CBO MEMORANDUM

THE ROLE OF FOREIGN AID IN DEVELOPMENT: SOUTH KOREA AND THE PHILIPPINES

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CONGRESSIONAL BUDGET OFFICE

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SECOND AND D STREETS, S.W.
WASHINGTON, D.C. 20515

NOTES

All years referred to in this memorandum are fiscal years unless otherwise noted.

All dollar amounts are expressed in 1997 dollars unless otherwise noted.

Numbers in text and tables may not add to totals because of rounding.

What role does foreign aid play in promoting the economic development and improving the social welfare of countries in Africa, Asia, and Latin America? That question is difficult to answer and has been the subject of much debate among development specialists as well as Members of Congress and the American public.

Drawing on the works of other scholars, this memorandum analyzes the role of foreign aid in the development of South Korea and the Philippines between 1953 and 1993. It is one of three memorandums that are being published as background for *The Role of Foreign Aid in Development,* a Congressional Budget Office (CBO) study published in May 1997. The memorandums are intended to illustrate more fully the themes identified in the main study.

Eric J. Labs of CBO's National Security Division prepared the memorandum under the general supervision of Cindy Williams and R. William Thomas. Richard Fernandez, Kim Kowalewski, and Christopher Williams, of CBO provided valuable comments. Many officials of the Agency for International Development (AID), the World Bank, the Asian Development Bank, and the Organization for Economic Cooperation and Development also provided information. In particular, the author would like to thank Ellen Peterson and Cheryl Warner. The author would also like to thank Nicholas Eberstadt of the American Enterprise Institute and Harvard University, who reviewed an earlier draft of the manuscript. The author and CBO, however, bear full responsibility for the final product.

Sherry Snyder edited the manuscript. Judith Cromwell prepared it for publication.

Questions about the analysis may be addressed to Eric Labs at (202) 226-2900.

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The Congressional Budget Office (CBO) is publishing a series of memorandums that describe the role that foreign aid has played in the development of various countries. The memorandums illustrate the broad themes identified in CBO's May 1997 study *The Role of Foreign Aid in Development.* The countries are studied in pairs: South Korea and the Philippines, Costa Rica and Honduras, and Botswana and Zambia. This memorandum examines the development history of South Korea and the Philippines. Although both countries have received substantial amounts of foreign assistance, South Korea has been relatively more successful in achieving long-term economic and social development.

In 1960, the Philippines was slightly richer than South Korea. The Philippines had a slightly larger per capita gross national product (GNP) and a far larger base of natural resources. By the 1990s, however, Korea's per capita GNP was three times greater than that of the Philippines. In addition, South Korea's social indicators have shown greater improvement.

Many different factors explain the divergence in development between South Korea and the Philippines. Some are unique to the individual countries. But what seemed to matter most was that the political and economic policies of South Korea over the past 30 years were much more favorable to long-term growth and development than those of the Philippines. Foreign aid helped South Korea's development somewhat, but it arguably hindered the Philippines' development by reinforcing the government's political and economic policies.

The most important period in South Korea's development began after the fall of the regime of Syngman Rhee in 1960. General Park Chung Hee, who took over in a military coup in 1961, instituted a process of economic reform. He devalued the currency, reformed interest rates, imposed tighter fiscal policies, lowered trade barriers, and, especially, put in place a number of incentives to encourage exports. In many ways, South Korea's exports were the central driver of its successful development. The government has maintained a relatively open, market-based economy ever since. In addition, the government has been stable and a competent administrator, with only relatively modest amounts of corruption.

Foreign aid after 1960 contributed to South Korea's successful development. It provided an extra pool of capital that the economy used for saving and investment. The Agency for International Development (AID) provided extensive technical support to the officials and agencies responsible for South Korea's export drive. U.S. military aid helped Korea with its defense needs and thus possibly freed up some resources that could be used for development rather than for the military. Foreign

assistance also helped improve South Korea's health, education, and agriculture sectors.

In contrast, the election of Ferdinand Marcos as the Philippine president in 1966 led the country down a path that was ultimately counterproductive to long-term development. Marcos pursued more inward-oriented economic policies than those pursued by South Korea. Marcos's policies produced aggregate economic growth initially, but in the 1980s the Philippine economy experienced a severe crisis, leading to substantial declines in per capita GNP. Moreover, the average rural or urban worker was far worse off at the end of the Marcos era than at its start. Corruption and self-aggrandizement on the part of Marcos and his family and friends contributed to the economy's problems. Reforms under Marcos's successors—Corazon Aquino and Fidel Ramos—have made some progress in reversing the damage done by the Marcos era, but the Philippines' future, though promising, remains uncertain.

The record of foreign aid to the Philippines is mixed. On the one hand, foreign aid contributed to some of the improvement in the social indicators, particularly those for health and education. On the other hand, to the extent that $33 billion in foreign assistance (in 1997 dollars) to Marcos perpetuated his hold on power, it undermined the Philippines' long-term development. Much of that money was apparently lost, wasted, or diverted by the Marcos government. However, foreign assistance has apparently helped the Philippines emerge from the problems created during the Marcos era.

INTRODUCTION

This memorandum is one of several to be published by the Congressional Budget Office (CBO) on various developing countries and the role that foreign aid has played in their development. CBO has published a study titled *The Role of Foreign Aid in Development* (May 1997). Through a broad review of the academic and policy literature on development, that study attempts to identify the conditions that seem to foster development and the role that foreign aid plays in that process. It also highlights the general themes gleaned from the literature with illustrations from eight developing countries: South Korea and the Philippines, Costa Rica and Honduras, Botswana and Zambia, and Tunisia and Egypt. This memorandum examines the development history of South Korea and the Philippines. Although both countries have received substantial amounts of foreign assistance, South Korea has been relatively more successful in achieving long-term economic and social development than has the Philippines.

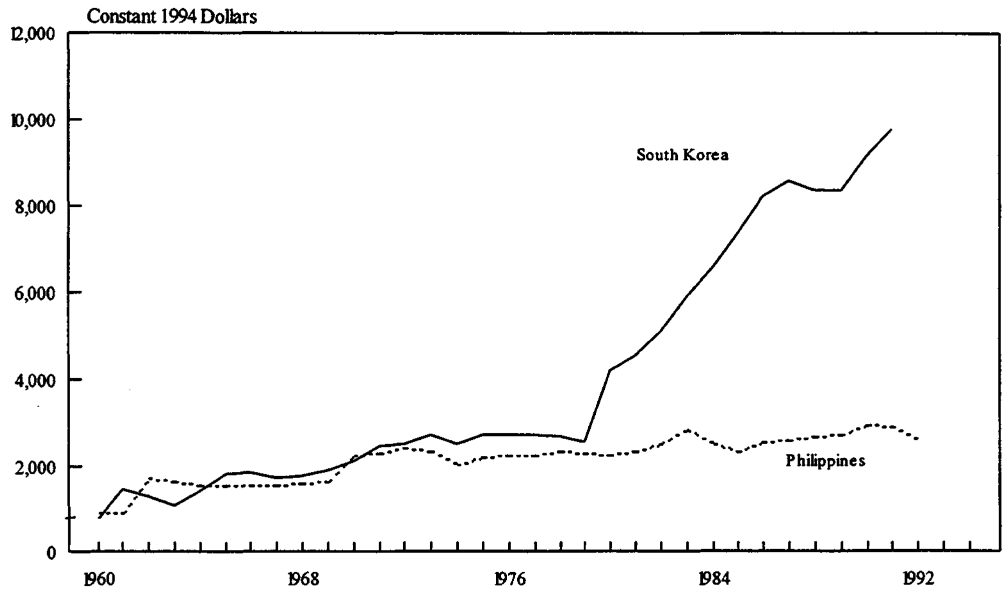
South Korea and the Philippines have two very different development histories. In 1960, the Philippines was the richer country. If one had polled development experts to ask which country was more likely to achieve the higher rate of growth over the next 30 years, most would probably have named the Philippines. In reality, few other developing countries have matched South Korea's rate of growth and overall success in development since the end of World War II, whereas the Philippines has grown much more slowly.

South Korea is the smaller country. In 1996, it had a population of 45 million, occupying 98,000 square kilometers of land. The Philippines had 75 million people living on an archipelago of nearly 300,000 square kilometers. The Philippines has a larger and more diverse base of natural resources. South Korea has a temperate climate; the Philippines' is tropical.

Furthermore, although both countries have relatively homogeneous ethnic populations, South Korea has more religious diversity. Nearly 96 percent of the Philippines is Malay, and South Korea is almost completely Korean. Most Filipinos are Christian, but South Koreans are divided fairly equally between Christians and Buddhists.

The development histories of both countries also point to significant differences. In 1960, the Philippines was still the richer of the two; its per capita gross national product (GNP), measured in 1994 dollars, was $911 compared with $800 for South Korea. By 1992, not only had that situation reversed, but the chasm between the two was enormous. South Korea's per capita GNP was three times greater than that of the Philippines (see Figure 1).

FIGURE 1. GROSS NATIONAL PRODUCT PER CAPITA FOR SOUTH KOREA AND THE PHILIPPINES, 1960-1994



SOURCE: Congressional Budget Office based on data from the World Bank and the University of Pennsylvania.

South Korea has made greater progress than the Philippines in other areas over the past 30 years. South Korea's infant mortality and fertility rates have fallen faster than those in the Philippines (see Table 1). Only a small fraction of either country's population has been illiterate since the late 1960s, although South Korea has had slightly higher literacy rates.

A variety of factors contributed to the separate paths that South Korea and the Philippines have taken. As would be true in any case, unique cultural and societal influence played a role. But the political and economic management of each country probably mattered as well. South Korea, for the most part, pursued outward-oriented economic policies and experienced only moderate corruption; the Philippines pursued inward-oriented economic policies, accompanied by massive corruption. Both countries received large quantities of U.S. and other international assistance. Depending on when and how it was given, foreign aid seemed to have a positive or negative effect in each case.

SOUTH KOREA'S HISTORICAL LEGACIES

South Korea is perhaps the preeminent development success story of the post-World War II era. In 40 years, it moved from being a war-torn, agrarian economy to a modern industrialized economy. Many cultural, political, and economic factors contributed to that outcome. Although most of the story revolves around political and economic management between 1953 and 1973, ignoring the legacies of Confucianism, the Japanese occupation, and the Korean War would distort the picture of South Korea's development.

Historically, Korea has been a stable and centralized society. It began its political existence as a unified, independent state around the 7th century A.D. and remained that way until Japan made it a colony in 1910. Since being freed from Japanese rule in 1945, Korea has been divided politically between the communist North and the capitalist South.

For centuries, Korea's outside contacts were mostly with China. As a result, the state philosophy of Korea became Confucianism. Two important legacies of that cultural influence were a "great emphasis on education and on a deference within the family, within the community, and within the society that tends to favor individual discipline and social stability."[1] Education was the route to prestige and employment

1. Edward S. Mason and others, *The Economic and Social Modernization of the Republic of Korea* (Cambridge: Harvard University Press, 1980), p. 446.

TABLE 1. SOCIAL INDICATORS FOR SOUTH KOREA AND THE PHILIPPINES, 1967 and 1992

Indicator	1967 South Korea	1967 Philippines	1992 South Korea	1992 Philippines
Infant Mortality Rate[a]	58	72	11	44
Literacy[b]	88[c]	83[c]	96[d]	90[d]
Fertility Rate[e]	4.5	6.0	1.7	3.9
Calorie Consumption[f]	2,547	1,802	3,285	2,255

SOURCE: Congressional Budget Office based on data from the World Bank and the Agency for International Development.

a. Deaths of infants under one year per 1,000 live births.

b. Percentage of literate people in the population over the age of 15.

c. Value is for 1970; value for 1967 is unavailable.

d. Value is for 1990; value for 1992 is unavailable.

e. Births per woman.

f. Per capita per day.

in the government bureaucracy, and many people in Korean society achieved literacy. The labor force became industrious and productive.

Another important legacy of Korea's long history is that it is one of the most ethnically homogenous nations in the world. This lack of social segmentation was beneficial: there were no ethnic impediments to development, no groups were disenfranchised, and no ethnic scores had to be settled. Education could be focused and the population mobilized with relative ease. In addition, no linguistic barriers existed to impede education or development.[2]

In some ways, the Japanese occupation of Korea between 1910 and 1945 may have aided Korea's later development. Japan's contributions included building infrastructure such as railroads, creating a modern monetary system, and establishing an agricultural extension service. It also built a manufacturing base in Korea to support the economic needs of Japan. The Japanese, however, dominated ownership, management, and the technical aspects of the manufacturing base, which ultimately limited the transfer of knowledge to Korea. But the Koreans who did learn something about those processes—both in Korea and as expatriates in Japan—brought their experience in a growing, export-driven economy to the postwar development process.[3]

The Japanese, also influenced by Confucianism, continued and strengthened the emphasis on education in Korean society. The Japanese considered an educated Korean population to be a prerequisite for their integration into the Japanese Empire. At the highest rungs of the educational ladder, a small number of students were educated, but compared with the experience of other countries ruled by different colonial powers, the number was still high.

Yet in other ways, Japan's occupation impeded Korea's development. When the Japanese left in 1945, much of the institutional and manufacturing apparatus was either changed or made unusable because trained and experienced personnel were no longer there to run it. The bitter experience of Japanese colonial rule soured political and economic relations with Japan into the 1960s. For example, during their occupation, the Japanese excluded Koreans from political activity and government. When the Koreans finally had to govern their own country, they were not sure how to do it. That contributed to the political instability of the 1940s and 1950s. As one

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2. David I. Steinberg, *Foreign Aid and the Development of the Republic of Korea: The Effectiveness of Concessional Assistance*, AID Special Study No. 42 (Agency for International Development, October 1985), pp. 9-10.

3. Mason and others, *Economic and Social Modernization of Korea*, pp. 77-79.

report puts it, "at a crucial point in Korean history, Koreans had been deprived of the opportunity to develop effective political institutions of their own."[4]

The Korean War greatly harmed the development enterprise and destroyed a large part of the industrial base. It helped make what was supposed to be a temporary political division in 1945 permanent. But as a result, the energy sources and remaining heavy industry were concentrated in the North, and the light industry and agriculture resided mostly in the South. The fear of another attack by the North caused South Korea to devote enormous resources to its defense, maintaining one of the largest armies in the world. Military influence permeated Korean society, which contributed to the coup of 1961 and the repressive nature of most South Korean governments since 1953.[5]

INFLUENCE OF GOVERNANCE ON SOUTH KOREA'S DEVELOPMENT

During the past 40 years, South Korea's governance—from a developmental perspective—has been better than that of most countries. Although sometimes suffering from internal corruption, the South Korean government has shown the political will to carry out land reform and institute economic and social policies that promote development.

The Structure of Government

South Korea's government from 1953 to 1988 was mostly stable but largely authoritarian. Syngman Rhee ruled South Korea with an iron fist in the 1950s.[6] All power flowed to and from his hands. Rhee was determined to unify the peninsula. Consequently, he was reluctant to invest in industries and activities, such as power generation and fertilizer, that existed in the North, because that would duplicate resources that he assumed he would eventually control once the country was reunited. Rhee was driven from power in 1960 by a student-led revolution.[7]

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4. Ibid., p. 451.

5. Ibid., pp. 86-93.

6. Following convention, CBO puts the family name first for Korean names. The only exceptions are Syngman Rhee, who is best known in the United States with the family name last, and authors of books who are Korean and have placed their family name last.

7. Steinberg, *Foreign Aid and the Development of Korea*, p. 22.

After a brief flowering of democracy, a military coup led by General Park Chung Hee took power in 1961. The coup was actually met with relief among many segments of Korean society. It put an end to the disorder and civil strife that had marked Korean politics since the last days of the Rhee regime. The Park government tried to institute a technocratic government that focused primarily on promoting economic and social development. A new constitution was drawn up in 1963. Under that document, the executive was extremely powerful and the legislature was weak. The trappings of democracy were few. In terms of growth and development, however, the Park government was a successful administration. South Korea's economy took off under Park's leadership.

The governmental structure Park created gave him a number of advantages. First, the military strongly backed the government. Many former officers staffed government ministries and public enterprises. Second, the government was able to implement policy changes that were in the national interest with almost no opposition. Those changes included periodic devaluations, which are often unpopular in developing countries. During the oil crisis of 1973, the government introduced conservation measures—quadrupling the price of gasoline—with little opposition. Third, government policy kept organized labor weak, and strikes were unknown. "Consequently, South Korea has avoided the pressure from organized labor that in many Third World countries has maintained urban wages at artificially high levels, has led to the overstaffing of public enterprises, and has frequently seriously disrupted production."[8]

In recent years, South Korea has evolved toward a more democratic system. After 19 years in power, President Park was assassinated in 1979; his ultimate replacement was another general, Chung Doo Hwan. As South Korea grew richer in the 1980s, the Korean people increasingly demanded more democracy. Roh Tae Woo, another army officer, replaced Chung in 1987. He recognized the growing strength of the democratic movement and merged his party organization with several other parties. Under that new organization, Kim Young Sam was elected president in 1992.

Corruption

Corruption under both Rhee and Park was significant, although hard data on its extent do not exist. Still, corruption in the 1950s was more detrimental than that in later years because of the economic policies pursued by the Rhee government.

8. Mason and others, *Economic and Social Modernization of Korea*, p. 487.

Corruption under Rhee took the form of payoffs from foreign aid funds and bank loans. "Inflation, an overvalued exchange rate, low interest rates, and elaborate government controls formed an environment in which such corruption operated profitably for those involved but to the detriment of sound investments or national economic development."[9]

In contrast, corruption under Park took the form of payoffs from private investment. But the payoffs took place in an economic environment more favorable to growth. Thus, the private capital—"despite payoffs and the like—fed an investment boom that followed reasonably accurate market indicators of real benefits and costs for the country."[10] Investments approved by the government, even though payoffs were extracted from them, had been tested and approved through feasibility studies and were generally consistent with Korea's economic plan.[11]

Education

The government's emphasis on education throughout the postwar period greatly aided the country's economic transformation. In 1945, almost 87 percent of the population was illiterate. That is no longer true, largely because the government has provided six years of free and compulsory education. By 1970, illiteracy had been reduced to 12 percent.

Moreover, enrollment at the secondary level now compares well with that in the advanced industrial countries. But the government cannot claim credit for that improvement. The average family usually must pay out of their own pocket to continue their children's education beyond the primary level. The willingness of the Korean people to make that sacrifice is especially evident in national education expenditures. The government spends about 3.5 percent of GDP on education. Private spending, however, has brought the total spending on education to 9 percent of GNP.[12] According to one study, increased education per worker accounted for

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9. David C. Cole and Princeton N. Lyman, *Korean Development: The Interplay of Politics and Economics* (Cambridge: Harvard University Press, 1971), p. 252.

10. Ibid.

11. Ibid.

12. Lawrence J. Lau, ed., *Models of Development: A Comparative Study of Economic Growth in South Korea and Taiwan* (San Francisco: ICS Press, 1990), pp. 131-132.

nearly 5 percent of South Korea's growth between 1963 and 1982, a rate higher than Japan's over a comparable period.[13]

Land Reform

Another major reform that the government directed was the redistribution of land that Korean landlords held at the end of World War II. Although most of that process took place between 1945 and 1953, it played an important role in Korea's development history. Lands owned by departing Japanese and large estates were broken up and distributed among small tenant farmers by the U.S. military government. But the newly elected Korean government in 1949 imposed land reform on Korean landlords on terms that one study described as "expropriation."[14] In 1945, 48 percent of families owned land. After land reform was completed, that figure rose to above 90 percent. That change had two important effects. It aided the equalization and distribution of wealth; South Korea's later growth was characterized by a high degree of equity. In addition, class tensions were largely diffused, eliminating a potential source of political instability. Moreover, agricultural production did not suffer in the process. Between 1954 and 1975, "the trend rate of growth of agricultural value added was about 3.5 percent per annum."[15]

Economic Leadership

Perhaps the most important role of South Korea's government has been its leadership in directing economic growth and development. In the 1950s under Syngman Rhee, the government pursued policies that in retrospect proved counterproductive. After Rhee's overthrow, however, the Park government adopted economic policies that were conducive to development. The South Korean government largely initiated, directed, and organized development by setting goals, establishing priorities, and backing them up with resources. Large, highly profitable private companies were clearly subordinate to the government, in part because the government controlled domestic credit as well as the right to borrow abroad.[16] It relied heavily on an outward-looking, export-oriented economic strategy, but not exclusively. In certain

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13. Kim Kwang-suk and Park Joon-kyung, *Sources of Economic Growth in Korea: 1963-1982* (Seoul: Korea Development Institute, 1985), p. 169.

14. Mason and others, *Economic and Social Modernization of Korea*, p. 10.

15. Ibid., pp. 10-11.

16. Ibid., p. 486.

sectors, such as rice production and heavy and defense-related industries, the government maintained a predominantly import-substitution strategy.

A good example of the government's leadership in the economy was its management of public enterprises. Under Park, those organizations were efficiently run and contributed to government resources, partly because of the sheer determination of the political leadership to generate growth and to reform anything that might be a drag on the economy. "In Korea, there have been numerous cases of divestiture, most notably in the 1967-1969 period. And if a Korean public enterprise considered important for development shows signs of becoming moribund, it is likely to be vigorously kicked back into life by drastic changes in management and operating procedures."[17] For example, the government asked a private firm to manage Korean Air Lines when it was not profitable as a public endeavor.

INFLUENCE OF DOMESTIC ECONOMIC POLICIES ON SOUTH KOREA'S DEVELOPMENT

The end of the Korean War left the South Korean economy in a devastated condition. The economy's infrastructure was severely damaged. Inflation was high, and the predominantly agrarian economy was constricted by an elaborate system of exchange controls and multiple exchange rates. The primary sector—agriculture, mining, and natural resources—accounted for 50 percent of GNP, and manufacturing represented a little more than 5 percent. Investment accounted for 12 percent of GNP, and the domestic saving rate was less than 7 percent. Foreign savings, mostly foreign aid, represented about 5 percent of GNP.

After the end of the Korean War, the first priority of the Rhee government was economic reconstruction, undertaken largely with foreign assistance.[18] The government kept interest rates low to accelerate investment, believing that domestic saving was not very responsive to changes in interest rates. Industrial policy followed an inward-looking, import-substitution strategy. High tariffs and quotas were used to protect domestic industry. The exchange rate was kept overvalued throughout the 1950s.[19] Promoting exports was a low priority. Exports in 1954 accounted for less than 1 percent of GNP. By 1962, they were still only 2 percent of

17. Ibid., p. 275.

18. Susan M. Collins and Won-Am Park, "External Debt and Macroeconomic Performance in South Korea," in Jeffrey D. Sachs and Susan M. Collins, *Developing Country Debt and Economic Performance*, vol. 3, *Country Studies—Indonesia, Korea, Philippines, Turkey* (Chicago: University of Chicago Press, 1989), p. 166.

19. Mason and others, *Economic and Social Modernization of Korea*, p. 95.

GNP. The government was most concerned with reconstruction and price stabilization.[20] Largely as a result of the reconstruction effort, the economy grew, but high inflation was the price.[21]

Policy Reform and Market Liberalization

By the late 1950s, Rhee's government began to recognize that the United States would not provide high levels of foreign assistance indefinitely and that policy reforms were necessary. The first step the government took was to tighten monetary and fiscal policies to bring inflation under control. Between 1953 and 1957, inflation averaged 31 percent a year, as measured by the implicit price deflator for GNP. After the tightening, the rate of inflation fell to 3.7 percent between 1957 and 1960.[22]

The new Park government made economic growth its first priority. Park changed the industrialization strategy to outward-looking, export-led growth. Perhaps the most important aspect of that effort was a large devaluation of the exchange rate.[23] The government also put in place a number of incentives—such as subsidies, access to subsidized credit, and rights to import goods duty-free—to promote exports. The government assured exporters that it would not allow the domestic rate of inflation to harm the real rate of return on their exports.[24] The government also reformed the national currency, the budget, and tax collections. It adopted the First Five-Year Economic Development Plan (1962-1966). The plan called for an ambitious growth rate—7.1 percent annually—adjusted for inflation.

In the mid-1960s, the Park government continued with reforms designed to promote exports and economic growth. The exchange rate was devalued again in May 1964, and in March 1965 the government adopted a floating exchange rate system. Interest rates on bank deposits and loans were doubled to increase private saving and to discourage wasteful credit. In 1967, the government introduced measures to liberalize imports and lower tariffs. The government did not pay much

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20. Collins and Park, "External Debt and Macroeconomic Performance in South Korea," p. 166.

21. Ibid., pp. 168-169.

22. Ibid., p. 169.

23. Mason and others, *Economic and Social Modernization of Korea*, p. 96.

24. Anne O. Krueger and Vernon W. Ruttan, "Assistance to Korea," in Anne O. Krueger, Constantine Michalopoulos, and Vernon W. Ruttan, eds., *Aid and Development* (Baltimore: Johns Hopkins University Press, 1989), p. 229.

attention to agriculture, however, although it did force farmers to accept a policy of low grain prices.

The First Five-Year Plan was succeeded by the Second (1967-1971), Third (1972-1976), and Fourth (1977-1981). In each case, the overall strategy was essentially the same: promote economic development through export-led growth. Specific policies were modified as necessary to ensure that South Korea's growth remained on track. In 1969, for example, the government began offering farmers prices for their grain products that were high enough to ensure a respectable return. The intent of that policy was to improve the environment of the farm village and increase agricultural production and income.[25]

The South Korean economy was transformed between 1962 and 1982. The primary sector of the economy fell from 45 percent of GNP to 19 percent (see Table 2). Manufacturing, on the other hand, grew from 9 percent of GNP to 34 percent.[26] Economic growth paralleled the rise of manufacturing in the economy. Between 1963 and 1976, GNP grew by 10.3 percent a year. Per capita growth was equally impressive at 7.2 percent a year. Those developments were largely financed by the dramatic rise in domestic saving that government policies had promoted. Domestic saving represented only 3.3 percent of GNP in 1962—half the rate of 1954. By 1982, however, the saving rate exceeded 21 percent of GNP.

Exports grew dramatically in quantity and variety. In 1962, exports accounted for only 2 percent of GNP. That percentage climbed to 16.4 percent in 1972 and to nearly 32 percent in 1982. The change in the number of countries to which Korea exported was particularly astonishing. In 1954, Korea exported to 5 countries. By 1976, it was exporting to 175 countries. According to one study, the expansion of exports accounted for 31.8 percent of the growth in Korea's industrial output between 1963 and 1975. Import substitution claimed only 3.7 percent. In contrast, over the 1955-1963 period, when Korea was still dominated by Rhee's policies, the expansion of exports accounted for 9.2 percent of growth in industrial output and import substitution for 16.5 percent.[27]

Still, the development process between 1962 and 1982 was not completely smooth. The oil shocks in the 1970s created some bumps in the road with which the government had to contend. The government-directed industrialization also created

25. Mason and others, *Economic and Social Modernization of Korea*, pp. 96-97. See also Collins and Park, "External Debt and Macroeconomic Performance in South Korea," pp. 184-185.

26. Kim and Park, *Sources of Economic Growth in Korea*, p. 9.

27. Mason and others, *Economic and Social Modernization of Korea*, pp. 152-153.

TABLE 2. TRANSFORMATION OF THE SOUTH KOREAN ECONOMY, 1954-1982 (As a percentage of gross national product)

	1954	1962	1972	1982
Primary Sector[a]	51.1	45.3	29.2	19.2
Manufacturing	5.3	9.1	20.9	34.2
Social Overhead and Services	43.6	45.6	49.9	46.6
Exports	0.8	2.0	16.4	31.8
Imports	7.2	15.6	23.7	36.5
Domestic Investment	11.9	12.8	21.7	26.2
Domestic Saving	6.6	3.3	15.7	21.5
Foreign Saving	5.3	10.7	5.2	4.8

SOURCE: Congressional Budget Office based on data from Kim Kwang-suk and Park Joon-kyung, *Sources of Economic Growth in Korea: 1963-1982* (Seoul: Korea Development Institute, 1985).

a. Agriculture and natural resources.

problems. In the 1970s, for example, the government decided to create and expand heavy industry. But in doing so, it created shortages in light industries and consumer goods, leading to steep inflation. Those decisions did not prove particularly detrimental, however, as they had in many other developing countries. The strength and diversity of the economy by the 1970s allowed it to weather the government's mistakes and external shocks.

A Modern Economy

South Korea today is by most accounts a modern industrial economy. Under President Park's successors—Chung Doo Hwan, Roh Tae Woo, and Kim Young Sam—South Korea continued along its outward-looking, export-oriented path to industrialization and growth. It suffered a minor setback in the worldwide recession in the early 1980s but quickly reestablished its rapid economic growth. It now is at the top of the World Bank's list of upper-middle-income countries. Table 3 illustrates Korea's emergence as a modern industrial economy, comparing several economic and social indicators with those of Japan in 1993.

ROLE OF FOREIGN ASSISTANCE IN SOUTH KOREA'S DEVELOPMENT

After fighting a war to defend South Korea, the United States had a strong interest in avoiding that country's political or economic collapse and the possibility of a communist revolution in South Korea. Consequently, the United States poured aid into Korea. Indeed, of the eight countries the Congressional Budget Office studied in depth, South Korea was second only to Egypt in the amount of U.S. aid received. That aid included large flows of military and economic support as well as substantial technical assistance (see Figure 2). The form that aid took varied over time: between 1953 and 1970, most U.S. economic assistance was in the form of grants; after 1970, most aid was in the form of concessional loans; by 1975, most U.S. assistance consisted of loans from the Export-Import Bank.

Other donors began giving assistance to South Korea in the 1960s. The World Bank—a major multilateral donor to Korea—first sent aid in 1962. In 1965, Japan began giving money to Korea. Finally, the Asian Development Bank began lending to Korea in 1968. Other donors, including the United Nations and the Federal Republic of Germany, have given smaller amounts of money.[28]

28. Steinberg, *Foreign Aid and the Development of Korea*, pp. 31-33.

TABLE 3. COMPARISON OF VARIOUS ECONOMIC AND SOCIAL INDICATORS FOR SOUTH KOREA AND JAPAN, 1994

Indicator	South Korea	Japan
Real GNP per Capita (Dollars)	10,330	21,130
Manufacturing as a Percentage of GDP	29	27
Agriculture as a Percentage of GDP	7	2
Energy Use per Capita[a]	3,000	3,825
Adult Illiteracy	b	b
Total Fertility Rate (Births per woman)	1.8	1.5
Infant Mortality Rate[c]	12	4
Urban Population as a Percentage of Total Population	80	78

SOURCE: Congressional Budget Office based on data from the World Bank.

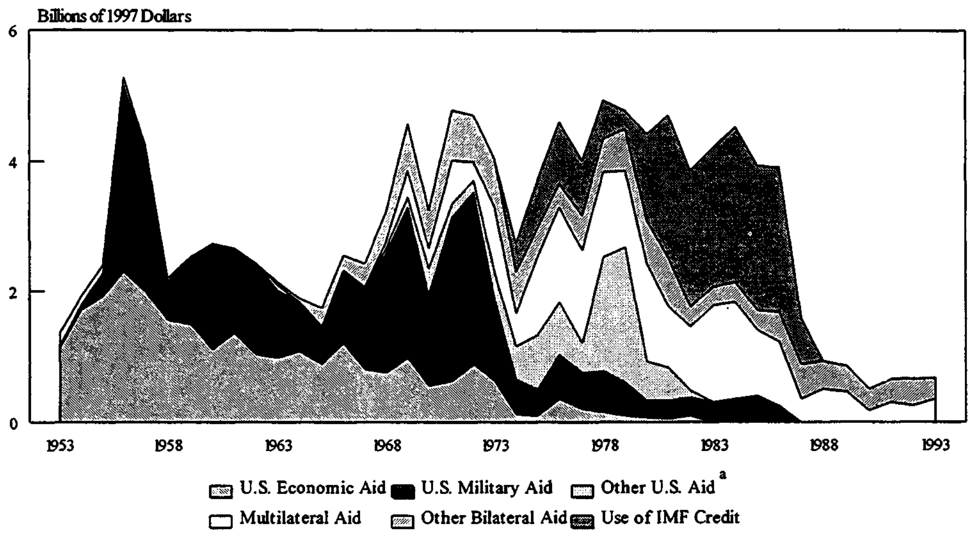
NOTE: GNP = gross national product; GDP = gross domestic product.

a. Kilograms of oil equivalent.

b. The World Bank reports this number as "less than 5 percent."

c. Deaths of infants under 1 year of age per 1,000 live births.

FIGURE 2. FOREIGN ASSISTANCE TO SOUTH KOREA, 1953-1993



SOURCE: Congressional Budget Office based on data from the Agency for International Development, the World Bank, and the Organization for Economic Cooperation and Development.

NOTE: IMF = International Monetary Fund.

a. Mostly loans from the Export-Import Bank.

This discussion of the role of foreign assistance in South Korea's development focuses primarily on U.S. assistance. The United States gave almost as much economic assistance to Korea as all other donors combined. Between 1953 and 1963, when the foundation of Korea's future growth was being laid, the United States provided almost all of that country's foreign assistance.

Health

South Korea has tended to neglect investment in social services, including health care. Both the South Korean government and U.S. aid agencies placed a relatively low priority on investment in health. Between 1954 and 1964, the United States spent about 3 percent of its project assistance on the health sector. Sanitation and water supply projects usually received the highest priorities. Although Korea's government spending on health has been low by Asian standards, private spending on health services between 1960 and 1974 rose from 2.3 percent of private consumption expenditures to 3.6 percent, reflecting in part rising incomes.[29]

Nevertheless, health conditions in Korea have improved considerably since the 1950s. The number of hospitals and clinics nearly doubled between 1955 and 1975. In 1955, there were 6,141 doctors in Korea; that figure rose to 16,800 in 1975. Infant mortality, a commonly used measure of access to health care, declined from 78 per thousand live births in 1955 to 49 in 1973. Finally, the death rate (deaths per thousand people) declined from 14 in 1955 to 9 in 1973. According to a 1981 study, despite those dramatic improvements, relatively low government involvement and spending on health care left rural areas "underserved."[30]

Education

Education played one of the most important roles in Korea's economic growth and development. Despite a strong cultural tradition that favored education, only 13.5 percent of the population was literate in 1945. But the government invested in building schools and compelled six years of primary education. To help Korea meet the demand for classrooms, which far exceeded the available supply, U.S. assistance helped build 23,000 classrooms between 1952 and 1966.[31] The United States spent about 4 percent of its project assistance on education.

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29. Mason and others, *Economic and Social Modernization of Korea,* p. 405.

30. Ibid., p. 407.

31. Krueger and Ruttan, "Assistance to Korea," p. 246.

By the 1970s, the illiteracy rate had declined dramatically. Primary schools were within walking distance for most village children. Middle schools, high schools, and colleges, however, were still located only in urban centers.

Investment in infrastructure and institutions of higher education was generated primarily by the private sector, although the Agency for International Development helped develop the College of Agriculture of Seoul National University. In the 1950s and 1960s, AID sent nearly 3,000 Koreans to the United States for training.

Overall, the role of foreign assistance in promoting educational achievement in Korea does not appear to have been a large one—not because foreign programs were ineffective or badly managed, but because the Korean government and especially Korean society placed considerable emphasis on education. The government invested large sums in schools and infrastructure, but the private sector—business and individual families—did more to support higher education.[32]

Population Growth

The major foreign aid organizations in this sector were the Agency for International Development and the United Nations Fund for Population Activities. Some international nongovernmental organizations, such as Planned Parenthood, were also involved.

During the 1950s, family planning and population programs were a low priority of the Korean government. President Rhee opposed them and, hence, devoted few resources to them. That view changed after President Park assumed power. He instituted a national family planning program. The donors played an important role in planning that program as well as providing funding and technical assistance. The role of foreign organizations and donors in population programs later declined, but they remained as providers of contraceptive supplies and as a source of research and advanced training in family planning and population.

Various indicators revealed a dramatic decline in Korea's population growth rate. Between 1960 and 1975, Korea's total fertility rate dropped from 6 births per woman to under 4. One scholar has described that as "one of the fastest [fertility declines] recorded in any nation in history."[33]

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32. Mason and others, *Economic and Social Modernization of Korea*, pp. 358-359.

33. Robert Repetto quoted in Mason and others, *Economic and Social Modernization of Korea*, p. 381.

It is difficult to say, of course, whether the slowing of Korea's population growth and the steady decline in the fertility rate would have occurred in the absence of President Park's national family planning program or foreign assistance. Some scholars argue that part of the decline in growth and fertility rates might have accompanied Korea's economic and social development regardless of official policy or programs.[34]

Agriculture

Foreign assistance played a substantial role in promoting agriculture in South Korea. Arguably, some of the U.S. foreign aid in the 1950s, notably P.L.480 food assistance grants, enabled the Rhee government to neglect agricultural production because it received a steady, cheap supply of foodstuffs from abroad. Nevertheless, foreign assistance programs played a large and positive role in promoting land reform and development, the use of fertilizer, and agricultural extension and research.

In the early 1960s, U.S. food aid was used to pay Korean laborers to create additional farmland from hillsides and tideland areas; those laborers then assumed ownership of the land. That program attempted to increased the available agricultural land by 15 percent. It was discontinued after 1967 because of questions about its management and cost-effectiveness. Some instances of corruption and mismanagement also occurred. Finally, AID, the Asian Development Bank, the World Bank, and the United Nations supported a massive irrigation effort between the early 1960s and the late 1970s. The results were positive, despite some cost overruns. Irrigated land increased from 662,000 hectares to 1,122,000.[35]

Between 1945 and the mid-1960s, U.S. assistance provided the primary funding for importing agricultural input such as pesticides, fertilizers, and new seed varieties. U.S. loans provided the means to build five fertilizer plants in Korea in the 1960s. When Korea became a net exporter of fertilizer as a result of those plants, the United States terminated its assistance in that area.

Agricultural output grew at an annual rate of 3.2 percent between 1946 and 1973. According to one study, "about 57 percent of total production growth is attributable to the increase of input and the remaining 42 percent to improvement in

34. See Robert Repetto and others, *Economic Development, Population Policy, and Demographic Transition in the Republic of Korea* (Cambridge: Harvard University Press, 1981), pp. 247-250.

35. Krueger and Ruttan, "Assistance to Korea," pp. 239-240.

productivity."[36] However, some problems occurred in the government's distribution of aid-financed fertilizer that caused inefficiencies and black-market activity. U.S. suggestions to privatize and improve distribution had little effect. Reforms in the late 1970s, long after U.S. assistance had ended in that area, solved those problems.[37]

U.S. assistance in the agricultural sector supported agricultural research and extension services. Initially, much of the money AID provided was diverted for other purposes. Agricultural research and extension had acquired a bad name because it had been associated with Japanese colonialism. In 1962, those efforts were reorganized. AID provided political and financial support to a newly created independent agricultural agency attached to the Ministry of Agriculture and Forestry. Its main efforts were devoted to agricultural research and the extension or transfer of technology to farmers. The Korean government was committed to that program, and the service became highly centralized, thus permitting the quick diffusion of new and innovative technology that raised agricultural yields. Yet sometimes the very effectiveness of the organization caused inappropriate technology to be diffused equally well.

Overall, during the 1973-1980 period, after the research and extension service was in place and foreign assistance in that sector was largely phased out, total agricultural output grew 5.4 percent a year. Productivity—output per unit of total input—grew 3.3 percent a year.[38]

Economic Growth

During the 1950s, U.S. economic assistance represented 69 percent of imports and 77 percent of all saving in South Korea. Food aid was particularly important in sustaining the Rhee government. One study estimated that without all that assistance, Korea's living standards would have been 10 percent to 15 percent lower.[39]

Nevertheless, the inward-looking, import-substitution policies of the Rhee government were constricting the economy, regardless of the size of aid flows. U.S. officials fully recognized that fact and tried to persuade the Korean government to

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36. Sung Hwan Ban, Pal Yong Moon, and Dwight H. Perkins, *Rural Development* (Cambridge: Harvard University Press, 1980), pp. 57-60.

37. Krueger and Ruttan, "Assistance to Korea," p. 242.

38. Ibid., pp. 243-244.

39. Mason and others, *Economic and Social Modernization of Korea*, p. 459.

make reforms. Although Rhee made a few concessions along those lines, such as a devaluation of the currency and an attempt at greater fiscal discipline, "the overall strategy of the Rhee government was to maximize the gap between domestic resources and expenditures for foreign aid to fill. Because the United States was politically committed to the maintenance of the South Korean government, U.S. bargaining power was relatively weak."[40]

In fact, Rhee's aid strategy included a measure of deception. For example, the Rhee government counseled its ministries to understate Korea's harvests "to try to maximize the inputs of United States agricultural products under the aid program . . ."[41] He apparently succeeded in that effort. In some years during the 1950s, the United States provided a third or more of the total budget for the government. In 1956, U.S. support for the Korean government's budget reached 58 percent of total expenditures.[42] One study has called that a policy of "coercive deficiency."[43]

Arguably, aid's most significant contribution to Korea's future economic growth was in providing infrastructure investment and technical assistance. U.S. assistance also helped Korea to recover from the war and rebuild as quickly as it did. The large amount of infrastructure construction—power systems, railroads, and port capacity—that the United States financed probably permitted faster economic growth in future years than otherwise would have been possible. In addition, Krueger and Ruttan have argued that "the experience gained in infrastructure construction in the 1950s and 1960s enabled Korea to become a major exporter of construction services to the Middle East in the 1970s and early 1980s."[44]

Many lower-level officials within the Rhee government received training in economics in the United States. They argued for economic reforms in the 1950s but were resisted at the upper echelons of the government. In the 1960s under the reform-minded Park government, however, their skills and expertise were put to good use in designing and implementing the outward-looking, export-oriented economic strategy that launched Korea on the path of rapid economic growth. According to one analyst, "one may sum up the pre-Park era on overall aid effectiveness as one in which foreign assistance was essential to the survival of the state but poorly used and unimaginatively planned and administered. Some

40. Krueger and Ruttan, "Assistance to Korea," p. 234.

41. Cole and Lyman, *Korean Development*, p. 79.

42. Steinberg, *Foreign Aid and the Development of Korea*, p. 23.

43. Mason and others, *Economic and Social Modernization of Korea*, p. 458.

44. Krueger and Ruttan, "Assistance to Korea," p. 235.

preconditions for growth were created: excess industrial capacity, an educated population, and foreign, modern specialized training in skills needed for development. The results, however, did not seem equal to the effort."[45]

In the late 1950s, U.S. officials began to place more emphasis on development. They warned the Rhee government that aid flows would gradually decline and eventually end. That warning, and the realization on the part of many Koreans that the United States actually meant it, stimulated efforts to put Korea's economic house in order. General Park justified his military coup in 1961 in part because the Rhee government had "frittered away" large quantities of foreign assistance.[46] The Park government began to reform economic policies in the early 1960s. Those reforms were crucial factors in Korea's successful development.

According to an AID study, by 1964 that agency was playing an extremely important role in planning, supporting, and sometimes even directing South Korea's export strategy—the key to its industrialization. AID personnel and advisers provided most of the expertise necessary to create the institutions, laws, and procedures to promote South Korean exports. AID personnel staffed the South Korean government entities that were making policy for the export drive, identified and encouraged foreign buyers of Korean exports, provided technical advice on improving Korean export products, funded trips by Korean business representatives to examine methods of promoting exports, and provided technical advice on almost every conceivable aspect of reorienting the South Korean economy toward exports. President Park provided the political will to reform and export, and AID provided the technical expertise for the first few years.[47]

The foreign aid South Korea received in the late 1960s and 1970s was important to its development in other ways. Primarily, that aid increased the pool of available investment capital. The period between 1965 and 1975 illustrates what a developing country can accomplish when it adopts sound economic policies, has favorable background conditions such as a well-educated labor force, and has extra capital provided by international sources and uses it for investment. Foreign transfers declined as a share of total domestic investment over that period, from an average of 75 percent in the 1960-1962 period to 5.1 percent in the 1973-1974 period

45. Steinberg, *Foreign Aid and the Development of Korea*, p. 27.

46. Cole and Lyman, *Korean Development*, p. 78.

47. Agency for International Development, Bureau for Global Programs, Field Support and Research, *USAID and Economic Policy Reform: Origins and Case Studies* (Forthcoming).

(see Table 4). By the 1970s, South Korea was sufficiently creditworthy to borrow the capital it needed on the international market.[48]

Could South Korea have developed just as quickly if it had not received such high levels of foreign assistance in the 1960s and 1970s? Some critics of foreign aid argue that South Korea began to make reforms only after the United States threatened to stop providing aid and that South Korea's growth trajectory soared only after U.S. aid ended. That argument, however, is somewhat misleading. On the one hand, the Rhee government was finally motivated to make some reforms when the United States informed it that aid flows would decline in the future. On the other hand, it is not clear that the Park government, which made the most important reforms, was motivated by the impending end of aid resources. Park wanted to reform the economy to make it grow in order to gain legitimacy for his government. Moreover, he did so with AID's help, particularly in promoting exports. Finally, South Korea continued to receive aid from multilateral institutions, war reparations from Japan, and credits from the Export-Import Bank.

The positive economic policies Korea adopted in the early 1960s and its strong base of human capital probably would have fostered significant economic growth in the succeeding 10 years regardless of the amount of foreign assistance it received. But growth would probably have been slower simply because the investment pool would have been smaller or, if Korea could have obtained the funds from the international capital markets, more government revenues would have been needed for servicing the debt.[49]

Military Assistance

U.S. military assistance to Korea between 1953 and 1960—approximately $8.7 billion in 1997 dollars—aided Korea's development in several different ways. First, U.S. assistance helped build up the strong military establishment that South Korea needed to ensure its defense after the Korean War. By providing support for the defense budget, the United States allowed South Korea to devote resources to other, more productive sectors.

Second, thousands of Korean military officers were trained in the United States. After they left military service, many of them assumed important roles in the civilian government and economy. According to an AID study, much of the early supply of skilled labor in the 1960s and 1970s, such as electricians and mechanics, came from the military.

48. Mason and others, *Economic and Social Modernization of Korea,* p. 459.

49. Ibid., p. 187.

TABLE 4. DOMESTIC AND FOREIGN SAVING IN SOUTH KOREA, 1958-1974
(Saving as a percentage of total investment)

	Total Investment as a Percentage of GNP	Domestic Saving		Foreign Saving[a]	
		Private	Government	Transfers	Borrowing
1958	12.9	62.5	-24.1	69.8	-8.2
1959	10.7	61.5	-25.0	67.0	-3.5
1960	10.9	33.2	-18.7	82.3	-4.0
1961	13.1	42.8	-13.6	69.5	-4.3
1962	13.0	22.1	-10.7	72.9	10.0
1963	18.4	39.0	-1.4	37.8	20.6
1964	14.5	44.8	3.5	43.5	5.1
1965	14.7	38.1	11.5	44.2	-2.0
1966	21.6	41.6	13.0	26.5	12.5
1967	21.9	35.5	18.5	21.7	18.5
1968	26.7	27.5	23.5	14.6	28.5
1969	29.8	38.0	20.8	11.4	25.5
1970	27.2	34.5	25.5	8.0	27.4
1971	25.6	33.3	23.6	7.4	36.6
1972	20.9	53.1	18.6	8.3	18.4
1973	26.2	66.9	17.4	5.9	9.5
1974	31.4	51.7	9.6	4.3	38.9

SOURCE: Congressional Budget Office based on data from the Korean Economic Planning Board.

NOTES: Domestic saving and foreign saving should total 100 percent. However, various statistical discrepancies may put such a total off by a few percent.

GNP = gross national product.

a. Foreign transfers and perhaps a small proportion of foreign borrowing represent foreign aid. Most foreign borrowing is private capital. Negative numbers indicate that loan repayments exceeded additional borrowing.

Indeed, a fair amount of the social mobility in Korean society during the 1960s and 1970s resulted from service in the military.

Third, Korea's development experience was largely a hierarchical and centralized process. The experience gained by many people in the command structure of the Korean military may have contributed to the success of many Korean development projects. Both President Park and President Chung were former army generals who pursued Korea's development from the top down. But no definitive analysis has been written—or perhaps can be written—about that contribution.

INFLUENCE OF GOVERNANCE ON THE PHILIPPINES' DEVELOPMENT

Development in the Philippines has lagged behind that of many other nations of East Asia. The poor development record reflects a climate of economic mismanagement and massive corruption, in addition to the waste of large amounts of foreign aid. The policies of Ferdinand Marcos, who ruled the Philippines from 1966 to 1986, deserve much of the blame for that state of affairs. During his tenure, the Philippines dropped from being one of the most prosperous nations in Asia to being one of the poorest. Although the Philippine economy grew during the Marcos presidency, poverty increased, natural resources were depleted, and foreign debt ballooned. Since Marcos left, the economy has improved, but the Philippines' prospects remain uncertain.

The Structure of Government

The Philippine democracy in the 1950s and 1960s was patterned after that of the United States, with a president, a congress, and an independent judiciary. In reality, the presidency in the Philippines was much stronger than its U.S. counterpart. Philippine politics were dominated by an oligarchy until 1972. A small number of wealthy, landed families controlled the congress and usually rotated the presidency among different regional power centers. As some scholars have observed, "the extended family was a particularly strong source of identification and status in the Philippines, and patron-client relationships linked the population to the oligarchic family in its area or region."[50] Members of that oligarchy, though by no means unanimous in their outlook, set the nation's economic and political policy. Ferdinand Marcos was only the second president since 1946 who was not considered a member

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50. Robert S. Dohner and Ponciano Intal, Jr., "The Marcos Legacy: Economic Policy and Foreign Debt in the Philippines," in Jeffrey D. Sachs and Susan M. Collins, *Developing Country Debt and Economic Performance*, vol. 3, *Country Studies—Indonesia, Korea, Philippines, Turkey* (Chicago: University of Chicago Press, 1989), p. 376.

of that ruling group. And the congress often served as the oligarchy's arena of elite representation and bargaining.

Ferdinand Marcos was elected president in 1966 and, breaking tradition, was reelected in 1969. In 1972, in the wake of domestic disorder, he staged a coup whereby he dissolved the legislature, shut down the media, and arrested hundreds of individuals in the name of restoring domestic political order. He ruled by decree and wrote a new constitution—actions that have been called "constitutional authoritarianism."[51] He ruled until driven from power by a "people's power" revolution in 1986.

Around the time of Marcos's coup, a Muslim-led insurgency broke out in the southern part of the country. The Philippines is overwhelmingly Christian, and the Muslim forces sought greater autonomy. Although that conflict was a seemingly intractable problem that took more than 20 years to end, it was confined and did not impinge much on the normal business of most of the country. Marcos also had to deal with the Marxist-oriented New People's Army in the northern part of the country.

Philippine politics under Marcos's successors—Corazon Aquino and Fidel Ramos—appear to resemble those of the pre-Marcos era. The oligarchy still dominates the political system, and the president is the strongest political force in the country. In addition, Aquino's first few years were characterized by numerous attempted coups and the communist insurgency. Those threats largely receded as her term ended, and she was succeeded by Fidel Ramos, a former army chief of staff and defense minister.

Corruption

A major impediment to development in the Philippines has been widespread government corruption, especially under Marcos. In the 1950s and 1960s, the Filipino political system was used to enrich members of the ruling elite. State-owned enterprises were generally badly run and corrupt, and side-payments and kickbacks to politicians were common. A major reason for running and holding office was to enjoy those "benefits." As one member of the Philippine senate put it: "What are we in power for? We are not hypocrites. Why should we pretend to be saints when

51. Ibid., p. 386.

in reality we are not?"[52] Indeed, access to credit at below-market rates was one of the privileges of government in the Philippines.

Under Marcos, however, the use of the political and economic system to benefit the president and his friends expanded on a massive scale. Robert Dohner and Ponciano Intal have characterized the behavior of that group as "crony capitalism" and attribute to it a major portion of the blame for the Philippines' underdevelopment. Crony capitalism was conducted through various means, such as awarding government contracts to the politically favored, padding expenses, and providing kickbacks. But "the most important aspect was the creation of monopolies, either through direct intervention to control an industry or through granting exemptions or exclusive privileges to favored individuals."[53] For example, in the forestry sector, some of the logging licenses went to government ministers and Marcos's friends. Even when land was allocated to others, Marcos's allies were allowed to log in those areas under the pretext of clearing the forest for settlement projects of the Ministry of Agrarian Reform.[54] According to one study, the cost to the Philippine economy of crony capitalism in the early 1980s represented at least 10 percent of government revenues, not counting all the investment it may have discouraged and capital flight it encouraged.[55]

Moreover, Yoshihara Kunio, in a comparative study of the Philippines and Thailand, has argued that corruption has extended to the Philippine police forces and judiciary. Many police have worked for criminal syndicates. High-ranking police officials receive a modest salary yet live luxuriously. The Philippine police, Yoshihara concluded, are "probably the most corrupt government agency in the Philippines."[56] Some judges were allegedly influenced by money during trials; even before martial law, the rich and powerful in the Philippines could evade punishment for many crimes, including murder.[57]

As martial law corrupted law enforcement and the economy deteriorated, the crime rate exploded. That contributed to the flight of domestic capital from the

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52. Quoted in James K. Boyce, *The Philippines: The Political Economy of Growth and Impoverishment in the Marcos Era* (Honolulu: University of Hawaii Press, 1993), p. 8.

53. Dohner and Intal, "The Marcos Legacy," p. 399.

54. Boyce, *The Philippines: The Political Economy of Growth and Impoverishment*, pp. 233-234.

55. Dohner and Intal, "The Marcos Legacy," pp. 478-479.

56. Yoshihara Kunio, *The Nation and Economic Growth: The Philippines and Thailand* (New York: Oxford University Press, 1994), p. 193.

57. Ibid., p. 194.

Philippines during the 1970s and 1980s. Private property of the poorer classes was often confiscated by wealthy individuals, and the poor could do little about it except join the rebels. Owners of small businesses would lose their businesses to criminals who used fake titles or legal gimmicks to claim property they did not own, and the judges would uphold their tactics.

Absence of Land Reform

Unlike South Korea, the Philippines has not implemented a major land reform program. Reform of land tenureship and ownership patterns, which many scholars say is necessary for improving rural life and alleviating poverty, has been extremely limited. As a remnant of the Spanish colonial era, some small peasant landholders coexist in the Philippines alongside large plantations that produce crops for export. Poverty in rural areas in the Philippines is severe and deepened during the Marcos era.

The powerful land-owning oligarchy, especially the sugar barons, have controlled the congress and resisted any attempt at land reform. In the 1950s, President Magasaysay managed to pass some very weak legislation, which had little substantive impact on ownership patterns. Marcos was frustrated by the congress in some land reform efforts during his elected administrations. Under martial law, he made some reforms that benefited the tenants and owners but bypassed the large pool of landless agricultural workers. Export agriculture has remained largely untouched by land reform efforts. Even President Aquino, a member of the oligarchy and daughter of a sugar plantation owner, declared that she opposed land reform of the sugar plantations because it would not be economically feasible. Erik Thorbecke suggests, however, that this view is mistaken. Production of crops such as sugar are likely to face constant or decreasing returns to scale—that is, as the farming enterprise becomes larger, the costs of production remain constant or increase. Only in processing activities are there increasing returns to scale.[58]

INFLUENCE OF DOMESTIC ECONOMIC POLICIES ON THE PHILIPPINES' DEVELOPMENT

Economic nationalism is a theme that has existed in Philippine politics and economic policymaking. There exists a strong desire to "Filipinize" the country's economy—that is, to reserve land ownership, use of natural resources, and participation in many

58. Erik Thorbecke, "The Political Economy of Development: Indonesia and the Philippines" (Inaugural Frank H. Golay Memorial Lecture, Cornell University, Ithaca, N.Y., November 11, 1994), p. 25.

economic activities for native Filipinos. That sentiment has included discouraging foreign investors and the Philippines' industrious and entrepreneurial Chinese minority throughout the post-World War II period.

Economic and trade policy in the 1950s was dominated by a struggle between the sugar barons and the owners of industry. The sugar barons favored "more liberal trade and exchange rate policies—avoiding overvaluation of the peso and limiting the degree of import protection."[59] Increasingly, however, they were challenged by the inward-looking, import-substituting industrial sector. By the end of the 1950s, that sector had emerged as a more powerful force, advocating and benefiting from protection and overvaluation of the currency.

Four factors seemed to account for the Philippines' economic growth in the 1950s. First and most important was the "accelerated social change in attitudes and values which determined the 'will to economize'—the intensity of economic activity."[60] Perhaps the critical source of that change was the public school system. Based on the U.S. model, it instilled in Filipinos the notion that individual dignity, security, and welfare depended as much on their own abilities as on birth or the vagaries of nature.

Second, the Philippines maintained a consistent economic policy of relying on private initiative and capitalism. Although a few state-run enterprises existed, Filipinos generally believed that growth came from private initiative and that socialism was not a path to the future. That is not to say that the government pursued a completely free-market approach; it used consumer price controls and invested in public enterprises that were not very profitable, but the government—primarily the congress—has been generally conservative in expanding the economic role of the state. The Filipinization of the economy through subsidized credit, domestic protection, and tax exemptions accelerated the growth of Filipino entrepreneurship and contributed to the accumulation of capital.

Third, foreign saving, primarily from the United States, covered the Philippines' current-account deficits and contributed the bulk of net investment in the 1950s. Finally, the government stimulated the domestic market through effective controls on the exchange rate and imports, creating a highly protectionist environment in which young businesses could grow.[61]

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59. Dohner and Intal, "The Marcos Legacy," p. 376.

60. Frank H. Golay, *The Philippines: Public Policy and National Economic Development* (Ithaca, N.Y.: Cornell University Press, 1961), p. 408.

61. Ibid., pp. 411-414.

The Marcos Presidency and Martial Law

Marcos immediately sought to accelerate growth through expansionary fiscal and monetary policies. The government greatly raised capital expenditures, especially on infrastructure—irrigation, roads, schools, and communications—in rural areas. Between 1964 and 1968, government expenditures rose by 43 percent in real terms from 11.5 percent to 14 percent as a percentage of GNP. Domestic credit was relaxed by the central bank; according to one study, credit increased by 40 percent between 1965 and 1967—more than twice the rise of nominal GNP.[62] GNP also grew, but the price of that growth was balance-of-payments and debt-service problems. As a percentage of GNP, external debt grew from 13 percent in the 1965-1968 period to 33 percent in 1970. Marcos himself stated that servicing the Philippines' debt in 1970 would "take over half our export earnings."[63] The International Monetary Fund and other credit institutions persuaded the Philippine government to implement a stabilization program that included cutting government expenditures and devaluing the peso. By the end of 1970, the peso's value had dropped by 43 percent relative to the dollar.

The early 1970s was a period of stabilization. External debt fell as a percentage of GNP, which was growing at a brisk pace (see Table 5). The current account went from deficit to surplus. But real wages declined between 1969 and 1973, despite a rising per capita GNP. The lower wages and the low value of the peso fueled the Philippines' exports, but that did not "translate into improvements in the lot of Filipino masses."[64]

Shortly after declaring martial law in 1972, Marcos sharply expanded the role of government in development. He formed the National Economic and Development Authority (NEDA) to plan it. The state took ownership of the Philippine Airlines, multinational oil companies sold their stakes to the state-owned Philippine National Oil Company, and the military acquired several private steel mills to form the National Steel Corporation.[65] Technocrats armed with economics, business, and engineering degrees increasingly staffed the bureaucracy.

62. Dohner and Intal, "The Marcos Legacy," p. 383.

63. Quoted in Dohner and Intal, "The Marcos Legacy," p. 382.

64. Ibid., pp. 383-384.

65. Bela Balassa, *Economic Policies in the Pacific Area Developing Countries* (New York: New York University Press, 1991), p. 166.

TABLE 5. ECONOMIC INDICATORS FOR THE PHILIPPINES, 1965-1973
(As a percentage of gross national product)

Indicator	1965-1968	1969	1970	1971	1972	1973
Real GNP (Percentage growth)	4.9[a]	5.2	3.9	6.5	5.4	9.3
Budget Surplus	-0.7	-3.5	0.2	-0.5	-2.4	-1.2
External Debt	13	22	33	27	26	22

SOURCE: Congressional Budget Office based on data from Robert S. Dohner and Ponciano Intal, Jr., "The Marcos Legacy: Economic Policy and Foreign Debt in the Philippines," in Jeffrey D. Sachs and Susan M. Collins, *Developing Country Debt and Economic Performance*, vol. 3, *Country Studies—Indonesia, Korea, Philippines, Turkey* (Chicago: University of Chicago Press, 1989), p. 384.

NOTE: GNP = gross national product.

a. Annual average.

Government expenditures rose after martial law was established in 1972 (see Table 6). By increasing the level of foreign borrowing, Marcos dramatically raised public investment. By 1978, it had risen to 7 percent of GNP, or 30 percent of total domestic capital formation.

For a few years Marcos's program seemed to work. GNP per capita grew at a vigorous average annual rate of 3.0 percent between 1973 and 1979. In addition, international prices for many of the Philippines' primary exports, such as copper and wood, rose dramatically. That growth, and massive increases in government spending, enabled the economy to weather the first oil crisis in 1973-1974.

The Philippine export base diversified during the 1970s. In 1970, over 90 percent of exports were primary or slightly processed commodities. By 1979, that proportion had fallen to 50 percent. In their place were labor-intensive, nontraditional manufactured exports. The manufacture of some goods for export contained a large amount of imported materials and thus required substantial foreign exchange to pay for them. But the government managed that debt carefully, and debt service did not increase very much as a percentage of export earnings. As a percentage of GNP, the Philippines' external debt was comparable with Korea's.

The average Filipino, however, did not participate in those economic gains. Real wage rates for agricultural workers declined by 25 percent between 1966 and 1986 (see Table 7). Urban workers, both skilled and unskilled, fared even worse: their real wages declined by 69 percent and 73 percent during the same period. Thus, although the economic pie was growing larger, the distribution of that pie appeared to be shifting against the poorest segments of the population. Between 1971 and 1985, the percentage of the population living in poverty increased dramatically, as shown below:[66]

Year	Percentage of Population in Poverty
1965	41.0
1971	43.8
1975	51.5
1985	58.9

66. Boyce, *The Philippines: The Political Economy of Growth and Impoverishment*, p. 46. Data on poverty should be treated with caution. Researchers have been unable to explain how poverty could increase and wages decline while per capita GNP increased during the 1970s. Moreover, poverty is not a clearly defined concept. In the Philippines, poverty lines have been based on estimates of the income needed to meet nutritional requirements. However, if the income of poor families has been understated over time, it could dramatically affect estimates of poverty trends. Furthermore, defining poverty in that manner gives no indication of how far below the poverty line people are.

TABLE 6. ECONOMIC INDICATORS FOR THE PHILIPPINES, 1973-1979
(As a percentage of gross national product)

Indicator	1973	1974	1975	1976	1977	1978	1979
Real GNP (Percentage growth)	9.3	5.6	5.8	7.4	6.3	5.8	6.9
Government Expenditure	14.3	11.7	16.0	15.2	14.9	14.8	13.7
Budget Surplus	-1.2	0.5	-1.6	-1.8	-1.9	-1.2	-0.2
Investment	21.9	26.7	30.6	31.3	29.0	29.1	31.0
Saving	27.0	25.4	25.3	25.4	25.8	24.4	26.6

SOURCE: Congressional Budget Office based on data from Robert S. Dohner and Ponciano Intal, Jr., "The Marcos Legacy: Economic Policy and Foreign Debt in the Philippines," in Jeffrey D. Sachs and Susan M. Collins, *Developing Country Debt and Economic Performance*, vol. 3, *Country Studies—Indonesia, Korea, Philippines, Turkey* (Chicago: University of Chicago Press, 1989), pp. 389, 391.

NOTE: GNP = gross national product.

TABLE 7. STANDARD-OF-LIVING INDICATORS FOR THE PHILIPPINES, 1962-1986

Indicator	1962	1966	1970	1974	1978	1982	1986
Wage Rate[a]							
Agricultural worker	100	93.6	75.9	54.2	87.6	65.0	70.7
Skilled urban worker	100	89.1	89.5	55.3	54.0	48.8[b]	27.8
Unskilled urban worker	100	96.1	103.3	63.0	57.2	41.1[b]	25.7
Unemployment Rate	21.8[c]	22.0	14.9[d]	10.6	14.7	24.1	22.9
Prices[e]							
Food	20.4	27.6	33.4	74.5	100	162.5	329.1
Nonfood	27.8	29.6	36.1	70.1	100	186.3	387.3

SOURCE: Congressional Budget Office based on data from James K. Boyce, *The Philippines: The Political Economy of Growth and Impoverishment in the Marcos Era* (Honolulu: University of Hawaii Press, 1993).

a. Real daily wage rate index: 1962 = 100.

b. Value shown is for 1983; value for 1982 is not available.

c. Value shown is for 1961; value for 1962 is not available.

d. Value shown is for 1971; value for 1970 is not available.

e. Real food price index: 1978 = 100.

The Economic Crisis of the 1980s

The economic situation in the Philippines deteriorated rapidly after the second oil shock in 1979-1980. Between 1980 and 1986, total GNP declined and per capita GNP fell by an average of 3.3 percent a year. Export earnings also dropped 5 percent a year from 1980 to 1983. The government tried to alleviate those conditions by increasing its expenditures and foreign borrowing. The external debt grew from 52 percent of GNP in 1980 to 93 percent in 1985. But foreign and domestic investors lacked the confidence that the economic problems were short term. Net foreign investment declined to almost nothing, and capital flight may have reached 5 percent of GNP in 1981 and 1982.[67]

In an effort to stem the decline, the government made a severe adjustment. Investment as a share of GNP declined by more than 50 percent between 1980 and 1985 (see Table 8). Government expenditures were cut to control inflation, which exceeded 50 percent in 1984. By the time Marcos left office in 1986, external debt was nearly equal to GNP. Income levels were no higher than they had been in 1974.

Four factors contributed to this state of affairs. First, the high level of public-sector investment did not translate into higher rates of economic growth. Second, the Philippines financed that investment through foreign borrowing. The government continued to borrow, it was unable to raise resources domestically, and export earnings were not growing fast enough to service the debt. The government maintained overvalued exchange rates and protectionist trade policies, which had a particularly negative impact on the agriculture sector, the source of much of the Philippines' foreign exchange. Imports of food products were cheap relative to domestic production, which tended to reduce farmers' income and production. Third, the absence of land reform contributed to the high incidence of poverty in rural areas.

Last and perhaps most important was corruption in the Marcos government. The government borrowed abroad to invest domestically. At every step in that process, there were bribes and kickbacks and other forms of self-aggrandizement by Marcos, his family, and his friends. According to Erik Thorbecke, the very purpose of the borrowing and the investment in many cases was to divert resources in the planning and construction phases.[68] The government was often obligated to pay back the loan even though it generated little return to the country. As one scholar put it, "to a real extent, the Philippines under martial law developed a [self-serving]. . .

67. Dohner and Intal, "The Marcos Legacy," p. 393.

68. Thorbecke, "The Political Economy of Development," p. 29.

TABLE 8. ECONOMIC INDICATORS FOR THE PHILIPPINES, 1980-1988

Indicator	1980	1981	1982	1983	1984	1985	1986	1987	1988
Real GNP (Percentage growth)	5.0	3.4	1.9	1.1	-7.1	-4.1	2.0	5.9	6.7
External Debt (Percentage of GNP)	49.0	n.a.	62.8	72.7	80.6	81.7	92.9	84.1	n.a.
Investment (Percentage of GNP)	30.7	30.7	28.8	27.5	19.2	14.3	13.2	15.4	18.2
Debt Service[a]	20.8	n.a.	38.1	38.2	43.4	36.9	34.0	35.3	n.a.

SOURCE: Congressional Budget Office based on data from Robert S. Dohner and Ponciano Intal, Jr., "The Marcos Legacy: Economic Policy and Foreign Debt in the Philippines," in Jeffrey D. Sachs and Susan M. Collins, *Developing Country Debt and Economic Performance*, vol. 3, *Country Studies—Indonesia, Korea, Philippines, Turkey* (Chicago: University of Chicago Press, 1989): pp. 392, 394.

NOTE: GNP = gross national product; n.a. = not available.

a. Total interest payments plus amortization of total medium- and long-term debt as a percentage of exports of goods and services.

government which over time would sap the energy of the domestic economy and which contributed significantly to the economic crisis of the 1980s."[69]

Economic Policy Under Aquino and Ramos

Economic policy under Corazon Aquino, who assumed the presidency in 1986, did not immediately resolve the Philippines' problems, but it made progress. Economic growth improved in the first few years after the fall of Marcos, largely as a result of a stabilization and adjustment program that the International Monetary Fund had imposed during the last few years of the Marcos government. GNP grew 4 percent a year between 1986 and 1992. Between 1987 and 1992, GNP per capita grew at an average annual rate of 1.9 percent. Some major changes included establishing a neutral export regime, reforming the tax and financial system, and curbing government intervention in the economy. However, not all problems were solved. For example, the depletion of natural resources continued, especially in the watersheds and fisheries, and poverty remained high.

In 1992, Fidel Ramos was elected to the presidency. He intended to carry out a comprehensive economic reform program. Ramos largely succeeded in reducing tariff barriers, privatizing state-owned industries, reducing external debt, cutting government expenditures, increasing private investment in infrastructure, increasing GNP, and reducing the poverty rate.

The Philippines seems on track to greater sustained growth. Many analysts believe that it has broken the cycle from its past. Yet there is some concern that this progress is dependent on Ramos, whose term expires in 1998 and who cannot run for reelection. And "crony capitalism," in the words of AID, "is not yet dead."[70]

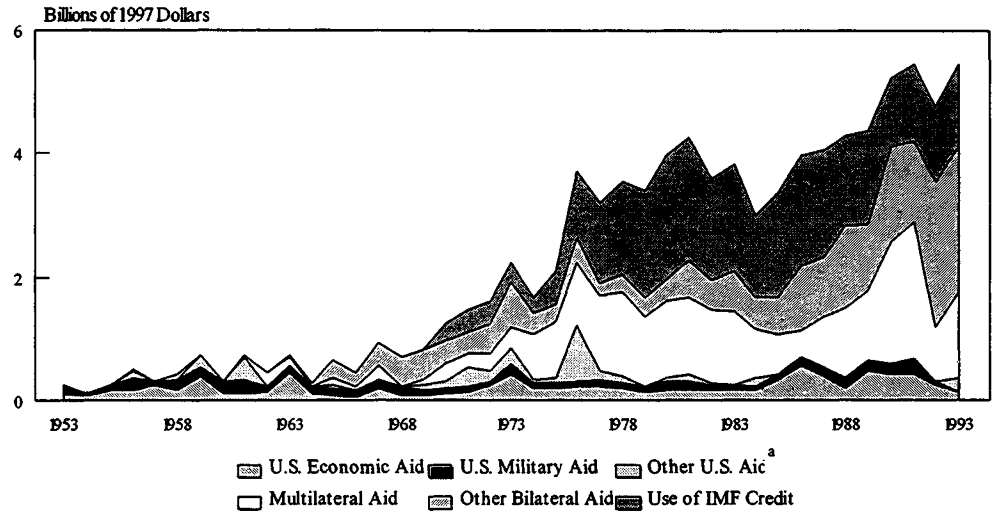
ROLE OF FOREIGN ASSISTANCE IN THE PHILIPPINES' DEVELOPMENT

The Philippines has received foreign assistance from a variety of sources during the past 40 years (see Figure 3). U.S. economic and military assistance accounted for two-thirds of the aid to the Philippines in the 1950s and 1960s. The World Bank

69. Dohner and Intal, "The Marcos Legacy," p. 389.

70. Agency for International Development, *Congressional Presentation: Fiscal Year 1996* (February 24, 1995), p. 332.

FIGURE 3. FOREIGN ASSISTANCE TO THE PHILIPPINES, 1953-1993



SOURCE: Congressional Budget Office based on data from the Agency for International Development, the World Bank, and the Organization for Economic Cooperation and Development..

NOTE: IMF = International Monetary Fund.

a. Mostly loans from the Export-Import Bank.

began lending to the Philippines in 1958 and eventually became a primary provider of foreign assistance to the Marcos government. The Asian Development Bank began lending to the Philippines in 1969. Other countries, particularly Japan, have also given assistance.

U.S. assistance was motivated partly by strategic considerations. The United States did not want to see the Philippines succumb to a communist-backed insurgency. Since a communist government was avoided, U.S. aid in one sense succeeded. But the aid may also have undermined the development goals of U.S. assistance.

Health

The role of foreign aid in the health sector is difficult to evaluate, but health indicators did improve. Between 1961 and 1993, the United States, the World Bank, and the Asian Development Bank allocated about 7 percent of their economic assistance to health. Infant mortality rates fell from 72 deaths per thousand in 1967 to 44 in 1992. The United States appeared to put particular emphasis on reducing infant mortality through various child survival programs.[71] Other measures also indicate improvement. For example, crude death rates—deaths per thousand—have declined, and life expectancy has increased.

Education

The population of the Philippines, like that of South Korea, has been well educated for some time. The literacy rate in 1970 already exceeded 80 percent. In 1992, the rate was 90 percent. Between 1961 and 1993, AID, the World Bank, and the Asian Development Bank allocated about 4 percent of their economic assistance to education. An AID evaluation describes the building of schools as one of its most "consistently successful" programs. Between 1980 and 1991, U.S. money helped build more than 2,300 school buildings—improving the standard of living and educational levels in the communities they serve. A school building is often the most well constructed building in a rural community and serves as protection for an entire town during severe storms, such as typhoons.[72]

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71. Benjamin P. Loevinsohn, *Setting Quantitative Objectives in Health Sector Programs: Lessons Learned from the Philippine Child Survival Program*, CSP Monograph No. 3 (Manila: Department of Health, Republic of the Philippines, 1993).

72. Agency for International Development, "AID Evaluation in Summary, Part 1," in *AID Impact Evaluation: Economic Support Fund Infrastructure Program, 1980 to 1991* (May 1991), p. 1.

Population Growth

In 1967, the Agency for International Development began providing assistance to the Philippines to deal with issues related to population. AID trained and supported personnel who staffed various clinics and other organizations. It also supported various methods of contraception. During the Marcos era, AID's population activities were highly integrated with those of the Philippine government. Those efforts, however, encountered some hostility from the Aquino government. Overall, major donors have not allocated a large percentage of their aid to population issues. Between 1961 and 1993, the United States, the World Bank, and the Asian Development Bank allocated approximately 1 percent of their economic assistance to population programs.

The Philippines has seen a slowing of population growth and a falling fertility rate. The prevalence of various methods of contraception, particularly voluntary sterilization and the pill, have grown substantially—from 15 percent to 36 percent between 1968 and 1988. Problems in those programs have included inadequate training, weak field supervision of programs, and some poorly conceived incentive programs. Although the fertility rate has declined, AID does not claim credit. In an evaluation of its contraceptive program, the agency stated that "fertility has continued to decrease at a rate that cannot be accounted for by the methods in which A.I.D. has made its greatest investment."[73]

Agriculture

Judging the usefulness of the agricultural aid provided by AID, the World Bank, and the Asian Development Bank is also difficult. Those organizations spent over 20 percent of their assistance on agriculture. Sectoral evaluations of efforts by the World Bank and the Asian Development Bank are not available, but a 1987 AID evaluation of its projects reported that its Bicol River Basin Development Program provided substantial benefits to one of the poorest regions of the Philippines. AID spent $29 million on that project—a small fraction of U.S. money spent in the agriculture sector. Household income in the area grew, irrigation increased, and crop yields rose substantially.[74]

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73. Agency for International Development, Center for Development Information and Evaluation, *Evaluation of AID's Family Planning Program in the Philippines*, AID Evaluation Highlights No. 11 (1992), p. 8.

74. Agency for International Development, Asia Near East Bureau, *The Impact of U.S. Development Assistance in Asia and the Near East* (1987), pp. 127-128.

The United States contributed relatively small amounts to agricultural research. But when combined with resources from other donors and the government of the Philippines, that aid yielded some impressive results. Those results included a first-class agricultural university and research efforts that eliminated diseases and increased agricultural yields, particularly for small farmers. The financial return of those efforts, according to AID, far exceeded their costs.

The broader picture, however, appears less positive. Although rice yields and those of agricultural products grown for export have risen since the 1960s, the benefits have accrued largely to the wealthy segments of Philippine society and, during the Marcos years, to Marcos and his allies in particular. Agricultural wage rates declined under Marcos, and the rural poor suffered considerably. In the absence of reform and improvements in many other areas—such as the overall policy environment—most Filipinos who worked in agriculture were not better off.[75]

Economic Growth

Not much is known about the effectiveness of U.S. aid programs to the Philippines during the 1950s and 1960s. U.S. money spent on building infrastructure produced some positive results, but at that time AID did not require systematic evaluations of the impact of its projects. Hence, CBO is unable to determine whether those projects were maintained, for example, or whether they had a negative environmental impact.[76]

Foreign aid provided to the Philippines under Marcos may have actually hurt the country's development by reinforcing his economic mismanagement and corruption. Between 1966 and 1986, the international community gave or lent approximately $33 billion (in 1997 dollars) to the Philippines, most of which was intended to promote economic growth. But per capita GNP averaged only 0.8 percent growth per year during that period. Moreover, poverty increased, and rural and urban wages declined dramatically. The Philippines' external debt as a percentage of GNP grew from 13 percent in the mid-1960s to 93 percent in 1986. And calculations of capital leaving the Philippines between 1962 and 1986 totaled over $19 billion, not including an adjustment for lost interest. Before being driven

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75. Boyce, *The Philippines: The Political Economy of Growth and Impoverishment*, p. 155.

76. Chris Hermann, *U.S. Assistance for Infrastructure Development from 1946 to 1995: Fifty Years of Accomplishment* (Agency for International Development, May 26, 1995), p. 10.

from power, Marcos, his family, and close associates "recycled" a substantial amount of the Philippines' external borrowing by sending or taking it out of the country.[77]

A long-term AID study on the building of infrastructure during the Marcos years reported positive results, especially in rural areas. Although very little information exists about the economic and social impact of infrastructure projects between the early 1960s and 1973, AID asserts that "it is fair to conclude that the construction of roads, bridges, irrigation systems and other small-scale projects helped meet local infrastructure [needs]."[78] During the period of martial law, AID continued to support many infrastructure projects designed to expand development in rural areas. Here, again, it is difficult to evaluate their impact on development. On the one hand, some analysts claim that many of those projects must have provided benefits to the populations and regions that they served, because the amount of resources going into infrastructure development was far greater than in any other sector. On the other hand, the actual record of per capita GNP growth under Marcos is uninspiring. If foreign aid projects were improving the conditions of the poor, the improvement did not show up in aggregate national indicators.

After Marcos was driven from power in 1986, the major foreign aid donors joined together in a cooperative assistance program to the Aquino government—the Multilateral Assistance Initiative (MAI). The MAI was an effort led by the United States to rally the international community to help rebuild the Philippine economy and support democracy. The reform program of Corazon Aquino and Fidel Ramos, Aquino's successor, has received strong support from the MAI donors. The United States, the International Monetary Fund, and the World Bank played critical roles in helping amplify, fine-tune, and promote the reform agenda.

The MAI also funded various regional development activities, placing particular emphasis on building infrastructure. Although determining the precise responsibility of foreign aid is difficult, those efforts helped build an economy that has flourished since the early 1990s. In 1995, Philippine Finance Secretary Roberto de Ocampo credited the MAI with helping bring that about: "A large part of the credit for our dramatic turnaround and persistent push towards a track of high growth can be owed to strong international support—specifically to the Multilateral Assistance Initiative."[79]

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77. Boyce, *The Philippines: The Political Economy of Growth and Impoverishment,* pp. 279, 295, 297. Some estimates put the amount in the billions of dollars.

78. Hermann, *U.S. Assistance for Infrastructure Development from 1946 to 1995*, p. 26.

79. Quoted in Agency for International Development, *The Philippines: Results Review and Resource Request* (March 1996), p. 5.

In comparing the development histories of South Korea and the Philippines, several observations seem particularly important. First, military expenditures did not seem to hinder development. Throughout the past 40 years, South Korea has devoted a greater percentage of its GNP to the military than the Philippines.

Second, the economic policy environment was probably the most important determinant of development. South Korea's inward-looking economic policies in the 1950s hindered its development, whereas the outward-looking policies of succeeding decades spurred economic growth. Marcos pursued economic policies that were similar to Rhee's in Korea during the 1950s, resulting in extremely slow growth, a large external debt, and a fragile, underdeveloped economy.

Third, Korea's moderate levels of corruption under the Park regime did not substantially undermine its growth prospects so long as it maintained an outward-looking, export-oriented economic policy. The high levels of corruption under Marcos, however, played an important role in undermining the Philippines' development, exacerbating the damage done by inward-looking economic policies.

Fourth, foreign aid is less effective when it is given for political as well as developmental reasons. Rhee knew that the United States was committed to supporting him and therefore was unwilling to make reforms. When that commitment seemed to waver in the late 1950s, he began to make some changes. Similarly, in the 1970s and 1980s, Marcos received aid from the United States in part because the United States did not wish to see his government fall to a communist insurrection.

Fifth, foreign bilateral and multilateral assistance appears to have improved education and health regardless of the overall policy environment. Still, the right policy environment is likely to make investments in human capital more effective. With respect to economic growth, the case of Korea suggests that foreign aid can play a modest and positive role in promoting development in a favorable economic environment. The opposite argument is less clear. On the one hand, foreign assistance given to countries with unfavorable economic policies—Rhee's Korea, Marcos's Philippines—may contribute to development, for example, by building necessary infrastructure. On the other hand, to the extent that foreign aid sustained the Marcos government and helped keep it in power longer, foreign aid may have actually harmed the development of the Philippines because of the destructive effect of that government's policies.

These cases also suggest that a strong base of human capital is not enough. Education alone, for example, was insufficient to generate growth in the Philippines.

Both South Korea and the Philippines have had well-educated populations for decades, but Korea's economy has grown at a dramatic rate and the Philippines' has not.

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