

Fischer, Bernhard

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Bernhard Fischer\*

## Developing Countries in the Process of Economic Globalisation

*The last decade has witnessed the emergence of a more global economy reflecting the continued rise in trade (especially of manufactures) as a proportion of output, a major shift of international specialisation, faster diffusion of technical progress and the globalisation of financial markets. What have been the effects of this process on developing countries?*

While economic globalisation and interdependence creates the potential for advancing human welfare around the world, a very striking feature of this process has been its uneven diffusion. Among developing countries, only a few have been able to participate in this process, to substantially improve their income levels and social standards and thus successfully adapt to the new possibilities for international specialisation.

Differences in basic economic, social, demographic and other development conditions, as well as domestic policies and the related diverging capacities to cope with the economic shocks and structural change of the 1970s and 1980s have contributed to an increasingly pronounced diversity in the economic and social performance of developing countries. Disparities in economic growth and social performance over the last two decades can be demonstrated by an illustrative set of developing countries which represent more than 90 per cent of the Third World's population (see Table 1). Some of the essential trends are:

- The greatest successes have been achieved in East and South East Asia in economic growth, participation in world trade and social welfare. Human resource development and effective economic policies are the important factors behind these achievements. This progress has not only been realized by the four Asian newly industrialising economies (NIEs) – South Korea, Taiwan, Hong Kong and Singapore – but also by some of the ASEAN countries (notably Thailand and Malaysia).
- China and India, the developing countries with the largest populations, have made significant advances in

economic and social development. But at the same time, they remain those with the greatest concentration of poverty, and their population continues to grow rapidly in absolute numbers. Remarkable progress in development has also been achieved in other highly populated low-income countries (LICs) in Asia, notably in Indonesia and Pakistan. In least-developed countries, such as Bangladesh, achievements have as yet been rather modest.

- Over the last two decades, Latin America has grown at a similar rate to the industrialised economies (2.6 per cent per annum). In the 1980s there have been serious setbacks as a result of policy deficiencies, imprudent debt management and unfavourable external economic conditions. Most of the more advanced countries still face immense social problems and there are many populations which are still poor and illiterate.
- Growth performance was especially weak in Sub-Saharan Africa, with 19 of the 30 countries having experienced negative or stagnant per capita income growth over the past two decades. With some exceptions, for the region as a whole per capita income today is lower than in 1960. Stagnation in GDP has been accompanied by a marked weakening of the fiscal and balance-of-payments situation. Sub-Saharan Africa suffers from a combination of economic, social, political, institutional and environmental handicaps which have so far largely defied development efforts by the African countries and their donors. Political instability is a major adverse factor and population growth causes unsustainable pressures on the natural base.

Strongly differentiated average annual growth rates of GDP and population have yielded wide differences in per capita income in 1987 ranging from an average of \$ 3,900 for the Asian NIEs over about \$ 1,900 for two of the NIEs in Latin America (Brazil and Mexico) to less

\* Institut für Weltwirtschaft, Kiel, West Germany. The author is presently on leave from the Kiel Institute and working in the Directorate for Development Cooperation at the OECD. The views expressed are the sole responsibility of the author, and should not be attributed to the OECD or its member governments.

than \$ 300 for low-income countries such as Bangladesh (\$ 160) and most of Sub-Saharan Africa.

In spite of the well-known caveats in using per capita income as a welfare indicator and despite the difficulties in comparing these figures internationally<sup>1</sup> the differences in economic and associated social performance are striking. It is even more challenging that major macroeconomic imbalances and structural trends in the world economy, the emerging demographic pattern, the uneven internal capacities to deal with the external factors, and domestic development challenges point to an even more pronounced heterogeneity among developing countries in the year 2000.

Estimates based on forecasts by international organisations reveal that under rather pessimistic assumptions on GDP and population growth most of the progress will continue to take place in Asia, notably in the Asian NIEs and some of the ASEAN countries (see Table 2). According to these estimates, most of the heavily indebted middle-income countries in Latin America will realize rather modest growth rates in per capita income, which is supposed to be somewhat higher in those middle-income countries exporting mainly oil and/or manufactured goods. Under a rather optimistic scenario, among the low-income developing countries probably only China, but perhaps also India,

will realize a significant step in development progress, while most of the other very poor countries will make rather modest progress, if at all. These forecasts are made under the critical assumptions that there will neither be any major changes in domestic policies nor any unforeseen external shocks. However, the trends can be substantiated by an assessment of those external and internal factors which will most likely affect the future trend of diversity of development performance among developing countries.

### External Imbalances

At present, the process of world economic integration is affected by a number of macroeconomic phenomena, namely by the payments imbalances among major OECD countries and associated exchange rate volatility, the Korean and Taiwanese surpluses and the Latin American debt problems. Any narrowing of these

<sup>1</sup> There has been growing interest in designing better measures of development, including modifications of GNP, social indicators and associated systems of social accounts and composite indices of development. A review of these approaches and concepts points to the conclusion that research has, up to now, failed to produce an alternative which is as readily accepted and comprehended as GNP per head though social indicators are useful for judging social performances. While purchasing-power-parities are a substantial improvement in avoiding exchange rate problems in international comparisons of income, these indicators are not available for recent years and for a wide coverage of countries.

**Table 1**  
**Economic and Social Performance in Selected Developing Country Groupings, 1965-1986**

	Average annual growth of						Increase in life expectancy at birth <sup>1</sup> (years) 1965-86	Decline in infant mortality rate (per 1000 births) 1965-86	Increase in adult literacy rate (% points) 1960-83
	Per capita income (%)		Real GDP (%)		Population (%)				
	1965-80	1980-86	1965-80	1980-86	1965-80	1980-86			
ASIA									
South-East Asia									
NICs <sup>2</sup>	7.5	6.4	9.4	7.8	1.9	1.4	11	34	18
Others <sup>3</sup>	4.9	0.6	7.4	2.9	2.5	2.3	10	45	21
Asian LICs									
China	4.2	9.3	6.4	10.5	2.2	1.2	14	56	26
India	1.4	2.7	3.7	4.9	2.3	2.2	11	65	8
Bangladesh	-0.3	1.1	2.4	3.7	2.7	2.6	6	32	2
Others <sup>4</sup>	1.4	3.1	4.4	5.7	2.7	2.6	7	44	8
LATIN AMERICA									
Brazil	6.6	0.5	9.0	2.7	2.4	2.2	7	39	17
Mexico	3.4	-1.8	6.5	0.4	3.1	2.2	7	34	18
Others <sup>5</sup>	2.2	-2.2	4.6	0.0	2.4	2.2	8	44	15 <sup>a</sup>
AFRICA									
Sub-Saharan Africa									
Nigeria	5.5	-6.5	8.0	-3.2	2.5	3.3	9	73	27
Others	0.5	-2.3	3.3	0.9	2.8	3.2	8	39	22
North Africa									
Egypt	4.3	2.0	6.7	4.7	2.4	2.7	11	84	18
Others <sup>6</sup>	2.6	1.1	6.4	3.8	2.7	2.7	9	69	26
INDUSTRIAL MARKET ECONOMIES									
	2.8	1.9	3.6	2.5	0.8	0.6	—	—	—

<sup>1</sup> Refers to males only. <sup>2</sup> Hong Kong, South Korea, Singapore. <sup>3</sup> Indonesia, Malaysia, Philippines and Thailand. <sup>4</sup> Burma, Nepal, Pakistan, Papua New Guinea and Sri Lanka. <sup>5</sup> Including Central America and the Caribbean. <sup>6</sup> Algeria, Morocco and Tunisia. <sup>a</sup> Excluding Costa Rica, Nicaragua and Uruguay.

Sources: World Bank: World Development Report 1988, Washington 1988; own calculations.

imbalances will have in the short and medium term very different effects on certain groups of developing countries, although it is difficult to specify the precise impact of the ongoing adjustment processes on economies other than those that will be directly affected.

A major concern is that of the possible consequences of a slow-down in the external demand of the United States.<sup>2</sup> Such a slow-down is likely to be brought about by fiscal contraction designed to reduce the budget deficit and partly by the decline in United States imports which will probably be produced by the depreciations of the dollar. Those developing countries which will be most affected by a reduction in the United States' external demand are the South-East Asian economies and Latin American countries (notably Mexico). But despite the heavy dependence of their exports on the US market, the South-East Asian economies have so far suffered little from United States efforts to improve their trade balance. Having experienced a depreciation vis-à-vis most of the major currencies, particularly the yen, their exports were stimulated both to the countries concerned and on third markets where they compete with exports from Japan and Western European countries. In addition, Japan's recent import boom was a major stimulant to Asian economies. This advantageous position has enabled these exporters to generate huge current account surpluses and to accumulate large foreign exchange reserves.

A protectionist solution to the US trade problem would seriously affect debt-ridden Latin American countries and could lead to an intensification of the debt problem. Growth of debtor exports of manufactures has been concentrated in products most vulnerable to protectionist curbs, such as motor vehicles and parts, clothing, footwear, iron and steel. Depressed export earnings would aggravate these countries' debt-servicing difficulties and reinforce the negative influence they are having on their economies and on their imports from the rest of the world. This scenario will be averted if the USA is able to tackle its own trade deficit by increasing exports rather than by reducing demand for imported goods. That, in turn, would require robust and prolonged economic growth in Europe and Japan, fuelled by domestic demand as well as by an increase in the low US savings rate.

Even if the negative consequences of a slow-down in the United States could be offset by a policy-induced acceleration in Western Europe and Japan, the distribution of its effects on developing countries will

very likely be different. An increase in the demand for imports by Japan and an accelerated growth of domestic demand in Europe would be particularly beneficial to the countries of South-East Asia. Due to the weak economic ties Latin America has with Europe, any acceleration in Western Europe is unlikely to offset the effects that the slow-down in the United States would have on the region. Whether the efforts to introduce a single market within the European Community by 1992 will bring Africa in a better position to exploit the increased export opportunities, which would arise from a stimulation of the Western European economies, critically depends on two factors: the success of the implementation of the structural adjustments now under way in Africa and the prevention of (potentially) rising protectionist attitudes in the European Community in the course of the unification of the markets.

## Revival of Capital Flows?

It remains an open question, whether a narrowing of the prevailing macroeconomic imbalances among the developed market economies will be accompanied by a revival of international capital flows to the developing countries. Flows of official development finance have not grown significantly during the 1980s, and public budget problems in many developed countries make it unlikely that there will be a major increase in the near future. A similar reluctance is observable among private commercial banks in providing fresh money especially to heavily indebted Latin American countries. Portfolio investments will be relevant only for those developing countries with a rather sophisticated domestic capital market. Finally, new foreign direct investment flows will most probably be concentrated in the Asian region both for economic and political reasons.

Most of the developing countries in Asia have retained their creditworthiness and avoided a debt crisis. Those which are performing especially well in growth and trade terms are deriving more of their financing needs from domestic savings and trade surpluses; that makes them less vulnerable to fluctuating rates of interest. Debt problems continue to centre around the intractability of the debt owed by Sub-Saharan countries and the economic policy problems of middle-income Latin American debtor countries. Although a substantial round of official debt relief is now under way for low-income African countries, this prospective debt relief may not always add decisively to the cash flows of the beneficiary countries, particularly in cases where the debt obligations involved are being accumulated rather than currently discharged. In the heavily indebted Latin American countries the growth process is still stalling

<sup>2</sup> Rüdiger Dornbusch: Debt Problems and the World Macro Economy, National Bureau of Economic Research, Working Paper No. 2379, Cambridge, 1987.

and, up to now, debtors, creditors and official agencies have not yet identified how the growth process can be restarted.

### Long-term Structural Trends

Some of the long-term economic trends in the world economy which most likely (continue to) intensify diversity among developing countries are the following: globalisation of trade and production structure and rising importance of service industries and intellectual property; declining importance of labour costs in the production of standard manufactured goods; falling commodity-intensity of manufacturing output; increased competition in the supply of industrial output; and in the field of agriculture, perhaps, a revolutionary impact from biotechnology.

The evolution of a more global economy – reflecting the continued rise in trade as a proportion of total world output,<sup>3</sup> faster diffusion of technological progress and the globalisation of financial markets – will largely benefit those developing countries which are already well integrated in the world economy, provide a favourable climate for foreign investment and pursue outward oriented policies. The rapidly growing and relatively high income Asian NIEs as well as some of the ASEAN economies figure prominently in this category.

Nearly 80 (60) per cent of total exports (imports) of the set of developing countries covered in Table 3 account for this group of countries. The extent to which Latin American NIEs such as Brazil and Mexico will benefit from the globalisation of production and markets will critically depend on their ability to reserve the debt-related plunge in their investment ratios and to find effective solutions to domestic stabilisation.

Another trend which will most likely continue, or even be reinforced in the next decade, is that of regional trade areas. Progress towards freer trade is being made largely in North America (the US-Canada agreement), Australasia (ANCER) and Europe (the EC's Single Market in 1992). Furthermore, and to some degree in response, there is now an intensive increased discussion on the concept of a Pacific free trade area. Trade relations between Asia and Japan are moving towards horizontal specialisation reflecting the expansion of domestic demand in Japan, the opening of its domestic markets, and an increase in exports to Japan from the affiliates of Japanese corporations in Asia. Linkage among Asian economies has been strengthened by the globalisation of corporate

<sup>3</sup> Accelerating trade growth occurred against the background of a steady 3 per cent annual growth in world output in each of the last three years. See GATT: International Trade 1987/88, Vol. I, Section 1, Geneva 1988.

**Table 2**  
**Basic Growth Indicators for Selected Developing Country Groupings, 1965-2000**

	Average annual growth of						Per capita income		Population	
	Per capita income (%)		Real GDP (%)		Population (%)		(US \$)		(millions)	
	1965-87	1987-2000	1965-87	1987-2000	1965-87	1987-2000	1987	2000	1987	2000
<b>ASIA</b>										
South-East Asia										
NICs <sup>1</sup>	6.7	4.6	8.6	5.8	1.9	1.2	3900	7000	70	82
Others <sup>2</sup>	3.7	2.8	6.1	4.7	2.4	1.9	690	990	297	379
Asian LICs										
China	5.9	5.0	7.0	6.4	2.0	1.4	300	570	1076	1289
India	1.8	3.1	4.1	4.9	2.3	1.8	270	400	799	1008
Bangladesh	0.4	0.6	3.1	3.1	2.7	2.5	160	170	106	146
Others <sup>3</sup>	2.3	1.8	5.0	4.5	2.7	2.7	340	430	179	253
<b>LATIN AMERICA</b>										
Brazil	4.3	1.9	6.8	3.8	2.5	1.9	1840	2350	142	181
Mexico	2.6	1.4	5.7	3.5	3.1	2.1	1890	2260	84	110
Others <sup>4</sup>	1.2	1.1	3.4	2.8	2.2	1.7	1450	1670	180	224
<b>AFRICA</b>										
Sub-Saharan Africa										
Nigeria	1.2	0.1	4.0	3.4	2.8	3.3	630	640	106	162
Others	0.3	0.6	3.2	3.7	2.9	3.1	280	300	362	538
North Africa										
Egypt	3.1	2.5	5.6	4.7	2.5	2.2	780	1080	51	68
Others <sup>5</sup>	2.8	2.1	5.6	4.7	2.8	2.6	1970	2580	58	81
<b>INDUSTRIAL MARKET ECONOMIES</b>										
	2.4	2.6	3.3	3.0	0.8	0.4	13100	18290	821	865

<sup>1</sup> Hong Kong, South Korea, Singapore and Taiwan. <sup>2</sup> Indonesia, Malaysia, Philippines and Thailand. <sup>3</sup> Burma, Nepal, Pakistan, Papua New Guinea and Sri Lanka. <sup>4</sup> Including Central America and the Caribbean. <sup>5</sup> Algeria, Libya, Morocco and Tunisia.

Sources: World Bank: World Development Report 1988 and World Tables 1987, Washington 1987; IMF: International Financial Statistics, Washington, April 1988; own estimates, based on forecasts by various international organisations.

production activities and increasing intra-industry trade. The growth of trade and investments will lead to greater interdependence among Pacific-basin economies.

### Foreign Direct Investment

The declining importance of labour costs in the production of manufactured goods due to the impact of micro-electronics on the manufacturing process is not implying that differences in labour costs will cease to affect the re-allocation of industrial activities.<sup>4</sup> However, this trend may reveal the importance of other factors influencing the attractiveness of an economy for foreign investment, including the flexibility of labour markets, the treatment of transnational corporations by governments and, in more general terms, socio-economic and political stability. Recent trends in foreign direct investment flows from major OECD countries clearly indicate a reorientation of these flows towards Asian developing countries. A considerable dynamism in foreign direct investment flows can also be observed among Asian countries; this dynamism can be attributed

to changes in the investment climate, exchange rate changes and the emerging horizontal division of labour within the region.

The implementation of debt conversion schemes has recently initiated an upsurge of direct investment flows from OECD countries towards Latin America. However, given the severe stabilisation problems and modest growth prospects in many of the Latin American economies one might not expect for the 1990s a flow of direct investment on the scale seen in the 1960s.

There are no indications for most of the African countries that they will succeed in attracting foreign capital to a large extent. The result will be a continuing lack of access to new technology and managerial skills, both generally associated with the inflow of foreign direct investments. Nevertheless, since the base is low, comparably small flows could already make a difference.

### Declining Commodity Prices

The predicted falling commodity intensity of manufacturing output due to new materials will contribute to a further decline in the growth of world demand for raw materials and impose a downward pressure on commodity prices, which have already fallen considerably in recent decades.<sup>5</sup> Given the

<sup>4</sup> Wilfried Lütkenhorst: Challenges from New Trends in Foreign Direct Investment, in: INTERECONOMICS, Vol. 23, No. 5, 1988, pp. 220-227.

<sup>5</sup> Enzo R. Grilli and Maw Cheng Yang: Primary Commodity Prices, Manufactured Goods Prices and the Terms of Trade of Developing Countries: What the Long Run Shows, in: The World Bank Economic Review, Vol. 2, 1988, No. 1, pp. 1-47.

**Table 3**  
**Exports and Imports of Selected Developing Country Groupings, 1986**  
\$ billion

	Total exports of goods and services	Exports to OECD countries	Total imports of goods and services	Imports from OECD countries	Total trade balance	Current account balance	ODF <sup>1</sup> Receipts
<b>ASIA</b>							
South-East Asia							
NICs <sup>2</sup>	130.2	87.0	108.9	65.7	18.6	6.7	(-0.1)
Others <sup>3</sup>	53.0	32.9	56.9	19.7	1.9	-3.1	3.3
Asian LICs							
China	30.7	16.3	38.1	22.4	-12.0	-7.0	2.6
India	15.1	6.7	21.1	10.5	-3.7	-3.9	1.6
Bangladesh	1.1	n.a.	2.7	n.a.	-1.4	-1.1	1.5
Others <sup>4</sup>	7.5	2.7	13.5	4.3	-3.4	-1.9	2.5
<b>LATINAMERICA</b>							
Brazil	25.3	18.1	30.3	9.5	6.8	-4.9	1.4
Mexico	23.8	22.4	25.5	15.7	4.0	-1.3	1.1
Others <sup>5</sup>	58.7	37.0	68.5	37.0	1.5	-9.5	7.1
<b>AFRICA</b>							
Sub-Saharan Africa							
Nigeria	12.5 <sup>6</sup>	7.8	6.4	3.8	1.0	0.4	0.6
Others	24.5	18.6	30.5	17.2	-2.1	-5.6	12.1
North Africa							
Egypt	8.2	2.6	17.1	7.7	-5.2	-6.4	1.8
Others <sup>6</sup>	26.1	18.8	28.6	15.0	-1.6	-5.0	1.7
<b>OECD COUNTRIES</b>	1454.0	—	—	—	—	—	—

<sup>1</sup> Net official development finance from all bilateral and multilateral agencies (excluding DOM/TOMs).

<sup>2</sup> Hong Kong, South Korea, Singapore and Taiwan. <sup>3</sup> Indonesia, Malaysia, Philippines and Thailand. <sup>4</sup> Burma, Nepal, Pakistan, Papua New Guinea and Sri Lanka. <sup>5</sup> Including Central America and the Caribbean. <sup>6</sup> Algeria, Libya, Morocco and Tunisia. <sup>8</sup> 1985.

Sources: IMF: International Financial Statistics, Washington, April 1988; OECD: Foreign Trade by Commodities 1988, Paris 1988; own calculations.

continuing heavy reliance especially by many low-income African countries upon commodities for generating domestic savings, export revenues and employment, this trend will continue to impose a serious burden for any development efforts by these countries. In addition, increased competition can be expected from some of the commodity producing middle-income countries, such as Indonesia, Malaysia and Brazil, which are able to further reduce production costs as a consequence of increased productivity through better technology and efficiency. The rising degree of competition in commodity production because of slowing growth in demand, more efficient organisation and investment on the supply side will impose more difficult "catch-up" problems for commodity export dependent less advanced developing countries. At the same time commodity importing developing countries – notably the Asian NIEs, but also countries such as India – will benefit from falls in commodity prices.

### Biotechnology

The impact of biotechnology in the agricultural field is much more difficult to assess. Potential industrial applications of biotechnological products include fighting diseases in humans and animals, increasing the yields of agricultural plants and animals, augmenting energy production and improving the environment. Although biotechnology could significantly support the development efforts of developing countries, major impacts of this technology are not expected until after the year 2000. There is also uncertainty as to what extent developing countries will benefit from these developments, e. g. in solving their nutrition problem. One may also expect that industrialised countries develop a comparative advantage in agriculture due to progress in this area.

At present, the world appears to be on the threshold of

a new technological era. Information technologies have already been incorporated into the production process of almost all sectors of the economies of the industrial countries. Discoveries in biotechnology and new materials are on the verge of being translated into commercially viable products and technologies. The information-based technological revolution – now under way – will have a major impact on the ways of handling production and economic organisation. If it was true in the past that at least some kind of industrial development was a *sine qua non* for economic advancement, so, in the next decade, will it be true for the information technologies. These will be a key determinant of production and trading advantages throughout manufacturing and agriculture.

Some of the major developing countries such as Brazil, Mexico and India have already formulated and are implementing policies regarding information and computing in particular. With respect to technology transfer, these countries have also been able to negotiate quite extensive technology agreements with major suppliers. For developing countries with less attractive domestic markets, smaller and less sophisticated industrial sectors, relatively fewer well-qualified people, and less articulated administrative and institutional structures for tackling technology transfer questions, the prospects of obtaining satisfactory technology arrangements are much more limited. Therefore, it is most likely that technological developments accentuate the income gap among various groups of developing countries.

### Corporate Strategies

In the past transnational corporations have made important contributions to developing countries in two critical and related areas, the transfer of technology and

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This quarterly report – compiled by the Department of World Business Trends of the Hamburg Institute for Economic Research (HWWA) – analyses and forecasts the economic development of the most important Western industrial nations and of the international raw materials markets.

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the transformation of many developing countries from being exporters of primary commodities to being exporters of manufactures.<sup>6</sup> Compared to the preceding two decades, there has been a marked slow-down of foreign direct investment (FDI) in the eighties, and the decline in the expansion has affected particularly the developing countries. Transnational corporations have reduced their investments in developing countries, partly in order to concentrate their resources in developed market economies, but also in response to the slow-down in growth that has gripped many developing countries. The exception to this generalisation is the expansion of FDI to NIEs for export-oriented industries.

As far as low-income countries are concerned, foreign corporations have generally played a minor role in the development of their economies. Based on data available for 40 low-income developing countries, FDI amounted to well under 1 per cent of gross domestic investment in all but seven countries. Many of them have recently introduced policies that are more favourable to investments by transnational corporations. In spite of these changes, some of which date back as far as the second half of the 1970s, the inflows of FDI to those countries have declined rather than increased, and one should not be too optimistic as regards the chances of a major reversal of the basic trend.

## Demographic Trends

Demographic dynamics have a serious impact on a number of sectors relevant to economic and social development, including food and nutrition, employment, migration, education and literacy, energy and environment. Unwanted high fertility adversely affects the health and welfare of individuals and families, especially among the poor. According to UN and World Bank estimates, demographic developments will continue to impose severe pressures on economic and social progress in a number of developing countries. Since trends are regionally very diverse, population pressures will contribute significantly to the diversity in development performance in the Third World. In this context, it is worth noting that in the more recent period (1980-86) those low income countries which managed to accelerate their GNP growth were also experiencing stable or declining average population growth rates, compared with the period 1965-80, whereas in the other countries, lower GNP growth rates were compounded by higher population growth (see Table 1).

Referring to the selected set of developing countries, population growth rates will decrease substantially in South-East Asian middle-income countries, but will remain relatively high – with the exception of China and India – for low-income countries in Asia (see Table 2). The growth rate for Asia as a whole is projected to be lower than that for Africa or Latin America, but because of its large base – in sheer numbers of people – the Asian population will still increase substantially. Population growth varies widely within Asia and, as is the case with other regions, the rate is highest among the poorer countries that are least able to support it. While progress in reducing population growth in Latin America is projected to be substantial, Africa will remain a problem area with average annual growth rates in population exceeding three per cent per year in the case of Sub-Saharan Africa. Projections of population in the year 2000 reveal that about three-quarters of the total population will be concentrated in developing countries presently classified as low-income countries.

## Domestic Policies

The nature of the trend in diversity of economic and social performance among developing countries in the past suggests that the fundamental requirements for development are dominantly domestic in nature. For example, many of the current difficulties in Latin American and African countries, such as high levels of public debt and fiscal rigidities, have their origin in the 1970s when governments let currencies become overvalued, interest rates were kept on too low levels, trade policies remained protectionist, and other excessive government interventions increasingly provided disincentives to savings and investment, both domestic and foreign. As a consequence, there was a concomitant weakening of the private sector.

For the more advanced developing countries three complementary sets of factors have shaped the international competitiveness of these countries in the world economy: the ability to adjust to external shocks, the choice between “outward-oriented” and “inward-oriented” development strategies, and the upgrading of the key productive factors, i. e. human and physical capital and technological and organisational know-how.

The prevailing macroeconomic imbalances imply in the short and medium term persisting or even greater uncertainty and fluctuation of major economic variables such as interest rates and exchange rates. The ability to adjust to external economic shocks successfully depends on the quality of macroeconomic management. Some of the key elements of economic

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<sup>6</sup> United Nations Centre on Financial Corporations: *Transnational Corporations in World Development*, New York 1988.



policy which enable countries to adjust to major and unforeseen changes in external circumstances are:

- ☐ outward orientation of development strategies with special emphasis on maintenance of appropriate real exchange rates;
- ☐ effectiveness of public administration and quality of public sector interventions;
- ☐ encouragement of private domestic savings;
- ☐ a high degree of flexibility and quick speed of policy responses within the framework of stability and predictability of basic objectives.

Essential prerequisites for sound economic policies are a high degree of political commitment to economic development and continuity of political and economic leadership and social consensus.

For those countries already relatively well integrated in the world economy – such as the Asian NIEs – the question arises as to whether and to what extent these economies might participate more actively in international processes designed to assure the sustainability of growth and development in the world economy at large. While export-led growth still constitutes the dominant strategy, shrinking US deficits and slower growth in other OECD economies would require further diversification of their exports markets and expansion of domestic markets. Given the comparatively advanced stage of Korea's and Taiwan's economies and their linkages with the world economy, such a re-orientation could be accompanied by policies to liberalise import and investment regimes and to deregulate domestic capital markets. One should not exclude in this context that Asian NIEs could become major capital exporters to developing countries (and others) as did the United Kingdom in the 19th century, the USA after 1945 and more recently Japan to the Asian NIEs.

Some of the ASEAN economies have experienced a rapid exit from performing mainly as primary commodity exporters. While – with the exception of Indonesia and the Philippines – these countries are free from severe stabilisation problems, continuing enhanced growth performance will require reinforced efforts to exploit opportunities for manufactured exports and to attract foreign capital including foreign direct investment.

Despite – or perhaps because of – its rich endowment with natural resources, Latin America has not succeeded in exploiting its major growth potential. For

the Latin American NIEs debt overhang and structural deficiencies are continuing problems. In the short term, the economic welfare of these economies will substantially depend on improvements in economic management, including serious efforts to eliminate inflationary pressures of essentially fiscal origin. In the medium and long term their economic development hinges on the ability to tackle the debt problem by generating higher domestic savings and attracting back foreign savings and flight capital. A prerequisite for accomplishing this end will be to sustain high rates of export growth, to liberalise imports and to adopt a more balanced incentive system as regards production for domestic and foreign markets. However, the adoption of more effective and equitable policies seems to be hampered in many cases by severe political, social and institutional constraints.

China and India, poor and heavily populated economies, have made significant advances in agricultural and industrial development. The more market-oriented and less inward-looking development strategies recently adopted are still confronted with severe domestic constraints, which show up so clearly partly because recent growth has been very rapid. The impact of the integration of China into the world economy on its neighbours and the world at large will be considerable and depends on a number of conditions. China is faced with shortages in managerial skills, technology, capital, energy and infrastructure and is now also grappling with substantial inflation. India's recent efforts to further liberalise domestic markets are taking place within a rigidly regulated economy. Administrative constraints in the Indian economy are widespread and entangled with established interests. Barriers such as controls over factor mobility constitute serious obstacles to growth-oriented structural change. Faced with the largest concentrations of poverty and with populations continuing to grow rapidly in absolute numbers, future prospects for both countries depend on the continuation of efficiency-oriented policies, massive infrastructure and investment in human resource development.

The development prospects of other low-income countries in Asia and particularly in Sub-Saharan Africa critically depend on the question of whether or not these countries can get a foothold in the process of international economic integration. Presently Sub-Saharan Africa faces some of the most intractable development problems in the world.<sup>7</sup> Some of them are of a deep-rooted structural nature. Export revenues come from a narrow range of commodities with unpredictable world market conditions and volatile prices; import dependence on manufactures, oil,

<sup>7</sup> UN: Financing Africa's Recovery. Report and Recommendations of the Advisory Group on Financial Flows for Africa, New York 1988.

services and food is heavy. Subsistence sectors still account for a large share of national income. Physical infrastructure is weak and suffers from a lack of maintenance. Populations are growing more rapidly than anywhere else in the world. There is a shortage of managerial, administrative and other skills. Fragile ecological systems have been subject to environmental damage, and drought is a recurrent feature. Political turmoil and instability and local wars have been widespread for a long time.

Although internal conditions for integrating these economies into the world economy are not very favourable at the moment this does not necessarily imply that the long-term outlook for Sub-Saharan Africa is hopeless. Some countries have coped with their difficulties, and a large number of them are engaged in policy changes to improve their economic performance. At the end of 1987, about 30 Sub-Saharan countries were undertaking economic adjustment programmes or were expected to resume them with the World Bank, the IMF, or the two institutions jointly. The questions hanging over these programmes of reforms are whether African governments have the determination and ability to persist in them, and to what extent external resources will be available to support their adjustment efforts.

## Development Co-operation

The observable trend towards diversity in the economic performance among developing countries will most likely be intensified in the next decade because of ongoing adjustment efforts to correct worldwide macroeconomic imbalances, long-term structural trends, demographic pressures and because of those internal policy-related divergences discussed above. This trend specifically points to the difficulties of poor countries in catching up in the development process and poses major challenges for development co-operation.

Firstly, a much more differentiated approach (including new forms of development co-operation) with regard to the different categories of developing countries is needed to help to meet the differentiated challenges of the various groups of countries. With regard to the problem debtors, for example, there is scope for international co-operation to help to define better the magnitude of the fiscal gap that must be bridged and to identify how that can be realistically accomplished through fiscal adjustment, modification of debt service obligations and new lending. With other middle-income countries, industrial, technological, scientific and cultural co-operation could play a catalytic role for integrating these countries more into the world economy. Least-developed countries, located mainly in

Sub-Saharan Africa but also elsewhere, will most likely remain priority areas for aid donors. In order to meet their needs, for example in such areas as institution-building and human resources development, major re-orientations in aid policies to meet these challenges will be necessary on behalf of the donor community.

Secondly, since aid is mainly supply-determined and aid volumes will scarcely be increased by a significant extent in the foreseeable future,<sup>8</sup> all efforts have to be undertaken to ensure that aid is used as efficiently as possible and as a catalyst with far-reaching multiplier effects on economic and social development. This implies that aid has to consider the domestic and institutional sustainability of broader sectoral and national efforts, national policies, and the economic efficiency and substantiability of aid financed projects and programmes. In addition, stronger emphasis on aid uses and aid policy dialogue on the role of the private sector and the market mechanism has to become an essential element of aid policies. Finally, considerable strengthening of international aid co-ordination and policy dialogue arrangements could help to ease scarcity in overall resources.

Thirdly, given the dimension of the requirement of intensified external assistance, increasing awareness is needed of the importance of establishing coherent approaches to development co-operation. In this context ways and means have to be found in which other OECD policies and official development assistance could reinforce each other in assisting developing countries to strengthen and diversify their economies and growth potential. Many developing countries facing balance-of-payments and debt difficulties are undertaking adjustment programmes supported by financial assistance from the IMF and World Bank. These programmes often include, *inter alia*, the pursuit of more outward-oriented development strategies and the promotion of exports with a view to establishing a viable balance-of-payments and external debt position and sustainable growth in the medium term. The success of these adjustment efforts will importantly be influenced by major trends in the world economy which are dominated by the economic performance and policies in industrial countries. The focus has to be linked to those areas of OECD countries' policies such as trade, agricultural and industrial policies, which have a major impact on the global economy and which may provide opportunities for those developing countries which are presently not, or insufficiently, integrated into the world economy.

<sup>8</sup> OECD: Development Co-operation, 1987 Report, Paris 1987, p. 63.