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Institutional Reform

The Case of Malaysia, Indonesia and Thailand During the Asian Crisis

Bachelor Thesis in Political Science

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Sammanfattning

Att assistera utvecklings- och tillväxtländer i deras strävan att lyftas ur fattigdom får mycket uppmärksamhet idag, och det har upprättats internationella institutioner för att handlägga utvecklingsfrågor. Denna studie undersöker giltigheten och legitimiteten av sådana internationella institutioners ingripande i tillväxtländer som står inför en kris, där speciellt internationella valutafonden assisterar med hjälp av konditionella lån. Dessa lån är beroende på att länderna ifråga genomgår ekonomisk reform, vilka i sin tur kräver förändringar i de institutionella arrangemangen för att uppnå tillväxt.

Studien görs i form av en fallstudie, där en litterär begreppsstudie avseende legitimitet och institutionell teori appliceras på fallen Malaysia, Indonesien och Thailand som stod inför Asienkrisen 1997 – 1998. Målet är att ta reda på om extern konditionell reform (på begäran av internationella valutafonden) är legitim, om graden av legitimitet är beroende på om ett land gått igenom konditionell reform eller ej, samt slutligen om studien visar någon indikation på vilken hypotes för ekonomisk tillväxt som passar för denna fallstudie.

De institutionella variablerna (korruption, socioekonomiska faktorer, regeringsstabilitiet och intern konflikt) visar att Malaysia, som inte åtog sig att genomgå konditionell reform, har presterat bäst av de undersökta länderna. Den ekonomiska indikatorn (BNP per capita) stödjer även detta resultat.

Institutionell teori av North, Ostrom och Sen används för att hitta de nödvändiga förutsättningarna för institutionell utveckling. I studien dras slutsatsen att det inte var legitimt i denna fallstudie med extern institutionell reform, vilket också stödjs av det presenterade teoretiska ramverket. Studien visar på en skillnad i grad av legitimitet, där Malaysia har högst legitimitet av länderna som undersöks. Det kan också beslutas att den institutionella hypotesen är överlägsen den geografiska hypotesen och policyhypotesen när det gäller att förklara ekonomisk tillväxt.

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Abstract

Helping developing and emerging countries out of poverty attracts much attention today, and there are international institutions implemented to deal with issues of development. This study examines the validity and legitimacy of IFIs intervening in emerging countries facing crisis, where particularly the IMF assists with conditional loans. The loans are conditioned upon economic reforms, which in turn require institutional arrangements to change in order to achieve economic growth.

The study is carried out as a case study where a conceptual literature study on legitimacy and institutional theory is applied to the cases, Malaysia, Indonesia and Thailand. This research aims at finding out if external conditional reform (demanded by the IMF) is legitimate, if there is a difference in legitimacy depending on whether a country has adopted these reform or not, and lastly, if there is an indication of which hypothesis for economic growth that suits the case study.

The institutional variables (corruption, socioeconomic conditions, government stability and internal conflict) show that Malaysia, the country that did not go through with IMF induced reforms, has performed the best out of the sampled countries. The economic indicator (GDP level per capita) also supports this finding.

Institutional theory by North, Ostrom and Sen is used in order to find the necessary conditions for institutional development. This study concludes that it was not legitimate in this particular case study with external institutional reform, which is also supported by the theoretical framework presented. There is a difference in degree of legitimacy, where Malaysia did enjoy the highest out of the countries presented. Also, it is concluded that the institutional hypothesis is superior to the geography hypothesis and the policy hypothesis in explaining economic growth.

List of Abbreviations

CPI	=	Corruption Perception Index
EU	=	European Union
FDI	=	Foreign Direct Investment
GDP	=	Gross Domestic Product
GNP	=	Gross National Product
ICRG	=	International Country Risk Guide
IFI	=	International Financial Institution
IMF	=	International Monetary Fund
MDGs	=	Millennium Development Goals
NGO	=	Non-Governmental Organization
NIEs	=	Newly Industrialized Economies
PPP	=	Purchasing Power Parity
PRGF	=	Poverty Reduction and Growth Facility
PRSP	=	Poverty Reduction Strategy Paper
UN	=	United Nations
US	=	United States
WB	=	World Bank
WTO	=	World Trade Organization
WWII	=	World War II

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1 Introduction

With increased international interaction in the economic, political and social spheres of society, the need for international institutions is evident. The United Nations (UN), the International Monetary Fund (IMF), the World Bank (WB) and the World Trade Organization (WTO) are examples of such institutions that monitor international activity. These institutions are in one way or another involved in development issues of what has been traditionally called 'third world' countries, or developing countries. Traditional economic theory would suggest that increased trade and international interaction would lead to increased specialization and to that everyone would be better off. The global aggregate income has indeed increased in accordance with what theory suggests, but in reality the disparities between rich and poor are more evident than ever.

After World War II (WWII) when the United States (U.S.) helped rebuild Europe through the Marshall Plan, focus has shifted towards helping less developed nations develop. Today, individual nations have their own development policies and governmental units who work with these questions. Also, the European Union (EU), the UN and Non-Governmental Organizations (NGOs) work continuously with development assistance. A substantial amount of financial aid flows out of mainly developed countries and into less developed ones every year. According to Alesina and Dollar (2000), motives to give bilateral aid vary largely among donor countries. Former colonies get more aid from their colonizers, and sometimes aid is also tied to the formation of political alliances with former colonial powers. Some countries give aid according to political interests without considering the poverty levels or the social and political situation in the recipient country. Other countries without a past as significant colonial forces, such as the Nordic countries, tend to give aid according to poverty level, quality of the institutional setting and degree of openness to international trade.

Multilateral institutions such as the WB, the IMF and the UN are extensively engaged in constructing development policies for less developed countries. The UN is mostly engaged in humanitarian aid and peacekeeping operations, whereas the WB gives aid and support projects and the IMF give loans and economic advice to countries with unstable finances.

In 2000, the Millennium Development Goals (MDGs) were established. It is a campaign consisting of eight goals, signed by 189 countries, with the objective to halve extreme poverty by 2015. Although the campaign signifies an ever-increasing interest for development and the commitment by almost all countries to help the poorest ones, the goals will not be achieved within the set up time frame (United Nations, 2009).

Multilateral and bilateral aid and other types of assistance are often tied to certain conditions, commonly referred to as conditionality. This type of policy is almost exclusively directed towards the implementation of free-market reforms to open up economies for international trade and other financial activity in the international arena. The general idea is that if countries go through with these reforms, they will be able to reach a higher level of economic growth which is believed to lift these countries out of poverty.

By studying the reforms imposed in developing countries along with the institutional changes that are required by the conditionality, there is a possibility to evaluate the effects. Researchers have been concerned with the effects of these reforms on economic growth, but there is also another side to the issue. If successful, these reforms should have increased the institutional quality where they have been implemented. This is so because economic reform will inevitably require institutional reforms. As will be discussed later in the thesis, there is also reason to believe that institutional performance might cause, or maintain, economic growth rates and induce political and social development. However, there is ambiguity in the literature regarding the validity of reforms imposed by external actors since developing countries often have limited, or no, impact in determining the design of reforms. Therefore, it is highly relevant to study the institutional perspective on reforms and conditionality.

1.1 Aim and Problem

The thesis aims at analyzing the legitimacy of conditional economic reform in economies in crisis. Particularly, the aim is to find out if these conditional reforms, initiated by the international community, have achieved any substantial development in the institutional setting, which is assumed to drive economic growth.

Legitimacy is a central concept in the thesis. It urges us to pose questions regarding objectives and conditions set up by the donor/creditor as well as to examine the perspective of the recipient/credit taker, in which short-term gains have to be weighed against long-term losses or vice versa.

Conditional reform refers here to the event of an International Financial Institution (IFI)[1] promising some kind of economic assistance in exchange for (often) fundamental changes regarding the economic system and institutional environment. The main questions that this thesis will attempt to answer are:

- Is it legitimate to impose external institutional reforms on countries facing economic crisis?
- Is there a difference in degree of legitimacy between countries that have and have not gone through conditional reform?
- Is there any indication of which hypothesis for economic growth is most appropriate in explaining the outcome of this study?

1.2 Method and Design

This thesis will use both quantitative and qualitative methods in order to answer the research questions. The qualitative part will consist of a case study, where three cases are chosen and compared through the use of secondary literature. The quantitative part will consist of statistics that are used to see the direct effects of the institutional reforms discussed later in the thesis. The statistics used are also from secondary sources that are believed to be the most credible available. More specifically, the majority of the statistics (the indices) come from the International Country Risk Guide (ICRG), which is commonly accepted as a serious source for indices on political risk.

The analysis will be based on a conceptual literature study and a case study. The conceptual literature study explores the concept of legitimacy as well as institutional theory, which will be applied to the case studies in order to analyze the results in accordance with the research questions.

The study is of a comparative character. Cases are compared in order to see if there is a difference in the variable subject to analysis (the dependent variable), in this case legitimacy of reform. In order to make use of the comparative study, the cases must show variation in

[1] IFIs will denote the WB and the IMF when referring to them collectively.

the variable that is believed to cause the difference in the dependent variable. Since this study is concerned with conditional reform as the explanation for degree of legitimacy, there must be variation in this variable (Esaiasson, Gilljam, Oscarsson & Wängnerud, 2004). Two categories will be dealt with in this thesis; conditional reform initiated by the IMF and non-conditional reform during the Asian crisis in 1997-1998.

On the other hand, the variable subject to analysis should preferably be as similar as possible for the cases used. This means that the countries should be relatively equal in other variables that may have an effect on the analysis (Esaiasson et al., 2004). Section 4.1 in the thesis provides the description for the selection procedure of the cases.

The empirical part in the thesis also validate the use of the particular countries. The variables examined indicate that at the starting point for the time period, the countries have relatively equal institutional settings (see section 4.5). 1993-2005 is the period used, since the ICRG index is only available to the author up until 2005. 1993 is believed to be a sufficient point in time to start at since it is enough time prior to crisis to understand the development of the indicators used.

It is important to note that using these methods means that the researcher selects and interprets the literature, which may produce biased results. The researcher is always affected by previous knowledge and his or her own philosophical assumptions, which constrains the possibility to take on a purely objective perspective. In this study there has been an attempt to use sources with a wide range to avoid such bias. However, some information is only available through organizations, such as guidelines for the IMF programs. Such information is considered credible, since before being published such information is assumed to be peer reviewed.

When discussing institutional reform, I will not consider reform advocated or included in bilateral agreements between a donor/creditor country and a recipient/loan-taking country. Only multilateral institutions as donors or creditors will be considered. Furthermore, the IMF and the WB will be the institutions discussed. Following the nature of the methodological choice for this study, the geographical constraints are evident. The examined countries are situated in the same geographical area, limiting the possibilities for generalization.

1.3 Disposition

Section two deals with causes of poverty and the institutions that deal with policy reform towards emerging or developing countries. In section three, the concepts of legitimacy and institutional theory will be dealt with. In order to apply the theoretical concepts on reality, section four consists of a comparison of three cases, namely Malaysia, Thailand and Indonesia. In section five, there will be an analysis of the three cases and the theories and concepts of legitimacy will be applied. Section six presents the conclusions for this study, as well as the answer to the research questions.

2 Poverty and the International Financial Institutions

Poverty, and more importantly, the development from poverty towards decent standards of living, is an issue attracting much attention in media, at universities, in political discussions and in many other forums. The WB has set the minimum income level to $2[2] a day and person to cover all necessary expenses such as housing, food, basic clothing, schooling and other basic needs. This means that below this amount of income, referred to as the 'poverty line', one is considered poor. If making less than $1.25 a day, one is extremely poor. The estimate of extreme poverty was revised recently, increasing from only $1. Today, 25% of the developing world is classified as extremely poor (The World Bank, 2009; United Nations, 2009). Many of the international institutions work continuously with the question of how to decrease the widespread poverty. One approach is, and has been, to induce reforms in poor countries.

2.1 The Cause(s) of Poverty

To know how to eradicate poverty, the causes for poverty must also be known. This is one of the main problems today. There is no clear-cut answer to what determines one country to be poor whereas another one is rich. Acemoglu, Johnson and Robinson (2006) note that some of the characteristics for a country with widespread poverty are no well-functioning markets, low education levels and limited physical capital and technology. Two main tracks commonly referred to by scholars, as they attempt to explain failure in sustainable economic growth, are the geography hypothesis and the institutional hypothesis. An additional track, used mainly by IFIs, is the policy hypothesis.

The Geography Hypothesis

This view on causes of poverty holds that the geographical location of a country determines the technology and the incentives of the population. The *climate* might affect the working ability, productivity and incentive structure of each individual. The particular *geography* of a country might affect its trade (if being landlocked) as well as the possibility to establish economies of scale which in turn will affect productivity. Also, people tend to struggle with particular *diseases* that hinder development, mostly in tropical zones. These can be malaria and other infectious diseases (Acemoglu et. al, 2006; Sachs, 2003; Easterly & Levine, 2003). According to this view, economic development will take place when the country has a favorable geographical location. This would imply that humans cannot affect the fundamental causes of poverty.

The Institutional Hypothesis

Many researchers, for example Acemoglu et al. (2006), Rodrik, Subramanian and Trebbi (2004) and Easterly and Levine (2003), have contested the geography hypothesis, and mean that geographical factors induce economic development only through the effects of institutions. Institutions are key in understanding the economic development of a society. This hypothesis argues that some societies have been more successful in building good institutions than others, and therefore they are richer. There is a positive aspect of the institutional hypothesis that is not present in the geography hypothesis, it assumes that humans can change and shape the institutions and lift themselves out of poverty (Acemoglu et. al,

[2] Purchasing Power Parity (PPP) in 2005 USD. PPP equalizes the currencies so that the effects of different price levels are accounted for.

2006). The institutional hypothesis also fits the development of the regions where Europeans settled during the colonization, where the geography hypothesis fails to explain economic development. European colonizers set up extractive institutions in areas that were rich at the time, for example sub-Saharan Africa. The only purpose of these institutions was to facilitate the exploitation of resources, and the colonizers did not have any interest in settling for good in these areas. Institutions has persisted over time, and tend to be of poor quality today. On the contrary, Europeans settled in areas where there was low resource availability, such as North America, and built institutions that were of good quality which has led to the prosperity of these areas today (Acemoglu, Johnson & Robinson, 2005).

The Policy Hypothesis

This view on economic development ignores history as an important factor and stress policies as the fundamental cause of long-run development. Improvement of macroeconomic variables, openness to trade and the abolishment of capital account controls are key for prosperity. This is the standpoint of IFIs such as the IMF and the WB, as will be seen later in this paper. If following the policies advocated by IFIs, developing countries should be able to rise out of poverty (Easterly & Levine, 2003). International trade is the most commonly used variable to explain economic growth in this hypothesis. Rodrik et al. (2004) emphasizes that all international trade should increase economic growth according to this hypothesis, regardless of the institutional arrangements. Frankel and Romer (1999) find that countries more open to international trade also enjoy higher standards of living. These researchers also account for the effects of geography on trade (i.e. being situated far away from large trading countries or being landlocked) and concludes that they contribute to the lack of economic development in countries that are experiencing these geographical traits. This view on economic development has been contested many times, for example by Easterly and Levine (2003) and Rodrik et. al. (2004).

2.2 Strategies to Combat Poverty by the IFIs

As stated in the previous section, the Policy Hypothesis embodies the strategies to combat poverty used by the IFIs, most notably the IMF and the WB. In the end of the 1980s, there was some consensus forming among the international institutions based in Washington D.C. on how to design the development policies. The term *Washington Consensus* originates from John Williamson (1990) and denotes the ten policy areas prescribed for developing countries involved with these institutions at the time. The policy advice was mainly based on the Latin American performance and situation, and streamlined into a framework used for all countries.

The ten policy requirements to fulfill under the Washington Consensus are, as outlined in Williamson (1990):

1. Fiscal Discipline – Countries need to recognize the need to control their fiscal deficits. The deficit is considered undisciplined if there is either high inflation/large payment deficits or large increases in the government debt to the Gross National Product (GNP) ratio.

2. Public Expenditure Priorities – Public spending should be cut back, and redirected to the groups in society that are particularly vulnerable.

3. Tax Reform – The tax system should be simplified and more equal for the entire society. Also, the countries should deal with the problem of, and taxation on, capital flight.

4. Financial Liberalization – Interest rates should be determined by the market and preferential interest rate settings should be abolished.

5. Exchange Rates – Multiple exchange rates should no longer exist, and the exchange rates should be kept at competitive levels to encourage export-led growth.

6. Trade Liberalization – This goes hand in hand with competitive exchange rate as part of a more outward-oriented policy. Reducing tariffs, abolishing import licences and facilitating the imports of goods needed for production are key for trade liberalization.

7. Foreign Direct Investment (FDI) – Allowing foreign capital and investments to enter into the country instead of refusing it. FDI is considered a source of technology improvement and increases in human capital.

8. Privatization – Government-owned firms should be sold out to private interests in order to make the firms more competitive and efficient.

9. Deregulation – Since the United States efficiently deregulated industries which were previously monopolies of the state such as airlines, telecommunications and other natural monopolies, the general belief is that such deregulation should be promoted.

10. Property Rights – A basic requirement for a capitalist system, which protects individuals from losing their property on arbitrary grounds.

These are the ten requirements that were needed to be fulfilled for a country seeking loans or grants at the IMF and the WB. The policy advice from these IFIs is similar today, only extended to include more institutional features. Here we can see that property rights is essentially the only institutional variable. The evolvement of the development policies by the IMF and the WB will be outlined in the next section (2.3).

The IMF and the WB are complementary institutions, both created at the Bretton Woods conference in 1944. The main goal for the IMF is to monitor the global, regional and national macroeconomic climate and the institution operates through technical assistance, policy advice and loans. The loans, which are of primary interest in this study since they are conditioned upon policy reform, are short-term to medium-term in length, monitored by a staff of mainly (macro)economists. The IMF only operates through governments in contrast to the WB that invests in, or lends to, projects, notably to strengthen quality of infrastructure, education, health care and other social goals. Technical assistance is also an important service. The WB has two different lending divisions depending on the poverty level of the country in need of financing, but it never competes with other interests in a project. Therefore it only operates where there is no other way to obtain financing. The two institutions are complementary and sometimes overlapping. They work closely together since the success of projects is often dependent upon macroeconomic conditions (IMF, 2009a).

2.3 After the Washington Consensus

The reforms advocated by the IMF and the WB are usually called *structural reforms* or *structural adjustments*. Structural reforms are often extensive since they aim at improving many variables at the same time. Following the Washington Consensus, the reforms are often shocks in the economies where they are implemented, since all or most of the policy points have to be considered. A particularly important objective when starting with the structural reforms was to finance imports to developing countries through the free-market adjustments that characterized the Washington Consensus. The most important actor in promoting these reforms was the IMF. However, the WB was also involved since large-scale reforms were expected to increase the productivity of individual projects. The evidence on these kinds of structural reforms is not convincing. Many countries received well over 20 structural adjustment loans and still had negative, or zero, growth rates (Easterly, 2006).

The apparent lack of success when performing structural reforms has been admitted by the IMF. The institution explained that this was probably due to the exclusion of governance issues in the reform requirement. Also, the institutional settings in the countries that borrowed were unsatisfactory for macroeconomic improvement to work (Taylor, 2004).

As a consequence, the IFIs have included governmental aspects such as targeting and eliminating corruption in the policy advice. The notion of *good governance* has been frequently used, both in the literature on conditionality and by the IFIs themselves. When explicitly addressing issues of governance, the IMF is operating outside its mandate. In the guidelines for IMF involvement in governance issues, it is clear that there should be no interference in the domestic or foreign policy of any member country. However, the IMF can address the authority of a specific country if poor governance is identified in the macroeconomic fields where the institution operates in principal (IMF, 1997).

The critique of such policy intervention has been heavy. In 2006, the 193 developing countries in the world held slightly less than 20% of the voting rights in the IMF. 24 industrialized countries have approximately 60% of the votes (the U.S. have 17% of these) although their need to borrow from the IMF is considered minimal. 20 emerging countries together hold 20% of the voting share, although it is not very likely that all these countries will have to borrow again (Truman, 2006). This skewness in the decision-making mechanism has lead critics to accuse the IFIs of implementing 'western', and especially U.S. policies on developing countries. Another target of critique is the inflexibility in policy-making and the failure to recognize that policies and reforms that have been successful in the west may not be applicable or appropriate in other parts of the world (Phillips, 2006; Martin, 2006; Beeson & Robison, 2000). The inflexibility in policy implementation and the requirements from the IFIs that differs little from case to case is labeled *monocropping* by Evans (2004). Such methods to reform public institutions in developing countries are not considered effective since they seldom succeed in reforming underlying practices within institutions such as how the operations are undertaken. It is also questionable if all countries necessarily need the same institutions in order to reach a stronger standing in the global economy. Evans (2004) compares the global political economy's constitution with an investment portfolio; it is better to spread risk by diversifying investments. By being made up by diverse institutional settings, the global world might be better equipped when facing crisis.

An IMF loan or any interference from the IFIs is in theory entirely voluntary. However, in reality, a country is often near desperation when turning to the IFIs. Other sources of financing are usually not possible to find, and this is also a precondition for the involvement of the WB. This puts the individual country in a particularly vulnerable position. The IFIs will require specific policy changes that not necessarily have public support. For example, less developed countries with debts might try to solve liquidity problems by printing more money which in turn will lead to imbalance in the macroeconomic system. Inflation will, as a consequence, rise rapidly and the country face crisis. The country has the possibility to turn to the IMF to receive assistance in constructing a plan on how to repay debts without printing more money, perhaps by taking an IMF loan. In a situation like this, government spending must be cut in order to decrease inflation and deficits. Here, the IMF starts to interfere in domestic politics, since the government will be advised or forced, to comply with policies that have no public support (Easterly, 2006).

In 1999, the IMF and the WB jointly launched a new strategy; called the *Poverty Reduction Strategy Paper (PRSP)* where poverty and economic growth are issues specifically addressed. If a government is seeking financial assistance from the IFIs, it has to describe in a PRSP what the loans will be used for. This means that the IFIs are no longer explicitly stating the conditions for the loan, instead the domestic government has to do so (IMF, 2009b). However, the PRSP will not be accepted if not satisfactory, hence the element of conditionality is still present, although more hidden. According to Easterly (2006), there is little difference between this method and the previous, where the IFIs initially stated the conditions. If the PRSP is satisfactory, the loan will be given under the *Poverty Reduction and Growth Facility (PRGF)*. This facility demands the inclusion of civil society and other development agents as well as the promotion of good governance. Despite the fact that PRGF has been operative for ten years loan-takers are still facing problems in reaching any significant level of growth. This is admitted by the IMF, although the institution claims that macroeconomic stability has improved in many countries (IMF, 2009b). The IMF is currently aspiring to introduce a new financial lending instrument, called the *Poverty Reduction and Growth Trust*, and to have it approved by its donor countries. This new facility will be more adjusted to fit the needs of the poor borrowers in terms of recognizing that there are different needs among countries. As a consequence, there will be more flexibility in policy-making (IMF 2009c).

Easterly (2006) argues that one major problem with development policies today is the lack of accountability in the field. There is no market-like function where the customers will let the supplier know if the delivery of the product is unsatisfactory by not purchasing it again or returning it. When suppliers are responsible for the product, they will suffer, or go out of business if the product does not keep its promise. In the same sense, the poor must be able to give feedback to aid agencies and projects, and to creditors. There is a major need for input from the affected group of people. Today, the IFIs are not accountable to the poor to this extent, but rather to their donors. Money must be spent in a way that satisfies the donors, and therefore there are many projects and reforms pushed onto poor countries, even though it might be too much for them to handle. Poor countries might not have resources to report back to the IFIs, or to monitor different projects and continue with reform implementation. Also, if many different projects and both IFIs and NGOs operate in the same area, it is impossible to say who or which agency is responsible for successful and failed projects. Therefore, it makes it harder to distinguish which approaches that work and which do not.

2.4 Summary

The main hypotheses used by scholars to explain economic growth are the geography hypothesis, the institutional hypothesis and the policy hypothesis. The geography hypothesis can be accounted for by examining countries in the same geographical area and so can also the institutional hypothesis through the use of both economic and institutional indicators. The policy hypothesis can be tested by including countries that went through with different policy reforms.

The IFIs commonly advocate macro-economic stability and free-market reforms, and in order for loans to be disbursed or projects to be started, the IFIs often demand policy reform. This is particularly evident when countries face economic, financial or political crisis and have limited possibilities to find financing elsewhere. The policy recommendations were stated initially in the Washington Consensus and they have been target of much critique since they were implemented. Common critique include the inability to recognize that not all countries may be suitable for 'western' policy frameworks and that the policy requirements are stipulated on western criteria, and in particular formed by the U.S. Increasingly, the IFIs have started to include institutional variables on a more fundamental level in the countries where they operate, such as targeting corruption and implementing good governance. Also, new measures, such as the PRSP has been implemented to allow countries to form the policy choices themselves. However, the country filing such paper must still conform with the general agenda of the IFIs and also include other targets such as including civil society in development policies. The main goal of the reforms is to eradicate poverty by enhancing economic growth. This goal has not been reached to any significant extent since the IFIs started these operations. Also, it is questionable if a uniform institutional environment is desired from a global perspective.

3 Legitimacy and Institutions

This section will be devoted to defining legitimacy as a concept, and give an account of several institutional theories. Legitimacy is explained in terms of how governments earn the legitimate right to exercise power over its people. Along with the definition of institutions, there will be an outlining of institutional theory and institutional development by three different theorists. This is to provide an understanding of the factors that cause institutions to develop and which functions institutions have in today's society. In section five, there will be an analysis concerning the effects institutional reform has had on the countries included in the case study and these concepts will be used to determine if IFI action has been legitimate or not.

3.1 Legitimacy

Legitimacy is a concept that comes with diverse definitions, some wider and some narrower. Perhaps even less clear is how to measure legitimacy, and if it is even measurable. In this section an attempt is made to outline the definitions by different authors to reach a point where it can be possible to form a general perception of what legitimacy can be and how it can be measured or approximated.

3.1.1 The Origin of the Concept of Legitimacy – Max Weber

Max Weber coined the three classical types of legitimate authority: *charismatic, traditional* and *legal-rational*. The legitimacy of charismatic authority stems from one individual who is extremely charismatic and who is the fundament of the political system, the most well-known case being Adolf Hitler in Germany. Traditional authority is legitimate through the belief that authority is inherited or deserved because of tradition. Emperors, kings and sultans would fall into this category if their right is divine or comes from traditional sources. Legal-rational legitimate authority comes from legal rules and bureaucratic procedures. The majority of people ruled must believe that the rules are appropriate, and when someone is assigned to govern others, he or she is superior. However, even the superior is subject to rules that constrain his or her possibility to act within the boundaries of government. This is due to natural law, which is the rational principle for political constraints, where all men are considered equals. Moreover, natural law is the norms that remain in place regardless of political authority (Friedman, 1981). In the modern state these could be freedom of speech, freedom of contract (safeguarding property rights), human rights and freedom of religion.

Friedman (1981) elaborates on how western states managed to legitimize the modern welfare state, where the state has the legitimate right to redistribute wealth. It is, at least at a first glance, remarkable that the legitimating of the state as a redistributor of such magnitude was institutionalized after the WWII, when the condition of many western states was fragile. The time before WWII was much colored by liberal thoughts, so the imposition of welfare states may be considered a real controversy during that time. The mere existence of welfare states contradicts the pure free-market view, where the allocation of goods and services would be a consequence of free markets[3]. In contrast, the welfare state takes on much of the responsibility to deliver welfare services to the citizens, in a sense protecting them from pure market forces. In the attempt to explain how welfare states succeeded in manifesting their existence, Friedman states that since natural law considers all individuals as

[3] Through the 'invisible' hand, coined by Adam Smith in 1776 in the book *An Inquiry into the Nature and Causes of the Wealth of Nations.*

equals, redistribution is legitimate when it is made impartially. This is so since the government's ultimate responsibility is to protect its citizens, which is done for example through guaranteeing a minimal standard of living and providing health care and education.

3.1.2 Using Weber's Concept Today – Mattei Dogan

As mentioned, legitimacy is considered a belief and especially so since democratic governments entered the political arena. "If people hold the belief that existing institutions are appropriate or morally proper, then those institutions are legitimate" (Dogan, 2004:110). This quotation represents the general idea of legitimate political institutions and governments today, but there are also other definitions. The concept of legitimacy is more important in a democracy than in an autocracy since democracies are based upon the support by the majority. However, it is an advantage also for autocratic regimes to adopt such institutions that enjoy legitimacy (Dogan, 2004).

There are four roughly distinguishable types of legitimacy derived from the last feature of Max Weber's definitions, the legal-rational-bureaucratic. In today's society this is the only out of the three original types of legitimacy that is still applicable:

1. In pluralist democracies where authority is based on the people, there is basically full legitimacy.

2. In authoritarian bureaucratic systems the regime receives some legitimacy from some part of the population. In these systems, civil rights are partly respected and the rulers are civilian.

3. Dictators, tyrants and totalitarian regimes fall into this category. The regime is not accepted by the majority, even though it is not publicly shown. Here, the number of coups d'état can be used as an approximate estimate for lack of legitimacy. However, only because there is no revolt, this does not mean that a regime is legitimate.

4. In this category regimes are neither accepted, nor rejected. People are so extremely poor that it does not matter who is ruling, because poverty is not assigned as the consequence of the regime, but rather to a god or to forces of nature. In this case, there is no need to talk about legitimacy.

According to Dogan (2004) there are many nations falling outside the Weberian type of legitimacy, and therefore the concept needs to be updated. It is commonly accepted that legitimacy can be derived from majority support. However, it is difficult to measure majority support directly. The type of support should be known; strong and intense support is clearly more legitimate than passive support. These variables are hard to measure, and therefore other variables are needed. If there is low legitimacy, there should also be a high degree of coercion. Essentially, this means that if people are consenting to a decision, they are doing it out of fear, or being coerced to do so, when there is low legitimacy. This can be measured by two indicators: absence (or degree of) political rights and absence of civil liberties. These are based on a number of governmental variables such as freedom of expression, fair elections and independent judicial institutions. An additional possibility is to measure degree of corruption, since corruption is the most vital symptom of illegitimacy of an institution. If there is high corruption in the institutional system, including the judicial one, we could eventually expect a breakdown of this particular institutional setting as a consequence of a legitimacy crisis (Dogan, 2004).

3.1.3 Adding to the Concept of Legitimacy – David Beetham

David Beetham (1991) adds to the concept of legitimacy as a mere belief by the governed, which has been the argumentation by Weber, to include more specific characteristics that need to be fulfilled. Only believing in the legitimacy of a current power system is not sufficient, since beliefs are easily influenced by public relations and propaganda. True legitimacy cannot be derived, according to Beetham, from the fact that the one(s) governing have succeeded in convincing the governed that the power exercised is legitimate. Power is legitimate when it fulfills the three following levels that are qualitatively different from each other:

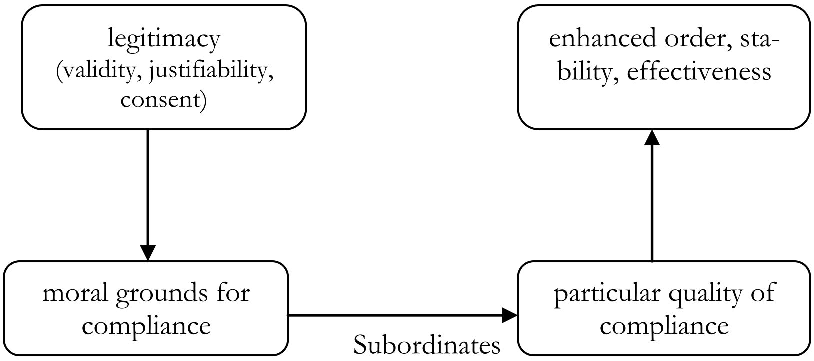
1. Rules are the basic level of legitimacy. In this first step of legitimacy, power needs to be obtained in conformity with existing rules, and also employed according to the established rules. It is important to note that rules are not necessarily the written law, even if it is often the case, they could also be non-written and informal (discussed further in section 3.2).

2. In turn, there is a need to legitimize the very rules that the power is exercised through. Therefore, the governing and the governed must necessarily share the belief that rules are justified. Power has to come from a valid source and the governing must have the appropriate qualities to perform their tasks. The structure of how power is used must be of such kind that it serves the general interest and not a specific group of people. As is obvious, these qualities of government can vary with different societal contexts, and it is not evident to which degree these qualities have to be fulfilled.

3. As a validation of the legitimacy, the governed must express consent in some way. By expressing consent, there will be a moral element introduced in the power relation, creating a commitment. The concept of consent to government can vary with culture, but it needs to be demonstrated by the governed through some manifestation (can be thought of as a ceremonial element), to show third parties that the authority enjoys legitimacy. Manifestations by the powerful themselves (propaganda) is not a feature that is considered legitimate. The governed should voluntarily and freely express their consent. Therefore, the opposite (public manifestation, passive resistance or civil disobedience) by the people that are eligible to give consent is considered the retraction of legitimacy (Beetham, 1991).

The above three levels of legitimate power are a framework for how to evaluate the existing, or lacking, legitimacy. The historical context, the culture and the type of society needs to be considered as well, since the three levels of legitimacy can produce various types of governing-governed relations.

Figure 3.1: Characteristics of a Power System or Relationship



Source: Beetham, 1991:34

Beetham (1991) discusses ways that power can be sustained but not necessarily in a legitimate manner. Legitimacy requires obedience by the subordinates, which is done voluntarily if power is legitimate even if the governed not always agree on all decisions. However, without legitimacy, power can be sustained through increasing coercion in order for the governed to comply, although such coercion is costly to maintain. As a consequence, the government only succeeds in maintaining office, but not in achieving other goals. Beetham illustrates this by using Eastern Europe as an example; economic reforms failed because the regimes suffered lack of legitimacy to demand short-term economic adjustments. Legitimacy can therefore be seen as a prerequisite for quality of policy outcomes and degree of cooperation, as can be seen from figure 3.1. If the governed assigns legitimacy to the governing, the legitimacy is built upon solid moral grounds that justify compliance. In consequence, the governed will comply in a way that ensures that the governing can provide better services to the subordinates.

3.2 New Institutionalism

Institutions can be seen as the very basis of studies in political science, however institutionalism has been neglected in favor of more individualistic approaches during a large part of the second half of the 20th century. The individual was seen as autonomous when making choices, and not really influenced by either informal or formal institutions (Peters, 2005). However, since the 1980s there has been more attention directed towards the belief that institutions are important for the political process.

New institutionalism differs from old institutionalism in the sense that it has relaxed the assumptions about institutions. In the old version, institutions are often seen as formal where generally the formal aspects of government and the law is the area of study (March and Olsen, 2006; Peters, 2005). In this view, the old approach to institutions and political life was perhaps too narrow, which might have led to the abandonment of it. New institutionalism assumes that institutions will affect political activity in all circumstances; even if the institution in itself did not directly cause the public policy (March and Olsen, 2006). The institutional theories in this section are chosen because of the belief that institutions evolve organically, affected by the surroundings and not because they are 'just there', as other theoretical tracks in this field might suggest.

3.2.1 North's Institutional Theory

Douglass C. North is a widely used author, and a Nobel Laureate in 1993, in the field of connecting institutions and economics. His theory on institutions is used mainly in explaining why some countries fail to develop economic growth, and thereby not rising out of poverty.

"Institutions are the rules of the game of society or, more formally, are the humanly devised constraints that shape human interaction" (North, 1990:3). Understanding institutions and institutional change is thereby important in grasping historical change, human exchange and economic performance.

When defining institutions according to North (1990), one can outline two sub-sets; informal and formal institutions. Informal institutions are the norms and codes of behavior in a societal context, whereas formal institutions are laws, regulations and rights. Informal institutions are the basis of formal institutions and they are a part of the culture. For example, laws often start off as norms in a society, to eventually evolve into formal constraints, adopted in printed form in the judicial systems. Hodgson (2006) clarifies that institutions can be constitutions, money, and language and so on. Institutions are the instances through which we can predict the behavior of others. Institutions constrain actions, in the obvious case through laws and regulations, but also through the norms in a society that shape what we as humans think is acceptable and not, right and wrong, and so on. However, this does not mean that institutions automatically decrease freedom. Institutions usually enable humans to pursue with actions and make choices that are not possible without institutions, such as communicating with others through the rules of language.

When discussing institutions and behavior in them, it is important to mention the notion of rules. "Rules include norms of behavior and social conventions as well as legal rules", and they are to some extent constrained by nature's law (Hodgson, 2006:3). Rules are not needed when there is only one possible outcome, but when multiple possible outcomes, rules with help make the choice between them. Rules are very contingent on culture and usually we follow rules without considering it, as in the case of using a system of money (Hodgson, 2006).

It is possible to make a distinction between rule and law. A law is formal, written down and may impose sanctions if broken. However, if the law is not successfully incorporated in customs and norms in a society, it is not a rule. An ignored law has not reached the place in society where it is customary and norm-breaking to violate it, and therefore it is not truly legitimate (Hodgson, 2006).

The purpose and the role of institutions are to reduce the uncertainty that is involved in any transaction between humans. By adopting a structured way to act and behave, there can be predictability and stability in the exchange between two or more parties. In economic terms this exchange is called transaction cost, and it will be remarkably lowered when institutions function efficiently. In reality, however, there is no guarantee that institutions function efficiently. What makes institutional theory of economic exchange different from other forms of economic theory is the fact that institutional theory can explain why inefficient exchange exist and why markets and agents do not self-correct when there is inefficiency present. In order for institutions to progress and develop, time is an important variable. Over time, institutions can learn how to be efficient, altough this might occur very slowly (North, 1990).

Informal rules and constraints generally change slowly, whereas formal rules can change quickly, for example through a reform. Formal rules can also act as a support to informal rules, in the sense of reducing the costs of exchange. If different groups in society have relatively even bargaining power in political decisions, the formal rules will tend to reflect more complicated ways of exchange. If there are few groups with bargaining power, the formal rules might be more directed towards benefitting only this small fraction of society. This would in turn mean that the formal rules of exchange are relatively non-complex. A society is constructed in such a way that the formal rules that build the very basis of society, such as the constitution, are much more difficult to alter than for example the formal rules of a written contract (North, 1990).

A critique that has often been highlighted when discussing institutional theory by North is his neglecting of organizations as institutions. North does not explicitly state that organizations are not institutions, but in his theory he reduces them to players in the institutions. If organizations are to be treated this way, the social structures, norms of behavior and other internal mechanisms within the organizations are ignored. Therefore it is important to stress that organizations are also institutions, although they can be reduced to a united player if we are not interested in the decision-making structure within it. For example, a nation can be treated as a united actor in a global institutional setting, although it is evidently made up by many different parts and have extremely complex decision-making procedures internally (Hodgson, 2006).

3.2.2 Ostrom's Theory of Institutions and Institutional Change

Elinor Ostrom, Nobel Prize Laureate in Economics in 2009, is concerned with economic governance, particularly governance of natural resources. Although it is a very specific field of research, there are lessons to be learned about institutions and institutional change. She contests the theories on collective action that indicates that there must be an external actor to implement institutional change in governance (Ostrom, 1990).

Institutions are defined as: "[...] the prescriptions that humans use to organize all forms of repetitive and structured interactions including those within families [...] and governments at all scales. Individuals interacting within rule-structured situations face choices regarding the actions and strategies they take, leading to consequences for themselves and for others" (Ostrom, 2005:3).

Rules are, of course, a central concept of the institutional understanding. The stability of rules is dependent on the enforcement possibilities and the monitoring associated with certain rules. Also, if rules are loosely maintained, predictability of an institution will decrease. A stable institutional climate is therefore highly dependent on the establishment, enforcement and monitoring of rules. If this is not done in a sufficient way, the real outcome may be very different from the predicted outcome (Ostrom, 2005).

Broadly speaking, there are three sets of rules; *operational rules, collective-choice rules* and *constitutional-choice rules*. Operational rules affect the daily decisions made in an institutional setting by the members, and are the easiest to change. Collective-choice rules are used to decide who can participate in the operational rule-setting and which rules to use when changing the operational activity. Collective-choice rules change much slower than operational rules and in turn constitutional-choice rules change at the slowest speed. Constitutional-choice rules affect both other types; first they affect collective-choice through participation decisions and in determining which rules to use to change collective-choice rules and they affect operational rules through the changes in collective-choice rules (Ostrom, 2005). This indicates that rules made at higher levels of decision-making have impacts on rules at lower levels as well and may well affect the everyday life of ordinary citizens. It is not possible to change macro-level rules without changing at the micro-level as well, which must be considered when dealing with reform of government policies.

As was seen when discussing North (1990), norms are also an important feature of institutional theory and change. Ostrom (2005) states that in changing an institution, norms may be more or less important. This depends on how strong the norm is and how much it can prohibit or allow a specific behavior. If an actor does not follow through with an action that is beneficial to him because of norms, the norms can be considered strong. If rules are not enforced efficiently and norms are weak, agreements among actors may be disrupted and instability will follow in the institutional system or the marketplace. This could be due to that those actors who benefit from norm-breaking and predatory behavior will also act in that way, which could distort the environment quickly.

Rules that are implemented in a specific institutional setting are unlikely to reach legitimate status if they are forced onto the individuals within the institution, since it is unlikely that norms will be developed to prohibit breaking the rules. Breaking the rules may on the other hand be rewarded, and therefore norms may be developed in favor of violation of rules. If rules are illegitimate it becomes very costly to monitor and enforce the rules up to the point needed, where rules are followed because the risk of being punished is high enough (Ostrom, 2005).

Ostrom's theory of institutions and institutional change is one where external implementation is regarded as insufficient to obtain legitimacy for decisions and reform. It is always better if the participants are included in the decision-making process, since they will be affected by the process. If participants are not included, elites may take advantage and form policies that are beneficial to only a small part of society. Also, policies such as property rights are expected to be more beneficial and effective when they are formed by non-external decision-makers. According to Ostrom (1990) institutional equilibrium will be reached when an institutional change has occurred and follow the path of a pre-determined plan.

3.2.3 Sen on Institutions

Amartya Sen, Nobel Prize Laureate in Economics in 1998, focuses on how institutions can help develop the human capabilities and the freedoms associated with them. These freedoms are the engines of development and therefore, there is a need to go beyond economic indicators alone to determine the development of a country or a region. Development should lead to that humans can lead the life that is most valuable to them, where economic development can be one of the means which we use to reach a higher end, and not necessarily an end in itself (Sen, 1999).

Political freedom is associated with democracy in its widest terms. It gives people the right to, for example: decide who should govern, on what terms, chose between different political parties, openly criticize parties and politicians and have a free press. *Economic facilities* mean that people should have the opportunity to consume, produce and trade which of course depends on markets, prices and other conditions of exchange. Distributional concerns of economic resources are important. *Social opportunities* affect the way people can enjoy their life through education and health, but also the way they can participate in other spheres of society. *Transparency guarantees* involve the trust that all societal activity is based upon. A transparent society, where information is disclosed and openly debated, should be less corrupt and have less possibilities for financial irresponsibility than non-transparent ones. *Protective security* is a measure that hinders people to fall into misery when they face some kind of crisis for example, usually referred to as social safety nets (Sen, 1999).

Sen (2009) questions the reliance on market economies and capitalism that is often the basis for analysis and recommendations issued by theorists and IFIs. Already in the 18^{th} century when Adam Smith was active, it was clear that even though self-interest is a mechanism driving trade, the fundament lies in mutual trust among the trading partners. Trust is essential in the exchange process; only if the customer trust the supplier to supply the goods and services promised, and the supplier trust the customer to pay for them, will the exchange take place. Institutions are the arenas that allow such activity to take place.

Furthermore, Sen (1999) states that when determining the development of a particular country, it is not sufficient to only analyze the economic growth rates. Rather, we should look at institutional variables that can be developed with the help of economic growth. After all, it does not matter if a country increases economic growth if the people cannot benefit from it, through for example increased quality of education and health care services. Increasing the accessibility of fundamental institutions, such as the aforementioned, provides the possibility to better profit from economic progress. It will allow people to participate more readily in economic, political and social activities of society that eventually leads to high rates of development. This view contests the mainstream development theories where development is generally seen as a consequence of economic progress. Sen, on the other hand, means that social goals can be fulfilled first even though the country is still very poor. This provides the country with the necessary skills to rise from poverty by itself.

By allowing a diversity of institutions to evolve, with regulations and services appropriate for where they are built "[...] we would be following rather than departing from the agenda of reform that Smith outlined as he both defended and criticized capitalism." (Sen, 2009:5). Therefore, we also need to recognize the different values and norms, which are not uniform, making up the institutional setting. By bringing up such subjects in public forums and discuss them deliberately, the chances for acquiring the most beneficial institutions will increase. Public policy implementation should be a consequence of the socially accepted norms and values and also an outcome of public debate (Sen, 1999).

3.3 Summary

The different concepts of legitimacy share a basic feature. They are all based on a common belief by the people governed that the government has legitimate right to exercise power over them. If a regime is not legitimate, the people may be forced to consent to decisions, or risk being ignored in policy making. Coercion can be approximated by absence (or degree of) political rights and absence of civil liberties. Such non-legitimate power exercise will lead to corruption, which according to Dogan (2004) is the most vital sign of illegitimacy. Beetham (1991) adds to the concept and states that since beliefs are easily influenced, the legitimate right to power should be obtained according to the rules set up by society, it should be exercised by people that have the right qualities to do so and power should benefit society as an entity, not only specific groups. The governed must also show their consent. If the political power is obtained in a legitimate way, the specific reforms required by the government will be followed and carried through more effectively with higher quality than otherwise, since legitimate power can demand some sacrifices by the governed people.

Institutions can be thought of as the instances that reduce transaction costs by making it possible to predict the behavior of others. They can be both informal (values, norms, culture) and formal (regulations, laws). It is evident from institutional theory that formal rules can change quickly but need the support of informal rules in order to be sustained in a longer run. This means that all reforms need to be accompanied by informal institutions that validates the new, or changed, institutions. The legitimacy of an institution can therefore be considered low when the informal parts of the institutional change does not follow a formal alteration, since the people working within it may not consider the formal rule appropriate. This naturally creates problem when carrying out reforms, since the outcome may not be so similar to what is expected. An illegitimate institution is also very costly to monitor, since the cost of enforcing the new policy is high. Institutions will always be more effective and legitimate when formed from 'within', i.e. without external forces. This leads to the conclusion that institutions are diverse, and that they should ideally be formed according to the norms and values that are underlying the social, political and economic structure of where they operate.

It is possible to see certain differences among the theorists presented previously in this section. North differs from Ostrom and Sen in the sense that North allows for the element of learning, which indicates that external implementation of governance reform is not necessarily hindering development. Ostrom and Sen, on the other hand, state that institutional diversity is desirable, and that external reform will impede development in a specific environment. The quality will also be higher if governance reform stems from internal decision-making.

4 The Asian Crisis and IFI response

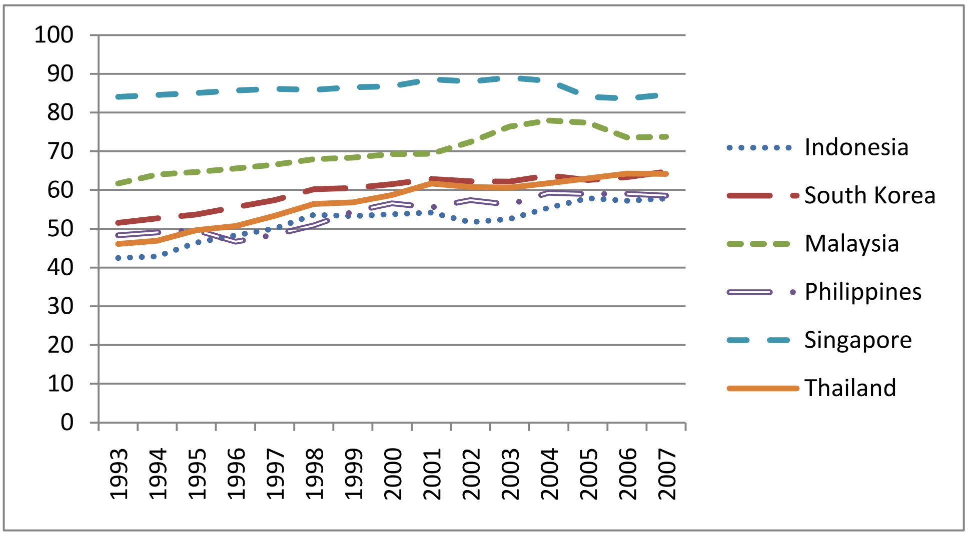
In this section, there will first be an explanation for the selection procedure for the countries subject to analysis. The policy response from the three countries will be outlined, followed by the institutional development before, during and after crisis.

4.1 Country Selection

The cases are chosen firstly on the basis that they all went through the same crisis, in this case the Asian crisis in 1997 – 1998. Secondly, they are chosen according to how they are situated geographically since close geographical location is believed by the author to indicate that the cases share some basic similarities regarding culture, values and norms. However, differences will always persist. In the current study Malaysia, Thailand and Indonesia are chosen for analysis although differences regarding religion exists. These types of differences would become even more evident as other countries outside the region are considered. There has also been a third selection based on certain variables connected to economic performance and state of development

As can be seen from graph 4.1, Malaysia, Indonesia and Thailand have fairly equal levels of globalization. The KOF Index of Globalization measures globalization in three sub-groups; economic globalization, social globalization and political globalization, and is updated annually (Dreher, 2006). The geographical selection eliminates South Korea since it is located far away from the other countries. As seen by the graph 4.1, Singapore experiences much more integration in the global economy than the rest of the countries. The countries left are Malaysia, Thailand, Indonesia and the Philippines. Malaysia needs to be included in order for one country to not have gone through with conditional reform.

Graph 4.1: Globalization Index 1993-2007



Source: Created by author based on Dreher (2006)

Following the methodological choice for this study, three countries in the same area of the world that went through the same crisis will be compared, two that got IMF assistance and one that did not turn to the IMF. The choice for the latter is Malaysia, a country that did not ask for IMF involvement. For the sake of choosing the most similar cases, the policy response used by Malaysia will be outlined, together with the IMF-induced reforms in Thailand and Indonesia. The reason for only including these two alternatives is that they are commonly referred to as the second-tier Newly Industrialized Economies (NIEs), where economic performance has been relatively equal prior to the crisis (Beeson & Robison, 2000). All of the countries experienced negative economic growth rates as a response to the crisis (Winters, 2000). The choice of these countries is also validated by previous research such as Kaplan and Rodrik (2001).

Later in this section (4.5) there will be an outlining of some institutional and economic variables and the development of them before, during and after the Asian crisis. The immediate effects as well as longer term effects will be examined in order to see if there is a difference between the countries, which will later be analyzed in section five.

In 1997, the Asian crisis started in Thailand as a currency crisis, and spread to Malaysia, Indonesia and the Philippines where currencies fell drastically, and later to other Asian countries. There were many reasons to why the crisis occurred, both micro- and macroeconomic such as foreign debt, overinvestment, and weak financial institutions (Sang Lee & Suh Park, 2000; Sharma, 2003). The crisis led to severe contractions of the affected Asian economies' Gross Domestic Product (GDP), and as a consequence unemployment and inflation rates were rising. Because of lacking social and economic safety nets, many people fell into poverty due to the crisis (Sharma, 2003).

The East Asian economies have been successful in reaching high levels of economic growth in a short period of time before the crisis set in, driven by a completely different kind of capitalism than in Western states. In East Asia, the state is an important actor in their version of a capitalistic society and the general belief is that the state should be participating extensively. This is in essence contradictory to what the IMF prescribes for the reform programs (Beeson & Robison, 2000).

4.2 Thailand

Thailand was the country where the crisis originated due to a combination of factors leading to that growth in exports fell to zero, thereby increasing the current account deficit. The currency depreciated heavily as a consequence and this crisis spread to other countries, with varying effects. Thailand had previously opened up the economy to foreign participation, with essential financial liberalization, and free movement of capital was allowed. This caused the other countries in the region with similar policy choices to also be deeply dragged into the crisis, whereas countries like China and India with capital controls did not experience the same contagion. The reason for Thailand to be especially sensitive to a currency crisis was the heavy reliance on short-term debt and its growing importance relative to the stock of reserves (Corden, 2007).

Thailand turned to the IMF for financial assistance and promised to commit to the reforms conditioned in the reform package. Domestic resistance to the rescue package was evident, but the Thai government was eager to keep IMF and the West content. The reforms required by IMF were advocated in order for Thailand to restore confidence in the economy. This was done mainly by enhancing the position of the private sector and by allowing more FDI and external participation in the economy. Thailand was also obliged to tighten the monetary policy, increase social safety nets and restructure the financial system. The government announced that satisfying the international community and its investors was the most important task to fulfill in order to restore confidence, and to do that the business system in Thailand was supposed to conform to international standards. This also included addressing corruption, transparency and deregulation measures (Hewison, 2000).

4.3 Malaysia

The Malaysian business climate has been marked by preferential relations among business leaders and the prime minister, which has made the imposition of good governance measures inadequate. Business leaders tend to be closely involved in shaping political decisions, and the political environment is often considered as lacking transparency (Teik, 2000).

In 1997, the Malaysian currency reached its lowest level ever compared to the U.S. dollar. Malaysia had a seemingly balanced macroeconomic climate and had induced financial liberalization, as advocated by most IFIs in general. However, there had been too much liberalization, causing financial sector investments (short-term investments) to dominate instead of investments in traditional sectors such as agriculture and manufacturing, which in turn caused huge current account deficits (Jomo, 1998). When the currency crisis set in, foreign capital was withdrawn, leaving the country with large foreign debts and no tangible investments. Instead of turning to the IMF, the Malaysian government dealt with the crisis without external assistance (Teik, 2000).

The Malaysian prime minister at the time insisted that the currency crisis was a product of the international financial climate which harmed weak economies since they were defenseless against speculations and exchange rate volatility. The majority of the actors in the international financial system argued that the crisis was due to the resistance to implement free market reforms in the affected countries (Teik, 2000).

However, as an initial policy response in 1997, the country announced raised interest rates and drastic decreases in government spending, in line with the policies of IMF. Also, there were signals that a flexible exchange rate regime would be adopted and that there was not going to be any capital controls. The IMF-like policies failed and there was not much sign of economic recovery. Malaysia introduced capital controls, fixed exchange rate, cut interest rates, and introduced a policy of reflation[4] in September of 1998. Because of the economy's reliance on FDI, such investments were not included in the capital controls. The changes of policy also reflected domestic political tensions, which generally is seen as risky for international investors and further induces uncertainty about the economy. The latter policy choice met heavy critique, especially since much of the Western world believes strongly in the neo-liberal policies promoted by the IMF. It turned out, however, that Malaysia recovered fast from the crisis (Kaplan & Rodrik, 2001).

Although the popular promotion of IMF reform for developing or emerging countries facing crisis, Malaysia showed that it is not a measure pre-conditioned for success. Teik (2000) argues that one of the reasons that Malaysia managed to step out of the crisis is because of the strong political fundament that was associated with the prime minister at the time. Even though not exercising *good governance* according to western standards, the government managed to keep ethnic tensions to a minimum during the crisis. The government did not explicitly set goals for minimizing ethnic tension other than attaining more equality in income distribution for different minorities. Despite no other policy regarding this, Malaysia managed to decrease poverty and even out the possibilities at hand for different groups in society, along with other societal progress.

[4] Reflation is a fiscal or monetary policy used to expand a country's output through lowering taxes, change money supply or decrease interest rates (Investopedia, 2010)

4.4 Indonesia

Prior to the crisis, Indonesia had started to liberalize markets and allow more foreign participation. Private participation was also increasing at a steady pace, and these factors were seen as positive by the WB and IMF. Since law and sound regulations were not following the liberalization, the new market opportunities were exploited by private interests who tried to reach monopoly situations where there had previously been state monopolies. These monopolies were not surprisingly seized by people close to the president (Robison & Rosser, 2000).

The Indonesian currency dropped 80% in value during a few months, which struck the economy hard as investors tried to withdraw as quickly as possible, causing massive capital flights from the country (Beeson & Robison, 2000; Robison & Rosser, 2000). Indonesia as well as Thailand borrowed in the form of debt from foreign or international banks (mainly) in US dollars. These funds were not hedged against domestic depreciation of the currency, and the Indonesian banks that had lent out money in domestic currency suffered great losses when the currency dropped (Corden, 2007).

Along with economic problems, there were also political issues. The conditionality set by the IMF was initially rejected by the Indonesian President, since it would lead to a decrease of political power for the Presidential family. Some very large projects of questionable contribution to the development of Indonesia were cancelled, but instead other projects connected to the President's family and friends were announced to take place. After receiving the IMF fund, the President did not fulfill the promises made before the announcement, but after the currency fell to extreme numbers, the reforms were adopted, although not as thoroughly as expected and desired (Corden, 2007; Winters, 2000). IMF conditionality and reforms included demands to close insolvent banks, abandon government/private monopolies, reduce tariffs and subsidies for exports, to impose transparency in government, and to establish new regulations to deal with bankruptcy and corporate governance. The IMF reform packages were negotiated several times due to hard domestic resistance for the changes required (Robison & Rosser, 2000). According to Corden (2007), the political problems added to the crisis in Indonesia and can be an explanation for why the country was more damaged by the crisis than the others. The President had to resign in 1998, due to the domestic situation in Indonesia, and the new President has been forced to comply to a greater extent with the will of IMF.

4.5 Institutional Development Before, During and After Crisis

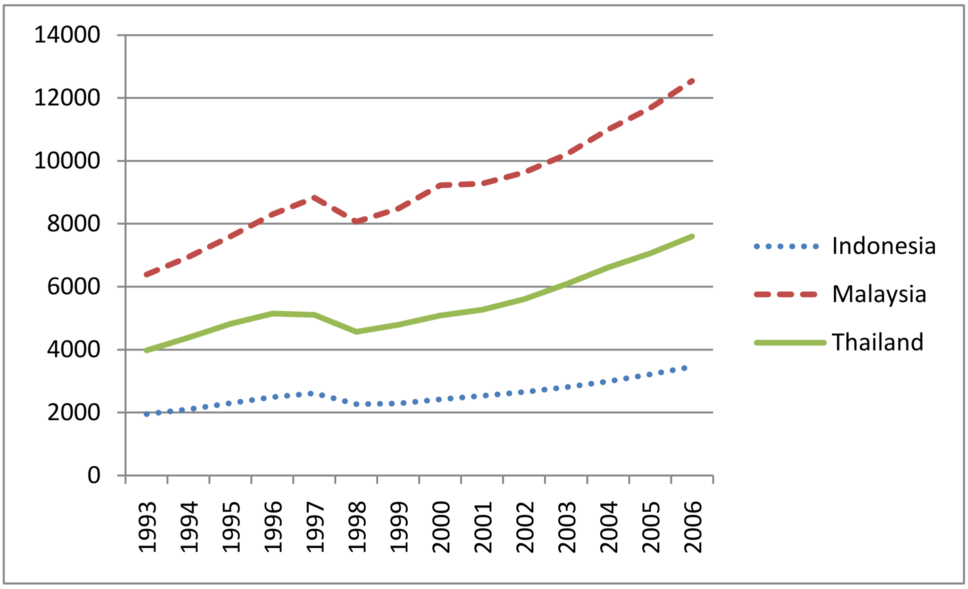
In this section, statistical data on several institutional variables, along with one economic growth indicator will be presented. The variables represent some of the underlying institutional arrangements in a society, necessary for real development to take place. This is in line both with the institutional theories, where especially Sen (1999; 2009) shows the importance of institutions in laying a stable foundation for development, and with the institutional hypothesis, where institutions are a fundamental necessity for economic growth.

IFIs such as WB and IMF are supposed to be watchdogs and alert the international community when countries are facing problems. However, the IFIs failed massively to do so prior to the Asian crisis, although there were warning signs. Other actors had knowledge about the state of the Southeast Asian countries, but did not alert the international community either (Winters, 2000). The reform packages offered by the IMF were grounded on the firm belief that the Asian form of capitalism – not capitalism in general – was the source of the crisis. Therefore, state intervention was seen as the major problem in these countries (Robison & Rosser, 2000).

Kaplan & Rodrik (2001) find in their analysis on the Malaysian performance after the crisis that Malaysia outperformed Korea, Indonesia and Thailand. Since Malaysia had a different time span of policy implementation than the countries receiving IMF assistance, the authors include this aspect and compare the speed of recovery. Although Korea and Thailand have also experienced favorable economic recovery, the conclusion is that Malaysia did much better thanks to the specific policies implemented.

By illustrating the GDP per capita levels from 1993-2006 in graph 4.2, there is evidence that as a direct consequence of the Asian financial crisis, GDP levels dropped for all countries. Indonesia has been the country to recover at the slowest pace, whereas Malaysia experienced fast recovery and maintained high GDP levels. Thailand falls in between with steady increases in GDP levels, although not at the same speed as Malaysia.

Graph 4.2: GDP per Capita in Current International $, 1993-2006



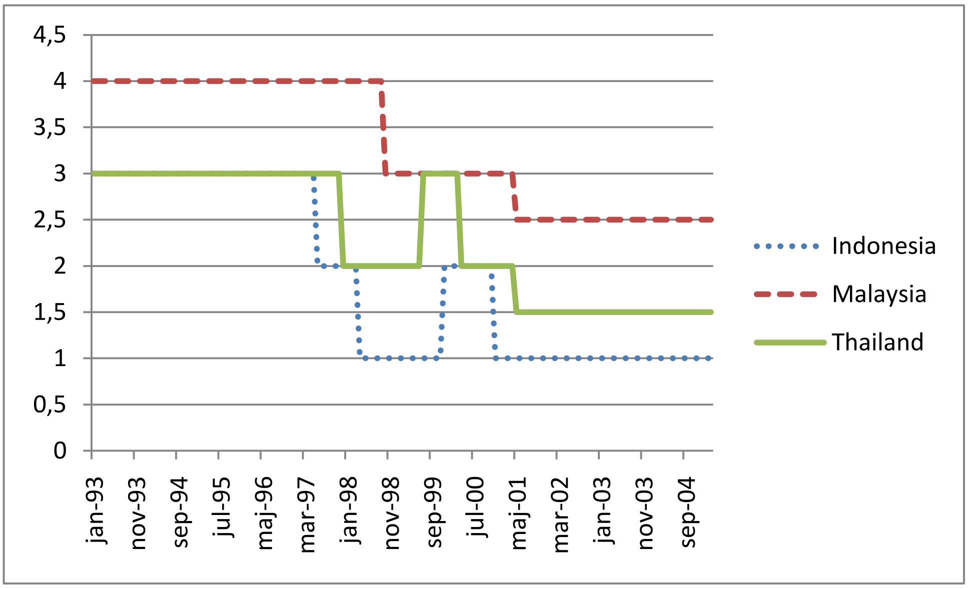
Source: Created by author with data from World Development Indicators 2008 from the World Bank.

Graph 4.3 describes corruption levels in the three countries from January 1993 to March 2005[5], using data from the ICRG, produced by the PRS group. The PRS group produces monthly data on political risk components, and have done so since the 1980's, making it one of the oldest indices in this particular field. Another index commonly used is the Transparency International's Corruption Perception Index (CPI); however, this index is not suitable for comparisons over time. The ICRG index of corruption ranges from zero to six, where six is no corruption and zero is severe corruption. The corruption assessment in this index is based on a number of factors, such as financial corruption in business, nepotism and ties between business and politics (ICRG, 2003).

[5] The reason for using these particular years as starting and ending points is because January 1993 provides enough time prior to the crisis in order to determine if levels were relatively stable, and March 2005 is the latest date with available information for this index.

As graph 4.3 reveals, the countries had increased corruption levels until 2005, with Indonesia as the leader in this sample. However, the interesting point in time is right after crisis, or, the response to the policies implemented to deal with the crisis. Malaysia did not drop as much as the other countries if expressed in percentage. Malaysia dropped later due to that the crisis hit the country somewhat later than it did in Thailand, where it started, and Indonesia. Malaysia is also the country that managed to keep a relatively stable level of corruption after crisis, whereas the other two countries have experienced more fluctuations. There is a fairly high decrease in corruption both in Indonesia and in Thailand approximately one year after the crisis, whereas Malaysia did not experience such decreases. On the other hand, the increase only lasted for about one year in Thailand and slightly longer in Indonesia, with additional increases in corruption for Thailand afterwards as compared to the immediate response to the crisis.

Graph 4.3: Corruption Levels, 1993-2005 (high number indicates less corruption)

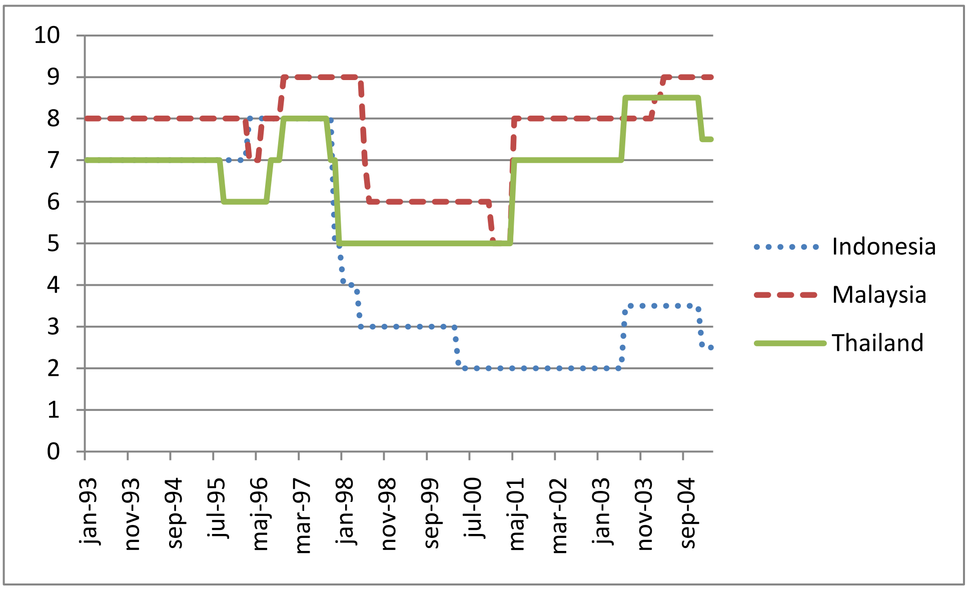


Source: Created by author using data from *International Country Risk Guide* (www.prsgroup.com).

Graph 4.4 shows the progress of socioeconomic conditions, based on unemployment, consumer confidence and poverty. The maximum score is twelve, and when experiencing high risk in this variable, a country generally experiences social dissatisfaction or constrained government action (ICRG, 2003).

Evidently, all countries experienced decreases in this variable too and again Indonesia dropped the most. Both Malaysia and Thailand have been able to reach their previous levels in this variable, although Indonesia has not. Thailand and Malaysia can be assumed to have had a relatively 'normal' catch-up in this variable, with increases starting in 2001. It should be noted that since Malaysia fell into crisis later, the country also experienced the best recovery rate of all countries since it starts at the same time as Thailand's rate. Although the conditions were relatively equal in all countries prior to crisis, it seems that Indonesia has not been able to impose policies that favors employment, reduces poverty and restores consumer confidence.

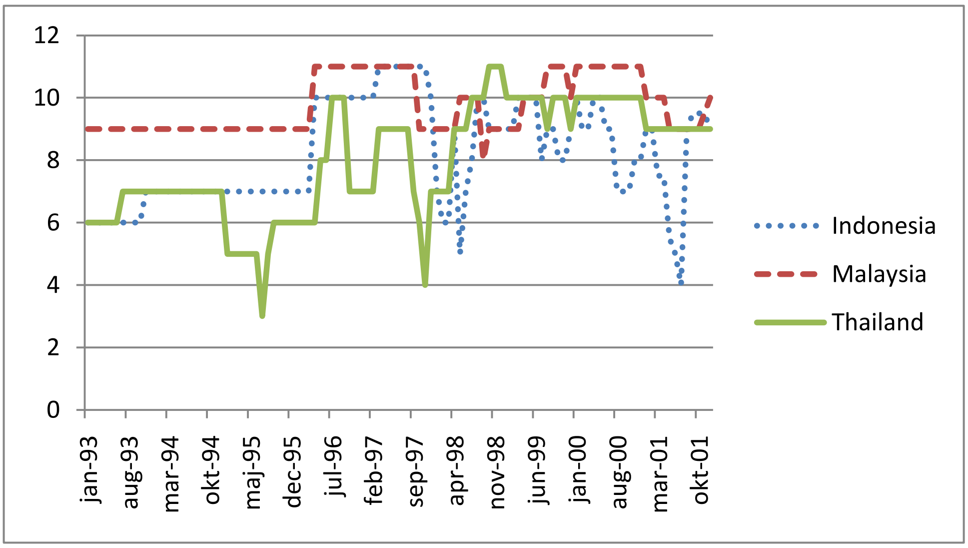
Graph 4.4: Socioeconomic Conditions, 1993-2005 **(high number indicates less risk)**



Source: Created by author using data from *International Country Risk Guide* (www.prsgroup.com).

The measure of government stability is of particular interest in this study (graph 4.5), since it measures the components of government unity, legislative strength and popular support. The maximum score is twelve points (ICRG, 2003). The three countries score remarkably well in this variable, as compared to the other variables outlined in this thesis. Both Thailand and Indonesia are experiencing many fluctuations in this variable, and the aftermath of the Asian crisis is no exception. Malaysia maintained relatively stable scores throughout the period, whereas Indonesia fluctuates even more after crisis, and Thailand experience huge drops but the regains stability in late 1998/early 1999.

Graph 4.5: Government Stability, 1993-2001[6] **(high number indicates less risk)**



Source: Created by author using data from *International Country Risk Guide* (www.prsgroup.com).

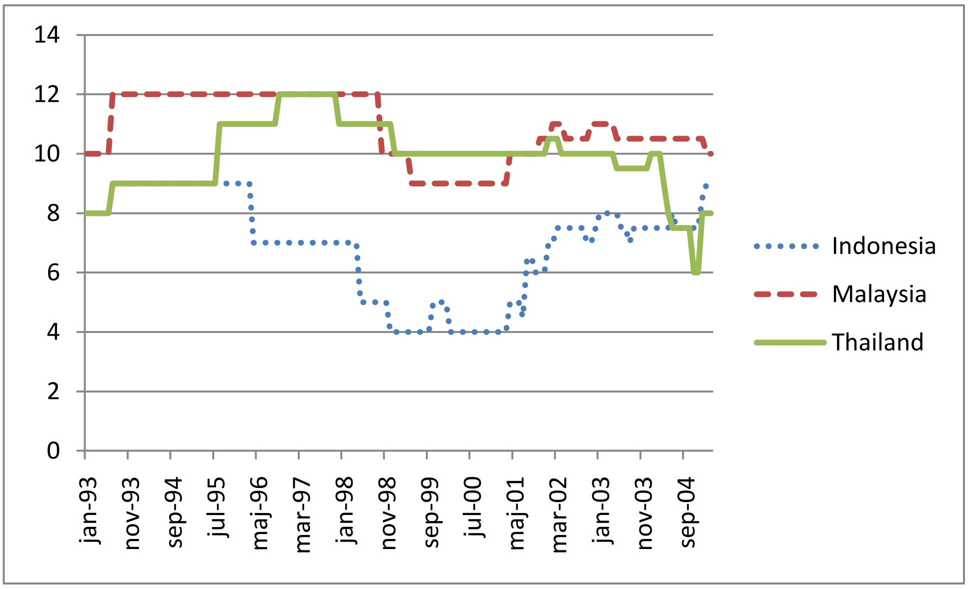
[6] Only measured until 2001 because of visual matters, see Appendix A for this variable measured between 1993-2005.

Appendix A shows the continuation of the government stability until 2005, where it also is evident that Malaysia keeps high levels throughout the period with Thailand slightly below. Indonesia, on the other hand, experiences short-term stability but starts a decreasing trend again towards the end of the period under examination. The period prior to crisis shows that both Malaysia and Indonesia enjoys stability in this variable, indicating that the government enjoyed support and was strong, but at least in Indonesia, this support was lost during and after the crisis.

Finally, graph 4.6 explores the internal conflicts in the discussed countries. This measure is based on the components of civil war/threat of coup, terrorism/political violence and civil disorder and can as a maximum give twelve points (ICRG, 2003). Internal conflict can be connected to the issue of validation of legitimacy, discussed in section 3. Internal conflict could arise as a response to non-legitimate exercise of power, i.e. delegitimation.

Thailand and Malaysia responded with some increases in internal conflict, although not so severe. Indonesia, on the other hand, experienced internal conflicts long before the crisis broke out, with additional increases as a consequence of crisis. Malaysia is the country that has been able to keep the internal conflicts at a minimum during the entire period, whereas Thailand decreased the tendencies for internal conflict before crisis, but in the aftermath there is a trend of increasing internal conflict.

Graph 4.6: Internal Conflict, 1993-2006 (high number indicates less risk)



Source: Created by author using data from *International Country Risk Guide* (www.prsgroup.com).

4.6 Summary

The variables used in this section of empirical evidence are GDP per capita level, corruption level, socioeconomic conditions, government stability and internal conflict. Indonesia has the lowest scores and the largest increases in risk associated with all institutional variables. Indonesia did not, however, have the worst initial conditions throughout the period. Most of the time the starting point is fairly equal, and therefore not an explanation for why Indonesia's scores are so much lower than the other countries' scores. Indonesia also experienced the slowest GDP per capita level of all cases. Malaysia is generally the most stable country with the least fluctuations in the different institutional variables and with the highest GDP levels. The general tendency for Malaysia is recovery at the same time as Thailand, although the crisis hit later in Malaysia. This means that Malaysia experienced the fastest recovery, and in most cases it also reaches the highest levels of development in the different variables, also in relative terms. Thailand falls mostly in the middle, fluctuating more than Malaysia but less than Indonesia most of the time. Even though Thailand experiences institutional development, it is not as stable as in Malaysia, and tends to show longer term effects that seems to show signs of increasing risk associated with the institutional variables. The case of Malaysia being most successful is also supported by the results from the studies mentioned in the beginning of section 4.5.

5 Analysis

Analyzing the matter of external intervention in individual economies is always difficult. External intervention might not produce immediate results, and only concentrating on economic growth, or lack of economic growth, that follows can in some circumstances produce results incapable of conveying the complex reality. In this study, concentrated on institutional development and the legitimacy of IFIs to intervene, economic growth is not sufficient as the only indicator. Nonetheless, it can be used as one of the parameters to measure development, in this case included as GDP per capita with comparable numbers, from 1993-2006 (see graph 4.2).

Malaysia, generally scoring the best in institutional variables, also show the fastest increase in GDP levels. Following the institutional hypothesis, outlined in section 2.1, this is not surprising. As Malaysia also had the best scores in all institutional variables, the institutional hypothesis would predict higher GDP growth as well. As is also argued in the theoretical section on institutions, and especially by Sen (1999; 2009), high quality institutions and institutional environments may induce the inhabitants to profit more from economic growth than if institutions are worse. This, in turn, would induce economic growth to increase even more. This will, eventually, lead to exponential increases in economic growth, since it is dependent on many different institutional aspects.

By comparing the corruption levels in the discussed countries (graph 4.3), there is reason to believe that Malaysia made more appropriate policy choices than the other countries as a response to the crisis. The increase in corruption may be due to the initial responses, regarding IMF-like policy implementation, or alternatively a consequence of the internal dealing with the crisis. However, since the other two countries carried out IMF induced policy reform and increased corruption to a higher extent if considering percentage changes, it is reasonable to believe that Malaysia had more legitimate ground for its decision-making than the other two countries.

There is indeed a short-term decrease in corruption about two years after the reform in Thailand and Indonesia; however it is doubtful if this can be accounted for by the reform implementation. If so, it is not a long-term consequence, not enough to carry out the necessary institutional changes needed to sustain economic development and poverty reduction in the long run. Short-term responses like this could be due to that enforcement in response to violating the reformed institutional framework is effective initially, but becomes too costly in a longer perspective. The additional drop in Thailand, to lower levels than the immediate response to the crisis is also worrying. Corruption should not increase more than the initial increase to the reform, if the institutions where corruption is present are legitimate. If the new rules are not legitimately imposed, mechanisms rewarding breaking the rules may develop, which have negative effects on corruption, increasing it even more. This can be one explanation for why Thailand has experienced such a large increase in corruption over time.

The socioeconomic conditions (graph 4.4) following the new policy reforms in the countries were worsened as an immediate consequence, but has in the long-run recovered in Thailand and Malaysia. However, since crisis hit Malaysia later than Thailand, but the two countries regained stability at the same point in time, recovery has been faster in Malaysia. Indonesia, however, has failed extensively in ensuring better socioeconomic conditions for its people. Social dissatisfaction and constrained government action can therefore be considered most severe in Indonesia, which seems to be a direct consequence of the response to the crisis, given the stable level prior to the outbreak.

The socioeconomic conditions can be related to what was discussed in section 3.1, namely if the government is working hard to maintain power on illegitimate grounds, there is less possibility to devote resources towards other goals. Both Malaysia and Thailand recovered at a relatively equal pace in this variable, although neither of the two countries managed to increase the quality of the conditions above the initial levels following the new policies. It is also interesting to compare the socioeconomic conditions with the growth in GDP per capita. Even though GDP increases quickly, institutional development does not increase at the same pace.

In addition, if socioeconomic conditions are actually worsened, it does not matter if GDP per capita increases, since poverty, unemployment and other negative social factors also increase. This shows that development cannot be determined by blindly examining economic growth, rather it should be evaluated by the situation of the people in the specific country. In extreme cases, economic growth can be attributed to only the economic and political elite, which then does little for the poor part of the population. This may be the case in Indonesia, where the socioeconomic conditions have worsened extensively, although it is still experiencing some increases in GDP per capita.

Following Ostrom's and Sen's theories on institutional change, the established institutions will be more effective and useful if they are developed internally within the institutional setting. Therefore, it is not very surprising that Malaysia maintained relatively equal levels of government stability (graph 4.5) in the aftermath of the crisis. Also, since a government is considered legitimate based on the acceptance of the people and popular support, this variable is also a good indication of legitimacy following the reforms.

It is evident that this variable fluctuated more for Thailand and Indonesia, with accompanying drops after the crisis. Malaysia also enjoyed a higher degree of government stability before the crisis than the other countries, which could be an indication of that the government had more legitimate grounds for imposing the relevant reforms than the other countries. What is perhaps most interesting when examining the development of this variable between the different countries, is that Indonesia had a relatively stable and increasing trend in government stability prior to the crisis. After crisis hit, the variable started to fluctuate extensively, and in the end of the period there were decreasing tendencies (see Appendix A). On the contrary, Thailand had larger fluctuations before rather than after the crisis. An explanation is that Indonesia was so resistant to the reform measures, leading to a cease in popular support when the reforms were imposed. Also, the government may not have had the legislative strength or legitimacy to enforce and implement the reforms demanded.

The reasoning in section 3.1 concerning legitimacy indicates that internal conflict may be the most important variable to analyze in order to arrive at answering the research questions. Since it measures the domestic resistance through civil disobedience, political violence and threat of coups, it is a good approximation for retraction of legitimacy. It is difficult to analyze the tendency of Indonesian internal conflict (graph 4.5) since there were such problems even before the crisis. Both Malaysia and Thailand, on the other hand, show immediate increases in internal conflict after the crisis. This could indicate that there were problems in both these countries after the reform implementations. In the long run, however, it seems like Malaysia has succeeded in keeping the conflicts at reasonable levels (Malaysia also experience maximum points in this variable prior to crisis). Thailand also shows tendencies of long-term negative consequences, since the variables starts to decrease in the end of the period. This could indicate that even though having reasonable levels of development after the crisis, there might have been higher development rates expected, which could cause people to show their dissatisfaction later on.

The general tendency of all the countries examined in this thesis is that they all experience increases in risk variables. Preferably, legitimate policy implementation would lead to an increase in the quality of compliance, in turn leading to more effective outcomes. None of the countries have succeeded to the full extent with this. Malaysia is the country that experienced less fluctuation in most variables and fastest economic recovery, which is the opposite of what could be expected if the IMF reforms were as effective as the institution itself believed at the time. By relating the reform implementations to institutional theory, it is evident that Malaysia should have been the most successful. Malaysian institutions were not subject to the same shock-reform as the other two countries, which allowed its institutions to deal with the crisis more appropriately to the customs and norms developed since the birth of the institutions.

Depending on which institutional theorist followed, there could be prospects for better institutions in the long run in Thailand and Indonesia considering that institutions learn with time and can adopt good institutional measures from other institutions present in the setting. This seems to be more likely in Thailand than in Indonesia, where the institutional variables appear to be more volatile. This volatility may indicate that institutional reforms are appropriate when they are implemented in cooperation between external and internal forces rather than being forced on to a country as in Indonesia, where domestic resistance was present to a larger extent.

The institutional theories by Ostrom (1990; 2005) and Sen (1999; 2009) fits the institutional development in the examined countries better than North's (1990) institutional theory. Ostrom and Sen proposes that in economies where the institutions are developed internally, i.e. by the people actually affected by them, institutional quality tend to be higher. This fits the general development of the countries in this study. Malaysia experiences higher quality institutions and also the general tendency points at less volatility in response to the crisis. North, on the other hand, would suggest that the institutions learn to adapt and be efficient. This would indicate that external reform is possible, since the institutions should realize that the new arrangements are better. However, this theory does not fit to the countries examined. Indonesia does certainly not show any tendencies of learning since institutional quality has dropped, and volatility has increased. As mentioned in the previous paragraph, there could be long-run prospective for Thailand to do so. However, in some variables there have been a decrease of institutional quality, which rather indicates that long-term stability and institutional development are negatively affected by external reform measures.

It should be emphasized that there is no suggestion in the thesis that the Malaysian government enjoys perfect legitimacy for the policies it has implemented and continues to implement. The suggestion from the analysis is rather that Malaysia did enjoy more legitimacy than the other countries considered in this thesis. None of the countries show perfect scores in any institutional variable, with the exception of Malaysia regarding internal conflict prior to the crisis. Generally, this indicates that all the countries have a long way to go before they can claim perfect legitimacy. Legitimacy would lead to greater quality of the actions and outcomes taken in line with new policies and in turn it would increase the institutional quality in the countries.

The results have been in line with the legitimacy concepts, institutional theories and also with the institutional hypothesis. Therefore, the geography and policy hypotheses can be discarded as explanations for development in these countries. The geography hypothesis would predict that the countries should experience relatively equal performance due to their geographical traits, which has shown not to hold. The policy hypothesis would suggest that the countries implementing IMF driven reforms should have reached a higher level of development and economic growth. As have been discussed in this section, this has not been the case. Rather, the institutional hypothesis, where the quality of institutions is the driver of economic growth seems to explain the differences in development pace for the three cases.

6 Conclusions

In this thesis, the question of legitimacy of external reform has been discussed and the validity of IFI involvement in shaping domestic policies in emerging economies in crisis.

Both qualitative and quantitative methods were used for analysis. The qualitative method consisted of a case study, carried out with the help of a conceptual literature study on legitimacy and institutional theory. Statistics are used as the quantitative part of the method to show the effect of the policy responses on different institutional variables.

The case study consists of the three countries Malaysia, Thailand and Indonesia where the latter two asked for IMF assistance during the Asian crisis, whereas Malaysia did not. According to the theories and legitimacy concepts outlined in this study, Malaysia should be better off today since the country resisted external intervention. This can be validated with the variables used in this thesis. Malaysia did experience more stable institutional variables compared to the other two countries, and also recovered faster than the other countries, considering the time when the crisis hit. Thailand fluctuated more in different variables, although it has managed to keep fairly steady levels throughout the period examined, with some tendencies to decreases in some variables towards the end of the time span. Indonesia was most severely hit by the crisis with respect to the institutional development, where almost all variables showed poor performance.

This thesis concludes that for this case study, dealing with crisis through internal policy making is more legitimate than having external forces implementing reforms. However, it is also concluded that an economy can reach institutional development with the help of external influence if it is willing to cooperate. However, such effects also show a tendency to be short-term in certain variables connected to institutional development. External reform without domestic willingness to comply causes more damage both in the short run and in the long run for domestic institutional and economic development. It should be noted however, that none of these countries can claim perfect legitimacy in their policy implementations, and that they generally have a long way to go before they can get close to do so.

Primarily, this study concludes that it has not been legitimate to impose external institutional reform in the countries examined. In order to conclude that external reform is legitimate, at least one of the externally reformed countries should have done better than the country with no external intervention. The institutional theories generally predict domestic policy making to be more effective than the external kind. However, when examining the countries in this case study, it is evident that there is a difference in institutional development that can be directly derived from the attitude and ability to enforce new norms and values.

Secondly, this study finds that there is a difference in degree of legitimacy following the reforms in the three different countries examined. Malaysia has maintained higher and more stable institutional variables, and therefore it is concluded that the legitimacy has been higher there than in Thailand and it has definitely been sustained to a larger extent when comparing to Indonesia.

Thirdly, the institutional hypothesis is concluded to be the most suitable explanation for economic growth in this analysis, which leads to the conclusion that the geography and policy hypotheses are not suitable for this particular area of study.

As a concluding remark, I would like to emphasize to the reader that these results cannot be generalized to other cases. Rather, the thesis should serve as a reminder that more research is needed in this area and that economic growth is not the only indicator of development. It is worth emphasizing the importance of good institutions, both as a driver for economic growth and for human development.

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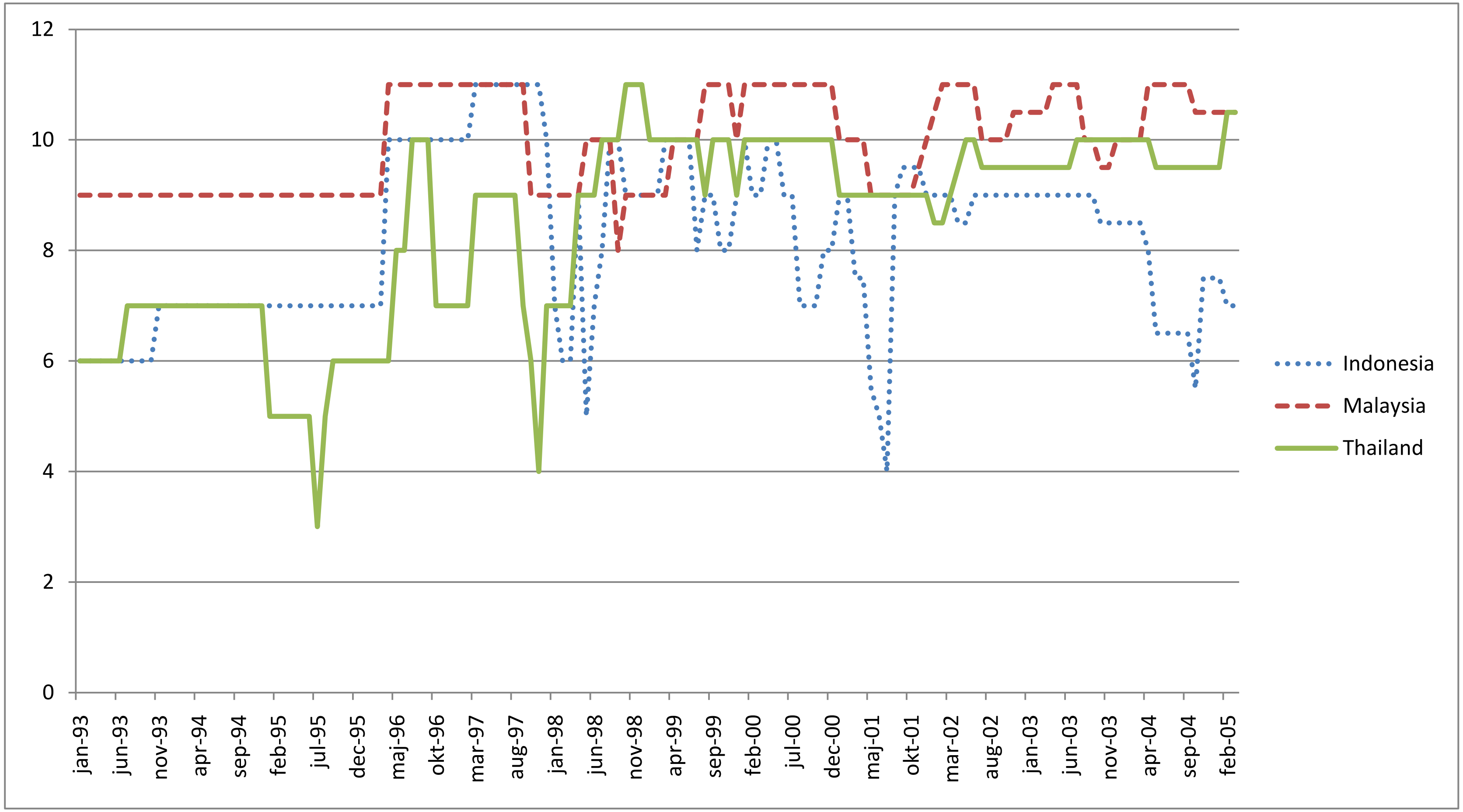
Appendix A: Government Stability, 1993-2005



Source: Created by author using data from *International Country Risk Guide* (www.prsgroup.com).