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DEVELOPMENT PAPERS NO. 12

CHALLENGES AND OPPORTUNITIES OF RESTRUCTURING THE DEVELOPING ESCAP ECONOMIES IN THE 1990s, WITH SPECIAL REFERENCE TO REGIONAL ECONOMIC COOPERATION

Economic and Social Commission for Asia and the Pacific
Bangkok

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FOREWORD

The Commission at its forty-fifth session considered the theme topic "Restructuring the developing ESCAP economies in the 1990s". In view of the importance of economic restructuring to the developing countries of the Asian and Pacific region and as it would be desirable to extend the secretariat's study on the subject in a number of directions, the Commission decided to continue with the same topic for its forty-sixth session. The Commission also recommended that the secretariat, in undertaking further work on the theme study, should focus on "the challenges and opportunities of the restructuring efforts of the developing ESCAP economies in the 1990s and the need for a conducive international economic environment, especially through enhanced regional cooperation". The present study was prepared in response to this recommendation of the Commission.

In preparing the study, the secretariat was assisted by consultants under a project funded by the United Nations Development Programme. An expert group meeting, the cost of which was partly met through funds made available by the Government of Japan, was also held in December 1989 to review the draft study. The secretariat, in finalizing the study for submission to the Commission, has made every effort to incorporate the many useful suggestions made at that meeting.

The present study builds upon and extends the previous study (ST/ESCAP/879) in three important ways. First, the present study takes a closer look at the major emerging trends in the world economy in the 1990s in order to identify the challenges and opportunities that these present to the developing ESCAP economies. Second, it analyses the main underlying domestic trends in the developing countries of the region and their implications for the restructuring of these economies. Finally, the study examines the role that regional cooperation could play in facilitating the restructuring efforts of these economies.

I wish to express my deep appreciation to the United Nations Development Programme and to the Government of Japan for their generous financial assistance which has been crucial in undertaking the study. I am also very grateful to the distinguished consultants and country experts for the keen interest they have taken and the valuable assistance provided to the secretariat in preparing the study.

The study is being presented on the sole responsibility of the secretariat and the views expressed herein do not reflect those of the Governments of the members and associate members of the Commission or the donors who provided financial support for the study.

S.A.M.S. Kibria
Executive Secretary

April 1991

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INTRODUCTION

At its forty-fifth session, the Commission decided to continue the theme topic "Restructuring the developing ESCAP economies in the 1990s" at its forty-sixth session. It recommended that the primary focus of the work to be undertaken by the secretariat should be on "The challenges and opportunities of the restructuring efforts of the developing ESCAP economies in the 1990s and the need for a conducive international economic environment, especially through enhanced regional cooperation".[1] The present publication has been prepared by the secretariat mainly in implementation of the Commission's recommendation in this regard.

The Commission also recommended that the secretariat should undertake "more in-depth studies of restructuring possibilities in particular groups of economies, especially the least developed and Pacific island countries, as well as, in due course, on socio-economic implications of adjustment policies and programmes and the prospects of sustainable development".[2] The secretariat has implemented the first part of this recommendation in part two of the *Economic and Social Survey of Asia and the Pacific 1989*. A project has been prepared to implement the second part of the recommendation and is awaiting the grant of extrabudgetary funding.

The present publication is a logical extension of the secretariat's earlier study, which has since been revised and published.[3] The present study extends that study in three important ways. First, it takes a more intensive look at the major emerging trends in the international economic environment in the 1990s with a view to identifying the challenges and opportunities that they present to the restructuring efforts of the developing economies of the ESCAP region. Second, the study analyses the major underlying domestic trends in restructuring developing economies of the region and the possibilities and challenges that are inherent in these trends. In particular, it looks at the major impulses for restructuring the different groups of developing economies of the region. Finally, it examines the role that regional cooperation could play in facilitating the restructuring efforts of these economies.

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[1] Report of the Commission on its forty-fifth session (*Official Records of the Economic and Social Council, 1989, Supplement No. 14* (E/1989/33-E/ESCAP/693)), para. 737 (b).

[2] Ibid., para. 737 (c).

[3] *Background Paper: Restructuring the Developing Economies of Asia and the Pacific in the 1990s* (ST/ESCAP/879).

The main thrust of the study concerns regional economic cooperation as a catalyst for the developing ESCAP region's economic restructuring efforts. Regionalism has begun to play a role of unprecedented importance in the world economy. While the world economy is becoming increasingly globalized, regional cooperation is gaining momentum among countries, both strong and weak, which find it to be a useful means of shielding themselves from the increasing vagaries of the external economic environment. Unfortunately, in some cases regionalism can also result in the creation of closed trading blocs that can threaten the evolution of the open trading system on which the hopes of many Asian and Pacific developing economies are based. Yet there is considerable scope for certain forms of regional cooperation which, while being a catalyst for growth and transformation within the region would also enhance the increased interdependence of the world economy.

The world economic environment has been in a continuous state of flux for over two decades. In the 1990s, the challenges posed by the external environment are likely to be even greater and more systemic in nature than in the past. Developing economies of the ESCAP region will have to learn to live with an increasingly complex and uncertain external economic environment by reshaping their economies to enable them to respond with greater flexibility to these challenges.

While the growth trend in the world economy has continued to be downward, economic performance has varied widely between different regions and country groups in the 1980s. Table 1 sets out changes in output, prices, export volumes and terms of trade in different parts of the world economy. As compared with the 1960s, the growth rates in both developed and developing economies have nearly halved. The developing countries, as a whole, have seen continued deceleration in their growth rate, which has fallen below that of industrialized countries.

The industrialized countries recovered from the recession of 1980-1982 and achieved sustained output and income growth, as well as low inflation rates. The annual compound rate of real GDP growth for the industrialized countries was 2.5 per cent over 1980-1987, and the consumer price index increased by 6.1 per cent per annum over the same period. Also, GDP growth in the industrialized countries over 1980-1987 has been marked by greater stability than in the period 1974-1980, though much lower than in the 1960s (as indicated by coefficients of variation in table 2).

The growth of industrialized economies since 1983 has improved considerably after a recession during 1980-1983 when output growth slowed down to 1.7 per cent annually. The inflation rate, which rose to just under

Table 1. Economic performance, 1980-1987
(Annual percentage change)

	GDP	*Consumer price index*	*Export volume*	*Terms of trade*
Industrialized countries	2.5	6.1	4.7	0.8
United States	2.3	5.9	0.4	0.2
Developing countries	2.2[a]	35.7	2.4	0.2
Western Hemisphere	1.6[b]	101.9	2.9	1.3[c]
Africa	0.9[a]	15.9	–2.3	0.2
Developing ESCAP economies	5.9	9.0	5.4	1.9
Developing ESCAP economies minus Iran (Islamic Republic of) plus Taiwan Province of China	6.6	7.7	6.2	0.1
Newly industrializing economies	7.4	7.1	12.4	0.1
South-East Asia	4.3	9.1	4.1	–0.5
South Asia	5.6	9.2	–0.2	0.3
Iran (Islamic Republic of)	2.4[a]	16.7[a]	1.8[a]	2.9

Sources: IMF, *International Financial Statistics*, various issues; and UNCTAD, *Handbook on Trade and Development Statistics*, various issues.

a/ 1980-1985 only.

b/ 1980-1986 only.

c/ 1980-1984 only.

9 per cent per annum during the latter period, has declined to less than half that level, while gloomy forecasts of a recession have been belied by rising growth rates in the late 1980s. Considerable credit for this improved performance is attributable to the macro-economic policy coordination among the Group of Seven (G-7) - France, Germany, Japan, United Kingdom, and United States plus Canada and Italy - which, notwithstanding its limited role, has in varying degrees reduced the turbulence in global currency and capital markets.

While efforts continue in search of new institutional mechanisms to make the interdependence of the world economy work more smoothly, it is still too early to say whether these will be firmly in place before the end of the century. Meanwhile, the possibility cannot be ruled out that new external shocks triggered by continuing uncertainties could seriously destabilize the international economy. In recent years the developing countries of the ESCAP region, along with Japan, have been increasingly drawn into the world economic and financial system. They must give serious consideration to evolving a mechanism that provides, especially to the weaker and more fragile economies of the region, a reliable safety net in case of a serious deterioration in the external environment.

Growth in developing countries in the 1980s varied substantially, with the developing ESCAP economies outperforming those of other developing regions. In sub-Saharan Africa and Latin America and the Caribbean, real per capita incomes fell during 1980-1987 at the annual rate of 2.5 per cent and 0.6 per cent, respectively. The 17 highly indebted developing countries - most of them belonging to Latin America - showed a similar predicament, with real per capita GDP declining at an annual rate of 1.2 per cent over the same period. The developing economies of Europe, the Middle East and North Africa showed only marginally better performance, with an aggregate per capita GDP growth of 0.7 per cent per annum over 1980-1987.

The performance of the developing ESCAP economies in the 1980s is characterized by both relatively high output growth and price stability *vis-à-vis* the other developing countries: output expanded at an annual compound rate of 5.9 per cent over 1980-1987, while per capita income gain was a remarkable 4.1 per cent per annum. It should be pointed out that the slow-down in the growth of the world economy since 1973 did not spare the developing ESCAP economies whose growth rates, despite a resurgence in recent years, still fell short of those achieved during 1961-1973. A remarkable feature of the developing ESCAP economies is that their growth rates during 1980-1987 were much more stable than in earlier periods. In contrast, the variation in the growth rates of other developing countries was not only much larger, but had actually increased.

Despite the uncertainties in the world economy, many developing economies in the ESCAP region have overcome the difficulties faced by them and have repeatedly demonstrated their economic resilience. This has, moreover, been done largely without any formal coordination of economic policies among them. Much of the impulse for restructuring has come from the changes in the external environment. However, in many economies the pressure has been generated mainly by domestic sources. In the 1990s, both kinds of pressure will be operative in developing economies of the ESCAP region. The success of the region's developing economies in the 1980s in overcoming the many external constraints faced by them and in maintaining their growth momentum has itself brought on them the necessity to meet the challenges of problems which are crying out for a solution.

While agriculture has performed well in most developing economies, the fall in commodity prices has often forced the agricultural sector to exploit

Table 2. Gross domestic product and coefficient of variation

	Average annual growth rate			*Coefficient of variation*		
	1961-1973	*1974-1987*	*1980-1987*	*1961-1973*	*1974-1987*	*1980-1987*
Industrialized countries	4.7	2.5	2.5	21.01	64.94	42.09
United States	3.9	2.4	2.3	43.38	106.81	109.91
Developing countries	5.7	3.7a/	2.2b/	16.80	54.06a/	59.37b/
Western Hemisphere	6.1	3.4c/	1.6d/	38.22	85.57a/	168.31d/
Africa	4.9	2.1a/	0.9b/	50.29	155.55a/	355.56b/
Developing ESCAP economies	6.1	5.4	5.9	54.03	43.07	32.22
Developing ESCAP economies minus Iran (Islamic Republic of) plus Taiwan Province of China	5.3	6.3	6.6	67.73	26.18	14.73
Newly industrializing economies	9.8	8.0	7.4	26.46	40.14	40.91
South-East Asia	5.8	5.5	4.3	39.62	39.09	44.41
South Asia	3.3	4.9	5.6	80.70	58.06	20.55
Iran (Islamic Republic of)	10.1	2.2a/	2.4b/	36.66	487.32a/	404.46b/
China	5.5	7.7	9.3	256.52	56.50	30.51

Sources: IMF, *International Financial Statistics*, various issues.

a/ 1974-1985 only.

b/ 1980-1985 only.

c/ 1974-1986 only.

d/ 1980-1986 only.

natural resources more intensively to maintain the same level of income and exports. This requires considerable restructuring of the agricultural sector. Industrial restructuring is a continuous process which the developing countries have to undertake in response to emerging technological changes and the changing international division of labour. A direct consequence of continuing growth in the 1980s in most countries of the region has been the rapid deterioration in their infrastructure. Most countries are beginning to experience cost-push inflation stemming from bottle-necks arising in transport, communications and energy, while urban overcrowding is raising the costs of housing and transport, with inevitable repercussions on wage costs. Social and environmental concerns, which remained subdued while maintaining growth was the policy imperative, cannot be left unattended any longer. Poverty, environmental degradation, population growth and unemployment will have to be given much greater policy attention than they received in the 1980s. The challenge to developing ESCAP economies will be to increasingly incorporate these concerns in their restructuring efforts without losing the external opportunities for accelerating their growth through an erosion of their export competitiveness or failure to benefit from appropriate transfers of technology.

Many of the restructuring efforts undertaken by the developing ESCAP economies were within the context of their own national policy frameworks and without any overall regional cooperation mechanism. In the 1990s, the need for cooperation will be increasingly felt. The end of the decade has already seen some attempts to forge a design for such a regional cooperation framework in the ESCAP region. A lesson to be learned from the current efforts at regonal cooperation in Europe is the attention paid to the development of its periphery - in both the South and the East - as a means of sustaining overall growth in the region. It will be a pity if the more dynamic nations of Asia choose to ignore this important lesson.

I. EMERGING GLOBAL CHALLENGES AND OPPORTUNITIES

A. EMERGING ISSUES

The continued growth and resilience of the developing ESCAP economies and the restructuring efforts needed to consolidate them will depend on the region's ability to meet increasing challenges from a changing world economic environment. These changes taking place in the world economy are significantly different from those which occurred in the previous two decades, in both quantitative and qualitative terms. The emerging changes are not likely to be in the nature of once-off shocks, but of an evolving systemic nature wherein the fortunes of different countries, in both the developing and the developed world, will change much more frequently than in past decades. As a result, the task of restructuring the developing economies of the region will become more complex and will require constant vigilance with respect to emerging trends, as well as an unceasing endeavour to respond flexibly, imaginatively and speedily to take advantage of the various emerging challenges and opportunities.

The international economic environment facing developing economies of the ESCAP region in the 1990s is likely to be characterized by an intensification of major trends from the 1980s and by the emergence of new ones, only the barest contours of which are discernible at present. Among these continuing trends and emerging tendencies, four are easily identifiable and likely to prove more pervasive.

First is the increasing globalization of economic activities, especially in production, evolution of technology and mobilization of capital resources. This is a direct consequence of the growth of world trade at a faster pace than that of world output and the growth and integration of world capital markets. Thus, during the period 1971-1988 the value of world trade grew more than 50 per cent faster than the volume of output. Deregulation of financial services and capital flows, along with the use of high-speed information technology, have resulted in the volume of world financial flows being 50 times larger than that of commodity trade flows.

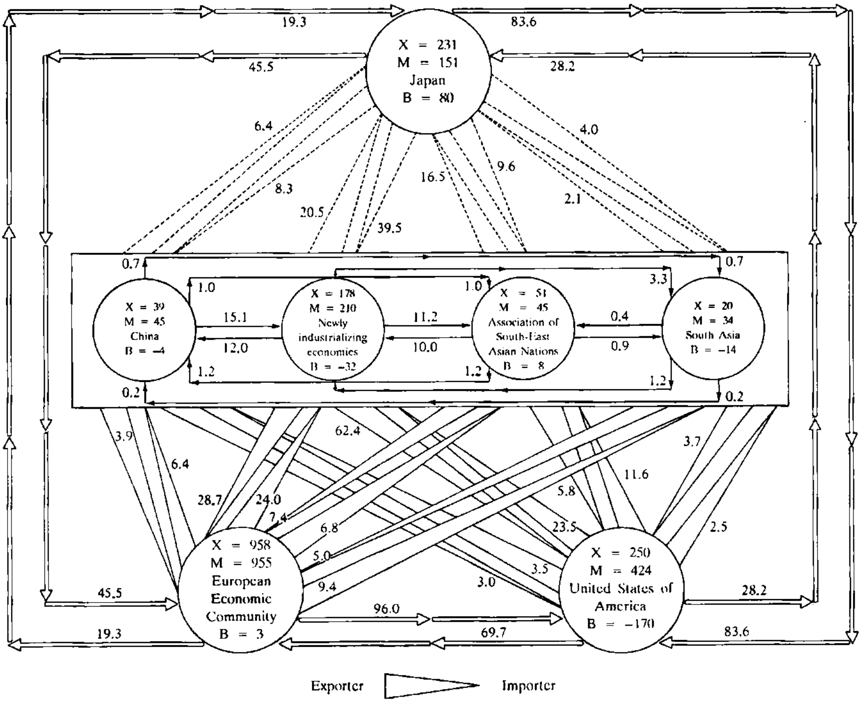
Second, an important aspect of the new global economic environment will be the rapidly changing configuration of economic power among major countries or country groups - a phenomenon often described as multipolarity. Economic and financial power is much more diffused today than it was at the beginning of the 1970s. While the share of the United States of America in world gross national product (GNP) has fallen to a fifth, the United States has turned from being the world's largest net creditor to the world's largest net debtor, with its external debt exceeding that of three of the world's next largest debtors. Japan and the European Economic Community have been emerging as powerful competitors in the world economy (see figure). Japan has emerged not only as the fastest growing developed country but as the world's largest creditor, with net assets abroad of over $300 billion by the end of 1988. This multipolarity is again a double-edged sword of challenge and opportunity; countries which had become used to being too closely allied with or heavily dependent on a particular economic power will find it necessary to adjust to a new world where such dependence is becoming increasingly unsustainable and disadvantageous. A multipolar world can give weak developing countries more room for economic manoeuvre to promote their own development.

The third - and as yet evolving - tendency is the emergence of regional economic alliances or blocs, centred on large domestic or international markets. While the formation of regional and subregional groupings has been attempted in various parts of the world in the past, the European Economic Community's plans for a complete integration of European economies by the end of 1992 have given rise to perceptions - by no means universally shared - that the open trading system which had been largely responsible for world economic growth during much of the second half of this century could degenerate into a regime of rival trading blocs. Regional cooperation, however, need not entail the formation of a restrictive trading bloc. It can serve the useful purpose of removing trade and communications barriers between neighbouring countries, standardizing production techniques and overcoming the limitations on the size of the market. A more useful aspect of such regional cooperation, from the point of view of restructuring, is its ability to draw the peripheral economies of the region into the mainstream of development.

Fourth, the emergence of Eastern Europe as a new and dynamic segment in the world economy is an event which would profoundly affect the challenges to and possibilities for restructuring the developing economies of the ESCAP region in the 1990s. The integration of these economies into the world trading and financial system may cause a certain degree of strain during the transitional period as they compete with developing countries for access to export markets, capital flows and technology transfer. However, since their human and physical infrastructure is generally well developed, their requirements in these areas are likely to be relatively modest compared with the needs of the developing countries. Nevertheless, there is genuine concern among the developing countries that Eastern Europe may preempt

Figure. Trade flows within the Asian and Pacific region and with the European Economic Community and the United States of America, 1987

(Billions of US dollars)



not only the attention and compassion of the developed countries but also some of the resources for development which remain scarce and are extremely limited.

The developing economies of the ESCAP region, especially the more dynamic economies, should find that in the long run this new factor in the world economy will provide them greater opportunities for trade, investment and technology transfer. Even in the short run, many countries of the region which are at present experiencing a slackening of demand and protectionist pressure in their traditional markets could benefit greatly from a sharp increase in imports to meet the pent-up demand for consumer goods and consumer durables. In the longer run, the integration of these economies into the global system of trade and finance will invigorate the world economy, a development which has in the past helped the ESCAP region to grow by restructuring its economies and by taking advantage of the emerging international division of labour.

A characteristic of world economic development in the 1980s - which is unlikely to change substantially in the coming decade - is the dualistic nature of growth in the world economy, wherein the growth centres in the world economy perform substantially better than those in the periphery. There is intense competition among various polarized groups, especially between and among other old established industrial powers, such as the United States, the European Economic Community and Japan, on the one hand, and newly emerging growth poles, such as the Asian and Latin American newly industrializing economies (NIEs) and members of the Association of South-East Asian Nations (ASEAN) on the other. However, the stagnant economies in Africa and the low-income and least developed countries of Asia receive inadequate and often belated attention from the world community. There is nevertheless increasing realization of the need for accommodation and adjustment both within and among various groups of economies, resulting from a perception of cooperation at both regional and global levels as a positive sum game.

The adjustments in such a complex world can hardly be expected to be smooth or self-correcting. A common response of many industrial countries to the rapid growth of output and exports of developing countries has been a resort to protectionism, especially in exports of manufactures. But such a response can only prove to be self-defeating in the long run as it can lead to stagnation in the protecting economies and their isolation from the dynamism of the economies from which they seek to protect themselves. In many cases, especially that of the United States, the correction of the balance-of-payments deficit requires macro-economic, rather than micro-economic or sectoral adjustments which protectionist policies address.

In the 1980s there have been a number of efforts, spontaneous as well as institutionalized, to seek adjustments to the emerging imbalances and tensions which have characterized the international economic environment. The external debt problem of the developing countries, which has preoccupied the world economy since 1982, has been the subject of a number of bilateral, and multilateral efforts to solve the problem. While its main victims have been a relatively few developing economies in the Western hemisphere, it has directly or indirectly affected almost all developing countries. Although certain debtor countries may be on the way to emerging from the debt trap, there seems to be little hope that the debt problem will disappear in the 1990s. The persistence of the debt crisis has not only adversely affected the growth of the highly indebted countries but has also put serious constraints on the growth of others, as access to external capital flows has been made increasingly difficult.

An aspect of the increasing globalization of the world economy has been the emergence of global capital markets which are likely to play an ever larger role in the mobilization of resource flows to developing countries in the 1990s. As the importance of concessional flows or official development assistance (ODA), as well as of sovereign risk lending by commercial banks - which dominated the scene in the 1970s - declines further, foreign direct investment and securitized investment will become the dominant vehicles of resource transfers.

The growth of the international capital market is partly related to the surplus on current account of the balance of payments that has steadily emerged during the past two decades. In 1986, the balance-of-payments surpluses of all surplus countries amounted to about $200 billion annually, compared with about $13 billion in 1970. However, a very small proportion of these surpluses has been used in the 1980s to finance the deficits of capital-poor developing countries (some of which have to produce current account surpluses to finance their debt-servicing obligations). While the problem in recent years has been largely related to the huge balance-of-payments deficit of the United States, some Asian developing countries, such as India and Thailand, have been able to mobilize significant borrowings from the international capital market.

With the continuing reduction in the balance-of-payments deficit of the United States, it should be possible for developing countries in the Asian and Pacific region to gain greater access to the global capital markets. However, developing countries wishing to gain access to these markets will have to adapt their macro-economic policy framework and develop the institutional capacity to enable them to take advantage of the new developments in the globally linked capital markets. The latter are currently driven largely by market forces rather than by interventions in a well coordinated policy framework - an issue which itself may require attention at the global level in the 1990s.

While the diffusion of economic power in a multipolar world, associated in popular perception with the decline in the predominant role of the United States in the world economy, has helped in the release of dynamic economic forces in many parts of the world, it has also created a vacuum in the process of global policy coordination and a weakening of the institutional framework for the management of the global economy.

In particular, this has had severe adverse consequences for international cooperation for development, which has been assigned much lower priority in the agenda of global economic policy issues. The preoccupation of global macro-economic policy coordination, to the limited extent it exists, has mainly been concerned with the stability in the exchange rates among key currencies and the avoidance of resurgence of inflation in the major developed economies.

The advent of macro-economic policy coordination among the G-7 countries since 1985 has tacitly accepted the existence of multipolarity in the world economy, but does not go far enough in the choice of either strategic issues for discussion or key participants. For example, while developing economies, especially the NIEs, are reminded of their obligations to the world economy and coerced to undertake exchange rate adjustments and other policy measures, without a corresponding offer of participation in its management, the interdependence of the world economy clearly calls for a greater role for the major developing economies in global economic management.

The institutional framework of the world monetary system has been evolving from one centred on the Bretton Woods institutions, with the United States in the leading role, to one based on the cooperation of a few key currency countries, principally the United States, Japan and Germany, with other major currency countries playing a subsidiary role. This implicit recognition of the multipolarity of the world economy has gone some way to restore the confidence of world financial markets. However, the markets continue to show considerable volatility and instability in achieving the required realignment of major currencies.

The macro-economic coordination among key currency countries has relied almost exclusively on monetary policies because changes in fiscal policies have generally been constrained by domestic political considerations and cannot be achieved easily. However, monetary policy is called upon to perform a multiplicity of objectives, for example to reduce inflation, sustain growth and stabilize exchange rates. In addition to the conflicts among these objectives, the heavy reliance on monetary policy by the key currency countries creates great uncertainty and instability in developing countries as the changes in interest rates and exchange rates are transmitted to them through globally integrated financial markets. Thus, the frequent changes in the monetary policy of key currency countries often prove very disruptive for production and trade activities in developing countries trying to achieve greater integration into the world economy.

The consequences of the structural changes in the world economy have not yet been reflected in the institutional mechanisms designed to foster international cooperation for development. While the 1950s and the 1960s were decades of relative stability, the 1970s and the 1980s can be characterized as decades of instability and crisis management. The new institutional mechanisms designed to cope with the emerging changes in the world economy have been heavily influenced by the experience of stagflation in the 1970s and early 1980s. Many of the changes in the world economy - such as the rapid accumulation of third world debt or the reverse flow of resources from developing countries - have been so rapid that attention has focused on short-term, rather than long-term adjustments to these developments. Moreover, given the asymmetric nature of interdependence and its insignificant influence in global policy-making, a disproportionate burden of adjustment has fallen on developing countries.

B. CONTINUING CONCERNS

1. Increasing protectionist pressures

A major source of dynamism in the world economy in the past few decades has been the openness of the international trading system, which has propelled the growth of world trade steadily ahead of that of world output. The increasing tendency towards "managed trade" and bilateral solutions is a serious threat to the continued dynamism of world trade and output. It is, therefore, of the utmost importance for the continued dynamism of the world economy that the Uruguay Round of multilateral trade negotiations under the General Agreement on Tariffs and Trade (GATT) are successfully concluded, as scheduled, by the end of 1990.

An increasing challenge to the dynamism of the industrializing countries in the Asian and Pacific region and their attempts to restructure their economies comes from the resurgence of protectionism in many developed countries. The main threat of the protectionist onslaught arises out of a misguided perception of the causes of the relative decline of industrial countries in the past two decades. Increasing structural rigidities in their own economies, rather than high tariff walls in their competitors' markets, are the main cause of the loss of their dynamism, which cannot be reversed by their attempts to adopt bilateralism and sectoralism in their trade policies.

The scope for tariff reduction has been significantly reduced by the last seven rounds of tariff negotiations under GATT. As a result of these tariff reductions, the average level of nominal tariffs on manufactures imports amounts to 4.4 per cent in the United States, 4.7 per cent in the EEC and 2.8 per cent in Japan. However, non-tariff barriers have increasingly been used to restrict the imports from developing countries and have become the tool for the structural policy of developed countries. Measures such as bilaterally negotiated "voluntary export restraints" and orderly marketing arrangements are particularly suited to the protection of declining or "sunset" industries. They tend to perpetuate rather than correct structural rigidities.

Increasingly, protectionist measures include non-tariff measures such as quotas, subsidized export credits, arbitrary changes in health and safety standards, labour market intervention, industrial policies, public procurement policies, voluntary export restraints, and regional policies, and more recently environment policies. Two aspects of increased protectionism are particularly relevant to developing ESCAP economies. First, new protectionist measures by the industrialized countries affect imports from developing economies relatively more than those from the industrialized countries;[4] and, second, awareness of an increased tendency towards protectionism serves as a deterrent to investment in export-oriented industries (and tradeables generally).[5]

The industrialized countries have also been promoting bilateral trade arrangements. The most disturbing example is the United States use of the 1988 Trade Act's "Super 301" clause. Although the "Super 301" process (involving bilateral consultations and possible retaliation) was initiated early in 1989 against Brazil (quantitative restrictions), India (trade-related investment measures and sale of insurance) and Japan (quantitative restrictions

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[4] Julio J. Nogues, Andrzej Olechowski, and L. Alan Winters, "The extent of non-tariff barriers to industrial countries imports", *IBRD Report No. DRD 115* (1985).

[5] The increase in protectionist sentiment and measures is widely documented. For an overview and a survey see, respectively, Christopher Allsop and Andrea Boltho, "The assessment: trade and trade policy", in *Oxford Review of Economic Policy*, vol. 3, No. 1 (1988), and Sheila Page, "The rise in protection since 1974", *Oxford Review of Economic Policy*, vol. 3, No. 1 (1988). These issues are also discussed in Robert Gilpin, The *Political Economy of International Relations* (Princeton, Princeton University Press, 1987); and in UNCTAD, *Trade and Development Report 1988*.

and government procurement policies), the potential threat led others, most notably the Republic of Korea and Taiwan Province of China, to take measures ahead of the announcement of the "Super 301" list that would help reduce the trade imbalance with the United States.[6]

The rise of protectionist tendencies and resort to bilateral trade arrangements are casting their shadows on the Uruguay Round negotiations. At the core of these negotiations are the United States proposals to include liberalization of trade in agriculture and services, and to ensure greater protection of technology and related knowledge. It is somewhat anomalous to seek greater protection under the GATT forum, which has traditionally been concerned with greater trade liberalization. Underlying the United States demands are the declining competitiveness of its manufactures exports generally, and its perceived competitive edge in agriculture, financial and other services, and in innovation and development of commercially/ industrially applicable technology. With respect to trade in both agriculture and services (especially finance), the United States sees itself as facing protected markets. Regarding technology and know-how, its concern is with piracy and "free riders". The liberalization of agricultural trade would on the whole be beneficial to the developing countries.[7] Moreover, liberalization of, for example, construction services or software services would benefit the Republic of Korea and other developing countries that have developed such sectors.

The issues on the Uruguay Round agenda represent the interests of various groups of countries. The success of the talks will inevitably require a balanced outcome and some compromises from initial positions. However, progress has been slow and in the view of one commentator, amounts to "an increasingly precise definition of the agenda".[8] For example, the EEC proposal presented in July 1989 for liberalizing the $160 billion trade in textiles and clothing envisages progressive elimination of the Multifibre

[6] See the *Financial Times*, Leader "Judge and jury", 30 May 1989, p. 22, and "South Korea eases market curbs to beat Super 301", 23 May 1989, p. 6.

[7] A study by Tyres and Anderson shows that world-wide liberalization of selected agricultural commodities (meats, coarse grains, wheat, dairy products and sugar) with the proviso that there is no "over-valuation" of exchange rates would have led to gains in 1985 of $18.3 billion (1980 dollars) for the developing countries and of $45.9 billion (1980 dollars) for the industrialized countries. Because (OECD protection has since increased, these liberalization gains would be substantially higher in 1989. Work by Valdez and Zietz on 99 agricultural commodities supports this latter finding that liberalization leads to gains for developing as well as industrialized countries. See Rodney Tyres and Kim Anderson, "Distortions in world food markets, a quantitative assessment", background paper cited in World Bank, *World Development Report 1986*, pp. 127-132.

[8] Martin Wolf, "From agenda to action", *Financial Times*, 14 July 1989, p. 19.

Arrangement and other trade restrictions that are incompatible with GATT rules. In the EEC proposal, the current restrictions, chiefly quotas, could be converted into tariffs and these tariffs could in turn be gradually reduced and eventually eliminated. The proposal however, avoids setting a date for completing the process, and the timetable itself is a matter to be negotiated. Furthermore, EEC makes any dismantling of quotas "dependent on concessions from exporting countries on a wide range of other issues under negotiation in the Uruguay Round".[9]

While it is important that the Uruguay Round should come to a successful conclusion, the actual developments of increased protectionism and recourse to bilateralism in the 1970s and the 1980s raise doubts about a complete reversal of these trends. These doubts have been strengthened by the non-observance of the "standstill" clause of the Punta del Este declaration.[10] Skeptics also note that the goals that the Uruguay Round seeks to achieve have eluded negotiators for decades, for example, liberalization in agriculture trade and the integration of the textile trade into the GATT code. A major problem relates to the interdependent nature of the multilateral negotiations in which resolution of one particular issue affects that of others.

The prospects for success of the Uruguay Round of negotiations have also been clouded by a number of proposals to form free trade areas (FTAs) or similar trading arrangements among groups of countries. The impetus for initiating the bilateral FTAs comes mainly from the United States as a result of its disillusionment with the preparatory phase of the current Uruguay Round negotiations, which did not start until 1986. The United States was increasingly concerned with its trade deficit, which it perceived could be reduced only by removing barriers to trade in agriculture, services and intellectual property. Other countries, while agreeing to the need for a new GATT Round, wanted the agenda to focus on trade in goods and the elimination of non-tariff barriers.

The long negotiations that led to final agreement on the agenda frustrated the United States trade representative. The United States, therefore, decided to continue parallel efforts to reduce its trade deficit through unilateral pressures (through the use of retaliatory action under Section 301 of the Trade Act of 1974) and through bilateral negotiation of FTAs.[11] The negotiation of FTAs became part of a United States dual strat-

[9] See the *Financial Times*, "Brussels seeks to phase out MFA", 25 July 1989, p. 6.

[10] UNCTAD, *Trade and Development Report 1988*, p. 234.

[11] Similarly, owing to the possibility of failure to launch and implement a new round of multilateral negotiations, Australian Prime Minister Hawke in December 1983 called for the undertaking of a Pacific round of trade negotiations as a fall-back measure.

egy to "provide a complement to, and potentially a substitute for multilateral efforts to liberalize trade".[12] The hasty conclusion of a United States-Israel FTA in 1985 was followed by negotiations for an FTA between the United States and Canada that came into force in January 1989. However, the momentum for the conclusion of additional FTAs has declined in the wake of the launching of and progress in the Uruguay Round negotiations. However, there have been proposals for potential FTAs with a number of United States trading partners, including Japan, the Republic of Korea, Taiwan Province of China, Mexico, the ASEAN countries and Australia. The countries involved are primarily located in the Pacific basin, reflecting the shift in the United States trade policy from the Atlantic to the Pacific. They generally have strong trade links with the United States, and except for Japan, the ratio of their GNP to the United States GNP is less than 5 per cent.[13]

As the interest in bilateral trade agreements began to subside, the passing of the Single European Act in mid-1987 to establish an integrated European market by 1992, revived interest in the formation of a regional trading area in the Pacific.[14] The perceptions about the extent to which the single European market will become more protectionist vary a great deal. The plans for the single market have so far concentrated on internal reforms and there is yet no clear-cut plan regarding the external policy of EEC. It is expected that increasing pressure for protectionism will build up as 1992 approaches, especially from weaker economies and sectors which may seek it as a compensation for making the painful adjustments needed for European integration.[15] The danger of protectionism against the manufactures exports of the Asian and Pacific countries is especially great. Given their increasing international competitiveness and the need to diversify exports away from the United States, the higher growth in the single European market will attract ever greater imports from the latter. The enlargement of EEC with member countries that have a relatively undeveloped industrial base will increase pressure for maintaining or strengthening export quotas and other quantitative restrictions. Any set-backs in the Uruguay Round negotiations or perceptions of an emerging trade bloc in Asia and the Pacific would also strengthen protectionist pressure in the single European market.

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[12] Jeffrey Schott, *Free Trade Areas and U.S. Trade Policy*, Institute for International Economics, Washington D.C., 1989.

[13] These United States-centred FTAs - shaped like a star with the United States at the centre - are bound to lose their attractiveness as an increasing number of countries join them in the expectation of benefiting from the access to the United States market.

[14] The implications of this are analysed in chapter III below.

[15] See, for example, Thomas Anderson, "EC 1992 and its implications to Asian economies", paper presented to the Bangkok Conference on the Future of Asia-Pacific Economics, Bangkok, 1989.

2. Resource transfers

A major challenge facing the developing ESCAP economies in the 1990s will be in regard to the availability of the huge capital flows required for the restructuring of these economies. The environment affecting the quantity and composition of capital flows in the world economy, as well as the demand for such flows, will be significantly different in the 1990s.

One of the most disturbing aspects of change in the international economic environment in the 1980s has been the reversal in the direction of capital transfers from developed to developing countries, which is starkly illustrated by comparing the net inflow of $41.7 billion in 1980 to a net outflow of $32.5 billion in 1988 - a turn-around of over $74 billion.[16] Notwithstanding these developments, not only has the external debt of developing countries almost doubled, from $633 billion (end of 1980) to $1,218 billion (end of 1987), but there has also been a decline in the flows of ODA in real terms (see table I.1) to developing countries, despite the moderately high growth in the donor industrial countries, especially in the second half of the 1980s.

Against this deterioration in the volume of net capital inflows to the developing countries must also be viewed the serious decline in living standards that has taken place in many developing countries, including those in the Asian and Pacific region, as a result of slow growth and reduced imports brought about by severe policies of structural adjustment.

Looking ahead to the 1990s, given the impoverishment and slow-down in growth that has occurred in the 1980s, which has been variously described as a "lost decade of development" or a "decade of adjustment", a much greater infusion of capital will be needed than in the past decades. The needs of different groups of developing countries across the globe for capital inflows will, of course, vary. For Africa, continued support will be needed not only for ensuring minimum consumption levels and adequate food supplies; for Latin America and other heavily indebted countries the need will be mainly for reducing the debt and debt-servicing burdens; for the Asian and Pacific developing countries, the need will be mostly for restructuring their economies, effecting improvements in infrastructure and promoting human resources development in order to maintain their growth momentum and to remedy the imbalances which have developed in the 1980s.

Another claim on capital transfers is likely to arise in order to assist the developing countries to incorporate environmental concerns in their

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16 "External debt crisis and development", Report of the Secretary-General, United Nations (A/44/628).

Table I.1. Net disbursements of official development assistance to Asian and Pacific subregions and economies and to all developing countries, 1980-1987

(Millions of current US dollars)

	1980	*1981*	*1982*	*1983*	*1984*	*1985*	*1986*	*1987 (prov)*
(a) Asian NIEs	160.3	369.7	56.0	39.6	23.6	26.1	20.5	53.3
(b) China	66.1	477.0	524.0	669.6	798.2	940.0	1,133.9	1,448.8
(c) India	2,146.5	1,982.6	1,643.9	1,840.0	1,672.3	1,592.1	2,123.6	1,852.2
(d) South-East Asia	1,802.7	1,901.7	1,764.2	1,782.2	1,871.2	1,800.9	2,357.2	2,893.0
(e) South Asia	3,336.3	2,814.6	3,217.8	2,796.9	2,919.7	3,079.9	3,768.5	3,812.3
(f) Indochina	550.6	407.4	217.7	172.3	160.9	163.9	207.9	189.4
(g) Pacific islands	531.1	516.3	476.8	500.3	461.6	394.9	447.2	585.1
(h) Asian and Pacific LDCs	1,951.0	1,725.1	1,995.1	1,693.6	1,800.0	1,887.3	2,344.6	2,642.1
(i) Developing Asia and Pacific	8,593.6	8,469.3	7,900.4	7,801.0	7,907.5	7,997.8	10,058.8	10,834.1
(j) All developing countries	33,780.0	32,910.7	29,780.6	29,159.7	30,173.9	32,382.9	38,346.5	40,210.9
Deflator of net disbursements of ODA	0.8734	0.8414	0.8255	0.8249	0.8075	0.8116	1.0000	1.1453

(Millions of constant US dollars) [a]

	1980	*1981*	*1982*	*1983*	*1984*	*1985*	*1986*	*1987 (prov)*
(a) Asian NIEs	184	439	68	48	29	32	21	47
(b) China	76	567	635	812	988	1,158	1,134	1,265
(c) India	2,458	2,356	1,991	2,231	2,071	1,962	2,124	1,617
(d) South-East Asia	2,064	2,260	2,137	2,161	2,317	2,219	2,357	2,526
(e) South Asia	3,820	3,345	3,898	3,391	3,616	3,795	3,769	3,329
(f) Indochina	630	484	264	209	199	202	208	165
(g) Pacific islands	608	614	578	607	572	487	447	511
(h) Asian and Pacific LDCs	2,234	2,050	2,417	2,053	2,229	2,326	2,345	2,307
(i) Developing Asia and Pacific	9,839	10,065	9,571	9,457	9,793	9,855	10,059	9,460
(j) All developing countries	38,677	39,113	36,076	35,351	37,368	39,902	38,347	35,110

Sources: OECD, *Geographical Distribution of Financial Flows to Developing Countries,* 1983/1986 and 1984/1987; and OECD, *Development Co-operation, 1988 Report* (Paris, 1988).

[a] Constant 1986 prices and exchange rates.

Notes: NIEs = newly industrializing economies.
LDCs = least developed countries.

development efforts - if environment is to be considered as a public good in which both developing and developed countries have a common stake. The larger environmental issues - the ozone layer, global warming and sustainable utilization of tropical forests - are tasks facing the world economy as a whole. At the same time, it would be difficult for developing countries to adopt these measures if they should imply a decline or slow-down in their growth below acceptable levels.

The crucial question in this regard is where will the needed external resources come from to support the development efforts in the 1990s. The current account surpluses generated in the world economy, however, are among the largest that have ever existed, including those during the period of the oil boom. It is, therefore, not so much a problem of volume of external resources being available, but their improper utilization - away from developing and towards developed countries, mainly the United States. The main problem in the 1990s in relation to the global availability and use of current account surpluses will, therefore, be how such a redirection in capital flows can be achieved without generating a recessionary impulse in the world economy.

The counterpart of any significant increase in the net inflows to developing countries will have to be a decrease in the current account deficit of the United States. This, however, is not going to be easy to achieve, as the developments in the 1980s have shown. Several reasons are cited for the persistence of the United States current account deficit, despite a very sharp fall in the value of the dollar. The problem largely stems from the low savings rate of the United States economy, which in turn is linked to the continuing high budget deficits arising from a reluctance to increase taxes and reduce military expenditure. At the same time, the high trade deficit of the United States has provided developing countries, especially those from the Asian and Pacific region, with an opportunity to expand their exports at phenomenal rates. Thus a sudden decline in the United States trade deficit is not only likely to cause a severe recession in the world economy, but would also seriously affect the growth of many export-oriented developing economies of Asia and the Pacific and cause a sharp decline in the current account surpluses of Japan and the NIEs. A sharp reduction in the United States trade deficit would be a mixed blessing for Asia and the Pacific.

However, there are two possibilities of reducing the United States current account deficit without causing either a major reduction in the availability of the surpluses of Japan, Germany and the NIEs for financing the development of developing countries, or of causing a recession in the world economy. The first is that of recycling some of these surpluses for the development of developing countries, which would enhance the latter's import capacity and cause an increase in the United States exports to developing countries.[17] The second possibility, which has only recently begun to be taken seriously, is that of a considerable reduction in the United States military expenditure abroad; the currently marked improvement in the superpower relationship and the political and economic changes in Eastern Europe have held out a strong hope for a "peace dividend" surplus.[18] There are a number of complexities attached to both these alternatives, but they do provide a considerable basis for hope in the 1990s. These possibilities, especially that of the recycling of the Japanese surplus for restructuring developing economies of the Asian and Pacific region, will be discussed elsewhere in the study.

The gap between the demand for capital flows and the limited supply will be filled in the 1990s by the increasing role of global capital markets, which will provide capital flows through a variety of financial instruments. During the 1980s, about 60 per cent of net capital flows to developing countries was provided by private capital markets, including commercial bank loans, supplier credits, securities, bonds and direct foreign investments. This trend is likely to continue and intensify in the 1990s, partly because in the 1980s it was interrupted by the debt crisis and structural adjustment financing, which increased the role of concessional finance.[19]

The implications of this scenario for developing ESCAP economies, the majority of which continue to depend on concessional finance, are rather serious. Although almost all developing countries, including the low-income and least developed categories, have had to resort to some degree of non-concessional borrowing in the 1980s, it would be both difficult and premature for them to engage in it much more extensively. Access to non-concessional finance is not only limited by a country's level of development and economic performance but also requires the use of sophisticated financial instruments which most developing countries of the region have had little experience with in the past or have inadequate institutional capacity for at the present. Moreover, private non-concessional finance is pro-cyclical in nature and costly in terms of debt servicing.

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[17] This is the essence of the World Institute for Development Economics Research (WIDER) proposals. See S. Okita, L. Jayawardena and A. Sengupta, "The potential of Japanese surplus for world economic development" (Helsinki, WIDER, 1986).

[18] The United States budget deficit, the United States current account deficit and the United States military expenditure in Europe are all of the order of $150 billion per annum.

[19] See Homi J. Kharas and Hisanobu Shishido, "The transition from aid to private capital flows", World Bank, September 1988.

In this respect, the contemporary developing countries of the ESCAP region, especially those belonging to the low-income and least developed countries, face a much more difficult task than the NIEs, which in the 1960s received strong doses of concessional finance. The need for concessional finance or ODA will exist even if foreign direct and portfolio investments can be considered as a viable or a necessary alternative. Many countries in the developing ESCAP region badly need infrastructure, both physical and human, and investments in energy, agriculture and other non-tradeable sectors. These sectors typically do not attract foreign investments and they are dependent on concessional loans; moreover, their development is often a precondition for attracting sizeable doses of foreign investment. There is, therefore, a synergistic relationship between concessional and non-concessinal capital flows.

It is in this context that there is a need for regional cooperation among the region's economies, which include those with large current account surpluses such as Japan, the Republic of Korea and Taiwan Province of China, along with a large number of deficit countries, principally among the low-income and the least developed countries. Thus, recycling of these surpluses, through both ODA and foreign investment flows, could become a most effective means of restructuring the developing economies of the ESCAP region.

3. Technological challenges

Technology is increasingly shaping not only production but also trade and investment patterns and will continue to play a dominant role in the 1990s. The possible impact of technology on production, trade and investment will vary with the type and level of technology in question. While advances in mature technology may benefit most developing countries, it is generally expected that only a limited number of such countries will gain from the emergence of new technologies.[20] Such technologies will only be transferred to countries with favourable economic and policy environments and the capacities to absorb them. There are few developing countries fulfilling such conditions at present. Nevertheless, all developing countries will feel the impact of the new technologies in the coming years.

In various fields of services and production, the new technologies have led to substantial cost reductions and improvements in efficiency. For example, developments in the semiconductor industry have increased the power and complexity of integrated circuits, while simultaneously reducing

[20] The term "new technologies" refers to significant technological advances such as microelectronics and bioengineering which have emerged in recent years.

their costs of production. Other new technologies, such as numerically-controlled machine tools and materials handling robots, are changing the scale of production processes. Of greater concern to developing countries is the way the new technologies have made it feasible for previously labour-intensive processes, such as the assembly of colour television sets, to be undertaken in the developed countries. Developing countries are even more concerned that the new technologies will have an adverse impact on their balance of trade, particularly as to primary commodities. The declining raw material content of finished products resulting from the generation of product innovations having a higher knowledge content, the widespread substitution of materials, reduced wastage and improved methods of processing, have contributed to the sluggish growth in the demand for raw materials, of which developing countries are the major suppliers. Apart from saving raw materials, the new technologies are also expected to achieve significant manpower savings. Such savings could counteract the trend for foreign investors to relocate production facilities in areas of the cheapest labour. For example, the intensive introduction of robotics into the automotive industry could prompt a relocation of new facilities in the developed countries.

The new technologies might be both more powerful and longer lasting than the current technologies because they are so pervasive. Instead of being limited to a single area or activity, they are increasingly influencing the nature and direction of production, trade and investment patterns. In view of the above, developing countries may have to acquire sufficient technological mastery to assimilate the new technologies so that they will be able to maintain, let alone improve, their competitive positions. More specifically, developing ESCAP economies will have to review their education and training policies in order to guard against the danger of a new technology gap. It could be useful to consider the nature and extent to which the private sector, including transnational corporations, are able to contribute to education and training on the grounds that industry needs satisfactory conditions to survive competition based on the new technologies.

II. EMERGING DOMESTIC CHALLENGES AND OPPORTUNITIES

A. DOMESTIC IMPULSES TO RESTRUCTURE AND THEIR POLICY IMPLICATIONS

Although external factors have been the prime impulse for restructuring in many countries of the developing ESCAP region, domestic factors have also provided a major motivation for undertaking basic structural changes in most economies in recent years. In part, the pursuit of growth and the positive response to external challenges in the form of intensified export promotion created domestic imbalances. However, the nature of domestic impulses differed widely among the region's developing countries, according to their level of development, degree of openness and other economic characteristics. Domestic impulses for restructuring often interact with external impulses in an interdependent world economy. In the ESCAP region this interdependence is closely linked with the changes taking place in the Japanese economy and in the NIEs. The other developing economies of the region do not yet have a significant degree of interdependence among them, as evidenced by the extremely low levels of intraregional trade flows among them. While external impulses for restructuring are important, in the cases of China and the South Asian economies domestic factors - especially the need to reduce poverty and unemployment, and demographic and environmental concerns - will play an equally important, if not a dominant role in the 1990s.[21] In this section the major impulses of domestic restructuring in the region are discussed.

A major source of future dynamism in the region will stem from the opportunities and possible benefits that are likely to emerge in the wake of the restructuring of the economy of Japan, the economic power-house of the region. There are strong impulses for restructuring the economy of Japan arising from a variety of domestic pressures. These are embodied in the growing realization that the quality of life of an average Japanese citizen, as reflected in the spartan housing and social amenities, the long hours of work, and the high cost of living in modern-day Japan, falls considerably short of the country's position as a leading economic, industrial and trading power in the world economy. Another growing concern in Japan relates to the continuing concentration of population and economic activity

[21] For a discussion of the restructuring impulses in the least developed and Pacific island countries, see *Survey 1989*, part two.

in Tokyo at the expense of the rest of the country. This is the result of the emergence of new patterns of demand which are being met by the growth of new industries based on sophisticated technologies and services. This calls for a major effort to promote balanced national economic and social restructuring aimed at revitalization of areas outside Tokyo.

Policy initiatives to respond to these concerns are contained in an official publication which was adopted by the Government of Japan in May 1988.[22] It was noted in this document that the promotion of far-reaching economic restructuring was the basic direction needed to augment and to consolidate the shift to a domestic demand-led economy, and three immediate tasks facing Japan were identified: (a) the necessity of reducing the large external imbalance; (b) the creation of diverse life-styles; and (c) the promotion of balanced nationwide economic and social development.

It is interesting that the report explicitly recognizes the complementarities between domestic and external objectives as a logical imperative of growing global interdependence. The report not only recommends the improvement of market access into Japan by lowering or eliminating tariffs, relaxing quantitative restrictions, facilitating import processing, promoting manufactured imports and encouraging direct overseas investment, but also makes concrete proposals for improving the quality and quantity of aid as well as increasing the efficiency of the aid-giving machinery through better staffing, coordination and organization. The implementation of these measures will have an important bearing on the expansion of trade, investment, aid and technology flows from Japan and could serve to reinforce the restructuring process in the developing economies of the ESCAP region, to the extent that these economies can benefit from the opportunities so created.

Similar considerations apply to the domestic impulses for restructuring in the Asian NIEs. Two major consequences of rapid growth provide the main impulses for restructuring in the NIEs. First, they are experiencing considerable strain on the social and economic infrastructures. In addition, growing prosperity has brought pressure for general economic and political liberalization which has created a demand for better income distribution, wage increases, and improved health and social amenities. This has brought strong pressure on the Asian NIEs to restructure their economies by tempering the pursuit of growth with increased concern for social harmony, equity and environmental sustainability.

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[22] Economic Planning Agency, *Economic Management within a Global Context* (Japan, 1988). The policy document is based on an earlier report of the Economic Council's Special Committee on Economic Restructuring, popularly known as the "Mayekawa Report".

The second main impulse for restructuring derives from the external implications of the domestic success of the NIEs. Most NIEs have in recent years generated sizeable current account surpluses, necessitating both internal and external economic adjustments. These adjustments though qualitatively similar to the adjustments required in Japan, are of course of a much lower order of magnitude. At the same time, the NIEs have the much more challenging task of relying increasingly on sources of domestic demand, without losing their competitive edge in external markets. They face, in particular, the problem of upgrading their industries through increased reliance on their own research and development efforts.

In the four resource-rich ASEAN economies (Indonesia, Malaysia, the Philippines and Thailand) which have adopted policies of increasing openness and integration into the world economy, the main aims of current restructuring efforts are continued success in their manufactures' export performance and reduced dependence on the primary sector. Their domestic policies have successfully energized the domestic private sector and have created a conducive climate for foreign investments. These policies have helped the restructuring efforts of these four countries in the recent past.

However, in countries like Malaysia and Thailand, rapid growth has resulted in overheating and severe strains have been brought to bear on the physical and human infrastructures. Social concern for better income distribution and to arrest the decline in the quality of the environment are also on the rise. These domestic impulses to restructure will gain in importance in the 1990s and are likely to become the major impulses for restructuring their economies.

The large low-income economies of the region, especially China, have already undertaken significant steps to integrate themselves into the world economy and to take advantage of the emerging opportunities to increase trade and investment flows for accelerating their development. They are, however, constrained by the limited availability of concessional capital flows and the need to minimize the risks of increasing balance-of-payments and inflationary pressure. The main impulses for restructuring their economies arise from the need to satisfy the basic needs of their large populations in an efficient and equitable manner. Large sections of the population, especially in South Asia, live under conditions of abject poverty, malnutrition and ill health. Education, especially at the primary level, is needed not only to increase productivity, but also to stem the rapid increase in population and to improve the status of women.

Many governments in the Asian and Pacific region have been playing an active part in implementing policies and supporting institutional mechanisms to facilitate the economic restructuring process. Prudent policies have served the region well in the past and they have been mainly responsible for its relatively better economic performance. New policy initiatives to respond to emerging global and domestic issues appear essential in order to promote further growth and structural transformation in the region as well as to take advantage of the growing possibilities for regional cooperation.

Since restructuring basically involves moving resources out of declining activities and into dynamic ones, measures that promote factor mobility are needed to facilitate the process. These include the relaxation of regulations that restrict the entry, exit and expansion of firms. Along with these, extension of deregulation and liberalization aimed at promoting efficiency through increased competition and freer play of market forces are also needed.

Although the trend towards liberalization and greater participation of the private sector in economic development is generally to be welcomed, it is also necessary to recognize that there is a need for government intervention in situations where there is not likely to be a satisfactory outcome through the operation of the market. Thus government support for research and development to enhance technological capability is considered a priority for successful restructuring in the coming decade. Equally important is assistance in imparting training, upgrading skills and supporting human resources development in general. Dissemination of information, improvement of infrastructural facilities and more effective measures to protect the environment represent other areas where the government is expected to play a major role.

Market forces are also likely to prove inadequate with regard to the social and political aspects associated with restructuring programmes. Restructuring is bound to hurt some sections of the population, sometimes the poorest of the poor. Often, the burden of restructuring falls heavily on certain geographic areas and ethnic groups; this compounds the social and political problems, seriously hampering the restructuring process. In such cases, public intervention to reduce the social cost of restructuring may become necessary. This may take the form of programmes to retrain or relocate workers, to create alternative employment opportunities, or to strengthen unemployment compensation and other forms of welfare payments. Coupled with these, there is growing recognition of the need for greater publicity and for public awareness campaigns to highlight the long-run social and economic benefits expected from restructuring in order to enhance its political acceptability.

B. INDUSTRIAL RESTRUCTURING

1. Patterns and changes in the industrial sector

It is generally accepted that industrialization involves a continuous process of restructuring not just across sectors, such as from agriculture to industry and services, but within the industrial sector itself.[23] Moreover, current discussion on industrial restructuring has tended to view the matter as bridging gaps between present performance of domestic industries and what would be required to make them competitive on the world market.[24] Viewed in this way, industrial restructuring can apply to an enterprise, an industrial sub-sector or to the industrial sector as a whole.

In the course of economic development, the relative share of industry in the GDP of most developing countries tends to increase, accompanied by a corresponding decrease in the relative share of agriculture. This trend can be observed in almost all the selected developing ESCAP economies, as shown in table II.1. The table shows that Indonesia registered the highest percentage increase in industry's share in GDP during the period 1965-1987. Other countries which show significant increases are the Asian NIEs, such as the Republic of Korea and Singapore. On the other hand, the least developed countries, such as Bangladesh and Nepal, show only slight increases in their industry's share in GDP.

The perceptible shift in the composition of GDP towards industry may be attributed largely to the relatively rapid industrial growth rate achieved by the selected developing ESCAP economies in the last 20 years. Table II.1 shows that this growth rate was quite high, especially during the period 1965-1980. Not unexpectedly, the Asian NIEs, in particular the Republic of Korea, dominated the industrial growth league.

An interesting aspect of the changing industrial pattern in the Asian and Pacific region has been the rise in manufactured exports. In 1987, there were 15 developing countries with an annual value of manufactured exports in excess of $2 billion, of which 11 belonged to the Asian and Pacific region, and included the Asian NIEs, the ASEAN-4 (Indonesia, Malaysia, the Philippines and Thailand), China, India and Pakistan (see table II.2).[25]

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[23] Industry is defined in accordance with the World Bank (1981) definition as that sector comprising mining, manufacturing, construction, electricity, water and gas.

[24] Ira Lieberman, *Industrial Restructuring - Policy and Practice*, World Bank, Industry Development Division, 20 March 1989, p. i.

[25] The remaining four countries, with the value of their manufactured exports in 1987, were as follows: Brazil ($15 billion), Mexico ($13.3 billion), Yugoslavia ($11.4 billion).

Table II.1. Economic structure of selected developing ESCAP economies, 1965 and 1987
(Percentage)

	Distribution of GDP						*Average annual growth rate of industry*	
	Agriculture		*Industry*		*Services*			
	1965	*1987*	*1965*	*1987*	*1965*	*1987*	*1965-1980*	*1980-1987*
Low income:								
Bangladesh	53	43	11	13	36	39	3.8	4.7
China	39	31	38	49	23	20	10.0	13.2
India	47	30	22	30	31	40	4.0	7.2
Indonesia	56	26	13	33	31	41	11.9	2.1
Nepal	65	57	11	14	23	29	...	...
Pakistan	40	23	20	28	40	49	6.4	9.1
Sri Lanka	28	27	21	27	51	46	4.7	4.2
Middle income:								
Malaysia	28	...	25	...	47	...	...	5.8
Papua New Guinea	42	34	18	26	41	40	...	6.3
Philippines	26	24	28	33	46	43	8.0	–2.8
Thailand	32	16	23	35	45	49	9.5	5.9
Upper middle high income:								
Hong Kong	2	0	40	29	58	70	...	...
Republic of Korea	38	11	25	43	37	46	16.5	10.8
Singapore	3	1	24	38	74	62	11.9	4.0

Source: World Bank, *World Development Report*, 1989 (Washington, D.C., 1989).

Table II.2. Manufactured exports from selected Asian and Pacific economies in 1970, 1980, 1987 and rates of growth for periods 1970-1980 and 1980-1987

	Value of exports ($ million)			*Share*	*Average annual growth rate*	
	1970	*1980*	*1987*	*1987 (per cent)*	*1970-1980 (per cent)*	*1980-1987 (per cent)*
(1) Taiwan Province of China	1,082	17,428	48,400	18.07	32.0	15.7
(2) Republic of Korea	635	15,622	43,537	16.25	37.8	15.8
(3) Hong Kong	1,945	13,079	23,930	8.93	21.0	9.0
(4) China	300	3,000	19,000	7.09	25.9	30.2
(5) Singapore	428	9,048	18,793	7.01	35.7	11.0
(6) India	1,140	4,404	6,723	2.51	14.5	6.2
(7) Malaysia	110	2,427	6,619	2.47	36.3	15.4
(8) Thailand	32	1,605	5,566	2.80	47.9	19.4
(9) Indonesia	12	501	4,275	1.60	45.2	35.9
(10) Philippines	135	2,246	3,514	1.31	32.5	6.6
(11) Pakistan	398	1,247	2,814	1.05	12.1	12.3
All developing economies	10,800	108,800	267,900	100.00	26.0	13.0

Source: UNCTAD, *Review of Trade in Manufactures of Developing Countries and Territories*, Statistical Annex (TD/B/C.2/228/Add.I), 14 August 1989, table 4, p. 5.

These 11 major Asian and Pacific exporters accounted for 68 per cent of total third world manufactured exports in 1987, their positions being built in the 1970s on the high growth rates of manufactured exports. For example, in current dollar terms, manufactured exports from Taiwan Province of China rose from $1.1 billion in 1970 to $17.4 billion in 1980 - an increase of 32 per cent per annum. Similarly, for the Republic of Korea, the inceases was from $635 million in 1970 to $15.6 billion in 1980, representing a rate of growth of 37.8 per cent per year. In the 1970s, the manufactured export performance of the ASEAN-4 matched those of the NIEs, with Malaysia and the Philippines recording over 30 per cent annual growth, while the corresponding rates for Indonesia and Thailand exceeded 45 per cent. China also emerged as an important trader on the regional scene, seeing its manufactured exports grow tenfold from $300 million in 1970 to $3 billion in 1980.

2. Need and forms of industrial restructuring

Although industrial development in the ESCAP region has been quite satisfactory, at least when compared with such development in other developing regions, there is still a need for more robust growth, especially if the region aspires to fulfil the objectives of the Lima target. The countries in the ESCAP region need to restructure their industries in line with recent changes in the global economic environment.[26] One of the most important changes is the drastic realignment of major currency exchange rates following the signing of the Plaza Accord in 1985. This and other developments, such as rising protectionism and the shifts in the pattern of comparative advantage which followed, have forced many countries to restructure their industries. Industrial restructuring is particularly crucial to the developing ESCAP economies that are keen to participate in the new international division of labour or simply to resolve some of the structural weaknesses in their industrial sectors. Two such weaknesses are the "shallowness" of many industries and the imbalance between large-scale and small-scale industries.

Table II.3 analyses the structure of the industrial sector in selected developing ESCAP economies, and shows that the most important manufacturing sub-sectors are food, textiles, other chemical, petroleum and electrical machinery products. It also shows that there is a wide range of manufacturing industries in the region. Apart from producing a few major products in common, each of the selected countries also produces a variety of other products. The range may not be very extensive compared with that of the developed countries, but it is sufficient to provide a basis for intraregional trade in manufactured exports.

[26] For details, see chapter I above.

Table II.3. Five major manufacturing industries (in terms of highest value added) in selected ESCAP developing economies, 1987

Country/area	*Standard industrial classification no./industry*									
	311 Food	*313 Beverages*	*314 Tobacco*	*321 Textiles*	*322 Wearing apparel*	*323 Leather*	*331 Wood*	*351 Industrial chemical*	*352 Other chemical*	*353 Petroleum*
Bangladesh	x		x	x				x	x	
Fiji	x	x			x				x	
Hong Kong				x	x					
India	x			x						
Indonesia	x		x	x			x			x
Republic of Korea	x			x						
Malaysia	x							x		
Pakistan	x		x	x				x	x	
Philippines	x	x	x						x	x
Singapore									x	x
Sri Lanka	x		x	x						x
Thailand	x	x		x	x					

Table II.3 *(continued)*

Country/area	355 Rubber	356 Plastic	369 Other non-metal mineral	371 Iron & steel	382 Non-elec. m/c	381 Metal products	383 Elec. m/c	384 Transport	390 Other
	Standard industrial classification no./industry								
Bangladesh									
Fiji			x						
Hong Kong		x				x	x		
India				x	x		x		
Indonesia									
Republic of Korea				x			x	x	
Malaysia	x		x				x		
Pakistan									
Philippines									
Singapore					x		x	x	
Sri Lanka			x						x
Thailand									

Source: UNIDO, *Industry and Development Global Report 1989/90*, Vienna, Statistical Annex.

A close analysis of table II.3 reveals that many of the manufacturing industries share certain common characteristics that reflect the shallow nature of industrial development in many developing ESCAP economies. For example, many of the above industries use labour-intensive, low-level technology to produce low-quality, low-price, simple consumer products. Where more sophisticated products, such as integrated circuits, are manufactured, the value added is generally low because of the large proportion of imported materials and components incorporated in the final product. At the same time, many of these products involve only simple processing (plywood), mixing (pharmaceuticals) or assembly (motor vehicles). The basic materials or components are generally manufactured abroad. Moreover, within each country there is a relatively narrow range of manufacturing industries in which linkages are significantly absent in many cases. In short, the manufacturing industries in many developing ESCAP economies are relatively narrow and shallow, a reflection of the youthful nature and nascent stage of their industrial development.

Clearly an important task in industrial restructuring for many developing ESCAP economies is to "deepen" their industrial structure. There is a need to increase the value added, moving from simple processing or mixing activities to manufacturing, by increasing the local content in the finished product. Equally important is the need for many developing countries to build linkage between the industrial, agricultural and service sectors so that the benefits of industrialization will extend beyond the metropolitan areas and help lay the foundation for a more balanced and equitable economy.

Another major task in industrial restructuring for several developing countries is the need to develop a balanced industrial sector. Analyses of several developing industrial sectors show that there is a predominance of small-scale industries, which in many countries may account for up to 90 per cent of the total number of industrial enterprises.[27] On the other hand, a large proportion of the industrial output comes from a relatively small proportion of large-scale enterprises, which are often transnational corporation subsidiaries or joint ventures. They are also generally more efficient and use relatively modern techniques of production. Consequently, they are able to produce proportionately more than the small enterprises and thereby to account for a larger proportion of total exports.

Unfortunately, there are minimal linkages between the large- and small-scale enterprises. Unlike the situation in Japan, where large- and small-

[27] I.M.D. Little, "Small manufacturing enterprises in developing countries", *The World Bank Economic Review*, vol. 1, No. 2, January 1987.

scale enterprises work closely together under the subcontracting system, there is little interaction between these two groups of enterprises in many developing countries. Large enterprises in developing countries prefer to import the components they need from abroad, often citing the relatively high price and low quality of locally produced components. To a certain extent, the complaints may be justified. Industrial policies in several developing countries tend to neglect small industries, leaving them underdeveloped and unable to take advantage of any modernization programme. Thus, one of the main tasks of industrial restructuring in these developing countries is to pay greater attention to the modernization of small-scale enterprises in order to enable them to play a more meaningful role in industrial development.

Industrial modernization will be an even greater task for the more advanced developing countries in view of the newly emerging international division of labour. These countries face the arduous task of transforming their "low- and middle-tech" industries into "high-tech" industries to enable the countries to adjust to their new niche of comparative advantage and to maintain their international competitiveness. ESCAP developing economies which will be confronting this problem include not only the Asian NIEs but also aspiring ones, such as Malaysia and Thailand. Many of these countries are establishing science parks to attract "high-tech" industries in much the same way that they developed export processing zones when they embarked on a campaign to attract labour-intensive industries. Examples include the Daeduk Science Park in the Republic of Korea (modelled after Tsukuba Science Park, Japan), the Jurong Science Park in Singapore (modelled after the Cambridge Science Park) and the Serdang Science Park in Malaysia. Besides attracting high-tech industries, the science parks are being used to encourage local research and development activities as well as collaboration between local research institutes and high-tech transnational corporations. Thus, most science parks are located close to technology-oriented universities or state-sponsored research laboratories.

In addition to the above, many of the developing ESCAP economies will have to undertake major reforms of their manufacturing sectors in order to improve the efficiency of resource use and the international competitiveness of their manufacturing industries. Such reforms may be undertaken by:

(a) Making better use of each country's current and prospective comparative advantage in industrial production;

(b) Promoting a more even regional dispersion of industries;

(c) Improving the mobilization of internal resources with respect to not only domestic savings, but also education, on-the-job training and the development of entrepreneurial skills;

(d) Removing administrative obstacles to industrial expansion, such as restrictive trade and investment regulations.

These comprehensive reforms will require policy adjustments in many countries in order to achieve a better mixture of market forces and government intervention than in the past. What mixture is appropriate will differ widely between the large developing countries with well-established industrial sectors, such as India, and the small, resource-poor least developed countries, such as Kiribati. Generally, the required policy reforms will include an adjustment of artificially distorted price structures caused by interest rate subsidies, overvalued exchange rates, and inflated minimum wages. Other reforms include removal of disincentives or obstacles to exports and the reformulation of investment incentives that favour large-scale, capital-intensive and urban-based projects. Overall, there seems to be scope for a more efficient use of available domestic resources to smooth the process of industrial restructuring.

No matter how difficult it may be to implement such a reform package, it has to be done if industrial restructuring is to be effectively undertaken. Industrial restructuring, in turn, has to be undertaken by developing ESCAP economies if they are to meet the challenge of improving labour productivity, and thereby to move up the industrial ladder and compete more effectively in world markets.

3. Problems and prospects for industrial restructuring

Developing countries can be expected to face a variety of problems with whatever form of industrial restructuring they undertake. The major problems, such as volatility in exchange rates and stagnant or sluggish growth in world demand for primary commodities, have been discussed in chapter I. These and other problems may dim the prospects for the rapid industrialization of developing countries and frustrate the efforts of others to modernize their industrial sectors. Fortunately, some of these problems may be partially alleviated by two recent developments: the regional relocation of industries and the globalization of world industry.

The drastic realignment of major currency exchange rates following the Plaza Accord, in particular the significant revaluation of the yen and, to a lesser extent, the Korean won and the Taiwanese and Singapore dollars, has pressured Japan and the Asian NIEs to relocate some of their industries abroad. So far the relocation has affected mainly labour-intensive industries such as processed food, toys and electronics. Some material-processing industries such as pulp, veneer wood and chemical fibre, have been moved to where local raw materials are in abundant supply. The exodus of industries from the high-cost to the low-cost countries has so far benefited mainly the ASEAN countries, especially Thailand and Malaysia, but may spread as the secondary effects of the expanding regional division of labour are set in motion. Some indications are already evident in, for example, the migration of textile industries to Bangladesh and Sri Lanka. The emergence of a new international division of labour in the Asian and Pacific region will enable the Asian NIEs and ASEAN countries to occupy the industrial niche vacated by Japan and to shift their more labour-intensive industries to the other developing countries lower down the industrial ladder.

The current trend towards globalization of world industry will also facilitate the process of industrial restructuring in the developing ESCAP economies. Driven partly by trade friction and partly by cost-reducing pressures from growing international competition, major industrial firms are now increasingly active in globalizing their production networks. Notable examples are motor vehicles, electronics and computer industries. The globalization trend is also reflected in the increase in overseas production. For example, the ratio of Japanese overseas production to domestic production is expected to reach 5 per cent in 1988 (as compared with 3.1 per cent in 1986) and to rise to 12 per cent by 1993.[28] During 1987, Japanese manufacturers invested $7.8 billion in overseas production units, which was exactly twice the amount they invested in 1986.[29] The globalization of industry will enhance the level of participation of the developing ESCAP economies in manufacturing and also improve global production efficiency (in line with the plea for industrial redeployment, as contained in the Lima Declaration and Plan of Action). Efficiency in production requires production facilities to move from high- to low-cost locations. The principle recognized as applicable to a national economy seeking to achieve locational efficiency is also applicable to the global economy. In the regional context, this means that the "sunset" industries in the developed ESCAP economies should be gradually relocated to the developing economies where they will be reincarnated as "sunrise" industries. The process of relocating industries will be facilitated as the developing economies gain cost advantages in an increasing number of industrial subsectors through accumulation of skills and hands-on experience.

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[28] UNIDO, *Industrial and Development Global Report 1988/89*, p. 19.

[29] Ibid.

Industrial restructuring and the process of relocation can be accelerated if the region adopts a cooperative strategy to deal more rationally with the structural problems affecting industries in both the developed and developing countries.[30] Regional cooperation will allow countries to take advantage more effectively of opportunities arising from globalization to modernize and deepen their industrial sectors.

C. AGRICULTURAL RESTRUCTURING

The performance of the region's agricultural sector can best be assessed within a long-term perspective. In the 1970s, propelled by several forces such as the uptake of yield-improving technologies, particularly in cereals, the associated greater use of inputs like irrigation, fertilizers and pesticides, the opening up of export markets coupled with periods of sharply rising prices that encouraged development of export crops, and policy incentives like input subsidies, institutional credit or marketing arrangements to raise production, the region's agricultural output recorded an annual growth rate approaching 4 per cent, while agricultural exports grew at over 3 per cent a year in real terms, the best performance among all developing country groups.[31]

During the period 1981-1987, however, the overall momentum of agricultural growth was barely maintained, while the rate of increase of regional agricultural exports stood at an annual average of less than 2 per cent in the period 1981-1987 (see table II.4). Explanations underlying the observed trends in the 1980s are not hard to find. First, improved technology, the main engine of agricultural growth since the 1960s, had already reached the most progressive pockets in the major producing countries of the region and could only be taken up with increased difficulty elsewhere. Second, the region's export markets encountered increased protectionism and restricted access in developed country markets while, simultaneously, world prices of agricultural commodities of interest to the region declined drastically, causing a 12 per cent worsening of the agricultural terms of trade in 1985 and an even sharper deterioration, of 23 per cent, in 1986.[32] Moreover, the need to reduce budgetary deficits in response to the rising costs of debt-servicing led to cut-backs in input subsidies and credit programmes that adversely affected output. These problems have already

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[30] For details, see chapter IV.

[31] FAO, *The State of Food and Agriculture 1987-1988* (Rome, 1988), p. 55.

[32] Ibid., p. 57.

Table II.4. Selected developing economies of the ESCAP region. Important indicators for the agricultural sectors

(Percentage)

	Agricultural labour 1981-1988[a]	*Agricultural population as percentage of total population 1987*	*Agricultural production 1981-1987*[a]	*Agricultural imports $ value 1981-1987*[a][b]	*Food imports volume 1981-1987*[a]	*Agricultural exports $ value 1981-1987*[a][b]	*Agricultural exports as percentage of total exports 1987*
Bangladesh	1.97	70	1.49	4.07	9.47	−1.77	14
Bhutan	1.75	91	5.08	8.36	15.44	1.22	...
Brunei Darussalam	3.36	54	8.25	8.00	5.33	23.07	...
China	1.30	70	5.32	−3.00	9.96	10.72	17
Fiji	0.43	...	2.23	−0.58	2.89	−2.97	...
India	1.51	64	2.79	2.08	8.26	−0.83	21
Indonesia	0.74	47	3.73	−3.31	−3.04	1.35	19
Malaysia	0.35	33	5.25	1.17	6.58	1.60	22
Myanmar	0.71	49	5.02	−10.21	−6.05	−10.34	35
Nepal	2.17	92	2.95	11.92	5.61	−0.55	37
Pakistan	1.99	54	4.63	5.42	13.92	0.38	25
Papua New Guinea	0.83	...	2.31	−2.49	3.04	0.42	...
Philippines	1.48	48	0.54	1.31	1.60	−7.55	20
Republic of Korea	−1.44	25	2.33	3.99	9.14	−1.44	2
Singapore	−3.06	1	0.33	2.82	3.35	4.20	6
Sri Lanka	1.25	52	0.12	−3.23	1.81	0.95	43
Thailand	1.34	63	1.86	1.83	−2.01	2.81	33
Asia and Pacific	1.34	...	3.75	−0.76	3.69	1.52	...

Source: FAO, *The State of Food and Agriculture 1989* (Rome 1989), tables 2.2 and annex table 11.

a/ Annual changes as the simple average of yearly percentage changes.

b/ In constant United States dollars.

Note: Three dots(...) indicate that data are not available.

been addressed at length in the previous ESCAP study on restructuring.[33] The present focus is therefore on problems which have received relatively inadequate attention in that study as well as other discussions on the subject.

A major concern in many of the region's economies with large populations has been that of food self-sufficiency. However, food security is complicated by difficulties on two fronts. One set of problems is due to post-production constraints such as inadequate storage facilities or improper distribution arrangements, while the other threat is posed by the vulnerability of sown crops to natural calamities. There are two further aspects to the issue of food security. At the household level, food security might be provided by a scheme which assures a given minimum quantity of food to households at a fixed price, but such rationing of food supplies often encounters administrative and financial difficulties. At the national level, food security requires the government to maintain a certain level of buffer-stocks, which, in turn, involves large public expenditure on storage and subsidies. Hence, the severe financial implications of food security in the regions' poorer economies often pre-empt a large part of their limited resources.

The pricing of agricultural products and staple foods is also a sensitive issue in most countries of the region, mainly because of its influence on poverty and income distribution. Accordingly, regional policies have mainly aimed to balance the twin objectives of providing food to consumers at affordable prices and offering adequate incentives to farmers. Most developing ESCAP economies have thus pursued policies involving guaranteed procurement prices for producers, and subsidization of consumer prices as well as of agricultural inputs; an essential aspect of the price issue therefore relates to the farm-gate ratios of crop-to-input prices as it impinges on the intensity of fertilizer application and, consequently, on productivity. In this regard, the nature and intensity of supportive policy interjections in the past have varied among the region's developing economies and have usually assumed the form of export quotas and taxes, or subsidies to agricultural marketing and procurement organizations in which food grains, mainly wheat, rice and maize absorbed the bulk of subsidies.

The overall constraint to agricultural growth imposed by the limited availability of land resources is another issue of the utmost importance as land is the principal productive asset contributing to growth and employment in the sector. The intensity of the problem has increased with demographic pressure and, according to one report, as many as eight countries in the

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[33] *Background Paper: Restructuring the Developing Economies of Asia and the Pacific in the 1990s* (ST/ESCAP/879).

region have less than 0.4 hectares of land per agricultural worker.[34] While the number of rural workers seeking jobs has been rising in the region, the growth of work opportunities in rural areas has failed to keep pace. The agrarian strategy in the developing ESCAP region will therefore have to seek more intensified use of arable land for sustaining the growth of the rural sector.

The trend towards dualism in the region's agriculture, which was at least partially the result of the selective introduction by area and/or by crop of the "green revolution" technology, also needs corrective action. A recent review of the agricultural development strategy and policy in India has argued that after the introduction of new technology, strengthening of peasant farming received low priority as there was much greater concentration on individual crop-oriented technologies taken in isolation.[35] Such an approach resulted in the rapid growth of agriculture in limited segments only. There is a need for the strategy to be made more broad-based through the development of technology and input policies to strengthen climatically handicapped regions and resource-deficient cultivating units.

Preoccupation with supply-side policies in agricultural development in the Asian and Pacific region has often resulted in the neglect of demand factors necessary for sustained growth in the agricultural sector. Agricultural growth, being highly concentrated in irrigated and developed regions, has benefited only particular sections of the rural economy, while the per capita consumption of a large part of the population stagnated. This, in turn has had a depressing impact on demand for farm produce. The challenge lies, therefore, in generating sufficient income growth for the rural population to sustain the growth of the sector through continuing increases in domestic demand. Accordingly, increasing rural off-farm employment through public works programmes has been recognized by several countries (particularly in South Asia) as a precursor to higher agricultural output, while in other economies rural industrialization based on agro-processing activities has been stressed.

While price interventions have received a great deal of attention, the critical nature of non-price interventions in Asian agriculture has been inadequately recognized. Thus, research and development of improved varieties, development of infrastructure, expanded access to institutional credit and effective implementation of tenurial reforms (which restores confidence in on-farm investment) can have a far greater impact on

[34] FAO, *The State of Food and Agriculture 1985* (Rome, 1986), p. 117.

[35] C.H. Hanumantha Rao, "Current agrarian scene: policy alternatives", *Economic and Political Weekly*, vol. XXIII, No. 13 (26 March 1988).

production than price incentives alone. In this regard, the priority of investment in less developed parts of the region would rest on the establishment of adequate infrastructure as sub-optimal use of modern inputs has often been the consequence of shortfalls in complementary irrigation, marketing or credit facilities. In the relatively more developed areas, restructuring of the sector would require the diversification of crop production away from food grains into cash crops and horticulture as well as added emphasis on allied activities like fishing and animal husbandry. Diversified farming, apart from providing insurance against crop failure, could also lead to increased incomes through gradual shifts into higher value products.

Last, to repeat an oft-voiced concern, international trade in agriculture remains a crucial issue. Trade patterns and flows of agricultural products to and from the region are directly affected by global developments and domestic agricultural policies in developed countries which lead to overproduction in these economies as well as depressed world prices. In this regard, it is hoped that the Uruguay Round will bring about a substantial reduction in agricultural protectionism, or else, that it will have serious implications for agricultural restructuring in many of the developing ESCAP economies which have been aspiring to become major exporters of farm produce.

D. ENVIRONMENTAL CONCERNS

The state of the environment was not perceived with serious concern until the mid-1980s. As a result, degradation of the environment and of the natural resource base is now assuming alarming proportions in some of the developing ESCAP economies, and thereby threatening sustainable development. Environmental damage in the region has taken many forms. While some aspects, such as deforestation, desertification, waterlogging and salinity, river pollution, industrial pollution and marine resources exhaustion, have become very visible, others, such as soil exhaustion, pollution of underground water sheets, and several types of industrial and urban pollution, are much less apparent.

Although the situation varies widely among countries, the most critical environmental problems in the region relate to indiscriminate deforestation and land-clearing for immediate economic gain. The tropical forests of Asia and the Pacific, occupying around 300 million hectares, are regarded as the most productive in the world, but during the last decade these forests have been disappearing at an alarming rate and one estimate projects the loss as at least 72 million hectares by the turn of the century.[36] Given the lack

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[36] ESCAP, *Review and Appraisal of Environmental Situation in the ESCAP Region* (Bangkok, 1982), p. 12.

of proper conservation measures, deforestation and land-clearing lead to soil erosion, rapid run-off of water and flooding, siltation of hydropower and irrigation schemes, and losses in crop yields in areas well beyond those originally cleared.[37] Moreover, high environmental accident risks are associated with the establishment of industrial plants built with narrow growth considerations only. In addition, the frequent occurrence of floods or droughts in various parts of the region has been largely attributed to destruction of the environment. Indeed, while in the short term the impact of environment damage might not be perceptible, high rates of economic growth at the cost of severe environmental degradation are unsustainable in the long run.

Degradation of the region's environment has been increasingly linked to the issue of poverty, for it is the poorest members of society that typically suffer most from its effects. Many of the region's populous low-income economies have witnessed a swelling stream of jobless migrants from the countryside to urban areas owing to inadequate growth of on-farm work opportunities. This rural exodus has confronted most large Asian cities not only with unnerving growth projections but also with severe difficulties in coping with soaring demand for housing, transport and other basic services and infrastructure. Therefore, along with large-scale deforestation in rural areas, urban pollution is a major environmental dilemma, with poverty a major factor in both. On one side, overcrowding, lack of sanitation, unsafe water and pollution related to poverty, industry and transport, together with malnutrition, underlie the serious health problems that multiply miseries in urban slums. At the other end, squalid living conditions and cultivation of marginalized land in countless impoverished villages across Asia are similarly detrimental to building a better rural life.

In most developing ESCAP economies, environmental degradation cannot be separated from rapid population growth which reduces the per capita availability of resources and weakens the relationship between people and their natural support system. Especially in low-income economies, its impact on the environment is most commonly reflected in the clearing of large wooded areas of woody vegetation for firewood as, for example, in the Sunderbans in Bangladesh and lower Himalayas in Nepal. In fact, a rapidly growing population, with its ever-increasing demand for food and firewood, can erode the very basis of future growth by degrading soils, polluting and depleting water supplies, destroying forests and eliminating plant species that are potentially useful.

[37] For a comprehensive overview, see ESCAP, *State of the Environment in Asia and the Pacific* (Bangkok, 1985).

A major reason for more intensive exploitation of natural resources by several countries of the region which continue to depend significantly on earnings from exports of primary commodities has been the steady decline in the unit price of these commodities.[38] An equally important cause for environmental degradation is associated with attempts at rapid growth of industries, especially for the production of chemicals, fertilizers and pesticides. In particular, it is well recognized that insufficient caution in industrial activities involving dangerous substances and processes constitutes a hazard of major proportions as was demonstrated by the Bhopal tragedy in 1984. Much of the environmental degradation in the region may also be attributed to the use of inappropriate technologies. Furthermore, in recent years there have arisen the associated problems of disposing of industrial effluents and sewage, owing to the growth of population, expansion of irrigation facilities and the increasing pace of industrialization.

The problems of environmental degradation are well known, but the ways of solving them are often constrained by technical ignorance and, in the low-income developing countries, by a lack of financial resources. Resolution of current concerns therefore calls for coordinated action by the region's developed and developing countries to refine action-oriented strategies and develop low-waste technologies for environmental protection and natural resources management. However, remedial policies and corrective measures require a sound understanding of the causes of environmental degradation, as well as the social and economic aspects of the phenomenon. A major handicap in this regard is that determining the causality of environmental problems becomes difficult because of the interdisciplinary nature of environmental issues, and the complex interaction of several sectoral forces, sometimes occurring over long periods of time. An additional complication is that environmental problems sometimes involve conflicts of interests to the extent that the powerful (such as, industrial conglomerates or lumbering contractors) neglect the interests of the weak, while satisfaction of urgent present-day needs threatens the well-being of future generations. In this setting, implementation of initiatives for environmental protection could well be delayed.

Uncontrolled economic development can be an important contributing factor to growing ecological imbalances, and several disaster relief agencies have cited environmentally unsound development as a major cause of natural disasters. Development strategies in the region must therefore take into account the environmental implications of individual projects and identify

[38] For a detailed review of the issues relating to trade in primary commodities, see *Economic and Social Survey of Asia and the Pacific 1987* (United Nations publication, Sales No. E.88.II.F.2).

schemes aimed at mitigation of environmental problems. On a broader plane, policy interventions will have to accord special attention to serious environmental concerns such as desertification and salinity, the threat of deforestation and problems associated with siltation, as well as severe exploitation of marine and coastal resources. In addition, initiatives are required to prevent atmospheric pollution emanating from increased industrial activity and in support of operations to conserve biological diversity and natural endowments. Moreover, as increasing demands for domestic, agricultural and industrial consumption of water in the region have placed growing pressure on resources, the adequate management of such resources is another major concern.

Lastly, the macro-economic importance of environmental problems should also be emphasized. The shortcomings of national income accounts in their treatment of the environment have been fairly well articulated. Of special relevance to many developing ESCAP economies is the absence of accounting for the drawing down of the stock of those resources that, in principle, are renewable, but which in practice, because of overexploitation, are being rapidly depleted. If compensating investments are not made, growth based on such a process is not sustainable and conventional national income measures may provide a misleadingly favourable impression of long-term economic prospects.

III. RATIONALE FOR REGIONAL COOPERATION

A. INTRODUCTION

Regional cooperation among developing countries has generally been advocated as an important element of an international development strategy and an essential contribution towards the economic development of developing countries. The economic rationale for regional cooperation is based on a number of factors not all of which are necessarily economic in nature. First, regional cooperation allows the participating countries to overcome the small size of their domestic markets, which is particularly important for many developing countries that are economically small and faced with the problem of attaining "critical mass" in many economic and technological activities. Regional cooperation enables the cooperating countries to achieve larger economies of scale in production and attain specialization.

Second, regional cooperation enables developing countries to make much fuller use of their underutilized economic potential in terms of human, technological and natural resources. Through regional cooperation, developing countries are enabled not only to expand existing industries, but also to establish new ones, especially those related to secondary import substitution. The increased scope for diversification reduces the developing countries' economic dependence and their vulnerability to external shocks.

Third, recent changes in the global and domestic economic environment, as discussed in chapters I and II above, provide a compelling rationale for regional cooperation. Two of these significant changes, namely, increasing protectionist pressure from the developed countries and the emerging complementarity among developing countries, strengthen the need for regional cooperation. Such cooperation could serve as leverage in a world of emerging regional trading blocs, contribute to a stronger bargaining position for the developing countries towards the buyers of their products, and create improved opportunities for the development of more appropriate technologies. At the same time, regional cooperation allows developing countries to respond more positively to the changing pattern of comparative advantage in the region.

Finally, regional cooperation could enhance the developing countries' capacity to meet the emerging challenges of the 1990s, especially in the globalization of production and in the application of new technologies. The market of the 1990s will be increasingly consolidated into a single global market. The most favourable opportunities for competing in such a market will be with those enterprises that operate on a global scale or can enter into "strategic alliances" with businesses in other regions. Developing countries may be able to sustain the competitiveness of their enterprises by encouraging the formation of regional transnational corporations and by regional cooperation to attain the critical mass needed for research and the development of new technologies.

Regional cooperation does not depend on a short-term reaction to the state of the world economy, but on the promotion of long-term growth and development. Regional cooperation has to be promoted as part of a long-term development strategy in line with the changing pattern of the regional and global economic environment. For this reason it cannot be limited to trade liberalization measures, particularly when the general concept of economic cooperation among developing countries takes the specific form of subregional or regional integration. It must also include more direct measures, through economic cooperation, to stimulate production in developing countries and expand intraregional trade and investment. The measures should include direct trade measures, joint efforts in regional industrial and agricultural restructuring, promotion of regional investment, environmental management, a certain degree of monetary and financial cooperation through payments and clearing and development financing arrangements, transfer of technology on equitable terms, human resource development and the development of appropriate physical infrastructure for the region.

Regional cooperation among developing countries may take different forms, depending, *inter alia,* on the degree of geographical and cultural proximity between the countries concerned. It may vary from broad consultations to a customs union. Whatever form regional cooperation assumes, it should not be "inward-looking", but should reach out to the rest of the world by developing common policies and joint actions towards third countries, groups of countries and other external entities. However, in many areas of activity, regional or subregional groups should be the basis for wider economic cooperation both within and outside the region.

Despite the benefits offered by regional cooperation, the participating countries face a dilemma since such benefits usually accrue over longer periods of time, and uncertainties about facing balance-of-payments problems preclude involvement in ambitious long-term cooperation programmes. In addition, benefits are not always equal for every country and tend to take longer to accrue to the relatively less developed countries.

Finally, historical factors have disrupted traditional channels of cooperation among developing countries in the region. Having only recently secured their independence, several countries are reluctant to have it subsumed in the wider interests of regional cooperation.

The above difficulties explain the slow progress of regional cooperation in the ESCAP region. Moves towards cooperation began to gain momentum in the post-war period in the wake of decolonization by Western countries. However, the effects of the cold war were so divisive that the movement for regional cooperation did not progress much beyond rhetorical pronouncements and expressions of political solidarity. In the economic fields, the countries of the region were drawn into the North-South stancing through the Non-Aligned Movement and the formation of the Group of 77 in the United Nations. There were few efforts of significance during the 1950s or the 1960s to foster economic cooperation among the region's developing countries. International efforts, both bilateral and multilateral, were focused more on fostering technical cooperation activities and exchange of experience than on linking or integrating these economies to reap the benefits of economies of scale or differences in comparative advantage.

The relatively slow pace of regional cooperation efforts in the ESCAP region in the early post-war decades was also explained by the need for consolidation, integration and development of the national economies, which are essential prerequisites for effective regional cooperation. By the middle of the 1960s and the early 1970s, however, many developing countries of the region had begun to realize the need for greater economic interaction with their neighbours as their production base broadened and became more diversified. Import substitution, though easy in its initial phases, became more difficult and inefficient as it progressed further and it became imperative that market expansion be sought, whether within or outside the region.

The main economic motivation for regional cooperation among developing countries was to overcome the limitations generated by import substitution. Such cooperation had the advantage of subjecting those countries to some degree of openness without risking severe balance-of-payments problems. It was thus viewed as a middle path between complete self-reliance at one end of the spectrum and total openness of the economy at the other. Its main rationale consisted in the possibility of increasing the degree of flexibility and the room for manoeuvre in pursuing national development strategies. This increased flexibility was seen to arise from two principal sources: (a) an increase in the economies of scale provided by pooling of resources and exploring the complementarities in production bases, and (b) increasing the size of markets, mostly through trade diversion but also through trade creation.

In the event, however, the developing countries of the Asian and Pacific region pursued widely divergent strategies of development. While most adopted import substitution as the main vehicle for their initial industrial transformation, others found export promotion - mainly directed towards and assisted by developed countries - to be a more profitable avenue of growth. The establishment of highly protected import-substituting industries in most developing countries of the region reduced the possibilities of intraregional trade and specialization in production activities.

Despite the theoretical attractiveness of regional cooperation, its actual progress in the Asian and Pacific region has been painfully slow. There have been only a few successful attempts to launch effective region-wide schemes of economic cooperation among developing countries of the region. Among the successful ventures, for example the Asian Highway, the Asia-Pacific Telecommunity and the establishment of a number of commodity trade agreements, including those relating to pepper, rubber, tin and coconut, have been established under the auspices of ESCAP (or ECAFE in earlier years). The Asian Development Bank, which was also established at the initiative of ESCAP and, in the face of considerable resistance from a number of countries, has concentrated mainly on the supply of finance and technical assistance to individual countries, rather than on fostering regional economic cooperation and financing of regional projects as its major concern. There have also been less successful attempts to forge several specialized networks of cooperative arrangements. These include the Bangkok Agreement, the Asian Clearing Union and the Asian Reinsurance Corporation.

Three countries of South Asia (Bangladesh, India and Sri Lanka), along with the Lao People's Democratic Republic and the Republic of Korea, belong to the Bangkok Agreement. The Agreement was signed, but not ratified, by two ASEAN members, the Philippines and Thailand. It entered into force in 1976 and aims at product-by-product negotiation of trade concessions among the partners. But trade among members accounts for an insignificant portion of the total trade of the member countries.[39] New initiatives to deepen and broaden the scope of the Bangkok Agreement are under consideration.

The Asian Clearing Union (ACU) was founded in 1973 under the auspices of ESCAP. The amount of funds channelled through ACU in 1981 amounted to the equivalent of only $228 million (transactions are denominated in Asian Monetary Units which are equivalent to special

[39] UNCTAD, "Economic co-operation and integration among developing countries: a review of recent developments in subregional, regional and interregional organizations and arrangements", report by the UNCTAD secretariat (TD/B/C.7/51)(Part III), vol. III, Asia and the Pacific, Arab States; Interregional.

drawing rights) and the Union excludes transactions between India and Nepal, and the Islamic Republic of Iran and Pakistan.

The Asian Reinsurance Corporation (ARC) has a broad membership that includes China, and is one of the best examples of regional ECDC (economic cooperation among developing countries) in the monetary field. The Bangkok-based ARC, which began underwriting business in 1980, helps reduce the leakages of foreign exchange from the region in the form of insurance and reinsurance premiums.

Finally, throughout the region there is a large and growing number of examples of ECDC assistance. For example, in the area of marine transport, India has assisted Viet Nam in undertaking surveys of coastal shipping, ports and inland waterways, and is extending assistance to Maldives in dredging. Malaysia has provided the Philippines with help on import management. China has sent experts to assist several countries of the region in developing their inland waterways. In the field of natural resources, Indonesia has provided advice to Myanmar on the preparation of production-sharing contracts. In the field of social development, the Philippines has provided training to Nepalese officials in the management of social service programmes, and the nationals of several countries have received training from specialized population institutes in India. Finally, in technology, the Republic of Korea receives a large number of trainees each year from the developing countries of the region.

Unfortunately, many of the cooperative arrangements and forms of South-South cooperation mentioned above lack universality. Their impact has been rather modest, despite several efforts to make them more effective and broadly-based.

Much more seems to have been achieved in the realm of subregional cooperation. ASEAN has been the most effective in that regard, but the South Pacific Commission (SPC) and the South Pacific Bureau for Economic Cooperation (SPEC) (now known as the Forum Secretariat) in the Pacific, and the South Asian Association for Regional Cooperation (SAARC) in South Asia, have emerged as established forums of subregional cooperation. However, in terms of economic integration and policy coordination, their achievements are modest at best. For example, the terms of reference of the various studies undertaken by SAARC appear to be addressed to an enhancement of national development strategies rather than integrative schemes.[40] Similary, ASEAN has so far failed to persuade all its member countries to move towards more effective integration in either trade or

[40] J. Nishikawa, "Subregional cooperation in the ESCAP region: part I: South Asia" (UNITAR, New York, 1983).

industry. The ASEAN Preferential Trading Arrangements have not increased intra-ASEAN trade significantly and the ASEAN Industrial Projects and Industrial Complementation Schemes have not promoted any major ASEAN industrial projects among the member countries.[41]

B. FUTURE PROSPECTS OF REGIONAL COOPERATION AND ITS LIKELY ROLE IN RESTRUCTURING

1. New initiatives in regional cooperation

The recent resurgence of interest in regional cooperation in the Asian and Pacific region stems mainly from the phenomenal growth of some of the leading economies of the region. Led by the post-war economic performance of Japan, which made double-digit annual growth rates a norm rather than a freak occurrence, the Asian NIEs in the 1960s and 1970s (as well as in the late 1980s), China and some of the ASEAN economies have repeated the performance in the 1980s, while the rest of the world has remained largely sluggish during the last decade. Other major economies in the region, especially India, have also shown remarkably resilient, if less sustained, growth during the 1980s. These economies constitute a highly significant proportion of the world's population, GDP and, most importantly, foreign trade.

Much of the world's attention has understandably centred on Japan, the Asian NIEs and the ASEAN countries, which have shared certain common characteristics during the process of their development. Among these the following seem to have been most significant: a high and rising ratio of exports to GDP, continuing increases in the ratio of manufactures to total exports, a highly dynamic private entrepreneur class, a dedicated and generally well-trained labour force, and Governments willing and able to intervene to ensure continuing high rates of growth and competitiveness of exports. These three groups of economies represent three waves of industrialization in Asia from the 1950s to the present decade.

These three waves of industrialization and the dynamism they brought to the region occurred without any formal arrangements for regional or subregional cooperation. Nevertheless, of late there has been a growing perception of interdependence among those economies and of their impact on the world economy. It is the nature of this complex interdependence and the need for avoiding the strains, not only among them but also on the world trading system as a whole, that have generated pressure for seeking

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41 For details, see N. Sopiee *et al.*, *ASEAN at the Crossroads*, Institute of Strategic and International Studies, Kuala Lumpur, 1987.

some formal arrangements for regional cooperation. These dynamic economies of Asia and the Pacific depend for their survival on an open world trading system and access to the markets of developed economies to which a majority of their exports are destined. As a result, these economies, as well as others in the ESCAP region, find it necessary to respond in a coordinated regional manner to the challenges confronting them. A number of options have been proposed in recent years.

The first option is to form a trading bloc under the leadership of Japan. This conforms to the perception that the world will eventually divide itself into three or four major economic blocs: the North American bloc, the European bloc, the socialist bloc and a Japanese bloc. Sometimes the proposition is made in terms of the leading currencies: the United States dollar, the European Currency Unit (ECU), the rouble and yen. This rather extreme scenario is unlikely to find much favour in the Asian and Pacific region, which has a commitment to an open trading system and which has strong links with both the American and European markets.

The stimulus for the second option arose from the Australian Prime Minister's initiative in January 1989, which resulted in the first meeting at the ministerial level, held at Canberra from 5 to 7 November 1989, of Asia Pacific Economic Cooperation (APEC). Member countries of ASEAN and Australia, Canada, Japan, New Zealand, the Republic of Korea and the United States of America were represented at that meeting. The Australian proposal stemmed from a recognition that the increasing interdependence of regional economies indicated a need for effective consultations among regional decision makers to:

(a) Help strengthen the multilateral trading system and enhance the prospects for success in the Uruguay Round;

(b) Provide an opportunity to assess prospects for, and obstacles to, increased trade and investment flows within the Asian and Pacific region;

(c) Identify the range of practical common economic interests.

The second option represented by APEC suffers from two major shortcomings. First, the developing regional members are limited to ASEAN and the Republic of Korea. Second, the focus is essentially on trade, rather than development issues.

Although trade has been the engine of economic growth in many Asian and Pacific countries, regional cooperation among developing countries need to be based on broader considerations. Domestic demand in several of the large and rapidly growing economies has also been important, often serving to provide a cushion against the impact of the vagaries of the external environment. High levels of investment, often with a high component of foreign direct investment, have also played a significant role. Thus trade, investment and other resource flows are matters of equal relevance to the Asian and Pacific region. For this reason, preoccupation with trade as a basis for regional cooperation not only may be misplaced but may also cause some concern to other countries.

In view of the shortcomings of the first two options, policy makers in the region may wish to consider a third alternative for regional cooperation, one which has not received the attention and articulation it deserves. It arises in the context of the restructuring efforts of developing countries of the region which are trying to find a niche for themselves in a world economy affected by an ever-changing pattern of international division of labour. This third option could provide for market expansion and increased intraregional trade. It could also provide the basis for sustained growth, which the more dynamic economies of the region are in danger of losing but which the slower growing economies of the region have so far found elusive.

Effective regional cooperation in economic restructuring would be based on broadening the narrow space for development available to the developing countries at present. The rapid growth of the region's developing economies during the last few decades has created considerable room for mutually supportive and complementary restructuring within the developing Asian and Pacific region. The process of differentiation in the region has now increased quite considerably to allow for greater complementarity that makes room for greater interdependence among them. This process is likely to intensify in the coming decade. Japan's need to utilize its surplus, restructure its domestic economy, relocate some of its industries and diversify its export markets will continue to provide the developing Asian and Pacific economies with not only a growing market for their exports but also a reservoir for finance and technology transfer.

The Asian NIEs can play the role of a second locomotive in energizing the developing economies of the region, while the ASEAN-4 will be the direct beneficiaries of the restructuring efforts in Japan and the Asian NIEs. The crucial issue for the 1990s is whether the process of the "flying geese" formation, which helped the East Asian and, to a more limited extent, the South-East Asian developing economies achieve a degree of restructuring, will continue and be able to involve the less dynamic countries of the region. It seems that this mechanism would not be as effective in the case of countries with large populations, low agricultural productivity and other institutional handicaps. In other words, the third or fourth wave of industrialization in the Asian and Pacific economies may not be as easy to achieve as the successful preceding waves.

The model of transformation through the changing division of labour among Asian and Pacific developing economies will, none the less, continue to have some degree of appeal and relevance in at least three crucial ways. The growing interdependence among the region's economies in the 1990s is likely to necessitate some degree of policy coordination. If the current trends of closer regional, subregional and bilateral trading relationships continue, the developing economies of the region will have to consider some new mechanisms for closer cooperation among themselves. A larger regional framework for Asian and Pacific cooperation based on widening complementarity of economic structures would provide ample opportunities for restructuring the economies of the region. At the same time, the pursuit and realization of genuine regional cooperation itself would boost the pace of the restructuring exercise. Finally, the second and third alternatives need not be mutually exclusive. They can complement each other, for the overall economic benefit of the ESCAP region.

2. The role of Japan and the Asian NIEs in Asian and Pacific regional cooperation

Successful regional cooperation depends on several factors, among which is the political will to cooperate. The extent of cooperation will depend on the willingness of developing countries to reconcile the urge for national self-sufficiency with the economic good sense of a mutually beneficial division of labour under cooperative arrangements. Its progress will be affected by the role of the developed countries, particularly Japan and the Asian NIEs.

In any credible scheme for wider regional economic cooperation, Japan and the Asian NIEs will have to play a central role. The significance of their role lies in their ability to enhance intraregional flows of trade, investment and technology transfer. Given their success in pursuing export-oriented strategies, their ability to generate large and continuing balance-of-payments surpluses, and their capacity for technological innovation, these countries can contribute greatly to the development of the low-income countries of the region. In the process they can create expanding markets for their industrial products that are beginning to face the effects of protectionism in the developed market economies of Europe and North America.

More specifically, Japan and the Asian NIEs will need to play a leading role in assisting the other developing economies of the region in their efforts at industrial restructuring. The role of Japan is particularly important because it is the most highly industrialized economy in Asia and the Pacific and its industrial experience is the most relevant for countries in the region. Its strategy of promoting small-scale industries, quality control, export promotion and technology development provides useful examples for developing economies of how to promote their own industrial development.

The same can be said of the Asian NIEs. Within the last decade or so, they have developed a competitive industrial sector and proceeded to amass substantial trade surpluses. For example, the Republic of Korea has accumulated the fourth largest trade surplus in the world, while Taiwan Province of China has acquired foreign currency reserves of about $75 billion during its recent export boom.

Japan can be instrumental in restructuring the economies of the ESCAP region in various ways. First, in line with the changing pattern of comparative advantage in the ESCAP region, Japan can facilitate the process of restructuring by encouraging its manufacturing enterprises not only to relocate but also to obtain more of their components from the region. Following the revaluation of the yen, the slow-down in labour force growth and the astronomical increase in land prices, the competitiveness of labour and land-intensive industries in Japan has increasingly been eroded and it would be more efficient if they were relocated to make room for higher value-added industries. The concern in Japan about the "hollowing-out" of the Japanese manufacturing industry seems exaggerated as it is a natural consequence of the restructuring process implied by the globalization of production activities. Indeed, such relocation could provide the Japanese economy with the opportunity to specialize in more skill-intensive, high-tech industries with large research and development components, while at the same time retaining its industrial leadership through its ability to initiate new product cycles.

A second impetus to the restructuring efforts of developing ESCAP economies could come from Japan's efforts to stimulate domestic demand and open up its market for more imports from the developing countries of the ESCAP region. It could play a major role as an "absorber" of Asian products and may aim at doubling its import of primary and labour-intensive manufactures from other countries of the region.[42]

As it increases its imports, it would be desirable for Japan to give greater priority to agricultural and manufactured products from the less

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[42] S. Okita, "The outlook for Pacific cooperation and the role of Japan", *Japan Review of International Affairs*, Spring/Summer 1987.

advanced developing economies of the ESCAP region. This will help these economies to benefit more from Japan's recent import liberalization.

Apart from market access, developing economies of the ESCAP region will need to acquire expertise and technology from Japan if restucturing is to be accomplished successfully. Japan has successfully developed the subcontracting system to increase productivity and efficiency in its manufacturing industries. The same may be said of its quality control system. The developing ESCAP region can benefit tremendously from the Japanese experience and expertise in these two areas. The developing countries will also have to acquire "hard" technology from Japan. There are several difficulties in acquiring technology from Japan. These include such factors as language barriers, the short stay of Japanese experts, and the lack of qualified local personnel and support industries, which lead to low absorptive capacity for technology. These problems could be partly overcome if the region's developing countries adopted appropriate human resources development strategies to create the required skills. Japanese assistance, such as provision of greater support to the Asian and Pacific Centre for Transfer of Technology in Bangalore, could also prove valuable. Easing the terms and conditions of technology transfer would also contribute significantly to restructuring the developing economies of Asia and the Pacific.

Finally, the most important and vital contribution Japan could make to help the developing economies of the ESCAP region achieve smoother restructuring is through the recycling of its current account surpluses to aid their industrial restructuring. Such recycling, would, however, require some initiatives on the part of Japan in the creation of new financial mechanisms, which would complement ODA (official development assistance) and lending through multilateral financial institutions such as the Asian Development Bank. It would also require Japanese assistance in the development of an integrated Asian capital market through financial deepening and deregulation. Japan and the NIEs could also help the development of other, more sophisticated, financial structures which could contribute to industrial restructuring, for example, the provision of venture capital and other forms of risk capital, such as the establishment of the so-called "growth funds" in the region. In short, Japan could play a very useful and effective role in intensifying the regional linkages among developing ESCAP economies.

Another compelling argument in favour of more effective recycling of Japanese surpluses to the developing economies of the ESCAP region derives from the rapidly changing configuration of world economic and financial power. Japanese investments in the United States and other developed countries have almost reached saturation point; they are becoming a source of trade friction and are creating downward pressure on the value of the yen, which itself is causing inflation and an erosion in the value of the Japanese current account surplus in dollar terms. It is, therefore, opportune for Japan to increase its investments in developing countries instead.

In this regard, Japan's current responsibility towards developing countries of the ESCAP region is similar to that which the United States played in Europe immediately after the Second World War by launching the Marshall Plan and which the Federal Republic of Germany is now poised to play in the restructuring of Europe's less dynamic economies in eastern and southern Europe. The current account surpluses of Japan and the Federal Republic of Germany were almost equal in 1989. The Japanese surplus could perform a similar function in the Asian and Pacific region, where the capital needs are much larger and far more pressing. Thus, the recycling of the Japanese surplus could take various forms, and a comprehensive effort could crystallize in a modified Marshall Plan for the region. It is crucial to increase significantly the small share of the Japanese surplus which has been channelled to the developing countries so far. Although Japan's New AID Plan signals a new trend, its scope needs to be generalized to include infrastructural as well as agricultural sectors. Even in the case of the industrial sector, the scope could be expanded to include projects outside the "flying geese" concept where the economic justification exists. In terms of geographical coverage, the New AID Plan could be extended to all the developing ESCAP economies.

The main problem with regard to the recycling of the Japanese surplus is that since a large part of it is privately owned, it is difficult to channel it into ODA or other means of Japanese assistance to developing countries. A number of imaginative proposals have been made in the WIDER report and elsewhere to overcome this problem.[43] These include changing the legal status of the Japan Development Bank, expanding the role of the Export-Import Bank of Japan, and tapping the resources of the Postal Saving System, which has deposits of over $700 billion, and of the government pension funds. If these proposals can be implemented, developing countries may be able to increase their share of the Japanese surplus.

There is evidence of strong public support in Japan for the country to assume a role centred on economic cooperation and development.[44] An opinion poll commissioned by the Public Relations Department of the Prime

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[43] See footnote 17.

[44] Takeshita Inoguchi, "Four Japanese scenarios for the future", *International Affairs* (1989), No. 1, pp. 15-28.

Minister's Office and conducted in October 1987 shows that the Japanese public decisively rejected a larger political and security role. Those polled opted instead for strengthening Japan's efforts to develop the world economy, to aid economic development in the developing countries, and to further scientific, technological and cultural exchanges.

Japan's ability and willingness to play the key role in ensuring the success of the restructuring efforts of developing ESCAP economies, however, would not be enough. Other countries in the region can also play a very useful support role. This applies in particular to the Asian NIEs.

In the last 25 years, the Asian NIEs have experienced rapid economic growth on the basis of export-oriented industrialization. Their dramatic rise is due largely to the transformation of their industrialization strategy of import substitution in the 1960s to that of export-led growth in the 1970s. Since 1970, the Asian NIEs have made enormous inroads into world markets. During that year, the Asian NIEs accounted for only 3.1 per cent of total world exports; by 1986, their share more than doubled to 6.4 per cent, making the Asian NIEs a significant world economic power. This will be even more evident when the Asian NIEs cement their increasingly close relationships with China and Japan.

Unfortunately, apart from China and Japan, the Asian NIEs have had little interaction with the rest of the ESCAP region. Although the Asian NIEs do invest in other ESCAP developing economies, the leading role of foreign direct investment has always been played by Japan. While the relative importance of trade between the Asian NIEs and other Asian and Pacific developing economies has increased significantly, the commodities they trade are largely primary and intermediate products. The markets for the final manufactured products exported by the Asian NIEs and other ESCAP developing economies continue to be the developed countries in the West.

Needless to say, the Asian NIEs cannot remain isolated from the rest of the region. Over the last few years, new factors have emerged that are likely to give further impetus to the Asian NIEs to interact more closely with the rest of the region. Among these is the relative decline of the United States as the world's economic leader and increased trade conflicts between the developed economies and the Asian NIEs. Another factor is the economic transformation of the Asian NIEs from the early stage of export-oriented industrialization, in which labour-intensive products were manufactured, to a more advanced stage in which more technologically advanced products are made and financial services developed. The increasing degree of complementarity between the Asian NIEs and other ESCAP developing economies offers an opportunity for bringing the two groups closer together and helping the latter to restructure.

The Asian NIEs have benefited greatly from the free trade regime of the world economy. They have become conspicuous exporters in the world, and have to prepare to play a greater role in promoting global economic stability. In this context, it would be desirable for them to make a firmer commitment with regard to trade liberalization through the lowering of tariffs and non-tariff barriers, exchange rate adjustment and graduation from preferential tariff treatment, as well as in making greater efforts to stimulate their domestic demand.

The appreciation of East Asian currencies further encourages the convergence of interests between the Asian NIEs and the rest of the region. With the revaluation of the yen, the Asian NIEs are able to continue their inroads into Japanese markets with nearly double-digit growth rates of GDP. On the other hand, the appreciation of their own currencies and increasingly tight labour markets are forcing the Asian NIEs to relocate some of their less competitive industries abroad. This process of relocation could be facilitated through provision of suitable incentives and other support measures by the public authorities of the Asian NIEs. Similar support could be provided to encourage direct investment and technology transfer to the other developing countries in the region.

Finally, greater financial assistance from the Asian NIEs to other ESCAP developing economies could prove very effective. By assisting the development of the region, the Asian NIEs will eventually benefit from the larger market that will emerge as living standards rise. The strong economic position of Japan and the Asian NIEs, coupled with changes in the international division of labour, provide good opportunities to pursue regional cooperation.

IV. INSTITUTIONAL ARRANGEMENTS

A. THE GENERAL SCOPE

The main thrust of regional economic cooperation should be to enable the developing ESCAP economies to take advantage of opportunities in the world economy more effectively and to better withstand the impact of adverse external developments. Regional cooperation will help harness extra-national efforts to further development goals, enhance the economic potential of the developing ESCAP economies, and also to directly promote the restructuring process in the region. It is a response to a perceived lacuna in the institutional framework of the world economy, and to the inadequacy of individual country efforts to capitalize on opportunities for successful restructuring. It also affords adequate protection against adverse economic circumstances that often arise in a world of continuing adjustments.

The institutional framework for regional economic cooperation should have a structure which caters for the differing needs of the various country groups. For example, for those developing ESCAP economies that are well placed to follow Japan and the NIEs in the "flying geese" formation, the cooperation framework could provide an enabling environment through the infusion of investment funds and technology, as well as access to export markets. It could also provide insurance against temporary slack in export demand and funds to help diversify the production base. Regional economic cooperation could provide trade finance along with insurance against short-term exchange rate gyrations in order to promote intraregional trade. For energy importers, it could provide a buffer stock arrangement and cooperation in the development of energy resources. For the indebted countries, it could provide some insurance against increases in applicable interest rates. For economies with a narrow production base (but also for other primary commodity producers), it could provide a scheme to cushion the economy against the impact of fluctuations in the demand and prices for primary commodities.

In seeking meaningful cooperation, the formation of a set of regional institutions may be considered. These could take the following forms:

(a) Development funding arrangements to provide long-term restructuring finance;

(b) Trade and balance-of-payments financing arrangements, as well as compensatory financing facilities for export losses, interest rate and exchange rate "losses";

(c) An energy agency that would make suitable buffer stock arrangements against sudden price increases and facilitate joint efforts in the discovery and development of energy resources;

(d) A free trade area and a currency area to facilitate intraregional trade and investment and thus to foster greater economic cohesiveness in the region;

(e) A "green fund" to help conserve and protect the environment in the interest of "sustainable development".

The economies of the region differ in their stages of economic development, levels of per capita income, economic structures and strategies, and in trade policies and orientation. This diversity implies differing interests. Their interests also vary with respect to changes in oil and commodity prices. These differences add to the task of attaining economic cooperation in the region. At the same time, the diversity among developing economies in the region provides wide scope for regional cooperation and cooperative arrangements may be envisaged in a variety of areas.

Agriculture is a good case in point. Agricultural development is vital to the economies of many developing economies in the ESCAP region, not only because the levels of nutrition in several of these countries are still very low but also because of the importance of agricultural exports to the region. The objectives and strategies for agricultural development in a large number of countries of the region have many similarities and therefore it is not difficult to envisage various areas of cooperation in agricultural development. Regional cooperation may be desirable in the production of agricultural inputs, such as fertilizers and insecticides, and in agricultural research on problems that are of common interest to the region, such as in plant-breeding and animal husbandry. Cooperation in training is desirable since the agricultural development programmes of the various countries stress the need to impart higher skills to a larger number of workers, especially in local extension work. Cooperation in marketing may help in addressing the problem of adverse movement and fluctuations in the terms of trade between the primary products that the region exports and the manufactured goods it imports. Finally, the coordination of farm policies may be desirable for more effective agricultural planning in the 1990s.

There appear to be good prospects for cooperation in forestry and forest products, as this sector plays a significant role in the economies of many developing countries of the region. Cooperation could help develop the trade of the ESCAP region in forest-based products by reducing the transport costs of logs, processed timber and timber products as well as by evolving better arrangements for the testing and marketing of new or little known timber species. It could also help in exchanging information on common problems of forest management, and in undertaking joint research in this field.

The efficient functioning of a regional transport and communications system is a prerequisite for effective regional cooperation. Improved transport and communication links between countries of the region would greatly facilitate intraregional flows of trade, investment and finance. The transport and communications systems in many developing countries of the region are primarily oriented towards the metropolitan or export centres. Roads and rail links are constructed to transport bulky primary products from the interior to the ports, and the hinterland is generally neglected. Regional cooperation may thus play a useful role in creating a more suitable transport and communications network to stimulate rural development.

Regional cooperation may assist the development of physical infrastructure such as utilities, river basin development and storage facilities. Development of infrastructure has usually been undertaken by the Government, notably in certain areas such as hydroelectricity. It would be desirable to allow the private sector, including transnational corporations, to participate in such ventures on a limited basis.

There is also considerable scope for regional cooperation in human resources development, especially in technical education and training. More specifically, cooperation may be instituted in the formulation of training programmes, exchange of experience in planning techniques and methodologies, and sharing of facilities and personnel. It might be useful at the initial stage to establish a data base on regional education and human resources needs. Particular attention may be given to the needs of small and medium-scale enterprises.

While most of the resources for regional development may have to be raised locally, it would be useful to supplement such resources with funds from outside the region. The dependence of developing ESCAP economies on external financial resources varies widely, with respect to both the level and the type of such resources. Given the sluggish growth of ODA, developing ESCAP economies may have to rely more on private flows. Accordingly, it may be relevant to consider the need for regional cooperation on matters relating to foreign direct investment and transnational corporations. These could include collaboration in foreign investment policies and incentives, promoting intraregional investment and joint ventures, and establishment of a regional information network on transnational corporations. Such cooperation will enable developing countries to reduce the negative impact of foreign direct investment while enhancing the positive aspects.

In addition to the above, regional cooperation may be undertaken in several other areas, such as energy, natural resources, the environment, financial arrangements, trade, industry and technology transfer. For the task of restructuring the developing ESCAP region, cooperation in the four last-named areas is likely to be particularly relevant, and is discussed below.

B. SPECIFIC MODALITIES

1. Monetary and financial cooperation

Monetary and financial cooperation represents one area of international and regional cooperation in which, on balance, there has been a measure of success in the past. Examples of successful cooperation include the European Recovery Program (Marshall Plan), Bretton Woods institutions of the World Bank and the International Monetary Fund (IMF), the European Payments Union and the European Monetary System (EMS), and the regional development banks in Africa, Asia and Latin America. These arrangements and institutions generally have a record of positive contribution to the growth and development of individual economies that they serve as well as to the world economy. There is therefore cause for optimism about the scope of and prospects for monetary and financial cooperation in the ESCAP region.

The European Monetary System is an example of monetary cooperation with the declared goal of establishing a common currency area. Its experience, though instructive, is not immediately applicable to the ESCAP region.[45] EMS aims at maintaining exchange rates within specified bands. Its efforts parallel moves to achieve factor mobility, including liberalization of capital flows, and standardization of banking procedures and financial regulations within the European Economic Community (EEC). These developments bring EEC closer to the concept of one country with several regions. Underlying EMS are the substantial trade flows within EEC, which total close to 60 per cent of its trade.

[45] For a discussion of the European Monetary System, see Giancarlo Gandolfo, *International Economics* (Berlin, Springer-Verlag, 1987).

The EMS structure is not practical for the developing ESCAP region at the present time. There are two reasons for this. First, the EMS economies are relatively homogeneous and economically cohesive, which facilitates the liberalization of capital flows and harmonization of banking and financial regulations. The ESCAP economies are diverse and many are underdeveloped. Second, the larger part of the EEC trade is intraregional, while most of the trade of the ESCAP region is with countries outside the region.[46]

Seven developing ESCAP economies have experimented with the Asian Clearing Union, which is a payments clearing arrangement for the participating countries. The low volume of business reflects the limited commerce between the member countries. For example, in 1987, trade within the Union constituted only 4.6 per cent of member countries' external trade (see table IV.1). As in the case of the Bangkok Agreement, the desire to cooperate is not a sufficient force for the institution to grow when the "pull" of economic forces lies elsewhere.

The point to be stressed, however, is that a currency area arrangement would be more effective once there was sizeable expansion of intraregional

Table IV.1. Trade between member countries of the Asian Clearing Union, 1987
(Percentage of total exports and imports)

	Exports to member countries	*Imports from member countries*
Bangladesh	6.5	5.1
India	2.7	4.0
Iran (Islamic Republic of)	7.6	2.3
Myanmar	5.3	0.8
Nepal	32.6	23.9
Pakistan	5.4	4.2
Sri Lanka	5.0	8.1

Source: IMF, *Direction of Trade Statistics Yearbook 1988.*

46 IMF, op. cit., pp. 56-60.

trade and investment, since such expansion would result in greater intraregional financial flows and transactions. The scope of the Asian Clearing Union could then be enlarged. For the present, a more appropriate course for the developing ESCAP region, and one that could boost intraregional trade, is greater transparency in financial and banking regulations.

A somewhat more ambitious goal is the establishment of financial arrangements to facilitate intraregional trade and investment, and to provide against losses from fluctuations in intraregional exchange rates. Present problems arise from the fact that the existing arrangements in the international monetary system lack an important aspect, namely the provision of sufficient "cover" against the risk of potential exchange rate losses.

Fluctuations in exchange rates, which are characteristic of a floating exchange rate system, imply losses for some of the economic agents. The risk of potential loss in turn discourages international trade and investment flows, particularly of investment in tradeable goods.[47] As far as the developing countries are concerned, there is no specific institutional arrangement that can provide insurance against potential exchange rate losses in a floating exchange rate system. The arrangements that exist are not general, but are usually for specific transactions. Table IV.2 summarizes the existing facilities in some of the ESCAP economies. But this table conceals as much as it reveals. To take one instance, the table answers "yes" to "cover provided by official agencies to debtors" in the case of the Philippines, though the "eligibility for participation was restricted to servicing debt outstanding at the time of a rescheduling".[48]

Let us now consider how exchange rate fluctuations impinge on the economic performance of the developing countries and, in particular, how they influence the external finance situation. Take the case of a developing country with its exports priced in dollars but which borrowed in yen in 1985 to finance, say, investments geared to exporting to a dollar area. By 1987, the country would have faced a substantial increase in its debt-service obligations relative to its export income solely because of the appreciation of the yen *vis-à-vis* the dollar, and without having in any way contributed to this adverse development. On a disaggregated level, the dilemma of exchange rate fluctuations can be visualized in terms of a prospective investor in a developing country who has to work out the feasibility

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[47] See discussion in R. Gilpin, *The Political Economy of International Relations* (Princeton, Princeton University Press, 1987).

[48] See Peter J. Quirk, Graham Hacche, Viktor Schoofs and Lothar Weniger, *Policies for Development Forward Foreign Exchange Markets,* IMF Occasional Paper No. 60, June 1988, pp. 12-14.

Table IV.2. Summary features of forward exchange arrangements in selected ESCAP economies, 31 December 1986

	Cover by private sector		*Cover provided by official agencies to*			*Forward cover provided by or through banks*
	Unregulated	*Regulated*	*Banks*	*Traders*	*Debtors*	
Bangladesh	No	Yes	Yes	No	Yes	Yes
India	No	Yes	Yes	Yes	No	Yes
Pakistan	No	Yes	Yes	No	Yes	Yes
Sri Lanka	Yes	No	Yes	No	No	Yes
Indonesia	Yes	No	Yes	No	No	Yes
Malaysia	Yes	No	Yes	No	No	Yes
Philippines	Yes	No	Yes	No	Yes	No
Thailand	Yes	No	No	No	No	No
Republic of Korea	Yes	No	Yes	No	No	Yes
Singapore	Yes	No	No	No	No	Yes
China	No	Yes	No	No	No	Yes

Source: Peter J. Quirk, Graham Hacche, Viktor Schoofs and *Lothar Weniger, Policies for Developing Forward Foreign Exchange Markets*, IMF Occasional Paper No. 60, June 1988.

of, say, a manufacturing facility where the plant is imported from countries A and B, some of the raw materials and inputs come from countries C and D, and the output is to be exported to countries E and F. The existence of "cover" against the foreign exchange risk could encourage the hypothetical investor to undertake the investment.

Exchange rate variability generally hinders international trade flows. More specifically, there are two reasons why exchange rate uncertainty seems to act to reduce exports of the developing economies more severely than for developed economies.[49] First, the developing economies are, generally speaking, more open (that is, in terms of their relatively higher trade/GNP ratios) than the industrialized countries and the more open economy "suffers" relatively more. Second, economic agents in the industrialized countries, compared with their counterparts in the developing economies, have greater access to financial markets that can help "cover" the exchange rate risk. It is therefore arguable that where the exchange rate risk "cover" is not available, as is often the case for most of the relevant transactions

[49] M.A. Akhtar and R. Spence Hilton, "Exchange rate uncertainty and international trade: some conceptual issues and new estimates for Germany and the United States", *Federal Reserve Bank Quarterly Review* (1984).

in the developing countries, the negative impact of exchange rate variability on trade and investment is going to be higher. It is not surprising to find, in relation to exports from six developing economies (including the Philippines and Thailand), "a clear and strong negative effect of exchange rate uncertainty".[50]

Loss of export trade implies a reduction in convertible currency earnings. This means a reduction in the financial capacity to import, which results in a loss of output growth and investment.

IMF has "sanctioned" a system of exchange rates that is characterized by a relatively high degree of variability. This system, however, is without any risk-hedging arrangement that would be conveniently accessible to the developing economies where private cover arrangements do not exist, or not to any meaningful extent. Regional cooperation can fill the need and provide some suitable arrangements to cover the foreign exchange risks for the developing economies. In addition, financial cooperation would be desirable in facilitating the transfer of savings from surplus economies in the ESCAP region (that export capital) to the deficit economies in the region (economies that are seeking growth-oriented adjustment and complement their savings with capital imports), and help alleviate some of the financial problems faced by the developing ESCAP economies. Table IV.3 indicates the surplus and deficit countries, and shows the directions for transferring savings.

The issue of raising funds in the surplus economies and their transfer to the deficit economies is of immediate practical relevance. A surplus in the current account of the balance of payments of a country is a reflection of its national savings, though not necessarily on government account or for the government to disburse. There is therefore a need to identify viable mechanisms for the transfer of savings from surplus economies to the deficit economies in the region.

The savings of an economy can be in the public sector and the private sector. The authority of the surplus country's legislature will usually be needed to transfer public funds. The government can also resort to raising loans from the private sector, but in such a case it would have to set up future amortization flows. Amortization should not present a problem where the borrowed funds are used productively.

Another method is to permit regional or international financial institutions, foreign banks, corporations and individuals to borrow funds.

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[50] See Ricardo J. Caballero and Vittorio Corbo, *How Does Uncertainty About the Real Exchange Rate Affect Exports?* IBRD Working Paper WPS 221, June 1989. The time period used in the empirical exercises is not specified in the paper.

Table IV.3. Current account balances, 1987
(Billions of US dollars)

	Exports	*Imports*	*Trade balance*	*Current account balance*
World	2,279.10	2,251.00	28.10	–43.20
EEC	916.81	886.16	30.64	39.14
Japan	224.63	128.17	96.46	87.00
United States	249.57	409.85	–160.28	–153.95
Developing ESCAP region	282.47	259.89	22.58	22.44
Newly industrializing economies	175.22	149.31	25.91	29.76
Hong Kong	48.48	48.46	0.01	1.20
Republic of Korea	46.24	38.59	7.66	9.85
Singapore	27.28	29.82	–2.54	0.54
Taiwan Province of China	53.22	32.44	20.78	18.17
South-East Asia	52.23	43.29	8.94	–0.44
Indonesia	17.21	12.71	4.50	–2.15
Malaysia	17.71	11.82	5.89	2.57
Philippines	5.72	6.74	–1.02	–0.50
Thailand	11.60	12.02	–0.42	–0.37
South Asia	18.79	29.36	–10.57	–6.85
Bangladesh	1.08	2.45	–1.37	–0.34
India	11.88	17.66	–5.78	–5.19
Myanmar (1986)	0.33	0.62	–0.29	–0.29
Nepal	0.16	0.51	–0.35	–0.12
Pakistan	3.94	6.25	–2.32	–0.56
Sri Lanka	1.39	1.87	–0.47	–0.34
China	34.73	36.40	–1.66	0.30

Sources: IMF, *World Economic Outlook*, April 1989 (for "World" data); IMF, *International Financial Statistics*, June and December 1989. For other economies: *World Bank, World Development Report 1989* and national sources.

Such borrowing can take the form of direct loans made by a bank in the surplus economy, loans syndicated by such a bank, loans from savings institutions and corporations where the surplus bank acts as an intermediary, and loans and equity raised via a stock exchange. Capital can also be raised in the context of a specific fund or project. A fundamental element in determining the success of such financial propositions is the commitment of the government and financial institutions to the task. Such a commitment is most unambiguously conveyed by the government's guarantees for the loans. Repayment also should have to be guaranteed by the borrower's government.

A related aspect of the problem is the manner in which individual governments are to be involved in the control over funds that have been raised multilaterally. A multilateral fund usually has two types of capital for such finance. One part of the capital, generally minor, carries voting rights that confer decision-making power. This category of capital, and hence the voting rights, can be subscribed to only by the governments of the region on the basis of an agreed formula that reflects the size of GDP, population and trade flows. The other type of capital, usually the largest part, can be raised as general purpose finance, or financing specific to projects or trade. There is a need to devise a mechanism to ensure that the recipient countries, especially the developing countries, have a strong say in the disbursement of multilateral funds.

2. Trade cooperation

The bulk of the developing ESCAP economies' trade is with the industrialized countries. In 1987, it accounted for 58.8 per cent of their exports and 58.7 per cent of their imports.[51] For the developing ESCAP economies as a whole, the United States is the main export market, followed, in order of size, by EEC and Japan.[52] The leading suppliers of imports are Japan, EEC and the United States, in that order. Trade between developing ESCAP economies represents only a relatively smaller proportion, approximately one fourth of the total. A major component of this intraregional trade is in primary commodities and trade in manufactures, and services are of much less significance.

The aggregated matrix of intraregional trade in Asia and the Pacific given in table IV.4 shows that the most significant trade flows were (i) China to the NIEs, (ii) ASEAN-4 to the NIEs and (iii) NIEs to the ASEAN-4. The trade flows between China and the NIEs largely represent trade between China and Hong Kong, whereas trade between the ASEAN-4 and the NIEs reflects, to some extent, the nexus between international investment and trade in recent years. It is striking that intra-subregional trade flows had little significance except for some modest trade flows within South Asia and among the NIEs. Most of the intraregional trade flows were determined by geographical proximity or historical links (for example, China and Hong

[51] Statistics cited are from IMF, *Direction of Trade Statistics Yearbook 1988* (Washington D.C., IMF, 1988), p. 26.

[52] Ibid.

Table IV.4. Distribution of total trade of the developing ESCAP region,[a] by subregions, 1987

	ASEAN-4	*NIEs*	*South Asia*	*China*	*Developing ESCAP region*[b]	*Japan*	*Australia and New Zealand*	*Total ESCAP region* [b]
ASEAN-4	4.5	5.0	3.0	2.9	4.4	6.8	3.4	5.2
NIEs	19.1	7.9	6.9	29.2	12.1	15.3	11.1	13.2
South Asia	1.7	1.2	2.6	1.1	1.5	1.6	1.1	1.5
China	2.6	7.3	1.5		4.9	4.1	2.7	4.5
Developing ESCAP region[b]	28.8	21.9	16.2	33.4	23.6	29.2	20.3	25.3
Japan	25.5	13.6	11.6	19.9	16.1		21.5	10.8
Australia and New Zealand	2.9	1.8	1.6	2.3	2.1	4.1	7.7	3.1
Total ESCAP region[b]	57.3	37.2	29.4	55.6	41.8	33.3	49.6	39.3
Industrial countries minus Australia, Japan and New Zealand	36.1	40.1	43.3	27.4	38.4	51.2	41.0	43.0
Rest of the world	6.6	22.7	27.3	17.0	19.8	15.5	9.4	17.7
World	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Sources: IMF, *Direction of Trade Statistics Yearbook 1988;* and national sources.

[a] Exports (f.o.b) and imports (c.i.f.) added together.

[b] Including Taiwan Province of China.

Kong or Singapore and Malaysia) rather than the results of efforts made at economic cooperation, such as in ASEAN and SAARC.

Several factors account for the relatively weak trade links among developing economies in this region. Historical links promoted the continuation of trade relations with former metropolitan countries. In addition, there was no adequate enabling framework for trade among developing economies, and financial facilities to support such trade are still in the early stages of development. Another limitation to trade among developing economies has undoubtedly been the high tariff and non-tariff barriers affecting imports to these countries. Quantitative controls are also widely used in the developing economies.[53]

Despite the above limitations, intraregional trade is expected to gain in importance in the coming decade, for a number of reasons.[54] First, recent currency realignments and rising protectionism in the developed countries have tended to impart fresh momentum to intraregional trade. Investment flows from the Asian NIEs, together with relocation of some of their industries in other parts of the region, in a manner similar to that between Japan and other economies of the region, are also creating similar trade expansion possibilities. In short, the ESCAP region is now much more diversified than it was some 30-40 years ago; hence, the prospects for intensified division of labour and expansion of trade among the developing countries are much brighter.

Second, there has been a significant change in the economic structure of Japan and the NIEs. The trend has been towards placing greater reliance on domestic demand, with a shift towards increased imports and to reduce the dependence on exports to the United States and EEC. This shift could strengthen considerably the efforts towards extensive restructuring of the developing ESCAP economies and the scope for trade cooperation among developing economies of the ESCAP region and Japan. However, such a change would, *inter alia*, also require Japan and the NIEs to shift out of some of their existing industrial and agricultural activities in order to bring

[53] The low level of intraregional trade has led some observers to conclude that the region's resource endowments were not sufficiently differentiated and diversified and precluded the possibility of greater economic diversification. This notion was refuted in a recent study of detailed analysis of factor endowments and factor intensities of trade flows from and into the region: see *Asian Development Review*, vol. 4, No. 2, 1986, p. 89 ff.

[54] "Growing importance of intraregional trade in the ESCAP region", *Economic and Social Survey of Asia and the Pacific 1988*, Box IV.1, p. 64. However, prospects for increased intraregional trade among the developing Pacific islands may be less promising, not only because of the competitive nature of their economies but also because of the serious diseconomies of scale due to the small quantities of traded merchandise.

about a more efficient division of labour. Although those employed in the activities being phased out will resist change, appropriate structural adjustment policies in Japan and the NIEs can be depended upon to overcome this problem.

However, any large-scale restructuring process would take time. There will have to be a transition from export-oriented production, which caters for a different range of goods for a specific market, for example, office machines and equipment produced on a large scale for the United States and EEC, to expansion of domestic demand, which requires investments in basic amenities, for example, housing. The production structure would need considerable flexibility to make the switch from export goods to goods in domestic demand in the short term. Over a period of time it is of course possible to alter the balance in the economy between the two types of goods by directing new investment away from export-oriented industry and into activities geared primarily to cater for the domestic demand. But Japan and the NIEs have shown considerable flexibility in their production structure and are unlikely to face any major problems.

Finally, the export-led development strategy now being adopted by an increasing number of economies in the region will contribute to the dynamism of the trade of the developing economies of the region. In line with this development, several of those economies are also adopting more liberal and open trading policies by scaling down substantially the degree of protection accorded to domestic industries. In addition, the recent phenomenon of liberalization of planned economies has encouraged countries such as Myanmar and Viet Nam to develop their external trade. All these developments should help boost intraregional trade.

However, certain measures may have to be taken in order to realize the full potential of expanding trade among developing countries of the ESCAP region. First, existing arrangements for trade preferences in the region may need to be reviewed and steps taken to improve their effectiveness. At present, these arrangements include the Bangkok Agreement, the ASEAN Preferential Trading Arrangements (PTA) and the South Pacific Area Regional Trade and Economic Cooperation Agreement (SPARTECA). The Bangkok Agreement attempted to set up trade preferences among some of the developing economies of the ESCAP region.[55] Unfortunately, the Agreement has neither led to trade creation nor has it meant trade diversion. Rather, trade among the participating economies continues to stagnate at low levels; intra-Bangkok Agreement

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[55] Members of the Bangkok Agreement include Bangladesh, India, the Lao People's Democratic Republic, the Philippines, the Republic of Korea, Sri Lanka and Thailand.

trade was approximately 2.5 per cent of the total trade of the participating economies in 1987 (see table IV.5). One of the constraints limiting the effectiveness of the Bangkok Agreement is its small membership.

The most important feature of the ASEAN PTA is the reduction in trade tariffs among member countries. Unfortunately, from the evidence of intra-ASEAN trade trends, the overall impact of the ASEAN PTA has so far been minor. As yet, the preferential tariff reductions have been small, bilateral rather than multilateral, and have pertained to traded items which, although numerous, are of relatively minor importance.

SPARTECA has been slightly more successful because of the concessions offered by the two developed country members, Australia and New Zealand, to the island members of the South Pacific Forum. Restrictive provisions concerning country-of-origin requirements for imports from Forum island members were relaxed in 1987 by Australia and New Zealand. Australia also granted across-the-board, duty-free and unrestricted access to all Forum island exports, except those on which Australian sectoral policies apply. In addition, island exports have been accorded duty-free and unrestricted access to the New Zealand market from 1988 onwards. As a result of the above concessions, the nominal value of commodity exports from the Forum islands to Australia and New Zealand has expanded since 1981.

Table IV.5. Intra-Bangkok Agreement trade, 1987
(Percentage of total exports and imports)

	Exports to other Bangkok Agreement countries	*Imports from other Bangkok Agreement countries*
Bangladesh	1.3	9.1
India	3.4	2.5
Lao People's Democratic Republic	22.7	45.7
Philippines	4.1	3.7
Republic of Korea	2.4	1.3
Sri Lanka	2.8	10.0
Thailand	3.9	4.4

Source: IMF, *Direction of Trade Statistics Yearbook 1988.*

Unfortunately, a high proportion of island exports has come from a few countries, especially Fiji, Nauru and Papua New Guinea.

The performance to date of the various trade arrangements in the region shows substantial scope for expanding the coverage and improving preferential treatment in existing regional and subregional trade arrangements. For example, the extension of the membership of the Bangkok Agreement by including other developing countries could help to strengthen its viability and effectiveness.

Second, in spite of recent changes, protectionist measures remain important barriers to trade among developing economies in the region. This follows a pattern common to most developing economies. To some extent it can be justified on grounds other than trade policy, for example, to raise government revenue, the protection of infant industry and balance-of-payments considerations. There is still scope for developing countries of the ESCAP region to reform systems of import protection through the reduction of tariffs, the rationalization of tariff structures and by the replacement of quantitative restrictions by tariffs in the interests of promoting trade among developing countries. In some of the developing countries, where the private sector is too weak to respond to trade liberalization, more direct measures may be necessary to stimulate intraregional trade. One possible avenue in this context could be cooperation among various state trading organizations which could enter into long-term contracts, or counter-trade organizations. Regional tariff-free quotas could be fixed for bulk procurement of essential government requirements - both civil and military.

Third, the bulk of trade among developed countries consist of intra-industry flows, and developing countries should also take advantage of relative efficiency in different processes and products within the same industry. For example, India might possess comparative advantage in the manufacture of cotton yarn and fabric, while the Republic of Korea might be a world leader in synthetic and blended fabric. Similarly, in garments, the Philippines occupies the niche of children's clothing, while Bangladesh, on account of cheap labour, specializes in fashion garment that require individual attention or production in small batches. One can see immediately how these countries can cooperate to mutual benefit by trading among themselves and by exporting to the rest of the world in a more specialized manner. The same pattern of trade can evolve in the case of automotive parts. Since trade on such a pattern is still minimal, there is tremendous scope for enhancing intraregional trade by exploiting the potential of intra-industry flows, especially in view of the trend towards increased intra-industry trade among the developing countries of the ESCAP region.

Finally, it may be noted that the best prospects for increasing intraregional trade are through regional cooperation. An important constraint limiting the expansion of intraregional trade among developing countries of the ESCAP region is the lack of an enabling framework of facilities and information systems. Such an institutional mechanism may be developed more cost effectively through regional cooperation. The enabling framework for stimulating intraregional trade should provide not only credit facilities and market channels but also a network of information, research and training facilities that will help developing countries exploit the emerging trade and business opportunities in the region. For example, much of the information and analysis required for sector selection by individual countries (or even, at the micro level, for market studies by exporters) would be common for many developing countries of the ESCAP region. Since the collection and analysis of such data and information involve considerable financial resources and expertise, there is much to be gained through undertaking such information gathering and analysis at the regional level, at least to supplement the efforts of individual countries. Similarly, given the general financial constraints faced by many developing countries of the ESCAP region, especially the least developed among them, the establishment of regional funds and financing mechanisms to promote intraregional trade would greatly aid effective implementation of individual strategies at the national level. A less ambitious goal for regional cooperation in trade is that of increasing the "transparency" of trade and investment-related regulations and procedures; this could provide an impulse to intraregional trade as well as investment flows.

3. Regional cooperation in industrial restructuring

There are at least three possible areas for regional cooperation in industrial restructuring among developing countries of the ESCAP region. The first relates to the need to coordinate a host of policies relating to industrial restructuring. Consider, for example, the new international division of labour that is gradually emerging following the recent changes in the pattern of comparative advantage. A smooth transition to stable and sustained high growth for the region as a whole requires a common and acceptable approach in structuring the new international division of labour. The basic objective is to ensure the smooth relocation of "sunset" industries from Japan and the Asian NIEs to the other developing countries in the region where they can re-emerge as "sunrise" industries. Several developing countries in the region have proved to be efficient locations for the production of an increasing number of new product lines. An increase in the level of their participation in manufacturing will not only enhance regional production efficiency but also create a larger regional market for the products of the developed countries. The achievement of this objective will require closer coordination between Japan and the Asian NIEs, on the one hand, and the rest of the region on the other. More specifically, it will require the harmonization of fiscal incentives and assistance to encourage and facilitate the exodus of industries from the home countries; it will likewise require financial assistance by host countries to accommodate the incoming industries. At a more general level, regional cooperation could help in achieving a greater internationalization of the yen as well as other regional monetary and fiscal adjustments. Similarly, regional cooperation can help attain a more open and liberal trading and investment regime by enhancing regional specialization in production according to comparative advantage and the horizontal division of labour among Japan, the Asian NIEs and the rest of the region.

Intraregional investment is another area in which closer coordination of policies and strategies could be useful. Industrialization and continued upgrading of industrial sectors will make all Asian and Pacific economies more dependent on each other. Table II.3 shows that developing countries of the region are beginning to produce a wider variety of manufactured products. This complementarity will boost intraregional trade, and this will be followed by corresponding increasing intraregional investment. A recent study shows that such an increase is already taking place, especially in the form of direct investment from the Asian NIEs to other developing countries in the region.[56] According to the study, foreign direct investment from developing Asian and Pacific economies accounts for 13 per cent of the total FDI stock. Various indicators from several host countries show, however, that in these countries, investments from other developing Asian countries assume considerably greater significance. For example, in several of the ASEAN host countries, intraregional investments account for at least 20 per cent of total FDI; these shares range from 20 to 25 per cent in Indonesia, from 16 to 24 per cent in Thailand, and from 33 to 46 per cent in the case of Malaysia. Only in the Philippines (where it ranges from 13 to 18 per cent) and Singapore (where it accounted for 25 per cent in 1980 but where the proportion has probably come down significantly since then), are the shares somewhat lower. However, in the Philippines, the share of developing country investors from the region has been increasing in recent years. In fact, in 1988, Taiwan Province of China became the largest foreign investor in the Philippines, easing out Japan and the United States, which had long been the dominant investors.[57]

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[56] ESCAP/UNCTC Joint Unit on Transnational Corporations, *Transnational Corporations from Developing Asian Economies: Host Country Perspectives*, Publication Series B, No. 12, Bangkok, 1988. See also ESCAP/UNCTC Joint Unit on Transnational Corporations, *Transnational Corporations from Developing Asian Economies*, ESCAP/UNCTC Publications, Series B, No. 7, Bangkok, 1985.

[57] Ibid.

In view of the growing importance of intraregional trade and investment, developing countries of the ESCAP region will need to coordinate their policies in order to facilitate the process of industrial restructuring.

The second possible area for regional cooperation lies in meeting the challenges presented by the current trend towards globalization of world industrial production. Manufacture of a single product now commonly spans several countries, with each country in this "global factory" performing tasks in which it has a cost advantage. For example, many countries in this region are involved in producing various parts and components for motor vehicles and computers. Globalization also implies viewing the whole world as a single market. Sales have to be made world-wide in order to recoup the enormous R and D expenses that enable the leading corporations to remain competitive. In line with this trend, major manufacturing enterprises are positioning themselves to expand their scale of operation through mergers and take-overs. Globalization will enable the major corporations not only to enjoy even larger economies of scale but will also to treat the whole world as their market. At the same time, these corporations are also seeking to reduce operational costs by sourcing their components world-wide through international subcontracting. Developing countries of the ESCAP region may be able to reduce the monopoly rents enjoyed by the transnational corporations if they can pool their resources and encourage the formation of their own transnational corporations. These corporations will need to cooperate closely with each other at the regional level in order to counter the threats posed by the global transnational corporations. If not, the benefits of regional integration will accrue mainly to transnational corporations from the developed countries.

Developing countries of the ESCAP region should also cooperate in building regional industries through subcontracting. An initiative has already been taken by a transnational corporation in Thailand to manufacture an ASEAN car using components obtained from various ASEAN countries. Perhaps it would be more desirable for local enterprises in the region to cooperate in a similar venture. One possibility is provided by the rapid development of information technology in the region. Several countries in East and South-East Asia are already manufacturing the integrated circuits, disk drives and other components and peripherals needed to make up the constituent parts of a computer. Developing countries in South Asia, with their huge reservoir of highly skilled but largely underutilized human resources, could cooperate in developing the software. Such cooperation could be the groundwork for a regional computer industry, marrying the capital-rich resources of the East and South-East Asian countries with the skilled manpower resources of South Asia.

The third potential area for regional cooperation in industrial restructuring is the development of small-scale industries. Although these industries comprise a very large proportion of the total number of enterprises, and play a significant role in the economic development of many developing countries, there are very few viable or modern small-scale industries and sectors in these countries. Governments have formulated various policies and instituted numerous programmes to develop small-scale industries, but many of these policies have been quite ineffective and the programmes have generally failed to achieve their objectives. It is rather unfortunate that such programmes are developed and implemented in different countries with little tangible gain from the experience of other countries in the region. The mistakes committed by one country are often repeated in others, while several innovative and effective programmes remain confined to the boundaries of the country of origin. Regional cooperation could be useful in enhancing national efforts to promote small-scale industries.

The key objective of regional cooperation in small-scale industries is to develop a viable and modern small-scale industry sector that can lay the foundation for a stronger industrial sector in the developing countries. Modern small-scale industries can contribute to the development of the subcontracting system and thus promote closer relations between such industries and their large-scale counterparts. In assisting these industries through regional cooperation, priority industries will be identified and means of action specified. Various schemes can be formulated to foster small-scale industries, such as technical and financial assistance, improved supply and marketing arrangements, promotion of industrial cooperation through complementary industrial activities and training of personnel. The major focus of all these measures will be the modernization of Asian and Pacific small-scale industries and, in turn, to increase productivity and overall industrial efficiency. The important means of increasing productivity in the small-scale industry sector is through modernization of plant and equipment and management, promotion of technical innovations and invention, and the introduction of low-cost automation. All these should form the focus for regional cooperation in small-scale industry development.

The general principle underlying regional cooperation in small-scale industries is to take advantage of the economies of scale when programmes are implemented at the optimum level. Just as cooperatives enable small-scale industries to take advantage of the economies of scale in marketing and purchasing at the national level, regional cooperation will enable national small-scale industry agencies to gain similar advantage in providing training, information and technical, financial and other forms of assistance at an optimum scale. For example, if priority is given to the modernization of small-scale industries though regional cooperation in developing software, then the development and adaptation of information technology for small-scale industry application can be reduced significantly.

If the above suggestion is accepted, then steps should be taken to establish an institutional mechanism for regional cooperation in small-scale industry development. One possibility is to set up a network of small-scale industry development agencies in the region. The nodal agency could be one of the institutes for small-scale industries in the region that has extensive experience in organizing regional programmes for such development. At a later stage, an Asian and Pacific centre for small-scale industry development could be set up to provide a more formal mechanism for regional cooperation in such development.

Developing countries with diverse needs and at different levels of development will obviously have to pursue different policies and strategies for industrial restructuring. For example, South Asian countries, which have not fully developed their export-oriented industries, might have to place a greater priority on quality control and marketing, while Asian NIEs will have to concentrate on upgrading their industrial structure. Nevertheless, as the above discussion points out, there are several potential areas for regional cooperation. The countries in the region, especially Japan and the Asian NIEs, may wish to take advantage of the new opportunities for regional cooperation in a spirit of partnership and shared goals. Such cooperation will be mutually beneficial, as many developing countries in the region have potentially rich resources and are well geared to become important partners in the new strategy of industrial restructuring through regional cooperation.

4. Technology transfer

Technological progress is a critical factor in the process of economic development and for the attainment by developing countries of their twin objectives of eradication of poverty and rapid industrialization. Developing countries in the ESCAP region are placing increased emphasis on the acquisition of technological capabilities, especially in the process of restructuring their economies. Efforts in this regard include indigenous technology development and technology transfers from the developed countries. While technology acquisition from non-commercial sources, such as universities, scientific and technical publications and public technical exchange programmes, constitutes an important part of the process, transfer of technology from commercial enterprises in industrialized economies represents an increasingly important avenue for the acquisition of technical knowledge.

A major issue concerning the transfer of technology to countries restructuring their economies concerns the cost and effectiveness of technology transfer. Although it is generally cheaper and quicker to import technology than to develop it locally, at least in the short run, the financial costs of technology transfer remain considerable and tend to increase as a country industrializes. For example, technology payments remitted from the Republic of Korea nearly doubled, from $58.1 million in 1977 to $107 million in 1981.[58] The actual costs of technology transfer are even higher if the indirect costs, which arise from the various restrictions imposed in technology transactions, are taken into account. For instance, the licensees may be required to purchase certain materials or components from the licensors at prices above the market rate. Similarly, there may be restrictive clauses relating to exports and handling of competing products.

An equally important issue confronting countries importing technology is how to ensure rapid and effective transfer of technology. Developing countries have often experienced that, in spite of spending large sums of money on the purchase of technology, they have been unable to achieve any significant level of technological development. The term "technology transfer" as used here means not only the act of importing but also the reduction of technological dependence on foreign sources. In this sense, technology is transferred when technological mastery is acquired or when the recipients have built up technological capabilities to comprehend, utilize, adapt, modify and further develop raw products or processes on their own.

The question of how to achieve an effective transfer of technology within a reasonable period of time is of particular interest to those developing countries that are in the midst of restructuring their economies. The answer to this question may lie partly in the source of technology and the channels through which it is transferred, and partly in local absorptive capacity, which is dependent upon the educational, scientific and research and development infrastructure of the recipient country.

Another major issue relates to the appropriateness of the technology transferred. In several instances, capital-intensive technology created in the developed countries has been transferred to labour-abundant developing countries that are characterized by a relative scarcity of capital. This may be due to a variety of reasons, such as factor price distortion or the high

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[58] ESCAP/UNCTC Joint Unit on Transnational Corporations, *Costs and Conditions of Technology Transfer through Transnational Corporations*, 1984, Publication Series B, No. 3.

cost of adapting technology to developing country environments.[59] Whatever the reason, the adoption of inappropriate technology not only leads to excess capacity but also reduces employment opportunities in a labour-surplus economy. All these in turn may frustrate the objectives of restructuring.

It is important to remember, however, that the most appropriate technology for developing countries need not always be the least sophisticated technology. In fact, developing countries need to acquire the latest technology in certain areas if they wish to stay competitive. In today's highly competitive world, it is not just a matter of having the required technology, but having technology that meets global rather than national or even regional standards. Fortunately, several developing countries have demonstrated that appropriate technology can be compatible with the most advanced technology. For example, India is now at the cutting edge of computer software that at the same time is appropriate to its resource endowments.

The above discussion suggests the need for a rational strategy for technology transfer among developing countries. Such a strategy should incorporate the careful selection of technologies, as well as measures aimed at facilitating technology absorption, assimilation, diffusion and innovation. A rational strategy also implies the exercise of deliberate control over and management of the technology transfer process. At the same time, developing countries will have to devote more effort to fostering indigenous technological capabilities. The strategy will have to take into account appropriate policies for the acquisition and development of the new technologies, keeping in mind that the high cost of developing them could force developing countries to focus on one or two carefully selected areas.

For example, South Asian countries with a huge reservoir of highly educated but unemployed labour might wish to specialize in "software" technology, while agriculture-based developing economies might target bio-technology. Resource-poor developing countries might place greater priority on new materials technology. All developing countries, however, will have to pay some attention to the acquisition of information technology, but with some differences in the areas of emphasis. They will need to implement policies to strengthen their capability to use information technology.

While a developing country might have to rely largely on its individual efforts in formulating and implementing an effective policy on technology transfer, regional cooperation will enhance these efforts and ensure a less

[59] L.J. White, "The evidence on appropriate factor proportions for manufacturing in less developed countries: a survey", *Economic Development and Cultural Change* (October 1978).

costly and more rapid transfer of technology. There is at present a wide-ranging scheme of regional cooperation on technology among developing countries of the ESCAP region. These projects range from remote sensing to the development of non-conventional energy sources. What is needed is to ensure the successful completion of these projects and the effective dissemination and diffusion of the technology to all developing countries. In the mean time, it is necessary to initiate close regional cooperation in research and development on the new technologies. Given their limited technical manpower and resources but the wide spectrum of new technologies, it would be desirable for developing countries of the region to pool, or at least coordinate, their research and development resources. By specializing and avoiding duplication, those countries will be able to advance more rapidly in harnessing the new technologies, a development that would be greatly facilitated by regional cooperation.

Regional cooperation among developing countries of the ESCAP region may also help to reduce the cost and improve the effectiveness of technology transfer. Several countries, including India, Malaysia, the Philippines and the Republic of Korea, have already established specialized agencies to regulate and monitor the transfer of technology. The approach to technology import regulation varies from one country to another.

India has an elaborate screening mechanism for technology transfer. Proposals for foreign collaboration have to be screened by the Technical Evaluation Committee, composed of a number of government and government-related technical agencies. The Committee judges each proposal on the following criteria: (a) availability, or the prospect of availability, of indigenous technology; (b) reasonableness of payments; (c) technical competence of the technology suppliers; and (d) how essential the technology is to the country. The terms and conditions laid down by the Government are relatively stringent. For example, the royalty is not normally allowed to exceed 5 per cent of the gross sales.

In the Republic of Korea, the management of imported technology has completed a full cycle, starting with a control-free system, followed by a fully regulated system, then an automatic approval system, and now a simple reporting system. Unlike many other countries, the Republic of Korea is interested not only in minimizing the cost and conditions attached to imported technology but also in ensuring effective transfer. Thus, the negotiating capacities of domestic enterprises with respect to technology contracts are supplemented by the provision of advisory services, including an effective technology infrastructure.

The impact of managing technology transfer has not been subjected to any systematic analysis. Studies show in general that countries without screening mechanisms tend to pay higher costs for technology. For example, in Thailand, where no regulatory measures exist, the royalty stipulated in technology agreements often exceeds 5 per cent of gross sales. In addition, several agreements have an unlimited duration, forcing licensees to pay for a technology long after it has became obsolete. On the other hand, a case study of the Malaysian experience indicates that technology prices are negotiable; many agreements that are often stated to be "standard" agreements and used world-wide can be renegotiated at lower costs. Government regulations have also successfully eliminated most of the restrictive business conditions imposed on Malaysian agreements. In short, it would appear that there are some advantages in regulating the transfer of technology.

For this reason, more and more countries are considering plans to set up technology transfer agencies. It would be desirable to strengthen the role of the Asian and Pacific Centre for Transfer of Technology located in Bangalore in coordinating the activities of these various agencies. Such coordination will ensure a more intensive level of competition in the regional market for technology and enable the developing countries of the region to obtain better technology at a lower price. Closer coordination of technology transfer policies will also prevent technology sellers from "playing" one developing country against another by threatening to withdraw technology collaboration projects in search of higher returns. Coordination and cooperation in technology transfer policies will help developing countries accelerate the development of indigenous technology and facilitate their diffusion to other countries in the region. In the long run, regional cooperation in technology transfer will help developing countries of the region reduce their technological dependence and narrow the technological gap with the developed countries.

In addition, regional cooperation to accelerate the transfer of technology can also take the form of training, exchange of experience, sharing of facilities and personnel and cooperating on the special needs of the least developed countries and island developing countries.[60] But whatever form such cooperation assumes, it is crucial in assisting developing countries of the ESCAP region in restructuring their economies.

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[60] ESCAP/UNCTC Joint Unit on Transnational Corporations, *Technology Transfer under Alternative Arrangements with Transnational Corporations, 1987*, Publications Series B, No. 11.

C. AN AGENDA FOR THE FUTURE

Progress will be slow in developing suitable mechanisms for regional cooperation which would facilitate the restructuring of developing economies of the ESCAP region. The relatively low volume of intraregional trade and investment flows, as well as the diversity of interests among the economies of the region, all suggest that it will take time to achieve concrete results. Institutional development is necessarily a slow process; institutions evolve gradually, with phases of activity interspersed by periods of reflection. The proposals set out below should therefore be seen as ideas pointing to the possibilities and potential of regional economic cooperation rather than as a set of specific arrangements to be instituted forthwith.

1. Objectives and principles

To set in motion the development of regional economic cooperation as an instrument for promoting restructuring policies, it would be necessary to agree on a set of common principles acceptable to all economies of the diverse ESCAP region. The main objective would be to restructure the economies in the region in line with the new international division of labour and to help accelerate growth and development in the region. The second imperative would be to ensure that the accelerated growth and development in the region will not be at the expense of the physical environment, either within the country or in its geographical neighbours. A third guiding principle of regional cooperation would be to avoid the emergence of economic and social disparties in the region and to bring the low-income and least developed countries into the mainstream of regional development through trade, investment and resource transfers.

There is also a need for the economies of the ESCAP region to agree on the principles on which the modalities of economic cooperation should be based. First, cooperation should recognize the diversity of the region, including differing social and economic systems and current levels of development. Second, in accordance with the interests of the economies of the region, cooperation should not weaken the open multilateral trading system which provides the basis for development in the region. Third, cooperation should build up and complement existing organizations in the region, including subregional groups such as ASEAN and SAARC. Finally, regional economic cooperation should not be confined to the official level but should promote initiatives from the private sector and the non-governmental organizations and should utilize their vitality to the maximum extent possible.

2. Institutional framework

Having agreed on the broad objectives of regional economic cooperation and the principles on which it should be based, a second and related activity is to define the institutional framework. New institutional arrangements need not imply the creation of new organizations. Existing organizations could broaden the scope of their work or shift the emphasis between different activities within their present charter of responsibilities. Nevertheless, a new institutional arrangement seems to be called for in order to coordinate and delineate the major directions for regional economic cooperation in the light of the current global challenges. This could best be achieved by the establishment of a thematic committee on regional economic cooperation as agreed, in principle, by the Commission at its forty-seventh session.

While the terms of reference, composition and operational modalities of the committee will be considered at the forty-eight Commission session in 1992, the following paragraphs reflect the current thinking of the secretariat on the thematic committee on regional economic cooperation.

In designing an institutional framework for a regional cooperation arrangement, the need for organizational simplicity and efficiency should be given very high priority. It is also necessary to reconcile considerations of efficiency and economy to the greatest extent possible. Above all, the interests of member countries should form the basis of any arrangement to strengthen regional cooperation.

Keeping in view the above parameters, and consistent with the terms of reference of the Commission, a high-level committee for regional economic cooperation within the intergovernmental structure subsidiary to the Commission is essential. The Committee would be entrusted with the responsibility of giving an impetus to the promotion of enhanced regional economic cooperation under the overall supervision of the Commission. In the context of the dynamism displayed in recent years by several members, which seems to be spreading to other countries of the region, as well as the overall pace of development, the Committee should focus attention on certain specific fields, as well as meet as often as required but not less than twice a year.

Specifically, the Committee should deal with policy issues concerning the promotion and strengthening of regional cooperation, review its work programme and discuss and recommend appropriate policy initiatives and practical measures to promote regional economic cooperation for development, which should be submitted to the Commission for its consideration. Since regional economic cooperation would depend so heavily on political will, it would be appropriate for the representation on the committee to be at the ministerial or sub-ministerial level. In order to be able to meet at short notice, if necessary, and perform its duties expeditiously and in a cost-effective manner, the Committee should be a representative body of a limited number of members, with the possibility of others contributing to the consideration of issues in which they are involved.

The Committee could recommend establishing task forces on specific subjects identified by it, and approved by the Commission, such as the enhancement of flows of financial resources to and within the region, the promotion of intraregional trade and investment, the transfer of technology and the facilitation of regional restructuring of the economies. It could also consider similar action-oriented measures, such as the establishment of working parties and the commissioning of studies. In undertaking these activities, the Committee could involve private sector organizations, such as chambers of commerce, which deal with various issues that offer a potential for regional cooperation in the areas of trade, industry, investment and technology. The task forces could deal with issues of concern in their multidisciplinary dimension by drawing on the experience and expertise available within the secretariat.

In conclusion, the widespread interests of the countries in the region in forging greater economic cooperation have been amply manifested in the several initiatives and arrangements at different levels. Given the great diversity of the Asian and Pacific region, the varied and manifold needs of its populations and its differing priorities, promotion of regional economic cooperation within a definite framework would be a complex undertaking. Yet, developments within the region and outside, as well as the growing potential for cooperation provide compelling grounds for the establishment of an institutional framework for economic cooperation covering the entire ESCAP region, under the Commission, if the region does not wish to lose the opportunity created by the momentum for development through partnership.

3. Analytical tasks

In laying the ground for the institutional framework, it would be useful to undertake various studies to analyse intraregional linkages. Important areas to be explored would include the identification of common problems, such as barriers to the region's manufactured exports, and specific identification of the "forces of change". These could include changes in international competitive positions, new products and technologies, particularly in export markets, changes in the structure of demand in the surplus economies in the region as well as in export markets outside the region, and changes in the production structure of the developing economies of the ESCAP region.

The objective would be to develop an analysis that would aid in understanding the links between the changes outlined above. Evaluation is needed of how restructuring would help countries take advantage of emerging opportunities, and the specific manner in which regional cooperation could facilitate the restructuring process. The regional and the international effects of the restructuring process would also need to be evaluated. The existing data base could be expanded to better analyse regional cooperation, and the institutional framework discussed above could be further studied.

Finally, an important aspect of the analytical task would be to deepen understanding of the mechanism and potential for the transfer of savings from the surplus economies. The study of this aspect could be initiated through a "round-table" of policy makers, bankers and other experts.

D. CONCLUSION

The outlook for the world economy remains uncertain. Rapid changes are taking place, the most important of which are the single European market in 1992 and the opening of Eastern Europe. Economic management and development in such an environment call for innovative instruments of economic policy. In developing the concepts and instruments of regional economic cooperation, an important aspect that needs to be kept in view is that cooperation is not an end in itself but a means. Cooperation should not become a force that shuts the region off from the rest of the world. Rather, regional economic cooperation should enable the developing economies to interact more gainfully with the world economy, and to capture more efficiently the opportunities that the world economy offers. The reasons for the lack of success of earlier attempts at economic cooperation in the ESCAP region, as well as the limited economic content of subregional arrangements, need to be borne in mind in undertaking new initiatives. Monitoring and review of activities would help improve he possibilities of early results.

If past growth trends continue, by the year 2000 the Asian and Pacific region will have emerged as a new global economic power. This development will boost intraregional trade and investment and encourage countries to pursue closer economic cooperation. The resource-based ASEAN-4 economies complement the manufacturing-based Asian NIEs, while both groups complement the highly developed Japanese economy. In addition, the huge economic potential of China and India offers further opportunity and increased leverage for the region. All these possibilities provide considerable scope for regional economic cooperation, and the prospects are excellent for the establishment of a regional mechanism to act as a catalyst.

However, the problems facing such regional cooperation are formidable. The Asian and Pacific region encompasses not only countries at different levels of development but also countries having different economic, political and cultural systems. For this reason, Asian and Pacific cooperation may be more difficult to achieve than in other regions. The problems might be alleviated to a certain extent if the key actors in this region, Japan and the Asian NIEs on the one hand and India and China on the other, were prepared to seize the initiative. There is every indication that converging economic and political trends will induce these countries, and the rest of the region, to move in that direction.

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