

# **MAS-ESS ESSAY COMPETITION 2001**

**East Asia in the New Economy: Problems and Challenges**

**Third Prize-Winner, Students Category**

**By**

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## **Summary**

### **EAST ASIA IN THE NEW ECONOMY**

#### **Opportunities & Challenges**

The New Economy is no longer a passing trend in East Asia. The New Economy signifies the need for change in the way the economy is run. Some of these changes bring about enormous potential for the development of an economy; but they also introduce challenges in many forms. Some economic changes include the need to open up one's economy and plug it into the global market, the need to lower costs through innovation and converge industries with common features to increase competitiveness. There are also political implications of the New Economy. They include the need for conservative governments to relax state control and give more autonomy to the private sector, and to be more transparent in their workings. Within these changes lie the opportunities and challenges awaiting East Asian countries. However, embracing the idea of the New Economy is one thing; achieving it and ultimately embodying it is another thing. This is another challenge posed by the New Economy. In conclusion, to meet up to the challenges of the New Economy and to prosper in this New Age, East Asian economies would have to be more outward looking and receptive to new ideas.

## **EAST ASIA IN THE NEW ECONOMY**

### **Opportunities & Challenges**

The trend of developing technology and the Internet has swept across the whole world. Every country, big or small, will have to think about how to move its economy and society into the Internet age, or rather the New Economy. The New Economy is no longer a passing trend. It is here to stay. As Cisco's CEO John Chambers said earlier this year, "The Internet is no longer nice to have, it is a matter of survival."

The New Economy is about change. It entails technological evolution fused with knowledge capital. Often synonymous with IT and Internet start-ups, it also encompasses a great deal of market dynamism as well as globalisation of markets. In contrast with the "Old Economy", which is the traditional "bricks and mortar" kind of industry symbolised by mass production and the automation of factories, the New Economy places emphasis on innovative start-ups (e-Ideas) and the creation of a global market. Governments, including those in East Asia have been modifying and restructuring their economies in order to adapt to the New Economy. The New Economy brings enormous potential for the development of their industries, but it also introduces challenges which can take many forms. Let us now take a step closer into examining what are the opportunities created, as well as the challenges posed for East Asian countries.

In the New Economy, the Internet will play a major role in the nascent business landscape of a country. For example, in the New Economy, we can expect consumer power to increase. The Internet as well as globalisation of markets has enabled consumers to compare prices and quality of goods across international boundaries. Hence, the less efficient firms will be forced out of business. Foreign competitors can now offer their services and products for sale without having to set up a branch in the country. This can be done through the Internet, with the creation of an e-Marketplace. East Asian countries may now find themselves competing with other foreign competitors such as the US and Germany. This formidable global competition may prematurely kill some of the infant industries in East Asia and put many aspiring entrepreneurs out of business.

However, it is possible for East Asian countries to harness these winds of change to their advantage. We all know that East Asia has a relatively small domestic market which hampers its economic growth. By opening up an East Asian market and plugging it into the global market, the country's products or services may then be able to cater to a larger group of consumers and compete with other foreign companies for a larger market share.<sup>1</sup> For example, Prime Minister Goh called for the creation of a pan-Asian IT grouping (Asian IT Belt) during the ASEAN Informal Summit

in November last year. This Belt would harness the complementary strengths of various countries in the region to increase Asia's competitiveness in the global market. Another classic example would be the imminent entry of China into the World Trade Organisation (WTO). China has always been the predominant power in East Asia with a population making up two-thirds of East Asia. With entrance into the WTO, China would compete with other economic powers not only in labour intensive industries but also in the technology manufacturing sectors such as semiconductors, electronics and IT machinery. To prepare the economy for the impending intense competition, the government has called for the merging of the Shanghai and Shenzhen banks. This is a measure taken by the country in order to protect its industries from the "big boys" like established companies such as Microsoft and IBM.

However, to open up a country's economy to foreign investors would mean overhauling traditional approaches to economic development and relaxing state control of the economy. The political implication is that the power of the government would be decentralised and the private sector would have more autonomy. East Asian countries, especially the more conservative ones such as China will find difficulty in balancing between the changes and loosening the reins of power.

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<sup>1</sup> Extracted from speech by Mr Yeo Cheow Tong, Minister for Communications and Information Technology at the Asia Society Conference in Bangalore, India.

Global competition in the New Economy may not necessarily take the form of competition in terms of goods and services. With advancements in technology especially in the communications sector, there is greater capital mobility and banks and financial institutions are able to move funds very rapidly across countries. As a result, investors gravitate towards countries with a skilled labour force, necessary infrastructure and a sound government. Similarly, skilled labour will also be attracted to a country which is economically sound and offers good prospects. Hence, we can see that by opening up an economy to the global market, it does not mean that we are ready to face up to any challenges posed by other countries outside East Asia. Should a country fail to provide all of the above requirements, there could be a very rapid capital flight as investors and IT professionals pull out of the country to find greener pastures elsewhere. This can be very devastating to an economy, both economically and socially. In the case of the US, Alan Greenspan called for the easing of immigration rules on talent so as to attract foreign talent. To face this challenge, East Asian countries would also have to grow and retain, as well as attract talent from all over the world. In the New Economy, talent is the catalyst for growth. Meeting up to this challenge would involve investing in education as well as starting exchange programmes between institutes of higher learning such as the one

between Singapore's National Technological University and the Indian Institute of Technology Chennai.

One feature of the New Economy, as pointed out in a speech by Senior Minister of State, Trade and Industry and Education Mr Peter Chen, is the phenomenon of value chain restructuring, or what we call "disintermediation".<sup>2</sup> This is due to the technological evolution in the New Economy which has eliminated the need for traditional middlemen in many markets, as information can now be disseminated easily and handled separately from physical flows of goods. Thus, many East Asian firms such as the small and medium sized enterprises (SMEs) in Singapore operating on simple buy-sell transactions will face a great risk of being eliminated.

On the other hand, the restructuring of value chains also creates new opportunities for us to tap. For example, we can value-add the information transferred during transactions before distributing them to the consumers through a sub-contracting relationship with the big firms. For example, many handphone outlets in Singapore, although not network providers, sub-contract the purchase and subscription of phone lines to local service providers such as Singtel. These SMEs are able to survive alongside their bigger counterparts and even thrive along with them. These SMEs play a small, but significant role in the development of the economy. Hence, by rising to the challenges of the New Economy and focusing on

innovation and constant adaptation, East Asian countries can in fact, find many opportunities lying among the challenges awaiting them.

Another important difference between the New Economy and the “Old Economy” is that industries now compete not only through lowering costs through economies of scale, but through innovation, quality and finally costs. Hence, economies that fared relatively well in the “Old Economy” may not necessarily thrive in the New Economy.<sup>3</sup> Examples are states which have relied on natural resources and low labour costs to attract investors. One example is India. In the New Economy, technological innovation and knowledge capital are the main determinants of a country’s economic success. However, India is constrained by a shortage of talent and strict government control. As Mr Narayana Murthy, chairman and CEO of Infosys rightly pointed out, “The greatest constraint of India’s growth will be the number of high-quality people available.” Despite the launching of economic liberalisation in August 1991, some old policies still remain. Duties on capital good imports, at 50 percent, remain high by East Asian standards, while energy production and distribution, and other heavy industries remain state sectors. Hence, the challenge to East Asian

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<sup>2</sup> Extracted from speech by Mr Peter Chen, Senior Minister of State, Trade and Industry and Education at the launch of the SME March.

<sup>3</sup> Extracted from *The State New Economy Index*.  
<http://www.neweconomyindex.org/states/strategies.html>



countries is once again, to focus state policies on innovation and transform from an Industrial Age to an Information Age.

On the flip side, this can also be seen as a chance for East Asian countries with low performance rates in the “Old Economy” to thrive. Poor performances in the “Old Economy” may be linked to a shortage of natural resources or a small pool of labour. But now, by fostering the transformation to a New Economy (eg. by transforming into a digital economy through encouraging e-commerce), a small country faced with land and labour constraints such as Singapore may be able to outperform other countries blessed with an abundance of natural resources.

However, it is not as easy as it seems. The transformation to a New Economy is not without its problems. Embracing the “spirit” and essence of the New Economy is one thing. Achieving and ultimately, embodying it is another. For some East Asian countries with poor economic infrastructure, the lack of transparency, high level of corruption and the poor credit standards for banks indicates a desperate need for reform. For such countries (eg. Indonesia), the challenge posed by the New Economy is greater than for any other country. Before they can innovate and improve, they must first stabilise their economies and correct their problems. Only then will investors feel safe to invest, and only then, will they have the necessary funds to carry out research and innovation.

Another feature of the New Economy is the convergence of industries, especially in the fields of telecommunications and IT due to the effects of globalisation; thus creating new competitors with diversified skills. East Asian firms would have to meet up with the challenge and adopt an “alliance and collaboration” policy instead of the current “go it alone” policy they are following. However, this may be hard to achieve as it may not be easy to persuade some of the more conservative parties to change their way of doing things overnight.

Similarly, this may also be seen as an opportunity for some East Asian countries. We are blessed with an abundance of energy resources and the use of English is widespread. Hence, we possess the attributes which make other firms want to merge with our industries. Thus, as long as East Asian entrepreneurs are willing to change their mentality, they can grab this chance to outsource for industries with similar characteristics to merge with in order to enjoy economies of scale. This mainly applies to entrepreneurs who are outward looking and receptive to different cultures and ideas.

Also, in many East Asian countries such as Singapore and Korea, the society’s tolerance level of failures is low. Hence, there is the risk averse problem as people tend to lack the “drive” and “fire” that entrepreneurs require. This social aspect of the New Economy cannot be neglected. The challenge to East Asian governments would be to improve

and amend the current education system which plainly emphasises on rote learning. This stifles creativity which is very important in the New Economy, as the New Economy is driven by the ability to create new and exciting products. East Asian governments also have to support aspiring entrepreneurs especially financially as only then, will the entrepreneurs have the courage to take the plunge. This is not a major problem in Western countries as their society is more tolerant of failures and it is also easier for start-ups to locate funding due to the established financial institutions there. Hence, to be able to compete on a more equal footing with the Western countries in the New Economy, East Asian countries would have to meet up with the challenge of cultivating more entrepreneurs and providing them with the support they need.

Of course, there are also political implications brought about by the New Economy. For example, the Internet will play a huge role in the political landscape of a country. Through the wide use of the Internet, the people can access many sources of information which would enrich their political knowledge and judgement. Hence, there is a need for government bodies to be more transparent in their workings so as to gain the trust of its people. Again, some conservative East Asian countries might find difficulty in achieving this, as it would mean depleting the power of the government and depriving them of the freedom to run the country the way they deem appropriate.

In conclusion, the New Economy offers many great opportunities for East Asian economies to develop, but it also introduces many challenges we can foresee, and many more we cannot predict. However, if our economies are willing to innovate and accept new ideas to meet up with the challenges of the New Economy, we will be able to succeed and enjoy prosperity. On the contrary, if we stubbornly hold on to traditional practices of the "Old Economy" and hinder the growth of the Internet, we will only end up with ailing economies. As Charles Darwin himself said: "It is not the strongest of the species that survive, nor the most intelligent, but the one most responsive to change."

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