Lorenz, Detlef

Article — Digitized Version

New situations facing the NICs in East Asia

Intereconomics

Suggested Citation: Lorenz, Detlef (1986) : New situations facing the NICs in East Asia, Intereconomics, ISSN 0020-5346, Verlag Weltarchiv, Hamburg, Vol. 21, Iss. 6, pp. 263-268, http://dx.doi.org/10.1007/BF02925171

This Version is available at: http://hdl.handle.net/10419/140048

Terms of use:
Documents in EconStor may be saved and copied for your personal and scholarly purposes.

You are not to copy documents for public or commercial purposes, to exhibit the documents publicly, to make them publicly available on the internet, or to distribute or otherwise use the documents in public.

If the documents have been made available under an Open Content Licence (especially Creative Commons Licences), you may exercise further usage rights as specified in the indicated licence.
New Situations facing the NICs in East Asia

by Detlef Lorenz, Berlin*

The newly industrialising countries (NICs) in the East Asian region are beginning to be faced with serious problems: problems involved not only in moving from an easy phase of import substitution to a more difficult second stage, but also in progressing from the first to the second more demanding phase of export orientation. Professor Lorenz analyses this new situation.

No sooner had it become more or less commonplace to say that the twenty-first century belonged to the Pacific than there appeared the first sobering reports of the "export-led slowdown" in the "gang of four", also known as the four little dragons or tigers. It was not only this group of countries that had to stomach an unaccustomed slowdown in growth, however; the so-called second generation of newly industrialising countries (NICs) in Asia, the ASEAN group, was hard hit by the fall in commodity prices, and China's new openness to foreign trade faltered as a result of sudden trade deficits. As Seiji Naya has observed, the NICs are "at the crossroads - they will have to decide whether to continue with export-oriented strategies or to change their policy orientation. It is ironical that this occurred at a time when other developing countries are making efforts to follow in the footsteps of the fast growing Asian NICs."4

The East Asian region (EAR) should be considered as comprising primarily the "four little dragons" - the NICs in the narrow sense - and the ASEAN NECs (newly exporting countries), or second generation of near-NICs.5 However, regional interdependence is such that neither Japan nor the People's Republic of China should be left out of the picture; indeed, these two major economic powers have a strong influence on the regional balance. The analysis that follows will nevertheless concentrate mainly on the NICs and NECs. The well-known and much discussed bilateral imbalance between Japan and the USA need not concern us here, but the regional imbalance between the EAR including Japan will be examined in detail below. First, however, it is necessary to describe the present situation of the new "industrial countries" of the EAR, so that the diversity of the region can be appreciated fully.

3 "The year 1985, however, signalled what appeared to many as a period of transition for Asia's much-heralded four little dragons. For the first time in 10 years, none of the four managed to grow by 6%. Their trade growth fell below the world average - a rarity for these economies which have become accustomed to 20% trade expansion annually." A. U. Periuet: The Asian NICs: in Transition?, in: Staff Memos, No. 10 (1986), Center for Research and Communication (Manila), p. 2. Meanwhile the slump seems to have been of a more temporary nature (compare Korea's development in 1986 for instance).
5 The Asian NICs are usually defined as Hong Kong, Singapore, Taiwan and South Korea; the ASEAN countries, or Asian NECs, are Singapore, Malaysia, Indonesia, Thailand, the Philippines and Brunei. Singapore's dual role is discussed further on in this article; Brunei will be left out of account, so that we are left with two groups of four countries.
generated by imports of development goods. This might ease the pressure caused by an ambitious export-oriented policy, provided the policy of liberalising foreign trade is not hampered by the problems of modernisation anyway. The reported precariousness of China’s situation in this regard has been proved dramatically by the sudden deterioration in the trade balance and movements in the country’s foreign exchange reserves. Both developments are also closely connected with the policy of establishing “free economic zones”, which has recently come under renewed strong criticism. 6

ASEAN and Integration

If one regards the member countries of ASEAN as a self-contained region – a view that may still be rather premature for a variety of reasons – this group of NECs is also a major unit not dissimilar to China, since it too has many EPZs. However, the successful export-oriented industrialisation of the ASEAN countries cannot conceal the fact that their industrial capacity is of course still not comparable with China’s, at least in quantitative terms. Along with the slowdown in the growth of industrial exports, this predominance of agriculture and raw materials has been an important contributory factor in depressing ASEAN economies as a result of the substantial deterioration in the terms of trade. 8

The significance of the community factor depends on the importance of regional economic policy; it is indicative that ASEAN politicians speak of co-operation within the community, not integration. It is probably safe to assume that until now the political aspects of ASEAN have been more important than its economic attributes. Economically, the region displays great diversity as regards not only the level of development and economic potential but also the accent of national reservations and interests. That has not prevented countries pursuing the same outward-looking policy, especially as regards the promotion of industrial exports and efforts at liberalisation, 9 including the liberalisation of domestic policy, but this aspect of community co-operation is to some extent “grafted on”, encouraged partly by the favourable conditions in world markets until the early eighties and partly by the general swing of development ideology in many developing countries towards greater deregulation in many spheres.

Until now, the ASEAN countries have lived with such a laissez-faire co-operation policy 10 without putting integration policies seriously to the test. Perhaps they have themselves been swayed by the propaganda value of their co-operation-based community, which is unique

9 See M. Ariff, H. Hill, op. cit.
among developing countries. However, the recent proposal to create an ASEAN common market by the year 2000 has revealed the shortcomings that had previously remained concealed. The new policy of integration, which is being urged particularly strongly by the Philippines for obvious political reasons, is an attempt to boost flagging intraregional development by generating compelling exogenous factors. This would entail reducing customs barriers in clearly defined stages within a customs union, but it would also mean employing other methods of expanding intra-industry trade via various co-operation or "complementarity" agreements. The task that still lies ahead can be gauged from the uncompromising summary of developments so far drawn by Rieger: 13 "... the ASEAN countries do not seem ready to move beyond the rhetoric of ASEAN cooperation to the establishment of mutually beneficial trading systems in the region. On the contrary, a review of developments in 1985 shows that, while ASEAN countries were united in deploring the protectionist measures of others, that solidarity was sadly lacking in internal relations."

Part of the problem stems from the diversity of a community consisting of such different countries as Singapore and Indonesia, or Malaysia and the Philippines. Since each of the countries has very strong national interests to defend, the Philippine integration proposal was rejected in the community's decision-making bodies. Quite apart from the question whether countries are willing to co-operate or integrate, the community faces a number of knotty problems that are to some extent a legacy of the past. One of these is the inordinately high level of trade between Singapore, Indonesia and Malaysia; trade among member countries is contracting noticeably if Singapore's traditional entrepot trade is excluded. 14 Another problem is the "Singapore syndrome", which consists in the fact that this far more highly developed city state (with NIC status) is also a member of the community of ASEAN NECs, where it is at home geographically and geopolitically rather than economically. This raises the economic problem that none of the forms of integration offered by trade theory and trade policy suit ASEAN if Singapore remains a member. According to Rieger's compromise proposal, this would be feasible only if the four "genuine" ASEAN states formed a customs union among themselves and collectively established a free trade area with Singapore. This would be the only way of preserving Singapore's traditional economic function, although even this is a contentious issue within ASEAN.

The "Four Little Dragons"

We come finally to the "four little dragons", the first of the true NICs and the ones that have been the most successful in the past. A comparative assessment of their recent performance shows surprisingly that Singapore had the worst record here too. 14 Each of the four states has been affected by specific exogenous and endogenous factors, such as the crisis in oil refining and the problematic policy on wage increases in Singapore, the China connection and the slowness to diversify in Hong Kong, Taiwan's particularly heavy reliance on the USA coupled with structural weaknesses and incomes policy problems, and the controversial policy of restructuring in South Korea, with its emphasis on "older" capital-intensive industries such as shipbuilding and vehicle manufacture, and the shortcomings of the "chaebols", the Korean version of the Japanese "zaibatsu"; nevertheless, there are a number of general trends and similarities that deserve to be highlighted. Surprisingly, they cast doubt on a number of clichés that are often associated with the economic miracles in the four paragons of neo-classical market theory.

For example, Chen 15 speaks of the misconception of many western economists (including Milton Friedman) "... that the Asian NICs represent the dreamland of the classical economists ... What distinguishes the Asian NICs from other developing countries is the effective implementation of export-promotion policies. This is brought about by an efficient, growth-oriented government and a harmonious government-business relationship in all Asian NICs." However, the example of Singapore shows that powerful assistance from the state does not guarantee faultless economic development. On the contrary, the "enlightened" developmental states have to accept serious criticism on issues such as the policy of raising wages, which was the main cause of Singapore's loss of competitiveness. On the other hand, the city state also displays cyclical
steadily gaining ground. the setback suffered by the NICs, a realisation that is another cliche is only partly to blame for economies (for example, hotel building, the construction of public housing and infrastructure projects) that the overheating and speculative activities typical of market economies (for example, hotel building, the construction of public housing and infrastructure projects) that the interventionist state has not taken steps to offset. To this extent, the protectionism practised by the industrialised countries – another cliche – is only partly to blame for the setback suffered by the NICs, a realisation that is steadily gaining ground.

Another important point is also being realised, namely that the development of the NICs that occurred in the favourable world economic climate of the sixties and seventies was quite exceptional and that it was too rapid and occurred in too many countries simultaneously to be long-lasting. The result was convergence towards a uniform economic structure and a massive multiplication of production capacity that could not possibly be matched by a corresponding growth in demand. To that extent, it would be well worth considering a slower expansion in future, despite the need for economic restructuring. "Economic recovery at a slower pace reduces the likelihood and the severity of potential bottlenecks in the future, because the economy would have more time and greater scope to respond to the shortages which might occur. At the same time, it would give the industrial countries greater room for adjustment, provided their mercantilistic competition did not itself lead to too rapid a "creative" destruction of market potential (Schumpeter).

There are other dangers or difficulties facing almost all NICs and NECs, including those in Latin America. Cheah's remarks regarding Singapore can be applied more widely: "In this respect, Singapore's development efforts to move into higher technology products and industries are drawing it closer to 'big league' competition; the stakes and the risks are substantially greater." However, it is not only international displacement competition that is causing the NICs serious problems; they showed an exemplary ability to adapt in the past, but the challenge may be too much for them in future. The control of modern economies by free market mechanisms or interventionist instruments is becoming ever more complex and complicated owing to rapid technological progress. The NICs are increasingly coming up against the capacity limitations of domestic markets and human resources. Chen points very plausibly and forcefully to the problems involved not only in moving from an easy phase of import substitution to a more difficult second stage, which is generally acknowledged to be a problem, but also in progressing from the first to the second more demanding phase of export orientation. Korea, Taiwan and to some extent Singapore as well appear to be embarking upon a doubly difficult mix of both strategies: "Thus, the Asian NICs have all entered a new stage of economic development, the transformation of EO 1 to EO 2. In this phase of development, production is no longer always for export. Many heavy and capital-intensive products are meant for the home market. This can therefore be called the secondary import-substitution-cum-export-promotion strategy of economic development, particularly in South Korea and Taiwan. The prospects of the Asian NICs hinge on how quickly and successfully they can attain sustained growth under EO 2." During this process, the mutual competition between NICs and NECs (country substitution) will make matters more difficult, a situation that Periquet has described aptly as follows with regard to the NICs: "For as they struggle to carve a market niche for themselves in the heavy and skill-intensive industries, the next batch of prospective Asian NICs – Malaysia, Thailand and the Philippines – are nibbling away at their comparative advantage in labour-intensive manufactures." Regional Imbalance

It is not possible to examine here the probable further course of the interesting and difficult process of adjustment in the NICs and NECs, but it does seem necessary to look more closely at the regional imbalance in the world economy associated with the EAR. The first point to note is the trade imbalance that has stubbornly persisted until the present day, and which consists in disproportionately large growth in trade with countries outside the region. This situation was analysed clearly and in detail in 1983 by a Japanese study, which found that "...the ultimate destination of exports from the region, in spite of the notable

---

16 In the seventies despite the exogenous oil price shock, but with the benefit of the boost in purchasing power it provided as a result of recycling.
18 Cheah Hock Beng, op. cit., p. 311.
21 Cheah Hock Beng, op. cit., p. 300.
23 E.Y. Chen, op. cit., p. 152.
development of intermediate commodities trade within the region, has been predominantly outside the region, mainly the United States and West Europe, and drew the logical conclusion that "... it seems only natural... to search for possibilities for more active intra-Pacific trade".  

The Japanese bias in East Asian countries' extraregional trade emerges particularly clearly from a more recent study by Branson, from which the figures in Table 1 are drawn. This shows that in 1981 the Asian NICs imported industrial goods in roughly equal proportions from Japan on the one hand and the USA plus the EC on the other (around $30 billion worth from each). However, Japan took only about 13% of the NICs' exports to the three industrialised countries or country groups, whereas the share of the USA was significantly larger (55%) and that of the EC more than 30%. Whereas the ASEAN group's dependence on Japan as an outlet for its exports of primary products (Table 2) is to some extent a natural consequence of that country's geographic proximity, the picture is very different as regards exports of industrial goods, particularly from the NICs of North-East Asia. In this regard, differences in structural factors and levels of protectionism in the three industrialised countries or country groups mean that in particular Japan, the hub of the Pacific region, has emerged as a problem case that has been severely criticised for some time.

This trade imbalance between the region and other groups of countries is not only an encumbrance to Japan as the leading power in the area and heightens protectionist pressure in the USA, it also affects the European position. It will undoubtedly strengthen expectations that the European markets will have to perform a "vent-for-surplus" function under the diversification policy of the NICs and NECs, in other words to serve as an alternative to the restricted Japanese market and as a substitute for the loss or slower expansion of sales potential in the USA. Moreover, the current theory about growth markets in the Far East will be qualified, since the regional imbalances cannot be attributed solely to the assumed inferiority of Western Europe or the EC in "trilateral competition". Admittedly, the competition for market shares in the Pacific basin will intensify, since the easier markets for European and American goods in the Arab oil states and Latin America have declined in importance. The losses sustained by OPEC and the import restrictions imposed in Latin America in connection with the debt crisis mean that these countries will certainly not be large importers in the future either. Whether the regional imbalance can be reduced by greatly expanding European and American exports to the Asian NICs is open to doubt, however.

In the final analysis, heed should be paid to the argument that the blatant trade imbalance between the

---

### Table 1

**Distribution of Developed Countries' Imports and Exports of Manufactures from/to Asian NICs, 1981**

<table>
<thead>
<tr>
<th></th>
<th>Imports (in billion $)</th>
<th>Exports (in billion $)</th>
</tr>
</thead>
<tbody>
<tr>
<td>EC</td>
<td>13.8</td>
<td>15.4</td>
</tr>
<tr>
<td>USA</td>
<td>25.0</td>
<td>14.6</td>
</tr>
<tr>
<td>EC + USA</td>
<td>38.8</td>
<td>30.0</td>
</tr>
<tr>
<td>Japan</td>
<td>6.0</td>
<td>30.7</td>
</tr>
</tbody>
</table>

**Source:** W. H. Branson: Trade and Structural Interdependence Between the U.S. and the NICs, Draft, prepared for NBER Conference in Kuala Lumpur, January 1984 (Revised May 1984).

### Table 2

**Exports and Imports of ASEAN to/from Japan, the USA and the EC**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Japan</td>
<td>0.5</td>
<td>0.9</td>
<td>0.8</td>
<td>8.2</td>
<td>16.8</td>
<td>16.4</td>
</tr>
<tr>
<td>Exp.</td>
<td>7.1</td>
<td>10.6</td>
<td>11.8</td>
<td>1.8</td>
<td>3.2</td>
<td>0.5</td>
</tr>
<tr>
<td>Imp.</td>
<td>1.7</td>
<td>3.2</td>
<td>4.0</td>
<td>5.6</td>
<td>8.0</td>
<td>5.0</td>
</tr>
</tbody>
</table>

**USA**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Exp.</td>
<td>4.4</td>
<td>6.4</td>
<td>7.4</td>
<td>0.8</td>
<td>1.4</td>
<td>0.6</td>
</tr>
<tr>
<td>Imp.</td>
<td>1.2</td>
<td>2.4</td>
<td>2.4</td>
<td>3.9</td>
<td>6.0</td>
<td>3.3</td>
</tr>
</tbody>
</table>

**EC**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Exp.</td>
<td>2.6</td>
<td>4.4</td>
<td>7.4</td>
<td>0.8</td>
<td>1.4</td>
<td>0.6</td>
</tr>
<tr>
<td>Imp.</td>
<td>1.2</td>
<td>2.4</td>
<td>4.0</td>
<td>3.9</td>
<td>6.0</td>
<td>3.3</td>
</tr>
</tbody>
</table>

---

1 SITC 5 to 8 less 67 and 68

East Asian region and other regions or countries is a stumbling-block to the satisfactory development of the international division of labour, and hence to interdependence. International co-operation via international organisations, which is frequently demanded, will only operate reasonably well if structural distortions do not become excessive. Consideration should therefore be given to reducing the extraregional imbalance by intensifying trade within the region, as suggested by the Japanese study quoted above. The controversial problems of encouraging greater South-South trade cannot be discussed here, but experiences in the EAR and other considerations suggest that intraregional trade may have a role to play in counteracting centrifugal tendencies.

**Perspectives**

The revealing book by Ariff and Hill, the paper by Erzan and Laird and as yet unpublished studies by the Asian Development Bank in Manila and the East-West Center in Honolulu provide evidence that intraregional (and intra-industry) trade within the ASEAN region and between these countries and the three other NICs in North-East Asia (Taiwan, South Korea and Hong Kong, and possibly China as well) is indeed expanding. Nevertheless, it is no secret that there are many widely reported obstacles in the way of a deliberate and substantial expansion in intra-industry trade via “complementarity agreements” within ASEAN, for example. The diversity of interests in East Asia is still too great for this and the reciprocal protectionism within the region is a barrier that will be overcome only slowly.

Naturally it is also argued that markets in the industrialised countries still offer a better return than the slowly developing domestic markets of the NICs and NECs themselves. The NICs and NECs send two-thirds of their industrial exports to the industrialised countries, and of course there can be no question of their redirecting this volume entirely towards less prosperous developing countries, practically no one envisages a shift of this magnitude. At most, there can only be fairly substantial corrections of asymmetry or distortions, not a radical change of course. In this connection, the following comment by Langhammer and Spinanger is particularly noteworthy and seems to fit ASEAN like a glove: “The ‘second generation’ countries that reached the threshold of industrialisation later and whose industrial structure is therefore not yet as firmly set are more likely to redirect their exports than the leading developing countries. Most of their exports of finished products also go to the industrial countries, it is true, but they are still relatively small in volume and are not tailored so strongly to specific export markets as those of the first generation. In the short term, therefore, changes in the regional structure of exports are more likely to occur among the second generation of developing countries.” Such a shift in emphasis between trade outside the region and within it may produce inappropriate preference policies, but it must also be realised that the regional imbalances that have developed do not facilitate international co-operation either. However, rather than continuing with further theoretical considerations along these lines, let us close with a look at the actual situation of Japan.

As has already been stated, Japan not only has its own bilateral imbalance in trade with the USA and the EC, but it also fosters the imbalance in the trade of the entire EAR in industrial goods with other regions. The figures contained in Tables 1 and 2 illustrate Japan’s chronic surplus in trade in industrial goods with the Asian NICs and NECs, which offset their deficits by shipping not only primary products to Japan but also a disproportionate share of their industrial exports to the USA and Europe. In their above-mentioned study, Yamazawa et al. have advocated intensifying the incipient vertical division of labour between Japan and the Asian developing countries; Japan would increase its imports of simple industrial substitute goods to offset its rising exports of complementary (“intermediate”) goods induced by the import demand of rapid industrialisation in the NICs and NECs. Such a pattern or strategy provides no safeguard against imbalances, however, since it does not preclude continued “export-surplus-led growth” by Japan, something that the latest study by Yamazawa does not rule out. It remains to be seen whether the substantial appreciation of the yen and efforts to strengthen regional co-operation among NICs and NECs, including an expansion in intraregional direct investment, will bring a change in the situation.

---

34 Cf. R.J. Langhammer, D. Spinanger, op. cit., p. 89.