



Australian Government

AusAID

Office of Development Effectiveness

Issues Note | February 2009

Lessons from the Asian Financial Crisis

Recent work by World Bank researchers indicates that almost 40 per cent of developing countries are highly exposed to the poverty effects of the Global Economic Crisis (GEC), and a further 56 per cent are moderately exposed.¹ Many of those countries considered highly exposed are major recipients of Australia's aid, including PNG, Indonesia, Philippines, Vietnam, Timor Leste and Laos PDR.²

The current recession is much broader in scale than the Asian Financial Crisis of the late 90s, and as such, pressures will emerge to help a wider range of countries – at the same time as many developed countries are responding to economic downturns in their own economies. In this context, it is imperative to take on board the lessons from the Asian Financial Crisis and ensure that assistance is timely, appropriately designed and effective. This brief attempts to capture the main lessons from the Asian Financial Crisis for Australian aid. In order to do this, first the lessons regarding the impacts of the crisis are examined, second, the response of partner governments and Australia is briefly explored and, emerging from these two sections, are lessons from the crisis response. The brief draws on similar notes prepared by the World Bank and on research papers analysing the response and impacts of the Asian Financial Crisis.

What we learned about the impacts of the Asian Financial Crisis

The Asian Financial Crisis happened suddenly and its impacts were very deep. It also came on top of a severe drought which was impacting on the availability of basic food-stuffs in many of the worst affected countries. The response of partner governments and donors was quick and large scale, and included three substantial IMF programs. In Indonesia, in particular, there was a strong emphasis on bank restructuring and other major reforms to the finance sector. Australia provided substantial technical assistance to help Indonesia on much of this work and on meeting other IMF requirements. Australia also increased the bilateral aid program by 11 per cent to the East Asian region. The Asia Crisis Fund was established – a three year \$24 million program which covered (predominately economic) governance projects.

A report prepared for APEC on the effects of the crisis on children, funded by AusAID, highlighted a number of common elements in the public sector response in Indonesia, the Philippines and Thailand. In all three economies governments put in place or reinforced programs targeting children's nutrition. They also moved to maintain access to primary health services and address the increased cost of pharmaceuticals. Governments tried to maintain school enrolments, using a range of methods including funding allocations, scholarship and community awareness campaigns. Both Indonesia and Thailand placed considerable emphasis on generating short term employment opportunities to maintain family income.

At the time there were projections that the impacts on poverty would be enormous and in Indonesia by some estimates they were, with GDP falling approximately 7 per cent in 1997/98 and some estimates

¹ World Bank (2009): The Global Economic Crisis: Assessing Vulnerability with a Poverty Lens. Policy Note

² To be considered highly vulnerable the researchers considered a projected drop in per capita economic growth and whether 20 per cent of more of households were below the \$1.25 poverty line in 2005.

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showing that poverty doubled³. However, many of the worst predictions did not prove to be accurate, as they did not factor in the effects of the response by partner governments and donors. Nor did they consider the effectiveness of communities' own coping mechanisms. Relevant lessons about the impact of the Asian financial crisis include:

- **Impact was not uniform amongst poor people.** In Indonesia research found sharp but geographically uneven increases in the poverty rate. Proportionate impacts were greatest in better off districts of Indonesia, perhaps reflecting the fact that the crisis began in the banking sector and hit wage earners first. Another study confirmed that the urban poor fared badly. In Thailand, it was the rural poor who suffered disproportionately – in part because of their greater integration with the urban economy (greater numbers of Thai farmers undertake off-farm work in urban areas).⁴ Real wages fell in all of the countries affected by the crisis.
- **Negative economic shocks can be more harmful to girls than boys.** ⁵Although data from the Asian financial crisis are inconclusive, research covering 59 developing countries over the period 1975-2004 concluded that the increase in female infant mortality associated with a one unit fall in GDP was almost five times larger than the increase for males.⁶
- **Some nutritional indicators deteriorated.** In Indonesia, this was found to have occurred for poor adult women. In the Philippines data suggested that adults were changing their diet to shield children.⁷ In Thailand the crisis highlighted a problem with iron deficiency and there was concern about the increased consumption of cheap fillers such as instant noodles.
- **Schooling was prioritised by parents.** For primary school, the level of drop-outs did not increase to the extent that was predicted. However, there was some evidence that school start was delayed in some cases. There was also evidence that secondary schooling attendance dropped, with the transition rate between primary and secondary school decreasing. This data was based on enrolments and it was noted that in Jakarta, school absences increased substantially.
- **Government budgets were under enormous pressure but social spending was mostly protected.** Revenues contracted as the tax base – particularly company profits and imports was eroded. In addition, the price of imported goods, particularly some food and pharmaceuticals increased. This was a particular issue for health as imported pharmaceuticals became more expensive and it threatened to undermine immunization programs, family planning and basic health needs. This happened at a time when more people were accessing government provided services.

Lessons for Governments and Donors

Fortunately, our major Asian aid partners have not been affected as suddenly by the GEC as they were during the Asian financial crisis. This means Governments and donors have some time to prepare their response. Several lessons from the Asian financial crisis appear relevant:

- **Government and partners need real-time information on the impacts of the crisis and the**

³ Ravallion M and Lokshin M (2007): *Lasting Impacts of Indonesia's Financial Crisis*, Development Research Group World Bank

⁴ World Bank (2008): *Lessons from World Bank Research on Financial Crises*, Development Research Group, Policy Research Working Paper 4779, p 10

⁵ World Bank (2009): *The Global Financial Crisis – Assessing Vulnerability of Women and Children*, World Bank Policy Brief

⁶ Baird S, Friedman J, Schady N (2007): *Aggregate Income Shocks and Infant Mortality in the Developing World*, World Bank Policy Research Paper 4346, p.26

⁷ AusAID (1999): *Impact of the Asian Crisis on Children: issues for social safety nets*, Centre for International Economics p. 53

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effectiveness of the response. AusAID support in this regard was highly valued and influential. It varied from initiating price surveys of basic commodities through projects during the 1997 drought to investing in a data clearing house on the crisis – housed at the ADB. In Indonesia, Australia supported a central independent unit to monitor a program of scholarships for up to 4 million primary school children via local post offices. Support was also provided for the establishment of the Social Monitoring and Early Response Unit (SMERU) to provide independent, reliable, real-time monitoring of the impacts of the crisis. An evaluation found that in looking at how social safety nets such as small-scale credit and rice subsidies to the poor worked, its findings had major impacts on policy.

- **Spending on health and education needs to be protected in the face of falling revenue and increased demand.** During the Asian Financial Crisis much of the policy dialogue on this issue was led by the multilateral institutions. Australian support for protecting social expenditures was largely achieved through contributions to IMF packages, financing to complement multilateral loans and through reducing requirements for partner government contributions to projects.
- **Good working relationships with multilaterals allowed Australia to respond quickly and comprehensively.** The World Bank, WFP and UNICEF in particular were vital partners in Australia's response. These institutions are able to draw on consolidated experience implementing social safety net programs, and in some cases were able to scale up and adjust existing programs. In Indonesia, for example, the WFP was providing food for drought relief in rural areas and scaled this up to meet emerging needs in urban areas.
- **Crisis responses can lead to longer term opportunities for reform.** In Indonesia, Australia's assistance to support the implementation of the IMF package evolved in time into an economic governance program. This program has supported ongoing economic reforms in Indonesia.

Specifically on social safety nets, the following lessons are relevant:

- **Be clear on the aim of the crisis response.** There was some confusion about whether the aim was to rescue poor and vulnerable people in an emergency or whether it was to deal with pre-existing and ongoing issues of poverty made worse by the crisis.⁸ This can translate into arguments around program design. For example the kind of program implemented to assist out of work garment workers will differ from what will help people who were already poor and must then deal with an increase in food prices. In addition, confusion around the aim can give rise to concerns about the generation of expectations of ongoing support that are unsustainable from the perspective of the government. This is particularly the case if social protection is funded through loans. Whatever the aim, all partners should be clear on the aim of the intervention and any specific crisis intervention should be consistent with longer term efforts to address poverty and vulnerability.
- **If successful social protection programs already exist, they can be used to respond to crises.** In Indonesia the Government's response to the crisis built on existing social welfare and poverty alleviation measures. Many of the most vulnerable families and villages had already been identified through these programs allowing for quicker mobilisation of additional assistance. Except for unconditional cash transfer programs, the only programs that were shown to work in Indonesia were those that were already working.
- **Social safety nets implemented to respond to a crisis can create a foundation for ongoing social protection measures.** Crises can highlight deficiencies in government's capacity to address the needs of

⁸ AusAID (1999) p.42

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the very poor and vulnerable. *PROGRESA* (now called *Oportunidades*), a much studied and successful conditional cash transfer program in Mexico was established during an economic crisis. In order to address the adverse welfare effects of the recent rise in food prices, the Government of Mexico provided a one-time top up payment through this program.⁹

- **Appropriate targeting involves a number of trade-offs and needs periodic review.** World Bank research suggests that finer targeting is not necessarily consistent with greater impact on poverty.¹⁰ Some of the trade-offs include speed and cost versus accuracy. For example, it can be very costly to identify the extreme poor as they often do not get captured in surveys. With tight clustering around poverty lines and little separating the incomes of people just above and below the poverty line, self-targeting mechanisms can be more efficient and effective than slow-moving targeting based on specific criteria.
- **Simple programs are easier to monitor.** Leakage from emergency programs can be high. In Indonesia the World Bank cancelled its social safety net program because of corruption and a refusal to apply sanctions. Programs with minimal discretion, direct transfers, simple criteria, only minor procurement if any and high levels of transparency are the easiest to monitor for leakage.

Conclusion

The impacts of the Global Economic Crisis are widespread and ongoing, with many of our development partners considered highly exposed. Efforts to support partners to respond to the crisis should acknowledge that many partner governments, particularly in Asia, are better prepared to respond to this crisis than they were the AFC in the late 1990s. In addition, our experience in responding to the Asian Financial Crisis of the 90s can provide relevant lessons for the aid program in 2009.

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⁹ The World Bank (2008): *Lessons from World Bank Research on Financial Crises*, Development Research Group November 2008, p 19.

¹⁰ The World Bank (2008): *Lessons from World Bank Research on Financial Crises*, Development Research Group November 2008, p 19.

