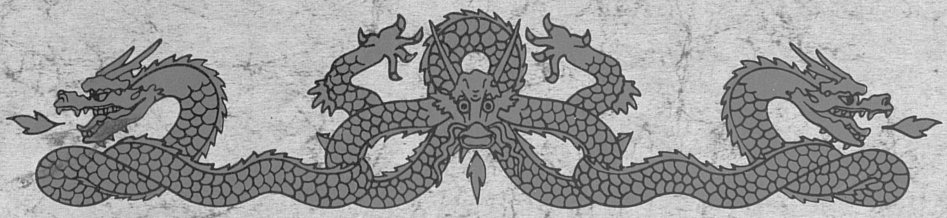
Asia's New Little Dragons

The Dynamic Emergence of Indonesia, Thailand, and Malaysia



STEVEN SCHLOSSSTEIN

Author of *The End of the American Century*

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In the 1970s and 1980s, in the wake of Japan's stunning postwar growth, the "Little Dragons"—South Korea, Taiwan, Singapore, and Hong Kong—prospered as well. Will Indonesia, Thailand, and Malaysia follow suit and become the Little Dragons of the 1990s? If so, what strategies and public policies should the United States adopt in response to these booming economies—and in response to the influence of the Big Dragon, Japan, on the region?

As the West confronts the challenge of a new Pacific Age, these are vital questions, and in *Asia's New Little Dragons* Asian affairs expert Steven Schlossstein answers them by examining both economic and noneconomic aspects of these three emerging nations and reaching conclusions that are always thoughtful and often surprising.

Through lively interviews with top Indonesian, Thai, and Malaysian businesspeople and policymakers, Schlossstein unravels the fascinating complexities of the culture, history, economy, politics, and foreign policy of these three nations, each one unique and little understood by Westerners. He shows Indonesia, the fifth most populous country in the world and a member of OPEC, poised for economic takeoff; Thailand, beset by a gridlocked infrastructure and the growing menace of an AIDS epidemic, in a less certain position despite a homogeneous Buddhist society, high literacy rate, and diversified foreign investment; and Malaysia, an Islamic nation seriously hampered by an unstable political system and extreme racial tensions.

Schlossstein also discusses how Japan is already investing aggressively in these diverse nations, and he suggests specific U.S. strategies for competing in what may soon become Asia's new Little Dragons.

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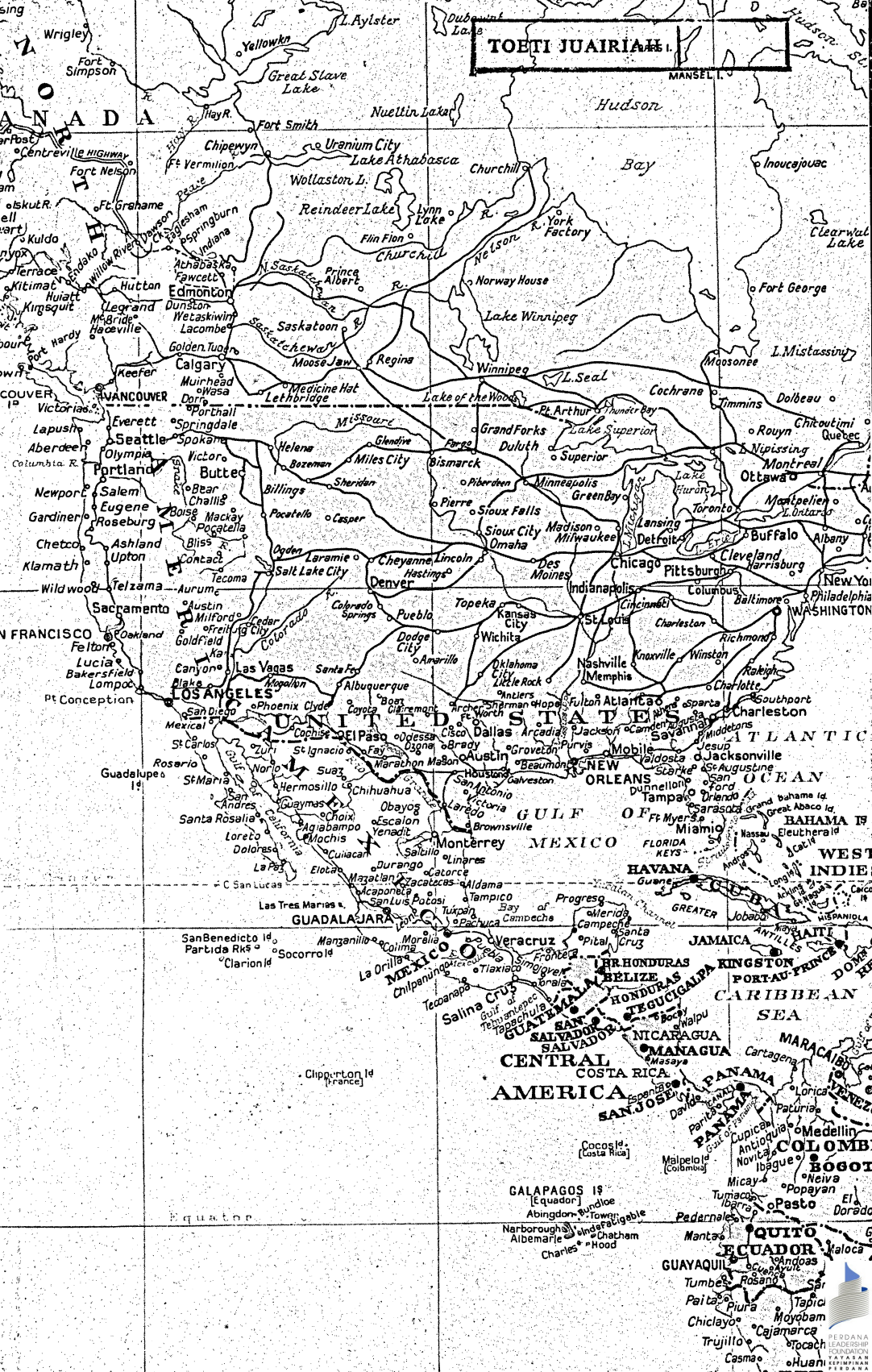
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Asia's New Little Dragons

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Asia's New Little Dragons

The Dynamic Emergence of Indonesia, Thailand, and Malaysia

STEVEN SCHLOSSSTEIN

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PERDANA LEADERSHIP FOUNDATION
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For the people of Southeast Asia—
whose hard work and arduous effort under often adverse conditions have produced dramatically higher living standards for their children and created a model of inspiration and hope for developing countries everywhere

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PREFACE

Thirty years ago Japan first caught the world's attention through its high-quality consumer goods, its near-neurotic attention to manufacturing detail, and its now-famous "economic miracle." Then, not long thereafter, came the so-called Little Dragons—Korea, Taiwan, Singapore, and Hong Kong—which replicated many of Japan's own commercial and economic successes. Their stories are now familiar, and most Americans have become aware of them—through popular products, new books, and TV.

Less familiar, however, are the stories of Indonesia, Thailand, and Malaysia, three nations that are laying a solid foundation for economic takeoff, yet to appear on the horizon, but already they are registering some of the highest rates of real economic growth in the world. Far removed from the fallout of the Cold War and untouched by America's public policy debates over mainly domestic issues—tax policy and the federal deficit, public education reform, the war on drugs, family policy and welfare reform, urban redevelopment, the repair and upgrading of our infrastructure, affordable housing, health care, the environment—these countries are fighting a quieter battle for higher living standards, for faster economic growth, for the creation of new wealth.

Can another group of countries in East Asia repeat the successes of Japan and the Little Dragons? And why have all the economic achievements by developing countries been in Asia? What policies are being created, and implemented, that consistently enable these Asian nations to succeed? Are there valuable lessons for their counterparts in Latin America and Africa? How much of their success is

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attributable to indigenous factors—political, social, cultural, educational—and how much to external developments? Why is Japan giving them such priority attention, while America is not? Will these three potential new Little Dragons, a few years from now, be as familiar to Americans as the four old Little Dragons are today? Or have we seen the end of the phenomenon called newly industrializing countries—the NICs? And what are the implications for American foreign and economic policy—in both the public and the private sectors—if these three nations do continue their explosive growth? Will they have a meaningful role to play in the new information age, and will they be our partners or our foes?

This book is an attempt to answer these and other related questions. It is an outgrowth of several months of research in the field, in the summer of 1989, when I was a visiting fellow at the Institute of Southeast Asian Studies (ISEAS) in Singapore, and its sister institutions in Jakarta, Bangkok, and Kuala Lumpur. During this period of time, from late May through early September, I conducted more than 200 background interviews with senior government officials, local business executives, educators, economists, taxidrivers, and shopkeepers, as well as with American and Japanese expatriates in each of these countries. Without their close cooperation and support, simply put, this project would have been impossible to complete.

Many of the issues raised in this book are not without controversy—opinions expressed about American and Japanese attitudes or policy or personal behavior, insights into sensitive cultural concerns like religion or prostitution or corruption, and observations on the efficacy of the local policy formulation process and the personal chemistry of government leaders involved therein. Understandably many senior Indonesian, Thai, and Malaysian informants preferred to speak off the record or without attribution. But I would like very much to acknowledge their invaluable assistance, as they were helpful in countless confidential, clandestine, and often controversial ways (with interviews, with information, or with introductions). Without their help this book would have been remarkably thin.

On the other hand, many people generously shared their time, their convictions, and their thoughts with me on the record. They are reflected (and named) in the many interviews that follow in the text;

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space limitations prevent listing them all here, but they must take credit for making the narrative so human and so lively. They know they have my heartfelt thanks and gratitude, for without their participation, interest, and effort this book would not have been possible.

To the trustees and staff of the Institute of Southeast Asian Studies in Singapore, and to its executive director, Kernial Sandhu—whose friendship, support, and constant encouragement I will always treasure—a special note of appreciation and thanks. ISEAS was (and will forever be) a "home away from home" for me, and I have only the highest praise for its professional standards and achievements.

To the Center for Strategic and International Studies (CSIS), Japan's Ministry of International Trade and Industry (MITI) representatives (and their voluminous background materials, in Japanese, always detailed and incredibly thorough), the U.S. embassy commercial and political staffs, and the Asia Foundation office, in Jakarta; to the Thailand Development Research Institute, the Institute for Strategic and International Studies, the MITI representatives, both the American and Japanese embassies and Chamber of Commerce staffs, and the Asia Foundation office, in Bangkok; to the Institute for Strategic and International Studies, the Malaysian Institute for Economic Research, the MITI representatives, the American and Japanese embassies and Chamber of Commerce staffs, and the Asia Foundation office, in Kuala Lumpur—my thanks for all their help in arranging introductions, providing valuable background data, and suggesting useful new sources that added considerable depth and perspective to the text.

To Hadi Soesastro of CSIS in Jakarta, Patcharee Sororos at Thammasat University in Bangkok, and Paul Low, chairman of Malaysian Sheet Glass Berhad in Kuala Lumpur, each of whom commented helpfully on early drafts of the manuscript, my grateful appreciation. They know that the opinions and ideas expressed herein are totally mine, and they are absolved of any responsibility for the positions taken (or predictions made) in the text.

To the research staff at the ISEAS Library (whose Xerox copiers achieved new levels of output during my stay), to the staff at Princeton University's Firestone Library, and to the reference librarians at the Princeton Public Library—especially Jane Clinton and Eric Greenfeldt—special thanks, as ever, for special help.

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To my agent, Dominick Abel, who is a gentleman in an often curmudgeonly business; to my publisher, Harvey Plotnick, a man of vision who senses trends (and leverages them) as well as anyone in the industry; to my editors, Bernard Shir-Cliff and Kathy Willhoite, who offered valuable suggestions that have made the text more accessible to the general reader; and to my manuscript editor, Christine M. Benton, who brought her usual high standards of professional performance to bear on both style and content—you each played a strong role in making this production successful, and you have my most grateful appreciation and deepest thanks.

Finally, to my wife, Marty, and our children, Claire and Peter, who shared so many of these experiences during our lengthy stay in Southeast Asia, my heartfelt gratitude and love for making our peripatetic family so strong, so flexible, and in the end analysis so durable.

Despite the generous assistance, advice, and guidance I have received from one and all, including those who preferred to remain anonymous, I alone remain responsible for the interpretations, opinions, and judgments rendered throughout the text, and any errors resulting therefrom are of course my own.

Princeton, New Jersey
January 1991

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Asia's New Little Dragons

1
INTRODUCTION
Of Dragons Old and New

The copycat days are over. Japanese industry is well on the way to becoming not just self-sufficient in technology, but a big exporter of know-how, as well. Its engineering laboratories are brimming with ideas that have been cultivated entirely at home. Japanese firms now have a virtual stranglehold on the technologies for making cars, cameras, semiconductor memory chips, video equipment, fiber optics, machine tools, industrial robots, flexible manufacturing systems, quality steels, and composite materials. Japanese firms are responsible for almost half of the patents being filed around the world. All this, and they are only just getting into their stride.

In the process, Japanese industry is being remade. Since 1986, Japan's economic growth has come exclusively from domestic demand; net exports have [declined as] imports have risen on the back of a soaring yen. Japanese firms have hastened the process along by exporting their know-how to subcontractors in South Korea, Thailand, and Taiwan, who then manufacture the goods for them and stick on Japanese labels. [This] new direction suggests a shift from the export of products to the export of software and services, centering on advanced technology.

—Nicholas Valéry, "Japanese Technology: Thinking Ahead," *The Economist*

During the past two decades, close on the heels of Asia's economic miracle—Japan—the world has witnessed the explosive growth of South Korea, Taiwan, Singapore, and Hong Kong, East Asia's so-called Little Dragons, whose aggressive export strategies, close

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government/business cooperation, strong public education systems, high rates of savings and capital formation, and soaring personal incomes have put American firms under increasing competitive pressure and have caused the United States to rethink its own neoclassical economic theory and free-trade philosophy.

For the past twenty years the Little Dragons have generated the highest rates of growth in the world, with the annual average at 9 percent compared with nearly 5 percent in Southeast Asia, less than 4 percent in Latin America, under 3 percent in Africa, and just over 2 percent for the United States. Most recently, for the five years from 1983 to 1988, their average growth rates were nearly in double digits: 10.2 percent for Taiwan, 9.5 percent for Korea, 9 percent for Singapore, and 8.1 percent for Hong Kong. What's more, these four countries *alone* accounted for almost two-thirds of *all* manufactured goods exported during that time. Together with the front-runner, Japan, two of them—Korea and Taiwan—had amassed nearly $200 billion in official foreign exchange reserves by 1988, around four times the U.S. level and nearly half the world's total, and the same three countries accounted for about two-thirds of America's total global trade deficit.

In fact the economic growth rates of the Little Dragons have been so strong—with their export strategies so aggressive and their per-capita incomes so high—that Washington has taken an increasingly harsh view, reacting with protectionist sentiment rather than attempting to adjust and adapt to these new forms of Asian-Pacific dynamism. But contrary to popular perception, the Little Dragons were not exporting just to America. By 1988, while some 30 percent of Korea's trade was with the United States, more than 25 percent was with Japan; Taiwan was shipping about a third of its exports to America but more than 20 percent to Japan; Hong Kong was sending 18 percent of its exports to the United States, but 12 percent to Japan; and 19 percent of Singapore's exports were going to the United States, but 15 percent to Japan. The best-kept secret of East Asian growth is that trade *within the region* now constitutes nearly half of its total: intraregional trade among the Little Dragons themselves exploded by almost 50 percent in 1988.

By early 1988 Washington had graduated all four countries from its Generalized System of Preferences (GSP), which previously gave certain of their exports preferential tariff treatment. In mid-1988

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Representative Richard Gephardt of Missouri, an early Democratic candidate in the presidential primaries (and now majority leader of the House), called for punitive tariffs against Korea's automobile exports to reduce their price competitiveness in the United States. And throughout 1989 America's trade officials pressed both Korea and Taiwan to "open" their markets further to American products, such as cigarettes and farm goods, creating an unprecedented amount of anti-American sentiment in these countries.

In the meantime some observers of these trends have argued that the strategies and tactics used by the Little Dragons cannot be sustained. That their success is a limited, one-shot achievement that cannot be replicated. That America will not be able to keep its market as open as it has in the past if these sorcerer's apprentice economies cannot learn to control their aggressive behavior. "It is time to ask," one analyst noted, "whether any more developing countries can really hope to become the South Korea of the late 1980s or the Hong Kong of the early 1990s."

But right behind the four Little Dragons are three *more* East Asian economies—Indonesia, Thailand, and Malaysia—sitting on the runway revving up for takeoff, expanding at double-digit rates of growth since 1986 or 1987. Thailand's growth has been so rapid that its physical infrastructure—roads, highways, and port facilities—has become saturated to the point of gridlock as more and more Thai manufactured exports head for foreign markets. Indonesia, in a period of less than three years, had a *higher* percentage of exports in manufactured goods by 1989 than it did in gas and oil, and this from a country which is a member of OPEC. Malaysia, in addition to being the world's number-one exporter of palm oil, rubber, and tin, is today the world's leading exporter of computer chips and the third-largest manufacturer of semiconductor devices overall after Japan and the United States.

Why has this been happening? How have three more East Asian nations been able to achieve rapid economic development so closely on the heels of their northeastern neighbors, while the sluggish economies of Latin America and Africa remain heavily burdened with debt, severely shackled by inflation, deeply mired in socialist ideology, and firmly entrenched as spectators of rather than participants in the international trading system that the dynamic nations of East Asia have so successfully mastered?

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THE ALPHABET SOUP

In the "old days," going back some thirty years, there were essentially just two categories of economic development: the industrialized (or developed) nations of the West (and Japan), and the developing nations, called lesser developed countries, or LDCs. Beginning around 1970, however, as the pace of economic growth in East Asia began to quicken, countries like Korea and Taiwan chafed at being categorized as "lesser developed"—especially since the noneconomic sides of their cultures, such as their social organization and rich historical traditions, were in fact highly developed—so they collectively became known as newly industrializing countries, or NICs, instead. Then, as their economic growth rates exploded throughout the 1970s and 1980s, the four East Asian NICs earned their popular nicknames—the Little Dragons. They quickly left the Philippines behind, even though that country had had the region's highest per-capita income a generation earlier.

Culturally, of course, China was the Big Dragon, even though its economy was wedded to the failing ideology of communism and concepts more appropriate to the nineteenth century. But economically Japan, too, was a Big Dragon since its GNP comprised about 80 percent of the total East Asian output of goods and services. Still, the four Little Dragons owed much if not all of their own cultural heritage to China: Taiwan was itself a former Chinese province, occupied and governed by mainlanders since 1949 as the Republic of China; the population of Singapore was three-quarters Chinese, although its society and government were characterized by strong multiracial interaction based also on Malay and Tamil traditions; Hong Kong was by origin virtually a Chinese city, despite its heritage as a British colony; and Korea had adapted its own Confucian traditions from China. All four of the Little Dragons were quintessentially chopstick cultures: like chopsticks, individually the people would break, but together they were strong and durable.

But by the mid-1980s, as the three Southeast Asian economies began accelerating, the terminology started getting a bit confused. Thailand, Indonesia, and Malaysia were being called the new NICs, to distinguish them from the Little Dragons, which had now become the old NICs, so a new designation clearly was needed.

Enter the newly industrializing economies, or NIEs (pronounced

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knees). But the NIEs clearly weren't yet industrializing as rapidly as the NICs. Whatever the yardstick, NIEs were by no means clones of NICs.

But the designation seems to have survived, so throughout this text the Little Dragons of Korea, Taiwan, Singapore, and Hong Kong are NICs, while the now rapidly growing economies of Indonesia, Thailand, and Malaysia are referred to as NIEs.

THE DESCRIPTIVE CHARACTERISTICS

Economists, businesspeople, and journalists tend to use just two or three simple yardsticks when measuring a country to see if it qualifies as a NIC: per-capita income, manufacturing as a percentage of total GNP, and manufactured goods as a share of total exports.

If we use these three conventional parameters of economic performance alone, how do Japan and the NICs fare?

ECONOMIC PERFORMANCE OF JAPAN AND THE NICs
(As of December 31, 1989; US$, %)

Category	*Japan*	*Korea*	*Taiwan*	*Singapore*	*Hong Kong*
Per-capita income	23,539	4,968	6,889	10,810	10,918
Manufacturing as % of GNP	30.9	34.5	35.6	30.1	26.7
Manufactured goods as % of total exports	86.7	94.5	96.8	81.3	88.0

The price of admission for joining the NICs' club is generally considered to be a per-capita income of at least $3,000, manufacturing equal to 25 percent or more of GNP, and manufactured goods comprising not less than 25 percent of total exports. All the Little Dragons qualify easily.

But while these three characteristics may represent a statistical snapshot of an economy's overall performance at any time, they overlook a number of more complex economic, historical, and cultural factors that are crucial in determining whether a country may in fact be called a NIC.

These factors—and there are about a dozen of them that are key—have played a seminal role in the impressive development of

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the NICs and, before them, Japan (though Japan had emerged as an industrial powerhouse long before the NIC terminology became popular). These twelve characteristics—with the first five or six being the most important—are discussed on the following pages in descending order of relevance.

1. An Authoritarian Political System

Perhaps the most frequently overlooked factor in the recent rise of East Asian economies, political authoritarianism has created a solid base of stability from which economic growth could proceed. *None* of these countries (Japan included) has picked representative democracy as the political model on which to base its economy. Since 1955 Japan has been dominated by a single-party system, controlled by the Liberal Democratic Party (the LDP), a group of conservatives whose primary policy focus has always been to maximize Japan's national economic interests by benefiting producers at the expense of consumers. Similarly, Singapore's politics have been controlled by Lee Kuan Yew's Political Action Party (the PAP) since well before the Lion City became an independent nation in 1965. These two systems have employed what some analysts call "soft" authoritarianism, in contrast to the "hard" variety of authoritarianism practiced until only very recently by South Korea and Taiwan.

From the time Park Chung-hee took control of South Korea in 1961 until his successor, Chun Doo-hwan, stepped down in 1987, the country's political system was virtually dominated by the army—a kind of martial law in mufti. Taiwan was literally ruled by the military from the time Generalissimo Chiang Kai-shek fled from the mainland in 1949 until his son, Chiang Ching-kuo, canceled the martial law order in September 1987, shortly before his death a few months later.

Both countries have now planted the delicate seeds of democracy, but their political economies were dominated by firm authoritarian rule for nearly three decades, the decades underpinning their rapid economic growth. Taiwan's political system is still controlled by a single party, the Kuomintang, despite recent liberalization that permits the participation of opposition parties. And by early 1990 Korea had merged two of its own opposition parties into the govern-

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"The more one probes the magnificent archipelago of Indonesia, with its uncompromising beauty, its rich storehouse of natural resources, and its incomparable depth of human talent, the more one comes away with the sense that for Indonesia the best is yet to come."

"Thailand has been increasingly singled out as the next Little Dragon. But against its extraordinary strengths, Thailand has a veritable abundance of shortcomings—a long list of liabilities that could eventually cause the Thai economy to stagnate and fall behind its regional competitors."

"Malaysia's bottom line is that it should have done much better. With its political system corrupt to the core, its people suppressed by a government that is moving ever closer to totalitarianism, and its social stability threatened by clearly racist policies, Malaysia is a nation with an inferiority complex."

Can Indonesia, Thailand, and Malaysia repeat the successes of Japan and the Little Dragons of the 1970s and 1980s? What policies are being created and implemented to enable these Asian nations to succeed? How much of their success is attributable to indigenous factors—political, social, cultural, educational—and how much relies on external developments? Why is Japan giving these three potential new Little Dragons priority attention, while America is not? What are the implications for American foreign and economic policy—in both the public and the private sectors—if these three nations continue their explosive growth? Will they be our partners or our foes? This book answers these questions and provides a framework

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