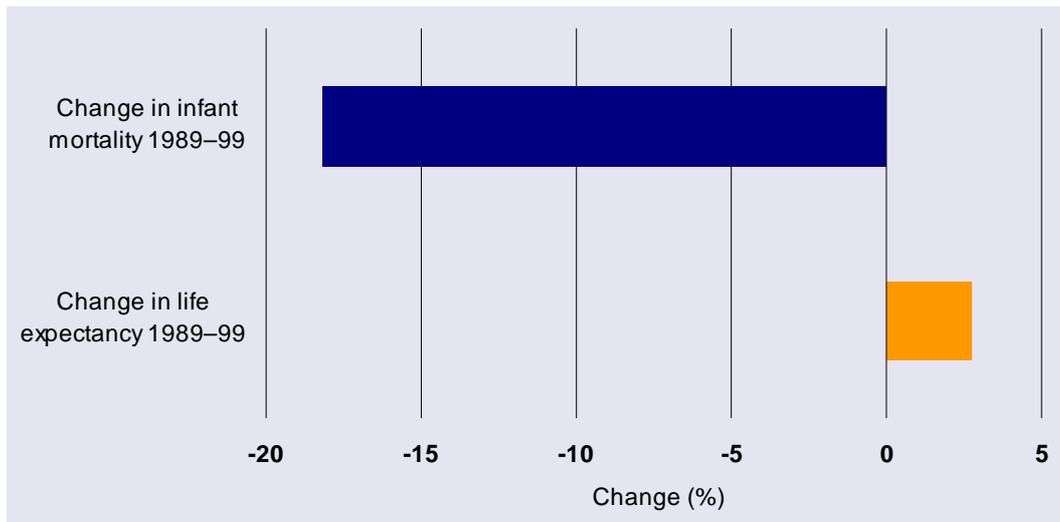
Data source: See technical note 9.

## Health is improving

Despite the recent financial crisis, lower income as well as high income APEC economies have continued to improve basic indicators of health. Infant mortality in lower income economies has fallen and life expectancy has risen since 1989 (chart 4.5), and high income economies have also experienced improvements in

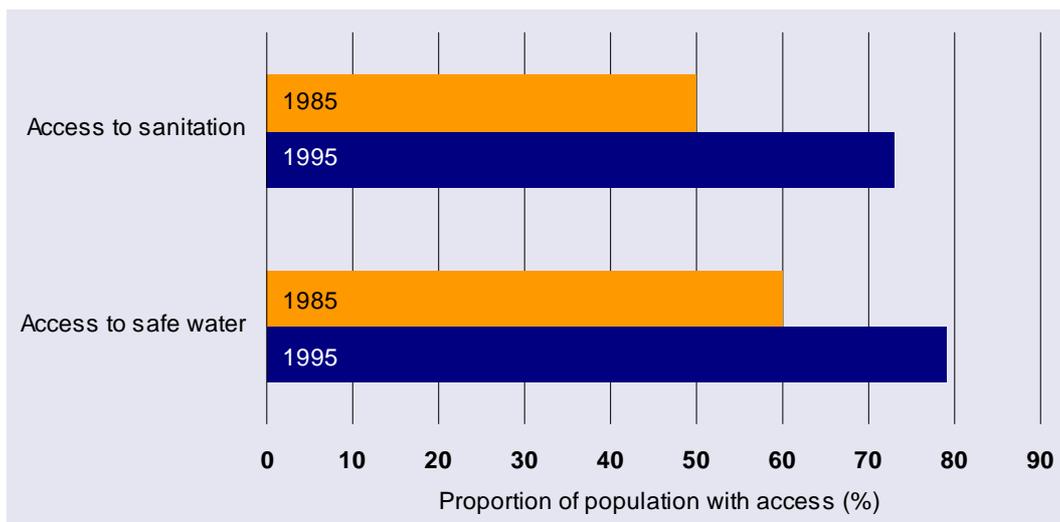
these indicators. Expanded access to safe water and sanitation has contributed to these improvements. Between 1985 and 1995, the share of the population in lower income economies with access to sanitation and safe water increased by 48 per cent and 28 per cent respectively (chart 4.6).

Chart 4.5 **Infant mortality has fallen and life expectancy has risen in lower income APEC economies**



Data source: See technical note 10.

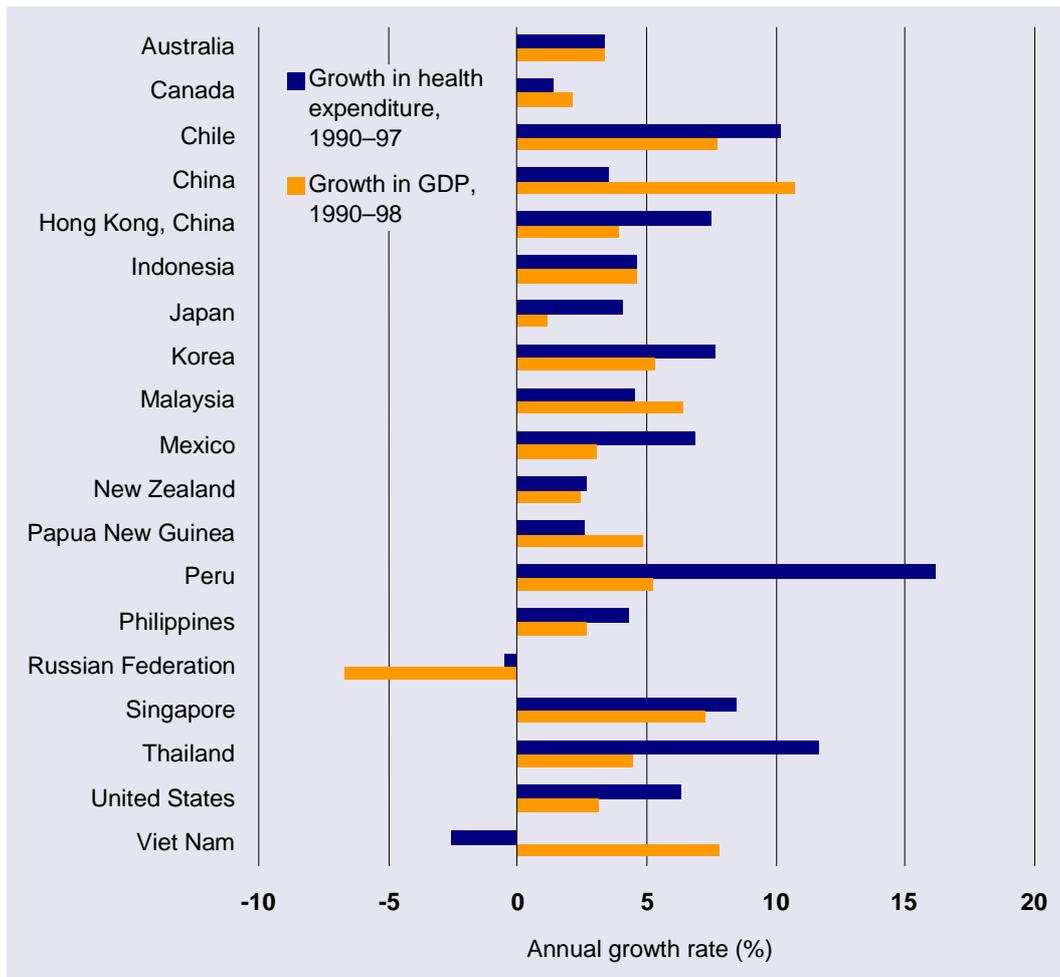
Chart 4.6 **Access to sanitation and safe water has expanded in lower income APEC economies**



Data source: See technical note 11.

APEC economies have increased real public expenditures on health (chart 4.7) — in most cases faster than the rate of economic growth — so the share of these expenditures in GDP has been rising.

Chart 4.7 **Public expenditures on health are generally growing faster than GDP**



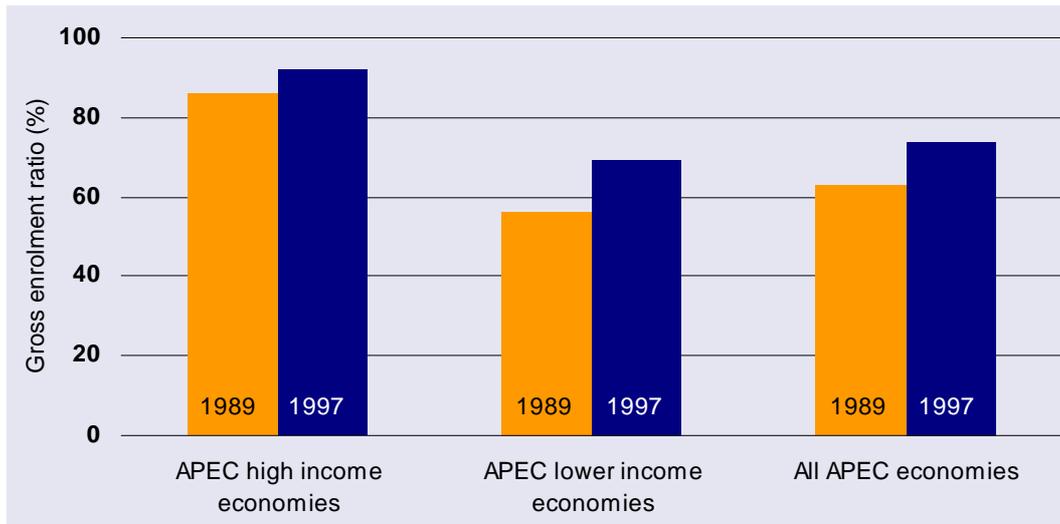
Data source: UNDP (1999).

### Educational opportunities are expanding

APEC economies have continued to expand investment in human capital as the combined enrolment rates in primary, secondary and tertiary education have increased in all lower income and most higher income economies (chart 4.8). Female enrolment rates in APEC economies compare favourably with those in counterpart economies (chart 4.9). Adult literacy rates in high and lower income APEC economies are among the highest in the world (chart 4.10).

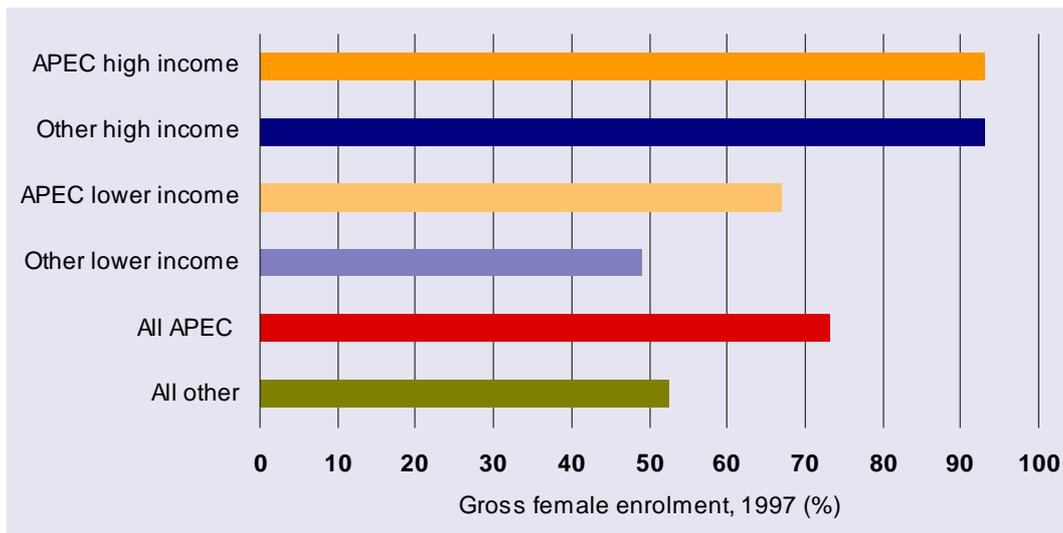
APEC economies have been increasing real public expenditures on education (chart 4.11), in most cases faster than GDP growth. Total expenditure on education has been growing far more rapidly, as families are devoting more of their growing incomes to private expenditure.

Chart 4.8 Education enrolment ratios have improved in APEC economies



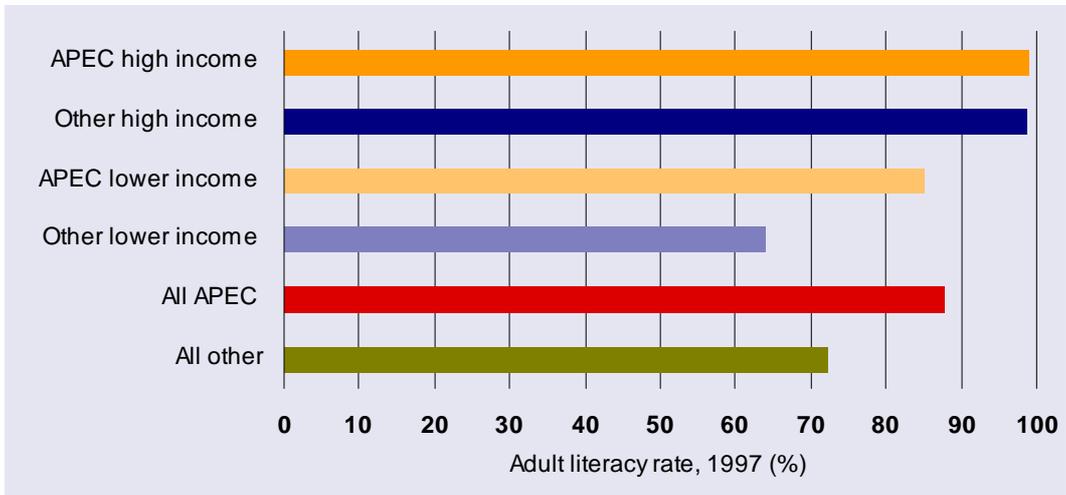
Data source: See technical note 12.

Chart 4.9 Women's enrolment in education compares favourably



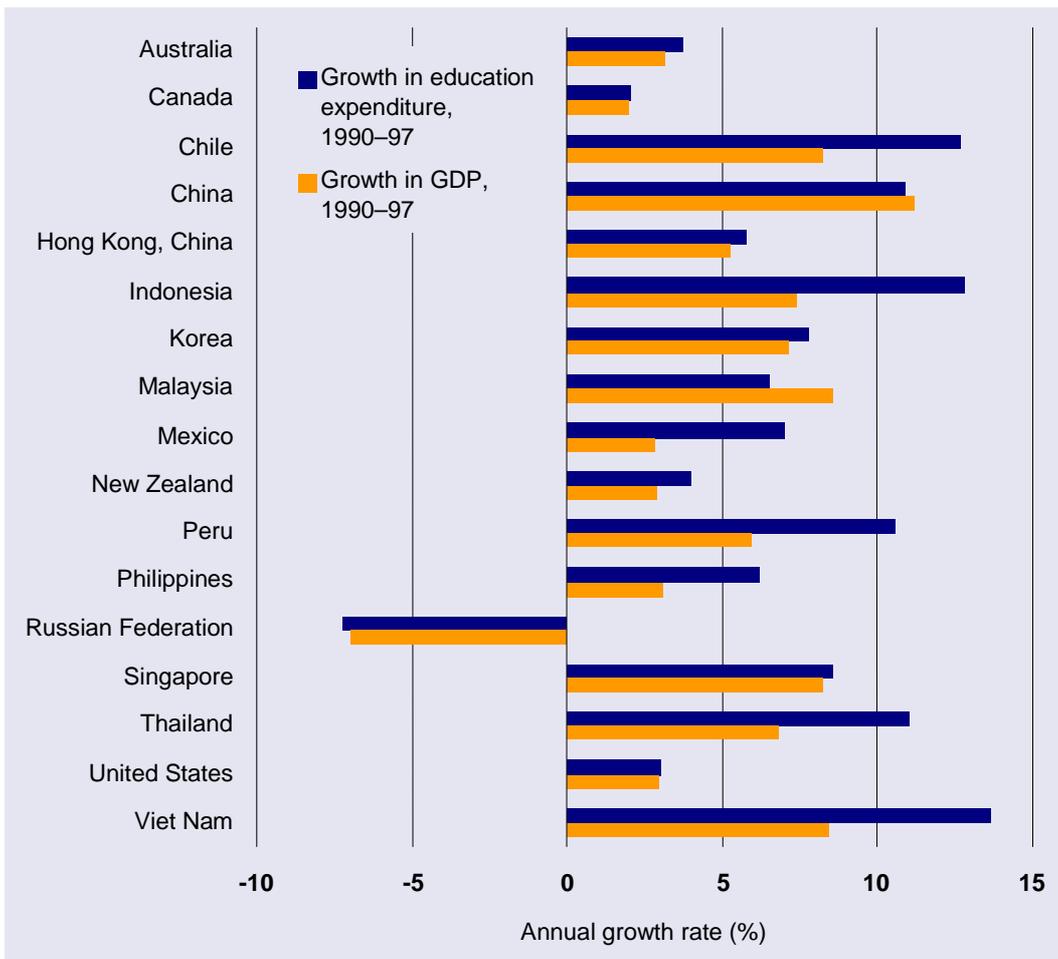
Data source: See technical note 13.

Chart 4.10 **Adult literacy rates in APEC economies are high**



Data source: See technical note 13.

Chart 4.11 **Public expenditures on education are generally rising faster than GDP**



Data source: UNDP (1999).

### **Environmental challenges are being tackled**

Rapid industrialisation and pressures created by population expansion have created significant environmental problems in APEC economies, as in other parts of the world. While this has occurred alongside trade and investment liberalisation and the growth this liberalisation has fostered, it has not been *caused* by liberalisation. Rather, it is generally due to a failure to price the environment appropriately.

Some of the worst cases of environmental degradation in the world have occurred in economies that have been relatively closed to international markets and investment, and in economies that remain poor as a result of growth-suppressing policies. The evidence suggests that the quality of governance and institutional capacity matter. A study by Torras and Boyce (1998) shows that, across economies with similar income per person, pollution levels tend to be higher in those with unequal income distributions, high levels of illiteracy and limited political and civil liberties.

The challenge for all economies is to adopt appropriately targeted policies to ensure that private decisions take better account of the social costs of environmental damage, and to reduce the poverty-related pressures that underpin many environmentally unsustainable practices.

### **Resource management has improved**

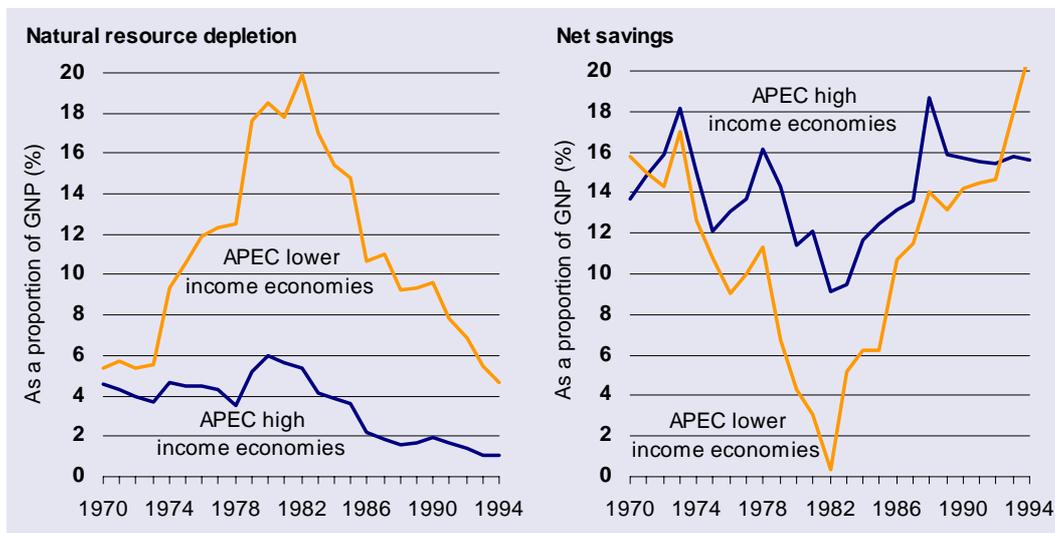
APEC economies have been managing their natural resources more effectively as they have become better able to afford such management. According to readily available measures the rate of natural resource depletion has been declining in both high and lower income APEC economies (chart 4.12). Equally importantly, the data suggest that, in APEC economies, savings invested in physical and human capital significantly exceed the loss of physical and environmental assets due to depreciation, resource depletion and pollution damage.

Chart 4.12 shows that in the lead-up to the mid-1990s both high and lower income APEC economies were saving more than they were depleting national environmental assets. Net savings — the excess of savings over depreciation, resource depletion and pollution costs — were a significant share of national income. The change in APEC lower income economies after 1982 is particularly notable. From 1982 to 1994, their net savings rose to 20 per cent of GNP.

Clearly this indicator is only one of many that must be considered in determining improvements to resource management. Nevertheless, it is important to know that the available data suggest that in APEC economies current generations will pass on to future generations at least as much wealth per person as they now enjoy.

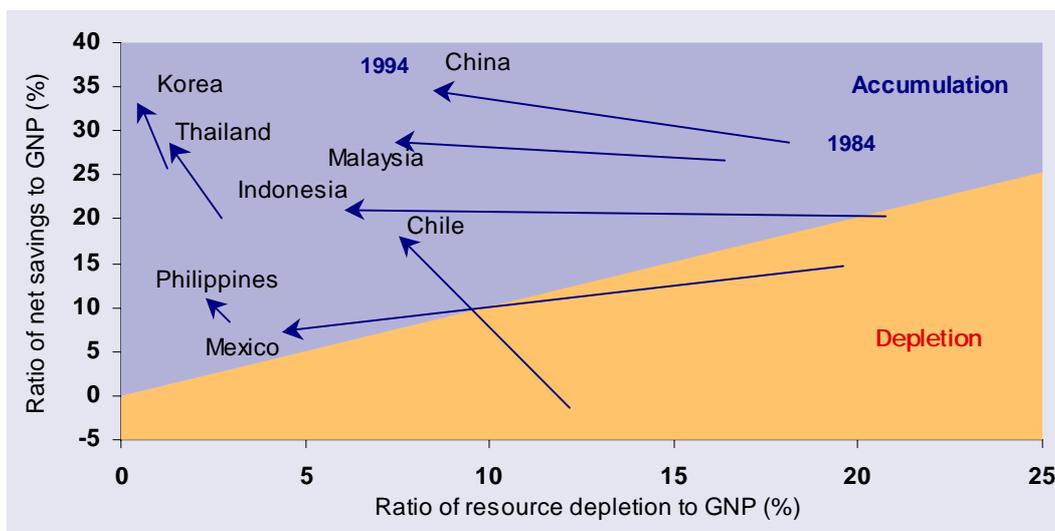
Chart 4.13 shows a marked shift in resource management in developing APEC economies between 1984 and 1994. For each economy represented, the ratio of

Chart 4.12 **Natural resource depletion is falling in APEC economies**



Data source: See technical note 14.

Chart 4.13 **Resource management in lower income APEC economies improved between 1984 and 1994**



Data source: See technical note 14.

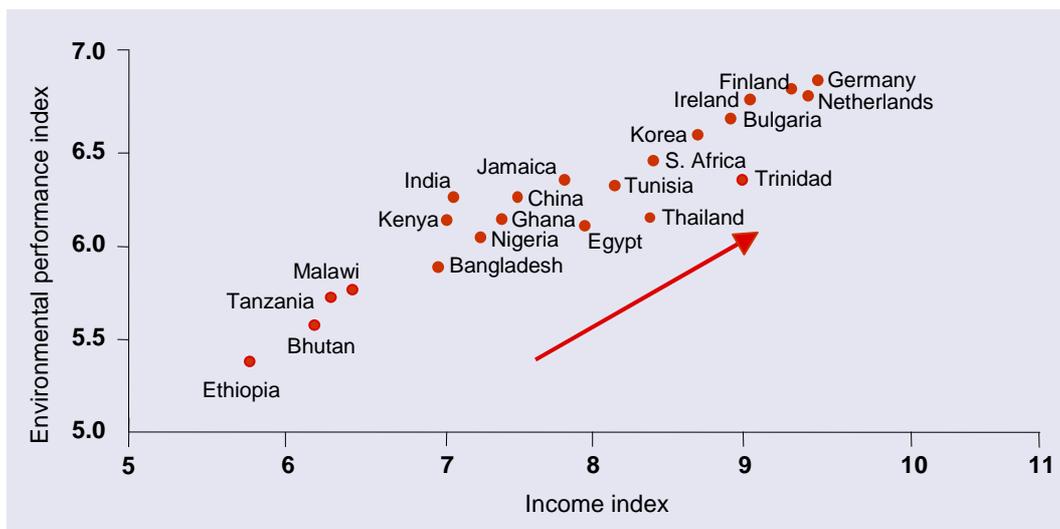
resource depletion to GNP fell below the ratio of net savings (gross savings less depreciation) to GNP. This evidence does not support the notion that environmental degradation has been ‘exported’ to developing APEC economies.

### Environmental outcomes reflect many influences

One concern of those who are worried about the effects of trade and investment liberalisation is that the improved social outcomes triggered by faster growth may come at the expense of the environment. There is no doubt that worrying environmental trends emerged in the latter half of the twentieth century. However, the links between economic integration, growth and environmental outcomes are complex.

While in some cases short-run growth can appear to be achieved at the expense of the environment, there are compensating factors. A major cause of environmental degradation in many economies is poverty, and the evidence suggests that, as incomes rise, economies are better able to afford environmental protection. It also seems that, as incomes grow, the value that people place on the environment increases. As chart 4.14 shows, there is evidence that greater prosperity leads to better outcomes for the environment. This may not be an automatic outcome, but more due to an induced policy response as awareness of and capacity to address environmental damage increases with greater national prosperity.

Chart 4.14 Economic prosperity need not come at the expense of the environment



Data source: OECD (1999).

There is considerable evidence in APEC economies that the increasing wealth generated by open economic policies has led to better environmental outcomes. Certainly, as economies have become wealthier, their expenditure on environmental protection has increased significantly. But there is also qualitative evidence of changing attitudes to the tradeoff between growth and the environment as economies become richer. In 1998 county-level governments in

### Box 4.1 Trade and investment liberalisation promoting environmental protection

One way in which liberalisation of international trade and investment can help to improve environmental outcomes is by facilitating access to environmentally friendly technology. In developing economies it can also facilitate access to the capital and technical and managerial expertise required to improve environmental protection.

A recent OECD (2000c) report presented examples of ‘win–win’ benefits accruing to developing economies from liberalising trade and investment in the water supply, waste water treatment and solid waste management sectors. After examining over 60 examples of foreign private participation in these sectors in developing economies in the past decade, the study identified a range of environmental and development ‘win–win’ outcomes.

Environmental wins included greater access to clean water and waste collection services, reduced wastage of, and/or inequitable access to, scarce water resources, increased availability of drinking water through recycling of effluent, waste recycling to generate electricity, spillovers in terms of environmental management and training, and access to more appropriate environmental technologies.

Economic development wins included reduced pressure on government budgets, job creation, attraction of foreign investment through the availability of water and waste management systems, spillovers to the local private sector through involvement in specialised projects, and reversion of build–operate–transfer facilities to local ownership.

Examples of win–win outcomes cited in the study included:

- the granting of concessions to foreign companies to operate water, wastewater, sewerage and solid waste facilities in Chile, China, Indonesia, Malaysia and the Philippines;
- the establishment of joint ventures between foreign and domestic firms in water and wastewater treatment in the Philippines and Chinese Taipei;
- the establishment of build–operate–transfer operations in water treatment, water distribution, and solid waste transfer in China, Hong Kong, China, Malaysia and Viet Nam; and
- the granting of contracts for service delivery to foreign firms in water services, and in water resource planning, operations and management in China, Indonesia and Malaysia.

Chinese Taipei refused permission for several multibillion dollar investment projects. Local investment in a naphtha cracker plant (part of a larger proposed steel mill project) was halted because of community concern about pollution, potential greenhouse gas emissions, conservation of fresh water and protection of an endangered wildlife species. And significant foreign investment in a chemicals plant was stopped because of concern that pollution would affect the local fishing industry. In Viet Nam microeconomic and legal reform that grants farmers long-term land use rights has facilitated the growth of farm forestry, which is underpinning an extensive reforestation program.

Concerns have also been expressed that economic integration triggers a ‘race for the bottom’ in that competition between economies for investment leads to the location of environmentally sensitive activities in developing economies with lower environmental standards or less capacity to enforce standards. The evidence seems to suggest, rather, that developed economies are increasingly the preferred location for pollution-intensive industries, despite increasingly stringent environmental standards. This probably reflects the fact that such industries are typically capital intensive and better suited to the endowment of wealthier economies and that abatement costs typically represent a small proportion of production costs (Nordstrom and Vaughan 1999).

Trade and investment liberalisation — and broader economic integration — may also have positive effects on environmental outcomes by facilitating the diffusion of environmentally friendly technologies and increasing awareness of problems that extend beyond national boundaries (box 4.1). This is not to say that integration provides an automatic solution to environmental degradation — for example, open trade could lead to the depletion of non-renewable natural resources if appropriate domestic controls are not in place. The relationships are complex and work in a number of directions.

Although income growth stimulated in part by closer integration may help to change the focus in economies from immediate concerns of poverty reduction to longer term environmental and sustainability issues, stronger environmental policies will be necessary to ensure better environmental outcomes.

## **5 APEC – maximising the benefits from increasing openness**

The APEC experience over the past decade clearly demonstrates that open economies achieve substantially greater economic growth and that this growth underpins significant improvements in the lives of their people.

APEC economies have grown strongly at the same time as they have significantly reduced tariffs, eliminated a large number of non-tariff barriers and liberalised foreign investment. Overall APEC GNP grew by about a third over this period, with GNP in lower income APEC economies growing by 74 per cent. GNP per person grew by 61 per cent in lower income APEC economies, at the same time as it fell in all other lower income economies.

APEC economies have reinforced this economic growth by adopting a range of microeconomic reforms, strengthening economic and corporate governance and actively managing change to ensure that they maximised the benefits flowing from open economic policies.

Microeconomic reform has covered financial sector restructuring and regulation, legal and judicial reform to improve the framework for contracting and enforcing debt, and taxation and public expenditure reform to improve incentives for private investment and increase the efficiency of delivery of social and infrastructure services. Priority has also been given to promoting competition through deregulation and the adoption of measures to counter anticompetitive practices. APEC economies are improving their economic governance.

Improved governance is being pursued through legal and judicial reform, improvements in the regulation and supervision of the financial sector and capital markets, and actions to strengthen accounting and financial reporting practices. Key international indexes reflecting many aspects of governance show improved performance in the decade since APEC was created.

APEC economies are also adopting labour market and other adjustment programs to facilitate adjustment to policy change, and are extending social safety nets to protect vulnerable groups from adverse developments as change occurs.

Open economic policies have contributed to unparalleled social progress in APEC economies, particularly in developing APEC economies. Over the past decade, the UNDP Human Development Index for lower income APEC economies has risen by almost 18 per cent. Poverty in APEC economies has been slashed by about a third, and 195 million new jobs have been created. In lower income APEC economies, infant mortality has fallen and life expectancy has improved. Access to sanitation and safe drinking water has been extended to a further one-fifth of the population of lower income APEC economies. Education opportunities and expenditure on education have also expanded significantly, with lower income APEC economies recording adult literacy rates about 20 percentage points higher than other lower income economies. Although environmental management remains problematic, there is no evidence that choosing open economic policies has exacerbated environmental problems. In fact, evidence suggests that over the past decade APEC economies have improved their resource management and substantially reduced their natural resource depletion, and are increasingly using their newfound wealth to achieve cleaner environments.

### **APEC is building on success ...**

Clearly APEC economies, both individually and collectively, have made remarkable achievements through the adoption of open economic policies. The spectacular economic growth rates of APEC member economies and the rapidly rising standard of living of the people of the region are indisputable. Still, APEC economies cannot rest on their laurels. APEC members recognise that further liberalisation and reform are essential to maintain the dynamic progress of the region and extend the gains of the past decade to all.

Just as APEC has played an important role in helping APEC members achieve the successes recorded to date, APEC cooperation will play a critical role in building on the progress of the past decade.

### **... by intensifying trade and investment liberalisation ...**

APEC economies have reaped substantial economic and social benefits from their trade and investment liberalisation efforts over the past decade. These efforts will need to be sustained and intensified in order to generate the growth necessary to

support the growing populations and increasing standards of living expected by the people of the Asia-Pacific region in the twenty-first century.

The launch of a new round of multilateral trade negotiations will be one of the most important keys to unlock the potential of the region. Broad-based and fundamental cuts to tariffs and protectionism can be achieved only in the context of a WTO round. APEC members can therefore be expected to maintain their collective efforts to secure the launch of a new round.

APEC economies are in a strong position to make an important contribution to preparing for a new round. Representing over half of the global economy and a range of levels of economic development and systems, APEC provides a valuable forum for discussing issues relating to the scope and content of a round. APEC is also helping to prepare its members for participation in a new round through assistance to build the capacity of developing member economies to implement fully their WTO obligations.

At the same time, APEC is increasingly drawing on its own experience to better explain the benefits of trade and investment liberalisation to the public. Misconceptions about the inherent impact of globalisation on communities remain an important obstacle to the launch of a new round. However, APEC's experience has been that open market policies, coupled with measures to strengthen domestic competitiveness and institutions and strategies to manage the impact of change, deliver substantial and real benefits to people at all levels of the societies that adopt such policies. A wider understanding of this will make an important contribution to removing obstacles to a new round.

While the launch of a new round is of particular importance, the record over the past decade shows that APEC economies derive substantial additional benefits from an ongoing process of liberalisation beyond their WTO commitments. Steps already taken to reinvigorate the IAP system will provide a strong basis for achieving the Bogor goals. Collective actions developed through the various APEC fora and subfora will also continue to play an important role in enabling APEC member economies to draw the full benefits of expanding trade and investment. And free trade areas that are truly liberalising can also provide building blocks towards reaching the Bogor goals.

### **... by strengthening domestic markets and institutions ...**

A key to APEC's success has clearly been the attention given by member economies to economic reform to create more internationally competitive markets and the work to improve economic and corporate governance. The Asian financial crisis of the late 1990s underlined this and focused APEC's collective attention on the importance of addressing these issues better. APEC can therefore be expected to continue to pay particular attention to strengthening the economic and corporate governance capabilities of member economies and intensifying work on competition policy and regulatory reform.

High quality economic and corporate governance is fundamental to the efficient operation of robust and open economies. APEC has made important progress in strengthening the governance capacities of member economies through the Finance Ministers process. The new work presently under way on strengthening economic legal infrastructure will be critical to APEC's governance work.

### **... and by building the 'new Asia-Pacific economy'**

APEC economies are placing particular priority on seizing the opportunities provided by the information and communications revolution to work together to build a 'new Asia-Pacific economy'. New technologies provide enormous potential to achieve previously unimaginable economic efficiencies, and APEC member economies are working together to ensure that the impact of these technologies permeates all sectors of their economies and societies. Failure to do so risks APEC economies losing their competitive edge and hence producing slower economic growth and stunting social progress.

The evidence suggests that, while APEC member economies are already achieving impressive growth rates in the numbers of people with access to the internet, the proportions of their populations with access vary widely. The challenge for APEC, therefore, is to devise strategies to rapidly expand the numbers of people, particularly in developing economies, with some degree of access to the internet through, for example, community-based access. In this way APEC would contribute to both increasing the penetration of the information and communications revolution throughout the economy and helping to ensure that all have access to the benefits.

APEC will also have an ongoing role in developing the technical, policy and legal infrastructure necessary to enable everyone to take full advantage of the potential that the information and communications revolution creates. The work already done on interconnectivity, internet charging arrangements, electronic transactions and paperless trading will need to be taken forward and further developed. The APEC moratorium on the imposition of customs duties on electronic transactions might provide a first step towards a broader commitment to open trade via the internet.

Of course, internet access is not only a matter of connections, but also the skills to take full advantage of the opportunities that the technology offers. Internet skills in developing economies provide the opportunity for those economies to use technology to 'leapfrog' the development process.

It is also important to recognise that, while the information and communications revolution underpins the development of the new Asia-Pacific economy, the new economy is about the infusion of a culture of technology and innovation into all economic activity. Knowledge-based economies require both business environments that encourage innovation and strategies that support human resource development. APEC provides a unique vehicle to help achieve these goals.

### **Managing change better is the challenge**

Economic and social progress cannot be achieved without change. The challenge is to manage rather than fear change and to ensure that the benefits of change are enjoyed by all. This will be of increasing importance as the information and communications revolution inevitably accelerates the pace of change.

As economies become increasingly knowledge based, the continuous development of human resources will be critical. Investing in quality education and training and renewing workforce skills are fundamental requirements for the new economy. High standards in literacy, mathematics, science and technology will provide the basis for effective participation in the emerging global economy. Economies will need to cultivate sound management practices among policy makers and practitioners to ensure affordability of and access to quality education, and responsiveness of education systems to the needs of different groups. APEC provides a valuable forum through which to share experiences and provide practical assistance so that all member economies are able to build the educational systems necessary to meet the needs of the twenty-first century.

The other key challenge to managing economic change is to help those most affected by change. The Asian financial crisis and its aftermath demonstrated clearly that it is important to have proactive structural adjustment strategies in place to blunt the impact of rapid changes. But change is not just a feature of crisis; change is inevitable and ongoing, and successful economies need to build high capacity to manage and adjust to change. APEC provides a valuable forum for sharing information on best practice policy and regulatory systems to respond to the needs of those affected by change.

Economic and social progress cannot be achieved without change. The challenge is ensure that the benefits of change are enjoyed by all. This will be of increasing importance as the information and communications revolution inevitably accelerates the pace of change.

Of course, there is no single, magical package of structural adjustment strategies that will address the particular needs of every economy in meeting the challenges of change. Strategies need to be developed in accordance with the particular economic and social conditions of each society and with reference to diverse cultural factors.

A key element is having a flexible and responsive workforce. Skills development and lifelong learning will be crucial, along with retraining for the existing workforce to adapt to new ways of working. The APEC framework provides a useful catalyst to help build a culture of public and private sector cooperation in providing skills development and retraining.

# Technical notes

To facilitate the graphical representation of data, in some instances APEC economies have been assigned to either a 'high income' or a 'lower income' group. The allocation of economies to income groups used in this report is based on the classifications used by the World Bank.

Only 17 of the current 21 APEC members have been included when reporting aggregate statistics. Four APEC economies — Brunei Darussalam, Peru, the Russian Federation and Viet Nam — have been omitted from these statistics either because they have only recently become members of APEC (Peru, the Russian Federation and Viet Nam became members in 1998) or because of the difficulty of obtaining comparable data due to the economy's relatively small size (Brunei Darussalam). In cases where relevant data are not available for other economies, these too have been omitted.

## **Technical note 1 (chart 2.3)**

The data were originally sourced from the Manila Action Plan for APEC and from various Individual Action Plans (1998). The data used vary between economies (that is, simple average or import weighted average) and are therefore not comparable. Data for Australia, Canada, Japan, Mexico and the United States are trade weighted. The 1995 figure for Papua New Guinea was sourced from Ai (1996) and the 1993 figure for Viet Nam was sourced from the CIE (1998b).

## **Technical note 2 (chart 2.5)**

Trade and nominal GDP values for 1989 were obtained from the World Bank's World Development Indicators 1999 CD-ROM. Trade and GDP figures for 1998 and 1999 were either obtained from DFAT (Australian Department of Foreign Affairs and Trade) sources or estimated using anticipated income group growth rates reported in the International Monetary Fund's *World Economic Outlook 2000*.

The World Bank does not report data for Chinese Taipei. Data for Chinese Taipei were derived from a range of sources, including the DFAT publication *The APEC Region Trade and Investment* (various years) and the Asian Development Bank's *Asian Development Outlook 1999*, or were derived from other DFAT sources.

## **Technical note 3 (charts 2.6 and 2.7)**

FDI inflow and outflow figures over the period 1989–98 were taken from the International Monetary Fund's *International Financial Statistics 1999 Yearbook* (lines 78bed and 78bdd respectively) and/or from UNCTAD's *World Investment Report 1999*. In the

few instances where data were not available, FDI inflow and outflow figures were estimated by assuming that the previous year's growth rates applied. Comparable inflow and outflow data for Chinese Taipei and Hong Kong, China were not available prior to 1992, so these economies are excluded from the statistics for the APEC economies presented in the charts.

#### **Technical note 4 (chart 2.8)**

Gross national product figures for APEC members and world income group aggregates for the years 1989–97 were obtained from the World Bank's World Development Indicators 1999 CD-ROM. GNP figures for 1998 and 1999 were estimated by applying anticipated real gross domestic product growth rates obtained from the International Monetary Fund's *World Economic Outlook 2000* to the reported 1997 data and (the then derived) 1998 figures.

Population figures for APEC members and world income group aggregates for the years 1989–97 were also obtained from the World Bank's World Development Indicators 1999 CD-ROM. Population figures for 1998 and 1999 were estimated by applying the estimated annual population growth rates over the period 1995–2000 to the reported figures. The estimated annual population growth rates were taken from the World Development Indicators 1999 CD-ROM.

Data for Chinese Taipei were derived from a variety of sources (see technical note 2).

#### **Technical note 5**

This estimate was prepared for the paper 'Economic benefits from an AFTA–CER free trade area: year 2000 study' prepared by the Centre for International Economics for the Australian Department of Foreign Affairs and Trade. The paper is available from the internet ([http://www.intecon.com.au/reports\\_list.htm](http://www.intecon.com.au/reports_list.htm)).

#### **Technical note 6 (chart 3.3)**

The index was obtained from the Fraser Institute's publication *Economic Freedom of the World 2000* (Gwartney, Lawson and Samida 2000). The averages for high and lower income APEC economies were calculated using GNP weights.

#### **Technical note 7 (chart 3.4)**

The indexes of risk rating were compiled from the *Composite International Country Risk Guide* indexes for February 1999 reported in the World Bank's *World Development Report 1998–99* and *World Development Report 1999–2000*. Averages were compiled using GNP weights. The Composite International Country Risk Guide is an overall risk index based

on 22 political, financial and economic risk components. Risk ratings range between 0 and 100. Ratings below 50 indicate very high risk and those above 80 very low risk.

### **Technical note 8 (chart 4.1)**

Human Development Indexes for APEC economies for 1985 and 1997 were obtained from the UNDP's *Human Development Report 1999*. APEC economies were then aggregated to income groups using population weights. The index is not reported for Chinese Taipei, and the index values for Chile, Mexico and Papua New Guinea are not available for 1985. Hence these economies were omitted from chart 4.1.

The Human Development Index reflects three indicators of development — life expectancy at birth, combined gross school enrolment ratio and adult literacy, and income per person.

### **Technical note 9 (chart 4.4)**

Employment figures were obtained from the International Labour Organisation's LABORSTA database (<http://laborsta.ilo.org>).

### **Technical note 10 (chart 4.5)**

Life expectancy and infant mortality for the years 1989–97 were obtained from the World Bank's World Development Indicators 1999 CD-ROM. Values for 1998 and 1999 were estimated by calculating the annual percentage improvement in life expectancy and infant mortality over period 1989–97, and then applying these rates to the 1997 data (and the then derived) 1998 data.

Total APEC and APEC income group totals were derived by using population and crude birth rate weights for life expectancy and infant mortality respectively. Crude birth rates were not available for all APEC economies in 1989. However, a complete set of rates was available for 1990. These rates were used to weight individual 1989 infant mortality figures for APEC economies to derive aggregate estimates of infant mortality.

To check for consistency, the estimated 1998 and 1999 values were compared with life expectancy and infant mortality rates reported elsewhere — for example, in the World Health Organization's *1999 World Health Report*.

The World Bank does not report life expectancy and infant mortality rates for Chinese Taipei; hence Chinese Taipei was omitted from the chart.

### **Technical note 11 (chart 4.6)**

The proportions of the populations of APEC economies with access to safe water and sanitation were obtained from the World Bank's World Development Indicators 1999 CD-

ROM. Population weights were used to derive lower income group aggregates. Safe water and sanitation access values for 1985 and 1995 were not available for all APEC lower income economies. Where this was the case, 1985 and 1995 values were approximated by using the closest available year's data. China was not included due to a lack of data.

Access to safe water is the proportion of the population with reasonable access to an adequate amount of safe water (20 litres a day per person). In urban areas the water source may be a public fountain or standpost located not more than 200 meters away. In rural areas the definition implies that household members do not have to spend a disproportionate part of their day fetching water. The definition of safe water has changed over time.

Access to sanitation refers to the proportion of the population with at least adequate human waste disposal facilities that can effectively prevent human, animal and insect contact with excreta.

#### **Technical note 12 (chart 4.8)**

Combined primary, secondary and tertiary level education gross enrolment ratios were obtained from the UNESCO Institute for Statistics education database (<http://unesco.org>). The gross enrolment ratio is defined as total enrolment in a specific level of education, regardless of age, expressed as a percentage of the official school age population corresponding to the same level of education. Gross enrolment ratios are used to show the general level of participation in a given level of education and to indicate the capacity of the education system to enrol students of a particular age group.

A high gross enrolment ratio generally indicates a high degree of student participation in that education level, whether students belong to the official age group or not. Gross enrolment ratios can be in excess of 100 per cent due to the inclusion of over-aged and under-aged students because of early or late entrants, grade repetition or, as in the case of Australia in the 1990s, retraining of the long-term unemployed.

Where the UNESCO education database did not report an economy's gross enrolment ratio for 1989, the closest year's ratio was used as a proxy. The UNDP's *Human Development Report 1999* was used to supply 1997 gross enrolment ratios when they were not available on the UNESCO education database.

#### **Technical note 13 (charts 4.9 and 4.10)**

Data on female gross enrolment ratios (chart 4.9) and adult literacy rates (chart 4.10) were taken from the UNDP's *Human Development Report 1999*. Rates for individual APEC economies were aggregated using population weights.

### Technical note 14 (charts 4.12 and 4.13)

Data on net savings and its various components — extended gross savings, depreciation, natural resource depletion and CO<sub>2</sub> emissions — were obtained from the World Bank's internet site (<http://www.worldbank.org>), where it is possible to download net savings results for a range of economies over the period 1970–94. The net savings measure reported is calculated as follows.

#### Genuine savings calculation

New savings	=	Gross domestic investment	+	Current education spending	+	Net official transfers	–	New foreign borrowing	(Extended gross savings)
		– Depreciation of capital							(Extended net savings)
		– Depletion of natural resources							(Extended genuine savings I)
		– Pollution damage							(Extended genuine savings II)

Current spending on education is included in the measure of genuine savings as it is considered to be an investment in human capital (rather than consumption as in the traditional national accounts). Natural resource depletion is limited to valuation of the resource rents for non-renewable resources (namely, minerals and fossil fuels) and the depletion of forests beyond replacement levels. Fisheries depletion is not included, nor are other environmental problems such as salinity or land degradation. As many pollution damages are localised and are therefore difficult to estimate without locational data, pollution damage estimates were restricted to the global damage caused by CO<sub>2</sub> emissions. The marginal social cost of a tonne of CO<sub>2</sub> emission was assumed to be US\$20 (Hamilton and Clemens 1999).

Where data were not available for a particular component of genuine savings, estimates were derived using growth rates calculated from World Development Indicators 1998 CD-ROM. For example, data on gross domestic investment in 1994 are not available for six APEC economies. For each economy a value was estimated by calculating the percentage change in domestic investment over the years 1993 and 1994 (for the appropriate economies) using data reported in the World Development Indicators 1998 CD-ROM. This growth rate was then applied to the reported value of 1993 gross domestic investment, thus deriving a 1994 value.

An estimate of the cost of CO<sub>2</sub> damage in Chinese Taipei was derived by multiplying the tonnage of national Chinese Taipei CO<sub>2</sub> emissions from fossil-fuel burning, cement manufacture and gas flaring by US\$20. CO<sub>2</sub> emissions for Chinese Taipei were obtained from the Carbon Dioxide Information Analysis Centre internet site (<http://www.cdiac.esd.ornl.gov>).

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