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No. 227/2012 dated 17 December 2012

Between Developmentalism and Populism: Walking a Tightrope in Southeast Asia

By Julius Cesar I. Trajano

Synopsis

Southeast Asian economies remain resilient to weak global growth primarily due to buoyant domestic consumption backed by strong government spending. Given the scarce resources of governments, they have to strike a balance between populist measures and fiscal discipline.

Commentary

DOMESTIC CONSUMPTION, primarily fuelled by household and government spending, currently serves as a driver of economic growth in Southeast Asia as exports are hit by weak global demand. In particular, the ASEAN 4 economies (Indonesia, the Philippines, Malaysia and Thailand) have been growing on the fast track. For the third quarter, the Philippine economy grew by 7.1%, Indonesia 6.2%, Malaysia 5.2% and Thailand 3%.

The ASEAN 4 governments adopt expansionary fiscal measures to spur growth and boost domestic consumption. Crucial to fiscal spending is the issue of how the state should distribute its scarce resources for public infrastructure and populist schemes.

Public infrastructure spending

Across Southeast Asia, massive infrastructure projects are being planned and implemented by governments in order to enhance domestic consumption.

In Indonesia, the major drivers of growth are private consumption and government spending, contributing 60% of GDP. This year's capital expenditure of USD16.2 billion will increase by 15% to USD20.3 billion next year with infrastructure development as the main priority. Indonesia targets to build more power plants, 560 kilometres of roads, 380 kilometres of rail tracks and 15 additional airports.

In the Philippines, where domestic consumption comprises 70% of GDP, the government allotted USD8 billion this year to infrastructure spending, which will hit a record high of USD9.6 billion next year. In Thailand, a USD1.5-billion highway is being constructed, spanning from Bangkok up to the Thai-Myanmar boundary. The construction of Bangkok-Nongkhai railway, which will be linked to Laos, will start in January. Over the next ten years, Thailand intends to spend USD80 billion for infrastructure and USD90 billion to improve connectivity in the Greater Mekong Region.

Malaysia allocated this year USD10 billion for public infrastructure, industrial and rural development. The construction of a new MRT line in Kuala Lumpur, estimated to be worth more than USD10 billion, has recently started. Next year, the government will spend USD16 billion on roads, railways and hospitals.

The accelerated infrastructure spending in the region is expected to boost ASEAN's connectivity. The building of roads, seaports, airports and railways strengthens the ASEAN Economic Community, facilitating unhampered flow of goods, capital and skilled labor across the region by 2015.

Furthermore, the recent and upcoming infrastructure projects will significantly lower the cost of doing business, improve market accessibility and enhance competitiveness of ASEAN countries. According to the World Economic Forum's 2012 Global Competitiveness Report, shoddy infrastructure is still dragging down the investment climate in both Indonesia and the Philippines. Analysts say Indonesia, in particular, can easily grow by 7% to 8% if it can improve its infrastructure.

Populist economics

The ASEAN 4 economies have also adopted populist measures, such as subsidies and cash dole-outs, which are not only aimed at inducing domestic spending, but also boosting the popularity of ruling political parties.

Indonesia's 2013 budget was drafted with populist considerations. Despite calls from economists to scrap the highly popular oil subsidy scheme and a World Bank report that such scheme does not really help the poor, fuel subsidies will increase by 36% from USD21 billion this year to USD29 billion in 2013.

Similarly, the Malaysian government has allocated USD14 billion worth of food and fuel subsidies, taking up 18% of its revenues this year. With a close eye on the forthcoming general election the Barisan Nasional government announced fiscal sweeteners this year such as educational aid to the ethnic Indian community, USD821 million worth of cash handouts to lower-income households and bonuses to 1.3 million civil servants as well as special payouts to retired employees amounting to USD714 million.

Under the populist rice buying programme, a key electoral pledge of Thai Prime Minister Yingluck Shinawatra's political party, Thailand's government purchases rice from farmers at 15,000 baht per tonne which is higher than the market rate of 9,000 per tonne. The Philippines likewise has its own version of cash handouts, the Conditional Cash Transfer (CCT) Programme. For this year, there are three million poor household beneficiaries of CCT with a budget of USD930 million, which will be increased to USD1 billion in 2013.

Populism versus fiscal prudence

Crucial to public spending is how governments identify their priorities. Clearly, populist 'band-aid' measures lead to a paucity of available resources for the needed infrastructure spending. For instance, the Philippines' infrastructure investment is merely equivalent to 3% of GDP, below the 5% average for the region. Indonesia, meanwhile, is even spending more on fuel subsidies (18% of the national budget) than infrastructure. Thailand expects to lose USD2.6 billion, or one-fifth of its budget deficit this year, from its rice intervention scheme.

Southeast Asian governments adopt populist measures not only to induce domestic consumption but also to strengthen their political/electoral base. These measures are essentially not grounded on economics but on political considerations.

With the declining popularity of Indonesia's ruling Democrat Party and the approaching legislative and presidential elections in the next two years, it would be difficult for the members of the Indonesian parliament to support an unpopular move such as scrapping fuel subsidies. One important political strategy of Malaysian Prime Minister Najib Razak is to use financial handouts to get electoral support of the Malay-Muslim majority, rural households and the mammoth government workforce.

Thailand's rice buying scheme is also intended to buttress the political base of PM Yingluck and her political party in the countryside. Far better for them to pursue long-term rural development measures that effectively address the highly politicised urban-rural socioeconomic dichotomy in Thailand. In the Philippines, critics of CCT are wary that the programme will be used by local officials to buy votes in the 2013 mid-term polls. While the intention of the government in implementing CCT may be noble, it would be better to channel more funds to its agrarian reform programme which could sustainably boost both the farmers' incomes and productivity.

Given their scarce fiscal resources, ASEAN governments would do well to reduce or completely stop funding populist-driven 'band-aid' measures and focus more on long-term state investments that would raise the people's disposable incomes and bring about sustainable economic growth and development. In short, governments must walk a tightrope between populism and fiscal discipline.

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