



# CONTENTS

Overview: The Unfolding of a Renaissance . . . . .	1
<b>1</b> Growth, Gravity, and Friction. . . . .	45
<b>2</b> Trade. . . . .	81
<b>3</b> Innovation. . . . .	123
<b>4</b> Finance. . . . .	195
<b>5</b> Cities . . . . .	231
<b>6</b> Cohesion . . . . .	271
<b>7</b> Corruption. . . . .	313

## Maps

1.1 East Asia Will Soon Be a Middle-Income Region. . .	44
2.1 Trade Ties Make East Asia a Tightly Knit Region . . .	80
3.1 Telecommunications Flows in East Asia Suggest a Vigorous Exchange of Ideas . . . . .	122
4.1 Investment Flows within East Asia Are Important. . . . .	194
5.1 East Asian Cities of All Sizes Will Expand Rapidly during the Next Decade. . . . .	230
6.1 Within-Country Differences in Poverty Are Considerable in East Asia . . . . .	270
7.1 The Quality of the Rule of Law Varies Considerably across East Asia. . . . .	312

**Boxes**

1 Renaissance Then and Now . . . . .	2
2 Growth, Gravity, and Friction in the Pearl River Delta . . . . .	10
1.1 Once Every Four Years: World Bank Regional Studies on East Asia . . . . .	46
1.2 "The East Asia Project": Achieving a Big Share in the World Economy . . . . .	67
1.3 Middle-Income Status: A Period of Significant Change . . . . .	69
3.1 Ideas and Knowledge: Nonexcludability and Nonrival Consumption . . . . .	126
3.2 Channels for Acquiring Technology from Abroad . . . . .	131
3.3 Scale Economies and the OEM and Design and Brand Manufacturing Sequence . . . . .	136
3.4 Foreign Technology and Domestic Innovation May Support Development . . . . .	150
3.5 Geography and Knowledge Spillovers . . . . .	167
5.1 Agglomeration Economies . . . . .	232
5.2 Optimal Urban Concentration? . . . . .	241
5.3 Differentials in City Performance in China . . . . .	249
5.4 Human Capital Externalities in Cities . . . . .	251
5.5 The Costs of Failure . . . . .	262
7.1 Singapore, Corruption, and the Civil Service . . . . .	326
7.2 Corrupt Governments as Joint Monopolists . . . . .	327
7.3 Competitive Corruption in Cambodia . . . . .	333
7.4 The History of Corruption in the United States . . . . .	342

**Figures**

1 East Asia Has Kept Pace Despite the 1997–98 Crisis and Japan's Stagnation . . . . .	4
2 More Than Half of East Asia's Trade Now Occurs within the Region . . . . .	8
3 Economic Growth in Middle-Income Countries . . . . .	9
4 East Asian Exports Are Growing in Sectors with Increasing Returns to Scale . . . . .	20
5 Intraindustry Trade Has Boomed in East Asia . . . . .	21
6 East Asia's Efforts in R&D Have Outpaced Those of the Rest of the World . . . . .	25
7 East Asia Shows Less Exposure to Bank Credit and a More Diversified Supply . . . . .	28
8 Inequality Is Rising in East Asia Despite Regional Convergence . . . . .	31
9 East Asia Is Falling Behind in the Control of Corruption . . . . .	33
1.1 Developing East Asia Is the Most Diverse Region . . . . .	51

1.2 A Second Group of East Asian Economies Has Caught Up with Latin America . . . . .	54
1.3 China, Korea, and Taiwan (China) Are Outspending Their Peers on R&D . . . . .	57
1.4 FDI Flows within East Asia Have Increased Since the Financial Crisis . . . . .	58
1.5 Large Cities in East Asia Are as Livable as Those in Latin America . . . . .	61
1.6 Inequality Has Been Rising in Much of East Asia Since 1990 . . . . .	64
1.7 East Asia and Latin America Do Equally Poorly in Controlling Corruption . . . . .	65
1.8 Regional Share of World GDP . . . . .	67
2.1 Freight Costs across the World: Asia Is Doing Well . . . . .	84
2.2 Average Tariffs Have Fallen . . . . .	85
2.3 FDI Has Played a Key Role in East Asia . . . . .	86
2.4 Over Half of China's Exports Originate through Multinationals . . . . .	87
2.5 China and ASEAN Are Intermediating More of East Asia's Trade . . . . .	90
2.6 The Exports of East Asian Countries Have Become More Similar . . . . .	94
2.7 Vertical and Horizontal Intraindustry Trade Have Become More Important . . . . .	95
2.8 Parts and Components Exports Are More Important in East Asia . . . . .	96
2.9 East Asian Exports Are More Sophisticated Than Predicted by Income Levels . . . . .	100
2.10 East Asian Exporters Recoup in China What They Lose Elsewhere to China . . . . .	101
2.11 China Is Displacing East Asian Countries in Many Markets, but Not in Europe . . . . .	103
2.12 Specialization and Efficiency Are Growing in High-Tech Machinery Exports . . . . .	106
2.13 Countries with Greater Export Variety Have Higher Productivity Growth . . . . .	108
2.14 China Has Become a Leader in the Development of New Exports . . . . .	109
2.15 Foreign Firms Are Increasingly Concentrated in High-Technology Trade . . . . .	110
2.16 Domestic Firms Dominate in China's Low-Technology Export Industries . . . . .	112
2.17 East Asian Free Trade Agreements Are Surging . . . . .	114
3.1 East Asia Shows High Imports of Machinery and Transport Equipment . . . . .	132
3.2 East Asian Countries Make Relatively Large Royalty Payments . . . . .	133

3.3 East Asia Is a Prolific Exporter of Machinery and Transport Equipment ..... 135

3.4 FDI Inflows Vary Considerably across East Asia ..... 141

3.5 FDI Stock in East Asia: Manufacturing Is High, and Services Are Low ..... 142

3.6 Indonesian Plants Acquired by Foreigners Experience Higher Productivity ..... 143

3.7 R&D Efforts Have Increased More Rapidly in East Asia ..... 148

3.8 Businesses Lead in the R&D Effort in East Asia ..... 152

3.9 The East Asian Tigers Are Extraordinary Generators of New Ideas .... 156

3.10 East Asia's Middle-Income Countries Are Merely Routine Patent Developers ..... 157

3.11 Patenting in East Asia Is Concentrated in a Relatively Few Sectors .... 159

3.12 East Asia Is Advancing the Technology Frontier in Electronics ..... 160

3.13 East Asian Patents Show Considerable Originality ..... 162

3.14 East Asian Patents Are Widely Applicable ..... 162

3.15 Japan and the United States Account for Most Patent Citations in East Asia ..... 163

3.16 Intraregional Knowledge Flows Have Increased Since the 1990s ..... 165

3.17 Geographical Proximity Increases Knowledge Exchanges ..... 166

3.18 Improvements in Higher Education Have Been Uneven in East Asia .. 176

4.1 FDI Is Important in China, Malaysia, and Vietnam ..... 201

4.2 The Constraints Most Frequently Cited by Firms ..... 204

4.3 Access to Finance Is a Problem for Exporters and Nonexporters ..... 205

4.4 Return Volatility Explained by Regional, Japanese, and U.S. News. ... 209

4.5 Foreign Exchange Reserves Have Grown Since the 1997–98 Crisis. ... 210

4.6 Effective Exchange Rates Have Fluctuated Considerably Since 1994 .. 211

4.7 East Asian Holdings of Foreign Assets Are Not Unusually High, 2004 ..... 214

4.8 The Share of Nonperforming Loans Has Shrunk Since 1997 ..... 219

4.9 Capital Adequacy Has Strengthened Since 1997 ..... 220

5.1 Rapid Urbanization Lies Ahead for East Asian Countries ..... 238

5.2 Urbanites in China's Coastal Cities Are Twice as Rich as Those in the Interior ..... 246

5.3 East Asia's Large Cities Are as Livable as Those in Other Middle-Income Regions ..... 252

5.4 A Third of East Asia's City Dwellers Live in Slums, 2001 ..... 257

5.5 East Asia's Infrastructure Needs Are Increasing, 1996–2010 ..... 261

6.1 Human Development Indicators in East Asia Have Improved Since 1990 ..... 274

6.2 Inequality Has Increased within and between Rural and Urban Areas in China ..... 278

6.3 Rural-Urban Differences in Income and Poverty Have Been Persistently Large ..... 279

6.4 Rural-Urban Differences in Social Indicators Are Considerable ..... 280

6.5 Spatial Differences in Human Development Are Large in East Asia ..... 282

6.6 Poverty in Rural China Varies with Location and Ethnicity, 2003 .... 284

6.7 Many of China's Rural Residents Move Into and Out of Poverty, 2001–04 ..... 286

6.8 Well-Educated Workers Are Earning More in High-Growth Countries. .... 287

6.9 FDI Is Spatially Concentrated in China and Vietnam ..... 293

6.10 Coastal China Has Nearly All the Country's Foreign Trade and Investment ..... 294

6.11 Subnational Governments Are Responsible for More Public Spending Today ..... 295

6.12 Needier Provinces Often Obtain Less ..... 296

6.13 Richer Provinces Spend More per Capita Than Do Poorer Provinces ..... 297

6.14 Political Stability Tends to Decline with Rising Inequality ..... 300

7.1 Indexes of Corruption Vary Widely across East Asia ..... 317

7.2 Richer Economies Show Better Outcomes in Global Corruption Indexes ..... 319

7.3 Is Corruption a Major Constraint on Business?: No Single Answer for East Asia ..... 323

7.4 Government Effectiveness Is Greater Than Corruption Indexes Imply, 2004 ..... 329

7.5 Good Human Development Outcomes Despite High Corruption Levels ..... 330

7.6 The Bribes Needed to Get Things Done Appear to Be Smaller in East Asia ..... 331

7.7 Political Rights and Civil Liberties Are Spreading in East Asia, 1976–2004 ..... 337

7.8 Subnational Governments Are Being Given Greater Responsibilities ..... 338

7.9 The Initial Impact of Decentralization in Indonesia, as Cited by Firms . . . . .	345
7.10 The Control of Corruption Is Seen as More Lax in East Asia in 1996–2004 . . . . .	347

### Tables

1 The Story of Dongguan in Numbers . . . . .	12
2 Gravity and Friction: Facts and Implications . . . . .	35
3 The Growing Complexity of Development: Economies of Scale . . . . .	37
4 The Growing Complexity of Development: The Distribution of Economic Rents . . . . .	39
1.1 East Asia Has Been Growing More Rapidly Than All Other Regions . . . . .	49
1.2 East Asian Growth Has Been Strong and Steady . . . . .	50
1.3 The Intraregional Trade Share Has Risen in High- and Middle-Income Countries . . . . .	56
1.4 Parts and Components Have Become More Important in East Asia's Trade . . . . .	56
1.5 Regional FDI Patterns Have Changed during the Last Two Decades . . . . .	59
1.6 East Asia's Urban Population Will Rise by More Than 500 Million in the Next 25 Years . . . . .	62
1.7 The Number of East Asians Living on Less Than US\$2 a Day Fell by 500 Million . . . . .	63
1.8 Recognizing the Importance of Scale Economies: Recent Theoretical Advances . . . . .	71
1.9 Economic Growth and Distribution: Recent Theoretical Advances . . . . .	73
2.1 East Asia Is a Trade Powerhouse . . . . .	84
2.2 East Asian Intraregional Exports Have Been Growing Thanks to China . . . . .	88
2.3 The Commodity Composition of Foreign Trade in East Asia . . . . .	91
2.4 The Share of Exports of Selected East Asian Countries in World Markets . . . . .	93
2.5 Intra-Asian Trade in Parts and Components . . . . .	97
2.6 Index of the Average Wage of Exports . . . . .	99
2.7 Is China Displacing the Exports of Other East Asian and Pacific Countries? . . . . .	102
2.8 The Threat Industries of China . . . . .	104
3.1 Indicators of the Dynamism of Firms . . . . .	128
3.2 Most Important Source of Technological Innovation . . . . .	130
3.3 The Top Five Electronic Contract Manufacturers, 1994 and 2004 . . . . .	138

3.4 R&D Expenditures . . . . .	147
3.5 R&D by Sector of Performance and Funding . . . . .	151
3.6 Patents Granted by the USPTO . . . . .	155
3.7 Citation Frequencies: Estimated Country-Pair Fixed Effects . . . . .	168
3.8 National Innovation Systems and the Business Environment: Selected Variables . . . . .	170
4.1 Trends in Capital Flows to Emerging East Asia, 1990–2005 . . . . .	200
4.2 East Asia NIEs Have Replaced Japan as the Regional Source of Portfolio Finance . . . . .	207
4.3 NIEs Are the Most Important Portfolio Investors in Developing East Asia . . . . .	207
4.4 Current and Capital Account Surpluses, 2002–05 . . . . .	212
4.5 Financial Markets, Especially Securities Markets, Have Surged Since 1997 . . . . .	216
5.1 Urban Populations Have Grown at Twice the Rate of Total Populations . . . . .	234
5.2 East Asia Has Mega, Primate, Capital, and Gateway Cities . . . . .	237
5.3 Chinese Cities Compare Poorly to Cities in the G-7 in Grime and Time Costs . . . . .	239
5.4 About 60 Percent of the Urban Population Lives in Cities of Less Than a Million . . . . .	241
5.5 Geography Influences the Returns to Labor in China . . . . .	243
5.6 China: Representative Factor and Transport Costs for Typical City-Pairs, 2005 . . . . .	244
5.7 Urban Transport and Road Safety Indicators . . . . .	253
5.8 Hong Kong (China) Leads the Region in Sustainable City Development . . . . .	254
5.9 Kuala Lumpur Has the Lowest Density Indicators among Metropolises, 2000–01 . . . . .	256
5.10 Urbanization Problems and Policy Responses . . . . .	259
5.11 China, Thailand, and Vietnam Have Raised Infrastructure Spending . . . . .	264
6.1 East Asia's Progress in Poverty Reduction Since 1990 . . . . .	273
6.2 Progress in Reducing US\$2-a-Day Poverty Since 1990 . . . . .	276
6.3 Evolution of Inequality in East Asia, 1990–2002: The Theil Index . . . . .	277
6.4 The Ethnic Dimension of Disparities in Lao PDR, 2002–03 . . . . .	283
6.5 The Ethnic Dimension of Disparities in Vietnam, 1993, 1998, and 2002 . . . . .	284
7.1 Corruption May Not Be a Severe Constraint on Enterprises in All of East Asia . . . . .	322
7.2 Potential Links between Corruption and Decentralization . . . . .	343