

The Pro-poor Infrastructure Development

By: Mr. Dyna Heng*

When the precondition of the basic infrastructure and human capital (health and education) are in place, markets are powerful engines of development.¹

-Jeffrey Sachs

Under the harsh winds of globalization, developing countries are struggling to develop. The member countries of the Association of Southeast Asian Nations (ASEAN) have been actively participating in the globalization process and are leading the community to develop to an appreciated level.

However, poverty remains a problem in most of the ASEAN countries. While Cambodia, for instance, has been integrated into the international community since the 1993 election, has implemented reforms, has strived to attract foreign direct investment (FDI) and has increased its exports of garment products, around 35% of its people still subsist on less than US\$1.00 a day.²

Meanwhile, economic prosperity does not arrive without larger societal ramifications. It brings the collateral effects of income inequality and environmental degradation. In many occasions, this affects the poor the most. Consequently, some of the poor have become poorer.

The poor are poor not because they are lazy or born to be poor. According to Dr. Muhammad Yunus, the 2006 Nobel peace laureate, poverty is:

Created by the social system, it is created by the institutions, it is created by policies that we pursue. We should not be looking for the causes of poverty among the poor. We should be looking at ourselves, those who make the decisions and design institutions³

Professor Joseph Stiglitz also discussed the cycle of poverty, saying that:

The poor are caught in a series of vicious spirals: lack of capital leads to that of foods and to ill health, which limits their earning ability, leading to still poorer health. Barely surviving, they cannot send their children to school, and without an education, their children are condemned to a life of poverty.⁴

Poverty reduction has become an increasingly important development priority. To deal with the problem, some economists argue for "trickle-down economics" (footnote 4), which means growth will benefit all and finally even the poor. Yes, growth and poverty reduction may be correlated, but the local government has much to do with its smooth correlation and even causality.

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¹ Sachs, Jeffrey. 2005. *The End of Poverty*. New York: Penguin Books.

² Asian Development Bank (ADB). 2005. *Annual Report*. Manila.

³ Yunus, Dr. Mohammad. 1995. *Overcoming Poverty through Entrepreneurial Empowerment*. Available: http://www.ms-foundation.org/awardees/1995/content/muhammad_yunus_speech_1995_en.pdf

⁴ Stiglitz, Joseph. 2002. *Globalization and Its Discontents*. New York: W.W Norton & Company.

How does the globalization of economic infrastructure affect poverty in each country? What policy measures would minimize the adverse effects and see benefits from infrastructure expansion at the same time?

Economic infrastructure, which could be categorized into hard and soft structures, plays an important role in the drama of answering these questions.⁵

This humble paper is divided in three parts. The first part briefly reviews the challenges in hard infrastructure development. The second part lays out the components of soft infrastructure, its development and its consequences for developing countries. The third part contains my personal views on future development in the Asia Pacific region.

The Pro-Poor Hard Infrastructure

Economic growth is often discussed in terms of industry, infrastructure, and monetary and fiscal policies. Economics focuses on the keys to growth as a mechanism to achieve broader future development.

For infrastructure, ASEAN has initiated many projects to build roads and bridges to connect its members. This fosters and smoothes the flow of goods, services and people, which contributes to economic integration and development within the region.

Cambodia is also in the mainstream. It has been under the globalization storm of economic infrastructure, both hard and soft. Nonetheless, some projects, such as those involving the building of dams and public roads, have hurt the poor who were relocated without fair compensation and attention from local authorities.

True, it is important to get the country connected to the region for economic purposes, but local governments should begin projects with more clear-cut and careful measures in order to minimize the impacts on the poor while also serving the good purposes of the project and the poor themselves.

The Pro-Poor Soft Infrastructure

The development of soft infrastructure is more complicated. It includes trade and financial liberalization, fiscal and monetary reforms, and governance. Most of these have to be accompanied by careful pacing and sequencing, as Professor Stiglitz noted in his book, *Globalization and Its Discontents* (footnote 4). For example, financial market liberalization has to be accompanied by appropriate regulations or it could cause economic instability. The 1997 East Asian financial crisis provided many lessons about this.

Without proper measures and implementation, soft infrastructure is the root of the gap between rich and poor and makes the poor even poorer as a result of environmental degradation.

Trade Liberalization. Utilizing the “comparative advantage” theory of David Ricardo,⁶ trade benefits all. Trade liberalization, which simply means reducing tariffs and dropping barriers, is the hot discussion in international economics and at the World Trade Organization (WTO).

⁵ I have used the terms “soft infrastructure” and “hard infrastructure” based on my comparison of “software” and “hardware” in the computer world.

⁶ Ricardo, David. 1817. *On The Principles of Political Economy and Taxation*. Third Edition. London: John Murray. Available: <http://socserv2.socsci.mcmaster.ca/~econ/ugcm/3ll3/ricardo/prin/index.html>

With trade liberalization, developing countries have been pressured to reduce their tariffs, which in many cases is the main source of their fiscal revenue. Through the lens of fiscal view, lower fiscal revenues will negatively affect the budgets for education and healthcare and the poor will be affected the most.

Through the lens of competition, swift liberalization without proper measures will hurt the economy. Developing countries, which are still equipped with poor infrastructure, may not be ready to compete. As a result, local firms could go bankrupt due to harsh competition from international firms (footnote 4). Jobs will be destroyed, and the poor will be the first to be affected again.

It is even more unfair when the rich countries close their doors to trade through barriers or subsidies while telling developing countries to open their markets.

Thus, the concept that trade benefits all does not make sense on its own. There is much to be done by local governments to ensure that this concept is fulfilled, and benefits from trade are realized.

With healthy infrastructure and careful implementation of trade liberalization, countries could benefit from trade. This is supported by the fact that countries such as Malaysia, People's Republic of China (PRC) and Singapore have reaped huge benefits from trade and globalization (footnote 4).

Hence, while being committed to development, developing countries should begin with a healthy safety net and measures before getting into the trade game. At the same time, the rules of the game, which are usually set by developed countries, should be fair.

Financial Structure. The financial sector is one of the most important parts of the economic infrastructure; however, it is also one of the main causes of economic volatility.

Financial market liberalization, one of the main pillars of the Washington Consensus,⁷ a set of policies designed to respond to trade issues in Latin America, often causes problems. It is usually argued that financial market liberalization can provide developing countries with access to the capital they need for economic development, which reduces poverty through job creation.

However, the financial crisis has provided many lessons on the flow of capital. Developing countries need to pay more attention to the types of capital, whether it is hot money or a long-term investment. As many economists have argued, the former was one of the main causes for the instability that led to the crisis.⁸

Failure in the financial sector can bring a country into recession. Developing countries are more likely to be affected by this, as they are still equipped with poor infrastructure. In that case, the poor are the first to be affected.

The sun shines after rain. While the 1997 financial crisis taught Asia a very painful lesson, it was also a starting point where developing countries became more cautious about performance and reform in the winds of globalization. Shortly after the crisis, for example, the Chiang Mai Initiative⁹ was formed to prevent countries from future exchange rate crises.

⁷ Center for International Development at Harvard University. *Global Negotiations Home Page: Washington Consensus*. Available: <http://www.cid.harvard.edu/cidtrade/issues/washington.html>

⁸ Ito, Takatoshi. 2001. Growth, Crisis, and the Future of Economic Recovery in Asia. In *Rethinking the East Asian Miracle*, edited by Joseph Stiglitz. Washington, DC: World Bank.

⁹ Institute for International Economics. *The Chiang Mai Initiative*. Available: http://www.iiie.com/publications/chapters_preview/345/3iie3381.pdf

Despite this, countries have to be cautious in forming policies and ready to forestall possible similar crises.

Fiscal and Monetary Policies. While monetary policy secures macro level stability through low inflation and unemployment, fiscal policy supports public welfare, mainly healthcare and education, and ensures fair income redistribution between the haves and have-nots. Recently, developing countries have successfully prevented hyperinflation and have been pressured by donor and creditor countries to pursue fiscal reform.

However, developing countries should be careful before taking any steps towards fiscal reform. According to Professor Stiglitz,

Fiscal austerity, pursued blindly, in the wrong circumstance, can lead to a high unemployment and a shredding of the social contract (footnote 4).

The Government is responsible not only for market failure but also social injustice.

Governance. Many studies point to the fact that good governance and FDI are interrelated. Good governance has been defined as:

The manner in which power is exercised in the management of a country's economic and social resources for development. Good governance ... is synonymous with sound development management.¹⁰

To compete and exploit the benefits of globalization, developing countries should focus on the quality of their governance and laws. Rules of law, control of corruption, accountability, political stability, government effectiveness, and regulatory quality are all important dimensions of governance that factor into a country's development and its ability to attract FDI.¹¹

FDI provides many benefits to a country. It creates jobs and brings technology to the host country. It provides access to foreign markets and sources of finance, which are important for development. The successful development of Malaysia, PRC and Singapore serve as an example of the importance of FDI (footnote 4).

Thus, developing countries should commit to improving the quality of governance as a pro-poor infrastructure that will not only provide good social services to their people, but also attract FDI, an indirect tool to alleviate poverty.

The Road Ahead

As seen in the history of economic development, industry and infrastructure developments are important and necessary for growth. At the same time, governments need to ensure that they have pro-poor industry and infrastructure. The poor must be guaranteed access to healthcare and education.

As a small bird in the forest, the Government of Cambodia needs to pay careful attention to its policy reforms and infrastructure development to ensure the benefits of

¹⁰ ADB. 1997. *Governance Bank Policies. Operations Manual*. Manila.

¹¹ Kaufmann, Daniel, Aart Kraay, and Pablo Zoido-Lobaton. 1999. *Governance Matters. Policy Research Working Paper, no. 2196*. Washington, DC: World Bank.

getting into the international community. Blindly following the guidance of foreign experts without thorough discussions could get the country into the wrong place and fail to exploit the flow of globalization. Meanwhile, Cambodia needs to be more aggressive and determined in designing and implementing pro-poor economic policies to alleviate poverty.

It is sometimes said that the twenty-first century is the century of Asia. I am optimistic and strongly believe that Asia can prove it. While the ASEAN countries are working hard to build up their ability to compete and develop, the leading geese,¹² mainly India, Japan, PRC and Republic of Korea, can play an important role in securing the region's political and economic stability. International institutions such the Asian Development Bank, International Monetary Fund and World Bank can also cooperate to provide technical and necessary assistance to the following geese.

The judgment of "bad" or "good" is applied not to globalization, but to how it is managed. It is a fact that globalization has brought huge benefits. East Asia's success was based on globalization, in particular, trade opportunities, increased access to markets, and technology. However, economic prosperity comes with a larger societal impact; it produces not only prosperity but also the collateral effects of income inequality and environmental degradation. The challenge facing governments and policymakers is how to address these problems while minimizing market distortions and without sacrificing growth. Countries should design more pro-poor policies while maintaining growth at the same time.

There is an old Chinese saying that "A thousand mile march begins with a small step." I believe that with a strong commitment to cordial relationships, Japan and the PRC can put their painful history behind them and focus more on the welfare of the people and development in the Asia Pacific region. The stability and desire for development-for-all would then create a good and stimulating environment for the development of other countries in the region; which is another step towards the achievement of Millennium Development Goals.

¹² Akamatsu, Kanae.1962. A Historical Pattern of Economic Growth in Developing Countries. *Journal of Developing Economies* 1 (March - August): 3-25.