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Country Briefs (E. Stern) - Briefs 01

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COUNTRY BRIEFCHINACOUNTRY PROFILE (1980) /a

Population (million)	977	Exports (GNFS)/GNP (%)	7
Growth rate (%)	1.3	Exports per capita (\$)	18
Labor force gr. rate (%)	2.0	Primary excluding food	5
GNP per capita (US\$)	256 /b	Manufactures	8
Growth rate (3 year average) (%)	7	Net petroleum imports p.c.(\$)	-
Investment/GNP (%)	29	Current account balance/GNP (%)	-0.5
Savings/GNP (%)	28	Debt service/GNP (%)	0
Poverty incidence (%):		Debt service ratio (%)	less than 3
Rural	n.a.	Net transfer/GNP (%)	
Urban	n.a.	Total medium & long term	0
Fertility	2.8	Bank	0
Adult literacy (%)	66	Bank opns. 1978-80 averages:	
Life expectancy (years)	64	Commitments/GNP (%)	0
		Number of projects per year	0
		Debt outstanding and disbursed (\$m)	3,400

/a Because data are more recent and because of differences in concepts and definitions, the country data are not directly comparable with those shown in Table 1.

/b for 1979.

Source: Country Data

Development Record

1. China has an extremely varied climate and terrain, huge energy resources, a vast, largely self-sufficient and diversified production base, and a highly literate, disciplined population. Over the past three decades, development efforts have been aimed at two main objectives: elimination of the worst aspects of poverty; and industrialization, with an emphasis on heavy industry. Chinese development strategy has been constrained by an extreme shortage of cultivable land and a high degree of international isolation.

2. Efforts directed at alleviating poverty began with an initial phase of redistribution, followed by agricultural development programs and widespread provision of social services, based mainly on local resources and initiative. Despite slow growth of agricultural production in relation to population, the results have been very impressive. At the same time, rapid industrialization of the economy resulted from a massive infusion of centrally mobilized capital, with little concern for cost-effectiveness, and using technology largely dating from Soviet designs of the 1950s. Growth of per capita GNP was well above the average for low-income countries (2.7% per year in 1957-59; per capita GDP of \$256 in 1979). However, consumption has grown significantly slower than income, owing to an unusually high savings rate (over 40% in 1957-79). Nonetheless, China's most remarkable achievement has been to make low-income groups far better off in terms of basic needs than their counterparts in most other poor countries. Over the past decade, the country has also been phenomenally successful in reducing its population growth.



3. After the Cultural Revolution (1966-1976), the new leadership initiated a set of reforms, aimed at providing lower-level units with more freedom of decision-making, stronger incentives and better signals. Although these reforms are well focused on basic weaknesses of China's socialist economic system and have improved cost consciousness of enterprises and communes and the range and quality of consumer goods and services, they represent comparatively minor changes in a system that remains highly regulated and very inefficient.

4. The new leadership also gave increased living standards higher priority as a development objective. It took steps to raise the share of consumption in aggregate demand and the share of consumer goods in aggregate production. It planned to reduce the share of investment in budget expenditures, and to spend more on housing, education, health, agriculture and light industry. Urban wages and agricultural procurement prices were raised substantially. Agricultural production, light industrial output, and real consumption per capita rose sharply from 1978 to 1980.

5. The new policies were less successful in other respects. The Government seriously miscalculated their effects on the budget and on the balance between aggregate demand and supply, partly because it failed to achieve the planned reductions in investment. There were large unplanned budget deficits in 1979 and 1980, coupled with strong inflationary pressure that was only partly suppressed by the price control system.

6. This led in early 1981 to a switch in emphasis from medium-term adjustment to sharp, short-term stabilization. Price controls were stiffened; some re-centralization of economic decision-making was introduced; and capital construction expenditures were to be slashed by 40% from 1980 to 1981, resulting in the abandonment of a large number of major projects, including those financed from foreign sources. However, efforts are being made to continue investment programs in priority sectors, easing critical constraints on further expansion of domestic production, most notably energy.

#### Key Economic Issues

7. The Government's drive to improve living standards will in the coming decade be subject to a tight set of interlocking constraints: agricultural land, domestic energy production, trained manpower, and foreign exchange and financial resources for new investments. In certain respects, however, prospects are more promising: population growth is slow; better planning and system reform could substantially increase efficiency; and access to foreign markets, technology and capital is much improved.

8. In agriculture, further output growth is limited by land scarcity and by the fact that the easier advances in intensive cultivation have already been made. The foodgrain balance will thus remain precarious. Even relatively modest output growth (2.3% per year for foodgrains, 3% for total agricultural output) will depend on vigorous and skilful implementation of policies of agricultural research, greater specialization of output mix in line with local comparative advantage, improved management of water and other resources, training of labor, and tightening of linkages for production teams between production and income. As in the past, however, rapid growth of industrial output of commune and brigade enterprises is likely to boost rural income growth.



9. The outlook for domestic energy production has recently deteriorated, with oil output peaking in 1979 (106 million tons) and likely to fall to about 90 million tons in 1985. With only modest growth rates projected for total primary energy production (2% per year) and electricity generation (4.3% per year) in 1980-85, prospects for economic growth depend critically on reducing energy use per unit of industrial output. The bulk of the large potential for energy saving is in heavy industry, which accounts for about 60% of commercial energy use. To accomplish this will require thorough advance planning by major subsectors, reform of energy allocation procedures, and changes in energy prices.

10. The performance of the industrial sector -- in economizing on energy, materials and capital, in earning foreign exchange, and in technological innovation -- will largely determine the extent to which the main constraints on economic growth can be eased. Expansion of manufactured exports must have high priority, based on the abundance of skilled low-wage labor and the enormous potential for economies of scale. But such rapid export growth is contingent on updating of industrial technology, improvements in the design of both consumer and capital goods, stronger incentives for innovation and economic efficiency, and various institutional changes enabling Chinese manufacturers to compete in world markets. Serious shortages of skilled and managerial manpower, due to the upheaval of ten years of Cultural Revolution, plague the industrial sector (and other sectors of the economy) and will take years to remedy.

11. The need for imports will be great -- imports of oil for fuel and raw materials, food to increase consumption, and capital goods to contribute to modernization. Faced with these needs, the Government must decide how much to borrow. In the longer term, two key determinants of the optimal level of China's foreign borrowing, namely the rate of growth of manufactured exports and the efficiency with which capital is used, are both dependent on reform of the economic system and improvement of economic management. But in the present situation of adjustment, borrowing decisions in a country that has large unused lines of foreign credit and small debt service commitments should also take account of the social and political utility of additional present consumption, benefits from fuller use of installed capacity, and the dampening effects of increased imports on domestic inflation.

#### Government Objectives

12. The virtual absence of medium-term planning since 1958 has aggravated the inefficiencies of the Chinese economic system. Apart from political interference, longer term planning efforts have been impaired by technical weaknesses in annual planning and project appraisal, a poor data base, and an unsatisfactory balance of responsibilities between central and local government.

13. The Sixth Five-Year Plan, due last year, will not be formulated until the end of 1981, at the earliest. The present substantial cuts in investment are not being made in the context of an overall medium-term investment program; therefore, their costs in terms of future capacity constraints on production growth in particular sectors could be very great. But with the current emphasis on short-term stabilization, little consideration seems to be given to alternative longer-term strategies.



14. In the absence of a long-term, economy-wide plan and, indeed, an adequate technical planning capacity, the Government has so far only indicated broad sectoral and sub-sectoral development priorities -- to be addressed within the constraints of its curtailed investment program: energy production and conservation; light industry; agriculture, with emphasis on new land development, irrigation, research and training; education, particularly higher and technical education; and transport, especially port development.

#### Bank Response and Dialogue

15. The formulation of a detailed, longer-term strategy of Bank assistance to China hinges on the elaboration of China's Five-Year Plan. It is also constrained by the Government's recent shift in emphasis from medium-term adjustment toward short-term stabilization of the economy.

16. The relationship between China and the Bank developed rapidly after the change of representation of China in the Bank, in May 1980. A first operational mission in July 1980 agreed with the Government on two parallel lines of action: (i) preparation of a major introductory economic report on the country's past development performance, economic system and future prospects, which -- together with the Sixth Five-Year Plan -- would serve as a foundation for formulating a program of cooperation in the first half of 1981; and (ii) work on an initial operations program of six projects (university education, irrigation, ports development, railways, hydro-power and thermal power) so that lending could commence soon.

17. A large economic mission spent over two months in China in late 1980; its report, including six sector studies, will be reviewed with the Government in May and sent to the Executive Directors soon thereafter. A number of project missions have worked with various sector ministries on the initial operations program. But the program has been affected by the recent drastic cut in the Government's investment program. The size of the most advanced operation, the University Development Project, has been reduced substantially. In its revised form, the loan is still to be approved by the Board in late FY81 or early FY82. The agriculture and ports projects are proceeding on schedule; the two power projects will probably proceed at a later time; and the railways project has been dropped.

18. China's low income per capita makes it eligible for large amounts of IDA lending. But the country's relatively small external debt and the alternative projections of the economic mission for the balance of payments and debt service capacity also indicate that China is creditworthy for substantial amounts of IBRD lending in the coming years. The Government's present policies of economic retrenchment have led to an increased reluctance to borrow large amounts on conventional (and IBRD) terms; the strong request for a 50/50 IDA/IBRD blend for its borrowing from the Bank Group during IDA VI and IDA VII (the Bank has agreed to a blend of \$400 million IDA and \$400 million or more IBRD for the remainder of IDA VI); the anticipation of a slower build-up of Bank operations to lower borrowing levels than indicated last July; and the request for smaller individual project and loan size in the early years (probably in the range of \$80-100 million per loan rather than \$170-200 million as assumed earlier). In the immediate future,



the Bank cannot expect to persuade the Government to request larger amounts of IBRD lending, thus hardening the IDA/IBRD blend. Rather, the Bank will initially have to develop a broad dialogue with the Government on how the country can best make use of available external resources to achieve its objectives of modernization and adjustment of the economy.

19. The findings of the economic mission indicate that the Bank should pursue the following basic objectives in its economic and lending work. The Bank should assist the Government in its efforts to (i) improve sector planning and investment criteria, and managerial and financial performance of institutions, in the course of the reform of the economic system; (ii) achieve better utilization of existing productive capacity and human resources, and quick production increases, required for the adjustment of the economy; (iii) remove critical constraints to longer term development, e.g. in energy, agriculture, education and transportation; and (iv) obtain an appropriate level of external concessionary funds, both from the Bank's own resources and from other sources, e.g. through cofinancing.

20. These objectives have not yet been translated into a detailed work program for the next years. After review of the economic report with the Government, the Bank plans in May to reach agreement with the Chinese authorities on the subsectors and types of lending which should receive initial priority in the Bank's work and on a program of economic and sector work for the coming year which would lead to the development of a pipeline of lending operations.

21. The tight set of interlocking constraints on development that China faces in the 1980s and the priorities set by the Government for its investment program indicate that the Bank's technical and financial assistance will focus on energy, industry, agriculture, education and transportation. In energy, the Government has expressed interest in involving the Bank in enhanced oil recovery in existing fields and on-shore petroleum exploration and development, coal mining, and power generation. In the industrial sector, the Bank might assist in energy conservation, training, selective large enterprise rehabilitation, and financial intermediation to support a large number of small investments. In agriculture, the Bank could support irrigation, cash-crop development, training and research, and credit. In the field of education, the Government has expressed interest in continued Bank involvement in university development, and in its assistance in developing vocational and technical training, adult education, and the training of teachers. Finally, in transport, the Bank expects to continue its financing of port improvement programs, and might assist in developing highways and railways.

22. Due to the absence of a systematic, longer-term planning framework in most of these sectors, work on projects will, in many cases, have to be preceded by careful sectoral and inter-sectoral studies. The Bank is therefore planning an extensive program of economic and sector work for the coming years.



COUNTRY BRIEF

INDONESIA

COUNTRY PROFILE (1980) /a

Population (million)	147.4	Exports (GNFS)/GNP (%)	35.6
Growth rate (%)	2.3	Exports per capita (\$)	152.8
Labor force gr. rate (%)	3.2	Primary excluding food	127.0
		Manufactures	7.4
GNP per capita (US\$)	405	Net petroleum exports p.c. (\$)	85.6
Growth rate (3 year average)(%)	3.5	Current account balance/GNP (%)	+5.6
Investment/GDP (%)	22.9	Debt service/GNP (%)	2.8
Savings/GDP (%)	28.2	Debt service ratio (%)	7.9
Poverty incidence (%):		Net transfer/GNP (%)	
Rural	51	Total medium & long-term	1.7
Urban	28	Bank	0.5
Fertility	4.9/b	Bank Opns. 1978-80 averages:	
Adult literacy (%)	62/c	Commitments/GNP (%)	1.35
		Number of projects per year	10.3
		Debt outstanding and disbursed (\$m)	13,272.5 /d

/a Because data are more recent and, because of some differences in concepts and definitions, the country data are not directly comparable with those shown in Table 1.

/b 1979.

/c 1978.

/d Medium and long-term, exclude private, non-guaranteed, 1979.

Source: Country Data

Development Record and Issues

1. Indonesia has a population of over 145 million people and a land area of about two million sq km. It has a very significant resource base in energy, including oil, natural gas, timber, coal and hydro-power, and a significant range of minerals and agricultural export crops. The oil price windfall (net export earnings of the oil sector were equivalent to about \$70 per capita in 1980) has transformed the country's external resource position, with large current account surpluses foreseen for the medium term, and has greatly improved the Government's budgetary revenues. However, the population remains extremely poor, with about half the population living below the poverty line, the majority in rural Java.

2. The present military regime came to power in 1966 during a highly turbulent period. Since then the country has been fairly stable, though discontent surfaced at least twice in the 1970s and briefly in 1980. The main focus has been the distribution of the oil wealth and the role of



ethnic Chinese in the economy. The running of the economy has been dominated by the de facto alliance between the military and a group of largely American trained technocrats. Forceful action was taken in the second half of the 1960s to liberalize the economy - this helped bring about rapid growth during the period of rehabilitation. However, during the 1970s the general trend of the Government has been toward greater intervention in the economy, both through expansion of public sector activity and through regulation of the private sector. Since about 1973/74 the large infusion of foreign exchange due to oil has been a key factor in sustaining growth rates of over 7% p.a. All sectors participated to some extent in the rapid growth, but at the beginning of the 1980s the manufacturing sector only accounts for 9% of GDP.

3. Although the agricultural sector has grown at a very creditable rate of about 3.5% p.a., non-rice food crops have suffered relative neglect and imports of wheat, sugar and soya have been rising fast. The Government policies helped bring about an excellent rice crop in 1980, but Indonesia remains the largest purchaser in the international rice market. The pattern of growth associated with the reliance on oil production also appears to have led to growing income disparities, at least between urban and rural areas. On the basis of household expenditure surveys, the 1979 Basic Economic Report concluded that the incomes of the poor are rising, but many observers continue to question whether the poorest 20-30%, including the landless, have in fact benefited. Social indicators, in particular relating to health and living conditions, have remained very poor by international standards.

4. The oil surplus has provided Indonesia with an unusual opportunity: the major question is whether the Government can make use of the resource windfall both to put the non-oil economy on a viable long-run growth path and to effectively reduce the incidence of poverty. To achieve this a number of issues will have to be tackled. First, rapid industrialization on a more labor-intensive export-oriented path will be necessary. This will require reform of the trade regime in order to create a more appropriate pattern of incentives for investment, effective deregulation of the economy, and adequate supplies of credit to the private sector. Second, in order to maintain food security and raise rural incomes, sustained agricultural growth will be required, both through continued infrastructural investment and an improved environment for farmers. Third, human resources development will require greater emphasis, both to directly improve the basic needs of the poor and to provide adequate supplies of skilled manpower to the economy. Fourth, the groundwork for long-run domestic resource mobilization will have to be laid, through an improved tax effort and the development of private financial intermediation. Fifth, the resources deriving from oil will have to be utilized in a manner that does not fuel domestic inflation and jeopardize the international competitiveness of the non-oil economy.

#### Government Plans

5. In the preparation of the Third Development Plan (1979/80 to 1983/84) the Government has placed much greater emphasis on equity; this is



reflected in increased allocations to the social sectors and in preferential treatment for economically weak indigenous entrepreneurs. A number of new programs have been developed in family planning, health and education infrastructure and other rural public works. Despite considerable success there is a continued need to develop innovative methods of delivery of basic social services to the population. So far the Government has appeared to be cautious in its attitude to policy reform, particularly in view of the forthcoming presidential elections in 1982. However, partly as a consequence of growing political pressure, there is an increasing awareness of the need to make use of the opportunity and to develop policy alternatives for the 1980s. There has already been some progress in the review of the trade policy environment and it is planned to form policy review committees for a number of key economic issues. There has also been some progress in the review and overhaul of the cumbersome administrative framework, notably in the area of project implementation procedures.

#### Bank Response and Dialogue

6. The Bank had provided 48 IDA credits totalling \$932 million and 53 Bank loans totalling \$3,147 million by January 31, 1981. Given Indonesia's institutional weakness it was decided, when operations were initiated in the country in 1968, to station a resident mission there to assist in project identification and preparation as well as in policy formulation. This mission has now grown to about 18 professional staff and the country dialogue on policy programs is largely managed from our Jakarta office. The Government has generally been receptive to the Bank's views of project-related issues. For example, there has been a productive interchange in the power, highways, agriculture, urban and population sectors. Indonesia's family planning program, which has been actively assisted by the Bank, has been particularly successful in encouraging the use of contraception and reducing fertility on Java and Bali. There has been increasing emphasis on institutional development in both project and sector work. This has an important influence, particularly in the power and family planning sectors, tree crops and in agricultural research and extension. Latterly, we have been trying to bring about a more productive dialogue on broader policy issues - for example, the Bank is concerned with the need to liberalize the trade regime, reduce the level of regulation and give greater support to the private sector, and also to address the broader issues of public administration. Because of the political constraints in which our government counterparts operate, it is difficult to judge progress in this area. However, initial indications are that we are receiving a positive response to our efforts to articulate policy alternatives. A noteworthy recent development is a request from the Government that the Bank identify key issues for the development of policy to tackle the country's central economic problems.

7. Although the oil surplus has reduced the need for external assistance on resource transfer grounds, Indonesia has an even more urgent need for the technology and technical and policy advice embodied in these transfers, if it is to effectively tackle its development problems. In view of this, our ability to justify the maintenance of a substantial lending program will depend on the government's continued receptivity to our advice



and ultimately its ability to implement the needed institutional and policy changes. This directly influences the Bank's assistance strategy: in the future it will concentrate on lending that is directly supportive of institutional development and policy improvements. This will involve a continued shift toward sector lending, and an emphasis on areas where the needed technical assistance policy advice is difficult to mobilize from private sources. This will be supported by a more highly focussed economic work to ensure that the analysis is directly relevant to the development of policy alternatives. The new Bank strategy is exemplified by the industrial sector: a thorough economic study of this sector is now forming the basis of detailed policy discussions with the Government. Future lending for industry will be related to execution of the reforms needed to encourage the development of efficient labor-intensive industrialization. There has already been good progress in the dialogue over the trade regime, but the discussions on deregulation and financial issues are likely to be much more difficult and future performance will be monitored closely. This model for the Bank's relationship with the Government will be applied in the future to the energy, education and financial sectors, each of which is now programmed for sector studies. In terms of other sectors, agriculture and rural development will continue to be of major importance; while the social sectors will receive increasing emphasis, power and transport will be of declining significance. Given the resource position of Indonesia at this time, there is not a case for concessional lending; IDA lending was discontinued in 1980, in spite of the fact that Indonesia's per capita income remains well below the IDA cut-off of \$625.

8. As a consequence of the rapid expansion of the total public investment program, project implementation performance has suffered in recent years. The rate of disbursement (annual disbursements as a percentage of the year's starting undisbursed balance) declined from 19% in FY78 to 14% in FY79 and FY80. However, following several Bank missions, a number of measures have been taken to improve implementation. These include joint implementation reviews and streamlined budgetary and financial procedures. This has already been reflected in both higher rates of expenditure from the domestic development budget and higher Bank disbursements. The disbursement rate is now expected to reach at least 16% in FY81.



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COUNTRY BRIEFKOREACOUNTRY PROFILE (1980)/a

Population (million)	38.2	Exports (GNFS)/GNP (%)	35.7
Growth rate (%)	1.5	Exports per capita (\$)	553.6
Labor force gr. rate (%)	1.7	Primary excluding food	11.2
GNP per capita (US\$)	1,549	Manufactures	311.6
Growth rate (3 year average) (%)	-1.3	Net petroleum imports p.c. (\$)	64.0
Investment/GDP (%)	30.2	Current account balance/GNP (%)	-9.5
Savings/GDP (%)	22.1	Debt service/GNP (%)	4.6
Poverty incidence (%):		Debt service ratio (%)	14.3/b
Rural	11.0	Net transfer/GNP (%)	
Urban	18.0	Total medium & long term	4.9/b
Fertility	2.8	Bank	0.7/b
Adult literacy (%)	93	Bank opns. 1978-80 averages:	
		Commitments/GNP (%)	0.9
		Number of projects per year	6.3
		Debt outstanding and disbursed (\$m)	15,068/c

/a Because data are more recent and because of differences in concepts and definitions, the country data are not directly comparable with those shown in Table 1.

/b 1979

/c MLT, 1979.

Source: Country Data.

Development Record and Issues

1. Korea's accession to the ranks of the so-called New Industrialized Countries owes little to its endowment of natural resources. Land availability, even on a gross basis, is very low, and then only a fifth of the land is cultivated. Still the country is almost self-sufficient in rice and barley, its staple foods, although it imports substantial quantities of wheat, animal feeds and beef. A low-grade anthracite coal is the only mineral produced. Korea's main resource is its human capital. Its population of 38 million (growing at 1.5% per annum) is unusually well-educated, disciplined and industrious.

2. During 1962-78 Korea achieved an average growth rate of about 9% p.a., while maintaining an income distribution that compares favorably with most developing countries. Korea's outstanding performance during this



period is attributable to the interaction of several factors whose relative importance cannot be easily gauged. Political stability, strong leadership and a firm commitment to development have provided the prerequisites for economic advance. For various historical and cultural reasons the society of post-war Korea was more homogeneous and less structured than in most other parts of Asia. There are no strong regional or religious differences, no deeply entrenched class or caste structure. Consequently, the pursuit of economic opportunity was less inhibited by tradition and class, and the mobility and adaptability of labor was relatively unrestricted by social limitations. The high quality of the labor force has already been mentioned. Large inflows of foreign grants and loans have also played an important role, particularly in the early stages of the industrialization process. Finally, and perhaps most importantly, there was an early recognition of the potential contribution of trade in manufactured goods in compensating for Korea's paucity of natural resources, leading to the adoption of a development strategy concentrating on the expansion of manufactured exports. The success was phenomenal, with exports increasing to an average annual rate of over 25% during 1962-78, and current account deficits declining from about 7% of GNP in the late 60s to virtual balance in 1976/77, before increasing again to 7% in 1979 and over 9% in 1980.

3. The resource transfer arising out of the 1973-74 oil shock and the inflationary surge that followed in its wake, caused much concern and briefly threatened to slow down the economy, but the tremendous growth momentum of the economy carried it rapidly through this period. However, in a burst of what can in hindsight be characterized as overconfidence, there was a large further spurt in investment, the labor market tightened considerably, wages shot up in nominal but also in real terms, and the economy became overheated. In 1979, the Government started to take measures to cool off the economy, but these coincided with a cyclical downturn. Thus the jump in oil prices which raised the import bill for petroleum from \$3.4 billion in 1979 to \$6.0 billion in 1980 came at a singularly inopportune moment. In addition, the political unrest which followed the assassination of President Park shook the confidence of local investors and foreign buyers alike. Only by July 1980 had the military regained a firm grip on the situation. Following General Chun's accession to the Presidency, the Government developed a series of new measures designed to reverse the deepening recession.

4. At that point, apart from the fact that the country was facing the worst harvest in 50 years, four major problems were evident: (a) the heavy machinery and automobile industries, each of which had been expanded very rapidly in the preceding five years, were in severe difficulties because of a shortage of demand, domestic as well as foreign; (b) inflation was accelerating; (c) the industrial sector, badly squeezed by declining sales and profits, was being brought under yet more pressure by the anti-inflationary tight credit policy; and (e) exports remained somewhat sluggish. While the new Government tackled these problems head-on (major industries were merged, credit policies eased, devaluation of the Won accelerated), the impact of



these measures as well as other policies adopted at various times during 1980 did not prevent the economy from registering its worst performance since post-Korean war days, with GNP declining by almost 6%, inflation continuing at about 40% p.a., and the balance of payments deficit on current account rising to a record \$5.5 billion, almost \$1.4 billion higher than the level of 1979.

#### Government Objectives

5. The Government has outlined its proposals in the Economic Management Plan for 1981. It lists four objectives: stimulation of the economy, a strengthening of the balance of payments, control of inflation, and restructuring of major heavy industries. Looking further ahead, Korea remains committed to a strategy emphasizing skill- and technology-intensive industries rather than those areas of light manufacturing rendered less competitive by rising wages. To cope with rising energy costs, the Government has embarked on an ambitious program of conservation and hopes to reduce dependence on oil which currently provides more than two thirds of total primary energy. Much importance is being given to the restructuring of energy prices. In the financial sector a move away from the system of directed credit is underway. Banks will be allowed greater freedom in making investment decisions and in fixing interest rates. Private foreign direct investment as well as an inflow of foreign capital into commercial banks and capital markets is being encouraged. There are plans for raising agricultural productivity through investment in machinery and infrastructure. In addition, the subsidy for fertilizers, which has involved the country in substantial expenditures, will be progressively lowered through the adjustment of fertilizer prices.

#### Bank Response and Dialogue

6. There has been close cooperation between the Bank and the Korean Government for many years. The economic dialogue has been carried on through our normal economic and sector work as well as through periodic meetings of the Consultative Group for Korea under Bank chairmanship. The Koreans have relied on the Bank for advice during critical periods, and the recent recession, coupled with the Bank's positive response to the Government's request to consider structural adjustment lending (SAL), has intensified the dialogue. By and large, there is broad agreement on the long-term strategy and major current policies although differences in emphasis remain which will be the subject of continuing discussion, particularly during the processing of the proposed SAL operations.

7. Given the country's stage of development and proven administrative capacity, the focus of Bank attention in its lending to Korea is moving progressively away from the details of project preparation and implementation and more towards issues of policy and institutions. In line with this approach special attention is being given to assisting the Government to address some of the medium-term issues mentioned above. A series of structural adjustment loans is planned through which we expect to reach



agreement on policies and actions in support of structural improvements in industry and energy. The first of these loans, now in preparation, is expected to focus on restructuring of heavy industry, energy pricing, and resource mobilization. Financial issues are being addressed through our lending for the major development finance institutions. In line with the growing maturity of these institutions, we adopted a sectoral approach for the first time in loans approved last December.

8. The Government's strategy of emphasizing skill-intensive industries gives rise to concomitant requirements of technological and manpower development. The Bank a year ago made its first sector loan for education in Korea. Given Korea's dependence on oil imports, another feature of Bank lending is support for the electric power company's shift away from oil-fired power generation. Preliminary discussions are also under way which may lead to a project for strengthening of institutions responsible for energy policy and programs, particularly in the petroleum field (and possibly also in energy conservation). Sectors such as agriculture and transportation, where we have been heavily involved in the past, are planned to receive relatively less emphasis in future lending, but still to command a significant share of total operations. In the urban sector, a first loan for low-income housing has recently been negotiated, a water supply project for secondary cities is in preparation, an urban transport project has been identified, and preparation is under way for a regional project designed to support an integrated approach to the development of several of the principal secondary cities and their surrounding areas.

9. Korea's performance in project implementation generally has been very good. Recently, however, progress on a number of projects has slowed on account of inadequate counterpart contributions from the Government's budget. The problem has arisen primarily because of the very tight fiscal policy being followed by the Government in a period of high inflation; it is under active review with the Government.



COUNTRY BRIEF

MALAYSIA

COUNTRY PROFILE (1980)/a

Population (million)	13.6	Exports (GNFS)/GNP (%)	56.4
Growth rate (%)	2.7	Exports per capita (\$)	808.9
Labor force gr. rate (%)	3.5	Primary excluding food	442.6
GNP per capita (US\$)	1,651	Manufacturers	197.1
Growth rate (3 year average) (%)	4.9	Net petroleum exports p.c. (\$)	98.6
Investment/GDP (%)	27.2	Current account balance/GNP (%)	6.2/e
Savings/GDP (%)	30.7	Debt service/GNP (%)	3.4/e
Poverty incidence (%):		Debt service ratio (%)	4.5/e
Rural	46/b	Net transfer/GNP (%)	
Urban	16/b	Total medium & long term	1.6/e
Fertility	4.1/c	Bank	0.1/e
Adult literacy (%)	55/d	Bank opns. 1978-80 averages:	
		Commitments/GNP (%)	1.4
		Number of projects per year	3.3
		Debt outstanding and disbursed (\$m)	3,384/f

/a Because data are more recent and because of differences in concepts and definitions, the country data are not directly comparable with those shown in Table 1.

/b 1978

/c 1975

/d 1970

/e 1979

/f MLT, 1979.

Source: Country Data.

Development Record and Issues

1. Malaysia's relatively high per capita income of \$1,651 in 1980 is based to a significant extent on the exploitation of its abundant natural resources. It is the world's largest exporter of natural rubber, palm oil, pepper and tin; a considerable exporter of tropical hardwoods; and has recently become a net exporter of petroleum. About 90% of the country's staple food, rice, is grown domestically. The country has rapidly developed an industrial base, following first an import substitution strategy and later adding manufactured goods exports. Traditionally, macro-economic policies have been cautious and conservative; the level of domestic resource mobilization is high, inflation has averaged around 5% in the last few years and the currency has gradually appreciated. Since 1970 GDP has grown by 7.9% p.a. For the last five years, the economy has experienced trade surpluses and secured a large reserve build-up, currently equal to five



months of imports. The country's credit rating is high and the external debt service ratio a low 4% of exports.

2. The country is ethnically diverse with some 13.6 million people, of whom slightly less than half are Malay, a third Chinese and the remainder Indians and indigenous tribes. It is a constitutional democracy and possesses an enviable record for political stability under the guiding hand of a multiracial coalition. Communal antagonisms are, nonetheless, often sharp. Also, Malaysia is a country characterized by a very high degree of income inequality and, relative to its resources, it has a high incidence of absolute poverty. This poverty is largely concentrated among farmers, the majority of whom are Malay. The dominant political theme of the last decade has been government sponsorship of the relatively disadvantaged Malay majority through policies designed to incorporate them into the mainstream of modern economic activity.

#### Government Objectives

3. Since 1970 successive governments have adopted poverty alleviation as a major strategic objective which, given the strong association of poverty with race, underpins a second objective, noted above, of incorporating Malays into the modern economy. The Government is highly committed to achieving these ends and indeed substantial progress has been made on both fronts. The incidence of absolute poverty (according to government estimates), for instance, declined from 49% in 1970 to 37% in 1978.

4. There is nevertheless ample justification for continuing action by the Government to reduce poverty. While the bulk of rural poverty alleviation will continue to be borne by the transfer of people out of agriculture into employment in the manufacturing and tertiary sectors, the condition of many who remain will be precarious. The Government estimates, for instance, that even assuming high overall growth and rapid labor absorption there will be over three million absolutely poor people in 1990. Moreover, as more becomes known about the poor, the problems of addressing their condition become less rather than more tractable. Fundamental constraints include the size of existing land holdings, uncertainty about the availability to poor households of additional productive land, diminishing prospects for extensive productivity increases through adoption of new technologies, a weak institutional organization to address poverty problems, and a host of group-specific social and cultural factors which restrain improvements in conditions of life.

5. Of key importance in the next few years will be the Government's ability, through its own direct economic interventions as well as through its capacity to create a favorable private investment climate, to maintain the momentum of GDP growth. Much of the recent success in poverty alleviation policies has stemmed from the high-growth manufacturing and service sectors generating income and employment opportunities and absorbing migrants from the rural areas. The Government is currently reviewing its manufacturing sector incentives policies to ensure an appropriate framework for continued expansion.



Bank Response and Dialogue

6. The overriding objective of the Bank's assistance to Malaysia is to strengthen the Government's policies and programs for poverty alleviation. A three-pronged approach is being followed to achieve this objective. First is provision of support for national policy reforms. The Bank's role in this area is to analyze existing policies and propose reforms that allow more effective use of land resources and the introduction of fiscal measures that directly supplement the incomes of the poor and improve their access to basic services. This is being accomplished through our economic and sector work, and also through studies financed under our projects. Second is the concentration of Bank project assistance on direct poverty alleviation. This is a continuation of the initiative begun in the 1970s, but with a greater emphasis on integrated development projects that take into account the multiple income sources of poverty households as well as their basic needs. Third is the provision of selective support to industry and infrastructure, based inter alia on a recent sector report on manufacturing.

7. About 60% of the proposed lending of \$1,080 million for FY82-86 focuses on direct poverty alleviation programs in rural areas. An important element in our operational work is to find mechanisms to enlarge land holdings by addressing the complex socio-economic issues of emigration and land abandonment, land titling and consolidation. In their design the projects will focus on the multiple needs of poverty households. The balance of the Bank's lending program of supporting industrial sector and expanding social services should also have a direct or indirect bearing on generating incomes for or raising the productivity of the poorer segments of the population.

8. Despite a strong overall economic performance and a well structured civil service, Malaysia exhibits some basic deficiencies in the preparation and timely implementation of projects, especially those with an antipoverty bias. This is so because, first, such projects are complex and multisectoral in focus, requiring the participation and coordination of a host of agencies of varying experience and maturity. Second, the preoccupation of development administration in Malaysia has, in the past, largely been with the traditional sectors and it is therefore not well prepared to cope with all the new demands of the poverty alleviation programs. In the 1970s the burgeoning demands of a rapidly expanding economy and the dimensions of Malaysia's antipoverty program have further strained the country's administrative capacity. Critical shortages of skilled manpower and experienced managers have surfaced in most agencies/departments; these are being exacerbated by the Government's hiring Malays in preference to available skilled Chinese. The Bank's ongoing projects have sizeable components of technical assistance which aim at strengthening the Government's project planning and implementation capacity and improving inter-agency coordination. Our forthcoming lending program places an even greater emphasis on institutional reform and provides assistance in overcoming shortages of skilled and technical manpower.



COUNTRY BRIEFPHILIPPINESCOUNTRY PROFILE (1980)/a

Population (million)	47.9	Exports (GNFS)/GNP (%)	21.0
Growth rate (%)	2.6	Exports per capita (\$)	129
Labor force gr. rate (%)	3.7	Primary excluding food	31
GNP per capita (US\$)	740	Manufacturers	40
Growth rate (3 year average) (%)	2.8	Net petroleum imports p.c. (\$)	48
Investment/GDP (%)	29.0	Current account balance/GNP (%)	-6.1
Savings/GDP (%)	23.5	Debt service/GNP (%)	3.8
Poverty incidence (%):		Debt service ratio (%)	16.5
Rural	42	Net transfer/GNP (%)	
Urban	35	Total medium & long term	3.5
Fertility	5.0	Bank	0.5
Adult literacy (%)	87	Bank opns. 1978-80 averages:	
		Commitments/GNP (%)	1.1
		Number of projects per year	8
		Debt outstanding and disbursed (\$m)	7,252/b

/a Because data are more recent and because of differences in concepts and definitions, the country data are not directly comparable with those shown in Table 1.

/b Medium and long term, 1979.

Source: Country Data.

Development Record and Issues

1. The Philippines is reasonably well endowed with mineral (especially copper), energy resources (particularly hydro and geothermal, and some small oil fields), and a climate which permits a year-round growing season. The country's highly literate and English-speaking population constitutes an important additional resource. These advantages, combined with good economic management by highly competent technocrats in the cabinet, allowed many impressive gains to be made during the 1970s. The trend growth rate of GNP was above 6% during the decade, public investment rose from 2% to 5.5% of GNP, the ratio of total fixed investment to GNP rose from 16% to 25%, and exports of nontraditional manufacturers grew rapidly in response to Government promotion efforts. Agriculture performed particularly well, and national foodgrain deficits were eliminated as a



result of the spread of high-yielding rice varieties and irrigation, more favorable price policies, and improvements in supporting services.

2. Still one's summary assessment of the Philippines' economic performance in the 1970s depends heavily on one's choice of comparator. Viewed in relation to the Philippines of the 1960s, or in relation to oil-importing developing countries generally, the accomplishments have been substantial. When viewed in relation to the magnitude of the country's development potentials, progress appears less satisfactory. Among the difficult problems which face the Philippines today, four should be noted.

3. First, the benefits of growth have been unevenly distributed. Historically, there has been a highly unequal distribution of rural land which has been exacerbated by rapid population growth (presently 2.6% per annum). The skewed distribution of rural wealth and incomes has been paralleled by a concentration of capital and incomes in the modern industrial sector. The Government has increasingly focussed on income distribution and poverty in its plans and programs, through land reform, industrial policy reforms that should encourage labor-intensive manufacturing and the spread of industry outside the Manila area, and through increased provision of basic infrastructure and services in the rural areas. Despite these efforts, an estimated 40-45% of the population still lives in absolute poverty, with the poverty incidence reaching 60-70% in the least developed regions. For the future it will be essential to further reduce population growth, accelerate the rate of employment generation and increase the productivity of small farmers on nonirrigated land.

4. Second, past development has taken place in an autocratic political environment, and the increasingly sophisticated technocratic structure does not appear to be supported by a strong political base. The "New Society" program initiated by President Marcos in the 1970s was intended to bring greater economic equality by stripping away the political and economic power of the old oligarchy, but many now believe that the old oligarchy has only been replaced by a new one. Opponents of the current regime have voiced their resentment over the lack of civil liberties, increasing corruption, continuing ineffectiveness of the bureaucracy, and abuses of power by the military. Traditional political activity has been suppressed since 1972 under martial law (now abolished) and by the self-imposed exile of major opposition leaders. Although the president is setting the stage for a gradual transition to more democratic rule, considerable uncertainty remains with respect to the Philippines' political future.

5. Third, the balance of payments constraint has become increasingly severe in recent years. The current account deficit has risen from below \$1 billion in the mid-1970s to \$2.1 billion in 1980 (6.1% of GNP). The primary cause has been the country's heavy dependence on imported oil. More than 80% of the economy's energy is supplied by imported oil (80 million barrels annually) and the increase in oil prices between 1978 and 1980 added almost \$1.5 billion to the import bill. Another important



factor has been the high import-dependence of the capital-intensive pattern of industrial development. A major structural adjustment effort will be needed if the government is to hold the balance of payments deficit within reasonable bounds. The government has recently taken major initiatives in industrial and trade policy and in energy conservation to address these problems. The target for the current account deficit is to reduce it gradually to below 4% of GNP by 1985 through aggressive export expansion and domestic energy development.

6. Given the recent and anticipated current account deficits the Philippines external capital requirements have risen to \$2.0-2.5 billion annually and will rise to \$2.5-3.0 billion annually over the next three years. Foreign aid (ODA) has increased dramatically over the 1970s to a level of about \$1 billion in 1980, and can be expected to increase moderately in coming years. The Bank Group has accounted for about half of ODA commitments in recent years and plans to continue to provide a similar share during 1981-85. (The other major donors are the Asian Development Bank, Japan and the U.S.) The Philippines has had an IMF program of some type every year since 1970 and is the largest developing country recipient of IMF assistance. Currently it is drawing SDR 410 million (\$530 million) over calendar years 1980-81 under a standby program. More than half of the Philippines external capital requirements have come and will continue to come from private sources. The Philippines has traditionally enjoyed good access to private capital markets and, assuming continued good financial management, should be able to obtain its external financing requirements. The debt service ratio has remained below 20% and, even with the heavy borrowing in recent years should not rise significantly above 20% during the 1980s.

7. Fourth, the rapid expansion in public investment over the past decade has led to strains in public administration. About three years ago the Bank and other external donors began noticing a widespread increase in project implementation problems and a general slowdown in disbursements. These problems seem to reflect increasing domestic resource constraints in an inflationary environment, inadequate links between medium-term plans and annual budgets, an over-centralization of government decision-making, a conflict between the goals of budgetary control and flexibility in the implementation of programs, and an increasing shortage of able staff within the civil service directly related to low government salaries. The government has taken steps to address some of these problems but others inherent in the government structure will necessarily take longer to resolve.

#### Government Objectives

8. The Philippines development objectives are set out in the Five-Year Development Plan for 1978-82. The principal goals are to provide for the basic needs of the population; to generate sufficient productive employment opportunities for the labor force, and to reduce economic disparities. We consider the Plan's objectives and strategy to be broadly appropriate and



its quantitative targets generally reasonable. While the Plan's overall growth target has to be scaled down in the face of world recession and balance of payments difficulties, the government is nevertheless making progress in pursuit of these objectives.

Bank Response and Dialogue

9. The dialogue between the government and the Bank is an excellent one. In recent years we have undertaken major studies of the industrial and financial sectors which have directly influenced the industrial policy reforms supported by the first structural adjustment loan and the financial reforms to be supported by our financial sector loan. A major study of poverty was carried out over the past two years with the collaboration of the government and was discussed at the Consultative Group Meeting in January 1981. A comprehensive study of the Philippine energy resources, policies and prospects was recently completed and will be discussed with the Government at the end of April. In an effort to find solutions to increasing implementation problems a joint project implementation review was held in Manila in May 1980 and another such comprehensive review is scheduled for later this year.

10. Through FY80 the Bank group had lent a total of \$2.5 billion to the Philippines, and during the current fiscal year a further \$475 million will be added to that total. The proposed FY82-86 lending program includes 42 operations for a total of \$3.7 billion. Over the past decade about one-third of our lending has been for agriculture and one-third for infrastructure (transport and power). In the future agriculture will remain the largest sector in terms of number of operations but its share of lending will decrease as larger capital-intensive irrigation projects are replaced by projects focussed on small-scale, nonirrigated farming, agro-forestry and low-income fishermen. Similarly the share of transportation will decline with a shift from trunk road construction to less costly rural roads and maintenance. The allocation to industry will increase reflecting the capital role of this sector in resolving the balance of payments and employment problems of the 1980s and our progress in reaching agreement on needed policy reforms.



COUNTRY BRIEFTHAILANDCOUNTRY PROFILE (1980) /a

Population (million)	46.5	Exports (GNFS)/GNP (%)	18.9
Growth rate (%)	2.1	Exports per capita (\$)	138.8
Labor force gr. rate (%)	2.7	Primary excluding food	38.3
		Manufactures	44.1
GNP per capita (US\$)	724	Net petroleum imports p.c. (\$)	63.0
Growth rate (3 year average)(%)	4.3	Current account balance/GNP (%)	-7.3 /c
Investment/GDP (%)	28.3	Debt service/GNP (%)	3.4 /c
Savings/GDP (%)	21.3	Debt service ratio (%)	13.9 /c
Poverty incidence (%):		Net transfer/GNP (%)	
Rural	34/b	Total medium & long-term	3.4 /c
Urban	15/b	Bank	0.3 /c
Fertility	4.5/b	Bank Opns. 1978-80 averages:	
Adult literacy (%)	84/b	Commitments/GNP (%)	1.2 /d
		Number of projects per year	8
		Debt outstanding and disbursed (\$m)	3,945 /e

/a Because data are more recent and, because of some differences in concepts and definitions, the country data are not directly comparable with those shown in Table 1.

/b 1978.

/c 1979.

/d 1977-78 average.

/e Medium and long-term, 1979.

Source: Country Data

Development Record and Issues

1. Thailand is a well endowed country. Substantial agricultural land reserves, vigorous entrepreneurship and an efficiently functioning labor market have contributed to a commendable growth record, with real GDP quadrupling and GDP per capita doubling during the last two decades. In this period poverty has been substantially reduced, life expectancy has increased from 51 to 61 years, and primary education has reached essentially the entire population.

2. The 1960s and 1970s saw a large expansion of agriculture into previously unutilized lands and forest areas. As a result agriculture played a major role in the growth of production and exports, with agricultural exports accounting for 60% of the total in 1979. In addition to the



traditional crops, rice and rubber, new crops such as cassava and sugarcane have produced significant export surpluses. However, as the population continues to grow, new land is becoming more scarce and Thailand is faced with the task of intensifying production on existing holdings, which has not occurred to a significant extent in the past.

3. The responsive labor force and a dynamic private sector are striking features of the Thai economy. Low-cost, reasonably well-educated labor gives Thailand a comparative advantage over many of its neighbors. This factor together with a substantial domestic market has induced many foreign investors to locate there, notwithstanding the country's uneasy relations with its neighbors.

4. Recent major finds in natural gas and lignite offer good opportunities for reducing Thailand's dependence on imported energy in the 1980s. About 40% of total foreign exchange earnings was used to pay for oil imports in 1980. With the development of indigenous resources, a fundamental shift in the energy supply mix will take place in the electricity sector, reducing the total petroleum import requirement by about 20% within five years. Thailand has also recently discovered oil shale deposits and intensive exploration for oil is going on. While mineral exploration has led to the discovery of deposits of potash, tin and soda ash, it is not expected that their exploitation will make major net contributions to the balance of payments in the 1980s.

5. Although Thailand's growth performance has been impressive over the past two decades, the country has not escaped the tensions associated with the transition from a traditional, subsistence oriented economy to a modern, market oriented economy. Average per capita income was only about \$750 in 1980, one third of the population lives below the poverty level, and differences in income and welfare levels between rural and urban areas and between different regions of the country are acute. The Northeast, with 35% of the country's population, is the poorest region, having an average per capita income that is only 40% of the national average and 15% of the average per capita income in Bangkok. While innovative efforts have been made to check the rapid growth in population, that growth is still estimated at 2%. During the period 1981-85 the labor force will continue to grow at a rate of well over 3% per annum, and given dwindling land resources and probably lower overall growth, it will be difficult to absorb the labor productively.

6. The ability of the Thai Government to deal effectively with these emerging social and economic problems is hampered by political and institutional weaknesses. Frequent changes in the coalitions between army officers and political parties which have governed Thailand since 1932 have led to discontinuity of policies and programs, and an unwillingness to take tough or unpopular decisions such as appropriate public sector service pricing, increased taxes, appropriate energy prices, and appropriate changes for the import tariff regime. Most of the pricing issues relate to the amount of subsidies for the urban population of Bangkok, which has an inordinate amount of political power. Changes in political leadership have also tended to



reinforce the resistance of a large, entrenched and highly centralized bureaucracy to much needed administrative reforms. On March 11, 1981, there was another cabinet change, followed by an unsuccessful military coup.

7. Inadequate domestic policies and a deteriorating external environment have since 1975 led to large financial imbalances, the current account deficit was 7% of GDP in 1980 and the fiscal deficit about 4%. Inflation in 1980 was running at 20%.

#### Government Objectives

8. Recently, the Government and the public have become better aware that the structural problems of poverty and inequality will have to be addressed, and that at the same time financial balances will have to be restored. The previous Government took significant steps to improve the situation and the present Government is committed to continue along the lines set by the previous one. As far as the medium term is concerned, this is being done in the context of the preparation of a new Five-Year Plan, the outline of which was completed in January 1980. Its main objectives and policies are to: reduce absolute poverty and accelerate rural development; maintain economic and financial stability through appropriate fiscal, monetary, pricing and foreign trade policy measures; restructure the production process in agriculture and industry; adjust the social structure by enhancing the income earning potential of the poor and improved access to public services; and reform the public administration system at the national and local levels through decentralization and the introduction of better planning processes. This strategy is consistent with the Bank's assessment of Thailand's development problems and needs and has been developed in close cooperation with the Bank.

#### Bank Response and Dialogue

9. Over the last several years the Bank has studied the Thai economy and its public administration very intensively. This work is highly regarded in Thailand, both at the political and at the technical level, and Bank reports are thoroughly analyzed and studied. The economic and sector work having the greatest impact on policies over the past three years include: the Basic Economic Report in 1978 and associated working papers, studies in poverty alleviation, agricultural and industrial strategy, institutional reforms, urban development and energy, and the last Country Economic Memorandum dated December 23, 1980.

10. At the same time that our strategy dialogue intensified, Bank lending to Thailand also increased rapidly and in 1980 was about the sixth largest of current Bank borrowers. Our lending strategy in the last CPP (1978) supported a reordering of priorities towards programs and projects to reduce income disparities both among regions and between urban and rural areas. A major objective of our economic and sector work is to assist the



Government both in analyzing in detail the location and causes of rural poverty and in developing appropriate agricultural policies and programs especially for rainfed agriculture. More emphasis is also being placed on rainfed agricultural projects, on projects to reduce disparities in access to economic and social infrastructure and on provincial development projects which will directly address the problems of those areas of the country that have been behind in the growth process. Recently an active energy lending program has been added. Increasingly we are attempting to link our project lending to policy reforms (i.e., removal of subsidies to state enterprises, higher utility tariffs, land reform, better distribution of services to rural areas and improved performance of implementing agencies). Now that the vehicle of SAL-lending has become available we intend to address even wider policy objectives such as a strengthening of planning and budgetary processes, improved resource mobilization and introduction of greater production and export incentives. Policy statements by the Thai governments in the past two years have reflected a better understanding of the consequences of failing to tackle these issues and a growing willingness to work with the Bank and the IMF in implementing a program of economic, fiscal and institutional changes. On this basis, the IMF expects to conclude a major standby operation soon.

11. Project implementation is generally proceeding satisfactorily. While in the past, the Thai government has experienced some difficulty in adhering to timetables for the implementation of agreed sectoral policy measures, the situation has been improving in this regard. With public sector performance becoming a more important factor in attaining Thailand's development objectives, institutional deficiencies are, however, likely to become critical constraints on the ability of the Thai government to continue its favorable development record.

12. In summary, Thailand can be classified as well above average in terms of its commitment to development objectives and policies which the Bank supports. However, the benefit of all the policies and programs now being initiated will take time to be felt. In the meantime disparities are growing, and a difficult period appears to lie ahead, in which the country will need broad support from the Bank.



COUNTRY BRIEFVIET NAMCOUNTRY PROFILE (1980) /a

Population (million)	54.4	Exports (GNFS)/GNP (%)	5
Growth rate (%)	2.9	Exports per capita (\$)	5
Labor force gr. rate (%)	3.0	Current account balance/GNP (%)	-6
		Bank Opns. 1978-80 averages:	One IDA cre-
GNP per capita (US\$)	180		dit in 1978
Growth rate (3 year average)(%)	Negative		for \$60 mil-
Investment/GDP (%)	18		lion.
Savings/GDP (%)	7		

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/a Because data are more recent and, because of some differences in concepts and definitions, the country data are not directly comparable with those shown in Table 1.

Source: Country Data

Development Record and Issues

1. With roughly 55 million people, Viet Nam has the fourth largest population in East Asia. Viet Nam's natural assets include potential arable land of 9-10 million ha of which only about 5.6 million ha is presently cultivated, some minerals, a long coast line, timber and a literate and well-organized population. Together these assets give Viet Nam considerable potential for development.
2. Thirty years of almost continuous warfare has left Viet Nam with immense and diverse problems. The destruction of infrastructure was extensive in the north, while in the south the abandonment of land and the rapid rise in the population of the larger cities have created problems of low productivity and unemployment. These problems have been compounded in the last three years by severe natural calamities - floods, typhoons and drought. Food rationing is universal and although rations today are smaller than at anytime during the war, no widespread starvation has been reported.
3. Industrial development has been hampered by the critical shortage of foreign exchange for the purchase of raw materials and spare parts. Deterioration of plant over the last five years could lead to the permanent loss of capacity.



4. Efforts to extend full socialization to the south, conflicts with China, lack of job opportunities and universal rationing of nearly all basic commodities and a falling per capita income (\$180 in 1980) has led to a major exodus of skilled manpower. Priority given to defense expenditures following the "China lesson" in 1979 and Viet Nam's move into Kampuchea in late 1978 has further exacerbated Viet Nam's development problems.
5. Limited access to capital on concessional terms and heavy commercial borrowing in the immediate post-war period have led to a heavy debt burden which Viet Nam may well have difficulty in servicing.
6. Despite these difficulties, Viet Nam has made a major effort to reconstruct the country and rebuild the economy on socialist principles. However, due to the acute shortage of machinery and spare parts, progress has been slow and has involved the mobilization of large labor work forces for project construction.

#### Bank Activities

7. An economic mission visited Viet Nam in 1977, a year after reunification, and the first IDA credit of \$60 million for the Dau Tieng irrigation project was approved in August 1978. The project is about two years behind schedule. About \$30 million of the credit has been disbursed. Projects to help rehabilitate industry in the south, to rehabilitate and develop the province of Nghe Tinh and the coal mines in Quang Ninh both in the north had been largely appraised by mid-1979.
8. In November 1979, the President informed the Executive Directors that the situation in Viet Nam was such that there was no reasonable assurance that the objectives of development projects financed by IDA could be achieved. Since then all Bank activities in Viet Nam other than the supervision of the Dau Tieng project have been in abeyance. In light of the recent IMF action (see below), the Bank may soon need to reassess its position.

#### IMF

9. In November 1980, the IMF sent a mission to Viet Nam to assess a request from the Government for support. It concluded that the Government had introduced a program of fundamental economic reforms which warranted IMF support. A credit tranche and standby totalling \$80 million was approved by the Fund Board on January 7, 1981 on a no objection basis with some members expressing concern about the possible diversion of resources to non-economic activities.



COUNTRY BRIEFS

LAOS

1. Laos, with a per capita income of \$90, is one of the poorest nations in the world. Most of the country's 3.2 million people live in absolute poverty. Malnutrition is widespread, infant mortality high, the country's sparse population is overwhelmingly rural and illiterate, and the small dispersed markets preclude economies of scale in production. Costs of imports are high in Laos, being a landlocked country, and the few exports are less competitive. While large forestry, mineral, and hydropower resources have been identified, the economics of their exploitation have not been established.

2. Laos has been severely affected by the war in Indochina over the past 30 years. The country is now for the first time embarking on a long-term economic development program. Its main thrust is to transform and develop agriculture and forestry, aiming particularly at self-sufficiency in food production. Because of the unimpressive performance of the economy, the Government initiated sweeping changes in late 1979, involving greater scope for the private sector and aiming at the rationalization of the price structure, the generation of increased domestic financial resources, and the expansion of production and exports. These reforms are progressing well.

3. IDA has a modest lending program in Laos. Between FY78 and FY80 three IDA credits, totalling US\$ 32 million were approved for agricultural rehabilitation. The future lending program, which is proposed to total US\$140 million for FY81-85, will continue to support projects for agricultural development including forestry, expansion of hydro-electric power generation for export to Thailand, and the re-construction of Route 13, the main north-south road.

KAMPUCHEA

Kampuchea became a member of the World Bank and IDA in July 1970, but has not yet borrowed from the World Bank Group. In 1970 the Bank sent an economic mission which concluded that because of the security problems facing the country there were no prospects for lending until the situation stabilized. The country has been in continuous upheaval since then. Neither of the two governments presently claiming to represent Kampuchea have approached the Bank or the Fund for any assistance. In the case of an application, lending would have to be considered in accordance with the considerations set forth in the OMS 1.27 dealing with de facto government.



PAPUA NEW GUINEA

1. PNG has been independent for six years, but is still heavily dependent on the outside world for manpower and budgetary support. Expatriates make up 7% of the public service, mainly at the higher technical levels, and an annual grant from Australia provides a declining, but still substantial, proportion of public revenue, presently about one-third of the total, or about 9% of GNP. The economy is dominated by a slow-growing agricultural sector and an enclave copper mine, with a second large gold and copper mine under way. Because of its relatively small population, its endowment of mineral and other natural resources and its potentially highly productive agricultural base, the long-term outlook for development is encouraging. The main goals of PNG's development strategy are to increase participation by the rural population in economic development and to achieve self-reliance, in both manpower and domestic revenue. The development of a public expenditure plan and a fund to stabilize the impact of copper revenues on the budget are important elements in this strategy, but the key to its success will be the Government's ability to stimulate more rapid growth in the agricultural sector. The critical constraint in the near term is likely to be the shortage of skilled manpower.

2. Despite the large transfer from Australia, equivalent to about one-quarter of exports, a current account deficit appeared in the balance of payments in 1980, the result of falling commodity prices, declining copper output, and high levels of imports, due in part to rising oil prices. Nonetheless, reserves remain at a healthy level of about five months worth of imports. External borrowing is relatively low, with debt service payments about 4% of exports.

3. The Bank lends US\$30-40 million of Bank/IDA blend for two operations per year with emphasis on agriculture, education and transport. Operations are becoming increasingly complex as we move into sector lending and integrated rural development projects, and a major issue that is developing is the capacity of an originally expatriate-dominated administration to continue performing at a high level. Bank-Government relations have been good and we have had an active policy dialogue on sector and macroeconomic issues.

FIJI, SOLOMON ISLANDS, WESTERN SAMOA

1. The smaller Pacific Island economies share a number of characteristics, including a large contribution of subsistence production of GDP, wide prevalence of traditional or "customary" land tenures, limited opportunities for wage and salary employment, substantial food imports and a high dependence



on foreign manpower. Although domestic resource mobilization has improved steadily, the reliance on external financing remains relatively high; Australia, New Zealand and the Asian Development Bank are the main sources for such financing. The countries' development strategies recognize the importance of agricultural development and greater self-reliance. Economic reports, prepared every three to four years, provide a framework for policy dialogue with these countries. The need for sector work is normally met in the context of project preparation.

2. In view of the pivotal role of agriculture in the development of these countries and the sparsity of our operations, which allows rather limited interaction with government agencies for institution building purposes, we have oriented our lending strategy as much as practically possible to the support of the agricultural sector (Fiji and Western Samoa). However, because of the small size of the countries involved, the active participation of other lending agencies, and the practical requirements to adapt to a different set of needs and absorptive capacities, we have also adopted a multisector approach in our lending program for Solomon Islands. In Fiji, we are developing a lending program of annual operations in the order of \$15-20 million. In the Solomon Islands and Western Samoa we have periodic operations (every 2 - 4 years) each amounting to about \$5 million (IDA) but recently we have also introduced a new lending format: cofinancing selected projects with the Asian Development Bank in the lead, especially in interim years between the larger Bank operations. Our share for such cofinancing projects is in the order of \$1 - 2 million per operation. The novel feature of such operations is the Bank's following ADB's lead and largely accepting the ADB appraisal and supervision of the project. Such cooperative action leads to a reduction of our lending costs for small loans in the Pacific Islands.



COUNTRY PROFILES (1980)/a

	Laos	Papua New Guinea	Fiji	Solomon Islands	Western Samoa
Population (million)	3.6	3.0	0.62/b	0.21/b	0.16/b
Growth rate (%)	2.4	2.3	1.8/b	3.5/e	0.7/g
GNP per capita (US\$)	90.0	740/j	1,690	430/b	350/b
Growth rate (3 year average) (%)	3.1	6.0/j	4.6	-	-
Investment/GDP (%)	9.5	22.5/j	19.3	15	-
Savings/GDP (%)	-	255/j	20.0/b	5	-
Poverty incidence - Rural (%)	-	75	30.0/b	33/b	-
Fertility	6.4	7/k	2.4/c	-	-
Adult literacy (%)	-	32	79/b	9/b	95/b
Exports (GNFS)/GNP (%)	9.4	47.4/j	41.5	45.0/f	4.3/h
Exports per capita (\$)	8.5	328.8	240.6/b	140.6/b	62.1/h
Primary excluding food	-	184.3	3.6/b	25.1/b	-
Manufacturers	-	-	19.6/b	49.5/b	-
Net petroleum imports p.c. (\$)	3.6	63.1	85.3/b	19.1/b	-
Current account balances/GNP (%)	-39.5	-3.5/j	-4.4/b	-1.3/f	-12.2/h
Debt service/GNP (%)	1.4	2.3/j	1.5/b	1.8/f	1.4/f
Debt service ratio (%)	10.8	4.3/j	4.6/b	4.1/f	8.0/h
Bank opns. 1978-80 averages:					
Commitments/GNP (%)	2.0	1.4	2.9	2	0.25/f
Number of projects per year	1.0	1.7	1	1	1/i
Debt outstanding and disbursed (\$m)	-	393/d	106/d	-	-

/a Because data are more recent and because of differences in concepts and definitions, the country data are not directly comparable with those shown in Table 1.

/b 1978

/c 1970

/d MLT, excludes private, non-guaranteed, 1979.

/e 1974-78

/f 1977

/g 1971-76

/h 1976

/i 1979-80

/j 1979

/k 1971

Source: Country Data



South Asia



Country Statements

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### IIIA. COUNTRY RELATIONS

#### 1. Bangladesh

##### Political Background

1. Ziaur Rahman, then Army Chief of Staff, became the effective leader in a martial law government, which followed a military coup in November 1975. He proceeded gradually to return the country to civilian rule. In June 1978 he won a Presidential election and his party, the Bangladesh National Party, won 68% of the 300 seats in Parliament in elections in February 1979. Martial law was lifted in March 1979. Most of the President's popular support seems to come from the urban middle class and the rural elite, the landed and well-to-do in towns and villages. He is attempting to gain broader support from the rural masses.

##### Economic Background

2. Major Constraints to Economic Development. Economic development in Bangladesh occurs in a difficult environment characterized by a set of fundamental conditions and constraints. The natural resource base is very limited, while the physical and social infrastructure is very underdeveloped. Extreme poverty, reflected in widespread malnutrition and low per capita incomes, inhibits savings and capital formation. A severe dearth of skilled manpower limits the country's managerial capabilities and the productivity of its labor force. Widespread illiteracy retards the dissemination of knowledge and of improved technology. A practically unrestrained growth in population underlies high rates of unemployment, underemployment and landlessness, and absorbs much of the benefit of whatever growth is achieved.

3. Economic Development Since Independence. The first years of independence were difficult for Bangladesh. With its economy already disrupted and its infrastructure severely damaged by the struggle for independence, the country was afflicted by poor harvests in FY72 and FY73 and by devastating floods in 1975. It was not until FY75 that GDP recovered to the pre-independence level, but between FY75 and FY80, it has increased by about 30% in real terms (or about 5.5% p.a.), despite serious setbacks in agricultural production in FY77 and again in FY79 and FY80. Output in manufacturing (as measured by the production index for large and medium-scale industries) rose by about 7.5% annually between FY75 and FY80, most of this growth taking place outside the jute industry.

4. The Second Five-Year Plan (issued in draft form in May 1980) accords top priority to three major efforts: (i) achievement of self-sufficiency in foodgrains by FY85; with domestic foodgrain production targeted to increase to an annual amount of 20 million tons by FY85; (ii) reduction of the population growth rate with a view of bringing the net reproduction rate down to unity by the year 1990; and (iii) progress towards mass literacy through the vehicle of free, universal primary education. Enhanced priority is also to be given to energy development, particularly through exploiting known reserves of natural gas.



Bank Group Lending, Policy Dialogue and Current Issues

5. Lending Strategy. In accordance with the Government's priorities, IDA's major focus has been on agriculture, especially projects that provide agricultural inputs, including in particular the provision of adequate fertilizer supplies to farmers. Emphasis has also been given to irrigation, improved seeds, research and extension, agricultural credit, and increased storage capacities. Other sectors which facilitate agricultural development, such as transportation and fertilizer manufacture, also have been stressed.

6. As part of the "core" of the Second Five-Year Plan, IDA assisted the Government in preparing a Medium-Term Foodgrain Production Plan, complete with project descriptions, to achieve the target of foodgrain self-sufficiency by FY85. This plan is technically feasible, but will require better performance in mobilizing the necessary resources, including managerial skills, than yet shown by the Government.

7. The large population (92.2 million in 1981) makes population planning an extremely high priority. Two population credits have been extended to Bangladesh. In industry, IDA has financed the Bangladesh Shilpa Bank (a development finance company), three small industry credits, and projects to rehabilitate the fertilizer and jute industries. In addition, industry has been the main beneficiary of the nine imports program credits which focused on: provision of raw materials and spare parts to help achieve a better utilization of industrial capacity; improved management and efficiency; improved maintenance; and better production planning and control. Attention also was directed at improved financial performance through asset rehabilitation and capital restructuring programs.

8. Economic Performance. As overall economic and project implementation performance has improved, the Bank Group's relations with Bangladesh have been increasingly concerned with high-level discussions of economic policy and preparing for expanded Bank Group lending in the FY81-FY85 period in support of the Second Five-Year Plan. Last year, President Ziaur Rahman requested Mr. McNamara to increase the volume of IDA lending to Bangladesh to \$600 million per annum beginning in FY81. In his reply, Mr. McNamara indicated that IDA might be able gradually to increase its lending to \$600 million per annum by FY85, if performance in economic management, in project preparation and in implementation continued to improve. Specific goals to be achieved and measures and criteria to monitor Bangladesh's economic and project performance over the five years were set out in an Aide-Memoire and covering letter from Mr. McNamara on April 19, 1980. A letter from Mr. Hopper on October 21 covered a second paper, which had been discussed and agreed with the Government, setting out specific goals for FY81. The FY81 IDA allocation to Bangladesh was increased by about 10% over the amount previously allocated. Future yearly lending levels will be decided following periodic reviews of the country's performance. The first such review of the "performance criteria" should take place in the first quarter of FY82. The Government propose to discuss progress with us in April. In the meantime, we have adopted for planning purposes a lending matrix which reaches the \$600 million level in FY85, and the Region has received additional staff allocations to prepare and appraise the expanded lending program.



9. Program Lending. In recent years, the "program justification" for program lending has focused increasingly on macroeconomic issues. In FY80 and again in FY81, the major thrust has been on food policy and foodgrain production issues. In FY82, we intend to introduce trade and industrial policy as a new focus.

10. Project Implementation. Project disbursements initially lagged behind expectations, owing largely to delays in the release of local funds, approval of contracts, employment of consultants, and appointment of staff. Underlying these delays were serious constraints that included a shortage of qualified staff, over-centralized bureaucratic procedures and organizational deficiencies. Progress has been made recently on these issues and the disbursement performance is improving although there are still problems. There are indications that (both now and in the past) corrupt practices contribute to the problems. IDA and GOB have given increased attention to regular monitoring and supervision in order to identify and resolve potential problems. IDA is providing assistance both under specific projects and under technical assistance credits to assist in improving planning, project preparation and implementation capabilities. Nevertheless, achieving further progress in reducing bottlenecks should be a major subject of attention in our assessment of performance over the next few years.

11. Balance of Payments and Aid Requirements. Bangladesh's balance of payments is characterized by a massive structural trade deficit and heavy dependence on foreign aid. Export earnings in FY80 represented less than 7% of GDP and less than 35% of the import bill. Bangladesh's FY80 foodgrain and petroleum purchases alone accounted for over three-quarters of the 51% increase in imports in that year. The trade deficit widened from about US\$950 million in FY79 to some US\$1.6 billion during FY80 and it is expected to reach US\$1.7 billion in FY81.

12. Recently, aid commitments have not grown as fast as either disbursements or the trade deficit. As a result, pipelines have been drawn down severely, especially for commodity aid. Thus we have recommended to the Aid Group for FY82 new aid commitments (food, project, and commodity) of US\$2.6 billion, including US\$900 million in commodity aid. We should increase our efforts, including more working level contacts with bilateral agencies, to mobilize more aid for Bangladesh, provided that we ourselves are satisfied with progress (as in paragraphs 8-10 above) and are willing to continue to increase our lending levels.

#### Aid Coordination

13. The Aid Group. The Bank Group has chaired the Bangladesh Aid Group, an informal organization of donor countries and international agencies, since its inception in 1975. The Aid Group meets regularly once a year (usually in Paris in April) to discuss the economic situation and to indicate aid for the forthcoming Bangladesh fiscal year (the same as the Bank Group's). There are occasional meetings on special subjects, such as family planning, or food aid and food policy. The Bank Group prepares for the annual Aid Group meeting a report on the economic situation and prospects for Bangladesh and the amount of aid recommended. This year's meeting (and report) also focused on the Second Five-Year Plan. The Government delegation, usually led by the Minister of Finance, also presents an annual memorandum to the Group. Aid coordination is



made more difficult by the fact that Bangladesh probably attracts more donors than any other country. In addition to the two dozen countries and international agencies who participate in the Aid Group, Bangladesh receives considerable quantities of aid from communist countries, including China, and Arab sources (of these, only the Islamic Development Bank is an observer in the Aid Group). The Resident Mission assists in aid coordination by chairing meetings of local representatives of Aid Group members; we are now attempting to bring non-Aid Group members into some of these meetings as a means of improving coordination.

March 20, 1981



### IIIA. COUNTRY RELATIONS

#### 2. India

##### General Political and Economic Background

In 34 years of independence, India has maintained a democratic political structure, with the sole exception of the 18 month emergency period in 1976-77. In the context of relatively open multi-party parliamentary system and an active, outspoken press, Indian policy-making proceeds in a fish-bowl atmosphere that affects significantly internal development priorities as well as India's external relations. Although Mrs. Gandhi and her Congress (I) party currently hold a 65% parliamentary majority, rapid shifts in public perceptions and the threat of constantly shifting political loyalties can result in dramatic political upheavals as both the 1977 and 1980 elections demonstrated (when Mrs. Gandhi was first turned out then returned to power by overwhelming margins). With the exception of the three-year Janata interlude, Mrs. Gandhi has been Prime Minister since 1966. During this period general relations with the Bank Group have consistently improved from the nadir reached shortly after the ill-starred Bank/Consortium sponsored rupee devaluation in June 1966.

Since independence the population of India has grown at an average rate of 2.1% p.a. reaching a total of 672 million by mid-1980. Agriculture continues to dominate India's economy, employing over two-thirds of the labor force. However, the land base is not sufficient to provide an adequate livelihood to all those engaged in agricultural activities, especially the landless or nearly landless who have only an insecure grasp on the means of existence. The share of agriculture in GDP at factor cost (measured in 1970/71 prices) has declined from 59.6% in 1950/51 to 40.7% in 1978/79. The share of industry has increased over the same period from 14.5% to 22.7%. But industrialization has not been rapid enough to absorb the growing labor force, nor to bring about the substantial economic transformation that has led to higher productivity and rapid urbanization in some other developing countries. The urban population was 18% of the total in 1960, and is 21% now.

Economic growth has been slow in the past. The trend growth rate of GDP was 3.7% per annum from 1950/51 to 1978/79. Slow growth in agriculture - 2.5% per annum over the same period - has constrained overall growth, not only because of the high share of agriculture in GDP but also because scarce foreign exchange has often been required to import food. Industrial value-added has grown more rapidly, at 5.4% per annum between 1950/51 and 1978/79, but this growth has not been as high as in many other countries, nor as high as required. Gross domestic saving more than doubled from 10% of GDP in 1950/51 to 24% in 1973/79. Similarly, gross domestic investment as a fraction of GDP rose from 10% in 1950/51 to just over 24% in 1978/79. Foreign savings have never financed a large portion of domestic investment: a peak of about 20% was reached during the early 1960s; by the end of the 1970s, the proportion had returned to much lower levels. External assistance has been low both as a percentage of GDP and in per capita terms. Net external assistance has never risen above 3% of GDP.



World Bank/India Relations. Relations of the Bank Group with India, its largest borrower, are firmly grounded in several generations of projects in key sectors and in the Bank's role as the convenor, chairman, and major donor of the Indian Aid Consortium. During the past decade both the development of projects and the economic analysis which underpins sectoral lending priorities have been concerned with two broad objectives: first, a significant improvement in the living standards and future prospects of the hundreds of millions of Indians living on the margin of subsistence, and second, a self-sustaining continuing structural transformation of the Indian economy, leading to improved efficiency in both agriculture and industry. India's size and complexity places limits on the direct contribution of any outside agency, including the Bank Group, to achieving these objectives. But through the Bank's experience in project implementation and its program of economic and sector work, a strong operational/technical relationship has developed both at the working and policy-making levels in several sectors.

Bank activities in the agricultural sector illustrate this process well. In placing heavy emphasis on both public and private investment in this sector the Bank has underscored the importance of increased food production as the critical factor in raising the living standards of India's poor, first through the creation and maintenance of adequate food supplies through India's public (and private) distribution system; and, second, through the widespread increases in purchasing power that accompany agricultural growth. While Government of India policy led the way in terms of overall strategy, the Bank has made important contributions to the design of irrigation systems, to the reorganization of agricultural extension and research and to the administration and targetting of agricultural credit. In each case the Bank's involvement has significantly improved the capacity of government programs to increase output and productivity while providing significant direct benefits to the poor. As a result, the Bank's analyses are now seriously considered in developing agricultural policy.

Bank-India relations in the industrial sector have taken a somewhat different course. India's experience of the past 15 years with relatively slow rates of industrial expansion and continuing rigidities in economic structure confirms the need for a growing industrial sector able to absorb the resources released by increasing agricultural productivity. In the industrial sector, divergent views on general policy directions have inhibited the strong project-grounded technical collaboration that has increased the Bank's leverage in agriculture. The series of non-project operations (eleven Industrial Imports Credits) that ended in the mid-1970s provided only a limited basis for industrial policy discussions. In an effort to lay the groundwork for a more productive relationship in the industrial sector, the Bank has begun a program of sector work designed to provide the macro-foundations essential to a meaningful policy dialogue in India. This sector work also has facilitated a growing industrial project pipeline which could ultimately lead to a relationship



analogous to that in agriculture, provided the Bank maintains a high level of technical expertise and the Indian government in turn evidences a willingness to begin a process of policy reform.

Crucial to India's structural adjustment prospects, is the more rapid development of energy resources. Even though relatively high rates of growth in energy production have been achieved periodically (particularly in power generation), faster and more consistent growth is required given the growing importance of commercial energy to both agriculture and industry. As a result of the Bank Group's extensive operations in the power sector, the Bank has identified several policy objectives. These include measures to improve the technical efficiency of plant operation and maintenance, the development of a long-term, integrated regional and national power planning system, and improvements in management and financial viability. The Government has responded to the substance of these concerns but our future relationship will depend crucially on the ability of the Government to design and implement programs based on mutually agreed policies.

A relatively new and rapidly developing area of Bank collaboration in India is in the oil and gas sector. The Bank's involvement has aimed at optimizing the development and utilization of India's oil and gas reserves, particularly the offshore fields. The Bank has played an important role in encouraging India to seek external, commercial financing in this key sector and to accelerate exploration activities through greater involvement of experienced foreign firms. The Bank has been able to use its limited financial resources and its influence as an impartial multilateral organization to achieve mutually agreed objectives.

In the coming decade, the Bank's role as India's largest creditor is going to assume even greater importance as India turns to new sources of external finance. As noted above, the Bank has already assisted in this process to a limited extent in the oil and gas sector. By the mid-1980s India's borrowing requirements are projected to increase greatly. As a result, the Bank dialogue with India on both sectoral and broader macro-economic policy issues is likely to become an increasingly important element in our relationship. This dialogue will inevitably take a more subtle form than in countries where the Bank may assume an explicit role in the development of economic policy; in the case of India our function is more one of an independent commentator whose views may, at best, provide the incremental weight to tip the scales in favor of policies that appear to promote India's development objectives most effectively. Given India's balance of payments prospects during the 1980s, non-project lending is likely to become relatively much more important in achieving these objectives and consequently in framing our relationship with India; but the strength of the Bank's relations should continue to be grounded in the detailed sectoral knowledge built up from project implementation, with a continuing emphasis on those sectors of the Bank's traditional



involvement, particularly agriculture, energy and other infrastructure, with the major initiative in the industrial sector.

Aid Coordination. The India Consortium was the first established by the Bank 24 years ago. It is comprised of 13 bilateral members and 7 international organizations and observers. The group was last convened in July 1980 when indications of assistance totalling US\$3.4 billion were made. This amount represented no increase, even in nominal terms, over indications made in 1979. The next Consortium meeting is scheduled for June 1981. Recent economic developments have been analyzed by Bank staff in a Country Economic Memorandum, now in draft, which will be circulated beforehand to all Consortium members and form the basis of discussion at the meeting.



### IIIA. COUNTRY RELATIONS

#### 3. Pakistan

##### General

1. Since its inception in 1947, Pakistan has had a difficult and eventful history fed by a tense relationship with India; tensions between the provinces, culminating in the loss of East Pakistan (Bangladesh) in 1971 and now mainly manifested by differences over resource allocations; incipient secessionist movements among the minority Baluchis and Pathans in the north; and conflicts between traditional Islamic and modernistic influences in society. Islam, however, the *raison d'etre* for Pakistan's creation, has remained a strong unifying factor and has received increased emphasis under the present military regime of General Zia ul Haq.

2. The Soviet invasion of Afghanistan, which has caused a massive influx of refugees (now estimated at 1.4 million) into Pakistan as well as necessitating increased expenditure on defense, has been a major new source of uncertainty for Pakistan and has created new dimensions in its international relationships. General Zia appears at the moment to remain in control, though there have recently been signs of increasing opposition to him. One of the justifications for a perpetuation of the present regime is the apparent absence of a viable civilian alternative. While postponing national elections indefinitely, General Zia has held municipal and local elections and has formed provincial and federal advisory bodies from among elected officials.

##### Economic Developments

3. Despite the unsettling events on Pakistan's borders, the Government has not ignored the pressing needs of the economy. On the contrary, the indefinite postponement of national elections in October 1979 had a positive effect on the Government's willingness and ability to adopt difficult economic measures, and the economic reforms of 1977-79 have been pursued with increased vigor, as evidenced by the recent conclusion of an Extended Fund Facility (EFF) agreement with the International Monetary Fund (IMF).

4. Pakistan's economic performance has improved significantly during the last three years in several respects. Gross Domestic Product (GDP) has grown by about 6% per annum since FY78 accompanied by record or near-record crops in the major agricultural commodities (wheat, cotton and rice); a recovery in private industry from the depressed levels of the mid-1970s; and substantial growth in exports. This performance contrasts markedly with the economic stagnation during much of the 1970s, when GDP growth averaged around 3-1/2% p.a. and export growth was negligible.



5. Several factors have aided the recovery in the economy since 1977, including favorable weather, improved foreign demand for Pakistan's exports, and higher domestic demand associated with better crops and workers' remittances from the Middle East. However, credit must also be given to the various policy changes introduced by the Government. In agriculture, price incentives and input supplies, particularly of fertilizer, have been improved. A start has been made in addressing the deep-seated problems affecting productivity at the farm level by improving extension services, agricultural research and water management. In industry, the Government has had some success in encouraging more private investment, despite the continued political uncertainties, and in increasing efficiency in the public sector. Tighter controls on government spending and increased revenues through higher taxes, prices and other measures have reduced the Budget deficit to less than 3% of GDP.

6. Notwithstanding recent improvements in the overall management of the economy, financial difficulties persist, notably in the balance of payments. Pakistan's gross oil import bill increased from \$400 million to \$1.24 billion between FY77 and FY80; for FY81 it is estimated at \$1.5 billion. Fertilizer and other imports have also risen sharply. Remittances from Pakistani workers abroad (mainly in the Middle East), which have jumped from \$578 million in FY77 to \$1.75 billion in FY80, have counteracted these increases. Nonetheless, the current account deficit in FY80 remained around \$1.1 billion, or 4.4% of GNP. Foreign exchange reserves are equivalent to about one month's imports.

7. The recent EFF agreement with the IMF, and a consequent agreement on a short-term debt rescheduling arrangement by bilateral creditor countries in the Pakistan Consortium, will alleviate the immediate financial pressure and improve the environment in which further economic reforms can be pursued. The EFF agreement with the IMF specifies a number of reforms which Pakistan will implement during the coming 2-3 years. These include substantial import liberalization; the provision of additional incentives to private industry, agriculture and exports; and measures to improve the performance of public enterprises. In addition, the Government is formulating a new public investment program for FY82 to FY84 which will give priority to quick-yielding investments designed to improve output and productivity, particularly in agriculture, irrigation and energy, and to the social sectors. Some key issues on which the Government should focus are discussed briefly below.

Issues

8. Savings Performance. Although national savings (at around 12% of GNP) are now substantially above the low levels of the mid-1970s, there has been little further improvement over the past two years and Pakistan's savings performance remains well below that of a number of other countries at a similar stage of development. The mobilization of private savings is likely to be made more difficult by the Government's decision to "Islamize" the banking system by introducing interest-free, profit-sharing lending in



parallel with conventional banking and by the general disuse of interest rates as a policy instrument. In addition, while public savings have been assisted by pricing decisions to limit budgetary subsidies, the Government should move away from the present complex system of government price controls and market intervention toward a more market-oriented economy. Such a change is likely to be one of the most effective ways of encouraging the revival of private investment and savings.

9. Agriculture. Considerable potential exists in Pakistan for the more rapid development of agriculture, principally through increases in yields, which could technically be doubled or trebled in most crops. The realization of this potential will mainly depend on the more efficient use of water, fertilizer and other inputs through the strengthening of advisory services to farmers, basic and adaptive research and water management. While Pakistan (with substantial Bank and other external assistance) has invested heavily over the past two decades in irrigation infrastructure in the Indus Basin (e.g., Mangla and Tarbela Dams), programs are now required to utilize the increased water supplies resulting from these past investments to better effect. The Bank is working closely with the Government in preparing and implementing projects to address these critical problems.

10. Energy Development. The development of domestic energy supplies in Pakistan is of the highest priority. Almost 40% of Pakistan's commercial energy needs are still met by petroleum, the bulk of which is imported. The Government's efforts over the past several years to encourage the exploration of domestic oil resources and the development and substitution of other domestically available energy forms (mainly hydro-electricity and natural gas) have met with encouraging success, and the Bank has supported these efforts with several projects for gas pipeline and electric power development as well as with a first project for the development of indigenous oil fields. However, a number of key issues threatens to affect the sector's development.

11. Energy policy is presently conducted in Pakistan in an uncoordinated manner; problems are largely dealt with on a day-to-day basis, with inadequate long-term consideration. There is an important need to develop a strong energy planning capability and to strengthen public institutions in the sector. Secondly, a long-term pricing policy is needed which provides adequate incentives to develop new and existing petroleum resources. The present level of well-head pricing for "old" oil and gas requires urgent review to ensure that unrealistically low price levels do not inhibit both public and private sector initiative. In addition, an immediate evaluation of the scope for more rapid development of existing gas fields is needed in order to avert an emerging shortage of natural gas. These various matters are being actively pursued with the Government in the context of our future lending operations.



12. Industry. GOP policy in the industrial sector is to provide more scope and incentives to private entrepreneurs, while improving the performance of the public sector. Private confidence, though restrained by regional political developments, has improved and an upturn in medium to large-scale private industrial investment is now evident.

13. Several actions, however, are required to facilitate more rapid progress, such as steps to improve the availability of both local and foreign financing to the private sector; further strengthening of Government procedures; more rapid provision of necessary utilities and other infrastructural requirements; and training programs to ease the increasing shortage of skilled manpower resulting from migration to the Middle East. A longer-term requirement is the introduction of an appropriate framework of incentives designed to rationalize the industrial structure consistent with Pakistan's comparative advantage. A study of industrial incentives is to be carried out by GOP with Bank assistance to provide the basis for making such adjustments. The Government's present cost-plus pricing policy also needs to be reviewed.

14. In the public industrial sector, GOP has begun to take steps to improve financial performance, management and capacity utilization; close chronically unprofitable units; and encourage greater private participation in selected industries. These efforts need to be sustained and intensified.

15. Population Planning. Pakistan continues to face substantial and rapidly growing problems in the social sectors, the most significant of which is population planning. The population growth rate remains around 3%, one of the highest in the world. Bank projections indicate that, even assuming some decline in fertility, the population will increase between 1980 and 1990 by a further 26 million, or over 30%, to about 108 million. Improved education and employment opportunities for women appear to be a key factor in reducing fertility rates; literacy among women is only about 11%.

16. The Government has recently shown greater awareness of the serious implications of the high growth rate. A revised population planning policy has been adopted which, inter alia, recognizes the key role of education and motivation programs and of special programs for women in changing attitudes towards family size. We intend to follow the progress of these plans closely during the coming months, to assess whether the recent initiatives are being followed up by necessary government action to strengthen programs at the field level and to determine whether there is scope for effective Bank assistance in this area. A population project, tentatively included in the lending program for FY84, will be brought forward if feasible.

#### Lending Program

17. Because of major deficiencies in government economic policies in the mid-1970s, IDA allocations to Pakistan were reduced, and all Bank lending was stopped in 1977. However, at the review of the latest Country Program Paper for Pakistan in December 1980, Mr. McNamara agreed that Pakistan's improved economic performance warranted a substantial increase



in its IDA allocations. He also agreed that resumption of Bank lending should be tied to agreement with Pakistan on a structural adjustment lending (SAL) program. Exploratory discussions with the Government on an SAL, tentatively scheduled for FY82, have been initiated focusing on such matters as the size and composition of public expenditure programs and policy issues in agriculture and the energy sectors; given the complexity of these issues, the rate of progress of these discussions is difficult to predict. Our proposed project lending is focused chiefly on the agricultural, irrigation and energy sectors; it would also support the development of industry, essential infrastructure and the social services. Further increases in the proposed lending program for Pakistan (which presently is equivalent to \$3.5 per capita per annum compared, for example, with \$6.1 for Indonesia) would depend on better project implementation by Pakistan as well as on a continuation of economic reform efforts.

#### Resident Mission

18. During 1978 and 1979 the Resident Mission in Pakistan worked with a very reduced number of staff and its project support function was limited. In 1980, the position of Resident Representative, which had been vacant for 20 months, was filled and the staff considerably strengthened. As a result, the Mission is now able to make an increasing contribution to: (i) easing operational problems on projects under execution or preparation; (ii) economic analysis and reporting; and (iii) the dialogue with the Government on policy matters. In light of the Region's growing involvement with new areas of lending, the Resident Mission needs to increase its capacity further, especially to supply implementation assistance for agricultural projects. The Mission will also take on more responsibility for the supervision of economic and sector work, which the Region intends to conduct increasingly through local research institutions.

#### Aid Coordination

19. The Pakistan Consortium, which was one of the first aid coordination groups established by the Bank, remains active; it presently comprises 12 member countries and 5 international organizations. The Consortium was last convened for a special meeting in January 1981 to discuss debt rescheduling (see paragraph 8 above); at this meeting Consortium countries agreed to reschedule 90% of debt service falling due on official concessional loans during the 18 months beginning mid-January 1981. At the last regular meeting of the Consortium in June 1980, total indications of assistance to Pakistan for FY81 amounted to about \$1 billion, substantially higher than for the previous year. The next Consortium meeting is scheduled for June 1981.

March 20, 1981



### III A. COUNTRY RELATIONS

#### 4. Other Countries in Region

##### Burma-Maldives-Nepal-Sri Lanka

###### Burma

1. Among developing countries, Burma has a favorable resource endowment, including substantial arable land, considerable and essentially unexploited marine life, valuable forest reserves and potentially extensive mineral resources. Burma is a net rice exporter and is roughly self-sufficient in petroleum. Economic performance during the 1960s and early 1970s was poor; however, Ne Win's Burma Socialist Program Party, which is the only authorized political party, initiated a new set of policies in the mid-1970s, hoping to reverse this trend. While retaining its ideological commitment to the Burmese Way to Socialism, which affirms the compatibility of socialist principles with traditional Buddhist values, the Government moved to institute more pragmatic economic policies and solicited foreign aid to assist in the development effort. Increasing emphasis has been placed on agricultural development, and in particular on paddy production, and on running the State Economic Enterprises more along commercial lines. The response of the economy has been encouraging, with real GDP growth averaging 6% in recent years. More rapid growth has, however, been accompanied by an increased need for domestic resource mobilization, higher export earnings, and a more efficient allocation of public investment. Burma is also facing a rising debt service ratio, due to contracting some medium-term suppliers' credits and commercial borrowings. Although the Government is aware of our views on these matters, the receptivity of officials to our advice on macro-economic issues is limited by the Burmese ideology.

2. IDA strategy in Burma is based on the recognition that change in overall economic policies will come about only slowly; we attempt to identify economically viable projects within the context of the present socio-political system. We expect improvements in economic performance to be achieved through carefully prepared projects aimed at limited but noticeable changes in sector policy and organization rather than through attempts at more intensive dialogue on macro-economic issues. Given past difficulties encountered in processing some projects (due to differences in views on project design, and especially the role of pricing, and procedures, such as ICB for civil works), we favor working with Government agencies (e.g., Ministry of Agriculture and Forests, Burma Ports Corporation, and Posts and Telecommunications Corporation) with which we have succeeded in developing a good relationship, based on mutual understanding of objectives and procedures, or which appear to be interested in working with the Bank. We are currently building up relations in new sectors (e.g., power) where we feel Bank involvement might contribute toward desirable policy reforms.

3. Although we have good relationships with officials at various levels, the lack of a coordinating point in the field between the Bank and the Burmese authorities has limited our ability to carry on a continuous dialogue. We are therefore discussing the possibility of establishing a one-person Resident Mission in Rangoon. Finally, we intend to continue our role in coordinating external assistance (through the Burma Aid Group) and arranging co-financing for projects, as required.



## Maldives

4. The Maldives is among the 20 poorest countries in the world, and receives little bilateral aid, depending largely on UN and Arab Fund programs for support of its development programs. Like most island developing countries, its resource base is narrow in relation to population, and it lacks known mineral resources. The country is heavily specialized in fishing and tourism and increasingly dependent on food imports. It has developed a successful shipping line which has also mitigated some of the disadvantages of remoteness. To date, Government development activities have been limited, but have involved investments in sectors where the country's comparative advantage is strong -- fishing, shipping, and tourism. The National Planning Agency is preparing to institute formal development planning for the future.

5. The Maldives became a member of the IMF and the World Bank in January 1978; its application for membership in IFC was accepted, and awaits only completion of formal procedures. The first IDA-assisted operation is seeking to expand the mechanized fishing fleet to enable the fleet to serve export markets. Progress has been good, with one-half of the credit already disbursed and the technical assistance program to be completed by the fall of 1981. A follow-up fisheries project to assist with the development of infrastructure such as local storage, collection and processing of fish products is under discussion. We are also exploring prospects for a rural development program to reach those islands whose fisheries prospects are limited. A full economic report was prepared in 1980, and has recently been released in red cover. The Government has proved to be quite pragmatic and resourceful and our relations have been extremely good.

## Nepal

6. A semi-feudal Kingdom, Nepal is one of the least developed countries; per capita income was \$120 in 1978 and health standards are well below the average in South Asia. In the hills, where the majority of the population lives, population growth is overwhelming the meagre resource base, exacerbating food deficits and resulting in ecological deterioration, manifested in severe fuelwood shortages and soil erosion. As a predominantly agricultural country, Nepal's present development strategy gives priority to the agricultural sector, while also stressing small industries and tourism and the need to meet minimum needs in food, fuel, drinking water and health (including family planning programs). Shortage of qualified manpower, a weak public administration, rugged topography and being land-locked with long transportation lines are severe constraints on Nepal's development. Achieving sustained economic progress will require a substantial increase in Nepal's development efforts. This can only occur with a much more efficient public administration and strong political will. However, decision-making has been weakened by the political uncertainties of the past two years. Recent constitutional reforms provide for direct elections to the National Parliament, but it remains to be seen whether the Government which emerges after the forthcoming elections will provide the strong leadership required.



7. To support Nepal's overall development strategy, IDA has focussed assistance on directly productive investments particularly in agriculture, complemented by investments in a wide range of infrastructure as well as in supporting sectors such as technical assistance and education. A major contribution of the Bank has been coordination of donors' generous support via the Nepal Aid Group, and this role will increase in importance as efforts expand in those development programs where several donors are active, which address general government institution building (public administration, credit, agricultural extension and education), or which overlap many sectors (erosion control and rural development).

8. IDA's future policy dialogue will focus on measures to increase absorptive capacity, while IDA assistance is likely to be directed at consolidating and enhancing ongoing programs, rather than launching new approaches. However, in addition to these programs, prospects exist for development of hydroelectric power (Nepal's potentially major resource) for the Indian market. If ongoing negotiations between Nepal and India on the Karnali project (\$2-3 billion, an amount far exceeding Nepal's current GNP) are successful, the Bank may be asked to finance engineering and other studies as well as ultimately to assist together with other donors in financing construction. Deliberations on the complex political, legal and financial issues involved will take considerable time.

#### Sri Lanka

9. In the general elections of July 1977, the United National Party, led by J.R. Jayawardene, won a landslide victory. For the sixth successive time, Sri Lanka's electorate voted out the Government in power. The UNP Government has interpreted its victory as a mandate for major political and economic changes. A presidential system of government modelled on the French Fifth Republic has replaced the Westminster style Parliamentary System. Major economic reforms have been introduced under a series of IMF programs, including unification of the exchange rate at a depreciated level, an associated liberalization of imports, the dismantling of administrative controls, and a substantial reduction in the burden of consumer subsidies in order to transfer budgetary resources from consumption to investment. The Government has succeeded in substantially raising the level of public investment through a number of new initiatives aimed at: (i) redressing past neglect of economic and social infrastructure; (ii) providing investment funds for the productive sectors; and (iii) substantial employment generation through three major new development programs: accelerated implementation of the Mahaweli river valley development program -- a major power and irrigation scheme involving the construction of four dams with power benefits of 500-600 MW, and irrigation of 117,000 ha of land, a major housing and urban renewal program, and a 200 square mile free trade zone north of Colombo with a view to attracting foreign private investment.

10. The response of the economy in 1978 and 1979 to the new policies and programs was impressive. Real GDP grew at an average of 7% annually, compared with 3% during 1970-77; there was a substantial decline in the high rate of unemployment and investment rose to 25% of GDP in 1979,



compared to an average of 16% in 1970-77. Foreign investment has also begun to flow in, though the sums involved are relatively small. Although 1980 has been another year of strong growth in the domestic economy (5.6%), a sharp deterioration in terms of trade and stagnant exports, together with an excessive acceleration in investment spending have resulted in an overall performance that is disturbing. This poor performance can be seen in the substantial net borrowings by Government from the banking system (10% of GDP), a sharp acceleration in domestic inflation (a 38% increase in consumer prices as against 19% in 1979), and a massive current account deficit in the balance of payments (19% of GDP as against 11% in 1979). The Government has begun to take corrective action in 1981 by proposing a substantial reduction in real terms in Government expenditures. The IMF, which suspended disbursements half way through the second year (1980) of a three year 260 million SDR Extended Fund Arrangement (when the Government exceeded the agreed credit ceilings), is currently negotiating a resumption of the program based on stabilization measures that are under preparation. In the absence of such corrective measures, Sri Lanka's economic situation for 1981 and 1982 could prove extremely difficult. These issues have been extensively reviewed with the Government during the past 18 months and will be the main focus of the discussions at the Sri Lanka Aid Group meeting in early July 1981.

11. The Bank group responded to the new policies and programs in Sri Lanka initiated in late 1977, with a substantial increase in the volume of its operations. The expanded program is designed to support the Government's efforts to accelerate implementation of the Mahaweli River development program, help finance the considerable rehabilitation needs of both the productive sectors and economic infrastructure, and at the same time to direct resources towards other quicker yielding investments that risk being neglected. The deterioration in economic performance in 1980, and most notably the resource crisis facing the Government, require a reexamination of this lending strategy. The high inflation during 1980 has further pushed up investment costs, especially for the major programs, while the Government's revenues appear relatively inelastic. As a result, the resources available for new activities are now extremely limited. The Government would, therefore, like the Bank to focus project lending towards what it regards as high priority projects and to shift remaining resources towards relatively quick disbursing program type lending, or structural adjustment lending. The extent to which we can respond to the request for structural adjustment lending will depend on the seriousness with which the Government pursues stabilization policies, and on its willingness to come to an agreement with the IMF. We have initiated a review of our lending program which we expect to complete by end-March.

March 20, 1981