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**SOCIAL CONSEQUENCES OF THE  
FINANCIAL CRISIS IN ASIA**

**The Deeper Crisis**

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## Foreword

The *EDRC Briefing Notes* are developed from notes prepared by staff of the Economics and Development Resource Center to brief Management and the Board of Directors. The *Notes* aim to provide succinct, nontechnical accounts of salient, current policy issues. They are not meant to be in-depth papers, nor intended to contribute to the state of current scientific knowledge. While prepared primarily for Bank readership, the *EDRC Briefing Notes* may be obtained by interested external readers upon request. The *Notes* reflect strictly the views and opinions of the staff and do not reflect Bank policy.

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**T**he Asian financial crisis has quickly led to marked contractions in gross domestic product (GDP) and employment in the affected economies. GDP shrinkages in 1998 ranged from nearly 14 percent in Indonesia to 0.5 percent in the Philippines. In turn, these have resulted in adverse social consequences. Although there are signs that the worst of the financial crisis is over and the crisis economies are getting on the road to recovery, the social impacts continue to unfold. The social crisis is likely to be deeper and can be expected to persist long after the crisis economies return to solid growth.

This note derives from a study that assesses the social impact of the crisis, based on data drawn from available recent surveys, and supplemented by primary information gathered from local communities and households using participatory methods.<sup>1</sup> The countries included in the study are Indonesia, Republic of Korea (Korea), Lao PDR, Malaysia, Philippines, and Thailand. The social impacts of the crisis can be gauged mainly in terms of changes in prices and assets, employment, incomes, income distribution and poverty, education, health, social capital, and environment.

## **SOCIAL IMPACT**

### **Prices and Assets**

The currency devaluations that signalled the onset of the crisis exerted an almost immediate upward pressure on the prices of imported goods and services or goods with a high import content. Inflation was moderated in some cases by government subsidies, price controls, and by additional imports of necessities. In Indonesia, for example, several commodities were subsidized during the crisis (e.g., gasoline, rice, sugar, cooking oil, and fertilizers). Nevertheless,

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<sup>1</sup>This note, based on a regional technical assistance study (RETA 5799), follows the earlier note on an initial assessment of the social impact of the crisis (Pernia and Knowles 1998).

Indonesia's consumer price index jumped to nearly 60 percent in 1998 from 6.6 percent in the previous year. In Lao PDR, inflation hit 90 percent, while in Korea it climbed to 7.5 in 1998 percent from the previous year's 4.5 percent. Since food prices generally increased more rapidly than nonfood prices, the impact of inflation was harsher on the poor, given that food accounts for a dominant share of their consumption. Inflation not only clipped purchasing power but, along with the collapse of stock markets and banks, also drastically reduced the real value of household savings. Inflation and reduction in real incomes effectively spread the cost of labor market adjustment beyond the unemployed workers.

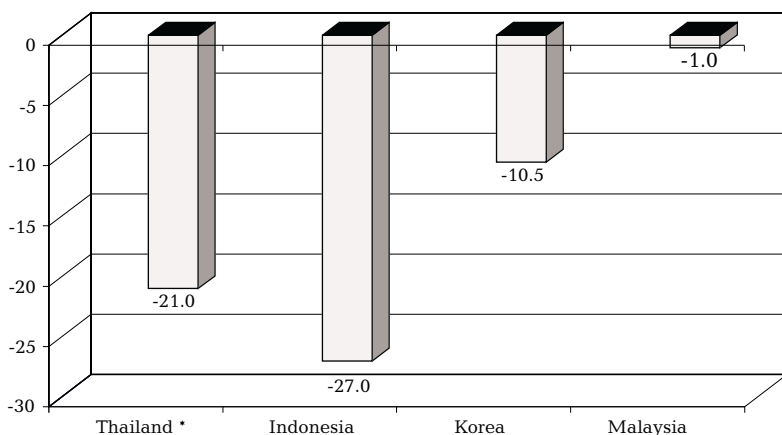
### **Employment and Incomes**

Unemployment rates increased in all countries, with the largest increase recorded in Korea, from 2.3 percent in 1997 to 7.4 percent in 1998. In the Philippines, unemployment rose from 7.9 to 9.6 percent, and in Malaysia, 2.5 to 3.9 percent. However, the unemployment rate can be a misleading indicator of employment effect particularly during a crisis because it does not reflect dropouts from the labor force (also referred to as discouraged workers). In Korea, for example, changes in unemployment rates give the appearance that males were more adversely affected than females (i.e., male unemployment rate increased from 2.8 to 7.7 percent while female unemployment rate increased from 2.3 to 5.6 percent). In fact, female labor force also declined by 3.8 percent while male labor force increased by 1.0 percent (Moon, Lee, and Yoo 1999).

Decreases in real earnings have occurred in all countries and have been more important in labor market adjustment during the crisis than either unemployment or decreases in the number of hours worked (Figure 1). The negative employment and earnings effect has been typically more severe in urban areas than in the countryside.

The construction sector and, to a lesser extent, the manufacturing sector were negatively affected in all countries (Table 1). By contrast, employment increased in the agriculture and service sectors in many countries. In Lao PDR, there is evidence that the steep currency devaluation led to an agricultural boom, with Lao

**Figure 1. Percentage Changes in Real Earnings per Worker, 1997-98**



\*Wet season (August).

Sources: Pongsapich and Brimble (1999), Sigit and Surbakti (1999), Moon et al. (1999), and Piei (1999).

farmers exporting large quantities of their relatively inexpensive produce to Thailand through informal channels (Chamberlain 1999). The informal sector share of total employment increased in Indonesia and Korea, but it decreased in Thailand.

The gender employment impact of the crisis is not completely clear. Although women fared significantly worse in Korea, and probably also in Thailand and the Philippines, the picture is mixed in the other countries. In Indonesia, for example, the female unemployment rate increased by 14 percent between 1997 and 1998, compared with a 27 percent increase among males, while female employment increased by 4.2 percent, compared with a 1.7 percent rise among males (Sigit and Surbakti 1999). Nevertheless, these comparisons do not reflect the additional burdens that women continued to carry beyond the workplace.

Youth (ages 15-29) have been most negatively affected by the employment and earnings impact of the crisis. In Korea, employment declined by more than 14 percent among persons ages 15-29, while it declined by less than 1 percent among those ages 30-49 (Moon, Lee, and Yoo 1999). Elderly workers have also been more

**Table 1. Declines in Construction and Manufacturing  
Employment, 1997-98**  
(percent)

<b>Country</b>	<b>Construction</b>	<b>Manufacturing</b>
Korea	-21.3	-13.3
Indonesia	-15.9	-9.8
Malaysia	-13.3	-2.9
Philippines	-7.9	-2.5
Thailand	-34.0	-3.0

Sources: Korea (Moon, Lee, and Yoo 1999); Indonesia (Sigit and Surbakti 1999); Malaysia (Piei, Johan, and Abubakar 1999); Philippines (Reyes, Manasan, Orbeta, and de Guzman 1999); Thailand (Pongsapich and Brimble 1999).

negatively affected in Indonesia and Korea, and probably also in Thailand, but they appear to have fared relatively well in the Philippines. More educated workers have been less hurt by the crisis in Korea, Philippines, and Thailand, while the available evidence is inconclusive in Indonesia.

The number of migrant workers leaving Indonesia increased by 392 percent, and the value of remittances flowing into the country also rose sharply (171 percent) between 1997 and 1998. For the Philippines, departing migrant workers rose by only 1 percent compared with a 13 percent increase in the previous period, while the dollar value of remittances fell by 13 percent. Meanwhile, the predominantly labor-importing countries of Korea, Malaysia, and Thailand used various measures to encourage the repatriation of illegal migrant workers.

Real per capita household income declined by 20 percent in Korea, and by 12 percent in the Philippines between 1997 and 1998. In Indonesia, real per capita household expenditure fell by 24 percent.

It is likely that the crisis has also significantly affected some forms of nonlabor income. Interest income has probably been affected, positively by the steep interest rates used by central banks to stabilize exchange rates, and negatively by the failure of many financial institutions and corporate borrowers to meet interest pay-

ments. Rental income has also probably been reduced by low occupancy rates and by the inability of many tenants to pay their rent. Profits and other forms of business income, which tend to be very sensitive to cyclical fluctuations in business activity, probably also declined sharply.

## **Inequality and Poverty**

Income inequality has increased in some countries. The income share of the rich has increased from 20.5 to 22.5 percent in Thailand, from 22 to 24.5 percent in Korea, and from 39.3 to 42.9 percent in the Philippines. By contrast, in Indonesia, data on changes in household expenditure suggest that the distribution of income has actually improved.

Poverty incidence has also increased in the crisis countries. In Indonesia, poverty increased from 11 in 1996-1997 to 14 percent in 1998-1999; some estimates are as high as 20 percent, but much less than many had predicted. In Korea, the poverty rate more than doubled, from 3 to 7.5 percent.<sup>2</sup>

The intracountry regional distribution of income has been affected by the crisis. In Thailand, metropolitan Bangkok and the central region improved relatively during the crisis while other regions worsened, especially the northeast region. In Indonesia the data clearly indicate that the worst impact of the crisis was in Java, where approximately two thirds of the population live and which was previously relatively prosperous.

## **Education**

Education budgets have been cut in the crisis countries. The exception is Malaysia, where initial steps to reduce education budgets were eventually reversed. Budget cuts have been particularly sharp in Thailand and the Philippines. In Thailand, moreover, there is some evidence that cuts were less in Bangkok than in other parts of the country. Budget cuts have generally spared the personnel line

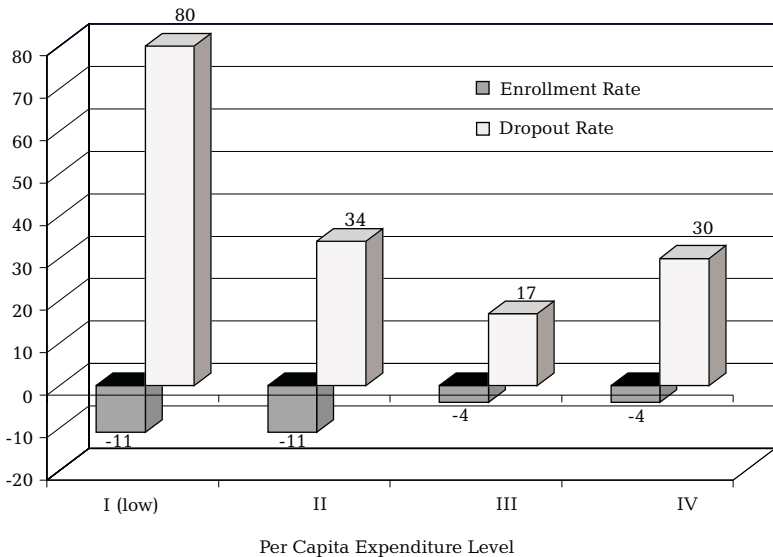
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<sup>2</sup>The poverty line in Korea is a relatively generous \$7 per day. However, the reported estimate is based on a workplace survey of employed urban workers (i.e., it does not include the unemployed or self-employed).

item and have instead fallen mainly on such traditionally under-budgeted line items as teaching materials and maintenance. In addition to budget cuts, schools have had to contend with reductions in off-budget sources of revenue (fees from parents and community contributions).

There is no strong evidence yet that the crisis has led to reduced primary school enrolments. However, it has already had negative effects on secondary school enrolment—particularly among girls and among the poor—in all countries for which data are available (Figure 2). In Korea, moreover, the crisis appears to have had a strong negative impact on kindergarten enrolment, due partly to income effects (kindergarten is often regarded as a luxury) and partly to diminished ability to pay for child care on the part of many women who have lost their jobs. The crisis has led to increased enrolment at the tertiary levels in several countries. This reflects not only reduced employment opportunities among youth but also the availability of crisis-related government scholarship and loan programs, as well as devaluation-induced shifts away from overseas to domestic schools (particularly in Malaysia).

**Figure 2. Percentage Changes in Enrollment and Dropout Rates among Indonesian Children Ages 13-19 (1997-98)**



In paying for their children's schooling, parents have contended with substantial price increases for many items paid for out-of-pocket (fees, uniforms, books and supplies, special activities, transportation, food, and tutoring). Nevertheless, due to falling incomes, private expenditure on schooling has declined (particularly among the poor), with probable adverse effects on learning. In Korea, household expenditure on tutoring declined by 24 percent overall, 39 percent among the lowest income group versus 13 percent among the highest income group.

Rates of entry into grade one and continuation rates from one level to the next have tended to decline more than overall enrolment. Parents who cannot afford to send all of their children to school have opted for withdrawing older children first and for delaying the entry of young children into grade one. Dropout rates have also increased in most countries—more so among boys than girls in Indonesia, Philippines, and Thailand. Besides dropout, absenteeism rose sharply in Korea.

Many children have been shifted from private to public schools (particularly in the Philippines, which has a relatively large private education sector). Absentee rates have increased for a variety of reasons, including skipped meals (many children arrive at school without breakfast or lunch) and the need to walk long distances to school instead of using public transport. Fewer children are participating in extracurricular activities (e.g., the scouting movement in the Philippines) due to the extra cost involved.

## **Health and Family Planning**

Public health budgets in real terms have declined significantly in all countries, except Malaysia. Whereas personnel line items have been protected in most cases, the availability of medicines has decreased noticeably, particularly in Indonesia and the Philippines. In Thailand, particularly Bangkok, public health facilities like education appear not to have experienced budget cuts to the same extent as facilities in other regions. Public health facilities have also contended with steep reductions in off-budget sources of revenue (user fees, charitable and community contributions).

The utilization of public health facilities has increased in all countries except Indonesia, reflecting significant shifts of consumers from relatively expensive private providers to less expensive public health facilities. In Indonesia, however, a combination of drug stockouts and fee increases in many public facilities has resulted in a shift of many consumers from the public sector to the private sector (Sigit and Surbakti 1999).

Household expenditure on health care has declined sharply in real terms in Indonesia, Korea, and Thailand. In Korea (but not in Thailand) the declines have been relatively greater among lower-income groups. Although the cost of medical care has increased more rapidly in some countries than the overall rate of inflation, it appears also that households delay or avoid medical care as one of their coping mechanisms during the crisis. Free health cards have been distributed to many low-income households in Indonesia and Thailand. They appear to have increased utilization in Thailand, but not in Indonesia (where they are viewed with suspicion).

There is no evidence yet that immunization coverage has declined in any country except the Philippines, where government service statistics indicate sharp declines in several regions (Reyes, Manasan, Orbeta, and de Guzman 1999). There are no consistent signs yet of increased malnutrition in any of the national surveys or government service statistics in the study countries; nor is there consistent evidence yet of a worsening in any other health outcomes during the crisis period. However, there are many reasons to believe that such evidence will appear as time goes on. For example, there is already some evidence of micronutrient deficiency in Indonesia, as well as cause for concern about the possible impact of the crisis on already high rates of tuberculosis prevalence in the region.

There is no evidence yet in most of the study countries that the crisis has altered previous trends in the use of contraceptives. However, in Korea contraceptive practice has risen and the demand for counselling services for unwanted pregnancies has gone up by 78 percent, suggesting a direct income effect on fertility (Moon, Lee, and Yoo 1999). On the other hand, in the Philippines, where contraceptive prevalence has continued to decline (particularly in rural areas), modern method use decreased for the first time in 1998, implying a price effect. Data from Korea and Thailand indicate no

changes yet in patterns of prenatal care or professionally attended births. In Indonesia, however, there has been a significant shift away from professionally attended births, particularly in urban areas (Sigit and Surbakti 1999).

## **Social Capital**

The crisis has had varying effects on social capital. Community-based initiatives appear to have flourished in Korea and Thailand, as farmers and women's groups organized to improve their economic and social situations. In Indonesia, traditional practices to help the poorest members of the community prospered in the early part of the crisis, but faltered, along with religious gatherings, as the crisis deepened. Crime rates have increased in Korea, Malaysia, and Thailand, with anecdotal reports of crime rising in the other countries as well.

## **Environment**

Government budgets for environmental protection have declined in Korea and Malaysia since the onset of the crisis, and probably also in the other crisis countries. Peoples' intense quest for additional income during the crisis has placed strains on forest, fishing, and water resources in most of the crisis countries. Although many casual observers have noted reduction in air pollution in capital cities owing to fewer vehicles on the road, the only country study reporting official levels (in Seoul) suggests that there has been no departure from previous trends (Moon, Lee, and Yoo 1999).

## **Especially Disadvantaged Groups**

Although the employment and income impact of the crisis has not been disproportionately heavier on the poor than on other groups, the poor have suffered more from its impact because their low incomes and education provide them with fewer options for coping with the crisis.

Women have had to add income-earning activities to their already heavy work burdens at home and on family farms. Many sold

food and other small items in market centers or as ambulant peddlers in their communities. Others cultivated backyard gardens, harvested forest products, joined fishing fleets, or hired out their services as laundresses or agricultural laborers.

In Korea, additionally, there is evidence that the heightened threat of layoffs has contributed to increased sexual harassment and abuse in the workplace, while increased unemployment among female heads of household has been associated with juvenile delinquency and lower high school continuation rates (Moon, Lee, and Yoo 1999). In Indonesia, declines in school enrolment have also been greater among female children.

There is some indirect evidence that in Indonesia, children have been pulled out of school to work, but not in the other countries. To date, school enrolment changes have been moderate in most countries and/or consistent with precrisis trends, probably owing in part to effective social safety net interventions supported by the ADB and other donors. However, enrolment declines have been slow to develop in earlier crises and have required many years to overcome, so it is too early to be complacent in this regard. Similarly, although there is no evidence yet that the crisis has significantly affected the health of most children, sanguine conclusions may be premature. Unfortunately, there has been an increase in the number of street children and reported child abuse cases in Indonesia, Philippines, and Thailand.

Institutionalized populations—both adults (e.g., the disabled and handicapped, older persons) and children in orphanages and boarding schools designed to serve ethnic minorities from remote areas—have been severely affected by the crisis in Lao PDR and Thailand due to reductions in government budgets, high inflation, and reductions in charitable donations.

Although there is evidence of relatively heavy labor market impact on older persons in Indonesia and Korea (coupled with a loss of independence in Korea), none of the country studies has yielded information on how the crisis may have affected the health of the elderly.

White-collar workers were initially hard-hit by the crisis, but many—particularly the more educated—have fairly easily found other jobs. However, there is evidence that white-collar workers have

displaced less educated or qualified workers in many jobs. The underemployment of overqualified white-collar workers is a significant, though less obvious, social cost of the crisis.

Government workers, whose salaries tend to be inflexible in the short run, have been particularly vulnerable to the crisis in countries experiencing rapid inflation, such as Indonesia and Lao PDR. In other countries, however, they have benefited relatively from higher levels of job security.

Overseas migrants working in other Asian countries have been harmed, both by reductions in employment opportunities and by currency devaluation. On the other hand, migrants working outside the region have benefited both from more stable employment opportunities and from relative currency appreciation.

Urban populations have been more adversely affected by the crisis than have rural populations. The exception is Thailand, where Bangkok appears to have benefited relative to other urban and rural populations.

Some ethnic and religious minorities have been seriously hurt by the crisis, e.g., the ethnic Chinese in Indonesia. However, other ethnic groups less well integrated into the market economy have been relatively isolated from the crisis, e.g., ethnic minorities residing in some of Indonesia's outlying islands, and some hill tribes in Thailand and Lao PDR.

## **RESPONSES TO THE CRISIS**

### **Household Coping Mechanisms**

Households have responded to the crisis in a variety of ways, including altering their consumption and savings behavior, borrowing and selling assets, postponing rental payments and debt repayments, increasing work effort, migrating to other areas or countries to obtain employment, and shifting from private to public providers of social services (Box 1). In most of their coping mechanisms, households have given more emphasis to satisfying current as compared to future needs. Whereas some of these adjustments are unlikely to have any negative long-term effects (e.g., postponing the purchase of consumer durables, substituting cheaper

staples for more expensive foods), others may have deleterious consequences. For example, going into debt, failing to make scheduled debt repayments, or selling productive assets is likely to reduce household resources to meet future needs. Similarly, reductions in health care expenditure may lead to poor health or to higher medical expenses in the future. Taking children out of school either to save money or to free them to work will have serious adverse consequences for the affected children's future lives. Such potentially harmful household coping mechanisms help to explain why an appreciable delay occurs between the economic crisis and its social impact.

### **Box 1. Family Cost-Cutting Measures**

All family members contributed to reducing expenditures. Many had to settle for second-hand clothing, hand-me-downs, and school uniforms left over from the previous year. Members walked long distances to school, work, or the market. They disconnected household appliances and lights to cut down on electricity. Some made a point of attending weddings, birthday parties, religious and other celebrations to take advantage of the better-quality food served. Fishermen slept longer hours in the morning so that their first meal at noon combined breakfast and lunch.

In school, teachers noticed pupils coming to class untidy or not in uniform because their parents could not afford laundry soap, there was no water for washing, or they only had one uniform. Several children did not have snacks at recess or even lunch. A few shared the food brought by their better-off friends. Students could not submit assigned projects for lack of money to purchase materials. Some scavenged paper from waste cans to use in school, or erased and re-used old notebooks and workbooks.

## **Government Responses**

One of government's most important crisis-coping mechanisms involves reallocating its budget, usually shifting funds away from infrastructure investments and national defense to meet more immediate needs, such as the salaries of government personnel,

basic social services and social safety nets, recapitalization of financial institutions, and repayment of foreign debt. Social safety nets have included a varying mix of:

- i) severance pay and restrictions on layoffs;
- ii) unemployment insurance and other forms of assistance to the unemployed;
- iii) job retraining and job creation;
- iv) pensions and provident funds;
- v) income maintenance programs, including public works;
- vi) price controls and subsidies on foods and other essential goods and services; and
- vii) measures designed to ensure continued access to social services for the poor and the unemployed.

Often, governments have sought the assistance of multilateral and bilateral agencies for their social safety net programs. Policy reforms (e.g., shifts to more targeted forms of support) have typically been part of the assistance agreements.

## **CONCLUSION AND IMPLICATIONS**

The Asian financial and economic crisis has already exerted a wide range of negative social impacts in most of the affected countries. The study—underlying this note—based on data collected relatively early in the crisis, documents many of these impacts. Although some are lesser in magnitude than were projected earlier, they are nevertheless significant and alarming when viewed against the backdrop of the sustained socioeconomic progress that preceded the crisis. In addition, there are good reasons to expect that the social crisis, as distinct from the economic crisis, has not yet peaked in severity. There is a danger, therefore, that improving economic

conditions may lull observers into thinking that social conditions have recovered when they may in fact be worsening.

At the same time, the Asian financial crisis provides a unique opportunity to learn how existing social systems function under duress. A clear example is provided by the various governmental programs constituting social safety nets. The crisis has revealed that considerable effort needs to be directed to the setting up or further development of social safety nets throughout the region. This is especially because traditional family systems of support—though resilient during the early part of the crisis—are likely to weaken over time, given continuing socioeconomic change and urbanization, and with further demands placed on them. “Shared poverty”, a common theme of community and household coping mechanisms during the crisis, has its limits.

Fortunately, governments are now more aware of their responsibilities than they were prior to the crisis. They are also more conscious of their weaknesses and constraints than they would have been had the region continued to enjoy the high rates of growth experienced before the crisis. The relatively undeveloped status of most countries' social safety nets provides an opportunity to develop them from the ground up, drawing on the views and “voices of the people”, besides learning from the experiences of other countries.

Despite the urgency of the needs they are designed to address, it is important to evaluate modifications and additions to social safety nets in terms of the standard criteria of efficiency and equity. Do the measures address critical market failures? Do most of the benefits reach the intended target groups? Are distortionary costs minimized? It is clear that some of the measures used currently in the region's social safety nets do not satisfy these criteria (e.g., subsidy of fuel oil). However, there should be no presumption that all the social safety net approaches used in the presently developed countries meet them either. Instead, innovative solutions may be needed to meet Asia's needs in the context of a global economy.

Many of the subsidies currently provided in the region are untargeted and do little to promote equity. Due to the limited funds available, particularly during a crisis, it is important to channel as much as possible to those in need. Although relatively effective, means testing is difficult (though not impossible) where employment

is mostly informal. However, a range of other targeting options is available, including geographic targeting, subsidy of goods and services consumed mainly by the poor, self-targeting, community-based targeting, and various ad hoc methods (e.g., fee-scaling at health clinics). Targeting is more difficult during a crisis because there is much "churning" into and out of the ranks of the poor (Poppele, Sumarto, and Pritchett 1999). A lot of experimentation and careful evaluation are therefore required to develop effective targeting mechanisms for social safety nets.

The crisis has placed heavy strains on public health and school systems, as many people shifted from private to public providers at a time when public budgets were being cut. Facilities became crowded, and quality declined. Consumers have been quick to register their dissatisfaction. In addition, private health providers and private schools have been hard-hit by the crisis. Economies can ill afford to lose what many observers believe are the most efficient providers of social services, and the ones the study shows are most valued by consumers. However, unless governments can find a way to level the playing field for both public and private providers—for example, by making greater use of demand-side instead of supply-side subsidies—future crises are likely to repeat this experience.

The employment impact of the crisis has fallen more heavily on youth, especially females and new entrants into the labor force. Some youth who would otherwise have been unemployed have managed to stay in school, while others who had been laid off have managed to return to school for additional training. Many, however, have been idle and have contributed to social problems (e.g., drugs and prostitution) or political instability. Yet, there is a tremendous need for upgrading the skills of most of the region's workforce—particularly its female workforce. Under these circumstances it would be wise for governments to prepare for future crises by developing training systems that would allow for the maximum number of unemployed youth to obtain additional skills. Scholarships, loans and vouchers should be part of such a program, and plans should be prepared to expand the supply of education and training services quickly, if needed (e.g., perhaps by employing the educated unemployed as temporary teachers).

Crisis monitoring systems are in need of further development in most countries. Existing statistical systems have evolved mainly to meet the needs of long-term planning. They are ill-equipped to provide timely data on the social impact of an economic crisis. Although macroeconomic and employment data are adequate in most countries, reliable data on the utilization of social services, on private expenditure for schooling and health care, and on many schooling and health outcomes tend to be available only at intervals of several years. One clear need is for medium-sized, annual multi-purpose household surveys based on a national, revolving panel sample. Another urgent need is for a community monitoring system that is flexible enough to provide both quantitative and qualitative data on pockets of intense social impact (e.g., urban slums and drought-stricken rural areas). An efficient social monitoring system would help forestall, or at least mitigate, future social crises.

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