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The Newly Industrializing Countries, Trade, and Adjustment in the OECD Economies

by Stephen Woolcock, London*

There has been much discussion of the Newly Industrializing Countries (NICs) in recent years and various studies of their impact have been made. Much of the concern about NICs in the industrialized countries is however based on what they portend for the future rather than their present impact. This article, which draws on the work of a group of researchers coordinated from the Royal Institute of International Affairs, London, discusses the implications of the NICs for trade and adjustment in the 1980s.

There are various possible definitions of an NIC, but one is essentially concerned with those developing countries which have emerged as significant exporters of manufactures. Included in any list of NICs are generally the Asian NICs such as Hong Kong, South Korea, Taiwan and Singapore, the Latin American NICs, Brazil and Mexico, but also the Southern European NICs such as Greece, Spain and Portugal, certain Eastern European Countries and finally China. Exactly which countries are included in any list of NICs is, however, less important than their implications for trade and adjustment in the OECD economies.

The non-OECD NICs account for about 8 % of total OECD imports of manufactures and the leading ten NICs account for about 80 % of total developing country exports of manufactures (cf. Table 1). Some impression of the relative importance of the Southern European NICs can be gained by considering that Spain exports about as much as Taiwan whilst Greece and Portugal export less than all of the above NICs with the exception of the last three. Macro studies¹ have shown that the OECD economies have a trade surplus with the NICs, so why, one might ask, all the fuss?

Impact of the NICs

Certainly it would be wrong to overstate the problems caused by the NICs, but it is necessary to consider the concern, expressed by governments and interest groups in the industrialized countries, which

ranges from the general problems of accommodating countries of different levels of development in a single trading system, to the particular problems caused in specific industries such as textiles and clothing. At the general level there has been some concern expressed that the NICs may become new Japans, and thus present a major competitive challenge to the advanced industrialized countries (AICs). In practice however, none of the NICs are likely to even approach Japan's performance. Countries which could, potentially, follow the Japanese model of development, such as South Korea and Taiwan, are constrained by the size of their markets, political instability and the relatively poor international economic climate of the 1980s compared to the 1950s and 1960s when Japan was reindustrializing.

Whilst the impact of NIC exports to Europe or North America fades in significance when compared to Japanese exports, imbalances in trade with the NICs can be expected to cause some friction during the 1980s. The OECD countries as a whole have a trade surplus with the NICs but the benefits of this trade are not always evenly distributed. For example the four Asian NICs, which account for more than half of NIC exports, have a trade deficit with the leading AICs (cf. Table 2), but this is entirely due to Japan's surplus with these countries. Japan's success reflects its geographical proximity but also its willingness to accept an international division of labour with its neighbouring NICs.

* The Royal Institute of International Affairs.

¹ OECD: The Impact of Newly Industrializing Countries in Production and Trade in Manufactures, Paris 1979.

NIC Characteristics

It is not easy to identify the reasons for the relative success of the NICs compared to other developing countries, and therefore difficult to say which other developing countries are potential NICs. Hong Kong and Singapore have been forced to export in order to survive, having no domestic market or raw materials on which to base industrialization. Both are also strongly influenced by Chinese entrepreneurial skills which are now being exported to other countries in the region to some extent.

South Korea and Taiwan, unlike Japan have had to industrialize from scratch. These two countries have emerged for a number of reasons including the

restricted scale of domestic markets, lack of raw materials, certain historical factors and a relatively low paid but well educated labour force. Both Korea and Taiwan have consistently followed policies of outward-looking export-led growth, but such a policy is, by itself, no guarantee of success.

This is evidenced by the experience of the larger NICs such as Brazil. Between 1968 and 1973 Brazil followed outward-looking policies and showed that it has the potential of becoming a dynamic exporter, but its performance has not been consistent. As in the case of India the large domestic market in Brazil enables economies of scale to be achieved which would only be possible by exporting in smaller countries. The availability of raw materials, although not sufficient oil, might also have made the exportation of manufactures less imperative.

Mexico has been strongly influenced by its proximity with the United States. Whilst domestic supplies of energy reduce the pressure to export manufactures in order to pay for imported oil, a problem facing many other NICs, revenue from oil and gas exports will provide Mexico with the means to invest in industrialization.

Other energy rich countries have begun to develop oil or energy intensive industries, such as the Gulf States' involvement in base petrochemicals. Here as in other instances it is more what the NICs portend for the future than their established presence which is at issue.

The indications are that rather than representing the tip of an iceberg the existing NICs represent the larger part of the same. In other words, with possibly one or two exceptions, there are few other developing countries likely to emerge as NICs during the 1980s². It is therefore not so much a question of accommodating an ever increasing number of NICs but of accommodating the existing NICs in the international trading system, and adjusting to changes in the pattern of trade created by increased and more diversified NIC exports. This requires some qualification in that the Southern European NICs are likely to increase the pressure for adjustment in Western Europe. Greece, however, is already a member of the European Community and Spain and Portugal are applicant countries. Any friction concerning these low cost countries will therefore have to be dealt with largely within the EC.

Table 1
Leading Developing Country
Exporters of Manufactures

Country or territory	Percentage share			Cumulative share 1976
	1965	1975	1976	
Hong Kong	21.5	15.8	17.2	17.2
Taiwan	4.1	12.2	15.2	32.4
South Korea	2.3	11.7	14.8	47.2
Yugoslavia	13.4	8.2	7.4	54.6
Singapore	6.5	6.3	6.4	61.0
Brazil	2.7	6.2	5.1	66.1
India	17.6	5.6	6.1	72.2
Mexico	3.6	5.9	4.4	76.6
Argentina	1.8	2.0	2.1	78.7
Malaysia	1.5	1.9	1.75	80.4
Pakistan	4.1	1.6	n.a.	—
All developing countries	100	100	100	100

Source: Louis Turner et al.: Living with the Newly Industrializing Countries, Chatham House Papers, Number seven, The Royal Institute of International Affairs, London 1980.

Table 2
Trade Balance of
Hong Kong, South Korea, Singapore and Taiwan
with the Major OECD Countries¹
(in mn current US \$)

	1966	1970	1975	1977	1978
USA	+ 140	+ 387	+ 85	+3891	+5171
Japan	- 700	-1862	-4189	-6242	-9264
EC	- 149	- 245	+ 508	+1657	+ 978
FR Germany	+ 22	- 37	+ 389	+ 744	+ 646
France	- 18	- 104	- 164	- 29	- 254
Italy	- 35	- 64	- 48	+ 20	- 127
UK	- 184	- 115	+ 107	+ 328	+ 248
Total	- 1501	-2767	-6337	-2997	-5496

¹ NIC exports f.o.b., imports c.i.f.

Source: Derived from IMF, Direction of Trade, various issues.

² Cf. Colin Bradford: The Newly Industrializing Countries in Global Perspective, in forthcoming book on the NICs to be published for The Royal Institute of International Affairs.

The fact that one is concerned with a limited number of NICs in the next few years should make the process of graduation³ easier to manage. Major problems, however, are likely to remain, notably finding forms of graduation which are acceptable to both NICs and AICs. The NICs have resisted any suggestion that they should give up their status as developing countries, which gives them exemption from certain GATT obligations. Indeed Mexico has recently decided against joining GATT. On the other hand the AICs feel that the NICs cannot continue to expect to benefit from special and differential treatment in international trade when they become significant competitors.

Accommodating the NICs

Industrialists and trade unionists in the AICs point to the sometimes prohibitively high tariffs imposed on imports in some NICs. When industries in the AICs are under pressure due to slow growth in demand or high wage costs compared to the NICs, such a lack of reciprocity in trade is seen as "unfair" and a justification for import regulation. There is some justification for this argument, and trade based on the principle of reciprocity would provide the NICs with a bargaining position they often lack at present. Nevertheless one should not lose sight of the fact that no definition of *fair trade* exists. Until it does there is a real danger that *fair trade* will be used as a licence for defensive or protectionist measures.

There has been some progress towards accommodating the NICs. After initial reticence an increasing number of NICs are now signing, or expressing interest in signing, the codes on non-tariff barriers to trade drawn-up during the Tokyo Round of multilateral trade negotiations. There is still a long way to go, however, before all the problems can be resolved. For example the US recently sought to impose countervailing duties on certain imports from India on the grounds that India would not produce a

³ Graduation is the process in which what were previously developing countries progressively assume the responsibilities of industrialized countries.

programme for phasing out export subsidies. Initially the US had undertaken to waive countervailing duties provided the exporting countries signed the GATT code on subsidies which India has; there was no obligation to provide detailed programmes for phasing out existing subsidies. In short, there remain problems in the implementation of existing procedures and rules even if the NICs accept them.

There has also been an attempt to involve some of the NICs in the OECD on an ad hoc basis. This occurred when the steel committee of the OECD, set up to seek an international solution to the problems of the industry, invited India, South Korea, Mexico and Brazil to participate in consultations on the industry. The response was mixed with some countries expressing interest in the international standing such participation would bring, whilst others thought this was not worth risking their standing with the Group of 77 countries, who might see participation as a selling-out of developing country interests in the general North-South dialogue. Some NICs also rightly pointed out that the problems of the steel industry in the AICs were not of their making.

There have also been consultative meetings on the steel and petrochemical industries in UNIDO, and the now dormant Euro-Arab dialogue, which is thought to have contributed to a greater understanding, on the part of the Arab states, of the limited capacity of OECD markets to absorb increased capacity in the oil rich NICs such as Saudi Arabia. There has therefore been a series of ad hoc approaches to the problems arising from AIC-NIC trade, of which the multi-fibre agreements (MFA) regulating NIC exports of textiles and clothing, have been the most far-reaching. One should perhaps also mention the Generalized System of Preferences (GSP) introduced by the EC and other AICs.

In the longer term there may well be a case for considering how these ad hoc measures can be brought into a more coherent whole, which could provide procedures and rules governing trade between

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countries at different levels of development. Of more immediate concern in the 1980s, however, is the apparent failure by the AICs to abide by the norms and rules, embodied in the GATT, that they themselves have devised. One example here is the undermining of the principle of non-selectivity and the failure to fill the gap left by an ineffective Art. 19 of GATT on selective safeguards by agreeing on a safeguards code in the Tokyo Round.

The AIC Response

This brings us to the particular problems in AIC-NIC trade and the question of adjustment. The first sector in which friction occurred was textiles and clothing. A study of this sector will show that selective action against exporters is not a recent development. Indeed the origins of the MFA can be traced to bilaterals between the US and Japan back in the 1930s. These set a precedent for subsequent bilateral agreements in the 1950s, which were then extended to cover the then leading exporters of cotton products in the long term agreement (LTA) on trade in cotton in 1962. The LTA and its more comprehensive successors, the 1973 and 1977 MFAs were anticipatory in the sense that exports from developing countries only accounted for about 8 % of total world production in the relevant industries in each case. The justification for taking such anticipatory action to restrict imports was based on the concept of market disruption, initially introduced into the GATT negotiations on the LTA by the USA. Once introduced by the USA or Europe restrictive measures in a given sector by one have tended to have a demonstration effect on the other, so that there has been a progressive tightening of restrictions on NIC imports of textiles and clothing. The case of textiles and clothing therefore provides not only a useful example of how trade regulation can spread but also a dangerous precedent for other hard pressed sectors.

In the case of steel the EC introduced controls on the volume and price of certain NIC steel exports to the Community at a time when the NICs only accounted for some eight per cent of world steel production in 1976. NIC capacity in steel can be expected to grow faster than in the AICs as they industrialize, but in general terms they will not achieve self-sufficiency until the end of the 1980s. In steel as in textiles therefore the AICs have taken anticipatory action to regulate NIC exports. The problems of the steel industry stem from a slowing of demand in the AICs. NICs are at the most an irritant which has compounded the problems of the AIC industries.

In other industries also selective action has been taken against NIC exports. In colour televisions the US restricted exports from South Korea and Taiwan by means of orderly marketing agreements after these countries stepped up exports to fill the gap left in the US after Japanese exports had been similarly restricted. In Europe there are also voluntary restrictions on exports of TVs from the Asian NICs and there is pressure to make these general restrictions for the EC as a whole as opposed to restrictions on imports into certain EC member states.

Changes in the pattern of trade in the form of increased NIC exports of clothing, TVs or other standard technology-price sensitive products is not the only structural change taking place in the AIC industrial structures. Increased energy costs are affecting energy or raw material intensive lines of production, there is a general slowing of growth which makes adjustment more difficult. Increased uncertainty caused by inflation and unstable exchange rates has also made investment more defensive so that innovative investment in new technologies has been affected. The impact of the NICs comes in addition to these changes, and it is important to see the impact of the NICs in this perspective. In textiles and clothing the NIC competitive challenge is of more central importance than in all the other sectors. This industry remains important in the AICs, despite its relative decline in recent years, largely because of its role as a provider of employment. In 1978 textiles and clothing provided between 4.5 % (Sweden) and 15 % (France and Italy) of industrial jobs in the OECD countries. The fact that NIC competition has tended to be concentrated in specific sectors has also strengthened the trend towards industry orientated trade policies and increased the demand for effective adjustment within the AICs.

Adjustment to NIC Competition

In the market economies of the OECD countries the prime responsibility for bringing about adjustment to increased NIC import competition or other structural changes rests with industry itself. Studies of various sectors suggest that corporate structure and strategies can influence whether a sector responds defensively or not.

Table 3 shows the general characteristics of some of the more important sectors in which the NICs have a presence. Major and repeated protectionist responses by AICs have occurred in sectors with a relatively low degree of multinationality (i. e. sectors in which there

are few multinational companies operating) of major companies and low product diversification, reflecting locational and product adjustment. Sectors which are important providers of industrial employment, either nationally or regionally, have also shown a high incidence of protectionist responses.

A detailed study of corporate strategies⁴ suggests that companies which develop longer term corporate strategies are more likely to adjust successfully than those operating on short term objectives. An important component of successful corporate adjustment has been the ability to drop lines of production once demand stagnates or NIC competition increases. Companies which have attempted to regain lost competitiveness in existing lines of production which face sluggish growth in demand and increased price competition have seldom been successful in the long run. Such defensive investment in existing product lines in order to increase productivity has reduced employment levels, as is clearly shown by the case of textiles. Such investment, however, increases capacity unless obsolete capacity is closed, which has not always been the case. The need to improve productivity still further often results from the intensification of competition, prices fall, and profit margins are reduced to a minimum. This has been especially the case in man-made fibres, but also steel. The companies concerned, and thus in some cases the industry, are then highly susceptible to any fluctuation in demand or increase in import competition.

Company strategy must therefore take account of long to medium term structural changes in industry, including the growth of NIC competition in certain more mature technology-price sensitive lines of production.

⁴ L. G. Franko: Corporate Responses to Export Thrusts of Newly Industrializing Countries, in forthcoming book on the NICs to be published for The Royal Institute of International Affairs in 1981.

In this regard the provision of information on global trends in industrial structure would help companies to adjust while they are still strong enough to do so without some form of temporary or permanent support. Such information would be particularly useful for small or medium sized companies which cannot afford to generate information themselves.

Better Use of Existing Instruments

At the national level there are often painful trade-offs between corporate viability and national employment or industrial policy objectives. Invariably some countries such as the UK, Italy and to a lesser degree France are relatively more dependent on NIC competitive industries. This implies that there may be greater recourse to measures designed to slow the pace of adjustment in such countries. In the USA specific trade related adjustment assistance programmes have been introduced, but in Western Europe governments already have well established policy instruments in the form of regional, social, industrial or manpower policies. In Europe therefore it is more a question of how such instruments can be used to promote adjustment to changes in the international division of labour rather than whether new adjustment assistance measures should be introduced.

At the national level there is also a case for taking a close look at the trend towards *fair trade*. Fair trade often involves providing domestic assistance to a particular industry in order to compensate for *unfair* advantages favouring foreign competitors in the same industry. A case in point is control of imports of textiles and clothing into the AICs in order to compensate for NIC export subsidies, tariffs, but primarily lower wage costs. Fair trade is therefore industry orientated as opposed to general welfare orientated *free* trade in which industries within a country compete for

Table 3
Some Characteristics of Industrial Structure by Sector in Advanced OECD Countries

Industry	Multinationality of Major Companies	Product Diversification of Major Companies	Presence of State Ownership	Importance in Total Employment in Manufacturing
Steel	Low	Low	High	High
Base Petrochemicals	High	High	Medium	Low
Synthetic Fibres	High	Medium-High	Medium-Low	Low
Clothing	Low	Low	Low	High
Consumer Electronics	High	High	Negligible	Medium

Source: Louis Turner et al.: Living with the Newly Industrializing Countries, op.cit.

resources. Fair trade also tends to neglect that subsidies provided to a foreign competitor benefit the domestic consumer.

It would be wrong to over-emphasize this point as it is, of course, far from simple to return to free as opposed to fair trade. The AICs still depend on manufacturing, and short term gains for consumers often entail long term costs for certain industries. Nor can one expect to remove selective import controls or public subsidies over night. All AIC governments intervene selectively to provide some form of assistance to specific industries, so one must look to ways of improving the existing forms of intervention. To put it in the terminology adopted by the OECD secretariat, intervention must be made more positive.

Need for Multilateral Surveillance

Assistance provided in the form of reconversion aid for those affected by the decline of an industry is least likely to create friction in international trading relations because it involves no subsidy for producers. It does however, require that industry and government accept that the industry will decline in importance. As this is seldom accepted, many governments provide some form of restructuring aid in an attempt to regain lost competitiveness. The provision of restructuring aid is

likely to lead to claims of unfair trade and the provision of compensatory aid by the governments of industries elsewhere. There is then a need for some form of multilateral surveillance and control over such subsidies. So far the GATT has only developed a means of coping with export subsidies and only the EC Commission has powers to control domestic aid so as to ensure that it promotes genuine or positive adjustment.

Whilst international constraints of this kind are needed, experience in the EC suggests that this will not suffice without constraints at the national level. One constraint on national defensive policies is the cost of supporting excess capacity. Such a constraint has been operative in France and the UK in the steel industry, where the scale of public support for the industries was such that retrenchment was forced through in order to reduce the costs incurred by national exchequers. Where the costs of providing assistance to an industry are visible there is less likelihood that assistance will become permanent. In the case of regulating imports from the NICs the costs, though real for the NICs and AIC consumers, are not visible. Consequently there is less pressure to make such assistance for AIC industries temporary and digressive.

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