Preface

Reshaping Economic Geography in East Asia illustrates how extensively spatial factors have influenced and informed by growth and development in the region. This study was conceived as a companion volume to and informed by the *World Development Report 2009: Reshaping Economic Geography* (WDR 2009). By providing case studies and illustrative examples and by deepening our understanding of the forces of economic geography in the East Asia region, this work helped to substantiate some of the key concepts in the WDR 2009. There is full consistency in terms of the analytical framework used and broad agreement on how economic geography has influenced growth trends across a diverse range of countries.

As in the WDR 2009, the underlying framework for this volume originates with the body of thought encompassed in the "new economic geography." The new economic geography explains how spatial factors affect production and, in turn, trade and growth patterns (Gill and Kharas 2007). It all starts with the choices that firms make about the location of their activity—that is, the desire to concentrate production in one location so as to enjoy plant-level economies of scale and to be near customers and suppliers to reduce transport costs. Once a market has reached a certain scale, other firms are encouraged to locate there to take advantage of market size, thereby giving rise to "agglomeration economies"—in other words, the advantages of coalescing geographically.

But history also matters. Normally, the existence of a large manufacturing sector gives suppliers an incentive to locate in major commercial centers to take advantage of the larger market and greater potential access, reinforcing the original advantages. Factors of production, however, especially labor, are not mobile between countries in the same way that they are mobile within countries; thus cost structures may drive firms from larger, higher-wage areas to smaller, lower-wage areas both within and across countries. The lower the transport costs that firms face, the less likely firms are to congregate in one major center or in one country.

Changing spatial and production patterns can adversely affect income distribution. Economies of scale are likely to exist in manufacturing and in urban areas but are largely absent in agriculture and in rural areas. If this is true, then it provides an explanation for the persistence of urban-rural wage differences as well as the widening gaps between leading and lagging areas. Indeed, economies of scale may also result in a premium for skilled relative to unskilled workers and thus explain the widening income gaps in relatively open and rapidly growing economies, where innovation is likely to be an important factor shaping growth. This is likely to be the case in the middle-income economies of East Asia today.

As discussed in the WDR 2009, as a country or a region develops, both people and firms tend to concentrate in cities and prosperous areas. The resulting disparities in living standards across space underlie the unevenness of the growth process. While location matters at all stages of development, it matters less in a rich country than in a poor one. While WDR 2009 looks at this issue at three spatial levels—at the international level between countries, at the country level, and at the local level—this volume is largely about country experiences and, within countries, about lagging versus leading regions and cities versus rural areas. This collection of studies focuses on how market forces and government policies influence the concentration of economic activities and the convergence of living standards across locations.

In this volume, the three dimensions of development highlighted in the WDR 2009—density, distance, and division—provide a conceptual framework for the geographic transformations.

- *Density* refers to the geographic "compactness" of economic activity and is measured by the level of output produced, or income generated, per unit of land area. It is thus highly correlated with both employment and population density. This is the defining characteristic of urbanization, and historically there is a very strong correlation between rising concentration of activity and level of development.
- *Distance* refers to the ease or difficulty of moving goods and factors of production between two locations. In this sense, distance is a physical as well as an economic concept. It is not just related to the physical distance between two locations but is also influenced by factors such as the quality and mode of transport and regulatory barriers. The main point is that locations closer to markets have an advantage. While the easiest way to reduce distance is through labor migration, improved connectivity through better transport and communications is also essential.
- *Division* refers mainly to the negative consequences of political borders separating countries and thus restricting the flow of goods, people, services, and ideas. However, division can also mean boundaries and regulatory barriers within countries, which impede the internal movement of factors of production. In our studies, the focus is largely on internal divisions within countries, although two studies discuss how cross-border issues can affect economic and social developments across countries.

For policy makers, the challenge is getting *density* right: fostering the appropriate concentration of economic activities to realize the potential benefits of agglomeration economies. If done well, convergence of living standards between lagging and leading areas and urban and rural areas will occur over time. But the *distance* between concentrated activities is also an important factor, which can be addressed both by favoring the mobility of labor and by reducing transport costs with infrastructure investment. In the process, any artificial or politically driven *division*—due to jurisdictional boundaries, ethnicity, language, or religion—can divide people, hamper economic activities, impede growth, and exacerbate social development.

Reshaping Economic Geography in East Asia also highlights the dramatic urbanization process under way in the region, evidenced by the number of globally recognized "mega cities" (those with populations over 10 million). Seven of the world's 21 mega cities are in East Asia. Cities in East Asia generate about three-quarters of annual output and between a half and two-thirds of exports. Often, much of this is concentrated in one major city: Bangkok. Bangkok accounts for 40 percent of Thailand's gross domestic product (GDP) and Manila for 30 percent. Other major centers such as Guangzhou, Jakarta, Seoul, Shanghai, and Tokyo are seen as driving their economies. East Asian cities have been able to deliver the agglomeration benefits required for growth and are now exceptionally well connected to the global economy. The region, excluding Japan, is home to 16 of the largest 25 seaports in the world and 14 of the largest 25 container ports. Without this improved connectivity, the region's rapid expansion in trade volumes would not have been possible.

This collection of studies is organized in four sections. The first section comprises chapters dealing with the "context and concepts" for this volume. The second deals with Southeast Asia, specifically, the Association of South East Asian Nations (ASEAN) countries, and the third deals with Northeast Asia: China and the Republic of Korea. The fourth section provides an overview of lessons learned. The time perspective for most of the studies spans several decades; in many cases, outcomes and policies can be traced back half a century or more.

Leading off section 1, Nobuaki Hamaguchi provides the regional context in his description of the evolution of East Asia's growth and trade patterns over the past several decades. He surveys the origins of East Asia's success story as depicted first by the "flying geese model," then by "the East Asian miracle," and, more recently, by the "East Asian renaissance," which highlights the rise of regional trade and financial networks and the emergence of China as an important economic player (Gill and Kharas 2007). A common theme is the role of agglomeration economies, the pattern of regional development, and the implications for income distribution at the regional and national levels.

The other papers in section 1 illustrate particular aspects of the three dimensions of the spatial transformations for economic development: density, distance, and division.

In chapter 2, Keijiro Otsuka and Tetsushi Sonobe explore an important facet of density, the agglomeration phenomenon: how do industrial clusters form, and what factors influence the degree and success of the processes involved? Drawing on several country case studies, they examine the pattern of cluster-based industrial development to identify key determinants, notably the role played by innovation. In chapter 3, Akihiko Ohno's study of Lao PDR illustrates some of the complexities that arise when both density and distance affect small, landlocked, low-income countries, where the challenge is connecting isolated clusters of rural artisans (producers) to national and global markets. His solution is the emergence of a special type of trader—the culture broker—who can gain the trust of local artisans but also understands the demands of the external market and thus can overcome the distance factor that hampers development.

In chapter 4, Futoshi Yamauchi, Megumi Muto, Reno Dewina, and Sony Sumaryanto deal with the "distance" factor, explaining how spatial connectivity through improvements in the quality of roads relative to distance to commercial centers can affect incomes in rural villages in Indonesia. Aside from investment in transport infrastructure, the chapter argues that improved education is also important.

In chapter 5, Manu Bhaskaran draws attention to the negative consequences of divisions, highlighting how the largely artificial borders that separate contiguous nations can discourage factor mobility and distort investment choices. In this case, a more coordinated and free flow of labor and investment between Singapore and the southern tip of Malaysia—known as the Iskandar Development Region—could, in theory, convey substantial benefits to both countries. But, not unexpected, overcoming political sensitivities may be the real challenge. In chapter 6, Jonathan Rigg and Chusak Wittayapak illustrate another aspect of the "division" problem. The Greater Mekong subregion straddles six countries, with areas inhabited largely by relatively poor, ethnic minorities and logistically difficult to access but potentially rich in resources. As documented in their chapter, stronger regional cooperation supported by major infrastructure investments is vital to overcoming international barriers, but the potential for social disruptions and the need to compensate losers in the process also need to be considered.

Section 2 deals with the larger countries in Southeast Asia: Indonesia, the Philippines, Thailand, and Vietnam. Section 3 deals with Northeast Asia: China and Korea. These country case studies provide a broad historic overview of how economic geography has been shaping development. The outcome is reflected in the spatial patterns of production, growth, population settlements, and, in many cases, spatially differentiated measures relating to income and access to social services. In all countries, governments have sought to influence the process, and, as proposed in the framework of the WDR 2009, these policies reflect the nature of institutions in providing basic services and influencing market forces, the significance of connective infrastructure, and the impact of spatially targeted incentives.

Section 2 begins with chapter 7, by Dang Kim Son, which documents how rapid growth in a largely agrarian, low-income economy such as Vietnam has created regional disparities. Although all regions have benefited from the country's recent successes, given Vietnam's stage of development, high priority has been—and should continue to be—given to policies designed to improve connectivity across regions and raise rural productivity.

The case of Indonesia's spatial development does not lend itself to easy caricature. In chapter 8, Hall Hill, Budy P. Resosudarmo, and Yogi Vidyattama provide a comprehensive view of the relationship between location and the patterns of growth, population movement, and disparities over the past several decades. Although Jakarta has benefited from being the capital and hence has better connectivity globally, some resource-rich areas have also flourished over time, but more episodically. Indeed, there is no clear natural resource advantage, and Jakarta continues to perform relatively better than other areas. There is a great diversity in social and economic outcomes, and large differences in living standards exist across the major island groups, but progress has been remarkably even overall. Conflict, as expected, is a negative factor. Not explicitly addressed in this or the other Indonesian chapters is whether a large population spread across many islands puts pressures on maintaining more diverse and self-sufficient productive capacities than would be the case otherwise. In chapter 9, Francisco Javier Arze del Granado takes a more in-depth view of how recent fiscal decentralization efforts have affected the spatial pattern of development in Indonesia. It is perhaps too early to reach definitive conclusions, but the initial results suggest that decentralization may be an effective means to improve local service delivery and discourage migration, but it has not made much of a difference in terms of reshaping the location of industrial activity. In chapter 10, Ari Kuncoro analyzes the characteristics of Indonesian industries that the government has encouraged to relocate to less congested areas, to see if agglomeration benefits are derived from localization factors that would favor smaller urban centers—or from urbanization factors that require larger and more diverse urban settings. He finds that, depending on the nature of the industrial subsector, relocating industries to smaller cities can be consistent with market solutions, especially if accompanied by investments that improve transport connectivity.

The cases of the Philippines and Thailand illustrate the importance of economic geography in shaping developmental outcomes, especially the regional dimension of poverty. In chapter 11, Arsenio M. Balisacan, Hal Hill, and Sharon Faye Piza survey the relatively disappointing growth of the Philippines over the past decades. Whether these outcomes reflect a spatial misallocation of public expenditures or a failure to unify national markets and encourage more factor mobility is not yet clear. However, the glaring regional disparities and concentrated pockets of poverty suggest that a sharp increase in infrastructure investments to improve connectivity between the lagging and leading areas is long over due. In chapter 12, Nitinant Wisaweisuan studies Thailand's experience, indicating that a quarter century of rapid growth has resulted in a sharp decline in the number of poor people. Nevertheless, significant regional disparities continue, although some regions appear to be catching up with the more densely settled Greater Bangkok area, in part because of industrialization dynamics linked to globalization.

Section 3 on China and the Republic of Korea begins with chapter 13, and an overview by Yukon Huang and Xubei Luo, of how China has reshaped its economic geography over a quarter of a century to create a more competitive productive structure and, in the process, has experienced major regional disparities. Drawing on the other China studies, the authors analyze the spatial impact of incentive and fiscal policies on investment patterns, industrial agglomeration, and regional growth trends. These policies have had a major distributional impact, as reflected in regional and rural-urban indicators of income and access to social services. In chapter 14, Yang Yao provides a broad sweep of how government policies over the past half century have shifted from decentralization to recentralization in response to historic events. He then relates these shifts to growth and distributional outcomes from a spatial perspective. His analysis provides revealing insights on the factors that have shaped government policies. In chapter 15, Zhao Chen and Ming Lu discuss how agglomeration economies have affected provincial growth rates and, in turn, given rise to rural-urban disparities. They note that more balanced interregional and urban-rural development is needed and that such policies will not necessarily compromise efficiency considerations. In chapter 16, Canfei He provides an in-depth analysis of the impact of agglomeration economies on the geographic clustering of industries. Using a comprehensive database, he shows how the location of industrial activity has shifted over time, with more agglomerated industries locating along the coast and more localized, resource-based, or domestic market–oriented industries expanding in the interior provinces. His findings are reinforced in chapter 17, in which Chong-En Bai and Xu Lin conclude that the spatial pattern of firm-level specialization and competitive pressures are leading to a more efficient industrial structure in China. In chapter 18, Yue-man Yueng and Jianfa Shen show how the three major growth centers of Guangzhou, Shanghai, and Beijing and their related subregions (Pearl River delta, Yangtze River delta, and the Bohai Bay area) have catalyzed China's modernization. In the process, this has triggered rapid urban restructuring and generated major spillover benefits to the surrounding secondary cities and rural areas.

The last chapter in this section (chapter 19), by Sam Ock Park, covers the experience of the Republic of Korea. With a per capita income far exceeding that of other countries (excluding Japan and Singapore), Korea illustrates the other end of the spectrum: how a successful country can transition from developing to developed status and from a low to a high degree of urbanization and, in the process, move from spatial disparity and bipolar concentration of industries to a new spatial division of labor between the core (Seoul) and the rest of the country. In the process, the spatial disparity of incomes and access to social services has been considerably reduced over time.

No region is as diverse as East Asia, endowed with a wide range of incomes and levels of development and with differing cultural and historical precedents. Section 4 contains a concluding chapter by Yukon Huang and Alessandro Magnoli Bocchi, which summarizes the diversity of country experiences, highlighting how the principles underpinning the new economic geography explain remarkably well the developmental experience of most East Asian economies. The "take-home" message is the following: independent of their particular stage in the development process, countries should work with—rather than try to counter—the forces of geography in shaping economic growth and development. Even under ideal circumstances, spatial disparities can be evidence of success rather than failure. But these processes take decades, if not generations, to work through. Policies that focus on making the growth dynamics more inclusive rather than more "balanced" will ultimately lead to outcomes that result not only in higher levels of income but also in more equitable living standards.

Yukon Huang and Alessandro Magnoli Bocchi

References

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