The Philippines vs. Indonesia: A Tale of Two Leaders

by

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Abstract:

Previous work emphasizes the correlation or casual impact between institutions and economic performance (e.g. property rights, independent judiciaries, and access to education all encouraging investment and growth). Economists, Peter Henry and Conrad Miller, provide a counterargument to this claim in their paper, “Institutions vs. Policies: A Tale of Two Islands.” They argue differences in macroeconomic policy choices, not differences in institutions, were responsible for the divergence of economic growth between Jamaica and Barbados throughout the late 20th century. This thesis provides another counterexample, but with particular emphasis on leadership. Specifically, the Philippines and Indonesia are two archipelagos that have had similar institutions in terms of weakness, but radically different economic outcomes, particularly under the leadership of dictators, Ferdinand Marcos (term: 1965-1986) and Suharto (term: 1968-1998), respectively. Indonesia’s average growth rate of Gross Domestic Product (GDP) per capita under Suharto was roughly four times greater than the Philippines’ under Marcos. Ultimately, the divergence of the economic growth between the Philippines vs. Indonesia, more than anything, is a story of these two corrupt leaders—with one having significantly more effective macroeconomic policies than the other.
Acknowledgements:

I would like to thank my thesis advisor, Professor Peter Henry, for his guidance throughout my senior year. His expertise in economic growth and encouragement were invaluable in helping me complete my thesis. It was also his and Professor Michael Spence’s course, “Growth in the Developing World and the Global Economy,” that sparked my interest in developing economies.

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Table of Contents

1. INTRODUCTION ................................................................................................................................. 5

2. COMMON CHARACTERISTICS FOR HIGH, SUSTAINED GROWTH ................................................... 11
   A. EFFECTIVE LEADERSHIP AND GOVERNANCE ........................................................................... 13
   B. OPENNESS TO GLOBALIZATION ............................................................................................... 18
   C. FUTURE ORIENTATION .................................................................................................................. 26
   D. MARKET ALLOCATION OF RESOURCES .................................................................................... 30
   E. MACROECONOMIC STABILITY .................................................................................................... 34

3. THE FALL OF MARCOS .................................................................................................................... 39

4. THE FALL OF SUHARTO .................................................................................................................... 40

5. CONCLUSION ....................................................................................................................................... 42

6. WORKS CITED .................................................................................................................................... 44
1. **Introduction:**

A long line of work highlights the correlation, or even causal impact, between institutions and economic performance (Smith, 1776; Lewis, 1956; North 1990; Acemoglu, Johnson, and Robinson 2001). Namely, secure property rights, checks against government power, independent judiciaries, and access to education are all important to encourage investment and growth. These works, however, do not illustrate the full picture of economic development. Economists, Peter Blair Henry and Conrad Miller, in their paper, “Institutions vs. Policies: A Tale of Two Islands,” offer a counterargument to this claim regarding the impact of institutions. They argue, “While institutions undoubtedly affect economic outcomes, the macroeconomic policies that governments choose to implement may exert just as much (or more) influence on the trajectory of their economies as the broader institutional framework within which those policy decisions take place.”

Henry and Miller focus on Barbados and Jamaica and their respective differences on macroeconomic policy that were responsible for such a divergence in growth over the latter half of the 20th century.

This thesis offers another counterexample, but with particular emphasis on leadership. Specifically, the Philippines and Indonesia are two countries that have had similar institutions in terms of weakness, but radically different economic outcomes, particularly under the leadership of two corrupt dictators, Ferdinand Marcos (term: 1965-1986) and Suharto (term: 1968-1998).

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During the 20th century, academics held a high regard for the Philippines’ economic potential. In fact, Asia as a whole was experiencing substantial economic growth, which many economists consider to be a modern world “Miracle.” But this substantial growth never occurred for the Philippines; it did not even come close. Despite the Philippines’ large population, initially democratic nature, and relationship with the United States (the world’s largest economy), growth still lagged significantly behind Indonesia, let alone East Asia, during this high growth period — with the country often considered the “Sick Man of Asia.”

The Philippines and Indonesia are both former colonies (Spain and the Netherlands, respectively), archipelagos, and presidential republics in Southeast Asia with large populations. Over the latter half of the 20th century, both countries faced the challenge of developing an economy that is spread over several thousand islands and made up of widely disparate cultural and linguistic groups. This posed a unusual challenge compared to the more controllable environments of other “Asian Miracle” stories such as Singapore, Taiwan, or South Korea, or even smaller success stories such as Thailand, given that these countries are more homogenous and less geographically scattered.

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Figure 1 plots the natural logarithm of an index of real GDP per capita (measured in US dollars) of the Philippines and Indonesia from 1960 to 2018 (indexing the graph at 0). This graph depicts a striking story. Even though Indonesia did not experience nearly the same rate of economic growth as the Asian Tigers or China, the economy still had healthy growth over nearly the last 60 years, especially when compared to the Philippines.

To be exact, by 2018, the natural log of the index is 1.826 for Indonesia and 1.048 for the Philippines, which means that the average annual growth rate between 1960-2018 for Indonesia is 3.1 percent (1.826 divided by 58) versus 1.8 percent for the Philippines (1.048 divided by 58). However, there is an even higher divergence between the two countries when examining the average annual growth rates prior to the 1997 Asian Financial Crisis: 1.1 percent (0.415 divided by 37) for the Philippines versus 3.4 percent for Indonesia. Even though Indonesia had negative
economic growth in the 1960s, it managed to catch up to the Philippines in the 1970s, and overtake it significantly by the 1980s.

Regarding the recent history of the Philippines, high levels of corruption may ostensibly appear to explain why the Philippines’ economy did not grow as much as other major Asian countries. However, “prior literature on the quantitative relationship between corruption and economic development has failed to produce a consensus.”5 For example:

“Researchers such as Krueger (1974), Myrdal (1989), and Tanzi (1997) argue corruption inefficiently allocates resources and discourages private investment. On the other hand, Kolstad and Wiig (2013) indicate that foreign investors prefer to invest in corrupt countries, and many instances of a negative correlation between corruption and growth seem to disappear once controlling for factors such as foreign investment (Mauro 1995), political stability (Mo 2001), or institutional quality (Méon and Sekkat 2005)”6

Additionally, that assumption regarding high levels of corruption becomes more complicated when examining the massive corruption present in both Indonesia and the Philippines throughout the late 20th century. Transparency International’s Global Corruption Report lists the most corrupt leaders in modern history and ranks them accordingly (based on estimated funds embezzled) (see Table 1). Remarkably, Suharto of Indonesia (1968-1998) and Ferdinand Marcos of the Philippines (1965-1986) take the number one and two spots, respectively.

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6 Ibid.
Table 1:

<table>
<thead>
<tr>
<th>Head of Government</th>
<th>Country/ Years in Office</th>
<th>Estimates of funds allegedly embezzled</th>
<th>GDP per Capita (2001)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Suharto</td>
<td>Indonesia, 1968-1998</td>
<td>US $ 15 to 35 billion</td>
<td>US $ 695</td>
</tr>
<tr>
<td>Ferdinand Marcos</td>
<td>Philippines, 1965-1986</td>
<td>US $ 5 to 10 billion</td>
<td>US $ 912</td>
</tr>
<tr>
<td>Slobodan Milosevic</td>
<td>Serbia/Yugoslavia, 1989-2000</td>
<td>US $ 1 billion</td>
<td>n/a</td>
</tr>
<tr>
<td>Jean-Claude Duvalier</td>
<td>Haiti, 1971-1986</td>
<td>US $ 300 to 800 million</td>
<td>US $460</td>
</tr>
<tr>
<td>Alberto Fujimori</td>
<td>Peru, 1990-2000</td>
<td>US $ 600 million</td>
<td>US $ 2051</td>
</tr>
<tr>
<td>Pavlo Lazarenko</td>
<td>Ukraine, 1996-1997</td>
<td>US $ 114 to 200 million</td>
<td>US $ 766</td>
</tr>
<tr>
<td>Arnoldo Alemán</td>
<td>Nicaragua, 1997-2002</td>
<td>US $ 100 million</td>
<td>US $ 490</td>
</tr>
</tbody>
</table>

Source: 2004 Global Corruption Report by Transparency International

Much of the stark difference in economic results between the Philippines and Indonesia can be traced back to the leadership of these two presidents. By framing the comparison in this manner, it becomes clearer that the Philippines and Indonesia of the late 20th century were two commodity-rich archipelagos both with large populations, multiple languages, dominant religions, aggressive military presence, weak institutions, and similar climates under the rule of two corrupt dictators. Both leaders’ terms included massive corruption, communist opposition, crony capitalism, and groups of highly-educated “technocrats” advising them on macroeconomic policy. Yet, despite these similarities, there are still significant variations in the GDP data. The Indonesian economy healthily grew while the Philippines economically suffered.
My hypothesis is the divergence of the economic growth of the Philippines versus Indonesia, more than anything, is a story of two corrupt leaders—with one having significantly more effective macroeconomic policies than the other.

**Figure 2:**

While Figure 2 also plots the natural logarithm of an index of real GDP per capita of the Philippines and Indonesia, it focuses on the years during which Marcos and Suharto ruled (1965-1986 and 1968-1998, respectively) and highlights the root of this divergence. To be exact, between 1965-1986 (Marcos’ rule), the natural log of the index increases from 0.00 to 0.18, which means the average annual growth rate under Marcos was 0.9 percent (.18 divided by 21). Meanwhile, between 1968-1998 (Suharto’s rule), the natural log of the index increases from .06 to 1.14, which means the average annual growth rate under Suharto was 3.6 percent (1.08 divided by 30). Even when factoring in Indonesia’s worst economic year on record (1998:
following the Asian Financial Crisis), economic growth under Suharto was still four times greater than Marcos.

2. **Common Characteristics for High, Sustained Growth:**

According to economist, Michael Spence, and the *Growth Commission Final Report*, there are five common characteristics for achieving high, sustained growth:7,8

◊ **Effective Leadership and Governance**

- Openness to Globalization
- Future Orientation
- Market Allocation of Resources
- Macroeconomic Stability

These are the characteristics 13 countries have shared since the post-WWII era to achieve a 7%+ average growth rate over a span of 25 years or longer, Indonesia included.9 Although all five may be considered essential, effective leadership and governance emerges as the most critical for economic development. Indeed, it is under the leadership and governance of a certain individual, regime, or administration that a country does or does not adopt policies that are consistent with the other four characteristics of high, sustained growth. Without effective leadership and governance, it is largely a matter of chance whether a country embraces such policies.

Despite the numerous important similarities between the Philippines and Indonesia, the striking contrast depicted in Figures 1 and 2 can be explained through the notion that Indonesia,

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8 The Growth Commission displays these five characteristics in a proportional figure and later argues openness to globalization is “the most important shared characteristic.” However, this thesis will argue that the characteristic of leadership and governance prevails before the four other characteristics, hence its heading and separation.
9 Ibid
unlike the Philippines, was constrained to remain within reasonable range of these five characteristics of development. The Philippines, by virtue of Marcos and the crony capitalists, was not. Therefore, this thesis merits its own lesson for economic growth: *even in corrupt environments, economic efficiency matters.*
A. Effective Leadership and Governance:

Although effective leadership seems rather obvious for an economy to achieve sustained growth, only recently has academic literature demonstrated its importance.10 Leadership becomes especially impactful when institutions are weak. This is because “one of the functions of well-built institutions is to pool expertise and to apply brakes to poor policy choices, including those of the leadership group.”11 Autocratic settings are another factor that amplifies the impact of a leader, which can be either positive or negative.12 Weak institutions and autocratic settings are two characteristics the Philippines and Indonesia have shared.

As economist Peter Blair Henry explains, “Leaders have no control over its location, colonial heritage, or legal origin, but they do have agency over the policies they implement.”13 This remark can be applied to the cases of Marcos and Suharto, whose decisions on economic policy over decades resulted in extremely different economic outcomes for the Philippines and Indonesia. As mentioned earlier, both presidents’ terms also included groups of highly-educated technocrats who would advise on such policy.

Suharto had no formal training in economics. He was a former general who gained power in a military coup.14 Nonetheless, he was obsessed with economic development.15 When Suharto came into power, Indonesia was bankrupt, and he decided to appoint a group of economic advisers who had received doctorates in economics from the University of California at Berkeley. Suharto developed a strong relationship with this team, and these technocrats would

11 Ibid
become known as “The Berkeley Mafia.” The regime as a whole would become known as “The New Order.” This commitment to growth became a way for Suharto to legitimize his presidency as well as the policies of the technocrats. Because of the Berkeley Mafia’s common education, these economists had a more unified view on economics and development that focused on free markets, private enterprise, and poverty alleviation. Suharto, for the most part, listened to his advisers, led by economists Wardhana and Widjojo. Wardhana even explained how Suharto “was trying to learn, to understand, what economics is all about” and the technocrats found the president “open-minded and willing to make different and potentially unpopular decisions.”

The problem, however, was there were also groups who stood in opposition to Wardhana and Widjojo. While the technocrats had their “market-driven, outward-looking philosophy,” another group, referred to as “the nationalists,” pushed for more “inward-looking, state-driven strategies.” Additionally, there were the cronies, also known as the businessmen who had close ties with Suharto and therefore had privileged access to special favors. This included monopoly rights on trade and production, “which distorted markets, impaired Indonesia’s competitiveness, and ran counter to the [technocrats’] efforts to open the economy.” Indonesia’s autocratic nature meant it was not possible to implement policy without Suharto. Consequently, these three groups were at odds for their president’s attention, and policies at times were not only incohesive, but rather contradictory. This also meant not all of the technocrats’ policy initiatives

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17 Ibid
20 Ibid
21 Ibid
22 Ibid
geared towards economic growth could come to fruition. However, the technocratic policies that Suharto did approve was still enough to set Indonesia on its way to 30 years of economic growth (which will be discussed throughout the other four common characteristics for economic development).

When Marcos became president, economists predicted the Philippines would be the next economic success story. Unlike Suharto, who had inherited a bankrupt economy through a political overthrow, Marcos was democratically elected in 1965 during a period of healthy growth for the Philippines. He even became the first presidential incumbent after defeating Senator Sergio Osmeña Jr. in 1969 (although the 1969 election was “democratic,” *Time* considered it the dirtiest, most violent, and most corrupt election in Philippine modern history due to Marcos’ vote buying, terrorism, and ballot snatching). Before Marcos’ presidency, between 1950 and 1965, the Philippines’ average growth rate was higher than all of Southeast Asia, Taiwan, and South Korea. Although not an economist nor a former general, Marcos came from an educated law background and had already solidified himself as a political leader. At the time, many academics, developmentalists, and politicians accepted the notion that strong and even authoritarian leadership would be beneficial for accelerating economic growth. This notion could be applied to the Philippines. Perhaps the country’s democratic setup was no longer adequate in the context of economic growth, as growth rates had slowed between the years of 1965-1970 (see Figure 2). Additionally, the Philippines had a U.S. style judicial system that

24 Morallo, Audrey. “Did the Philippines have the best democracy under Marcos?” https://newslab.philstar.com/31-years-of-amnesia/best-democracy
26 Ibid
could not cope with several issues such as high levels of crime which included widespread private weapons and daylight robberies. Under this system, the poor were deprived and decisions on complex procedures were delayed. The patronage system also hindered the process of removing corrupt and incompetent civil servants. Additionally, high levels of social inequality remained rooted in flawed land rights and landlord systems. Because of the Philippines’ democratic system, Marcos faced a “constitutional prohibition” on running for a third term. However, under the guise of strong communist opposition in Manila, Marcos was able to justify martial law in 1972 (even though in actuality there were less than 800 communist guerillas). This regime as a whole would come to be known as the “New Society,” similar in diction but contrasting in economic effectiveness versus Suharto’s “New Order.”

Reactions to such a drastic change in leadership structure were actually mostly favorable. There was “little official international condemnation” against this enactment and “American business literature began predicting that the Philippines would be the next ‘Asian economic miracle.’” Theoretically, authoritarian leadership allows one to bypass potentially strong but inefficient/ineffective institutions. This structure, coupled with sound economic policies, could make the difference in achieving significant economic growth. While it would be unlikely for a political leader with no formal background in economics to generate such policies himself, Marcos, similar to Suharto, appointed world-class technocrats such as Alejandro Melchor, Vicente Paterno, and Cesar Virata. These appointments brought confidence to foreign

29 Ibid
30 Ibid
31 Ibid
32 Ibid
33 Ibid
34 Hawes, Gary. Southeast Asian Capitalists. Chapter Title: Marcos, His Cronies, and the Philippines’ Failure to Develop. Cornell University Press, Southeast Asia Program Publications at Cornell University. (1992)
governments and attracted support from international banks.\textsuperscript{35} And yet, in spite of these competitive advantages and improvements (e.g. abundant natural resources, economic advisers, investor confidence, and external support), what actually happened during Marcos’ rule deviated far from this prediction of economic success.

Marcos’ rule, similar to Suharto’s, also consisted of a battle for attention between interest groups. There was an ongoing conflict between the technocrats, the crony capitalists, and even his wife, Imelda Marcos. But in the Philippines’ case, his cronies won triumphantly. While Suharto’s economic advisers, to an extent, fended off the cronies and remained true to its unified, outward looking economic perspective, Marcos’ economic advisers completely lost. Eventually, “Key technocrats lost jobs or confidence. Melchor was fired; Paterno quit, Virata moved to Washington.”\textsuperscript{36} Crony capitalism had taken over the Philippines.

Ultimately, the authoritarian leadership in both Indonesia and the Philippines became a breeding ground for corruption. However, as mentioned previously, even in corrupt environments, economic efficiency matters, and the Filipino economy was much less efficient. The quality of leadership and resulting policy decisions in both of these cases acts as the precursor/ seed for the other four common characteristics (or lack thereof) of high, sustained economic growth. This paper will dissect the contrast of economic efficiencies and inefficiencies between Indonesia and the Philippines that were responsible for such a divergence in growth.

\textsuperscript{36} Ibid
B. Openness to Globalization:

Sustained growth at high levels has only been possible since the 1950s due to countries’ ability to capitalize on the global economy. There are two ways in which high-growth countries have done this. First, “they imported ideas, technology, and know-how from the rest of the world.”37 Second, “they exploited global demand, which provided a deep, elastic market for their goods.”38 As a developing economy, it is easier to imitate ideas and practices that have previously worked well compared to creating something new. Naturally, developing economies also have unique comparative advantages versus developed economies (e.g. cheaper labor), making it economically beneficial to engage in trade. In the case of Suharto’s Indonesia, the country benefitted from both of these global approaches.

Foreign direct investment played a crucial role in Indonesia’s economic development. One of the first steps towards high growth came in 1967 when the New Order passed a new investment law welcoming back foreign investors.39 Additionally, the government returned assets to foreign owners that had been nationalized under Indonesia’s previous president, Sukarno. This reform convinced foreign creditors to restructure massive debt burdens. Between 1966 and 1973, the New Order received over $4 billion in foreign aid as well as $2.6 billion in foreign investment capital. In addition to critical foreign investment, the New Order’s decision to open up to foreign demand turned over a new leaf for the economy. One of Indonesia’s competitive advantages is its abundance of natural resources, most importantly its large oil reserves. While Indonesia’s political predecessors chose to protect its reserves from “foreign

38 Ibid
exploitation,” the New Order welcomed it.\textsuperscript{40} With high domestic production as well as high domestic and world prices at the time, gross earnings between 1968 and 1974 increased from $235 million to approximately $4.5 billion, enough to finance national development.\textsuperscript{41}

Based on this information, it may be easy then to assume perhaps the economic success period of Indonesia was actually driven by its large oil reserves (a resource most countries are not gifted with), and not necessarily by the effective leadership of Suharto’s New Order. However, other factors were at play. It is true Indonesia’s GDP growth coincided with one with of the largest oil booms in modern history (price per barrel increased from roughly $21 in 1970 to $124 in 1980).\textsuperscript{42} But even when oil prices plummeted, Indonesia’s GDP continued to increase.

Figure 3:

![Oil Historical Price Chart](https://www.macrotrends.net/1369/crude-oil-price-history-chart)

The technocrats saw Indonesia’s dependence on oil reserves as an economic weakness. Fortunately, Indonesia had another competitive advantage, which was a lower cost environment

\textsuperscript{40} Ibid
\textsuperscript{41} Ibid
\textsuperscript{42} Macrotrends, accessible at https://www.macrotrends.net/1369/crude-oil-price-history-chart
for basic manufacturing, especially as costs rose in Japan, South Korea, Taiwan, and Hong Kong. Companies were moving operations into Indonesia. However, up until the late 1970s, foreigners still encountered many impediments, which included barred entry to entire sectors, license requirements, and non-tariff barriers. As long as oil prices remained high, these barriers were not as problematic, but it still made the economy extremely vulnerable. If oil prices plummeted, so would a significant portion of Indonesia’s trade revenue, which is why it was essential for Wardhana and Widjojo to illustrate to Suharto the economic severity of the situation. During this crucial period Suharto, at the expense of his cronies’ business interests, made the personally difficult and economically beneficial decision to listen to his technocrats' advice on shifting the economy away from dependence on oil exports.

The surrounding years can be considered a period of Indonesian diversification and deregulation in the midst of what became known globally as the “the 1980s Oil Glut.” Oil prices crashed as a result of increased supply and decreased demand. Beginning in 1983, the New Order implemented several economic reforms. They “deregulated Indonesia’s financial sector to strengthen banks and capital markets.” They also improved trade conditions and focused on low-wage and low-technology industries such as textiles. As a whole, exporters could now bypass import monopolies on raw materials. Additionally, the New Order even terminated a plastics import monopoly that involved two of Suharto’s sons as partners.

Regarding investment, they “raised ceilings on foreign ownership in local operations, especially

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44 Ibid
in export industries, granted foreign firms tax breaks and access to special credit schemes, and lifted restrictions on foreign investment in specific sectors." As a result of these reforms, Indonesia continued on its path of economic growth. In approximately a decade, foreign investment increased twenty-four fold and between 1985 and 1996, non-oil exports increased 650 percent.

However, the process of the technocrats achieving economic efficiency was not one without conflict. One individual who stood in direct opposition was Habibie, an engineer and chief of the nationalist faction who was a long-time friend of Suharto. Rather than capitalizing on global demand and utilizing Indonesia’s cheap labor, Habibie wanted Indonesia to focus on industrial policy and high-technology — following the “Picking Winners” models of other economic success stories such as Japan and South Korea, but this time with an even more prominent state role. In 1974, Suharto made Habibie the chief of the advanced technology division of the state oil company, Pertamina. By 1978, although Pertamina had defaulted on foreign debt, Suharto promoted Habibie to minister for research and technology. This position allowed Habibie to manage a governmental conglomerate of ten firms backed by “nearly limitless government funds.” Industries included armaments, telecommunications, steel, and heavy equipment. His planning commission for high-technology industries competed with the technocrats’ planning board. The technocrats “believed the high-tech industries favored by Habibie were far too advanced for a country just beginning to feed itself, nor were they comfortable with the state taking the primary role in building these industries.”

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49 Ibid
50 Ibid
51 Ibid
52 Ibid
53 Ibid
Wardhana used their influence to block some of these initiatives. However, because of Habibie’s unique friendship with Suharto, several of Habibie’s inefficient megaprojects were adopted. The most notable of these was Habibie’s controversial passion project: Industri Pesawat Terbang Nusantera (IPTN), a state company aimed at developing Indonesia’s own aircraft, which spanned multiple decades and cost over $2 billion in public funds.\(^\text{54}\)

Despite nationalist sentiment and proposals from individuals such as Habibie throughout Suharto’s rule, the technocrats still did enough to set Indonesia en route to sustained, high growth. Ultimately, it was during times of crisis that Suharto listened to them and adopted their outward policies. Because of this, Indonesia reduced its dependency on oil, effectively exploited global demand, and attracted foreign investment, making itself reasonably constrained to the necessary economic characteristic of openness to globalization.

Unlike Suharto and Indonesia, Marcos was unsuccessful in adhering to this characteristic of development. Marcos had initially promised to attract foreign investors and encourage exports over existing import substitution trade policies.\(^\text{55}\) However, the Philippines under the majority of his rule did not effectively import ideas/technology, nor exploit global demand. Even though Marcos’ regime reduced tariffs, that action was counteracted by quotas, licenses, customs practices, and tax harassment. An overvalued peso also made exports more expensive for other countries.\(^\text{56}\) Eventually, Marcos even raised tariffs for certain industries, and overall, high levels of protectionism remained in place. Despite the economic inefficiency in all of this, Marcos

\(^{56}\) Ibid
enacted these measures to protect his cronies and their businesses. By the late 1970s, the Philippines’ GDP growth rate began to slow.

While labor costs were rising in Japan, South Korea, Taiwan, and Hong Kong, Marcos had the ability to capitalize on this opportunity and make it more accessible for foreign companies to pursue operations in the Philippines. This could have provided labor-intensive employment opportunities for the Filipino population and lined up with the country’s comparative advantage of cheaper labor costs. Instead, the “New Society” focused on capital-intensive industries such as nuclear power, steel, aluminum, and copper — comprising eleven major industrial projects.\textsuperscript{57} These projects were justified by nationalist rhetoric and dependence theory: the notion that “the Marcos regime would relieve the oppressed Filipino people of their excessive dependence on imperialist Western corporations.”\textsuperscript{58} This was very similar to Habibie’s nationalist perspective in Indonesia. Even liberal academic and media elite accepted this justification.\textsuperscript{59} However, not only was this method unsustainable, but it also spawned further corruption (which will be expanded upon in the market allocation and macroeconomic stability sections).

While the Philippines did not properly capitalize on its labor advantage and focus on manufacturing through low-wage and low-technology industries like Indonesia, it did make use of its natural resources. Although the country was not gifted with oil, it was still rich with other commodities such as coconuts, sugar, and copper. It even held 60% of the world’s coconut oil market.\textsuperscript{60} Part of the Philippines’ growth immediately after the declaration of martial law can be

\textsuperscript{57} Ibid
\textsuperscript{58} Ibid
\textsuperscript{59} Ibid
\textsuperscript{60} Ibid
attributed to a commodity boom, as prices of coconuts and sugar increased.\(^6\) The issue, however, was the economy depended on these resources, which made it vulnerable. Filipino economist, Arsenio Balisacan explains that “it is often asserted that, at critical junctures in Philippine history, there has been an awful lot of bad luck, or at least unfortunate timing.”\(^6\) Part of what he is referring to is the negative trade shock the Philippines experienced during Marcos’ rule. When the “1980s Oil Glut” occurred, it was not just oil prices that dropped, but also commodities. Sugar and coconut prices plummeted between 1974-1975 and 1980-1981, respectively, and oil prices rose between 1978-1979 (See Figure 4).\(^6\) While these economic shocks were unavoidable, economic mismanagement and poor policymaking amplified their impact. In essence, the Philippines and Indonesia both had “bad luck.” But while Suharto effectively diversified the economy away from commodity dependence (in this case, oil), Marcos did not. As a result, Indonesia avoided a crisis while the Philippines did not.

**Figure 4:**

[![Sugar Historical Price Chart](chart.jpg)](chart.jpg)

Source: *Macrotrends*

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\(^6\) Ibid
Copper Historical Price

Source: Macrotrends
C. Future Orientation:

An economy that is future-oriented involves high rates of savings and investment, especially public investment in infrastructure. The objective is for an economy to forgo “consumption in the present in pursuit of a higher level income in the future.”

Figure 5:

Figure 5 displays the savings rates of Indonesia and the Philippines during the years which Suharto and Marcos ruled. Surprisingly, Indonesia’s average savings rate under Suharto was virtually the same as that of the Philippines under Marcos (23.9% vs. 24.0% respectively). In Suharto’s case, however, as Indonesia recovered from its bankrupt situation in the late 1960s, the savings rate increased significantly until the mid 1970s, eventually reaching similar levels to the Philippines until the Philippines’ savings rate dips. Meanwhile, the savings rate under Marcos was relatively more consistent.

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65 Ibid
66 World Bank
A major difference, however, between these leader’s respective economic positions on future orientation, was public investment as well as other long-term reforms. Despite Marcos’ rejection to properly opening up to the global economy, the beginning of his martial rule consisted of long-term investments and other proposals that were initially promising. This included substantial investments to expand infrastructure and improving laws on taxation.\textsuperscript{67} Even the World Bank strongly supported his projects and policies.\textsuperscript{68} Perhaps Marcos’ most significant initiative was that he addressed the Philippines’ deeply rooted issues of its land ownership system that greatly favored oligarchical elites over common Filipinos. He implemented more land reform than what had occurred in the prior two decades.\textsuperscript{69} Further reforms included “roads, subsidized credit for farmers, rural electrification, and irrigation [which] led to a boom in rice production and to near self-sufficiency in rice by 1976.” (Suharto did not achieve self-sufficiency in rice until 1984).\textsuperscript{70,71} All of these changes suggested a bright future for the Philippines.

These economic accomplishments, however, were only temporary. As already stated, by the late 1970s, the Philippines’ GDP growth rate began to slow, but inward-looking policies and an overvalued peso are not the only explanations. Rice self-sufficiency and rice exports eventually failed (while Suharto’s agricultural/rice reforms achieved great success).\textsuperscript{72,73} Additionally, corruption and red tape took a toll on these other initially promising reforms. While the Ministry of Agrarian Reform announced growing issuances of Certificates of Land Transfer,

\textsuperscript{68} Ibid
\textsuperscript{69} Ibid
\textsuperscript{70} Ibid
the certificates were stored in a safe rather than being given to the actual tenants.\textsuperscript{74} In fact, “only 10% of tenants made payments on the government loans received to purchase their land.”\textsuperscript{75} Common Filipinos eventually sold land back to landlords illegally. Additionally, many of Marcos’ cronies became wealthy by accumulating land for businesses.

Infrastructure failures also damaged the overall economy. For example, “the power industry greatly reduced planning and investment for the future.”\textsuperscript{76} This led to an extensive shortage of capacity and caused nearly daily power failures throughout the Philippines.\textsuperscript{77} Additionally, “Enraged at the efforts of an American phone company to comply with U.S. anti-corruption laws, the regime turned instead to vastly inferior European equipment, thereby worsening the unreliability of the national telephone system for the ensuing decade.”\textsuperscript{78} According to economist Emmanuel Dios, a majority of the construction projects, “both in the private and public sectors… were not very productive and many were outright wasteful.”\textsuperscript{79} These projects were often vehicles for private gain (which will be discussed in the macroeconomic stability section). Savings and investment rates also did not match up throughout the second half of the 1970s. Government and private construction expenditures (with the majority coming from government finances) quadrupled as savings remained fairly constant.\textsuperscript{80}

There were key differences between Marcos’ and Suharto’s investment priorities and budgets. Notably, while Suharto’s rule saw access to education and healthcare improve dramatically, Marcos shifted budget allocations away from social services as a whole (which

\textsuperscript{75} Ibid
\textsuperscript{76} Ibid
\textsuperscript{77} Ibid
\textsuperscript{78} Ibid
\textsuperscript{80} Ibid
included education, health, and housing and saw a decrease from 44% in 1965 to 23% in 1972). 81,82 Education and health are two other forms of public investment that Spence and the Growth Report identify as crucial policy ingredients that fall under the characteristic of future orientation. Ultimately, although initially hopeful, Marcos’ management of investments was not nearly adequate enough to ensure a proper future-oriented economy for the Philippines.

D. Market Allocation of Resources:

Market allocation refers to the presence of a functioning market system. This includes price signals, decentralized decision making, and incentives to supply whatever is in demand.\(^{83}\) Private businesses will compete in an effort to gain market share. However, these functions become distorted in the presence of government-supported monopolies. In both the cases of Indonesia and the Philippines, the presence of large monopolies greatly hindered proper market allocation and therefore reduced economic efficiency. Thus, Indonesia under Suharto, did not become one of thirteen countries in the post-WWII era to achieve high sustained growth for 25+ years as a result of a *highly* competitive free market, but rather did so often in spite of significant market distortions. Both Marcos and Suharto granted their respective cronies with privileged access to certain industries. Neither group of technocrats supported this, but more often than not, they were unable to persuade their leaders otherwise (with Marcos being particularly obstinate).

Macros controlled various sectors of the Filipino economy through his cronies. This included Edward Conjuango: “The Coconut King,” Antonio Floriendo: “The Banana King,” Herminio Disini: “The Tobacco King,” Jose Campos: “The Pharmaceutical King,” and Roberto Benedicto: “The Sugar King.”\(^{84}\) While taking a percentage of earnings, Marcos would economically protect each of them. For example, he made Conjuango the head of the Philippine Coconut Authority and gave him near-monopoly access to coconut oil exports.\(^{85}\) He gave Floriendo a region of land that was formally a prison camp to grow bananas.\(^{86}\) For his crony Disini, Marcos “impos[ed] a 100 percent duty on imported materials used by Disini’s

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\(^{84}\) Crewdson, John. “Marcos Graft Staggering.”

\(^{85}\) Ibid

\(^{86}\) Ibid
competitors in the cigarette filter business, but not on those imported by Disini himself.87

Marcos granted Campos, the godfather of his children, exclusive import licenses for his pharmaceutical company.88 Internationally, the U.S. and other foreign firms were required to pay the cronies “in return for licenses and contracts to do business in the Philippines.”89 These are only some of the practices in which Marcos distorted Filipino markets for personal gain.

Suharto, through his own set of cronies, also manipulated several industries in the Indonesian economy. One crony who was particularly troubling was Mohamad “Bob” Hasan. Suharto gave him substantial control of the plywood/timber industry, leading to the government raising export taxes on logs and eventually banning exports altogether.90 Further policy decisions transformed Hasan’s Indonesian Wood Panel Producers Association (Apkindo) into a cartel to “minimize competition and stabilize prices.”91 He would then share the profits with Suharto and military interests. These initiatives would also occur within other sectors of the Indonesian economy where cronies and their massive business empires gave rise to a “lack of transparency, corruption, and nepotism.”92

Suharto’s cronies even included members of his own family. This dynamic became particularly damaging for the economy when Suharto’s children grew older and pursued their own business interests. Suharto granted them “special licenses, monopoly rights, [and] choice contracts from governments firms.”93 Family stakes included “insurance, sugar, plywood, toll road, milk powder, baby food, television broadcasting, and cooking oil ventures.”94 One

87 Ibid
88 Ibid
89 Ibid
91 Ibid
92 Ibid
93 Ibid
94 Ibid
prominent example involves Suharto’s son, Tommy Suharto who, “secured a monopoly from the government on the distribution of cloves.”95 His plan was to sell cloves to cigarette companies at inflated prices. He promised to pay farmers significantly above-market prices for their crop and ended up distorting the market. Rather than purchasing from Tommy, cigarette companies used existing stocks to avoid being overcharged. But Indonesian farmers had already grown large clove supplies.96 Consequently, Tommy’s business failed, and the farmers ended up bearing the brunt of this type of crony capitalism.

One may allude to other models where elements of corruption have coexisted with substantial business growth. Within the story of the “Asian Miracle,” some economies have actually benefitted from leaders and governments showing nepotism towards certain individuals and corporations. One notable example can be found in the authoritarian regime of South Korea under the leadership of Park Chung-hee. His regime gave rise to the Chaebol: large (mostly family-run) conglomerates that received privileged perks from the government and even Park Chung-hee himself.97 But while Suharto’s and Marcos’ business relationships are often negatively referred to as “crony capitalism,” nepotism under Park has often been viewed in a much more positive light (i.e. “state-run capitalism”). Ostensibly, several of these leaders’ practices towards companies sound very similar: easy access to capital, tax exemptions, and other protectionist measures. However, there were two major differences between Park Chung-hee’s and Marcos’/Suharto’s mentalities: 1) the promotion of competition and 2) the variance in standards. Park placed an emphasis on quality to the point where Korean companies had to compete internationally. Often if a company’s performance was not up to his standards, he would

95 Ibid
96 Ibid
97 Albert, Eleanor. “South Korea’s Chaebol Challenge” https://www.cfr.org/backgrounder/south-koreas-chaebol-challenge
cut funding. The same cannot be said for Marcos or Suharto. They both tolerated such inefficiencies for either personal or familial gain and did not demand cronies to properly compete on a global level, consequently leaving no incentive to innovate.

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E. Macroeconomic Stability:

It is not possible for an economy to maintain sustained high growth if it is not macroeconomically stable. That is why it is important for an economy to prevent volatile fluctuations in exchange rates, interest rates, and tax burdens. Controlled inflation rates and responsible fiscal spending also contribute to macroeconomic stability. While some high-growth economies at times experienced moderately high inflation (e.g. South Korea and China), prices were “stable enough not to scramble market signals, cloud the view of long-term investors, or deter savers from entrusting their wealth to banks.”99 Additionally, a government can still accumulate debt and be considered fiscally responsible, as long as public spending does not get out of control.

Figure 6:
Figure 6 displays the inflation rates of Indonesia and the Philippines during the years which Suharto and Marcos ruled. Surprisingly, neither inflation rate is ideal. Both are significantly higher than the general consensus that inflation rates should remain in the single digits.\textsuperscript{100} In fact, Indonesia’s average inflation rate under Suharto was actually higher than that of the Philippines under Marcos (17\% vs. 13\%). However, a major difference was Suharto’s regime maintained consistency over a longer period than Marcos’. As noted earlier though, Suharto inherited a bankrupt economy; Marcos did not. Prior to the beginning of his official term in 1968, inflation rates were extraordinarily high: 307\% in 1965, 1135\% in 1966, and 106\% in 1967 (years prior to 1967 are not displayed in the figure to prevent large visual distortions).\textsuperscript{101} After the New Order implemented a new investment law in 1967 (as previously mentioned), not only did foreign direct investment increase, but inflation rates were brought down to a more controllable level. From that point onwards, Indonesia’s inflation rates remained relatively consistent.

One major similarity between the inflation rates of both economies is both the Suharto and Marcos regimes reached high levels and variance of inflation by the end of their respective rules (1998 and 1986, respectively). These were indeed periods of macroeconomic instability that occurred during the Asian Financial Crisis and People Power Revolution, respectively (this will be further expanded upon).

Fiscal policy under Marcos was not only extremely corrupt, but also reckless. One of his first measures during martial law was removing the ceiling of public indebtedness that the Philippine Parliament had originally established.\textsuperscript{102} Consequently, the amount of debt Marcos

\textsuperscript{100} Ibid
\textsuperscript{101} World Bank, accessible at https://data.worldbank.org
borrowed during his presidency was unprecedented for the Philippines and was even more damaging because he used the proceeds inefficiently. External debt rose from approximately $1 billion in 1972 to $26 billion in 1984.\textsuperscript{103} Marcos used the 11 major capital-intensive industrial projects to permit such large foreign borrowings, from which he siphoned off much of into Swiss bank accounts.\textsuperscript{104} The borrowing did not end there. In addition to sponsoring his cronies’ business projects, Marcos used debt to finance activities and investments that did not even appear practical on paper. This included “massive expenditures on hotels (estimated at $300 million),\textsuperscript{105} showcase cultural projects, and expensive international assemblages, ironically including an annual meeting of the International Monetary Fund where every delegate was assigned a brand new Mercedes Benz that was sold as a used car after the meeting.”\textsuperscript{106}

Throughout Marcos’ leadership, his wife, Imelda Marcos, also had considerable influence on the Filipino economy. She held 14 major positions in government office and controlled 50% of the total government budget.\textsuperscript{107} She used this budget for even more extravagant purchases including $300 million worth of New York Real estate, $21 million worth of jewelry, and 3,000 pairs of shoes.\textsuperscript{108,109,110} Imelda also created private foundations in Switzerland to hide stolen funds.\textsuperscript{108,109,110}

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Outside of her inefficient infrastructure expenditures on “beautification” and cultural projects (also using borrowed funds), she even selected an island to ship exotic animals from Africa and start her own personal safari (and in the process displaced 254 Filipino families). Ultimately, Marcos can also be held responsible for Imelda’s corruption and mismanagement of the Filipino economy since he gave her these governing positions in the first place.

A proxy that effectively emphasizes the inefficiency during the Marcos regime is the incremental capital output ratio. This ratio explains the relationship between investment and national output.

**Table 2:**

<table>
<thead>
<tr>
<th>Country</th>
<th>Ratio</th>
</tr>
</thead>
<tbody>
<tr>
<td>South Korea</td>
<td>3</td>
</tr>
<tr>
<td>Malaysia</td>
<td>4</td>
</tr>
<tr>
<td>Thailand</td>
<td>4</td>
</tr>
<tr>
<td>Indonesia</td>
<td>5.25</td>
</tr>
<tr>
<td>Philippines</td>
<td>9</td>
</tr>
</tbody>
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Despite corruption and inefficiencies under both Marcos and Suharto, based on these estimates, Indonesian investment spending was still nearly twice as efficient as the Philippines. Ultimately,

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112 Pascual, Jam. “Remember Calauit? The new Imelda docu takes us back to one of the Marcoses’ absurd legacies” https://news.abs-cbn.com/ancx/culture/spotlight/01/31/20/remember-calauit-the-new-imelda-docu-takes-us-back-to-one-of-the-marcoses-absurd-legacies
Marcos’ debt-driven practices crippled the Philippines’ economy because he did not use the debt efficiently.

The financial system was another instability within the Filipino economy. While Suharto decided to reform the banking system in the 1980s in the midst of his diversification policies, the banking system in the Philippines collapsed. Coupled with a plummet in commodity prices, this combination took a toll on the Philippines’ economy. International lenders were already worried about the financial condition of the Philippines as growth rates and exports were not keeping up with these large increases in debt.113,114 The banking collapse began with one of Marcos’ cronies, Dewey Dee, a “banking and textile tycoon,” who fled the Philippines with approximately $83 million in debt.115 These debts were divided amongst “sixteen commercial banks, twelve investment houses, and seventeen other financial institutions”116 It was more the action itself than the amount of money that created a domino effect of a crisis in confidence and led to a widespread bank-run.117 Despite the worsening situation, “Marcos insisted that the banking system remained sound despite ‘defalcations by some individual bankers.’”118

Other extremely leveraged crony-associated firms experienced their own financial crises, but the government bailed them out. Jaime Ongpin, president of a major mining firm, criticized the government saying they were “throwing good money after bad” and called the bailout “the most the most obscene, brazen and disgraceful misallocation of taxpayers’ money in the history of the Philippines.”119 Capital flight also followed. During this time, the Central Bank even

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115 Ibid
117 Ibid
118 Ibid
119 Ibid
overstated its foreign reserves to reassure foreign investors and lenders. By 1983, the banking crisis peaked. Many businessmen (who were not cronies), and even the Catholic Church actively criticized Marcos’ crony policies.

3. The Fall of Marcos:

The 1980s crisis in the Philippines was just as political as it was economic. During this period, Marcos’ health was deteriorating. Exiled former Senator, Benigno Aquino Jr., Marcos’ long-time political opponent, saw the economic and political uncertainty as an opportunity to return to the Philippines from the U.S. in pursuit of becoming the next president. On August 21, 1983, upon exiting the airplane at Manila Airport, Aquino was gunned down immediately. Although never officially confirmed, Aquino’s assassination is widely believed to be connected to the Marcos regime. The impact of Aquino’s assassination was immense, as it “sparked outrage and led to civil unrest.” Support for the Marcos administration was truly waning.

The Filipino economy also continued to deteriorate. Investors relocated operations to other parts of Asia. Financing institutions closed credit lines to the Philippines, and the government could not service its debt. Businesses shut down. Unemployment and underemployment rose and inflation also skyrocketed. GDP per capita for 1984 and 1985

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125 Ibid
126 Ibid
127 Ibid
declined by 10%, respectively. The Philippines’ GDP per capita would not fully recover until 2004 (See Figure 1).

In 1986, Corazon Aquino, Senator Benigno Aquino’s widow, ran against Marcos for the presidency. While Marcos had successfully rigged elections in the past, this time he failed. His regime lost all of its credibility (and to an extent, even internally), and citizens revolted against the failed election process. Corazon Aquino and two million Filipinos (including members of the church and military) flocked to the streets in a nonviolent revolutionary event that is now known as “The People Power Revolution.”128 Marcos was forced to flee and democracy returned to the Philippines as the country transitioned to the new Aquino Administration.

4. The Fall of Suharto:

This comparative growth story between the Philippines and Indonesia would be incomplete if it did not also address the eventual downfall of Suharto. Although Suharto’s Indonesia experienced 30 years of virtually uninterrupted growth, it all came to an abrupt end during the 1997 Asian Financial Crisis. The Asian Financial Crisis began with the collapse of the Thai Baht and caused a ripple effect throughout other Asian economies as speculators abandoned currencies throughout the region. Indonesia was hit the hardest.129

In response to the crisis, Suharto initially resorted to his technocrats. Although they recommended a reform package, Suharto rejected it (deviating from his traditional pattern of listening to his technocrats during times of crisis). During this time, Indonesian companies also “collectively owed approximately $80 billion in corporate debt to foreign banks.”130

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130 Murphy, Ann Marie. “Indonesia and Globalization.” Asian Perspective, Vol. 23, No. 4, Special Issue on Globalization in East Asia (1999), 229-259
to the currency drop, they bought dollars to repay this debt, which consequently made the Indonesian rupiah decline even further.

Indonesia had to turn to the IMF to restore market confidence. Chief technocrat Widjojo oversaw negotiations and by the end of October, the technocrats and the IMF agreed on a reform package.\textsuperscript{131} This package had several requirements including “cutting the budget, liberalizing trade, ending certain monopolies, and liquidating certain banks.”\textsuperscript{132} Suharto signed the agreement, but he did not actually listen. For example, instead of keeping certain banks closed, he reopened two banks that had ties to his family. To make matters worse, on January 6, 1998, “Indonesia presented a budget based upon assumptions many considered unrealistic” and observers interpreted this as Suharto’s “unwilling[ness] to respond effectively to the crisis.”\textsuperscript{133} As a result, investors abandoned Indonesian assets and the rupiah lost half its value in five days.\textsuperscript{134} Even U.S. president Clinton called Suharto to urge him to adhere to IMF reforms. Although Suharto finally signed a second letter of intent, further problems ensued.

During the crisis, Suharto announced his intention to serve a seventh five-year term and chose nationalist, Habibie, as his potential vice president. Markets reacted negatively to the potential influence of Habibie (whose inward-looking proposals were constantly at odds with the technocrats), and the rupiah dropped even further.\textsuperscript{135} Despite objections from the IMF, Suharto maintained his loyalty to Habibie as vice president. Even though Suharto had the opportunity to restore global confidence by selecting other proper advisors to his new cabinet, he instead chose

\textsuperscript{132} Ibid
\textsuperscript{133} Murphy, Ann Marie. “Indonesia and Globalization.” \textit{Asian Perspective}, Vol. 23, No. 4, Special Issue on Globalization in East Asia (1999), 229-259
\textsuperscript{134} Ibid
\textsuperscript{135} Ibid
family and cronyism. Suharto appointed his daughter as Minister of Social affairs and Mohamad “Bob” Hasan as Minister of Trade and Industry, which caused further criticism.\textsuperscript{136}

The economic crisis evolved into a political crisis. Amidst rising inflation and unemployment as well as the blatant corruption within the regime, Indonesian citizens blamed Suharto for the crisis and formed expansive protests.\textsuperscript{137} During the protests, “an estimated 150,000 people, mostly Chinese Indonesians and foreigners (including the IMF team), left the country.”\textsuperscript{138} By the end, “1000 Indonesians were dead and thousands of shops and houses were destroyed.”\textsuperscript{139} On May 21, 1998, in response to increasing pressure, Suharto finally resigned.

5. Conclusion:

Although this thesis focuses on an economic comparison between Suharto and Marcos, the magnitude of human rights abuses under both of these regimes should not be ignored. Nevertheless, one cannot explain the differences in economic performance by the notion that morally repugnant leaders were in power. Economically speaking, one leader was worse than the other. As this thesis demonstrates, while corruption and crony capitalism were rampant in both regimes, there was still a remarkable divergence in economic growth between the Philippines and Indonesia. Marcos, unlike Suharto, was unable to constrain the Philippines to remain within reasonable range of the five characteristics for high, sustained growth. He consistently made too many harmful policy decisions that favored himself and the crony capitalists over technocratic advice and the rest of the Filipino economy. On the other hand, although Suharto managed to implement enough key policy ingredients for an extended period of time to constrain Indonesia

\textsuperscript{136} Ibid
\textsuperscript{137} Ibid
\textsuperscript{138} Ibid
\textsuperscript{139} Ibid
to these characteristics, the end of his dictatorship was defined by a major recession. Suharto’s presidency consisted of a mixture of favorable and flawed policy choices due to the ongoing conflicts between the technocrats, the nationalists, and the crony capitalists. But towards the end, even he eventually leaned towards poor policy decisions (against the guidance of his technocrats), which contributed to Indonesia’s economic crisis. While Suharto obviously did not cause the Asian Financial Crisis himself, his decision to favor the nationalists and his cronies/family still amplified its effects on Indonesia and contributed towards the country’s economic downfall.

Nonetheless, there are important lessons attached to this Southeast Asian tale. Perhaps both the Philippines and Indonesia may have had better economic performances with stronger institutions. However, while institutions explain one side of the coin, policies explain the other. Even in corrupt environments, economic efficiency matters and leadership and policy decisions lie at the root of such efficiency. Namely, a leader’s choices between components such as globalization vs. nationalization, free-markets vs. monopolies, present consumption vs. future investment, and stability vs. instability (to note just a few examples) have a major impact on economic growth. While these stories remain in the past, these previous leaders and respective policy choices still have tangible effects on current and even future generations to come.
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