ECONOMIC AND SOCIAL SURVEY OF ASIA AND THE PACIFIC 1997

Asia and the Pacific into the Twenty-first Century: Development Challenges and Opportunities

UNITED NATIONS

ECONOMIC AND SOCIAL COMMISSION FOR ASIA AND THE PACIFIC

ECONOMIC AND SOCIAL SURVEY OF ASIA AND THE PACIFIC 1997

UNITED NATIONS

New York
1997

UNITED NATIONS
ECONOMIC AND SOCIAL SURVEY OF ASIA AND THE PACIFIC
1997

ST/ESCAP/1727

UNITED NATIONS PUBLICATION

ISBN: 92-1-119739-2 ISSN: 0252-5704

With best wishes
Marin Gri
22/4/97

FOREWORD

The annual *Economic and Social Survey of Asia and the Pacific* is an important medium for disseminating information on development performance and policies. This fiftieth issue assumes particular importance as it coincides with the fiftieth anniversary of the founding of ESCAP.

During the past half-century, the ESCAP region has made major strides in economic and social progress. Per capita income growth has been much faster than elsewhere in the world. There has been a remarkable increase in the region's share of global flows of trade, private finance and investment. Many economies have undergone fundamental transformations in the structure of output, employment and exports. Substantial gains have been recorded in social development, and these are reflected in a wider spread of education, increased life expectancy and reduced infant mortality.

However, these achievements have remained uneven among countries and peoples. A large majority of the world's absolute poor live in the region. Economic and social progress has been both inadequate and erratic in most of the least developed and Pacific island countries, and the economies in transition have experienced a sharp reversal of earlier achievements.

The region faces the twenty-first century in an environment of intensified globalization and regionalization. Rapid changes in production methods, transport and communications and information technology have accelerated internationalization of markets for goods, services, finance and production factors. These have been reinforced by new policy stances that are increasingly focused on openness, liberalization and deregulation. These changes offer great opportunities for national development, but they also pose major challenges. The opportunities lie in the prospects for greater participation in international trade, investment and financial flows. The challenges arise from the need to develop a supportive infrastructure, particularly for transport and communications. There is also a need for articulation of appropriate policy responses and for development of institutions to participate effectively in the globalization and regionalization processes.

Policy responses to the emerging opportunities and challenges will have to vary to suit the unique conditions of each individual country. In general, maintaining internal and external stability is a basic prerequisite, and further liberalization of trade, investment and financial policies will be needed. Upgrading human resources through the expansion of education, training and research is important to enhance competitiveness in the global market. The disadvantaged groups of economies have to be mainstreamed through accelerated financial and technical assistance and improvement in market access for products of particular interest to them, and a fair and full implementation of the Uruguay Round agreements must be ensured for all countries. Regional cooperation in trade, investment and transport and communication linkages needs to be strengthened to exploit more fully the complementarities among neighbouring countries.

The *Survey* presents a detailed analytical perspective of the policy directions to be pursued at the various levels in the light of the emerging opportunities and challenges for the ESCAP region in the twenty-first century. It will serve as valuable reference material for policy dialogue.

Kofi Annan
Secretary-General

March 1997

CONTENTS

CONTENTS *(continued)*

CONTENTS *(continued)*

BOXES

TABLES

TABLES *(continued)*

FIGURES

EXPLANATORY NOTES

The term "ESCAP region" is used in the present issue of the *Survey* to include Afghanistan, American Samoa, Armenia, Australia, Azerbaijan, Bangladesh, Bhutan, Brunei Darussalam, Cambodia, China, Cook Islands, Democratic People's Republic of Korea, Fiji, French Polynesia, Guam, Hong Kong, India, Indonesia, Iran (Islamic Republic of), Japan, Kazakstan, Kiribati, Kyrgyzstan, Lao People's Democratic Republic, Macau, Malaysia, Maldives, Marshall Islands, Micronesia (Federated States of), Mongolia, Myanmar, Nauru, Nepal, New Caledonia, New Zealand, Niue, Northern Mariana Islands, Pakistan, Palau, Papua New Guinea, Philippines, Republic of Korea, Russian Federation, Samoa, Singapore, Solomon Islands, Sri Lanka, Tajikistan, Thailand, Tonga, Turkey, Turkmenistan, Tuvalu, Uzbekistan, Vanuatu and Viet Nam. The term "developing ESCAP region" excludes Australia, Japan and New Zealand.

The term "Central Asian republics" in this issue of the *Survey* refers to Armenia, Azerbaijan, Kazakstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan.

The designations employed and the presentation of the material in this publication do not imply the expression of any opinion whatsoever on the part of the Secretariat of the United Nations concerning the legal status of any country, territory, city or area or of its authorities, or concerning the delimitation of its frontiers.

Mention of firm names and commercial products does not imply the endorsement of the United Nations.

The abbreviated title *Survey* in footnotes refers to *Economic and Social Survey of Asia and the Pacific* for the year indicated.

Many figures used in the *Survey* are on a fiscal year basis and are assigned to the calendar year which covers the major part or second half of the fiscal year.

Reference to "tons" indicates metric tons.

Values are in United States dollars unless specified otherwise.

The term "billion" signifies a thousand million. The term "trillion" signifies a million million.

In the tables, two dots (..) indicate that data are not available or are not separately reported, a dash (–) indicates that the amount is nil or negligible, and a blank indicates that the item is not applicable.

In dates, a hyphen (-) is used to signify the full period involved, including the beginning and end years, and a stroke (/) indicates a crop year, a fiscal year or plan year. The fiscal years, currencies and 1996 exchange rates of the economies in the ESCAP region are listed in the following table:

Country or area	*Fiscal year*	*Currency and abbreviation*	*Mid-point rate of exchange for $1 as of June 1996*
Afghanistan	21 March to 20 March	afghani (Af)	50.600
American Samoa	..	United States dollar ($)	1.000
Armenia	1 January to 31 December	dram	403.000
Australia	1 July to 30 June	Australian dollar ($A)	1.267
Azerbaijan	1 January to 31 December	manat (M)	4 335.000
Bangladesh	1 July to 30 June	taka (Tk)	41.750
Bhutan	1 April to 31 March	ngultrum (Nu)	35.060
Brunei Darussalam	1 January to 31 December	Brunei dollar (B$)	1.420[a]
Cambodia	1 January to 31 December	riel (CR)	2 619.000
China	1 January to 31 December	yuan renminbi (Y)	8.00
Cook Islands	1 April to 31 March	New Zealand dollar ($NZ)	1.462
Democratic People's Republic of Korea	..	won (W)	..
Fiji	1 January to 31 December	Fiji dollar (F$)	1.404
French Polynesia	..	French Pacific Community franc (FCFP)	93.673

Country or area	Fiscal year	Currency and abbreviation	Mid-point rate of exchange for $1 as of June 1996
Guam	1 October to 30 September	United States dollar ($)	1.000
Hong Kong	1 April to 31 March	Hong Kong dollar (HK$)	7.740
India	1 April to 31 March	Indian rupee (Rs)	35.060
Indonesia	1 April to 31 March	Indonesian rupiah (Rp)	2 342.000
Iran (Islamic Republic of)	21 March to 20 March	Iranian rial (Rls)	1 749.500
Japan	1 April to 31 March	yen (¥)	109.420
Kazakstan	1 January to 31 December	tenge (T)	66.800
Kiribati	1 January to 31 December	Australian dollar ($A)	1.267
Kyrgyzstan	1 January to 31 December	som (som)	12.500
Lao People's Democratic Republic	1 July to 30 June	new kip (NK)	918.600
Macau	..	pataca (P)	7.972[b]
Malaysia	1 January to 31 December	ringgit (M$)	2.495
Maldives	1 January to 31 December	rufiyaa (Rf)	11.770
Marshall Islands	1 October to 30 September	United States dollar ($)	1.000
Micronesia (Federated States of)	1 October to 30 September	United States dollar ($)	1.000
Mongolia	1 January to 31 December	tugrik (Tug)	531.150
Myanmar	1 April to 31 March	kyat (K)	5.956
Nauru	1 July to 30 June	Australian dollar ($A)	1.267
Nepal	16 July to 15 July	Nepalese rupee (NRs)	56.025
New Caledonia	..	French Pacific Community franc (FCFP)	93.673
New Zealand	1 April to 31 March	New Zealand dollar ($NZ)	1.462
Niue	1 April to 31 March	New Zealand dollar ($NZ)	1.462
Northern Mariana Islands	1 October to 30 September	United States dollar ($)	1.000
Pakistan	1 July to 30 June	Pakistan rupee (PRs)	35.100
Palau	1 October to 30 September	United States dollar($)	1.000
Papua New Guinea	1 January to 31 December	kina (K)	1.285
Philippines	1 January to 31 December	Philippine peso (P)	26.203
Republic of Korea	1 January to 31 December	won (W)	810.600
Russian Federation	1 January to 31 December	rouble (R)	5 108.000
Samoa	1 July to 30 June	tala (WS$)	2.452
Singapore	1 April to 31 March	Singapore dollar (S$)	1.410
Solomon Islands	1 January to 31 December	Solomon Islands dollar (SI$)	3.550
Sri Lanka	1 January to 31 December	Sri Lanka rupee (SL Rs)	55.237
Tajikistan	1 January to 31 December	Tajik rouble (TR)	275.000
Thailand	1 October to 30 September	baht (B)	25.360
Tonga	1 July to 30 June	pa'anga (T$)	1.232
Turkey	1 January to 31 December	lira (LT)	81 485.000
Turkmenistan	1 January to 31 December	manat (M)	3 965.000[c]
Tuvalu	1 January to 31 December	Australian dollar ($A)	1.267
Uzbekistan	1 January to 31 December	som (som)	36.100
Vanuatu	1 January to 31 December	vatu (VT)	111.350
Viet Nam	1 January to 31 December	dong (D)	11 018.000[d]

Sources: United Nations, *Monthly Bulletin of Statistics*, vol. LI, No. 1 (January 1997); United Nations, *Statistical Indicators for Asia and the Pacific*, vol. XXVI, No. 4 (December 1996); International Monetary Fund, *International Financial Statistics* (January 1997); and national sources.

[a] February 1996.
[b] Monthly average.
[c] May 1996.
[d] August 1996.

ABBREVIATIONS

ADB	Asian Development Bank
AFTA	ASEAN Free Trade Area
AIDA	Asia Infrastructure Development Alliance
ALTID	Asian land transport infrastructure development (project)
APEC	Asia-Pacific Economic Cooperation (forum)
ASEAN	Association of South East Asian Nations
ASEM	Asia-Europe Meeting
BOO	build-own-operate
BOT	build-operate-transfer
CBO	community-based organization
CER	Closer Economic Relations Agreement between Australia and New Zealand
EAEC	East Asia Economic Caucus
ECDC/TCDC	economic cooperation among developing countries/technical cooperation among developing countries
ECE	Economic Commission for Europe
ECO	Economic Cooperation Organization
EDI	electronic data interchange
EFTA	European Free Trade Agreement
FDI	foreign direct investment
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GDP	gross domestic product
GNP	gross national product
GSP	generalized system of preferences
HDI	human development index
HIV/AIDS	human immunodeficiency virus/acquired immune deficiency syndrome
HS	Harmonized Commodity Description and Coding System
ICAO	International Civil Aviation Organization
ILO	International Labour Organization
IMF	International Monetary Fund
IMO	International Maritime Organization

ABBREVIATIONS *(continued)*

IOM	International Organization for Migration
ISO	International Organization for Standardization
ITC	International Trade Centre
ITU	International Telecommunication Union
MFA	Multifibre Arrangement
MFN	most-favoured-nation
MIGA	Multilateral Investment Guarantee Agency (World Bank)
NGO	non-governmental organization
NIE	newly industrializing economy
ODA	official development assistance
OECD	Organisation for Economic Cooperation and Development
SAARC	South Asian Association for Regional Cooperation
SAPTA	South Asian Preferential Trading Arrangement
SPARTECA	South Pacific Regional Trade and Economic Cooperation Agreement
SPC	South Pacific Commission
TRIMs	trade-related investment measures
TRIPs	trade-related aspects of intellectual property rights
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Programme
UNESCO	United Nations Educational, Scientific and Cultural Organization
VAT	value added tax
WHO	World Health Organization
WPI	wholesale price index
WTO	World Trade Organization

INTRODUCTION

As far back as 1960, a group of experts commissioned by the then Economic Commission for Asia and the Far East (ECAFE), under the chairmanship of Professor Jan Tinbergen, a Nobel laureate in economics, identified the most commonly accepted development objectives in the region. These were, in no order of priority, a rapid increase in per capita income, a high level of employment, a relatively stable price level, equilibrium in the balance of payments, a reduction of inequalities in income distribution, the avoidance of marked disparities in the prosperity and growth of different regions within a country, and a diversified economy. These objectives remain as relevant today as they were nearly four decades ago. A new addition is environmental sustainability.

An overwhelming majority of developing economies in the region fall into the low-income or lower middle-income category. This highlights the continuing need to emphasize a rapid increase in per capita income. The relative stability of the price level, equilibrium in the balance of payments and the diversification of output have important implications for the growth of income as well as for equity. A reduction of inequality in terms of both income distribution and disparities among regions within a country retains its validity as an important objective. There are many countries in the region where relative income inequality has worsened. In the more populous countries of the region, the problem of poverty remains serious. In fact, the Asian and Pacific region is home to over two thirds of the world's absolute poor. The lack of adequate opportunities for productive employment is closely connected to poverty. The spectre of rapid depletion of natural resources and the mounting incidence of pollution have led to the acceptance of environmental sustainability as a core development objective.

The strategic approaches to the realization of those objectives, however, are greatly different now, as is the external environment. Aided by a buoyant global economy, a series of commodity price booms and accelerated official development assistance, the 1960s witnessed the vigorous pursuit of a development strategy led by the public sector. Typically, this strategy also emphasized an inward-oriented development path with import substitution as a key element.

The 1970s and the early 1980s were marked by a series of destabilizing shocks, including a high rate of global inflation, an upsurge in energy prices, considerable exchange rate instability, recession and severe debt problems in many developing countries. These factors seriously undermined the edifice on which the earlier development strategy had been based.

From about the mid-1980s, there has been a major boost to the globalization and regionalization of the world economy. Spurred by intensified competition, rapid progress in information, transport and communications technologies and a growing convergence of demand patterns, the 1990s have seen a tremendous upsurge in the cross-border exchange of goods, services, private finance and investment. These changes in the external environment have been complemented by an unprecedented liberalization of policy regimes in developing countries with respect to international trade, capital, finance and technology and by a vastly increased emphasis on the role of the private sector in development. This approach has been inspired partly by the unsatisfactory results of the earlier strategy. To some extent, the policy changes have been in response to the need to participate in the globalization and regionalization processes, as failure to do so would risk marginalization.

All current indications are that the momentum of globalization and regionalization is likely to continue into the twenty-first century. Against this background, the present issue of the *Economic and Social Survey of Asia and the Pacific* deals with opportunities and challenges for the Asian and Pacific region into the twenty-first century from the perspective of closer integration with the globalization and regionalization processes. The objective is to investigate the opportunities offered by such integration for promoting national development objectives and the policy measures needed to deal with the attendant challenges.

Chapter I gives an overview of the role of the region in the emerging trends and prospects of globalization and regionalization. Chapter II undertakes a detailed examination of selected aspects of the national socio-economic situation which bear on the participation of developing countries of the region in the globalization and regionalization processes. That is followed by analyses of the progress in and prospects for the development of effective linkages intraregionally and globally in terms of foreign trade (chapter III), external finance (chapter IV) and transport and communications (chapter V). Chapter VI derives some policy conclusions drawing on, but not limited to, the analyses in the previous chapters.

CHAPTER I

EMERGING GLOBAL TRENDS AND THE ESCAP REGION

I

GLOBALIZATION

Major determining factors

Globalization has been a much discussed topic in recent years. It involves greater interaction across national boundaries and affects many aspects of life: economic, social, cultural and political. The focus of the analysis in this chapter is on the economic aspects. In this context, globalization essentially implies increasing cross-border movement of goods, services, finance and factors of production. This process is being driven by a number of mutually reinforcing factors which encompass market- and technology-related factors as well as policy changes at the national and supranational levels.

Market- and technology-related factors

Perhaps the most important market-related factor is the intensification of competition in the international economy. This is encouraging firms and nations to seek out the most profitable markets for exports and the cheapest sources for imports. The increasing emphasis on allocative efficiency and productivity growth in developing countries and the economies in transition provides an impetus to greater engagement in international trade and efforts to attract FDI.

The pressures of competition are providing a strong incentive for transnational corporations to minimize costs. One way of achieving this is to undertake locational specialization along the value-added chain. Transnational corporations are demonstrating increasing willingness to locate parts of various functional activities (for example, research and development, finance and accounting as well as production) wherever they can be performed most efficiently. This allows participation of a greater number of countries in different parts of the value-added process. The relocation of manufacturing industries is a distinct element in this process. A growing range of manufacturing activities, associated not only with labour-intensive products but also with many components of low-wage routine tasks in hi-tech industries, have been shifted to offshore locations. This has led to enhanced flow of goods in international trade. Growing imports of components produced or assembled abroad into the home country of transnational corporations, or to affiliates at other locations, constitute as much as 40 per cent of world trade in industrial goods.

The management of global networks requires service facilities, including transport and communications, and a variety of professional business and financial services. Transnational corporations have come to play a significant role in the production and sale of those services as well. They have become important in the international delivery of a wide range of services through wholly owned foreign investment, joint ventures and various forms of contractual arrangements. These deliveries consist, *inter alia*, of professional services such as accounting, advertising, management consulting, legal and computer services. Some developing countries are also participating in the growing trade in some of the professional services, notably computer software and financial services, along with the traditional services related to transport and travel.

A series of developments in the financial markets since the 1970s involving innovations in institutions and instruments, the creation of offshore banking centres, and the establishment of regional markets have served to internationalize the financial industry. These have contributed to a vast increase in the volume of international flows of finance and related services.

The trend towards urbanization, which usually accompanies a production mix with higher shares of manufacturing and services, is a major force in the globalization process. Urban life everywhere tends to develop similar tastes, preferences and demand patterns that easily take on a global character, backed up by easy access to information in urban locations on standards and styles. The increasing convergence of consumer tastes across national boundaries is helping to boost the globalization of the market for goods ranging from apparel to electronics. The process has been aided again by the growing involvement of large transnational corporations in the retailing of consumer services. The possibilities of

economies of scale in the delivery of such services, and the increasingly open and expanding markets for them have induced large corporations to produce the consumer services that used to be produced only by small, single-site, local firms. This is evident in a wide variety of services, such as hotels, restaurants, movie theatres, car rentals, photo-processing and development, real estate, movement and storage, various repair services and retail outlets for a broad range of consumer goods.

Movement of capital, goods and services has been paralleled by the movement of labour. Millions of people have migrated from their countries of origin in the post-war era. One estimate put approximately 125 million people living outside their country of birth at the beginning of 1995, which may have included 25 million contract workers outside their homelands and over one million short-term skilled and professional workers.[1]

People have migrated for a variety of reasons. Many of them, however, have been motivated by economic considerations. The recent upsurge in FDI, in part associated with the relocation of production to low-wage developing countries, has not succeeded in bridging wage differentials across countries. Lack of adequate employment opportunities at home and expected high potential earnings abroad continued to induce people from developing countries to migrate to more economically advanced countries.

The market-related factors propelling the globalization process have been aided by technological advances. Technology permits greater "componentization" of production and creates the scope for producing different components in different countries. At the same time, advances in informatics and telecommunications have contributed to the convergence of demand patterns and have increased the capacity to process and communicate the information required for cross-border transactions, while reducing the cost. For example, the price of a computer with a processing power of 4.5 million instructions per second fell from $4.5 million in 1980 to $100,000 in 1990 (current prices) and is projected to come down to $10,000 by the year 2000.[2]

Electronic commerce is increasingly facilitating trade through the systematic rationalization of procedures and documentation for international trade. The delivery of a wide range of services, including financial services, across national borders would be severely constrained in the absence of improvements in information and communications technologies that have been taking place over the past few years. Transnational corporations depend heavily on information technology to coordinate their activities throughout the value chain located in different parts of the world. Similarly, developments in transport technologies have facilitated the globalization process through faster and cheaper movement of goods and people.

Policies at the national and international levels

The market- and technology-related forces leading the globalization process have been reinforced by the policy stance adopted at the national and international levels. At the international level, there is an increasing emphasis on securing multilateral agreements on the rules affecting international transactions and increasing the transparency of those rules. At the national level, restrictions and controls on domestic and international transactions of goods as well as a wide variety of services have been and are being progressively removed or eased. Investment rules have been liberalized to encourage foreign investment in the domestic economy. Financial transactions have been eased by removal or relaxation of controls on capital movements as well as entry and operation of banking and other financial institutions.

The liberalization process, which started early in the developed countries, is now being repeated worldwide. The former socialist countries, often designated as economies in transition, have come to accept the principle of openness towards the outside world. They have already introduced significant liberalization and deregulation measures.

Most of the developing countries and the economies in transition are seeking to open their economies to international trade on the basis of freedom of access to markets according to their comparative advantage. This has often entailed trade liberalization measures, including reductions in tariff rates and relaxation of quantitative controls or other non-tariff barriers to trade.

---

[1] UNCTAD, *Foreign Direct Investment, Trade, Aid and Migration* (United Nations publication, Sales No. E.96.II.A.8), p. 5.

[2] UNCTAD, *World Investment Report 1995* (United Nations publication, Sales No. E.95.II.A.9).

Since the late 1970s and the early 1980s, most of the developed countries have removed existing statutory regulations governing their financial institutions, particularly those relating to controls on the movement of funds, interest rates and the separation of areas of business of commercial banks from those of securities firms. To varying degrees, similar measures are also being adopted by developing countries. There has been a discernible move in many developing countries towards deregulation of interest rates, relaxation of directed credit requirements and easing of entry and operating conditions for foreign banks. The deregulation has facilitated the internationalization of the financial market with the participation of investors and borrowers from all over the world. Tremendous growth in the activities of the financial markets has resulted since then; however, traditional bank lending declined in favour of various forms of securitized financing.

The globalization of financial markets has also been aided by developments in foreign exchange regimes. There has been wider adoption of flexible exchange rates. Many developing countries have not only removed restrictions on foreign exchange transactions under the current account but have also substantially reduced controls on capital accounts.

There has been a marked policy shift, particularly in developing countries, towards FDI. The policy objective appears to be increasingly one of promotion of, rather than restriction on, such investment. The measures used typically include opening up sectors previously reserved for domestic investors (public or private), relaxing performance requirements and providing fiscal and financial incentives.

At the international level, the Uruguay Round is viewed as the most comprehensive set of agreements on multilateral rules ever devised to govern most areas of cross-border transactions. Altogether, 21 multilateral agreements and understandings were reached, in addition to the umbrella agreement to set up WTO. The phase of their implementation began with the establishment of WTO as of 1 January 1995. WTO is not only to oversee the implementation of the agreements that have been reached but also to continue as a forum for further negotiations of multilateral agreements on trade and related issues. Although many hurdles must be cleared before the agreements already reached can be fully implemented and difficult negotiations lie ahead on issues still unresolved, the Uruguay Round and WTO provide the framework for a further push towards globalization by freeing the markets for goods, services, finance and technology (box I.1).

Efforts are also being made at the international level to enhance the stability of macroeconomic parameters affecting financial transactions and to improve the functioning of financial institutions. The economic summits of the group of seven major industrial countries, instituted since 1975, have increasingly focused on policy initiatives to impart a degree of stability to exchange rates among the countries' currencies. The 1988 Basle accord, a major policy initiative, increased and harmonized risk-weighted capital ratios for banks in 10 major industrialized countries. Following the Mexican crisis, efforts are under way in a joint forum, comprising banking, security and insurance supervisors from these countries, to examine ways of improving the supervision of international financial conglomerates. Meanwhile, IMF has instituted new arrangements to borrow, which will double the credit lines available to the Fund for use in the event of a systemic crisis.

REGIONALIZATION

The process of globalization has been paralleled by a trend towards regionalization of economies throughout the world. In the present context, regionalization is viewed as a process whereby groups of countries agree to cooperate on economic relations among them within an agreed framework of policies and institutions. Since the initiation of the first regional cooperation arrangement among the Western European countries in the late 1950s with the signing of the Treaty of Rome, regional cooperation arrangements have proliferated over most of the world, usually involving developed countries or developing countries exclusively, but sometimes mixed. Almost every OECD country is now a member of some sort of regional cooperation arrangement. Similarly, nearly all the countries in Latin America and the Caribbean are involved in one type of regional cooperation arrangement or another,

Box I.1. Highlights of decisions taken at the World Trade Organization Ministerial Conference

The first WTO Ministerial Conference was held in Singapore from 9 to 13 December 1996. The Conference was the first regular biennial meeting of WTO at the Ministerial level, as called for under Article IV of the Marrakesh Agreement establishing the World Trade Organization. The Ministerial Declaration issued at the end of the Conference re-emphasized the importance of growth in global trade, facilitated by trade liberalization within a rule-based multilateral system, as a means for the promotion of sustainable growth and development and the creation of better-paid jobs in many countries. It was accepted that changes in the international economy, including trade in services and direct investment, would require ongoing adjustments by economies and societies. The ministers committed themselves to addressing the attendant challenges.

Various issues were raised at the Conference relating to the opportunities and challenges that the process of integration was creating and the role that WTO could play in that context. One of the contentious issues discussed was the question of core labour standards. It was agreed that ILO was the competent body to set and deal with these standards. The Declaration rejected the use of labour standards for protectionist purposes.

The Conference reiterated its commitment to full and faithful implementation of the provisions of the Agreement on Textiles and Clothing. It agreed that the use of safeguard measures in accordance with the provisions of that Agreement should be as sparing as possible. This is of great importance to developing economies in the ESCAP region as textiles and clothing constitute a significant export item for many of them.

A significant outcome of the Conference was the Ministerial Declaration on Trade in Information Technology Products. The signatories, which included several members and associate members of ESCAP, agreed to eliminate tariffs on a range of information technology products, in a series of steps, by the year 2000. Information technology applications will be a key element in shaping the future pattern of global economic growth. The elimination of tariffs is expected to stimulate greater trade in information technology products. This development, together with the agreement signed by 68 countries in February 1997 to liberalize their telecommunications markets, promises to reduce the cost of using information technology significantly and thereby promote growth in the ESCAP region.

Another important issue addressed in the Conference related to the interaction between investment and competition policy. It was agreed that a working group would be set up to study issues related to such interaction, on the understanding that the work undertaken would not prejudge whether negotiations would be initiated in the future.

The Conference adopted a Plan of Action for enhancing the integration of the least developed countries in the multilateral world trading system. The Plan seeks to improve their access to the markets of all developed countries through, for example, preferential duty-free access, and to foster the expansion and diversification of their exports. The Conference agreed that WTO would organize a meeting jointly with UNCTAD and ITC in 1997, with the participation of donor agencies, multilateral financial institutions and least developed countries themselves, to develop an integrated approach towards assisting these countries in enhancing their trading opportunities.

The Conference noted the continuing expansion of regional trading agreements in different parts of the world. It reaffirmed the primacy of the multilateral trading system but accepted that these agreements could promote further liberalization and facilitate the integration of the least developed, developing and transition economies into the world trading system. In this regard, the Ministers renewed their commitment to ensure that regional trading agreements would be complementary to, and consistent with, the rules of the multilateral trading system.

The Uruguay Round and the creation of WTO are landmark steps in fostering international economic integration, enhancing trade linkages among countries and ensuring that the benefits of trade are shared more widely. The maintenance and strengthening of the current upsurge in the growth of world trade in both goods and services rest on the full implementation of the liberalization measures envisaged in the Uruguay Round. The emphasis laid in the first WTO Ministerial Conference on the necessity of adhering to the timetable for implementation of the agreements in the years ahead is of particular significance in this context.

as are those in Africa.[3] The former socialist countries were also bound under a type of regional cooperation arrangement which collapsed after the dissolution of the Union of Soviet Socialist Republics, but new forms of arrangements are being forged to enhance cooperation among some of them. Countries in the Asian and Pacific region are grouped into a number of arrangements that include ASEAN, ECO, SAARC, SPC, South Pacific Forum and, more recently, APEC.

The motivation to form regional cooperation arrangements among various groups of countries has been diverse. In some cases these arrangements were initiated for defence or security objectives, but their focus later shifted to economic cooperation. In general, regional cooperation arrangements have been motivated by the desire to reap the economic benefits that could accrue from better utilization of complementarities and economies of scale from an enlarged market across a wider geographical space. Geographical contiguity offers advantages in terms of savings in transport and transaction costs as well as the chance of better understanding and collaboration based on the relative closeness of cultures, values and attitudes.

Regional cooperation arrangements find another justification on more practical grounds: it is much easier to negotiate and reach agreements on relevant issues within relatively homogeneous and smaller groups than in multilateral negotiations involving many countries worldwide. Furthermore, negotiations within a bloc can facilitate agreements in multilateral forums, as was found to have been happening during the course of the Uruguay Round negotiations. Agreements within groups can lead to faster and deeper reductions in barriers to trade and other cross-border economic activities than would be possible in multilateral negotiations. Regional cooperation groups can thus provide the so-called "cutting edge" in the movement towards freer multilateral trade and economic relations rather than being a hindrance. However, there is the risk that such arrangements may degenerate into inward-looking blocs to the detriment of the growth of non-discriminatory multilateral economic relations.

[3] For a comprehensive review of regional cooperation arrangements throughout the world, see Percy S. Mistry, *Regional Integration and Development: Panacea or Pitfalls?*, RIS Occasional Paper No. 47 (New Delhi, Research and Information System for the Non-Aligned and Other Developing Countries, 1995).

THE OUTCOMES

The outcomes of globalization are more easily quantifiable in terms of data on flows of trade, investment and finance. Data on these variables clearly show tremendous growth over the past three decades or so and demonstrate growing global economic interaction and interdependence. The origin and the distribution of these flows indicate the extent to which groups of countries and territories are participating in the process.

Trade flows

The nominal dollar value of world exports of goods and services increased from just above $400 billion in 1971 to $6.7 trillion in 1994, or by a factor of 16.2. Comparison with 1971 may, however, reflect the monetary and exchange rate upheavals that have taken place since then and exaggerate the real growth in the volume of international trade since that year. Between 1980 and 1994, the value of trade in goods and services rose by a factor of 2.6. The services component of trade rose by a factor of 3.7 between 1980 and 1993.

The value of world merchandise trade constituted 16.5 per cent of world GDP in 1994, rising from about 10 per cent in 1970. The value of trade in goods and services combined, however, rose to 27 per cent of world GDP in 1993 compared with 11.4 per cent in 1971. The underlying rates of growth in trade in goods and services have thus been faster than the rate of growth in world GDP during the same period. A faster growth rate for trade in services is also implied. The share of services trade as a proportion of world GDP more than doubled between 1971 and 1993 while that of merchandise trade increased about 1.5 times. Growth in merchandise trade has been associated with a growing share of manufactured products in total trade. These trends towards a rising proportion of world output entering world trade are the clearest and most frequently quoted indicators of globalization.

Developing countries as a group have enhanced their share of international trade in goods and services. The share of their exports in world trade in goods and services rose to 23 per cent in 1994 from 15 per cent in 1971. The developing countries' share in merchandise exports, however,

was 27 per cent in 1994, having risen from about 17 per cent in 1971, and their share in exports of services stood at 15 per cent compared with 10 per cent in 1971. The better performance of developing countries in merchandise trade is also reflected in the dramatic rise in their share of the world exports of manufactured goods from 6 per cent in 1970 to almost 25 per cent in 1994. That left close to 75 per cent of such trade to the industrialized countries. The industrialized countries' share in total services trade was 82 per cent in 1994 compared with 90 per cent in 1971. In merchandise trade, their share came down from 83 per cent in 1971 to about 72 per cent in 1994.

It is noteworthy that developing countries in the ESCAP region have vigorously participated in this process, outperforming other developing countries. This is clearly brought out by the fact that developing countries' share of world exports of goods and services increased by a factor of 1.5 between 1971 and 1994, whereas the share of developing countries in the ESCAP region more than doubled. In the case of services, their performance was even better, as their share tripled over the same period. Practically all of the increase in the developing countries' share of manufactured exports is accounted for by developing countries in the ESCAP region.

The picture is broadly similar with respect to imports. Developing countries in the region have outperformed other developing countries and increased their share of imports. Between 1971 and 1994, developing countries as a group increased their share of world imports from 10 to 27 per cent; developing countries in the ESCAP region tripled their share from 6 to 18 per cent. It is also noteworthy that the import growth of developing countries in the ESCAP region was faster than their export growth, leading to a greater current account deficit, which was financed by inflows from external sources (see chapter IV).

Financial and investment flows

In recent years, developing countries, particularly those in Asia and the Pacific, have become progressively more integrated with international financial and capital markets. Over a 10-year period from the mid-1980s to the mid-1990s, world stock market capitalization rose from $4.7 trillion to $15.2 trillion or by a factor of 3.2. During the same period, capitalization in emerging markets, which included a number of developing Asian markets, rose from less than 4 to 13 per cent of total world capitalization. The value of shares traded in emerging markets increased from less than 3 per cent of the $1.6 trillion world total in 1985 to 17 per cent of the $9.6 trillion value of shares traded on all of the world's exchanges in 1994. International investors have increasingly participated in this rapid development of emerging stock markets. Portfolio flows of equity investment to emerging markets rose to $39 billion in 1995 from a mere $100 million in 1985.[4] The share of developing countries in international equity issues rose from 14 per cent in 1990 to 35 per cent in 1995, largely owing to an increase in issues originating in South and South-East Asia.[5]

The 1995 FDI outflows amounted to 1.2 per cent of world GDP and 7.6 per cent of world merchandise trade. However, FDI flows as a proportion of world GDP and global gross fixed capital formation doubled between 1980 and 1994. The value of FDI stock, at $2.7 trillion, was about 10 per cent of world GDP. Notwithstanding its small relative size, FDI has a significant impact on world production and trade. The value added of all affiliates (numbering 270,000) of 39,000 transnational corporations accounted for 6 per cent of world GDP in 1991, having risen from 2 per cent in 1982. The intra-trade among the companies and their affiliates accounted for 40 per cent of world trade in industrial goods.[6]

In the area of FDI, developing countries in the region have also become active participants. In terms of inflows, they increased their share of world inflows from an average of under 9 per cent during the period 1984-1989 to 21 per cent in 1995, with the share of total inflow to developing countries rising from 45 to 66 per cent over the same time

---

[4] Asli Demirgüç-Kunt and Ross Levine, "Stock markets, corporate finance, and economic growth: an overview", *The World Bank Economic Review*, vol. 10, No. 2, May 1996, p. 223.

[5] UNCTAD, *Trade and Development Report 1996* (United Nations publication, Sales No. E.96.II.D.6).

[6] UNCTAD, *World Investment Report 1996, Investment, Trade and International Policy Arrangements: Overview* (UNCTAD/DTCI/32 (Overview)) (New York and Geneva, 1996).

period. In terms of outflows, their shares rose from 4 to 13 per cent of the world total and from 68 to 88 per cent of the developing country total. Developing countries in the region have thus increased their importance as both recipients and sources of FDI.

Overall, net external resource inflows to developing countries from private sources increased from $25 billion in 1987 to $167 billion in 1995. The developing Asian countries increased their share of these flows from 19 per cent in 1987 to 62 per cent in 1995.[7]

* * *

The active participation of developing countries in the region in the global flows has been accompanied by substantial increases in intraregional flows. The share of intraregional trade flows in terms of merchandise exports increased from about one fourth in 1980 to nearly two fifths by 1995.[8] Similarly, intraregional sources from among developing economies have become increasingly important in FDI. For the economies of China, Hong Kong, Indonesia, Malaysia, the Philippines, the Republic of Korea, Singapore, Taiwan Province of China and Thailand, the share of the inward stock from among themselves increased from 25 per cent in 1980 to 37 per cent in 1993.[9]

THE PROSPECTS

There are always many uncertainties about any prediction of the future. Nevertheless, there are several factors which suggest that the trend towards intensified participation by developing countries in the ESCAP region in the globalization and regionalization processes is likely to continue into the twenty-first century.

First, despite a notable increase in intraregional trade among developing countries in the region, the share of their merchandise exports absorbed by OECD countries remains high (53 per cent in 1994). Their ability to export is therefore significantly dependent on the absorption capacity of the developed market economies, which, in turn, is partly dependent on growth prospects. The available projections indicate healthy growth for those countries into the twenty-first century, well above the actual achievement of the 1991-1995 period (table I.1).

Second, projections of world trade into the twenty-first century are promising. The World Bank forecasts a 6.3 per cent annual increase in the volume of world merchandise trade over the period 1996-2005.[10] IMF projects an annual average growth rate of 7 per cent in the volume of world trade in goods and services over the period 1998-2001.[11]

Given the demonstrated ability of Asian and Pacific countries to benefit from growing international trade, the above projections augur well. In fact, the World Bank projects that the export volume of goods and non-factor services of South Asia will increase by 7.3 per cent annually over the period 1996-2005 and that of East and South-East Asia by 10.1 per cent.

Third, prospects for private financial flows appear favourable. Moderate international interest rates likely to result from lower inflationary expectations and continued fiscal consolidation in industrial countries would imply lower yields on financial assets in those countries. The consequential pressures to diversify portfolios will favour the ESCAP region because of higher growth prospects and the expected continuation of liberalization and deregulation of financial sector policy regimes.

Fourth, the following factors should continue to promote the flow of FDI: the rising per capita income in developing countries in the region at rates higher than in the rest of the developing world; increasing competition in the industrial as well as the developing countries and the resultant pressures on their transnational firms to locate abroad in search of reduced production costs; and the strong likelihood of further liberalization of trade and investment policies in developing countries in the region.

---

7 World Bank, *World Debt Tables, various issues* (Washington DC).

8 Based on UNCTAD, *Handbook of International Trade and Development Statistics*, various issues.

9 UNCTAD, *World Investment Report 1995* (United Nations publication, Sales No. E.95.II.A.9).

10 World Bank, *Global Economic Prospects and the Developing Countries* (Washington DC, 1996).

11 IMF, *World Economic Outlook* (Washington DC, October 1996).

Table I.1. Projections of world economic growth

(Percentage)

	Average						
	1981–1990[1]	*1991–1995*[1]	*1996–2000*[2]	*2001–2010*[2]	*2011–2015*[2]	*1996–2005*[3]	*1995–1999*[4]
World	**2.9**	**1.4**	**2.7**	**2.5**	**2.6**	**3.5**	**2.9**
Developed market economies	2.9	1.5	2.1	2.0	2.1	2.9[a]	2.3
Major industrialized countries (G7)	2.9	1.5	..	..	..	2.8	..
Germany	..	1.4	1.4	1.9	2.1	..	2.0
Japan	4.1	1.3	2.3	2.8	3.1	..	2.1
United States	2.9	1.9	2.4	2.1	2.2	..	2.2
Other industrialized countries	2.3	1.5	..	..	..	2.7	2.5
European Union[b]	2.3	1.3	1.6	1.5	1.5	..	2.4
Developing countries	3.1	4.8	4.9	4.3	4.0	5.4[c]	5.7
Africa	2.0	1.6	2.3	2.4	2.3	3.8	3.4
Latin America and Caribbean	1.2	2.7	3.0	2.4	2.6	3.8	3.4
Asia and Pacific	7.0	7.2	6.7	5.8	5.1	7.2	7.1[d]
West Asia	–1.3	2.3	4.0	2.6	2.1	..	2.9
Economies in transition	2.0	–7.7	3.3	2.3	1.8	..	4.8

Sources:

(1) *World Economic and Social Survey* (United Nations publication, various issues).
(2) Akira Onishi, Soka University, "Long-term projections of the world economy, 1996-2015: baseline and policy simulations on sustainable development".
(3) World Bank, *Global Economic Prospects and the Developing Countries 1996* (Washington DC, 1996).
(4) United Nations, University of Pennsylvania and University of Toronto, Project LINK World Outlook, Summary, 30 September 1996.

a High-income economies as classified by the World Bank.
b Mr Onishi's figures are for Western Europe.
c Low- and middle-income economies as classified by the World Bank.
d ESCAP estimate based on LINK Projections.

Similarly, the prospects for regional cooperation in trade and investment are likely to gather stronger momentum. In part, this would be due to rising income and per capita consumption, overall export growth, moderate inflation and modest current account deficits projected for South, East and South-East Asian countries (table I.2). To some extent, it can be anticipated that there will be a further intensification of regional cooperation within the various institutional arrangements currently in existence. Moves in this direction are already visible.

Since its establishment in 1967, ASEAN has been continually evolving and has adopted a plan to establish the ASEAN Free Trade Area (AFTA) by the year 2003. There is also the expectation of expansion of its membership from the current 7 to 10 countries. SAARC, which started with a sector-by-sector technical cooperation approach, has embraced cooperation in the field of trade under its South Asian Preferential Trading Arrangement (SAPTA) scheme. The negotiations under this arrangement are in progress, and it was recently agreed that the number of products to be covered would be substantially increased (see chapter III for details). Following the expansion of its membership from 3 to 10 in 1992, ECO adopted an economic cooperation strategy in 1993, focusing on cooperation in trade, transport and communications, and energy. There are detailed plans for implementation over a 10-year period. The plans aim at, *inter alia*, the progressive removal of trade barriers among

Table I.2. South, South-East and East Asia: forecast average annual growth rates

(Percentage)

	1986-1995	*1996-2005 (Baseline)*
South Asia		
GDP	5.1	5.4
Consumption per capita	2.4	3.1
GDP per capita	2.9	3.7
Export volume[a]	9.2	7.3
Median inflation[b]	9.1	6.4
Current account/GDP	–2.1	–2.3
East and South-East Asia		
GDP	8.5	7.9
Consumption per capita	5.6	6.8
GDP per capita	6.9	6.9
Export volume[a]	13.4	10.1
Median inflation[b]	6.8	5.8
Current account/GDP	–0.7	–1.5

Source: World Bank, *Global Economic Prospects and the Developing Countries* (Washington DC, 1996), tables A2-1 and A2-2.

[a] Goods and non-factor services.
[b] GDP deflator.

ECO member countries, the facilitation of transportation and transit of goods and passengers among them through short-, medium- and long-term measures and the preparation of an energy master plan.[12]

APEC, 14 of whose 18 members belong to the ESCAP region, has set the goal of major liberalization of trade, a goal to be reached by its industrialized member countries by 2010, whereas the developing member countries would do so by 2020. At the Ministerial Meeting of APEC, held in Manila on 22 and 23 November 1996, the Manila Action Plan for APEC 1996 was adopted on the basis of the individual action plans submitted by the countries on a voluntary basis and outlining their proposed paths towards intensified cooperation. APEC has kept its membership open to other countries although a moratorium on membership is currently in force.

Economic cooperation efforts are being intensified among the component states of the former Soviet Union, including Central Asian members of ESCAP. In 1994, Kazakstan, Kyrgyzstan and Uzbekistan created the Central Asian Economic Union with the objective of establishing a common market in Central Asia. An agreement on the promotion of integration in economic and humanitarian areas was signed by Belarus, Kazakstan, Kyrgyzstan and the Russian Federation in March 1996. In accordance with the agreement, the four countries formed a customs union. The main objectives of the Union are to remove barriers hampering the movement of goods, services and capital and to shape common economic space on the basis of common customs territory and uniform economic regulations. Unified rules with regard to re-export and modalities of trade with third countries have been adopted by the countries concerned, and a common system of preferences for developing countries has been introduced. Alongside the customs union, these countries are working out a payment and settlement facility within the framework of an agreement on establishing a payments union.

In addition to formal groups, a unique emerging feature of regional cooperation in the Asian and Pacific region, particularly in East and South-East Asia, is the establishment of growth zones involving parts of several neighbouring countries. These have various configurations and are called growth triangles, quadrangles or the like. A few such zones are already functioning successfully, and several more are at various stages of implementation. The possibility of setting up such growth zones is also being investigated in other subregions.

The ESCAP region now extends to 37 per cent of the world's land area and is home to 62 per cent of its population. It offers in itself a vast market. Estimates currently put more than a billion people in the region, a number that far exceeds the total population of all the developed countries of the world, with per capita incomes of more than $10,000. Such figures signify the region's current market potential and, given the prospects for future expansion noted above, there will be immense opportunities to strengthen intraregional economic linkages.

12 For details, see ECO, "Economic cooperation strategy for the ECO region" *Treaty of Izmir and Related Documents*, ECO/ES dated 9 May 1996 (Ministry of Foreign Affairs, Ankara, 1996).

THE CHALLENGES

The analysis in the preceding sections has clearly pointed to the growing participation of developing countries generally, and those in the ESCAP region in particular, in globalization and regionalization. For the region as a whole, prospects in the twenty-first century appear promising. However, such participation is not necessarily smooth; nor does it guarantee equitable gains for all countries and peoples. Many challenges have to be met along the way, some of these are briefly analysed below.

Persistent disparities

One major challenge concerns the persistence of disparities between and within countries. While globalization and regionalization are opening up new opportunities for trade, investment and growth, the benefits seem to be bypassing a large number of people in both developed and developing countries. It should be noted that the outcomes noted below in support of this proposition are not necessarily the consequences of globalization and regionalization. They do, however, illustrate that the globalization and regionalization processes can coexist with increasing disparities, and hence specific remedial policies may be required.

Twenty-four high-income countries with 4.5 per cent of the world population accounted for close to 80 per cent of the global GDP in 1995, giving them a per capita income of about $23,000. In contrast, 5 per cent of the global GDP was generated by 45 low-income countries with about 55 per cent of the world population and a per capita income of about $324.[13] The gap in per capita income between the industrial and the developing countries tripled between 1960 and 1993.

Personal income distribution worldwide and within countries has become more skewed. Between 1960 and 1991, the share of the richest 20 per cent of the world's population rose from 70 per cent of global income to 85 per cent, while that of the poorest 20 per cent declined from 2.3 to 1.4 per cent. The ratio of the shares of the richest and the poorest increased from 30:1 to 61:1. All but the richest quintile of the population saw their income share fall so that by 1991 more than 85 per cent of the world's population received only 15 per cent of its income. The disparities between the world's rich and the poor are further dramatized when it is discovered that the world's 358 richest people have a combined net worth equivalent to the total income of the poorest 45 per cent of the world's population, or 2.3 billion people.[14]

Within the ESCAP region, large disparities persist between and within countries. According to classifications made by the World Bank, out of 50 of the members and associate members of ESCAP, 17 fell into the low-income category (7 in South Asia, 6 in South-East Asia and 4 in Central Asia), 21 fell into the lower middle-income category (most of them Pacific islands and 3 in South-East Asia), 4 in the upper middle-income category (Guam, Malaysia, New Caledonia and the Republic of Korea), and 8 in the high-income category (Australia, Brunei, French Polynesia, Japan, Hong Kong, Macau, New Zealand and Singapore).[15] The range of disparities in terms of per capita income remains wide (see chapter II).

Some 70 per cent of the world's poor people live in the ESCAP region. Although most countries in the region have been able to reduce the incidence of poverty in terms of the head-count ratio, the rate of reduction appears to have slowed down since the mid-1980s in many countries. In several countries, this has led either to an increase or to virtually no change in the absolute number of poor people.

There are also wide variations among countries in levels and speed of integration with the world economy. The World Bank has recently calculated indices of the level and speed of integration of different countries. These indices are based on changes in the ratios of foreign trade to

---

[13] Mihály Simai, "Globalization, multilateral cooperation and the development process: the UN agenda and end-of-century realities", Hungarian Academy of Sciences, Working Paper No. 63 (Budapest, Institute for World Economics, April 1996), p. 15.

[14] UNDP, *Human Development Report 1996* (New York, Oxford University Press, 1996), p. 13.

[15] World Bank, *Global Economic Prospects and the Developing Countries* (Washington DC, 1996).

GDP, foreign direct investment to GDP, share of manufactured products in exports and the institutional investors' credit ratings. According to these calculations, the speed of integration of developing countries in the region ranged from –0.42 for Myanmar to +3.52 for Singapore.

Risks in liberalization and openness

The developing countries in the region have generally made voluntary moves towards policy liberalization in wide areas of trade, investment, finance and the services, with the expectation that such liberalization would have a favourable long-term impact on their economies. This attests to their willing participation in the globalization process. However, to some extent, the pace and pattern of the reforms and adjustments are subjected to the imperatives of the external circumstances. It has not been easy for the countries to adjust to the changes in the external environment, such as wide fluctuations in the exchange rates of major currencies, the oil shocks or precipitous declines in non-oil commodity prices in the past. The conditionalities that donors and financing agencies insist on have been another external imperative. In the current phase, the demand for changes seems to be much more extensive than at any time before, originating from trade partners through bilateral pressures, from multilateral organizations through conditionalities for assistance or from the need to comply with multilateral agreements.

The developing countries' trade regimes, for example, would have to become significantly more open than in the past within a relatively short period of time under the commitments for reduction of trade barriers in the Uruguay Round. Competition both in the export and the domestic markets will be much more intense. Policy instruments that were used earlier to pursue export-led strategies may no longer be feasible.

The agreements reached under the Uruguay Round on TRIMs and TRIPs would impose additional obligations on the developing countries. The TRIMs agreement, for instance, effectively prevents the application of trade-related performance requirements, such as local content and trade balancing, to foreign-owned enterprises. Such policies played a significant role in the FDI policies of some of the fast-growing economies of East and South-East Asia.

Similarly, there is a concern that the TRIPs agreement may reduce the developing countries' access to technology and increase its cost. Moreover, compliance with the agreement will require changes in domestic legislation in wide range of areas covering, *inter alia*, patents, trade marks, copyright, industrial design and protection of trade secrets. Many low-income countries with limited administrative capacity and legal expertise may find it costly to make the necessary changes.

Although the agreements reached under GATS are limited in scope, they will increase the pressure on developing countries in WTO and other forums to open their markets further in many service areas. As indicated above, the share of developing countries in the ESCAP region in world trade in services is currently small. Some of the countries are fast developing capacities in certain services, such as computer software. They have to ensure that their nascent domestic facilities are not overwhelmed by competition from the powerful transnational corporations. As mentioned above, transnational corporations have been entering domestic service industries in wide-ranging areas, either through fully owned subsidiaries in developing countries or through local partnerships and other contractual arrangements.

Despite some provisions in the Uruguay Round aimed at restraining the use of non-tariff barriers, many developing countries are concerned that such barriers may continue to be applied for protectionist purposes, limiting market access to their exports. These barriers could arise from, *inter alia*, anti-dumping actions, domestic subsidies, safeguard measures, technical standards and labour welfare criteria.

FDI is being welcomed as a more preferred form of foreign capital since it does not give rise to immediate debt obligations and usually brings higher management skills and technology, which may eventually spread throughout the domestic economy. Nevertheless, it gives rise to large payment obligations in the future and burdens the balance of payments in subsequent time periods. Some of the earlier recipients of large inflows of FDI are already experiencing sizeable outgoings owing to existing foreign investment stocks in their economies.

One risk of greater external openness is the instability that can be generated in the domestic economy by the export sector. Many of the developing economies in the region have now substantially reduced their dependence on primary commodities and the risk of fluctuations in their economies originating from the variations in the prices of such commodities. Nevertheless, the risk of a sudden decline in particular sectors remains owing to the concentration of exports in a narrow range of products within the category of manufactured products. Several countries in the region are currently experiencing this because of a decline in the demand for and prices of electronic goods. Most analysts seem to agree that this is a temporary phenomenon and that it should not have any significant bearing on the medium- to long-term growth prospects of the region. Nevertheless, it illustrates the nature of the risk and points to the need for diversification of exports.

Another element of risk has now been introduced through the financial sector, which is becoming more open externally. Greater freedom has been given to domestic commercial banks to establish credit lines abroad and to domestic non-bank borrowers to participate in foreign capital markets; at the same time, foreign investors have been allowed greater freedom to participate in the domestic capital market. Such openings make the domestic financial and capital markets more sensitive to changes in international interest rates, the perception of credit risks by foreign financial institutions and other creditors, and the speculative moves that market players can trigger. The developing countries in the ESCAP region have not so far suffered a major crisis on this account, though several countries which have further liberalized the financial sector have felt the underlying pressures in recent years.

There are some distributional and welfare concerns closely connected to liberalization, deregulation and openness. For example, as the role of transnational corporations increases in an economy, questions arise about the distribution of gains between the host country and the transnational corporations as well as among population groups within the host country. The liberalization of prices may increase the cost of basic necessities for poor households without bringing a compensatory increase in income. Import liberalization and industrial restructuring may cause job losses for workers, some of whom may not easily find alternative employment. Similarly, there are concerns about the implications of a more liberalized and globalized economy for environmental sustainability. For example, stronger export orientation may cause faster depletion of natural resources or greater discharge of industrial effluents into the river systems unless adequate countervailing measures are adopted.

Infrastructure

The successful integration of the economies in the region will be partly conditioned by progress in the development of a supportive infrastructure of various sorts, such as power, transport and communications. Infrastructural inadequacies impose a major constraint on both trade and financial or investment flows. The speed with which effective transport and communications linkages can be developed is particularly important in this context. For example, the lower degree of integration of vast inner territories on the Asian continent can be partly explained by the lack of access to sea transportation and port facilities, which the dynamic East and South-East Asian countries possess. There would have to be considerable improvements in surface transportation systems for territories in the inner areas to be able to connect effectively with outside economies.

It is thus vital to develop the Asian land transport infrastructure system, centred around two projects long sponsored by ESCAP: the Asian Highway and the Trans-Asian Railway. Such systems also carry the potential for establishing a more effective economic linkage between Asia and Europe, permitting a further spread of development impulses from developed Europe into Asia through its western and north-western borders. Europe's connection to Asia has been through the long, winding sea routes for the past several centuries since the historic silk route extending from China to Europe fell into disuse. By rebuilding a modern surface transport system, the region can develop truly global links through two geographically open ends of its borders.

The Asian Highway and the Trans-Asian Railway are but two examples. The importance of developing other routes and modes of transport

cannot be overemphasized. The development of communications is a prerequisite for integration with the regional and international economies. The issues connected with transport and communications are dealt with in greater detail in a subsequent chapter.

Mainstreaming the lagging economies

The unevenness in the process of integration among countries has already been referred to. There are a number of disadvantaged economies in the region. These include the least developed countries, the Pacific island countries and the economies in transition. Despite their efforts to deregulate and liberalize their policy regimes with the aim of greater participation in the international division of labour, their capacity to do so is inherently limited. The small size of these economies, the poor state of development of their transport and communication infrastructures, the meagre endowment of both natural and human resources and, for many, land-locked or sea-locked geographical locations far away from the major metropolitan centres of international trade and finance pose formidable constraints on their speedy integration with the globalization and regionalization processes. These disadvantaged economies will therefore require continued support from the international community in order to create the basic conditions favourable to their regional and international integration.

In this context, it is a matter of deep concern that there has been a marked decline in ODA, on which the disadvantaged economies heavily depend. Their capacity to attract private flows is severely limited by the characteristic features mentioned above. The dramatic increase in the importance of private capital flows, which as a proportion of aggregate resource flows to Asia increased their share from 28 per cent in 1987 to 86 per cent in 1995, constrains the access of the disadvantaged economies to external resources.

Domestic budgetary and social problems in donor countries, together with increasing doubts about the effectiveness of aid, have dimmed the prospects of growth in ODA flows. In fact, ODA as a percentage of the GNP of the member countries of the OECD Development Assistance Committee declined from an average of 0.34 per cent during the period 1980-1984 to 0.27 per cent in 1995, the lowest figure since 1950 and a far cry from the 0.7 per cent internationally agreed target. This has adversely affected developing countries in Asia and the Pacific. Long-term net resource inflows to the region from official sources declined from $17.2 billion in 1991 to $14 billion in 1994, but rose to $16.7 billion in 1995. The least developed countries in the region experienced an annual decline of 6.5 per cent in ODA flows at constant prices and exchange rates over the period 1990-1993.

* * *

Greater openness in the economies of the region in the face of the current trends towards globalization and regionalization offers promising opportunities for infusing greater dynamism into their domestic economies. However, this entails risks which countries must be aware of and must develop the capacity to manage. These capacities differ widely across the large number of countries and territories in this vast region. Further attention is paid to these differences in the following chapters.

CHAPTER II

SOCIO-ECONOMIC TRENDS AND PROSPECTS IN THE ESCAP REGION

II

AN OVERVIEW OF THE CURRENT SITUATION

The ESCAP region now covers an overwhelming mass of the continent of Asia. The region also extends over a vast span of the Pacific Ocean. The continual expansion of the Commission's membership has not only extended the region's geographical span but also added to its diversity. Such diversities in terms of territorial and population sizes, current levels of development and the current socio-economic structure have led to wide variations in the level and speed of integration, as mentioned in the preceding chapter.

The variations in the level and speed of integration are partly influenced by several variables related to macroeconomic and social development. The recent performance of developing countries in the ESCAP region with respect to some key variables is presented in table II.1. It should be noted that there is not necessarily a close correlation between a country's achievement in terms of these indicators and the level or the speed of integration with the global or the regional economy. There are a number of other policy and structural variables which determine a country's willingness and ability to achieve integration.

Nevertheless, it can be hypothesized that the indicators listed in table II.1 would have a significant influence. For example, the level of per capita income together with its population size is a major indication of a country's market size, which, in turn, is an important determinant of a country's ability to attract FDI. A similar comment also applies to the growth rate of GDP as foreign investors generally take into account both the size of the market and its growth potential in decisions concerning investment locations. These considerations are particularly important for domestic market-oriented FDI. The elements of macroeconomic balance and stability, such as inflation, fiscal deficits and current account deficits (which reflect the gap between domestic savings and investment) are widely acknowledged to affect foreign trade and external financial inflows through their effects on, *inter alia*, interest rates, exchange rates, rates of return on investments and credit ratings.

Participation in globalization processes requires a healthy and educated population. For example, a country with poor health conditions cannot be expected to maintain the level of productivity required of its workforce in order to preserve and enhance its competitiveness in the global economy. The development, acquisition and diffusion of modern technology require a critical mass of skilled workers as well as scientific, technical, research and management personnel. Indicators related to health and education are thus an important part of the initial conditions which are likely to impinge on a country's ability to integrate with the global and the regional economies.

As is evident from the data in table II.1, there are striking differences among countries in the region. In terms of annual per capita income, the most basic and widely used indicator of living standards, the difference between Japan's $40,740 and Bhutan's $170 is stark. Comparing Japan, or for that matter Australia and New Zealand, which are classified as the region's three developed countries, with Bhutan may be considered far-fetched. Among the developing economies themselves, Singapore and Hong Kong, where per capita incomes exceed those of Australia and New Zealand, stand at one end, whereas Bhutan and the other least developed countries with per capita incomes below $300 stand at the other. There are also wide differences among economies which stand between these extremes.

Per capita income level is often regarded as an inadequate indicator of development. However, from the data in table II.1 one could easily discern that indicators of social and human resources development, such as adult literacy, infant mortality and life expectancy, closely correspond to per capita incomes. This correspondence is also visible if the countries' ranks in terms of per capita income levels are compared with their ranks in terms of human development index (HDI) values. HDI is a composite index that UNDP has been calculating over the past several years.

Table II.1. Selected aspects of socio-economic development in the ESCAP region

Country/area[a]	Per capita GDP/GNP (US$) 1995	Population (million) 1995	Annual average GDP growth rate 1991-1995	Savings rate (% of GDP) 1995	Investment rate (% of GDP) 1995	Budgetary balance/ GDP (%) 1991-1995	Average annual inflation rates 1991-1995	Adult literacy rate (%) 1995	Infant mortality rate (per 1000) 1994	Life expectancy at birth (years) 1994	Rank in HDI value[b] 1993
Japan	40 740	125.2	1.3	32.0[c]	30.0[c]	-0.7	1.4	95+	4	79.0	1
Singapore	27 990	3.0	8.5	52.0	33.2	4.7	2.6	91	5	75.0	6
Hong Kong	23 130	6.2	5.5	32.6	34.9	1.8	9.3	92	5	78.0	4
Australia	19 260	18.0	2.7	19.0[c]	20.0[c]	-2.8	2.5	95+	6	77.0	2
New Zealand	16 120	3.5	1.7	24.0[c]	21.0[c]	0.0	2.1	95+	7	76.0	3
Brunei Darussalam	15 950[c]	0.3	1.4	..	..	..	2.4[d]	88	8[e]	71.5	7
Republic of Korea	10 160	44.8	7.5	36.7	37.1	-0.3	6.2	95+	15	72.5	5
Malaysia	4 240	19.9	8.6	37.2	40.6	-0.3	4.1	83	14	71.0	10
Thailand	2 810	59.4	8.5	36.5	43.1	2.9	4.8	94	34	68.5	9
Turkey	2 670	61.9	3.4	23.0[c]	22.0[c]	-5.1[d]	80.4	82	62	67.0	14
Russian Federation	2 340[e]	147.0	-10.5	29.0[c]	27.0[c]	-10.4[f]	589.9	99[e]	19	64.0	11
Fiji	2 170	0.8	2.4	18.1[c]	12.2[c]	-3.6	3.9	92	22	72.0	8
Iran (Islamic Republic of)	1 720	67.3	5.8	25.1	16.5	-1.1[d]	29.0	72	39	67.5	12
Tonga	1 720	0.1	3.8	-12.8[g]	17.4[g]	..	5.0	..	18	67.0[h]	..
Kazakstan	1 560[e]	17.1	-14.4	20.0[c]	24.0[c]	-2.9[f]	1 068.3	98[e]	22	69.5	13
Turkmenistan	1 390[g]	4.1	-9.9	..	..	2.4[f]	1 306.8[d]	98	48	66.5	17
Tuvalu	1 330[c]	0.01	6.7	..	..	..	2.6	..	..	..	..
Papua New Guinea	1 180	4.3	7.6	23.4[g]	23.8[g]	-3.8	7.3	72	52	56.5	31
Vanuatu	1 150[c]	0.2	2.7	9.5[e]	34.2[e]	-6.0[i]	3.8	65[e]	47[h]	66.0	29
Maldives	1 070	0.3	6.5	..	..	-12.2	15.2	93	51	64.0	25
Philippines	1 050	67.6	2.2	14.7	22.3	-0.6	10.5	95	39	66.0	20
Indonesia	1 010	195.8	7.8	35.8	37.8	-0.3	8.9	84	56	63.5	23
Uzbekistan	970[e]	22.8	-3.7	24.0[c]	23.0[c]	-10.2[f]	722.8	97[e]	32	69.5	19
Samoa	890	0.2	0.5	..	..	-24.7	5.7	98[e]	64[j]	69.0	15
Kyrgyzstan	850[e]	4.7	-12.0	14.0[c]	30.0[c]	-12.4[f]	545.1	97[e]	27	70.0	22
Solomon Islands	800[c]	0.4	5.0	..	..	-18.9[d]	11.4	62[e]	26	71.0	28
Azerbaijan	730[e]	7.6	-17.1	4.0[c]	23.0[c]	-7.1[f]	847.9	96[e]	22	72.0	21
Kiribati	730[g]	0.1	2.3	..	..	..	..	..	51	61.0	..
Sri Lanka	720	18.4	5.4	15.9	25.7	-7.8	10.3	90	23	72.0	16
Armenia	660[e]	3.6	-13.0	-19.0[c]	10.0[c]	-23.7[f]	1 579.6	99[e]	15	71.1	18
China	570	1 227.0	11.3	42.3	39.5	-0.9	11.6	81	26	69.3	26
Tajikistan	470[e]	6.1	-16.4	..	..	-17.2[f]	789.9	97[e]	40	66.6	24

(Continued on next page)

Table II.1 *(continued)*

Country/area[a]	*Per capita GDP/GNP (US$) 1995*	*Population (million) 1995*	*Annual average GDP growth rate 1991-1995*	*Savings rate (% of GDP) 1995*	*Investment rate (% of GDP) 1995*	*Budgetary balance/ GDP (%) 1991-1995*	*Average annual inflation rates 1991-1995*	*Adult literacy rate (%) 1995*	*Infant mortality rate (per 1000) 1994*	*Life expectancy at birth (years) 1994*	*Rank in HDI value*[b] *1993*
Pakistan	450	130.7	4.9	15.7	18.7	–7.2	11.3	38	95	60.0	33
Mongolia	380	2.4	–2.6	15.9	24.7	–6.8	127.2	82[e]	58	64.5	27
India	370	935.7	4.8	25.0	26.6	–6.2	10.2	52	84	62.0	34
Lao People's Democratic Republic	360	4.9	6.4	..	..	–4.7[i]	11.1	57	94	52.0	36
Cambodia	290	10.2	5.9	8.3	21.5	–5.3	65.0	35[e]	112	52.0	38
Viet Nam	260	74.5	8.2	19.0	27.1	–3.4	23.5	94	35	64.5	30
Bangladesh	240	120.4	4.3	7.7	16.6	–5.7	4.2	38	83	57.0	35
Myanmar	235[c]	46.5	6.5	12.2	13.0	–2.5	27.1[f]	83	78	58.5	32
Nepal	210	21.9	4.8	10.3	20.2	–5.9	11.2	27	95	54.0	37
Bhutan	170	1.6	5.2	36.0	54.5	–0.5	11.0	42	123	49.5	39

Sources: ESCAP, *1995 ESCAP Population Data Sheet* (Bangkok, 1995); *World Population Prospects: The 1994 Revision* (United Nations publication, Sales No. E.95.XIII.16); United Nations, *Monthly Bulletin of Statistics*, various issues; *World Urbanization Prospects: The 1994 Revision* (United Nations publication, Sales No. E.95.XIII.12); UNDP, *Human Development Report* (New York, Oxford University Press), various issues; World Bank, *Social Indicators of Development 1996* (The Johns Hopkins University Press, 1996); ADB, *Key Indicators of Developing Asian and Pacific Countries 1996* (Oxford University Press, 1996) and *Asian Development Outlook* (Hong Kong, Oxford University Press), various issues; FAO, *FAO Production Yearbook 1994* (Rome, 1995); IMF, tape No. 93023F; IMF, *International Financial Statistics*, vol. XLIX, No. 9, September 1996 (Washington DC, 1996); *World Bank, World Tables 1995* (The Johns Hopkins University Press, 1995) and ECE, *Economic Survey of Europe* (New York and Geneva), various issues.

[a] Listed in order of per capita income levels from the highest to the lowest.
[b] The ranks are based on descending order of human development index (HDI) value estimated in UNDP, *Human Development Report 1996*.
[c] 1994.
[d] 1991-1994.
[e] 1993.
[f] 1992-1995.
[g] 1992.
[h] Most recent estimate between 1989 and 1994.
[i] 1991-1993.
[j] 1990-1995.

The exceptions are the former socialist groups of countries, where high levels of social spending in the past achieved high levels of health and educational standards that would normally be associated with high levels of per capita income. These spending levels, however, became difficult to sustain owing to faltering growth, falling per capita income and budgetary problems.

A vast number, estimated at 731 million as of 1990,[1] of Asia's population remains absolutely poor. Poverty, in terms of both absolute numbers and proportion of the population, remains concentrated either in the more populous countries of the region or in countries which have not been able to achieve high rates of economic growth in the past. Special efforts and sizeable resource commitments continue to be needed in these countries to directly address the issue of poverty alleviational (box II.1). Between 1970 and 1990, the incidence of poverty, both in absolute numbers and the proportion of population, has declined throughout the region.[2] The rates of decline, however, appear to have slowed down since the mid-1980s.

Although absolute poverty has declined rapidly in the fast-growing economies of the region, disparities in the growth of different regions within countries and inequalities in income distribution seem to be appearing as a challenge. For example, the southern coastal belts of China benefited more from the rapid growth of the past two decades and prospered much faster than the rest of the country. The provinces of Guangdong, Zhejiang, Fujian, Shandong, Jiangsu and Xinjiang recorded the fastest rates of economic growth and made the most rapid gains in the country's total GDP and per capita incomes. Guangdong, for example, accounted for 10 per cent of the country's total GDP in 1993 compared with a share of only 2.3 per cent in 1978.[3] Similar situations are also emerging in Indonesia, Malaysia, the Philippines and Viet Nam. At the same time, inequality in personal income distribution has tended to worsen over the years. In Thailand, for example, the gap in the per capita income level between the top and bottom 10 per cent of the population widened from 17 times to 38 times between 1982 and 1992.[4]

The rates of economic growth have been rapid in most economies of East and South-East Asia. Their performance has earned the region the reputation of being the most dynamic in the world. Their rapid growth has been associated with high rates of domestic savings and investment, better fiscal balance, and generally well-managed monetary and exchange rate regimes to ensure domestic and external stability reflected in generally low rates of domestic inflation, smaller savings-investment gaps and competitive exchange rates. These economies are also characterized by high rates of participation in international trade, as indicated by the ratio of imports and exports to GDP. Their economic and social environments have raised their international credit standing to induce very substantial private investment and financial flows. The countries within this group which were lagging behind, such as the Philippines, and even the least developed countries, such as Cambodia and the Lao People's Democratic Republic, have lately improved their performance.

In South and South-West Asia, rates of economic growth have tended to accelerate with the recent implementation of considerable macroeconomic and structural reforms, though no firm trend has yet been established. Further reform and liberalization of policies in various areas are on the agenda of most governments with the objectives, *inter alia*, of promoting domestic savings, investment and exports, ensuring better budgetary balance and containing inflation. High rates of inflation have been a major concern, especially in the Islamic Republic of Iran and Turkey. In India, Pakistan and Sri Lanka, inflation rates remain relatively high despite considerable moderation in recent years.

The structural changes that have taken place in the course of economic growth still leave the

---

1 ESCAP, "Incidence, causes and correlates of poverty in Asia and the Pacific" (E/ESCAP/CPA(2)/1).

2 See ESCAP, *Role of the Informal Service Sector in Urban Poverty Alleviation* (ST/ESCAP/1706).

3 Angang Hu, "Regional disparity in China", Beijing, Chinese Academy of Sciences.

4 Pasuk Phongpaichit, "The Thai economy in the mid-1990s", *Southeast Asian Affairs 1996* (Singapore, Institute of Southeast Asian Studies, 1996).

Box II.1. Coping with poverty in South Asia: increasing the effectiveness of antipoverty programmes

Poverty is a widespread phenomenon in the six South Asian countries of Bangladesh, Bhutan, India, Nepal, Pakistan and Sri Lanka. It is estimated that the number of absolute poor in these countries exceeds 550 million. Reducing poverty in South Asia will require faster economic growth and a further lowering of the rates of population growth, which still exceed 2 per cent annually on average. The governments of these countries have been implementing wide-ranging policy reforms to accelerate economic growth, but they have not been able to rely entirely on the growth process for alleviating poverty, given the magnitude of the problem. It can take a long time for the effects of economic growth to trickle down to the poor. Such delays are socially unacceptable. The governments therefore continue to intervene directly and seek to alleviate poverty by implementing specific and target-oriented poverty alleviation programmes.

Many poverty alleviation programmes oriented towards target groups have been implemented in the past with varying degrees of success. The targeted programmes which are carried out in the South Asian countries can be grouped into three broad categories: (a) programmes providing opportunities for income generation through self-employment, public employment and employment in rural industries; (b) programmes which enhance the capacity of the poor in terms of skills and assets by providing education, training and access to credit; and (c) programmes which provide basic needs such as health care, nutrition, housing and sanitation. Thus, the focus of the programmes has been on capacity-building of the poor to undertake remunerative activities as well as on improving the physical and social conditions in which the poor live.

A substantial amount of government resources are allocated to finance poverty alleviation activities in South Asian countries. The 1996-1997 central government budget of India, for example, provided Rs 64.4 billion ($1.8 billion) for rural employment and poverty alleviation programmes. In the context of increasing resource constraints and the mounting need to reduce the fiscal deficit, enhancing effectiveness in the use of resources is receiving greater attention. Many issues are involved in making the poverty alleviation programmes more effective. These relate to the design, organization, financing and targeting of such programmes.

Most poverty alleviation programmes in the South Asian countries are designed centrally but implemented at the local level by a number of government agencies. Simultaneously, many non-governmental organizations (NGOs) and community-based organizations (CBOs) undertake a wide variety of activities to alleviate poverty in the same localities. Two important issues come up in this context. The first is related to beneficiary participation in the design and implementation of programmes, without which the programmes remain agency-driven and unresponsive to the real needs of the poor. The second concerns the need for proper coordination among the multiple agencies in order to avoid duplication, minimize friction and utilize synergies. In South Asia, the key administrative unit below the national or provincial level is the district. Although a number of official government committees exist at the district level to coordinate developmental activities of the government, none of them focuses exclusively on poverty alleviation programmes. NGos, CBOs or beneficiaries are not usually involved in any of them.

Under a project entitled "SAARC seven sisters: district coordination and improved antipoverty project design" implemented by ESCAP in cooperation with the governments concerned, a mechanism has been set up to address these issues. A forum in one district of each of the participating countries named the Committee of Agents and Beneficiaries of Poverty Alleviation Programmes at District Level (CABPAD) has been established. It comprises representatives of all agencies, including NGOs and CBOs, implementing poverty alleviation programmes and of the beneficiaries, particularly women beneficiaries. It functions with the chief of the district administration as the focal point. It organizes frequent meetings to monitor progress in the implementation of programmes, facilitate the flow of information among the agencies and the beneficiaries, avoid overlaps and strengthen complementarities. The districts were nominated by governments on the basis of two major criteria: a high incidence of poverty and the existence of several poverty alleviation programmes implemented by government agencies as well as NGOs and CBOs. A subregional forum named the Network of Agents and Beneficiaries of Poverty Alleviation Programmes at District Level (NABPAD) has also been set up. This provides a forum for CABPADs to exchange experience and learn from each other's best practices.

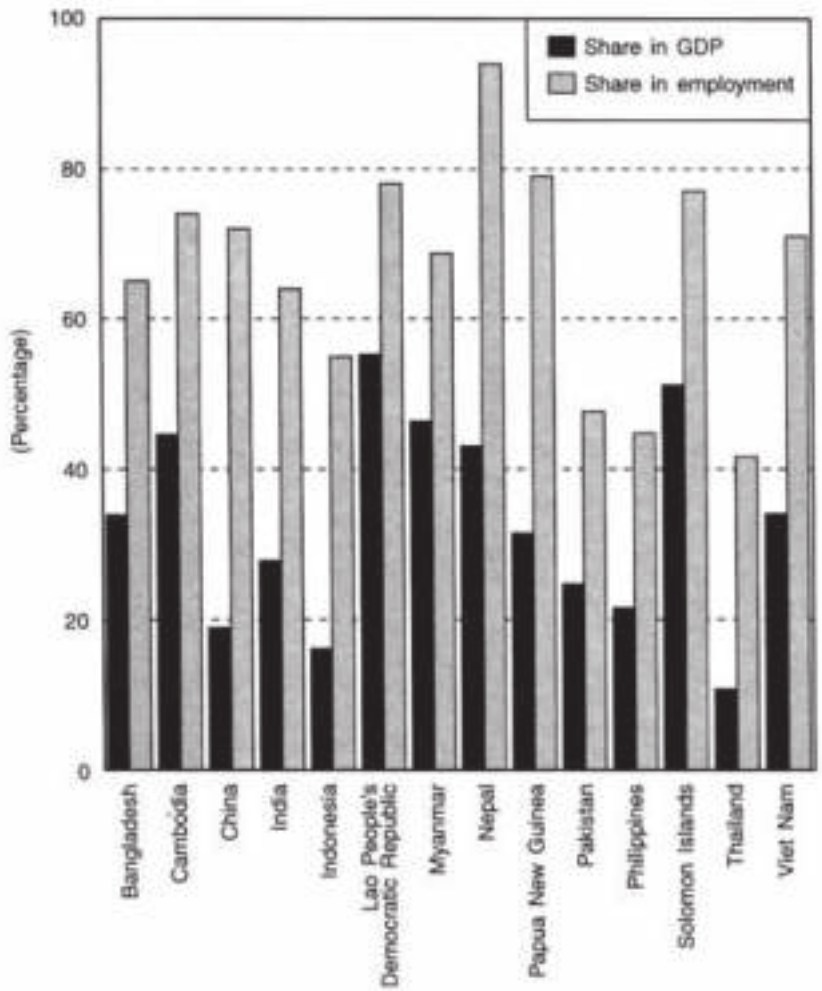
Initial evaluation and field visits suggest that CABPADs in the participating countries have been able to initiate concrete action in fostering coordination among agents and between agents and beneficiaries of poverty alleviation programmes. The participating countries have expressed strong interest in replicating CABPADs in other districts.

The subregional forum, NABPAD, has been found to be extremely useful. It provides a strong motivation to CABPADs to continuously improve their functioning as they are required to report to NABPAD on their activities. It also enhances the visibility of the role of CABPADs to policy makers.

The CABPAD-NABPAD model of increasing beneficiary participation and coordination at local level is found to be viable. It does not involve the creation of any new bureaucracy. It is thus an inexpensive mechanism to enhance the effectiveness of poverty alleviation programmes.

overwhelming proportion of the people dependent on the agricultural sector for employment and for livlihood while the share of the sector in the economy's total income shrank considerably (figure II.1). That tends to accentuate the problem of distributional inequity in many countries. Rates of growth and structural change, with a few exceptions, have remained low in the region's least developed economies and the small island economies of the Pacific. Agriculture remains the most important sector of these economies for both income generation and employment.

Figure II.1. Share of agriculture in output and employment in selected developing countries in the ESCAP region, 1995



Sources: ADB, *Key Indicators of Developing Asian and Pacific Countries 1996* (Oxford University Press, 1996); ILO, *Yearbook of Labour Statistics 1995* (Geneva, 1995); *Statistical Yearbook for Asia and the Pacific 1995* (United Nations publication, Sales No. E/F.96.II.F.1, 1996); World Bank, *Social Indicators of Development 1996* (Baltimore and London, The Johns Hopkins University Press, 1996) and national sources.

Note: Latest available data between the year 1992-1994.

The problems that economies in transition have come to encounter in their move from central planning to market orientation are still daunting despite some recent success in containing inflation and arresting negative growth. These countries have yet to develop effective institutional structures to suit the needs of a well-functioning market economy. During the whole period from 1991 to 1995, all these countries experienced severe contraction of their total and per capita incomes amid hyperinflationary situations. Only during the past couple of years have some of these economies shown signs of positive growth and moderating inflation.

The challenges facing the different groups of countries in the region are thus of very different orders of magnitude, and in some cases, of a somewhat different nature. The countries lagging behind, especially the least developed, the Pacific island and the transition economies, have considerable leeway to make up in order to join the regional mainstream and the global economy. That would require these countries to invest tremendous national efforts, but their success would still depend greatly on special support from the international community.

MACROECONOMIC TRENDS FROM 1980 TO 1995

Growth and structural change

Data on average rates of GDP growth for 1981-1990 and 1991-1995, as well as the shares of the three major sectors (agriculture, industry and services), GDP and the economically active population in 1995 are presented in table II.2 on pp. 32-33. These data form the basis of the subsequent discussion on the growth and structural change experienced by different groups of economies in the region.

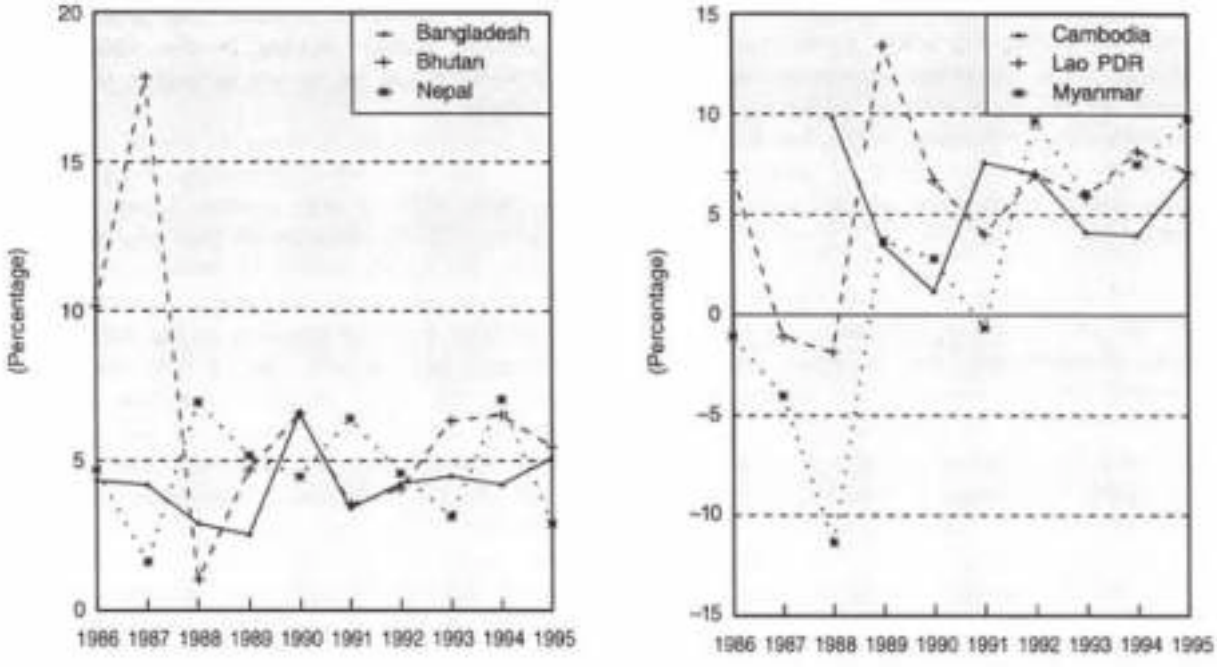
Least developed countries

Six of the 13 least developed countries of the region had per capita incomes below $300 in 1995, and that of the Lao People's Democratic Republic was an estimated $360. The six island least developed countries, including Maldives, had per capita incomes ranging from Kiribati's $730 to Tuvalu's $1,330. For Afghanistan and Cambodia, the 1980s could be regarded as a "lost decade", as both countries were embroiled in military conflicts that could only serve to cause their economic decline with extensive damage to their infrastructures and the production process. Cambodia's economy, however, started reviving in the 1990s whereas Afghanistan has yet to see an end to the damaging conflicts.

The five least developed Pacific countries achieved little, if any, positive growth during the 1980s. Taking into account their population growth rates, per capita income in these countries tended either to fall or to stagnate. Myanmar had experienced a similar situation in the 1980s, with an average GDP growth rate of only 1.4 per cent. Among the other countries, Maldives attained an average annual growth rate of 12 per cent in GDP (the highest), followed by Bhutan with an average rate of 7.4 per cent. Bangladesh and Nepal achieved rather moderate rates of growth, with averages of 4.3 per cent and 4.8 per cent respectively. Population growth rates exceeding 2 per cent left little room for any perceptible rise in per capita income.

In the first half of the 1990s, the growth performance of the least developed Pacific island countries, with the exceptions of Solomon Islands' 5 per cent and Tuvalu's 6.7 per cent average growth rates, remained poor. All of them, however, have shown improvements over the performance of the 1980s. In Kiribati, Samoa and Vanuatu, whose growth rates averaged 2.3, 0.5 and 2.7 per cent respectively, progress was still insufficient. The 5 and 6.7 per cent average rates of growth achieved by Solomon Islands and Tuvalu respectively during the first half of the decade are major improvements over their performance in the 1980s. Among the other countries, Cambodia, the Lao People's Democratic Republic, Maldives and Myanmar recorded rates of growth of 6 per cent or above during the first half of the 1990s. While growth decelerated to 5.2 per cent in Bhutan and 6.5 per cent in Maldives from the higher averages of the 1980s, Bangladesh and Nepal recorded moderate rates of growth above 4 per cent during the same period, as in the 1980s. Recent data indicate that the annual variation in the rates of growth has been much smaller than before and the trend is upward in several of the countries (figure II.2).

Figure II.2. Variation in annual rates of growth of real GDP of selected least developed countries in the ESCAP region, 1986-1995



Sources: ADB, *Key Indicators of Developing Asian and Pacific Countries 1996* (Oxford University Press, 1996) and *Asian Development Outlook 1996 and 1997* (Oxford University Press, 1996) and national sources.

Available information and data for 1995 and 1996 indicate that most of the least developed countries, with the exception of some of the least developed Pacific island countries, have succeeded in accelerating growth rates to 6 per cent or above in 1995-1996 and expect to reach the 7 per cent target rate by the turn of the century. Both Bangladesh and Nepal are estimated to have grown at 6 per cent in 1996. Cambodia, the Lao People's Democratic Republic and Myanmar have shown more dynamism with growth rates, respectively, of 7, 7.1 and 9.8 per cent in 1995. All of them are expecting their growth rates to accelerate further. These three countries are becoming increasingly interlinked with their prospective ASEAN partners, who are providing them with investment, trade and technical support.

Growth has been associated with some degree of change in the structure of the output of these economies. The changes, however, are less visible in the least developed island countries. Industry has made little headway in raising its share of GDP in most of the least developed island countries, and agriculture continues to retain its important role next to that of services in most of them as well. By 1995, however, Maldives had reduced the share of agriculture in GDP to one half that of 1980 while substantially raising the share of services. In relatively large countries, such as Bangladesh and Nepal, the share of agriculture has come down noticeably with corresponding advances in the shares of industry and services. In Cambodia, the Lao People's Democratic Republic and Myanmar, agriculture retains a

share of 45 to 55 per cent of GDP and the share of industry remains below 20 per cent.

A fairly common characteristic of the least developed countries is an overwhelming dependence on agriculture for people's livelihood. The 1995 data suggest that agriculture accounted for the lion's share of the economically active population, ranging from 65 per cent in Bangladesh to 94 per cent in Nepal. That also suggests a continued overcrowding of the agricultural sector and extremely poor living conditions in rural areas, giving rise to pressure for rural-to-urban migration in search of employment and other opportunities. The overwhelming dependence on agriculture also limits the capacity of these countries to participate in international trade or to attract FDI.

Pacific island economies

The 19 Pacific island members and associate members of ESCAP show diverse physical and economic characteristics (five of them are least developed). At one end of the spectrum is Papua New Guinea, with a land area of 462,864 sq km and a rich endowment of agricultural and mineral resources, and a population of over 4.3 million. At the other end is Tuvalu, one of the five Pacific island countries classified as least developed, with a population of only 10,000 and a land area of 26 sq km, most of which is unfertile and unsuitable for agricultural use. In brief, the common problems faced by Pacific island countries are the following: small economies with a narrow range of primary commodity exports but high trade/GDP ratios and therefore high vulnerability to fluctuations in the prices of export commodities; small and fragmented domestic markets; high transport costs in view of the distance from main external markets and inadequate air and sea route connections; and lack of skill, finance and technology. The public sector's dominant role in the economy, supported by high per capita aid receipts, has been the main basis for their past development (box II.2).

Box II.2. Options for the integration of Pacific island countries with the global and regional economies

The special constraints on the economic development of Pacific island countries related to their smallness, their remoteness and so on have been highlighted on numerous occasions. The international community has explicitly recognized the need for differential treatment for these countries through initiatives such as the Barbados Programme of Action for the Sustainable Development of Small Island Developing States and, in the Asian and Pacific context, the establishment of the ESCAP Pacific Operations Centre, the only outpost office of the Commission. During the 1980s, many Pacific island countries achieved a good deal of stability in macroeconomic variables, with manageable inflation rates and budget deficits which were often lower than those attained in other parts of the region. By the early 1990s, while this situation continued in several countries through the concerted efforts of a few multilateral and bilateral donors and national officials, economic management in the subregion was coming under increasing strain.

Several factors, including the rapid liberalization of Asian economies, the declining trend in official aid from the traditional donors and the strengthening drive to liberalize world trade and finance have combined to provide an impetus to expose Pacific island countries to seek greater international with the global and regional economy. Progressive environmental pressures and high population-to-land ratios, along with relatively undiversified economies where import bills are often several times larger than export revenues, severely complicate the task of trying to integrate these islands into the new world economic order. These problems are further compounded by the very limited human resources with the appropriate skills to lead the economic management of these countries in the new environment.

Important changes are taking place at the moment that could facilitate closer integration of the Pacific island countries with the global and regional economies. For example, technical advances in telecommunications now enable Pacific island populations to have instant access to world news and ideas. There is a small but growing number of local private businessmen who are better educated and more widely travelled, and so better

(Continued overleaf)

(Continued from preceding page)

prepared to meet the emerging challenges. Neighbouring Asian countries are actively looking for new sources of minerals, timber and food, and are offering in return a full range of modern consumer goods. At present, Asia, including Japan, takes up to 80 per cent of the exports of individual Pacific islands and accounts for between 15 and 50 per cent of their imports. Asian firms have invested and are operating enterprises in logging, fisheries, agriculture, tourism, banking and property developments in several Pacific island countries. Asia is also the fastest-growing market for tourists to Pacific island countries and Asian governments are providing an increasing share of official aid to these countries.

There are some visible signs of the growing eagerness on the part of Pacific islanders to integrate their economies with the outside world, especially the dynamic Asian economies. This is evident from several relatively recent initiatives, such as the interest in understanding the implications of, if not joining, WTO and APEC, the interest in expanding the functioning of the Melanesian Spearhead Group towards the ASEAN model, the efforts towards revitalization of the South Pacific Forum and the South Pacific Commission as more focused and technically competent organizations of subregional economic cooperation, as well as heightened interest in participating in ESCAP activities that involve exchanges of experience and ideas with mainland Asia.

In addition, several of the islands are in the process of internalizing the policies that are required for a modern market-oriented economy. They are, for example, making efforts to downsize and strengthen their public sector. The aim is to change the role of the public sector from being the main provider of employment, as well as the most important supplier of many goods and services, towards being a facilitator and promoter of private sector activities. They have embraced privatization as a policy goal, although visible progress is rare, partly because there is limited opportunity for the sale of public assets.

Notwithstanding these positive developments, there are strict limits on the possibilities for the integration of the Pacific island economies with the world and regional economies. The need to replicate the very sizeable supervisory and regulatory institutions which lie at the heart of the macroeconomic fundamentals required for integration is constrained by human resource scarcities. The requirements in the area of fiscal policy in terms of the design and implementation of a broad-based tax system which is not based on trade-related taxes of various sorts cannot easily be met in small and undiversified economies. The design of a modern financial system to encourage savings and investment through a diversity of modalities is limited by the exceedingly small number of players which can be accommodated in small economies and make the development of national capital markets infeasible. Thus, to impose the usual set of institutions on these economies seems not to be a desirable option and considerably more thought needs to be put into the most appropriate construct of market institutions for these countries. The option of strengthened subregional economic coordination and cooperation has thus become imperative.

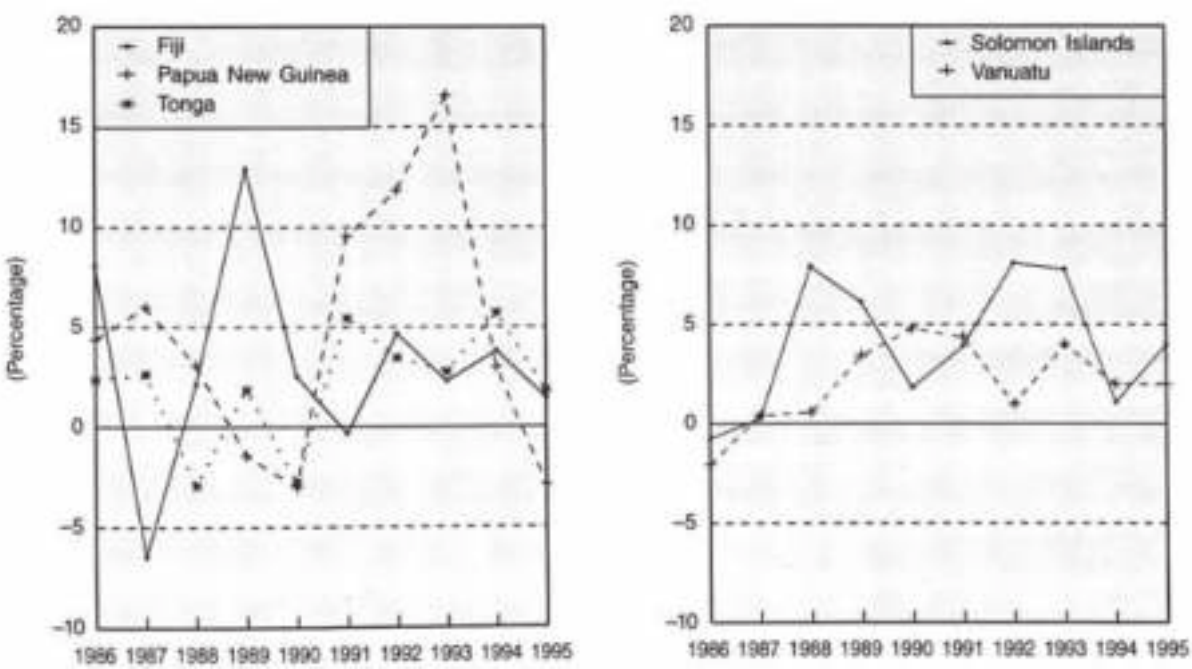
Given the ecological and environmental fragility of these countries and the limited possibility of their attracting much investment in manufacturing especially as preference margins which acted as a *raison d'être* for existing investments are reduced, they will have to assess realistically their options for trade and investment. At present, these seem to lie in the areas of speciality niche agricultural products marketed as environmentally friendly, of exploitation of natural resources such as fish and of timber, and of tourism. The challenge for them will be to ensure that these activities are developed in a sustainable manner, consistent with protecting their environment while at the same time deriving maximum returns for the local economy. Recent multi-country cooperation in the area of fisheries development provides some optimism that this is feasible.

In the final analysis, as Pacific island countries adopt these policies, most, aside from the larger Melanesian countries, will perforce continue to depend heavily on the goodwill of international assistance. It is likely that they will demand and receive special treatment such as concessional loans, some market preferences or guarantees for their products, specified exemptions from the obligations which come with membership of organizations such as WTO, and continued financial assistance. Nevertheless, as Pacific island countries confront the need to compete from a position of absolute disadvantage in a fast-changing, almost barrierless world, they will have to raise the standards of their own economic management. A more vigorous pursuit of technical assistance provided by Asian developing countries under ECDC/TCDC modalities as a means of sharing and learning from the experience of others could assist in this respect. However, while aid and technical assistance are important, a greater readiness on the part of the international community to leave Pacific island countries to work out the parameters of their integration is more likely to produce home-grown, self-reliant solutions to problems with a lasting impact on their economies.

Rates of economic growth during the 1980s and 1990s, despite some improvements during the first half of the latter, have been low. Given the high population growth rates, most Pacific island countries have experienced static or declining living standards. Growth has not only been slow but erratic and uneven. Papua New Guinea, Solomon Islands and Tuvalu experienced an acceleration in growth rates in the first half of the 1990s, averaging 7.6 per cent in Papua New Guinea, 5 per cent in Solomon Islands and 6.7 per cent in Tuvalu. Others have achieved rates of growth averaging 2 to 3 per cent, generally an improvement over the average rates achieved during the 1980s. The average growth rate in the Cook Islands declined sharply, however, from 5.8 per cent in the 1980s to 1.7 per cent in 1991-1995. Samoa, one of the five least developed countries among Pacific island countries, showed positive rates of economic growth in 1995 and 1996 after years of decline largely caused by a number of devastating cyclones. The recovery was due to a revival of exports of coconut products and expansion in the tourism sector. Papua New Guinea, on the other hand, experienced an output contraction in 1995 owing mainly to a drop in mining output, a sharp reversal of rapid growth averaging 10 per cent in 1991-1994. Growth of less than 2 per cent is estimated for 1996.

Several factors contributed to the stop-and-go pattern of the economic growth of the Pacific island countries during the 1980s and early 1990s (figure II.3). Since the Pacific island countries are dependent on a few agricultural products for exports, the collapse of commodity prices along with the steep increases in oil prices and real interest rates in the early and mid-1980s adversely affected their performance. Their problems were further compounded by their high vulnerability to natural disasters, especially droughts, tropical cyclones and volcanic

Figure II.3. Variation in annual rates of growth of real GDP of selected Pacific island economies, 1986-1995



Sources: ADB, *Key Indicators of Developing Asian and Pacific Countries 1996* (Oxford University Press, 1996) and *Asian Development Outlook 1996 and 1997* (Oxford University Press, 1996) and national sources.

Table II.2. Growth and structure of real GDP for selected economies in the ESCAP region

(Percentage)

Country/area	Average annual growth rate of real GDP		Sectoral share of gross domestic product						Sectoral share of economically active population		
			Agriculture		Industry		Services		Agriculture	Industry	Services
	1981-1990	1991-1995	1980	1995	1980	1995	1980	1995	1995	1995	1995
Least developed countries											
Bangladesh[a]	4.3	4.3	43.9	33.8	15.6	20.2	40.5	46.0	65.0	16.0	19.0
Bhutan	7.4	5.2	56.7	38.4	12.2	28.9	31.1	32.7	..	..	..
Cambodia[a]	4.8[b]	5.9	..	44.5	..	18.7	..	36.7	74.0	8.0	18.0
Lao People's Democratic Republic[a]	5.7[c]	6.4	..	55.2	..	18.5	..	26.3	78.0	6.0	16.0
Maldives	12.1	6.5	40.8[d]	19.7	15.4[d]	17.3	43.8[d]	63.1	..	..	..
Myanmar	1.4	6.5	47.9	46.3	12.3	15.5	39.8	38.2	68.7[e]	9.8[e]	21.5[e]
Nepal[a]	4.8	4.8	58.8	43.0	41.2[f]	19.8	..	37.2	94.0	0.0	6.0
Pacific island countries											
Cook Islands	5.8	1.7	24.8[g]	13.7	5.5[g]	7.6	69.7[g]	78.7	..	..	..
Fiji[a]	1.2	2.4	22.5	20.4	21.7	18.5	55.8	61.1	46.0	15.0	39.0
Kiribati	0.3[h]	2.3	25.3[g]	29.1[i]	9.1[g]	8.5[i]	65.6[g]	62.4[i]	..	..	..
Papua New Guinea[a]	1.4	7.6	33.0	31.4	27.0	36.2	40.0	32.4	79.0	7.0	14.0
Samoa	..	0.5	..	..	..	..	..	..	..	..	..
Solomon Islands[a]	3.7	5.0	52.5	51.1[i]	10.0	4.7[i]	37.5	44.2[i]	77.0	7.0	16.0
Tonga	1.5	3.8	42.2	38.9	13.7	12.1	44.1	49.0	..	..	..
Tuvalu	..	6.7	..	..	..	..	..	..	..	..	..
Vanuatu	1.1[j]	2.7	26.1[k]	21.5[j]	7.6[k]	13.9[j]	66.3[k]	64.6[j]	..	..	..
North and Central Asia[mno]											
Armenia	3.3	–13.0	15.9	51.6[j]	70.5	27.0[j]	13.7	21.4[j]	34.2	29.3	36.5
Azerbaijan	2.1	–17.1	28.0	28.5[j]	53.9	33.7[j]	18.1	37.8[j]	33.5	21.7	44.8
Kazakstan	1.5	–14.4	25.9	11.5[j]	47.4	38.7[j]	26.6	49.8[j]	20.5	24.6	54.9
Kyrgyzstan	4.2	–12.0	30.4	44.8	48.1	23.3	21.5	31.9	39.6	19.2	41.2
Tajikistan	2.9	–16.4	34.5	..	45.8	..	19.7	..	53.7	16.0	30.3
Turkmenistan	3.6	–9.9	34.3	..	42.9	..	22.9	..	42.9	20.0	37.1
Uzbekistan	3.4	–3.7	34.1	30.8[j]	44.5	34.6[j]	21.4	34.6[j]	43.5	19.9	36.6
Russian Federation	1.9	–10.5	9.9	7.9	66.4	37.3	23.7	54.7	14.8	35.3	49.9
South and South-West Asia											
India[a]	5.7	4.8	38.1	27.8	25.9	30.7	36.0	41.5	64.0	16.0	20.0
Iran (Islamic Republic of)[a]	..	5.8	..	27.3	..	41.5	..	31.2	39.0	23.0	38.0
Pakistan	6.1	4.9	30.6	24.7	25.5	26.5	43.9	48.9	47.6	15.9	31.7
Sri Lanka	4.3	5.4	26.5	19.8	27.4	31.3	46.1	48.9	34.6[e]	20.5[e]	44.9[e]
Turkey[a]	5.2	3.4	25.1	15.0	28.4	34.3	46.5	50.7	53.0	18.0	29.0
South-East Asia											
Brunei Darussalam	–1.4	1.5	0.8	1.6[e]	81.3	56.5[e]	17.9	41.9[e]	2.0[p]	24.1[p]	73.8[p]
Indonesia	5.7	7.8	30.7	16.1	31.0	41.9	38.4	42.0	54.9[i]	14.1[i]	31.1[i]
Malaysia	6.0	8.6	22.9	13.5	35.8	47.4	41.3	39.1	18.0	35.6	46.3
Philippines	1.8	2.2	23.5	21.5	40.5	35.5	36.0	43.0	44.7[e]	15.8[e]	39.5[e]
Singapore	7.4	8.5	1.1	0.2	38.8	36.9	60.0	62.9	0.3	32.7	67.0
Thailand	7.9	8.5	20.2	10.8	30.1	42.4	49.7	46.8	41.6[e]	23.7[e]	34.7[e]
Viet Nam	7.1	8.2	42.1[g]	34.0	24.1[g]	27.7	33.8[g]	38.2	71.0[a]	14.0[a]	15.0[a]

(Continued on next page)

Table II.2 *(continued)*

(Percentage)

Country/area	Average annual growth rate of real GDP		Sectoral share of gross domestic product						Sectoral share of economically active population		
			Agriculture		Industry		Services		Agriculture	Industry	Services
	1981-1990	1991-1995	1980	1995	1980	1995	1980	1995	1995	1995	1995
East and North-East Asia											
China	10.4	11.3	25.6	18.9	51.5	53.0	22.9	28.1	72.0[a]	15.0[a]	13.0[a]
Hong Kong	6.6	5.5	..	..	..	..	..	..	0.6[e]	28.0[e]	71.4[e]
Mongolia	5.4	–2.6	33.0	34.5	33.6	35.0	33.4	30.5	32.0[a]	23.0[a]	45.0[a]
Republic of Korea	9.2	7.5	14.2	6.5	37.8	44.2	48.1	49.3	12.5	32.9	54.7
Taiwan Province of China	8.0	6.6	7.3	3.0	45.3	38.9	47.4	58.2	13.3	49.0	37.7
Developed countries											
Australia	3.2	2.6	4.4	3.2	36.7	29.2	59.0	67.6	5.1[e]	24.2[e]	70.7[e]
Japan	4.0	1.3	3.4	2.2[j]	40.2	42.9[j]	56.4	54.9[j]	5.8[e]	34.0[e]	59.7[e]
New Zealand	2.3	1.7	8.4	7.7	31.4	32.4	60.3	59.9	9.7	25.5	64.8

Sources: Calculated on the basis of data from ADB, *Asian Development Outlook 1996 and 1997* (Hong Kong, Oxford University Press, 1996) and *Key Indicators of Developing Asian and Pacific Countries 1996* (Oxford University Press, 1996); IMF, *International Financial Statistics Yearbook 1995* (Washington DC, 1995) and *International Financial Statistics*, No. 9 (Washington DC, September 1996); World Bank, *Social Indicators of Development 1996* (Baltimore and London, The Johns Hopkins University Press, 1996); ILO, *Yearbook of Labour Statistics 1995* (Geneva, 1995); ECE, *Economic Survey of Europe in 1994-1995* (United Nations publication, Sales No. E.95.II.E.1) and *Economic Survey of Europe in 1995-1996* (United Nations publication, Sales No. E.96.II.E.1) and World Bank, *World Development Report 1996* (Washington DC, Oxford University Press, 1996); and Interstate Statistical Committee of the Commonwealth of Independent States (Moscow), *Commonwealth of Independent States 1996: Statistical Portrait*; World Bank, *Statistical Handbook 1993, The Countries of the Former Soviet Union* (Washington DC, 1993); United Nations, *Statistical Yearbook for Asia and the Pacific 1995* (United Nations publication, Sales No. E/F.96.II.F.1); The Economist Intelligence Unit (London), *Country Report: Kyrgyz Republic, Tajikistan, Turkmenistan, Uzbekistan*, 4th quarter 1996 and national sources.

Note: Economically active population excluding unemployed labour.

[a] Labour force based on average of 1989-1994.
[b] 1988-1990.
[c] 1982-1990.
[d] 1981.
[e] 1994.
[f] Including services.
[g] 1982.
[h] 1983-1990.
[i] 1992.
[j] 1984-1990.
[k] 1983.
[l] 1993.
[m] Average annual growth rate of real GDP for period 1981-1990 refers to the period 1980-1990.
[n] Sectoral share of GDP refers to sectoral share of national income.
[o] Economically active population refers to civil employment.
[p] 1991.

eruptions in Papua New Guinea. Given the small size of these economies, a single event of that nature may endanger sizeable segments of the population, create critical food shortages, destroy the infrastructure and damage export crops which may take years to replace because of the largely perennial nature of the crops. The 1980s witnessed one or more severe cyclones which passed through Fiji, Solomon Islands, Tonga and Vanuatu, among other Pacific island countries. Apart from causing loss of life, several of them wiped out significant portions of the countries' housing stock, infrastructures, subsistence and export crops, and livestock. Direct losses were equivalent to several percentage points of GDP (Tonga in 1982; Fiji in 1980, 1983 and 1985; and Solomon Islands in 1986), up to nine tenths in that of Solomon Islands in 1987. The construction and rehabilitation, which took several years to complete, produced an adverse impact on the continued development of the Pacific island countries.

Inappropriate domestic policies, such as overregulation of the labour market and the commercial and financial sectors, the public sector's dominant role in trade and production and overvaluation of the exchange rates are also blamed for the sluggish economic performance of the Pacific island countries. Many of them have come to realize this and have undertaken economic reforms in recent years. In many cases, reforms have been spurred by factors such as severe aid cuts, spiralling government debts, serious budgetary and balance-of-payments deficits, or critical shortages of foreign exchange.

The reform measures implemented by these countries included a sharp contraction in domestic spending through tightened fiscal and monetary policies, and exchange rate devaluations. At the same time, selective deregulation and promotion of private investment and production were pursued through a variety of supportive policy measures.

Available data indicate that the economies of the Pacific island countries have experienced very little change in their output composition and employment patterns. The services sector continued to be dominant in many Pacific island countries in 1995, ranging from a low of 32 per cent of GDP in Papua New Guinea to a high of over 79 per cent in the Cook Islands. The agricultural sector is also a major contributor to GDP in most Pacific island economies, with its share ranging from a low of 13.7 per cent in the Cook Islands to over 51 per cent in Solomon Islands. The industrial sector, except for Papua New Guinea, where it accounts for over a third of GDP, contributed less than one fifth of GDP, reflecting the minor role of the manufacturing sector, which accounted for only 4.7 per cent of GDP in Solomon Islands in 1992.

The pattern observed in the first half of the 1990s represents very little change from the 1980s. In the Cook Islands, Fiji, Solomon Islands and Tonga, the share of services has shown moderate increases, while in others it has shown a decline. Agriculture retained its importance except in the Cook Islands, where it lost substantially to services. In Papua New Guinea, Fiji, the Cook Islands and Vanuatu, the share of industry showed some advance. Within each sector a single activity dominates, such as tourism in the services sector. Agriculture remains largely undiversified except in a few cases, such as Papua New Guinea. In terms of the sectoral share of employment, data are extremely inadequate, but agriculture seems to employ the bulk of the labour force, followed by services. Fiji is the only country to have a more balanced distribution of the labour force among agriculture, industry and services.

North and Central Asia

At the beginning of the 1990s, seven Central Asian republics and the Russian Federation abandoned central planning in favour of market-oriented economic systems. Since then, they have had to cope with formidable challenges to carry out the necessary reforms and restructuring in order to embark on a new development path. Following the disintegration of the former Soviet Union, production systems and trading links of these countries suffered severe disruptions. In consequence, they have experienced a drastic decline in output accompanied by hyperinflation, high levels of unemployment, reduced social security provisions, and widening income and wealth differences in society.

During the first half of the 1990s, the GDPs of the Central Asian republics and the Russian Federation declined by more than half their 1989 levels, while prices rose by a factor of 1500-2000. During the period 1991-1995, these countries experienced an average annual decline in GDP ranging from 10 per cent in Turkmenistan and the Russian Federation to 17 per cent in Azerbaijan. Uzbekistan experienced the lowest rate of decline, with an annual average of 3.7 per cent.

With the exception of Tajikistan, the countries appear to have ended the worst part of the recession, with some growing positively by 1995-1996. The first sign of economic recovery was recorded in Armenia in 1995, when the country registered a GDP growth of more than 5 per cent. By the first half of 1996, the recession had come to an end in Kyrgyzstan and Uzbekistan as well with real GDP growth of 0.3 and 1.4 per cent respectively, compared with the same period in 1995. The 1996 annual growth in Kyrgyzstan could reach as high as 3.4 per cent. Positive shifts in economic performance in some of the other countries in the first half of 1996 were also noticeable. Tajikistan, where output had again contracted by more than 20 per cent, remained an exception.

Recovery in output, where it occurred, came mainly from the industrial sector. Gross industrial output grew strongly in Kyrgyzstan, Turkmenistan and Uzbekistan in the first six months of 1996. On the other hand Azerbaijan, the Russian Federation and Tajikistan experienced further declines. In 1996, industrial production and real GDP in the Russian Federation fell by 5 and 6 per cent respectively compared with 1995. Positive GDP growth is projected only for 1998.

Available data on the sectoral composition of GDP showed radical changes taking place in all sectors. Industry and construction have experienced a sharp fall in their contribution to GDP since 1991. The share of agriculture in GDP has risen, especially in Armenia and Kyrgyzstan, partly reflecting the decline of the industrial sector. Kazakstan, on the other hand, experienced a sharp fall in the agricultural share of GDP. The agricultural share in GDP showed a more moderate decline in other countries. The services sector has been the fastest-expanding sector in all the countries. Services accounted for approximately 55 per cent of GDP in the Russian Federation, almost 50 per cent in Kazakstan and more than 30 per cent in other Central Asian countries in 1995. The banking and financial sectors underwent a deep institutional and functional reform, and their weight in the economy grew considerably. In addition, private sector activities appeared in many areas of services and recorded the fastest growth.

Changes in the sectoral shares of GDP resulted in changing employment patterns. The changes in the share of the main sectors in total employment were similar for all the countries: a significant decline in industry and agriculture and an increase in the services sector. The countries have experienced a sharp decline in total employment and high rates of underemployment, reflecting the continued decline in industrial and agricultural production as well as the impact of restructuring. The cumulative fall in employment over the period 1991-1994 varied from 4.2 per cent in Tajikistan to 11.9 per cent in Kazakstan. Open unemployment has become more common in all the countries. The number of unemployed persons increased by 30 per cent in Armenia, doubled in Uzbekistan and more than tripled in Kazakstan and Kyrgyzstan between 1993 and 1995.

South and South-West Asia

The Islamic Republic of Iran and Turkey belong to the lower middle-income group of developing countries along with a number of economies in East and South-East Asia. The Iranian economy suffered a setback in the 1980s as a result of a war with Iraq. However, the Islamic Republic of Iran resumed its reconstruction and development following the end of the war in 1988 and has made substantial progress since then, with an average GDP growth rate of 5.8 per cent during the period 1991-1995. The economy, however, still has the basic problem of excessive dependence on the production and sale of oil and oil products. The economy of Turkey had grown at a rate of 5.2 per cent annual average during 1981-1990, but the rate of growth decelerated to an average of 3.4 per cent during the first half of the 1990s. The economy ran into a severe crisis in 1994, when real GNP contracted by more than 6 per cent and inflation reached an annual rate of 125 per cent. In 1995, with a number of stabilization measures in place, the economy recovered and recorded a GNP growth rate of more than 8 per cent, but inflation remained at an annual rate of about 80 per cent.

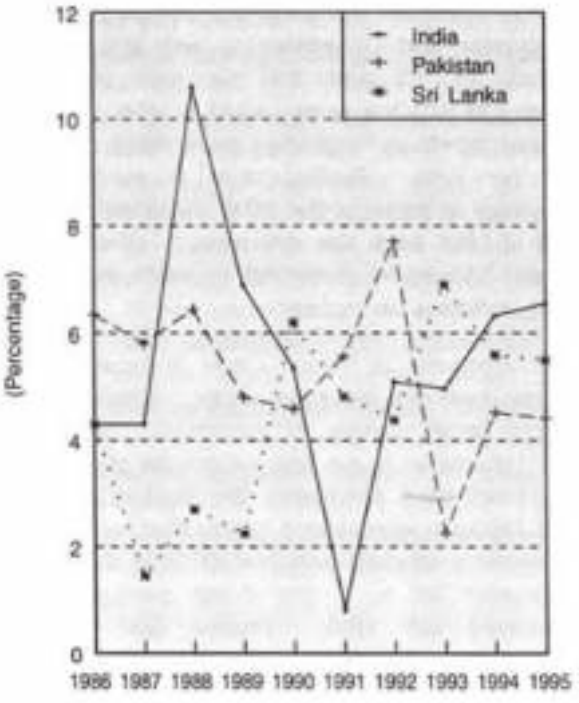
In terms of production and employment structure, the Iranian economy seems to be better balanced sectorally than the economies of many other developing countries in the region with comparable population size and level of development. The agricultural sector accounted for 27 per cent of GDP and 39 per cent of the economically active population. As in other developing countries with similar levels of per capita income and population size, the

agricultural sector's share of employment in the Iranian economy is still relatively high but not disproportionate to its share in income. The services sector seems to be less developed as its share in both income generation and employment is much lower than in countries with levels of development similar to those of the Islamic Republic of Iran. The Turkish economy, on the other hand, displays a typical imbalance between the sectoral share of income and employment, as do many other countries with similar population size and level of development. Thus, in 1995, the agricultural sector generated only 15 per cent of income while retaining 53 per cent of the economically active population. On the other hand, industry and services, with income shares of 34 and 51 per cent respectively, accommodated only 18 and 29 per cent of the economically active population.

Four of the seven member countries of SAARC and Afghanistan are designated as least developed countries. The other three countries, India, Pakistan and Sri Lanka, have made modest advances during the 1980s and the 1990s. The Indian economy grew at an average annual rate of 5.7 per cent from 1981 to 1990, breaking its earlier trend of around 3.5 per cent per year. Generally favourable conditions for agricultural production, including advances in green-revolution technology, permitted the growth rate of the economy to accelerate. The economy faced a severe balance-of-payments crisis in 1991 which had to be resolved by drastic cutbacks in domestic expenditures and restrictions on imports. As a result, the economy's growth rate slumped to a mere 0.8 per cent in 1991 (figure II.4). After the initial moves for short-term stabilization, policies concentrated on liberalizing trade, investment and foreign exchange regimes and introducing fiscal and financial reforms. In 1992, the economy resumed its growth momentum, which gradually accelerated and exceeded 6 per cent in 1995-1996. The reduction of fiscal deficits has remained an elusive goal of Indian economic policy.

Pakistan had the best record of economic growth in South Asia, with an average of 6.1 per cent per year in 1981-1990. That rate, however, decelerated to an average of 4.9 per cent in 1991-1995. Sri Lanka, on the other hand, succeeded in raising its average economic growth rate from 4.3 per cent in 1981-1990 to 5.4 per cent in 1991-1995. As is the case with India, fiscal deficits are still high.

Figure II.4. Variation in annual rates of growth of real GDP of selected South Asian economies, 1986-1995



Sources: ADB, *Key Indicators of Developing Asian and Pacific Countries 1996* (Oxford University Press, 1996) and *Asian Development Outlook 1996 and 1997* (Oxford University Press, 1996) and national sources.

This partly explains the similar rates of double-digit inflation in all three countries.

As in other developing countries, a structural shift in all three South Asian economies has taken place, especially in respect of the share of GDP produced in agriculture. The following figures indicate the shift in the share of the agricultural, industrial and services sectors in GDP from 1980 to 1995: the agricultural share in GDP fell from 38 to 28 per cent in India, from 31 to 25 per cent in Pakistan and from just above 26 to 20 per cent in Sri Lanka. The share of the industrial sector in GDP rose from 26 to 31 per cent in India, from just above 25 to 26 per cent in Pakistan, and from 27 to 31 per cent in Sri Lanka. The share of

services in GDP rose from 36 to 41 in India, from 44 to 49 per cent in Pakistan and from 46 to 49 per cent in Sri Lanka. In both India and Pakistan, however, the share of the economically active population in agriculture, estimated at 64 and about 48 per cent respectively, was disproportionately large.

The industrial sector in both India and Pakistan employed about 16 per cent of the labour force, while the services sector employed 20 per cent in India and about 32 per cent in Pakistan. In that respect, Sri Lanka had a better distributional balance between the income and population share of the three sectors, with agriculture employing about 35 per cent of the economically active population, industry about 21 per cent and services about 45 per cent.

These features indicate that the outcome of past development strategies has not met the expectations of these countries, which had emphasized import-substituting industrialization as a source of rapid growth. There is renewed emphasis on export-oriented, labour-intensive industrialization, complemented by a greater openness towards foreign investment. The development of the service industries, which were relatively neglected in the past, is also being emphasized. Inadequate progress in the structural transformation of the two large economies of India and Pakistan may be partially attributed to past efforts to subsidize agricultural production and to sustain huge populations through subsidized food and other essentials. The two countries have been implementing reform measures which include the reducion of subsidies and budgetary deficits, liberalization of trade and investment regimes, promotion of and support for both domestic and foreign private sector investment, and liberalization and deregulation of financial and foreign exchange regimes.

South-East Asia

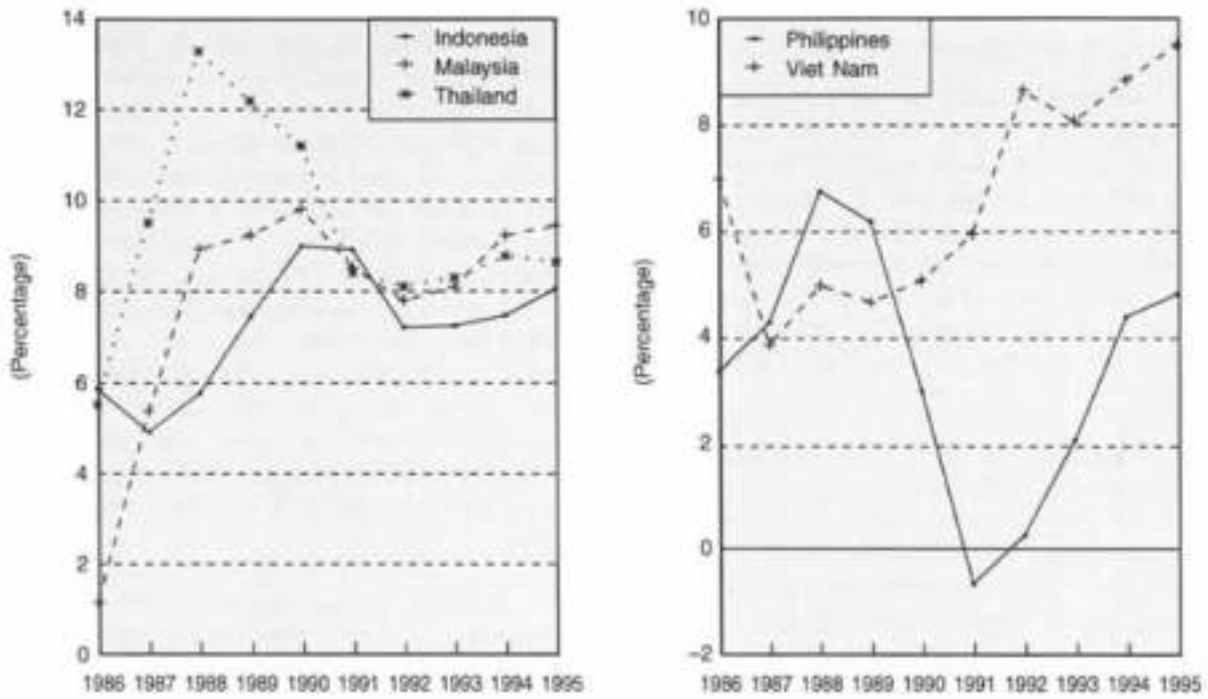
The 10 South-East Asian countries, including the three Indo-Chinese countries, and Myanmar, have been moving towards greater economic cohesiveness. This process will be consolidated with the expected inclusion of Cambodia, the Lao People's Democratic Republic and Myanmar as ASEAN members in the near future. Most of these economies have displayed considerable dynamism in recent years.

Viet Nam achieved an average rate of economic growth of 7 per cent in 1981-1990 and above 8 per cent during the period 1991-1995 with the help of radical economic reforms and policy changes launched in the late 1970s and accelerated since 1986. Among the other six members of the ASEAN group, with the exceptions of Brunei Darussalam and the Philippines, annual economic growth rates have been some of the highest in the region (figure II.5). Four of them, Indonesia, Malaysia, Singapore and Thailand, achieved average growth rates of 8 per cent or above per year during the period 1991-1995. The average growth rate of the Philippine economy remained at 2.2 per cent per year during the same period, reflecting the economy's poor performance in 1991-1993. Since 1995, the growth rate has been above 5 per cent and it is expected to accelerate further throughout the 1990s. The small economy of Brunei Darussalam, with its dependence on the production and export of oil, has also grown slowly with the decline in oil prices since the mid-1980s.

In terms of the structure of production, the economies of Brunei Darussalam and Singapore have virtually no agricultural activity, the share of the sector in GDP being less than 2 per cent. The production structure of these two economies is dominated by industry and services. In both of these economies, the share of services in GDP has been increasing, currently accounting for 40 per cent of GDP in Brunei Darussalam compared with 18 per cent in 1980, while in Singapore services accounted for 63 per cent of GDP compared with 60 per cent in 1980. In the case of Brunei Darussalam, the rise in the services share of GDP reflects efforts to reduce the economy's excessive dependence on the oil industry. In Singapore, though a diversified industrial structure has contributed more than one third of GDP, the economy is concentrating more on services, since its location, lightly developed infrastructure and skilled manpower are among the country's many advantages in the production and distribution of a variety of services.

Indonesia, Malaysia and Thailand have experienced very rapid change in the structure of their production, with a decline in the share of agriculture in GDP from 31 to 16 per cent in Indonesia, from 23 to 13 per cent in Malaysia, and from 20 to 11 per cent in Thailand. Industry and services have been contributing almost equal shares to non-agricultural

Figure II.5. Variation in annual rates of growth of real GDP of selected South-East Asian economies, 1986-1995



Sources: ADB, *Key Indicators of Developing Asian and Pacific Countries 1996* (Oxford University Press, 1996) and *Asian Development Outlook 1996 and 1997* (Oxford University Press, 1996) and national sources.

GDP, though the share of services is higher in Indonesia and Thailand, whereas that of industry is higher in Malaysia. All three countries have experienced rapid rates of industrial growth since 1980. As a result, the share of industry in GDP has risen while the agricultural sector lost considerable ground in terms of its share of contribution to GDP. The economies of the Philippines and Viet Nam have also shown some changes in the composition of their output, but the changes have not been as marked as in the case of the other three countries.

In respect of the percentage of the labour force engaged in the three sectors of the economy, however, the agricultural sector continues to account for a high share, disproportionate to its contribution to GDP. Thus, in Indonesia, the share of the labour force in agriculture remains at about 55 per cent. In Thailand, the share of the labour force in agriculture declined from 71 per cent in 1980 to about 42 per cent. Employment expanded most importantly in industry and to a lesser extent in services. In Malaysia, the share of the labour force in agriculture declined from about 40 per cent in 1980 to about 20 per cent in 1995. In the Philippines, it declined from about 52 per cent to about 45 per cent. Whereas the expansion in employment occurred in the industrial sector in Malaysia, the change in the employment structure in the Philippines reflected a rise in the share of services in employment. Viet Nam seems to have experienced little change in this respect, with more than 70 per cent of the labour force remaining in the agricultural sector.

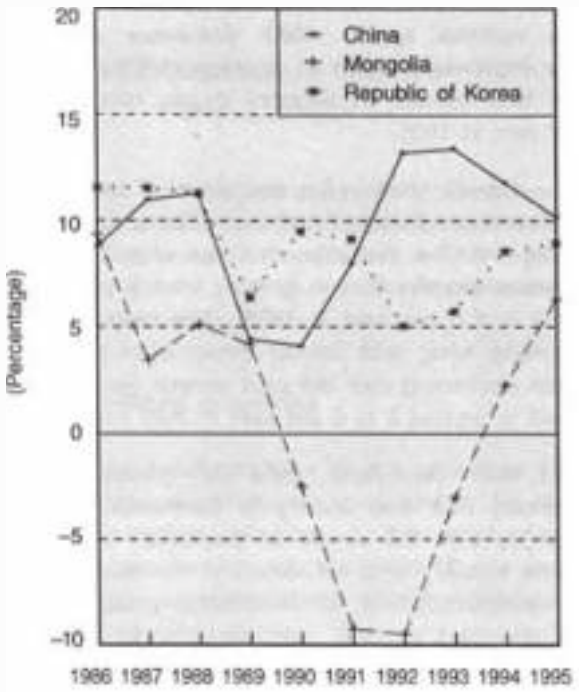
This imbalance between the sectoral share of output and employment of these relatively large and populous countries is a source of continuing concern, as it reflects a rise in the disparity between the income levels of the urban industrial sector and the rural agricultural sector. Concentration of poverty in rural areas serves as an inducement to rural/urban migration in search of more gainful employment in urban areas, which are often ill-prepared to receive such influxes, not only in terms of employment opportunities but also of a wide variety of services, including housing, sanitation, transportation, education and health. A relatively small proportion of the population of these countries is currently urban. In Thailand and Viet Nam, for example, only about 20 per cent of the population lives in urban areas, a further indication of the disparity in living conditions in urban and rural areas and of the potential for a further exodus from rural areas.

East and North-East Asia

Three of the four original newly industrializing economies of Asia (Hong Kong, the Republic of Korea, Singapore and Taiwan Province of China) are in East Asia. In the 1980s, China and the three tiger economies of East Asia Hong Kong, the Republic of Korea and Taiwan Province of China achieved rates of growth in GDP that were among the highest in the world. During that decade, China's economy grew at an average of 10.4 per cent per year, that of the Republic of Korea at a rate of 9.2 per cent and that of Hong Kong at 6.6 per cent. During 1991-1995 these economies grew at average annual rates of 11.3, 7.5 and 5.5 per cent respectively. Growth rates had slowed in China during 1989-1991 owing mainly to domestic constraints. In the Republic of Korea also, rates of economic growth were considerably reduced during 1991-1993 owing mainly to export slowdown occasioned by the recession in the international economy at that time (figure II.6).

In 1996, the growth rate of China's economy is estimated to have decelerated to 9.2 per cent compared with a 10.2 per cent, growth in 1995. The slowdown was due to the impact of tight monetary policies pursued since 1994 with a view to curbing inflation. In addition, agricultural production was disrupted by severe flooding which affected certain parts of the country and caused extensive damage. Industry and services were the main sources of growth.

Figure II.6. Variation in annual rates of growth of real GDP of selected East and North-East Asian economies, 1986-1995



Sources: ADB, *Key Indicators of Developing Asian and Pacific Countries 1996* (Oxford University Press, 1996) and *Asian Development Outlook 1996 and 1997* (Oxford University Press, 1996) and national sources.

During the 1980s, Mongolia's economy had grown at 5.4 per cent, but the economy contracted at an average rate of -2.6 per cent during the period 1991-1995. However, the country succeeded in quickly turning around the declining trend of the early 1990s and has achieved positive rates of growth since 1994; it expects the growth rate to climb further as the restructuring of the economy progresses. The economy continued its recovery in 1996 although the rate of GDP growth fell to 4.5 from 6.3 per cent in 1995. The industrial sector, which contributes 35 per cent of GDP, continued to lead the recovery with production gains in power generation, non-ferrous metals, chemicals, building

materials, timber and textile goods. Agricultural production, particularly in the crop sector, has been adversely affected during the past several years owing to adverse weather conditions, a reduction in the area under cultivation, and government price controls on grain and other cultural commodities which perhaps acted as a disincentive. However, the livestock sector, which dominates agriculture, saw improvement with an increase of 6.5 per cent in the total number of livestock heads, reaching 28.6 per cent in 1995.

Growth rates in the economies of the Republic of Korea and Taiwan Province of China slackened in 1996, with the Republic of Korea experiencing the sharpest deceleration in growth, from 9 per cent in 1995 to 6.6 per cent in 1996. The pace of growth in Hong Kong and Taiwan Province of China has been slackening over the past several years, settling down to around 5 to 6 per cent in both economies.

With the rapid pace of growth, China's economy has also undergone substantial structural change, with the weight of production shifting towards industry and services and the relative share of agriculture falling. In 1995, industry accounted for 53 per cent of GDP, and services 28 per cent, leaving agriculture a share of 19 per cent. Agricultural production increased by an average of 3.9 per cent from 1992 to 1995, which is a considerable rate of growth in agriculture by any standard. However, industry and services grew at average rates of 17.3 and 9.6 per cent respectively during the same period, thus enhancing their share in GDP. As is typical of other populous countries, the largest share of the economically active population in China remains in the agricultural sector (72 per cent) compared with 15 per cent in industry and 13 per cent in services.

The production structure of the Mongolian economy seems to be well-balanced, with agriculture and industry each accounting for 35 per cent of GDP and services contributing the remaining 30 per cent. With recent growth trends, in which industry has been growing at a much faster rate (21 per cent in 1995) than the other sectors, this pattern is likely to change soon. The statistics probably underestimate the growth of the services sector as they do not seem to capture adequately the private sector activities in the services sector, which employs the largest share of the economically active population of the country.

While the economy of Hong Kong has virtually no agriculture and both production and employment are concentrated in industry and services, it appears that the economy has shifted more and more towards service orientation, which now employs more than 70 per cent of the active population. The economy of the Republic of Korea seems to have undergone a very rapid but also a reasonably well-balanced transformation. As of 1995, agriculture contributed 6.5 per cent of the Republic of Korea's GDP, while industry contributed 44.2 per cent and services 49.3 per cent. In 1980, these shares were 14.2, 37.8 and 48.1 per cent respectively. The 1995 figures indicate the continued shift in the weight of production from agriculture to industry and services. The share of the labour force in the three sectors has also shifted in tandem to proportions that seem reasonably balanced with their respective shares in total GDP.

The developed countries

The three developed countries of the region have been growing at slower rates, typically in line with many other developed countries of the world. The average rate of GDP growth between 1981 and 1990 in Japan was, at 4 per cent, the highest of the three, followed by Australia with 3.2 per cent and New Zealand with 2.3 per cent. Average growth rates decelerated sharply during the first half of the 1990s, which largely reflected the impact of the recession that many of the industrial countries experienced until 1993. The economies of Australia and New Zealand came out of the recession strongly with growth rates of 4 to 5 per cent in 1993-1994. In 1995-1996, Australia maintained strong growth at 3.1 per cent in 1995 and an estimated 4 per cent in 1996. In New Zealand, the growth rates in those same years slipped to 2.5 and 2 per cent.

Japan's economy fell into recession in 1992, later than the economies of Australia and New Zealand, and has yet to embark on a firm course of recovery. The annual rate of growth remained below 1 per cent through 1995. For 1996, the GDP growth rate is estimated at 3.7 per cent, which, if confirmed, will finally end the country's economic recession.

The share of industry in GDP exceeds 40 per cent in Japan, and one third or more in Australia

and New Zealand. The agricultural share in GDP is the highest in New Zealand, at about 8 per cent, followed by about 3 per cent in Australia and 2 per cent in Japan. Services contribute 55 per cent in Japan, almost 68 per cent in Australia and 60 per cent in New Zealand.

Apart from the recession that these countries have experienced in recent years, they had their own structural problems which were reflected, *inter alia*, in large budget and balance-of-payments deficits and rising wage pressures and inflation, particularly in Australia and New Zealand during the 1980s. The two countries implemented a series of fiscal, financial and labour market reforms to overcome these problems and have succeeded in substantially reducing budget and balance-of-payments deficits as well as inflation. Inflation rates came down from an average of 8 to 10 per cent in 1981-1990 to an average of 2 to 2.5 per cent in 1991-1995. Japan's structural problem was of a different kind. Until recently, the public budget had remained in surplus, and the unemployment and inflation rates remained the lowest among the industrial countries. However, the country experienced rising trade and balance-of-payments surpluses during the 1980s which spilled over into the domestic economy, raising consumption levels and speculative investments in real property and financial assets. The prices of both the categories of assets rose to unprecedented heights in the late 1980s. The speculative boom ended, however, in the early 1990s, which also coincided with the onset of a recession in a number of other industrialized countries. The subsequent decline in property and stock prices particularly affected banking and financial institutions, many of which became burdened with bad debts and losses. The government has taken a number of steps to stimulate the economy and revive growth. These include several packages of increased public spending, which is reflected currently in a widening budget deficit. Monetary measures included a lowering of interest rates to the lowest level anywhere in the world, and reforms of the financial industry aimed at liquidating existing bad debts and avoiding similar problems in the future.[5]

[5] For more details see *Survey 1996*, pp. 72-77.

With Japan's recovery completed, the three countries may be expected to continue their expansion, as is normal for mature economies. Their expansion will continue to have a significant impact on trade and investment relations between them and the developing economies of the region.

Macroeconomic balance and stability

Data on selected indicators of macroeconomic balance and stability for 1981-1990 and 1991-1995 for the various groups of economies in the region are given in table II.3 on pp. 46-47. The following discussions are based on those data.

Least developed countries

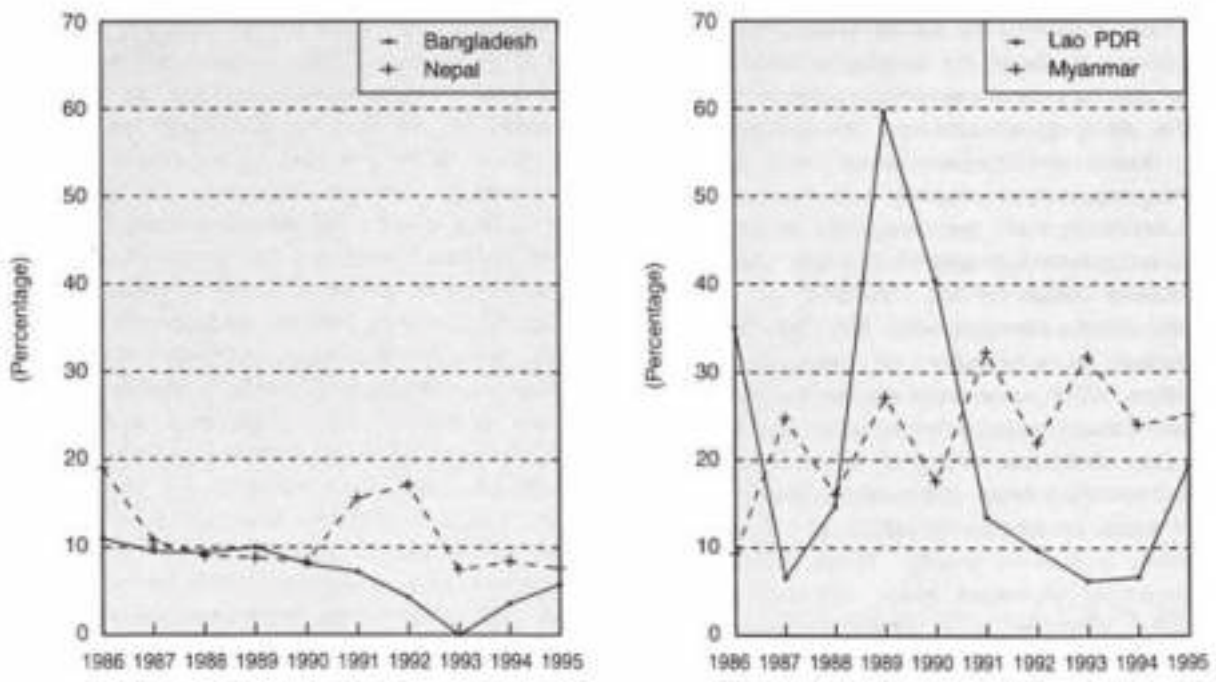
A fundamental constraint on the growth of the least developed countries has continued to be the paucity of investible resources in their economies. Investment rates have hardly exceeded 20 per cent of GDP in any of them. Even with those modest rates of investment, resource shortages frequently exceed 10 per cent of GDP, which means that at least 50 to 60 per cent of investment had to be financed by external resources. In some of the least developed Pacific island countries, the resource gap exceeded even the domestic investment rates, indicating that a part of domestic consumption was also supported by external resource inflows. Where the resource gap was relatively small, as in Myanmar, the rate of domestic investment was much lower, at around 12 to 13 per cent, which could be mostly financed from domestic savings. External resources have come mostly in the form of foreign aid. Resource shortfalls have also been reflected in the budget deficits experienced by most of these countries, with the deficits running typically at 5 to 7 per cent of GDP. Tax-GDP ratios hardly exceeded 10 per cent of GDP, whereas public expenditure has typically exceeded 15 per cent of GDP.

Inflation rates remained relatively high in most of the countries throughout the 1980s and the 1990s. In Cambodia, the Lao People's Democratic Republic and Myanmar, the rate of inflation accelerated considerably during the 1990s as the countries initiated liberal economic reforms to reorient their economies towards market-based systems. The

latest data, however, confirm that these countries succeeded in considerably reducing inflation rates by 1995 or 1996. In Bhutan and Nepal, annual inflation rates averaged about 11 per cent, with indications that the rates were coming down. Bangladesh has been most successful in reducing the average annual inflation rate from about 10 per cent in 1981-1990 to just above 4 per cent in 1991-1995. The most recent trends indicate a tendency for inflation to stabilize at that low level or to come down further (figure II.7). In most of the least developed Pacific island countries, with the exception of Solomon Islands, inflation rates have been reduced to an average as low as 3 to 5 per cent in 1991-1995.

Recent policy initiatives in most countries have emphasized continued price stability along with greater mobilization of domestic resources. Towards that end, monetary and fiscal reforms have been carried out. Tax efforts have been stepped up, and expenditure growth has been restrained to reduce fiscal deficits. Monetary and banking reforms included relaxation of government controls on interest rates and allocations of bank credit. Effective implementation of policies however suffers as a result of institutional shortcomings and inadequate coordination among institutions and agencies for policy formulation and implementation (box II.3).

Figure II.7. Variation in annual rates of inflation in selected least developed countries, 1986-1995



Sources: IMF, *International Financial Statistics Yearbook 1995* (Washington DC, 1995) and *International Financial Statistics* (Washington DC, September 1996); ADB, *Asian Development Outlook* (Oxford University Press), various issues and national sources.

Note: Inflation rates measured by changes in consumer price index.

Box II.3. Institutional aspects of macroeconomic management in least developed economies*

Many domestic and external factors determine the macroeconomic performance of a country. One important domestic factor is the consistency or compatibility of the policy regime. Policy compatibility is a broad notion; it implies consistency among various macroeconomic instruments, such as monetary, fiscal and exchange rate policies, as well as between these policies and sectoral ones. In this regard, institutions matter because an incompatible policy regime is often the result of inadequate institutional capacity. While technical capacity is critical in devising compatible policies, institutional coordination and credibility often greatly affect the outcome.

A sound institutional capacity depends on several factors, among which are human resources, organizational mandates and powers, economic data and information, technical support and coordinating mechanisms among various government bodies (including their semi-independent think-tanks). The least developed countries generally suffer from constraints in all these aspects. Human resources equipped with the relevant technical skills in institutions responsible for advising, formulating and implementing macroeconomic policies are often in short supply. Frequently, there is a lack of communication among various institutions. Various schemes for secondment and in-service training involving government officers, politicians, experts and academics, such as those found in the Republic of Korea and Thailand, for example, could help to improve policy consistency.

It is vital that central banks, ministries of finance and planning bodies have clear mandates and powers as the degree of autonomy that these institutions possess affects their ability to provide professional policy analysis and recommendations to the political authorities responsible for making final decisions. Although there appear to be no major *de jure* difference from one country to another in this respect, in practice the least developed countries compare unfavourably with the other developing countries in the region. For instance, there are ample cases where numerous instances of ad hoc policy interference led to undesirable outcomes. Of course, policy interference always exists in almost any country, but where economic policy institutions have been demonstrably capable of developing a well-articulated and consistent policy stance over time, undue pressures are minimized. In addition, strict policy rules, such as those operating in Indonesia and Thailand to control budget deficits, could be instrumental in moderating such interference.

As is well known, a central bank must have adequate powers of supervision over the financial sector in order to conduct monetary policy effectively. This is not always the case in least developed countries. In Samoa, for example, burgeoning non-bank financial institutions are beyond the central bank's supervisory arm, and the bank's ability to conduct monetary policy has been blunted as domestic credits have continued to expand through these institutions.

Institutional issues are also important for the conduct of an effective fiscal policy. The institutional capacity for determining the tax structure and tax rates and for efficient tax collection are critical for government revenue. The relatively low tax collection rates in Bangladesh, the Lao People's Democratic Republic and Samoa may be partly attributed to inadequate development of these capabilities. On the expenditure side, fiscal overruns are often a result of poor institutional capacity for monitoring and enforcement of control mechanisms.

A mechanism for coordination among economic policy institutions is vital. The intensity and quality of coordination are usually inadequate in least developed countries. The frequency of regular meetings, quality of technical support papers, availability of reliable data, among other things, are all important elements in effective coordination. Little coordination appears to take place in Samoa, where the Macroeconomic Policy Co-ordinating Committee meets only three or four times per year. In the case of Bangladesh, coordination appears to be constrained by the absence of sound analysis of short-term trends and prospects of the economy. Policy coordination has to be attained through lengthy high-level meetings involving various agencies.

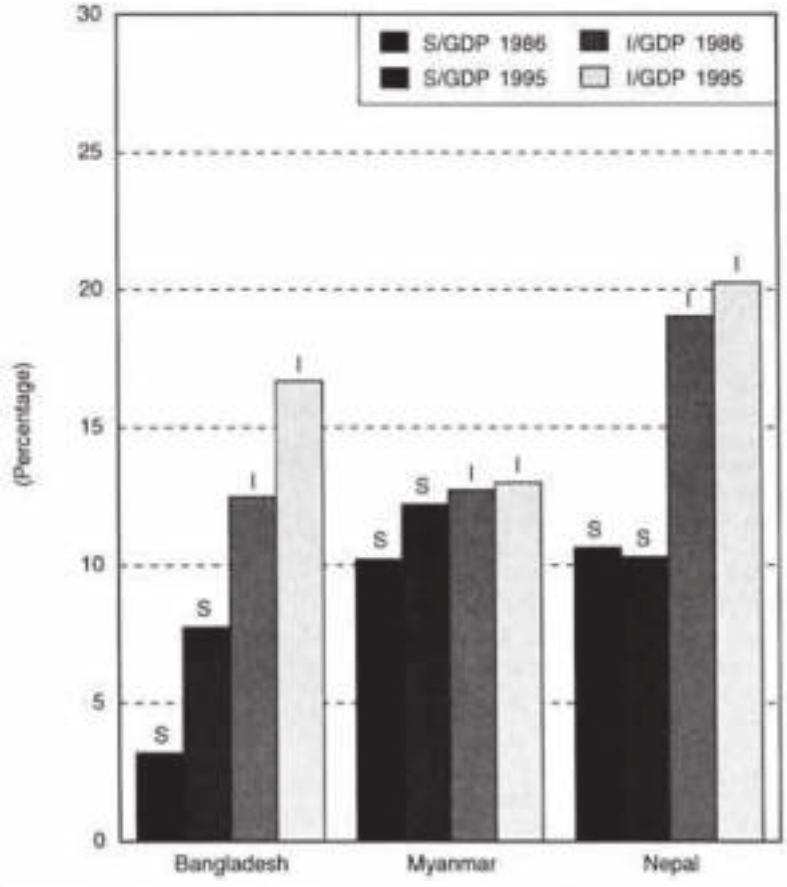
To some extent, the above-mentioned institutional shortcomings of the least developed countries are consequences of their relatively lower stage of development. However, it is also true that a sound institutional capacity needs a conscious development strategy. In both the Republic of Korea and Thailand, there have been various schemes to develop a sound human resource base. Many fellowships and research grants have been offered to the most talented people from relevant institutions for postgraduate studies overseas. Often, this is coupled with the sponsorship of secondment arrangements in outstanding international institutions. In addition, think-tanks have been involved in the secondment schemes and in providing technical assistance and training to government officials and politicians. It is interesting to note that there is growing cooperation between developing countries with respect to institutional development. For example, the Korea Development Institute has recently been active in providing technical assistance to develop the Vietnam Development Institute. More efforts in this direction are urgently needed to assist the least developed countries.

---

* The information in this box is based on document E/ESCAP/SB/LDC(3)/2 and other sources cited therein.

The gap between domestic savings rates and the modest investment rates prevailing in the economy (figure II.8) as well as between the public sector revenue and expenditure remains too wide. Efforts to accelerate domestic savings and investments are being further strengthened. As acceleration of external aid flows is unlikely, most of the countries have actively sought FDI by liberalizing foreign investment laws and regulations, streamlining incentive structures, and improving administrative procedures.

Figure II.8. Savings (S) and investment (I) rates of selected least developed countries, 1986 and 1995



Source: ADB, *Key Indicators of Developing Asian and Pacific Countries 1996* (Oxford University Press, 1996).

Pacific island economies

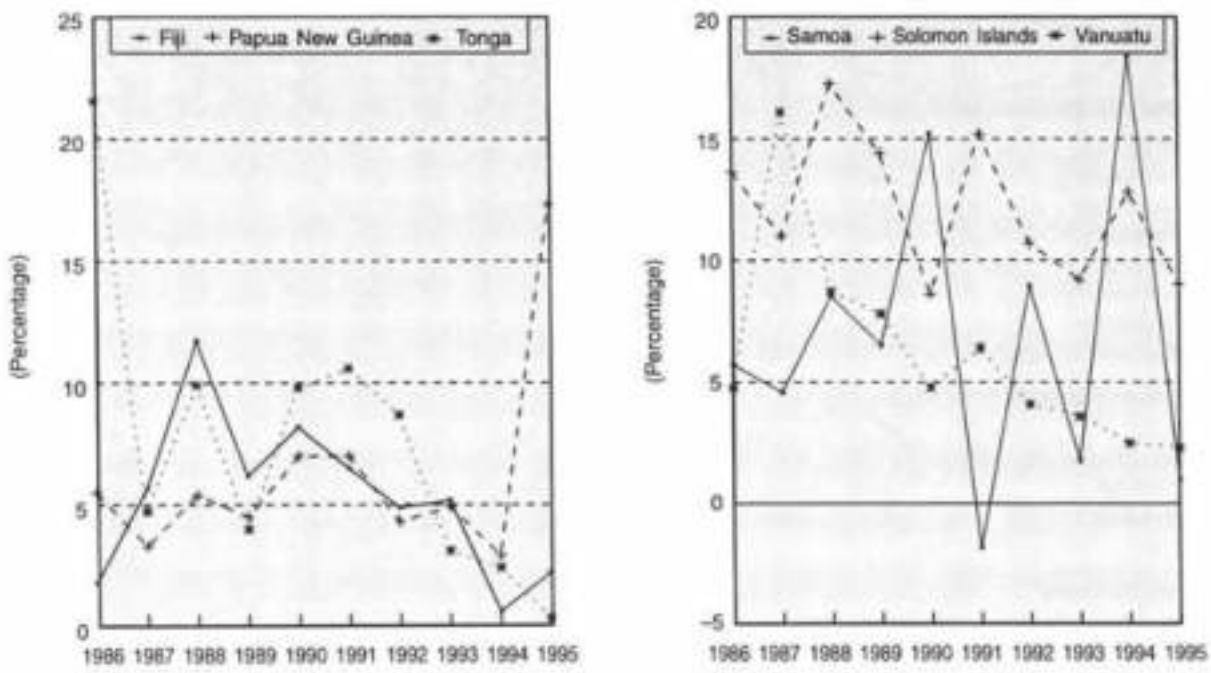
Savings and investment is an area in which Pacific island countries have continually performed poorly. Data in this area are scanty, but indications are that, with few exceptions, domestic savings have been very low or negative. The resource shortfalls have often exceeded 25 per cent of GDP, exceeding domestic investment rates, an indication that external resources have supported at least part of domestic consumption. Tonga and Vanuatu, for example, recorded average annual resource deficits of almost 32 and 27 per cent of GDP during the early 1990s. With the exception of Fiji and Papua New Guinea, the situation has not changed compared with the 1980s. Countries have made up for the shortfalls through inward ODA, private remittances and, in some of the resource-rich countries, such as Papua New Guinea, Solomon Islands and Vanuatu, through FDI.

One of the major factors behind the poor record of economic performance by Pacific island countries has been their inability to mobilize sufficient domestic savings. Along with inadequacies in supportive policies and institutions, paucity of savings has retarded private investment in the economy. In the absence of a vibrant private sector, the state sector had to undertake most of the capital expenditure.

However, the experiences of Pacific island countries show that macroeconomic stability is not sufficient for rapid economic growth. Except for a few countries, such as Samoa, Solomon Islands and Tonga, the Pacific island countries have contained inflation well. Considerable price stability prevailed in most the Pacific island countries during the 1980s and early 1990s. In fact, only in three countries, namely Samoa, Solomon Islands and Tonga, did inflation rates reach double digits in 1981-1990. In the 1990s, Solomon Islands is the only country among the Pacific island countries to record a double digit inflation rate, averaging 11.4 per cent in 1991-1995. Several Pacific island countries, among them the Cook Islands, Fiji, Samoa, Solomon Islands and Vanuatu, recorded improvements in inflation rates in 1991-1995 compared with the period 1981-1990 (figure II.9). One of the contributing factors to the ability to maintain price stability has been the low inflation prevailing in their main trading partners, namely Australia, New Zealand and the United States of America.

With a few exceptions, such as Solomon Islands and Samoa, Pacific island countries kept their budget deficits to below 6 per cent of GDP during the 1980s and the early 1990s. External grants, however, have been a major factor in

Figure II.9. Variation in annual rates of inflation in selected Pacific island economies, 1986-1995



Sources: IMF, *International Financial Statistics Yearbook 1995* (Washington DC, 1995) and *International Financial Statistics* (Washington DC, September 1996); ADB, *Asian Development Outlook 1996 and 1997* (Oxford University Press, 1996) and national sources.

Note: Inflation rates measured by changes in consumer price index.

Table II.3. Macroeconomic indicators of balance and stability for selected economies in the ESCAP region

(Percentage)

Country/area	Resource gap[a]		Budgetary balance/ GDP[b]		Average annual M_2/GDP		Interest rates[c]	Exchange rates[d]	Average annual inflation rates[e]	
	1981-1990	1991-1995	1981-1990	1991-1995	1981-1990	1991-1995	1991-1995	1986-1995	1961-1990	1991-1995
Least developed countries										
Bangladesh	-10.8	-7.2	-6.5	-5.7	27.4	35.1	6.0[f]	-3.30	10.7	4.2
Bhutan	-23.6	-15.0	-5.7	-0.5	18.2	26.6[f]	-2.2	..	9.2	11.0
Cambodia	..	-7.5	-1.6[g]	-5.3	7.6[g]	7.7	..	..	..	65.0
Lao People's Democratic Republic	..	..	-9.3[h]	-4.7[i]	8.1	11.6	4.4	..	42.5	11.1
Maldives	..	..	-5.7	-12.2	39.2	42.7	..	..	6.8	15.2
Myanmar	-3.3	-1.0	0.2	-2.5	30.7	31.9	..	17.68	11.8	27.1
Nepal	-9.8	-9.8	-6.6	-5.9	27.2	33.4	0.1	15.40	10.2	11.2
Pacific island countries										
Cook Islands	..	..	..	..	..	..	..	..	8.8	4.8[f]
Fiji	-1.6	1.6[f]	-5.0	-3.6	39.7	52.9[f]	-0.2	-1.71	6.8	3.9
Papua New Guinea	-9.8	-5.4[j]	-2.7	-3.8	29.9	33.4[f]	0.0	3.16	5.8	7.3
Samoa	..	..	-17.8[k]	-24.7	33.7[k]	43.6	0.6	0.20	11.7	5.7
Solomon Islands	..	..	-12.9	-18.9[f]	30.7	33.9[j]	-1.4	-2.81[l]	12.1	11.4
Tonga	-39.6	-31.8[j]	-2.3	..	27.1	27.5	1.1	2.10	10.9	5.0
Tuvalu	..	..	..	..	..	..	..	..	..	2.6
Vanuatu	-25.1	-26.6[j]	-3.2[m]	-6.0[j]	107.9[k]	116.5[j]	1.3[f]	-2.22[j]	7.2	3.8
North and Central Asia[n o]										
Armenia	8.0	-29.0	..	-23.7	..	..	..	..	..	1 579.6
Azerbaijan	18.0	-19.0	..	-7.1	..	..	..	..	..	847.9
Kazakstan	-13.0	-4.0	..	-2.9	..	..	..	..	..	1 068.3
Kyrgyzstan	-11.0	-16.0	..	-12.4	..	..	..	..	..	545.1
Tajikistan	-6.0	..	..	-17.2	..	..	..	..	..	789.9
Turkmenistan	4.0	..	..	2.4	..	..	..	..	..	1 306.8[f]
Uzbekistan	-5.0	1.0	..	-10.2	..	..	..	..	..	722.8
Russian Federation	0.0	2.0	..	-10.4	..	..	..	..	..	589.9
South and South-West Asia										
India	-21.0	-1.0	-7.6	-6.2	45.9	47.0[f]	0.0[f]	-8.03	9.1	10.2
Iran (Islamic Republic of)	..	..	-6.1	-1.1[f]	..	..	..	..	18.5	29.0
Pakistan	-8.4	-3.3	-6.7	-7.2	41.3	44.3	-0.4	-3.34	7.3	11.3
Sri Lanka	-12.2	-10.1	-10.4	-7.8	31.2	32.3	4.6	-0.23	12.4	10.3
Turkey	..	..	-4.1[m]	-5.1[f]	26.0	29.2	-8.4	..	46.5	80.4
South-East Asia										
Brunei Darussalam	..	..	..	..	54.6[k]	85.5[f]	..	..	3.0	2.4[f]
Indonesia	1.7	1.2	-3.0	-0.3	25.2	44.4	13.5[j]	-2.73	8.6	8.9
Malaysia	2.6	-1.3	-8.2	-0.3	67.2	83.6	2.9	-2.30	3.3	4.0
Philippines	0.5	-7.4	-3.1	-0.6	30.0	41.8	1.2	1.05	14.7	10.5
Singapore	1.7	13.3	1.2	4.7	77.0	89.7	1.2	2.40	2.3	2.6
Thailand	-2.9	-5.3	-2.1	2.9	55.8	77.1	4.4	-0.59	4.5	4.8
Viet Nam	-11.9[k]	-7.2	-6.6[p]	-3.4	..	23.7	..	..	187.4	23.5

(Continued on next page)

Table II.3 *(continued)*

(Percentage)

Country/area	Resource gap[a]		Budgetary balance/ GDP[b]		Average annual M_2/GDP		Interest rates[c]	Exchange rates[d]	Average annual inflation rates[e]	
	1981-1990	1991-1995	1981-1990	1991-1995	1981-1990	1991-1995	1991-1995	1986-1995	1981-1990	1991-1995
East and North-East Asia										
China	-0.04	1.7	-0.5	-0.9	57.3	96.7	-1.9	9.99	7.5	11.6
Hong Kong	6.3	3.7	0.3	1.8	148.7	200.0	-4.0	4.40	8.3	9.3
Mongolia	-35.2	-13.9	-12.6	-6.8	28.9	31.8	40.5[q]	..	..	127.2
Republic of Korea	1.8	-0.9	-0.8	-0.3	36.0	41.6	3.3[r]	1.24	6.4	6.2
Taiwan Province of China	10.1	2.5	0.1	-3.0	109.3	171.9	3.8	3.28	3.1	3.8
Developed countries[nst]										
Australia	-1.0	-1.0	-1.2	-2.8	45.2	61.1	..	-0.72	8.1	2.5
Japan	-1.0	2.0	-0.7	-0.7	101.3	112.2	1.0	4.49	2.1	1.4
New Zealand	-1.0	3.0	-1.7[g]	-0.0	33.5	78.0	5.2	-0.61	10.8	2.1

Sources: Calculated on the basis of data from ADB, *Key Indicators of Developing Asian and Pacific Countries 1996*, vol. XXVII (Oxford University Press, 1996) and *Asian Development Outlook 1996 and 1997* (Oxford University Press, 1996); IMF, *International Financial Statistics Yearbook 1995* (Washington DC, 1995) and *International Financial Statistics* (Washington DC, September 1996); ECE, *Economic Survey of Europe in 1994-1995* (United Nations publication, Sales No. E.95.II.E.1), p. 97, and *Economic Survey of Europe in 1995-1996* (United Nations publication, Sales No. E.96.II.E.1), p. 96; World Bank, *World Development Report 1996* (Oxford University Press, 1996); IMF, *World Economic Outlook October 1996* (Washington DC, 1996); OECD, *OECD Economic Outlook* 59, June 1996 (Paris, OECD, 1996) and national sources.

[a] Resource gap is defined as gross domestic savings/GDP minus gross domestic investment/GDP.
[b] Budgetary balance/GDP of Bangladesh, Cambodia, Myanmar, Samoa, India, Islamic Republic of Iran, Indonesia, Malaysia, Viet Nam, China, Hong Kong and Republic of Korea excludes grants.
[c] Real interest rates on time deposits of 12 months.
[d] Refers to trend growth rate of real effective exchange rate.
[e] Refers to changes in consumer price index.
[f] 1991-1994.
[g] 1987-1990.
[h] 1985-1990.
[i] 1991-1993.
[j] 1991-1992.
[k] 1982-1990.
[l] 1986-1994.
[m] 1983-1990.
[n] Resource gap refers to period 1960 and 1994.
[o] Budgetary balance/GDP refers to period 1992-1995.
[p] 1984-1990.
[q] 1992-1995.
[r] Time deposits of over 12 months.
[s] Interest rates refer to real interest rate offered to resident customers for demand, time or savings deposits.
[t] Budgetary balance/GDP of Australia and Japan refers to general government fiscal balance.

keeping the budget deficits apparently low in most cases. The figures for Samoa, for example, indicate that the budget deficit, exclusive of grants, increased to 24.7 per cent of GDP in 1992-1995 from 17.8 per cent in 1982-1990. Receipts of ODA by Pacific island countries declined by 2 per cent per annum in real terms over the period 1983-1993. In 1987-1988, ODA accounted for an average of over 40 per cent of GNP but had declined to 24.3 per cent by 1992-1993. Even so, ODA inflows per capita are still substantial.

In that context of the trend towards declining ODA, public sector wage restraints and rationalization of trade and industrial policies are crucial for improving fiscal balance, ensuring macroeconomic stability and enhancing international competitiveness.

Pacific island countries that have their own currencies (Kiribati and Tuvalu use the currency of a major trading partner) have used the exchange rate as the main instrument for controlling domestic prices. Except for Papua New Guinea, which floated its exchange rate in 1995 to prevent the heavy outflow of capital following the devaluation of the currency as part of a stabilization package, most Pacific island countries have adopted some type of fixed exchange rate system. Papua New Guinea, like several other Pacific island countries, had pegged its currency to a currency basket which included the currencies of major trading partners. Earlier, Papua New Guinea had used the "hard kina" strategy to contain its domestic price level. As a result, the currency had appreciated by an average of 3.2 per cent in 1986-1995, which may have adversely affected exports. The changes introduced in 1995 have helped to correct the distortion. However, the currencies of Fiji, Solomon Islands and Vanuatu depreciated during the same period.

It is worth noting that even if competitiveness were enhanced using nominal exchange rate flexibility, other factors, such as rising wages, could erode such gains. It is therefore important that exchange rate adjustments be accompanied by other appropriate policy adjustments. In recognition of this fact, Fiji, while devaluing its currency following the 1987 change of government, also did away with linking wages to the consumer price index. Similarly, Papua New Guinea introduced flexibility in the system of wage indexation in 1989. In Samoa, Solomon Islands, Tonga and Vanuatu, wages are more flexible and are determined to a great extent by market forces.

North and Central Asia

The economic recession and the macroeconomic instability in this group of economies in transition had a deterrent effect on domestic savings and investment. The current savings and investment rates in those countries are much lower than in many other developing ESCAP member countries where savings averaged at least one fourth of GDP and investment at least one third.

Since the beginning of the process of economic transition in the Central Asian countries and the Russian Federation, domestic savings in general and household savings in particular have declined sharply. During the period 1993-1995, the household savings ratio declined from 56 per cent of total savings to 16 per cent in Armenia and from 35.5 to 14.9 per cent in Azerbaijan. In Turkmenistan, this ratio fell from 64 per cent in 1993 to 44 per cent in 1994, and in Uzbekistan from 45 to 25 per cent. Savings of industrial and agricultural enterprises have also fallen dramatically during the recession owing to their non-profitability or operation at low output levels. The problem has been further aggravated by huge inter-enterprise arrears inherited from the former Soviet Union.

The investment performance of the countries of Central Asia and the Russian Federation has not shown any visible signs of recovery since 1992. In 1992-1995, investment fell in most of these countries. In 1995, the decline in real gross investment outlays was 72 per cent in Azerbaijan, 25 to 27 per cent in Kazakstan and Tajikistan, and 13 per cent in the Russian Federation. By 1995, investment recovery had taken place only in two countries, Kyrgyzstan and Uzbekistan. Despite a drastic decline in investment rates, large shortages of investible resources appeared in most of these countries.

Declining domestic savings, coupled with insufficient tax realizations, have led to a considerable fall in budgetary resources in all of the countries. Budgetary expenditure remained high owing to continued state subsidies in some areas, particularly social services. Budget deficits have been one of the main problems undermining economic recovery. In 1992-1995, the budget deficit as a proportion of GDP averaged 23.7 per cent in Armenia, 17.2 per cent in Tajikistan, 12.4 per cent in Kyrgyzstan and above 10 per cent in Uzbekistan and the Russian Federation. The budget deficits have been financed mainly by money creation and, in some cases by bond issues.

The scarcity of domestic investment funds in the Central Asian countries and the Russian Federation has been partly met by an inflow of FDI. The total stock of FDI in the Russian Federation reached $5.5 billion in 1995. The volume of FDI in the other countries has been much lower than in the Russian Federation and has been unevenly distributed across those countries. Cumulative FDI flows reached $2.88 billion in Kazakstan, $268 million in Armenia and $238 million in Kyrgyzstan in 1995. Foreign investment has not been sufficient to offset the scarcity of domestic resources in those countries.

A marked slow-down in inflation rates has been a major achievement. Hyperinflation, which had reached almost 2,000 per cent per year in most of the countries of North and Central Asia in 1992-1994, was arrested in 1995 by radical stabilization programmes. With the crucial support of international financial institutions such as IMF and the World Bank, governments sought to tighten monetary and fiscal policies, resulting in a considerable reduction in inflation rates.

In Kyrgyzstan, the average inflation rate fell from 1,290 per cent in 1993 to 380 per cent in 1994 and to 52 per cent in 1995, one of the lowest rates among the Central Asian countries. Both consumer and producer price inflation decelerated in other countries in 1995-1996. Prices in the Russian Federation rose by only 15.5 per cent in the first half of 1996 compared with 78 per cent in the corresponding period of 1995. An exception in this respect was Tajikistan, which experienced a new outburst of high inflation in 1995. Reducing annual inflation rates remains a policy priority for all of the Central Asian countries.

All governments have responded to the economic crisis by introducing packages of reform measures aimed at revitalizing economic growth with greater reliance on market forces. Those have encompassed macroeconomic stabilization, price and trade liberalization, privatization of selected state enterprises, the development of the institutional and legal framework for a market economy, including the creation of a market-based financial system, and the reduction of subsidies coupled with the provision of social safety nets.

One of the immediate consequences of these reforms in the countries has been a major increase in the role of the private sector. By 1995, the private sector accounted for about half of all economic activities, particularly in the services sector. The share of the private sector in total employment increased to 24 per cent in Azerbaijan, 34 per cent in Kazakstan, and between 55 and 60 per cent in Kyrgyzstan, the Russian Federation and Uzbekistan.

In order to bring budget deficits under control, governments have made significant efforts to increase tax revenue through the introduction of new taxation policies and to reduce government spending. New taxation policies included such measures as widening the tax base, simplifying the tax code, reducing the nominal tax burden and improving the efficiency of tax collection (box II.4).

Stabilization of national currencies was another matter of concern for macroeconomic stability. Since their introduction in 1993, the national currencies of the Central Asian countries have undergone continued depreciation. The value of the currencies of Armenia, Azerbaijan and Turkmenistan fell by 440, 13,000 and 25,000 per cent respectively during the period 1993-1995. The reasons behind the dramatic decline of national currencies were high levels of inflation, lack of confidence in the currencies, and initial overvaluation of the currencies. As a measure to firm up the national currencies, the governments established currency exchange auctions or used multiple exchange rate systems to discourage unofficial and hidden transactions in foreign currencies. As a result of tight monetary policies and the recent easing of inflationary pressures, the currencies of a number of countries tended to stabilize by 1995-1996.

The liberalization of output prices and the establishment of a two-tier banking structure in the Central Asian countries and the Russian Federation made it possible to use monetary policy as a tool for macroeconomic management. Monetary policies introduced by the central banks in those countries in the course of economic reforms have started to assume a greater role in determining price levels and interest rates. However, inflationary pressure has forced the central banks to keep interest rates as high as 200 to 300 per cent per year at the first stage of reforms, which hampered economic recovery. As a consequence, many industrial and agricultural enterprises were unable to borrow money and postponed the payment of their bills, wages and taxes. In line with falling inflation, the central banks have cut refinancing rates. For example, by the middle of 1995, the annual refinancing rate was reduced from 200 to 130 per cent in the Russian Federation and from 300 to 214 per cent in Uzbekistan.

Box II.4. Strengthening the revenue system in the countries of North and Central Asia

Government expenditure and revenue have tended to decline drastically in the economies of North and Central Asia. At the beginning of the 1990s, the countries of Central Asia continued to receive intergovernmental transfers which could amount up to 20 per cent of GDP under arrangements developed within the former Soviet Union. The continued receipt of such transfers and the sudden upsurge of revenue from hard currency sales of natural resources allowed countries to maintain or enhance revenue during the years 1991-1992. Revenue has dropped considerably in subsequent years, partly as a result of the loss of these intergovernmental transfers. Government spending remained high or even increased owing to the rapid expansion of social transfers and subsidies to loss-making enterprises during the years 1991-1993. Despite some reduction in expenditure proportions since then, budgetary deficits have emerged as one of the most intractable problems for most of these economies (see table).

Even though government expenditure has been declining fast since 1994, in most of the countries public spending continued to exceed revenue by large margins. These countries therefore needed to take urgent measures to improve their budgetary balance as part the means of stabilizing their economies. Further reduction of government expenditure, which had already been reduced substantially, has not been a feasible option for them as that would entail cuts in many social services and aggravate serious social problems in situations characterized by falling per capita income and high rates of inflation. Mobilization of revenue was, therefore, a more appropriate way to improve the state of the budget not only to overcome present difficulties but also to put their public finances on a sound footing for the future.

Ratio of government revenue and expenditure to GDP in the countries of North and Central Asia, 1991-1995

(Percentage)

		1991	*1992*	*1993*	*1994*	*1995*
Armenia	(a)	26.0	27.0	24.0	16.0	14.0
	(b)	28.0	64.2	68.6	43.7	27.0
	(a-b)	-2.0	-37.2	-44.6	-27.7	-13.0
Azerbaijan	(a)	36.0	48.0	41.0	26.0	19.0
	(b)	40.7	46.4	58.0	46.5	30.0
	(a-b	-4.7	1.6	-17.0	-20.5	-11.0
Kazakstan	(a)	21.0	23.0	22.0	17.0	16.0
	(b)	32.9	31.9	24.7	24.0	18.8
	(a-b)	-11.9	-8.9	-2.7	-7.0	-2.8
Kyrgyzstan	(a)	22.0	16.0	15.0	19.0	15.0
	(b)	30.3	33.9	36.6	28.6	23.5
	(a-b)	-8.3	-17.9	-21.6	-9.6	-8.5
Russian Federation	(a)	46.0	46.0	41.0	37.0	36.0
	(b)	..	..	..	..	..
Tajikistan	(a)	33.0	36.0	36.0	54.0	14.0
	(b)	49.6	57.8	52.1	55.0	30.6
	(a-b)	-16.6	-21.8	-16.1	-1.0	-16.6
Turkmenistan	(a)	38.0	42.0	19.0	10.0	9.0
	(b)	38.2	42.2	19.2	10.4	10.0
	(a-b)	-0.2	-0.2	-0.2	-0.4	-1.0
Uzbekistan	(a)	31.0	32.0	42.0	36.0	35.0
	(b)	52.7	49.7	53.0	38.4	39.2
	(a-b)	-21.7	-17.7	-11.0	-2.4	-4.2

Sources: Adrienne Cheasty, "The revenue decline in the countries of the former Soviet Union", *Finance and Development*, vol. 33, No. 2, 1996, p. 33 and European Bank for Reconstruction and Development, *Transition Report 1996: Infrastructure and Savings* (London, 1996).

Notes: (a) = government revenue.
(b) = government expenditure.

The erosion of traditional tax bases has been a basic cause of revenue decline in most of the economies. Production and consumption taxes in the form of levies on enterprises and turnover in distribution and sales were the most important common sources of revenue in the countries of the former Soviet Union. Taxes on enterprises and consumption each accounted for about one third of the budget revenue in 1989 in the former Soviet Union. Revenue contributions from both these sources have declined since then. Between 1989 and 1994, the share of taxes paid by enterprises fell from 12.3 to 7.1 per cent of GDP and taxes on consumption fell from 12 to 9 per cent of GDP in aggregate for all countries of the Commonwealth of Independent States.

Payment of taxes by enterprises was seriously affected by a decline in production and the problem of inter-enterprise arrears clogging the entire payment system throughout the economy. In 1996, the tax arrears of the 185 largest industrial enterprises in the Russian Federation amounted to $2.2 billion to the federal budget and $4.6 billion to local budgets. In Kazakstan, 35 industrial firms owed $13.5 million to the state budget in the same year. Declining real wages and rising unemployment have also led to a considerable fall in personal income and payroll taxes. In 1996, income taxes amounted to only 6 per cent of the aggregate personal incomes of the population in the Russian Federation.

Other major problems of the tax systems of these countries are extensive tax exemptions and evasions. Often, tax exemptions are allowed in the energy and agriculture sectors, which significantly erode tax bases. In most countries, exemptions to agriculture were meant to encourage the development of that sector and to reduce the negative impact of price liberalization. Most of these economies are among the major producers of oil, gas and minerals. Revenue from these sectors is much smaller compared with international norms, mainly because of exemptions granted to the sector. For example, in 1995, the oil and gas sector of the Russian Federation paid less than 2 per cent of GDP in taxes. A sector of similar size in other oil- and gas-rich countries generated tax revenue equal to 5-8 per cent of GDP.

The increasing number of tax evaders has affected tax collection and the inadequacy of the tax administration has aggravated the problem of tax evasion and avoidance. Collection often fell far short of the assessed potential. In the first nine months of 1996, the Government of the Russian Federation, for example, could collect only three-quarters of the planned revenue.

In order to reverse the revenue decline, governments have taken measures to improve their tax legislation. Kazakstan and Kyrgyzstan have introduced new tax codes, which have simplified and modernized the tax systems by reducing the number of taxes. In 1996, the Government of the Russian Federation submitted a new tax code for parliamentary approval. The new code envisaged cutting down the number of federal and local taxes from 100 to 30, included new provisions for income and profit taxes aimed at shifting more of the burden from companies to individuals, and proposed new tax administration laws. However, the code was not approved for implementation in 1997 as planned.

Rehabilitation of tax revenue in these countries requires both an improvement of the tax collection machinery and a broadening of existing tax bases. Tax collection can be improved through training and the skill development of tax officials and further development of institutions. An improvement in tax administration, accounting procedures and audits, as well as in legal systems, should bring new taxpayers into the tax net. The main new taxpayers should be in the private sector. So far, the emerging private sector has not been fully captured in the tax net. Many transactions and income-generating activities take place outside the formal economy. Other important subjects for expansion of the tax base are property and land. Extension of the tax base to the private sector, to property and to land appears to be the main policy option to improve the revenue performance of these countries.

Considerable progress has been made by some of the countries in consolidation and mergers of banks, many of which were too small to be viable. For instance, the number of banks operating in Kazakstan was reduced from 210 in 1993 to 113 in 1996. The country is expected to have only 50 to 70 banks by the end of 1998. In 1995, the Central Bank of the Russian Federation revoked the licences of 225 banks. The reforms in the banking systems also included measures aimed at strengthening the institutional capacity of the central banks with respect to more effective performance of supervisory and regulatory functions and improving the human resources capacity within commercial banks with a view to performing new functions under a market-oriented system.

The state of the economies in the Central Asian countries and the Russian Federation, after five years of economic reforms, makes it obvious that the transition to a market-oriented system will be long and difficult. Some progress has been achieved in macroeconomic stabilization and in creating the basic institutions of a market economy. The economic and social cost of transition has been high, but the foundation for future progress appears to have been laid.

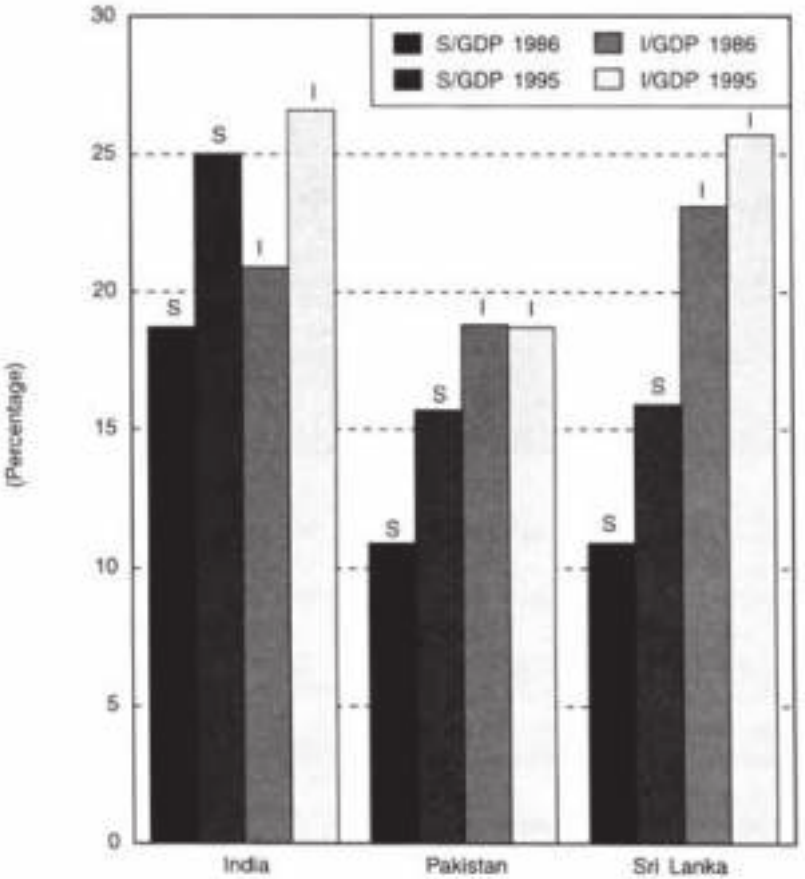
South and South-West Asia

The five economies under review have generally been characterized by relatively low rates of domestic savings and investment. Data for the

latest available years on these variables indicate that the investment rates exceeded 25 per cent in India and Sri Lanka, accompanied by a rise in domestic saving rates also (figure II.10). There does not seem to be any firm upward trend in investment rates in any of these countries.

For lack of available data, it is not possible to discern any saving-investment trends in the economies of the Islamic Republic of Iran and Turkey. The data reported for 1995 indicate a 16.5 per cent rate of investment in the Iranian economy, whereas a 25 per cent savings rate is indicated. Government budget deficits have also been slashed to a level of just above 1 per cent of GDP during the period 1991-1994 from an average of more than 6 per cent of GDP during the 1980s. However, the inflation rate in the economy seems to have accelerated considerably, rising to an average of 29 per cent in 1991-1995 compared with a rate of 18 per cent during the 1980s. An investment rate of 22 per cent is indicated in the Turkish economy along with a savings rate of 21.6 per cent in 1995. The Government of Turkey, however, has been running a relatively high rate of budget deficits, equivalent to 5 per cent of GDP on average in 1991-1994 compared with an average of 4 per cent during the 1980s. Inflation in the Turkish economy has traditionally been high but it has accelerated considerably in the 1990s, running at an average rate of 80 per cent in 1991-1995 compared with an average rate of 46 per cent in the 1980s.

Figure II.10. Savings (S) and investment (I) rates of selected South Asian economies, 1986 and 1995



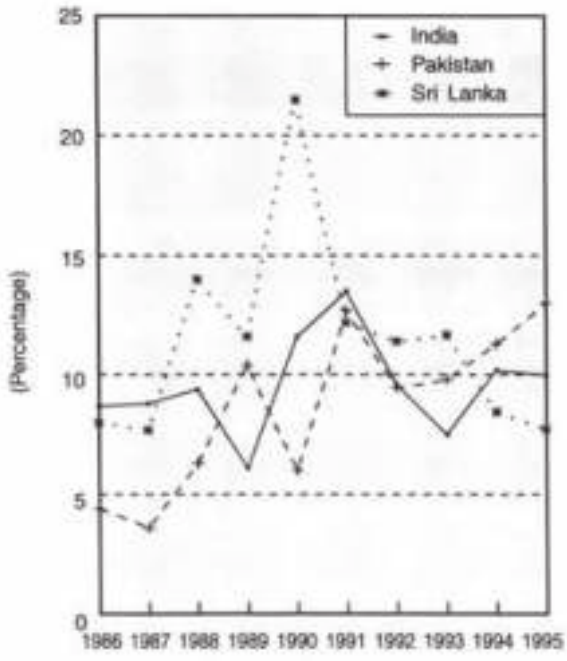
Sources: ADB, *Key Indicators of Developing Asian and Pacific Countries 1996* (Oxford University Press, 1996) and national sources.

In Sri Lanka, investment rates had reached well above 30 per cent during the early 1980s. However, that could not be sustained as the domestic savings rate failed to catch up with the investment rate, leaving huge shortfalls in resources. Despite lower investment rates and moderate advances in savings rates, a resource gap equivalent to more than 10 per cent of GDP on average remained in 1991-1995, slightly lower than the average gap of above 12 per cent of GDP during the 1980s. The resource shortage has been further reflected in government budgetary deficits running at an average of more than 10 per cent of GDP in the 1980s and at about 8 per cent on average in 1991-1995. Much of the domestic deficit has been monetized, leading to inflationary pressures in the economy. The average rate of annual inflation was 10 per cent in 1991-1995, having slowed from an average of more than 12 per cent during the 1980s. The recent trends have indicated a gradual rise in both savings and investments rates, the investment rate rising to above 25 per cent and the savings rate to about 16 per cent in 1995. That still leaves a gap of around 9 per cent of GDP. There does not yet seem to have been any relief from the continuing shortfall in overall resources and the high rates of inflation in the economy.

In Pakistan, the investment rate seems to have remained stable at around 18 to 19 per cent of GDP almost throughout the past decade and a half. With the savings rates of around 10 per cent of GDP in the 1980s, that level of investment left the country a resource shortfall equivalent to 8.4 per cent of GDP on average during the 1980s. In the face of a drastic fall in foreign aid resources on which the country has traditionally depended, Pakistan had to make serious efforts to improve its domestic savings performance. The efforts seem to have paid off since the savings rates increased to almost 16 per cent in 1995, doubling from about 8 per cent in 1980. With the investment rates remaining stable at the low 18 to 19 per cent level, the country was still left with a resource shortfall of around 3.3 per cent of GDP on average in 1991-1995. Like Sri Lanka, Pakistan ran a budget deficit averaging more than 7 per cent of GDP in 1991-1995. As a sizeable part of the deficit had to be monetized, the economy experienced an average annual rate of inflation above 11 per cent in 1991-1995, having accelerated from an average of 7 per cent during the 1980s.

Unlike those of Pakistan and Sri Lanka, the savings and investment rates in India have stayed close to each other, leaving the country a resource gap of around 1 to 2 per cent of GDP. Even that low level of deficits, however, translates into huge absolute sums for a country of India's size. India could not therefore aim to push its investment rates far ahead of the domestic savings rate without landing the economy in crisis. That seems to have happened in 1990, when the investment rate had reached 27 per cent while the savings rate remained below 24 per cent, leading to the 1991 crisis. Public sector deficits remained high, running at an average of 6.2 per cent in 1991-1995, although this was lower than the 7.6 per cent average of the 1980s. Inflation in the economy averaged more than 10 per cent during the first half of the 1990s compared with an average of just above 9 per cent in the 1980s (figure II.11).

Figure II.11. Variation in annual rates of inflation in selected South Asian economies, 1986-1995



Sources: ADB, *Asian Development Outlook* (Oxford University Press), various issues and national sources.

Note: Inflation rates measured by changes in consumer price index.

Data on monetary variables for the Iranian economy are not available to make any observations on that score. In the presence of large budget deficits, monetary restraints have been the principal means of keeping inflation in check in the economies of the other four countries. Interest rates and credit allocations, until recently, were largely under discretionary controls. The rates of monetary growth in India, Pakistan and Sri Lanka have remained moderate with an average of 13 per cent in India, 19 per cent in Pakistan and 20 per cent in Sri Lanka during the period 1991-1995. The rate of monetary expansion in the Turkish economy has been very high, averaging almost 95 per cent annually in 1991-1995. However, the rate of monetary growth has been more or less in line with the sum of real output expansion and inflation in the economy, thus keeping the money supply as a ratio to nominal GDP largely stable in all of these economies. The overall rate of monetization of these economies has, in the process, remained not only stable but relatively low, with India having the highest ratio of M_2 to GDP of 47 per cent on average in 1991-1995, followed by Pakistan with 44 per cent, Sri Lanka with 32 per cent and Turkey with 29 per cent. These ratios are not very different from the averages for the 1980s. These low levels of monetization also suggest a limited intermediation role by the financial systems.

Real interest rates on bank deposits despite, a recent relaxation of the regulations governing nominal interest rates, turned negative, except in Sri Lanka, as nominal interest rates did not fully adjust to the rates of inflation in the economy. However, the real exchange rates have been allowed to depreciate in all of these countries through large periodic adjustments in India, Pakistan and Turkey over the period 1986-1995. In Sri Lanka, the rate has also depreciated moderately during this period owing to the earlier introduction of flexibility into the exchange rate regime. Although the exports of these countries, other than India's, are narrowly based, the depreciation in the real exchange rate has apparently had favourable effects on the growth of exports, which are mainly composed of simple manufactured products. Accelerated rates of export growth have been the most noteworthy positive achievement of these economies in recent years.

South-East Asia

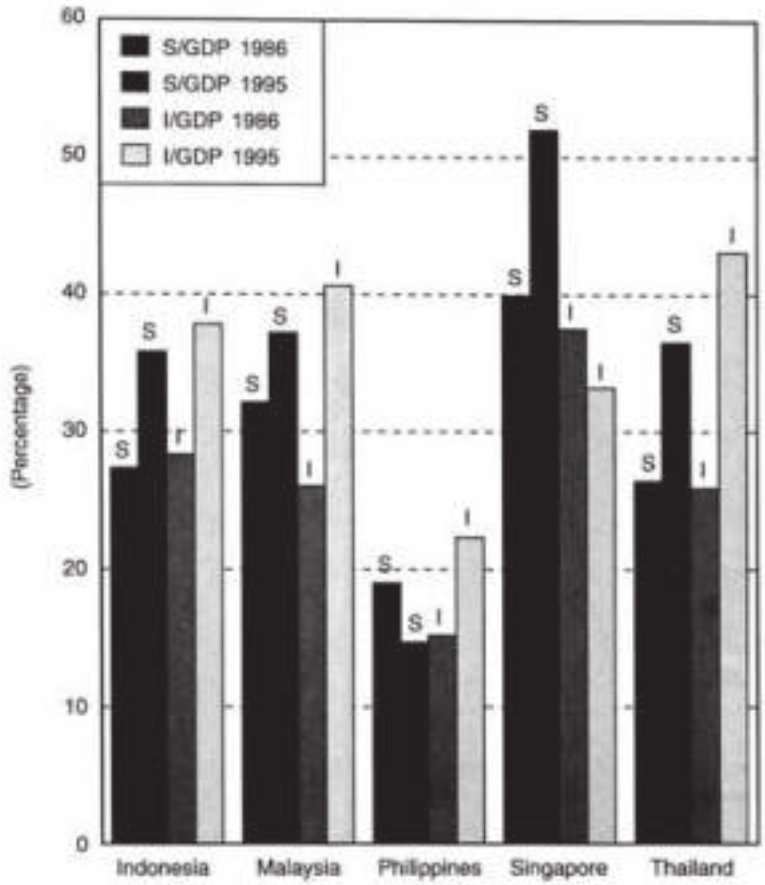
The economic growth of these countries has been supported by high rates of domestic investment and savings (figure II.12). Domestic investment in Indonesia, Malaysia and Thailand rose to around 40 per cent of GDP in 1995 from 30 per cent in 1980. In Singapore, however, the investment rate came down from 46 per cent in 1980 to 33 per cent in 1995, reflecting the scaling down of hectic construction activities in public housing and large-scale infrastructure projects, including the construction of an underground subway system. The Vietnamese economy has also experienced substantial acceleration in the investment rate albeit from a small base, with the rate rising from 12 per cent in 1986 to 27 per cent of GDP in 1995. In the Philippines, the investment rate recovered to 22 per cent in 1995 after a serious decline in the mid-1980s.

Investment has been financed largely by domestic savings, which registered a similar rise through the years to reach 36 per cent of GDP or more in 1995 in Indonesia, Malaysia and Thailand. The savings rate in Singapore stood at 52 per cent in 1995, far exceeding the domestic investment rate. The savings rate in the Philippines seems to have declined to around 15 per cent in 1995 from about 19 per cent in the early 1990s. Viet Nam has made a remarkable gain with a 19 per cent saving rate in 1995, up from about 3 per cent in 1990.

There have been many attempts to explain what has enabled these and economies in East Asia to achieve the observed high rates of economic growth, domestic savings and investment. Thrift, hard work and entrepreneurship are among the causes of high rates of savings and investment. There is also an interrelationship between economic growth and domestic savings or investment in that the former is both a cause and a consequence of the latter. High domestic savings notwithstanding, a gap of the order of 4 to 5 per cent remained between domestic savings and investment. That crucial gap has been substantially financed by the inflow of FDI into these economies.

Indonesia, Malaysia and Thailand have been among the largest recipients of FDI flows not only in the region but among all the world's developing countries. Viet Nam, with a substantial acceleration of inward FDI flows in recent years, is also emerging as one of the largest recipients of annual investment

Figure II.12. Savings (S) and investment (I) rates of selected South-East Asian economies, 1986 and 1995



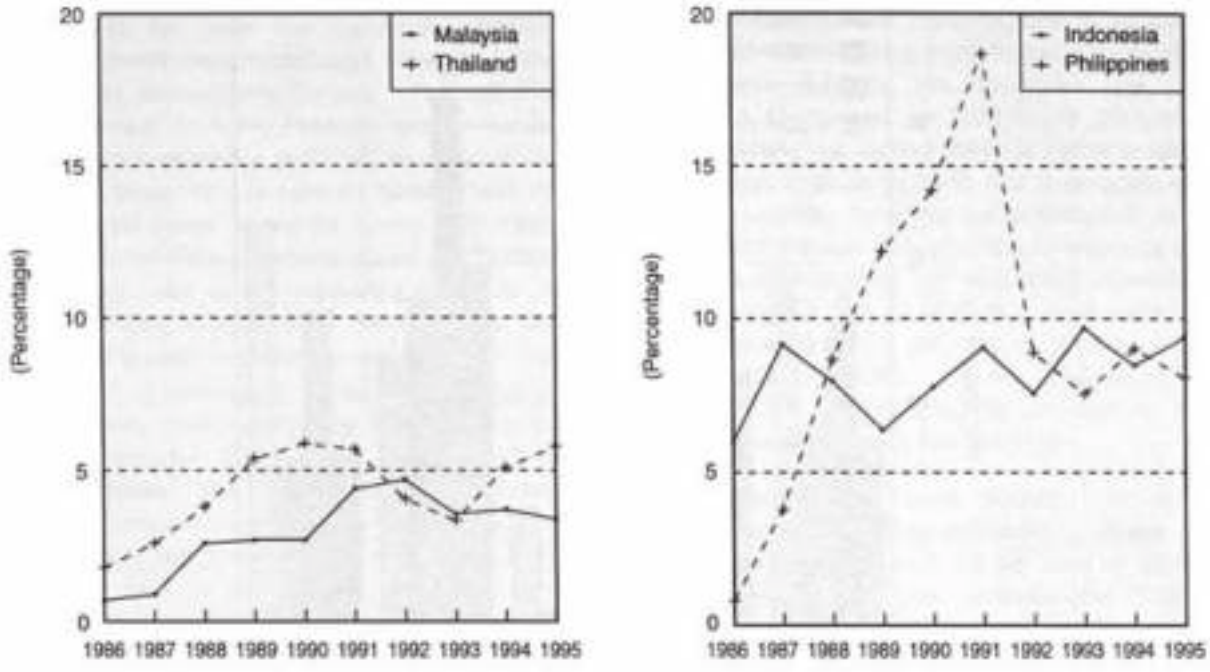
Sources: ADB, *Key Indicators of Developing Asian and Pacific Countries 1996* (Oxford University Press, 1996) and national sources.

flows. The Philippines lagged behind in this respect, but lately it has been attracting substantial volumes of flows.

The monetary and fiscal policies pursued by the governments of these countries have been generally prudent. That has enabled the maintenance of price and exchange rate stability. Budget deficits have been kept low. With the further tightening of fiscal policy in the wake of a tendency for budget deficits to widen and inflation to accelerate in the 1980s, Malaysia, the Philippines, Singapore and Thailand were able to turn the budget deficits into surpluses during the past several years. Monetary policies have similarly been geared towards the maintenance of stability while promoting certain strategic sectoral objectives. The recent moves towards reform and liberalization of financial sectors have further encouraged financialization of savings, as reflected in a rise in the ratio of broad money (M_2) to GDP.

Price stability has been a hallmark of the economic performance of these countries. Inflation has not exceeded 3 to 4 per cent in Brunei Darussalam, Malaysia and Singapore since 1981 and has hardly exceeded 5 per cent in Thailand (figure II.13). Indonesia experienced a stable average inflation rate of about 8.5 per cent during the same period. The Philippines, however,

Figure II.13. Variation in annual rates of inflation in selected South-East Asian economies, 1986-1995



Sources: IMF, *International Financial Statistics* (Washington DC, September 1996); ADB, *Asian Development Outlook* (Oxford University Press), various issues and national sources.

Note: Inflation rates measured by changes in consumer price index.

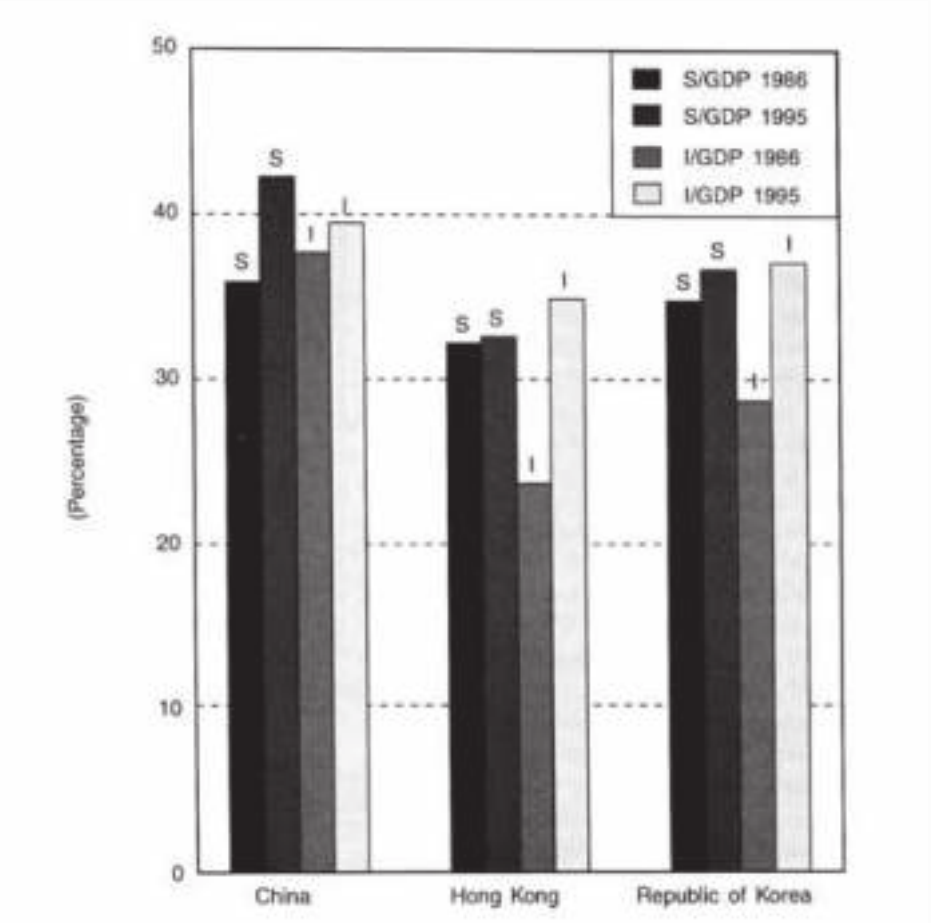
experienced high rates of inflation averaging almost 15 per cent in the 1980s. The rate has slowed down considerably since then, currently running below 10 per cent. Viet Nam experienced a period of hyperinflation, the annual rate being close to 200 per cent during the 1980s, but the country has achieved remarkable success in reducing the inflation rate to its current level below 8 per cent.

Thus, all the elements usually advanced as conducive to successful economic growth have been present in the economies of these countries. Government policies and attitudes generally have been what is often referred to as business-friendly. The economic dynamism and stability and the business-friendly environment created conditions that attracted investment from both domestic and foreign investors, which considerably reduced the need for debt financing, a source of instability in many other developing countries. Domestic price stability has also enabled the currency exchange rates to be kept relatively stable. In the cases of Indonesia, the Philippines and Viet Nam, where inflation rates have been relatively high, the nominal exchange rates have been allowed to depreciate so that real exchange rates have either depreciated or remained stable to benefit exports.

East and North-East Asia

Rapid economic growth in China, as well as in the three newly industrializing economies of East Asia, has been associated with high rates of mestic investment in these economies (figure II.14).

Figure II.14. Savings (S) and investment (I) rates of selected East and North-East Asian economies, 1986 and 1995



Sources: ADB, *Key Indicators of Developing Asian and Pacific Countries 1996* (Oxford University Press, 1996) and national sources.

Investment rates typically exceed 35 per cent of GDP and in some cases approach 40 per cent. Investment rates, both in China and the Republic of Korea, have accelerated in recent years, reaching 39.5 per cent in China and 37 per cent in the Republic of Korea in 1995. In Hong Kong, investment rates, after some deceleration, picked up in 1995 to almost 35 per cent, partly owing to large infrastructure investments, including the construction of a new international airport complex.

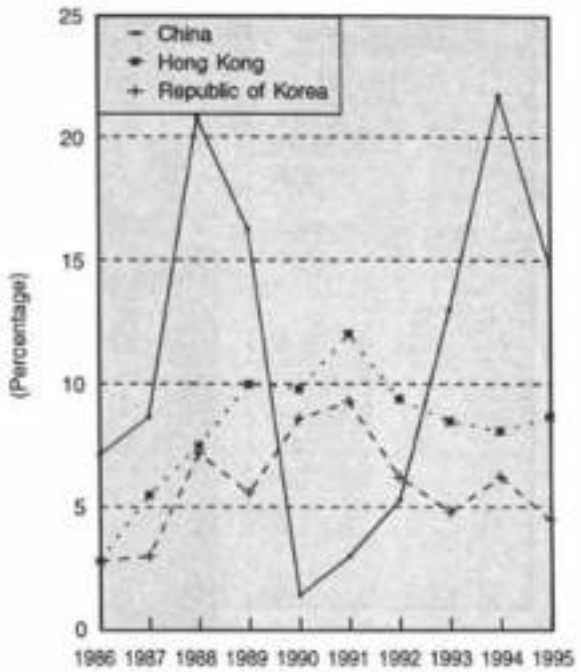
Mongolia suffered a setback in domestic investment early in the 1990s. However, it has quickly recovered and achieved an investment rate of almost 25 per cent in 1995. Mongolia's investment, however, remains critically dependent on the inflow of external resources, as domestic savings rates are well below investment rates. However, the savings rate almost doubled to 16 per cent of GDP in 1995 compared with 8 per cent in 1990. For the period 1991 to 1995, the country experienced an average savings-investment gap of almost 14 per cent of GDP.

In China, Hong Kong, and the Republic of Korea, domestic savings rates have ranged between 35 and 40 per cent. That has left a 2 to 3 per cent gap on average between the domestic investment and savings rates during the period 1991-1995. The shortfall has been considerably smaller than the resource shortage that they experienced in the 1980s. The Republic of Korea even produced a small surplus during the first half of the 1990s. All these economies have been recipients of large volumes of FDI as the principal means of financing investment in excess of domestic savings. Such inflows accelerated considerably in the 1990s. China has been the largest developing country recipient of FDI inflow since 1992, accounting for some 40 per cent of all flows into developing countries in 1994. Subsequently, the inflows slowed because of certain recent changes in policies with regard to FDI that gradually eliminate some of the special concessions offered to foreign investors.

China, Hong Kong, Mongolia and the Republic of Korea have experienced different degrees of inflationary pressures (figure II.15). Mongolia experienced an average rate of inflation of 127 per cent during the period 1991-1995. That average largely reflected the sudden burst of inflation with the ushering in of a market-based economic regime. Stabilizing the economy has been a major focus of government policies since then, and the country has done remarkably well in containing inflation from a monthly rate of 12.5 per cent in 1992 to an average rate of 3.6 per cent in 1995.

China also experienced a relatively high average rate of inflation of 11.6 per cent in 1991-1995. Inflation had reached very high levels in 1988-1989, which had prompted the government to apply some stringent measures of fiscal and monetary control. That brought inflation down to 2 to 3 per cent in 1990-1991, but it also brought a sharp slowdown in economic growth. Subsequent relaxation of policy controls, while reviving the economy's fast-paced growth, also revived inflation, which reached a new height of 21.7 per cent in 1994. Restraining inflation has therefore remained a major plank in the policy of the Government of China, though the measures applied have been less restrictive and more gradual in order not to jeopardize the economy's continued high growth, as was the case in the early 1990s. Inflation rates in Hong Kong, at an average of above 9 per cent in 1991-1995, and in the Republic of Korea, at above 6 per cent during the same period, have also been comparatively modest. Nevertheless, stabilizing the price level has remained a major policy concern. The Republic of Korea succeeded better than Hong Kong in containing inflation.

Figure II.15. Variation in annual rates of inflation in selected East and North-East Asian economies, 1986-1995



Sources: IMF, *International Financial Statistics Yearbook 1995* (Washington DC, 1995) and *International Financial Statistics* (Washington DC, September 1996); ADB, *Asian Development Outlook 1996 and 1997* (Oxford University Press, 1996) and national sources.

Note: Inflation rates measured by changes in consumer price index.

The success of the East Asian economies, as in the case of South-East Asian economies, is again partly attributed to the success of government policies. Apart from the concern for price stabilization with fiscal and monetary measures, policies affecting the real sectors of these economies have been geared towards encouraging investment and production with stress on production for export. That has enabled all these economies to experience high,

export-driven economic growth rates over the years and to attract a substantial volume of FDI. As noted above, high rates of investment have also been supported commensurably by high rates of domestic savings.

Most of the governments have kept low budget deficits as policy targets. China has shown concern at the tendency of its budget deficits to rise, though the size of the central government's deficits rose to just above 1 per cent of GDP in 1995. Both Hong Kong and the Republic of Korea have had surpluses in their government budgets.

All of these economies have experienced a rapid escalation of monetary growth. China had a 33 per cent average expansion, and the Republic of Korea 17.5 per cent during the period 1991-1995. These expansions have been responsible for the relatively high rates of inflation which they have experienced. Interest rates in China, which remain largely regulated, did not adjust to the price movements in the economy. As a result, real interest rates tended to turn negative during the period 1991-1995. Apparently, this did not have an impact on the saving rates in the economy. Real interest rates also turned negative in Hong Kong, but they remained positive in the Republic of Korea.

Other than in Hong Kong, nominal exchange rates in other economies have been flexible, with periodic adjustments or daily floating. However, the adjustments apparently have not been sufficient in relation to the relative rates of inflation at home and abroad, and so the real exchange rates of the domestic currencies of all of them have tended to appreciate. In China, there was almost a 10 per cent average appreciation in 1986-1995. A downward adjustment in the nominal exchange rate was made in 1994 as a corrective measure.

THE PROSPECTS

A question that has frequently been discussed in recent years is whether the fast-growing economies of the region can sustain their growth in the long run. The question has generated wide interest in the backdrop of a slowdown in some of the region's fast-growing economies recently, in part owing to drops in export growth. Speculation has centred on whether the slowdown is a temporary downturn or a permanent structural feature caused by loss of export competitiveness, the prime engine of past growth. Another important question for the region is whether the slow-growing and weaker economies of the region can accelerate growth and successfully join the regional and global mainstreams.

The growth performance of the fast-growing economies of the region is not attributable to any one single factor. Thrift, hard work and entrepreneurship, as well as government policies that provide positive support and encouragement to private enterprise within a reasonably stable macroeconomic framework, have all been advanced as causes for the successful economic performance of these economies. Currently, both governments and private enterpreneurs are refocusing their attention on overcoming the constraints that have been emerging as a result of years of rapid growth. These constraints, which include shortages of skills and expertise, rising labour costs and structural and infrastuctural bottlenecks, are affecting their ability to compete internationally.

To overcome these difficulties, countries have initiated extensive programmes, *inter alia*, to upgrade the educational level of the people, refocusing education to meet the requirements of modern business and technology, to step up research and development in order to upgrade technology, and to improve the quality of essential infrastructures, such as power, transport and communications, and extend their coverage. At the same time, businesses in the private sector have been stepping up efforts to train and retrain their workforce, upgrade technology, raise productivity and reduce costs.

With rising wage costs and limited prospects for further increase in already high levels of savings, a gradual move away from factor-intensive industrialization towards more skill and technology intensive growth has emerged as a core development strategy. This strategic approach is being complemented by intensification of trade and financial reforms and enhancement of the role of the private sector not only in industrial and trading activities but also in building and running a variety of power, transport and communications infrastructures. The basic aim is to maintain or enhance international competitiveness and sustain the "fast-growing" status.

Economies such as those of China, Malaysia, Thailand and Viet Nam are still projected to grow at rates ranging between 7 and 10 per cent in 1996-2000 (table II.4). The economy of the Philippines,

Table II.4. Forecast of growth and inflation for selected economies in the ESCAP region

(Percentage)

Country/area	1995	1996 (Estimate)	1996-2000 (Forecast)
East and South-East Asia			
China			
GDP growth	10.2	9.2	8.7
Inflation rate	14.8	9.2	8.2[ab]
Hong Kong			
GDP growth	4.6	5.0	4.4
Inflation rate	8.7	6.3	6.9[ac]
Indonesia			
GDP growth	8.1	7.2	7.0
Inflation rate	9.4	7.5[c]	9.5[ac]
Malaysia			
GDP growth	9.5	8.2	8.3
Inflation rate	3.4	3.6	2.4[ab]
Philippines			
GDP growth	4.8	5.5	7.0
Inflation rate	8.1	8.8	6.2
Republic of Korea			
GDP growth	9.0	6.6	6.6
Inflation rate	4.5	4.9	3.8
Singapore			
GDP growth	8.9	6.0	6.7
Inflation rate	1.8	2.3	2.5
Taiwan Province of China			
GDP growth	6.1	6.0	6.2
Inflation rate	3.7	3.0	0.4[c]
Thailand			
GDP growth	8.6	6.7	7.3
Inflation rate	5.8	5.8	4.7[ab]
Viet Nam			
GDP growth	9.5	9.4	9.9
Inflation rate	12.7	7.4	8.8
South and South-West Asia			
India			
GDP growth	6.6	6.6	7.0
Inflation rate	10.0	7.0[d]	5.6[d]
Iran (Islamic Republic of)			
GDP growth	4.5	5.1	5.1
Inflation rate	49.7	..	..
Pakistan			
GDP growth	4.4	6.1	6.7
Inflation rate	13.0	10.8	8.9[ab]
Sri Lanka			
GDP growth	5.5	3.6	5.7
Inflation rate	7.7	9.6	9.7[e]
Turkey			
GDP growth	7.4	5.0	5.8
Inflation rate	93.6	6.0[b]	7.1[b]
Least developed and Pacific island countries			
Bangladesh			
GDP growth	5.1	6.0	7.0
Inflation rate	5.8	4.7	5.3
Cambodia			
GDP growth	7.0	7.4	7.1
Inflation rate	3.5	5.2	5.0
Fiji			
GDP growth	1.4	5.0	..
Inflation rate	2.2	3.0[f]	..
Lao People's Democratic Republic			
GDP growth	7.1	7.5	8.3
Inflation rate	19.4	13.8	9.8[e]
Myanmar			
GDP growth	9.8	6.1	6.0
Inflation rate	25.2	..	..
Nepal			
GDP growth	2.9	6.1	6.0
Inflation rate	7.6	8.5	..
Papua New Guinea			
GDP growth	-2.9	1.8	1.4[a]
Inflation rate	17.3	5.3	5.6[a]
Samoa			
GDP growth	7.0	5.0	3.8
Inflation rate	1.0	..	..
Developed countries			
Australia			
GDP growth	3.1	4.0	2.9
Inflation rate	4.7	2.7	3.4
Japan			
GDP growth	0.9	3.7	2.6[a]
Inflation rate	-0.1	-0.1	0.9[a]
New Zealand			
GDP growth	2.5	2.0	4.8
Inflation rate	3.7	2.4	1.4

Sources: ESCAP secretariat calculations based on United Nations, "Project LINK World Outlook: Countries and regions", 14 November 1996; World Bank, *Cambodia: From Recovery to Sustained Development*, Report No. 15593-KH, 31 May 1996; and forecasts made by individuals and research organizations.

[a] 1996-1999.
[b] Refers to GNP deflators.
[c] Refers to GDP deflators.
[d] In terms of wholesale price index.
[e] 1996-1997.
[f] Up to November 1996.

whose growth has picked up recently, is also expected to grow at an accelerated rate of 7 per cent during the period 1996-2000. These rates may be somewhat slower than the achievements of most of these countries in the recent past but the rates are still high enough to enable their current economic size to double within a period of 7 to 10 years. The minor slowdown may also be consistent with their policy objectives of maintaining economic stability and promoting equity and a regional balance in the economy. However, the first-generation NIEs, such as Hong Kong, the Republic of Korea, Singapore and the Taiwan Province of China, are expected to record a more pronounced slowdown as a natural consequence of maturing economies.

Among the comparatively slow-growing South Asian economies, India, with its vast market size, skilled manpower and advanced technological base, is well placed to see further acceleration of its growth rates, which in recent years have exceeded 6 per cent. The 7 per cent growth projected in its ninth five-year plan is realistically achievable. Pakistan's economy has a less diversified base than India's, yet it can realize its 6 to 7 per cent rates of annual growth beyond the year 2000. Both these countries plan to move on with their reform agendas, which include, *inter alia*, trade, fiscal and financial reforms, downsizing of the public sector and enhancing the role of private sector in the economy. With their vast populations, lower spread of basic education and generally low living standards for the masses, these countries may see social issues impose a greater constraining effect on the pace at which reforms could be implemented. The Islamic Republic of Iran, Sri Lanka and Turkey, also on the path to reform and liberalization and with the advantage of better educated manpower bases, can be expected to sustain 5 to 6 per cent average growth rates.

The economies in transition in the North and Central Asian subregion are expected to stabilize fully and set themselves on a path to positive growth by the turn of the century. Some of them have already stabilized substantially and resumed growth or arrested further decline. Their technological and educational bases are generally high by developing country standards, which can be expected to stand them in good stead as their ongoing macroeconomic and institutional reforms take stronger hold.

The least developed and the Pacific island economies form the weakest link in the chain of countries and territories of the region which can expect to join the growing circle of regional prosperity, though the prospects for all of them may not be so bleak. Some of them, such as Bangladesh, Cambodia, the Lao People's Democratic Republic and Myanmar, have already succeeded in accelerating their growth rates to 6 per cent or more and could reasonably expect to grow at 6 to 7 per cent rates per annum in the coming years. High population growth rates and low levels of literacy in countries such as Bangladesh, Bhutan and Nepal, together with the current low levels of living standards, will continue to constrain the rapid pace of macroeconomic and structural reforms to which they have committed themselves. Countries such as the Lao People's Democratic Republic, Maldives and Myanmar have an advantage arising from their achievement of a higher level in basic education at least. The structural characteristics of the Pacific island economies (small domestic markets, remoteness from major centres of international trade and finance and narrow bases of production and exports) bring significant uncertainties to any projections of their growth performance. In the face of declining ODA, much will depend on the capacity of these countries to improve their savings performance, which is currently weak, and to strengthen policy reforms.

In general, the lesser developed economies of the region, including the least developed, the Pacific island and transition economies, can expect to benefit from a continuing structural differentiation of the economies of the region. As the more advanced economies tend to lose their competitiveness and face a more saturated domestic market in certain products, they have been seeking market and invest opportunities elsewhere within the region. This is evident from a growing investment and trade interest shown by the East and South-East Asian countries in South Asia, North and Central Asia, and Indo-China and Myanmar. The lesser developed countries may thus have an opportunity to enhance production and exports of labour-intensive and low-tech industries where their comparative advantages are greater. They have to concentrate on strengthening their infrastructures and expanding their educational bases as these are basic requirements for exploiting such opportunities.

SELECTED ASPECTS OF SOCIAL DEVELOPMENT: ACHIEVEMENTS AND PROSPECTS

Population dynamics

Size and growth

The emerging demographic dynamics (size, growth, age structure of the population and its distribution, particularly between rural and urban areas) will continue to have important implications for development and participation in the globalization and regionalization processes. The ability of individual countries to adapt, adjust to and benefit from the process of globalization will be conditioned by their specific demographic situation. Globalization itself, through its impact on various factors, such as female employment, rural-to-urban migration and metropolitanization, will influence demographic change, as will access to knowledge and information. The following review will focus on the emerging patterns of demographic change in the region and their impact, especially on health, education and employment, which, in turn, affect a country's ability and willingness to participate in the globalization and regionalization processes.

According to United Nations estimates,[6] countries comprising the ESCAP region reached a combined population of 3.5 billion by mid-1995, representing approximately 60 per cent of the world total. The estimates also reveal that by the year 2020 the region's population will increase by 30 per cent to 4.7 billion. Data on population size and growth for individual countries and for the different sub-groups presented in table II.5 reflect the significant diversity that exists among them. At one end are the three developed countries of the ESCAP region, Australia, Japan and New Zealand, which will register only a marginal increase in their combined population from 147 million in 1995 to 152 million in 2020. At the other extreme are the region's least developed countries, including the small island countries and the territories of the Pacific, with populations of 226 million and 7 million respectively, where an estimated 60 per cent increase in the population is expected to occur by the year 2020.

Among the other developing economies of the two major subregions, South and South-West and East and North-East Asia, which account for 36.0 and 38.7 per cent of the region's total population, respectively, the increase during the same period is estimated to be about 50 and 21 per cent respectively. Countries of North and Central Asia, including the Russian Federation, are estimated to register a combined increase of about 10 per cent in their populations during the same period.

It should be noted, however, that these averages mask the variations that exist between individual countries, even countries within the same subregion. For example, while the populations of Afghanistan, Maldives, the Marshall Islands and the Federated States of Micronesia are expected to double by the year 2020, in Japan the population is expected to register a modest decline. Within South Asia, while Pakistan's population is expected to double, that of Sri Lanka will increase by around 30 per cent during the same period. In Central Asia as well, while the population of Russian Federation is expected to decline, those of other newly formed countries are expected to register modest increases.

The above trend is also reflected in the rates of growth of population shown in the table. It can be seen that despite a continuing decline, the rate of population growth has averaged around 1.5 per cent in the developing economies of the region, compared with 0.4 per cent in the developed economies during the 1990s. The rate of growth is the highest in the least developed countries (2.6 per cent) followed by the Pacific island countries (2.2 per cent). For individual countries, the rates vary even more significantly, reflecting the impact of migration and/or refugee movements also.

For the region as a whole, the average annual rate of population growth is projected to decelerate within the next two decades, and this would imply a decrease in the average annual additions to the total population from around 54 million currently to 44 million during the period 2010-2020. Estimates also indicate that nearly all of this increase will occur in the region's developing and least developed

[6] *World Population Prospects: The 1994 Revision* (United Nations publication, Sales No. E.95.XIII.16).

Table II.5. Estimates of total population, 1995-2020, and rate of growth of population, 1960-2020

Country/area	Population in thousands		Annual compound growth rate (percentage)					
	1995	2020	1960-1970	1970-1980	1980-1990	1990-2000	2000-2010	2010-2020
Developing economies	**3 360 935**	**4 558 029**	**2.3**	**2.0**	**1.8**	**1.5**	**1.3**	**1.0**
South and South-West Asia	**1 213 986**	**1 815 062**	**2.4**	**2.3**	**2.4**	**2.0**	**1.7**	**1.3**
India	935 744	1 327 110	2.3	2.2	2.1	1.9	1.5	1.1
Iran (Islamic Republic of)	67 283	115 524	2.8	3.3	4.1	2.4	2.5	2.0
Pakistan	130 660	261 866	2.8	2.6	3.6	2.9	2.6	2.2
Sri Lanka	18 354	24 049	2.4	1.7	1.5	1.3	1.1	1.0
Turkey	61 945	86 513	2.5	2.3	2.4	1.9	1.4	1.1
South-East Asia	**420 511**	**580 095**	**2.5**	**2.4**	**2.0**	**1.7**	**1.3**	**1.0**
Brunei Darussalam	292	405	4.7	4.0	2.9	2.0	1.4	1.2
Indonesia	195 756	264 103	2.3	2.3	1.9	1.5	1.2	1.0
Malaysia	19 948	29 787	2.9	2.4	2.7	2.2	1.6	1.3
Philippines	67 581	99 335	3.1	2.6	2.3	2.1	1.7	1.2
Singapore	2 988	3 295	2.4	1.5	1.1	0.9	0.6	0.5
Thailand	59 401	71 503	3.1	2.7	1.8	1.1	0.8	0.6
Viet Nam	74 545	111 667	2.1	2.3	2.2	2.2	1.8	1.3
East and North-East Asia	**1 280 468**	**1 551 003**	**2.4**	**1.9**	**1.5**	**1.1**	**0.8**	**0.6**
China	1 227 000	1 488 075	2.4	1.9	1.5	1.1	0.8	0.7
Hong Kong	6 207	6 007	2.5	2.5	1.2	0.5	0.1	–0.1
Mongolia	2 410	3 628	2.7	2.8	2.7	2.0	1.8	1.3
Republic of Korea	44 851	53 293	2.5	1.8	1.2	1.0	0.7	0.5
Pacific Island economies	**6 871**	**11 150**	**2.5**	**2.4**	**2.1**	**2.2**	**2.1**	**1.7**
American Samoa	54	98	3.0	1.7	3.9	3.0	2.7	1.8
Cook Islands	19	27	1.6	–1.5	0.0	1.1	1.8	1.2
Fiji	784	1 105	2.8	2.0	1.4	1.5	1.5	1.2
French Polynesia	220	322	3.5	3.1	2.7	2.1	1.6	1.2
Guam	150	209	2.4	2.3	2.3	2.0	1.4	1.1
Kiribati	80	132	2.3	2.0	1.7	1.9	2.2	2.0
Marshall Islands	54	113	3.3	3.4	2.8	3.2	3.2	2.8
Micronesia (Federated States of)	124	253	3.3	3.1	2.7	2.9	3.1	2.6
Nauru	11	21	4.1	1.6	3.6	1.8	3.5	2.1
New Caledonia	181	244	3.2	2.8	1.6	1.5	1.2	1.0
Niue	2	2	0.0	–5.0	–4.0	0.0	0.0	0.0
Northern Mariana Islands	47	68	2.7	2.7	9.7	1.7	1.6	1.3
Palau	17	31	3.6	1.8	2.3	2.4	2.8	2.2
Papua New Guinea	4 302	7 034	2.3	2.5	2.2	2.3	2.1	1.7
Samoa	171	283	2.6	0.9	0.2	1.4	2.4	1.8
Solomon Islands	378	762	3.2	3.5	3.5	3.3	3.0	2.5
Tonga	98	127	2.5	1.2	0.4	0.6	1.1	1.1
Tuvalu	10	14	1.8	2.9	1.2	1.1	1.8	1.6
Vanuatu	169	305	3.1	3.0	2.4	2.6	2.5	2.2

(Continued on next page)

Table II.5 *(continued)*

Country/area	Population in thousands		Annual compound growth rate (percentage)					
	1995	2020	1960-1970	1970-1980	1980-1990	1990-2000	2000-2010	2010-2020
Least developed economies	**226 044**	**365 837**	**2.4**	**2.4**	**2.0**	**2.6**	**2.0**	**1.5**
Afghanistan	20 141	41 290	2.4	1.7	-0.7	5.9	2.5	2.0
Bangladesh	120 433	185 190	2.6	2.8	2.1	2.2	1.9	1.3
Bhutan	1 638	2 852	1.8	2.0	2.2	1.8	2.3	2.1
Cambodia	10 251	18 027	2.5	-0.7	3.1	2.8	2.3	2.1
Lao People's Democratic Republic	4 882	8 910	2.2	1.7	2.7	2.9	2.5	2.2
Maldives	254	509	2.0	2.7	3.2	3.2	3.0	2.5
Myanmar	46 527	71 311	2.2	2.2	2.1	2.1	1.8	1.5
Nepal	21 916	37 748	2.0	2.6	2.6	2.6	2.3	1.9
North and Central Asia	**213 056**	**234 882**	**1.3**	**1.0**	**1.0**	**0.4**	**0.4**	**0.4**
Armenia	3 599	4 564	3.0	2.0	0.9	1.3	1.0	0.8
Azerbaijan	7 558	9 714	2.9	1.8	1.5	1.1	1.0	1.0
Kazakstan	17 111	21 014	2.8	1.3	1.1	0.6	0.9	0.8
Kyrgyzstan	4 745	6 728	3.2	2.0	1.9	1.7	1.5	1.2
Russian Federation	147 000	140 283	0.8	0.6	0.7	-0.2	-0.2	-0.2
Tajikistan	6 101	10 886	3.5	3.0	2.9	2.8	2.4	2.1
Turkmenistan	4 099	6 267	3.2	2.7	2.5	2.2	1.8	1.4
Uzbekistan	22 843	35 426	3.4	2.9	2.5	2.2	1.9	1.4
Developed economies	**146 827**	**151 828**	**1.2**	**1.2**	**0.7**	**0.4**	**0.2**	**0.0**
Australia	18 040	23 586	2.0	1.5	1.5	1.3	1.1	1.0
Japan	125 251	123 973	1.0	1.1	0.6	0.2	0.1	-0.3
New Zealand	3 536	4 269	1.7	1.0	0.8	1.1	0.7	0.6
ESCAP	**3 507 762**	**4 709 857**	**2.2**	**2.0**	**1.8**	**1.5**	**2.0**	**2.2**
World (million)	**5 639**	**7 888**	**2.0**	**1.9**	**1.7**	**1.5**	**1.4**	**1.2**
As percentage of the world total	**62.2**	**59.7**	-	-	-	-	-	-

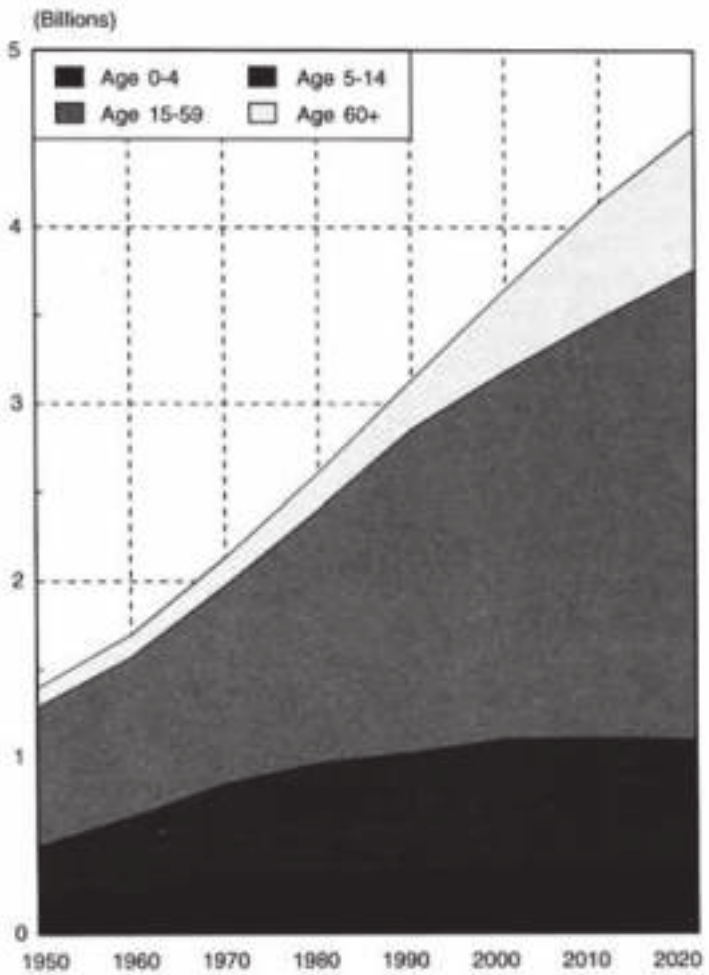
Sources: *1995 ESCAP Population Data Sheet; World Population Prospects: The 1994 Revision* (United Nations publication, Sales No. E.95.XIII.16); *Monthly Bulletin of Statistics*, July 1996 (ST/ESA/STAT/SER.Q/283) and *Statistical Yearbook of China* (Beijing, China Statistical Publishing House), various issues.

economies, with the countries of South and South-West Asia accounting for well over 60 per cent of it. Moreover, there are a number of countries in the ESCAP region where the annual additions to the population due to natural increase (the difference between births and deaths) will not start to decline until the year 2010 or even considerably later. This is because the effect of the decline in fertility would be more than offset by the number of women entering reproductive age, a number that would continue to increase for three to four decades even after the onset of fertility decline. This phenomenon is termed the "momentum" of population growth. The timing of the decline in the average annual addition to the population due to natural increase will thus vary from country to country depending on the timing, pace and pattern of the fertility decline and the trends in mortality.

Age structure

The patterns of change described above will manifest themselves in the population age structures of countries, with important implications for development as well as for the ability of countries to adapt to the process of globalization. A profile of the age composition of the population of the developing economies of the ESCAP region from 1950 through 2020 is shown in figure II.16. As of 1995, about 32 per cent of the population of the developing economies in the region is below age 15, another 8 per cent is over age 60 and the remaining 60 per cent is in the productive age group 15-59, yielding a total dependency ratio of 67

Figure II.16. Population in different age groups in the developing economies of the ESCAP region, 1950-2020



Source: *World Population Prospects: The 1994 Revision* (United Nations publication, Sales No. E.95.XIII.16).

per cent.[7] In contrast, the developed economies have 17 per cent of their populations below age 15, 19 per cent over age 60 and 64 per cent in the working ages, resulting in a dependency ratio slightly lower than that of the developing economies. By the year 2020, it is estimated that the developing economies of today will have a fourth of their populations below age 25 and about 12 per cent over age 60, implying a decline in the dependency ratio to the levels currently prevailing in the region's developed countries. However, the latter group of countries will have only 15 per cent of their populations below age 15, whereas nearly twice as many would be over age 60, reflecting a significant rise in their dependency ratios, contributed by a substantial increase in the population at older ages.

Variations are even more pronounced among the different sub-groups of countries as well as among countries (figure II.17). For example, the least developed countries and a few others, such as the Islamic Republic of Iran, Pakistan and Tajikistan, are characterized by a very young age structure, with 40 to 45 per cent of the population below age 15 and between 4 and 6 per cent over 60, resulting in a dependency ratio of 100. There are many more countries in the region, such as Bangladesh, India, the Philippines, Solomon Islands, Uzbekistan and Turkmenistan, where children below age 15 comprise 35 to 40 per cent of the total population. Yet, many more have well over 30 per cent in this age range, which is considerably above the average of 17 per cent in the developed countries of the region. These figures demonstrate the fact that, in a majority of the developing countries of the ESCAP region, the early decades of the next millennium will see a continuing growth in the total population as well as in the school-age and the working-age populations.

The United Nations projections[8] also indicate that during the next two decades there will be a major shift in the population age structure of all countries in the region, with significant increases in the elderly population aged 60 years and over. The proportion of the elderly in the total population will increase to 25-30 per cent in the region's three developed countries and in some developing countries, and to 10-20 per cent in many others, but it will be below 10 per cent in a few countries, such as the Islamic Republic of Iran, Pakistan, the Philippines and Nepal.

This characteristic feature of the age structure and the pace *or* rapidity of its transformation[9] occurring at a decisive moment in the economic and social development of individual countries is among the factors that would have important implications for their development. Opportunities and challenges differ from country to country, requiring different policy responses.

Urbanization

Another important factor that would influence and would be influenced by development and globalization is the change in the rural-urban distribution of the populations. Among the world's major regions, Asia remains one of the least urbanized, with about 35 per cent of its population living in areas classified as urban. The other region with a low level of urbanization is Africa. This regional average, however, masks the significant differences in the level of urbanization among countries and among the broad sub-groups of countries. It should be noted that a meaningful comparison of the level of urbanization among countries is affected by the differences in the definition of urban areas adopted by the countries concerned. The situation is further complicated by the concentration of population occurring outside the urban periphery that is functionally linked to the urban area but is not included as "urban". Notwithstanding the problems of comparability,[10] it can be seen from table II.6 that the level of urbanization, defined as the percentage of population living in urban areas so classified, varies from 20 per cent in the least developed and small island economies of the Pacific to about 80 per cent in the developed countries of the region.

---

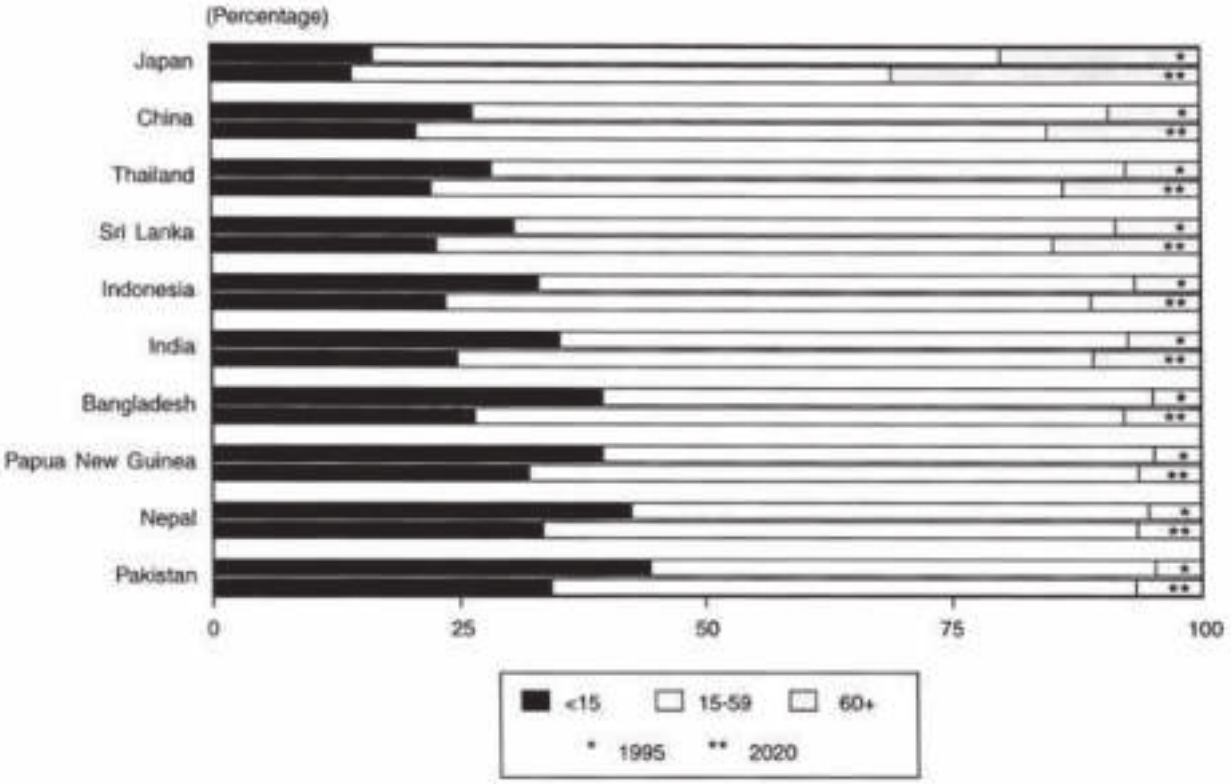
[7] Agriculture being the dominant sector of most countries, labour force participation rates remain high until about age 65. However, age 60 has been used here as the cut-off point. This will not affect the pattern or the implications discussed in this section.

[8] *World Population Prospects: The 1994 Revision* (United Nations publication, Sales No. E.95.XIII.16).

[9] The pace of decline in mortality has been steep in all countries once it has begun. However, the timing and pace of decline in fertility has varied as it is closely linked to the progress made in economic and social development, the effect of programme interventions and the influence of other factors. This determines the timing and rapidity of change in age structure, which interfaces with other developmental factors.

[10] For a detailed discussion on this issue, particularly with regard to the process of urbanization in China, see Sidney Goldstein, "Urbanization in China, 1982-87: effects of migration and reclassification", *Population and Development Review*, vol. 16, No. 4, December 1990, p. 673.

Figure II.17. Age structure of population in selected countries: 1995 and 2020



Note: Countries are arranged according to the stage of demographic transition from the most advanced to those in the early stages of the transition.

The level of urbanization is high (67 per cent) in Central Asia if the Russian Federation is included. If the latter is excluded, the percentage of urban population in the newly formed countries of Central Asia drops but is still well above the average of other major groups of countries. In the other developing economies of East and North-East, South-East, and South and South-West Asia, the level of urbanization remains moderate, with around 30 to 35 per cent of their populations living in urban centres. Data presented in table II.6 also reveal significant variations among countries. In general, they reflect a weak association between the level of development and the level of urbanization.

It is also estimated that the region as a whole will experience a rapid growth of the urban population and a significant increase in the level of urbanization. For instance, the percentage of the urban population in the developing economies is projected to increase to 50 per cent within the next 25 years.[11] This would mean an increase in the urban population from its current size of 1.2 billion to around 2.4 billion, representing a doubling of the urban population. It also means that the estimated increase of 1.2 billion in the ESCAP region's total population during the same period will have to be absorbed by urban areas. This massive increase in the urban population would be accounted for by

[11] *World Urbanization Prospects: The 1994 Revision* (United Nationals publication, Sales No. E.95.XIII.12).

Table II.6. Percentage of urban population, urban population and rate of growth, 1995 and 2020

Country/area	Urban population				Rate of growth (percentage)		
	Percentage		Thousands				
	1995	2020	1995	2020	1995-2000	2000-2010	2010-2020
Developing economies	**33.9**	**50.4**	**1 136 614**	**2 294 811**	**3.2**	**3.0**	**2.6**
South and South-West Asia	**31.6**	**47.1**	**385 845**	**853 904**	**3.3**	**3.3**	**3.1**
India	27.0	41.3	250 681	547 442	3.2	3.2	3.1
Iran (Islamic Republic of)	59.0	72.6	39 716	83 836	3.1	3.4	2.7
Pakistan	35.0	53.1	48 742	139 106	4.7	4.5	3.8
Sri Lanka	22.0	38.6	4 108	9 278	2.8	3.5	3.3
Turkey	69.0	85.8	42 596	74 242	3.5	2.4	1.5
South-East Asia	**36.5**	**53.7**	**147 699**	**311 642**	**3.8**	**3.2**	**2.5**
Brunei Darussalam	58.0	70.0	165	283	2.2	2.3	2.1
Indonesia	35.0	57.4	69 992	151 487	4.2	3.3	2.4
Malaysia	54.0	70.2	10 814	20 902	3.5	2.8	2.1
Philippines	54.0	71.9	36 614	71 442	3.7	2.9	2.0
Singapore	100.0	100.0	2 848	3 295	0.8	0.6	0.5
Thailand	32.0[a]	35.1	11 787	25 088	2.8	3.1	3.2
Viet Nam	21.0	35.1	15 479	39 145	3.5	3.9	3.8
East and North-East Asia	**32.2**	**52.5**	**413 106**	**814 112**	**3.5**	**2.9**	**2.3**
China	30.0	50.8	369 492	755 942	3.7	3.0	2.4
Hong Kong	95.0	97.1	5 574	5 833	0.5	0.2	0.0
Mongolia	61.0	74.3	1 486	2 696	3.0	2.7	2.0
Republic of Korea	81.0	93.1	36 572	49 641	2.1	1.3	0.7
Pacific Island economies	**24.1**	**36.7**	**1 641**	**4 056**	**3.4**	**3.7**	**3.7**
Cook Islands	60.4	73.5	12	20	2.1	2.1	2.3
Fiji	41.0	56.1	319	621	2.5	2.9	2.6
French Polynesia	56.4	67.4	124	217	2.2	2.4	2.2
Guam	38.2	52.1	57	109	2.3	2.6	2.8
Kiribati	35.7	49.9	28	66	3.3	3.4	3.7
Marshall Islands	69.1	80.8	37	91	4.0	3.9	3.3
Micronesia (Federated States of)	28.0	45.6	35	115	4.7	5.2	4.6
Nauru	100.0	100.0	11	21	1.8	3.5	2.1
New Caledonia	62.0	74.4	112	182	2.4	2.0	1.8
Niue	29.0	38.5	1	1	0.0	0.0	0.0
Northern Mariana Islands	54.0	66.2	25	45	2.3	2.5	2.3
Palau	70.6	80.0	12	25	3.1	3.1	2.8
Papua New Guinea	16.0	28.5	690	2 002	4.1	4.4	4.5
Samoa	21.0	31.7	36	90	2.6	3.7	4.3
Solomon Islands	17.0	34.3	65	261	6.5	6.0	5.1
Tonga	41.0	62.9	40	80	3.7	2.9	2.3
Tuvalu	46.0	67.4	4	9	3.9	3.4	2.5
Vanuatu	19.0	33.2	33	101	3.9	4.6	4.8
North and Central Asia	**67.5**	**74.9**	**143 723**	**175 813**	**0.7**	**0.8**	**0.8**
Armenia	69.0	78.3	2 473	3 572	1.6	1.5	1.4
Azerbaijan	56.0	68.6	4 216	6 662	1.7	1.9	1.9
Kazakstan	60.0	72.5	10 218	15 225	1.4	1.7	1.6
Kyrgyzstan	39.0	53.7	1 847	3 610	2.4	2.8	2.8
Russian Federation	76.0	84.4	111 736	118 379	0.3	0.3	0.2
Tajikistan	32.0	46.0	1 964	5 006	3.3	3.9	4.0
Turkmenistan	45.0	57.8	1 839	3 622	2.5	2.8	2.8
Uzbekistan	41.0	55.7	9 430	19 737	2.9	3.1	2.9

(Continued on next page)

Table II.6 *(continued)*

Country/area	Urban population				Rate of growth (percentage)		
	Percentage		Thousands				
	1995	2020	1995	2020	1995-2000	2000-2010	2010-2020
Least developed economies	**19.6**	**37.0**	**44 600**	**135 284**	**5.3**	**4.7**	**4.0**
Afghanistan	20.0	35.9	4 026	14 822	7.7	4.9	4.5
Bangladesh	18.0	36.0	22 034	66 644	5.4	4.8	3.8
Bhutan	6.0	16.2	105	461	6.5	6.2	5.8
Cambodia	21.0	39.5	2 123	7 123	5.8	5.1	4.4
Lao People's Democratic Republic	21.7	40.6	1 060	3 613	5.8	5.2	4.4
Maldives	27.0	41.9	68	213	4.3	4.9	4.7
Myanmar	26.0	43.4	12 188	30 927	3.7	4.1	3.6
Nepal	14.0	30.4	2 996	11 481	6.5	5.7	4.7
Developed economies	**78.8**	**84.3**	**115 515**	**128 047**	**0.5**	**0.5**	**0.3**
Australia	85.0	87.6	15 318	20 655	1.2	1.2	1.2
Japan	78.0	83.5	97 120	103 511	0.4	0.3	0.1
New Zealand	86.1	90.9	3 077	3 881	1.3	0.9	0.8

Sources: *World Urbanization Prospects: The 1994 Revision* (United Nations publication, Sales No. E.95.XIII.12); *World Population Prospects: The 1994 Revision* (United Nations publication, Sales No. E.95.XIII.16) and *1995 ESCAP Population Data Sheet.*

[a] 1994.

rural-to-urban migration, natural increase of current urban populations and the reclassification of certain rural areas (including boundary adjustments) as urban. With the rural population still accounting for about two thirds of the region's population, the contribution of rural-to-urban migration would be substantial even if natural increase were assumed to be the same in rural and urban areas[12].

The emerging process of globalization and the associated patterns of investment and enhanced communications, would, if anything, only accelerate the pace of urbanization to levels higher than those assumed in the above projections. Moreover, they may also contribute, in a significant way, to a pattern of urbanization whereby the population of large cities, including the capital cities of many countries, would increase substantially. According to a recent study, the number of cities in Asia with populations exceeding one million will increase from 118 out of a total of 282 in 1990 to 272 out of a total of 543 in the year 2000.[13] However, an unexplained feature of urbanization during the past two decades, noted in a recent ESCAP study,[14] is the gradually declining proportion of the urban population living in large cities. It remains unclear whether this reflects a response to policy interventions or the inability of data to capture population growth occurring in urban peripheries owing to lack of boundary adjustments.

Migration

The volume and characteristics of migrants are influenced by a number of economic and social factors. Migration, whether internal or international, occurs in response to differential economic opportunities between the sending and receiving areas, although other factors, such as distance and family

12 In general, natural increase in urban areas is lower than in the rural areas because fertility levels are much lower in the former than in the latter. Consequently, an estimate of rural-urban migration based on the assumption that natural increase is the same in both rural and urban areas would be lower than the actual numbers.

13 *World Urbanization Prospects: The 1994 Revision* (United Nations publication, Sales No. E.95.XIII.12).

14 ESCAP, *State of Urbanization in Asia and the Pacific, 1993* (ST/ESCAP/1300).

ties, play a part. Of particular importance in the context of globalization and development is migration between rural and urban areas and between countries, though rural-to-rural migration, urban-to-urban migration and migration between different geographic and administrative divisions of a country would also influence and be influenced by the process. A comparative analysis of the level, trend and patterns of internal and international migration, and an accurate assessment of the contribution of the rural-to-urban migration to urban growth is hampered by a lack of adequate data. Moreover, the relative contribution of various components also depends upon the current level of urbanization, the differentials in natural increase between rural and urban areas, and the rate of rural-to-urban migration.

Recent ESCAP publications attribute about 40 to 50 per cent of the total urban growth during the period 1990-1995 to natural increase, and the rest to rural-to-urban migration and to the effect of reclassification of areas as urban. However, it is estimated that about 40 per cent of the increase in the urban population is due to rural-to-urban migration.[15] This would mean a net transfer of about 250-300 million persons from rural to urban areas during the last two decades. If this trend were to continue during the next 25 years, there would then be a net transfer from rural to urban areas of at least half a billion people; however, in all likelihood the number will be higher, perhaps as high as 600 to 700 million, since the process of globalization and development could accelerate the pace of urbanization, and the rate of natural increase in populations is likely to remain higher in rural areas. Moreover, an increasing proportion of the rural-to-urban migrants will have to be absorbed in the larger urban centres in the developing economies of the region.

Concurrently with the increasing levels and changing patterns of urbanization and rural-to-urban migration, international migration, both among the countries of the ESCAP region and between the ESCAP region and other regions, is likely to increase significantly. A recent study by UNCTAD and IOM estimates the total number of international migrants within the region (excluding refugees and migration outside the region, but including the Middle East) to be around 40 million,[16] which represents a little over 1 per cent of the total population of the region.

Evidence suggests that migration between countries of the region of various types (permanent and temporary, documented and undocumented) has increased substantially. In addition to the developed countries of the region, the NIEs have also attracted migrants. Labour market imbalances in some countries, such as Thailand, have also created a situation wherein those countries are simultaneously receiving and sending migrants.

Another important feature of the emerging patterns of migration is the increasing number of female migrants[17] in recent years, a trend which is likely to continue and even accelerate in the future. This phenomenon is linked to the increase in the education of women, to the patterns of investment, and to the emphasis in policies and programmes, all of which contribute to increased mobility of females.[18]

Human resources development

The demographic trends and prospects described above will play an important part in the attainment of the goals of developing countries related to health, education and employment and in promoting gender equity. Improvements in these areas are critical because they determine the capability of countries to take part in and benefit from globalization and regionalization.

Health

It can be seen from the data presented in table II.7 that mortality has declined to low levels in most countries of the region, with the expectation of

15 ESCAP, *State of Urbanization in Asia and the Pacific, 1993* (ST/ESCAP/1300). The ESCAP *Economic and Social Survey of Asia and the Pacific 1993* gave an estimate of 50 per cent as the contribution of rural-to-urban migration to urban population growth.

16 UNCTAD and IOM, *Foreign Direct Investment, Trade, Aid and Migration* (United Nations publication, Sales No. E.96.II.A.8).

17 *Proceedings of the United Nations Expert Group Meeting on International Migration Policies and the Status of Female Migrants*, San Miniato, Italy, 28-31 March 1990 (ST/ESA/Ser.R/26). See also ESCAP, *State of Urbanization in Asia and the Pacific, 1993*. (ST/ESCAP/1300).

18 See also *Survey 1993*, chaps. V and VI for discussions of issues raised in this section.

Table II.7. Selected estimates of mortality, circa 1990-1995

Country/area	Infant mortality rate 1990-1995	Under 5 mortality rate 1994	Expectation of life at birth 1990-1995	Maternal mortality ratio (per 100 000 live births) 1990
Developing economies	**60**	..	**64.6**	..
South and South-West Asia	**79**	..	**61.4**	..
India	82	119	60.4	570
Iran (Islamic Republic of)	36	51	67.5	120
Pakistan	91	137	61.5	340
Sri Lanka	18	19	71.9	140
Turkey	65	55	66.5	180
South-East Asia	**47**	..	**65.1**	..
Brunei Darussalam	8	10	74.2	60
Indonesia	58	111	62.7	650
Malaysia	13	15	70.8	80
Philippines	44	57	66.3	280
Singapore	6	6	74.8	10
Thailand	37	32	69.0	200
Viet Nam	42	46	65.2	160
East and North-East Asia	**43**	..	**68.6**	..
China	44	43	68.5	95
Hong Kong	7	6	78.6	7
Mongolia	60	76	63.7	65
Republic of Korea	11	9	71.1	130
Pacific Island economies	**57**	..	**63.5**	..
Fiji	23	27	71.5	90
Guam	8	..	75.3	..
Papua New Guinea	68	95	55.8	930
Samoa	64	55	67.6	35
Solomon Islands	27	32	70.4	..
Vanuatu	47	59	65.2	280
North and Central Asia	**26**	..	**68.2**	..
Armenia	21	..	72.6	50
Azerbaijan	28	..	70.6	22
Kazakstan	30	..	69.6	80
Kyrgyzstan	35	..	69.0	110
Russian Federation	21	..	67.6	75
Tajikistan	48	..	70.2	130
Turkmenistan	57	..	65.0	55
Uzbekistan	41	..	69.2	55
Least developed economies	**110**	**51.2**	**51.2**	..
Afghanistan	163	257	43.5	1 700
Bangladesh	108	117	55.6	850
Bhutan	124	193	50.7	1 600
Cambodia	116	177	51.6	900
Lao People's Democratic Republic	97	138	51.0	650
Maldives	60	78	62.1	..
Myanmar	84	109	57.6	580
Nepal	99	118	53.5	1 500

(Continued on next page)

Table II.7 *(continued)*

Country/area	Infant mortality rate 1990-1995	Under 5 mortality rate 1994	Expectation of life at birth 1990-1995	Maternal mortality ratio (per 100 000 live births) 1990
Developed economies	**4**	..	**79.2**	..
Australia	7	..	77.6	9
Japan	4	..	79.5	18
New Zealand	9	..	75.5	25

Sources: *World Population Prospects: The 1994 Revision* (United Nations publication, Sales No. E.95.XIII.16); UNDP, *Human Development Report 1996* (New York, Oxford University Press, 1996); and WHO, *Revised 1990 Estimates of Maternal Mortality: A New Approach by WHO and UNICEF* (WHO/FRH/MSM/96.11), April 1996.

Note: Under-5 mortality should be higher than infant mortality. Deviation from this, for some countries, arises because these two estimates have been obtained from different sources.

life at birth averaging above 65 years, except in the least developed countries, where it is only 55 years. In some of the least developed countries, such as Afghanistan and Cambodia, it is as low as 45 years. In many of the developing countries where the overall mortality rate is low, it is high among infants, children and pregnant mothers, as reflected by the infant, under-5 and maternal mortality rates shown in the table. It can be safely stated that mortality will continue to decline, and that the decline will be faster in countries where it remains high. While this will be generally true of most countries, the changes in the age structure, particularly in developed countries and in the NIEs, will bring about a significant change in the causes of death from the traditional infectious diseases to cardiovascular ailments and cancer, for instance. Moreover, unless an effective and affordable treatment is found, the spread of HIV/AIDS could contribute to an increase in mortality and morbidity in most age groups in many countries.

In the least developed countries as well as in many of the other developing countries, including the most populous countries (Bangladesh, China, India, Indonesia and Pakistan), the quality of health care and access to it remain severely limited for large numbers of people. Meeting the health needs of a growing population, of the increasing number of women of reproductive age, including those in the early adult years, and reaching the goal of "health for all by the year 2000" will remain a daunting task for many countries.[19] That goal, *inter alia*, includes the attainment of reductions in infant, childhood and maternal mortality by half and the universal provision of services through the primary health care system.

Education

Table II.8 shows the current adult literacy rates and gross enrolment ratios at the primary, secondary and tertiary levels for selected countries of the ESCAP region.[20] Enrolment is high at the primary level in most countries. The attainment of universal primary education is a goal set by most countries. Yet, there are a few countries (for example, Afghanistan, Bangladesh, Pakistan and Papua New Guinea) where enrolment at the primary level is very low and few others where further efforts are needed to reach the goal. Even in countries such as India, where the gross enrolment ratio is above 100, the reality of the situation, particularly in remote parts of the country, is that enrolment of primary school-age

[19] For an extended analysis of health and nutrition, see *Survey 1992*, chap. V.

[20] Gross enrolment ratios are defined as those enrolled at different levels in relation to the population in the corresponding age groups, which can be above 100 if people of higher/lower ages are enrolled. Thus, it may not accurately reflect the enrolment of children of appropriate school age categories.

Table II.8. Gross enrolment ratios and adult literacy rates

Country/area	Year	Enrolment ratios						Adult literacy rate 1995
		Primary	Secondary	Tertiary	All level (1993)			
					All	Female	Male	
South and South-West Asia								
India	1993	102	49	..	55	46	63	52
Iran (Islamic Republic of)	1993	105	66	15	67	61	72	72
Pakistan	1990	44	21	3	37	24	49	38
Sri Lanka	1993	106	74	6	66	67	66	90
Turkey	1993	103	61	16	62	55	69	82
South-East Asia								
Brunei Darussalam	1993	107	71	..	70	70	69	88
Indonesia	1992	114	43	10	61	58	64	84
Malaysia	1993	93	59	..	61	62	60	83
Philippines	1993	111	79	26	77	78	76	95
Singapore	1991	107	68	..	68	67	69	91
Thailand	1992	98	37	19	54	55	54	94
Viet Nam	1993	111	35	2	51	49	53	94
East and North-East Asia								
China	1993	118	55	4	57	54	60	81
Hong Kong	1991	102	..	20	71	71	71	92
Mongolia	1990	97	86	14	62	65	58	82[a]
Republic of Korea	1994	96	92	51	81	77	85	95+
Taiwan Province of China	1994	101	96	96	..	..	..	..
Pacific island economies								
Fiji	1992	128	64	..	79	79	80	92
Papua New Guinea	1992	74	13	..	35	31	38	72
Samoa	1993	..	..	..	74	..	..	98[a]
Solomon Islands	1993	94	17	..	46	..	..	62[a]
Vanuatu	1992	106	20	..	52	..	..	65[a]
North and Central Asia								
Armenia	1993	90	85	..	78	83	73	99[a]
Azerbaijan	1993	89	88	..	72	70	73	96[a]
Kazakstan	1993	86	90	42	65	66	64	98[a]
Kyrgyzstan	1993	..	..	21	70	72	68	97[a]
Russian Federation	1993	107	88	45	79	82	76	99[a]
Tajikistan	1993	89	100	..	69	..	..	97[a]
Turkmenistan	1990	..	..	22	77	..	..	98[a]
Uzbekistan	1993	80	94	..	73	..	..	97[a]
Least developed economies								
Afghanistan	1993	31	15	..	18	9	26	31
Bangladesh	1990	79	17	4	40	34	45	38
Bhutan	..	..	..	..	31	..	..	42
Cambodia	1993	..	..	..	30	..	..	35[a]
Lao People's Democratic Republic	1993	107	25	2	50	42	59	57
Maldives	1993	134	49	..	..	70	70	93
Myanmar	1990	105	23	..	49	48	49	83
Nepal	1992	109	35	..	57	43	71	27

Sources: UNESCO, *Statistical Yearbook 1995* (Paris and Lanham, Maryland, USA, UNESCO Publishing and Bernan Press, 1995) and UNDP, *Human Development Report 1996* (New York, Oxford University Press, 1996).

[a] 1993.

children is still not close to being universal. Adult literacy rates in several least developed and South Asian countries are close to or below 50 per cent. Illiteracy among large segments of the adult population, especially women, is a drag on socio-economic development.

As for enrolment at the secondary level, the region's developed countries and the newly independent countries of Central Asia, as well as a few others, show fairly high levels of enrolment. Differences among countries are wider with regard to secondary school enrolment. Even at the secondary and higher levels, education remains generally low even in the fast-growing economies of East and South-East Asia, which are under increasing pressure to improve their educational attainments to create the skill base required to maintain their competitiveness.

Estimates also indicate that the primary and secondary school-age populations will continue to increase significantly in most countries, though at a declining rate. There are some peculiarities, however, resulting from past demographic trends in fertility and migration. For example, in China the one-child family policy of the 1980s resulted in a decline in the school-age population by 55 million between 1980 and 1990. Migration and refugee movements also affect the patterns in Afghanistan, the Islamic Republic of Iran and Pakistan. Leaving aside these special cases, given the increase of the school-age population, attaining universal primary education and increasing enrolment at the secondary and tertiary levels will remain a challenging task for many countries in the region. This challenge will be greater for the least developed countries as well as some other countries where enrolment levels are currently low and where significant increases in the school-age population are expected to occur.

Employment

With the exception of the developed countries and some of the East and South-East Asian economies, countries in the ESCAP region are characterized by the prevalence of high levels of unemployment and underemployment. The unemployment problem is particularly acute among the younger cohorts entering the labour force. This situation is a result of a continued increase in the labour supply resulting from past high rates of natural increase, and slow growth in demand for labour owing to inadequate output growth, savings and investment.[21]

A comparison of the rate of population growth given in table II.5 above and the labour force growth and projections for selected economies given in table II.9 shows that labour force growth exceeds population growth in most of the developing economies in the region, a trend which is likely to continue into the first two decades of the next century. This reflects the net effect of changes in the age structure, increasing participation rates at younger and older ages as well as of females, resulting from improved education, increasing urbanization and other socio-economic factors. Moreover, projections also indicate that the average annual additions to the labour force, reflected by the population aged 15-24, will continue to increase well into the second decade of the next century, though at a declining rate as shown in table II.9.

In countries such as Bhutan, Cambodia, the Lao People's Democratic Republic, Maldives and Pakistan, where fertility remains high, the rate of labour force growth will remain high even in subsequent decades. Data given in the table also reflect some peculiarities, as noted above, resulting from past trends in fertility, migration and refugee movements. For example, in China there will be a significant decline in the number of 15 to 24-year-old cohorts from 1995 onwards as a result of the one-child policy initiated in 1980. Thus, the influence of demographic factors on the labour supply will continue to be significant for all countries. While in some of the least developed countries the demographic trends will keep labour force growth rates high, it will be declining or moderating in the developed countries, the NIEs and China.

---

21 The labour supply is determined by the size and age structure of the population as well as the age/sex-specific participation rates. While the size and age structure of the population is influenced by demographic factors (mortality, fertility and migration), age/sex-specific participation rates are determined by economic, social and cultural factors. Implicit in economic factors is the influence of demand for labour on supply.

Table II.9. Changing profile of the labour force in selected Asian countries

Country	Rate of growth			Relative increase 1980-1990 = 100		Median age			Non-working elderly (65+) to labour force (%)		
	1980-1990	1990-2000	2000-2010	1990-2000	2000-2010	1980	2000	2010	1990	2000	2010
Bangladesh	3.46	3.60	3.27	140	173	30.4	30.6	32.4	6	6	6
China	2.43	1.22	0.87	63	50	29.2	33.9	37.3	8	10	12
India	2.17	2.09	2.03	117	138	32.7	34.0	35.1	8	10	12
Indonesia	2.74	2.35	1.68	109	96	32.8	33.9	36.4	6	8	11
Japan	0.92	0.36	−0.35	43	−43	39.6	43.1	43.2	18	25	34
Malaysia	3.17	2.93	2.58	121	138	31.1	33.9	35.1	7	8	10
Nepal	2.35	2.69	2.47	142	165	30.5	30.1	31.0	4	4	5
Pakistan	3.92	3.66	4.29	130	208	29.5	31.8	31.5	7	8	8
Philippines	2.82	2.82	2.64	128	154	31.1	33.0	34.0	7	7	9
Republic of Korea	2.84	1.81	1.08	82	58	33.2	37.3	39.9	9	12	16
Singapore	1.63	0.62	0.30	44	22	29.0	36.9	38.8	10	13	18
Thailand	2.53	1.77	1.00	87	58	29.4	33.2	36.3	6	7	10

Source: John Bauer, "Demographic change and Asian labor markets in the 1990s", *Population and Development Review*, vol. 16, No. 4, 1990, tables 1 to 4, p. 615.

These trends could keep wage levels low in the least developed countries, and result in labour shortages and wage increases in China, the NIEs and the developed countries. The outcomes would also be influenced by developments in regard to improvements in the education and skill levels of the labour force, and the differential impacts of globalization and regionalization on the demand for and supply of labour.[22]

Further prospects

It has been well recognized that population and development are interrelated in that demographic dynamics influence development trends and are in turn influenced by them. The nature and degree of these relationships, however, will vary in the differing context of the current demographic situations of countries in the region and their expected evolution. In the developed countries (Australia, Japan and New Zealand) and the NIEs (Hong Kong, Republic of Korea, Singapore and Taiwan Province of China) past demographic trends and socio-economic development have resulted in labour shortages in relation to domestic demand. These economies are also experiencing rapid ageing of their populations, requiring adaptation of their health services and social security provision to meet the emerging needs. The ageing of the population would also call for new technological adaptations as substitutes for labour or for augmentation for labour supplies from the existing stock or from a dwindling stock.

Even if technological developments increase productivity, allowing immigration may become unavoidable for these economies to overcome labour shortages, though the type and characteristics (temporary versus long-term) of such migration would have to be determined by the nature of demand and other factors. Partial solution to the problem of their labour shortages has been sought by increasing transfer of capital for investment in other developing countries of the region where labour is abundant and cheaper, a trend that is quite evident from the overseas investments of Japan and the Republic of Korea.

22 See also *Survey 1993*, chap. VI for discussions on health, education and employment issues.

At the other end of the spectrum are the countries classified as least developed, where the wage levels are low, unemployment is high and educational and skill levels are deficient. While these and some of the other low-income countries could attract investment with the abundant labour supply and low wage levels, attracting foreign investment into manufacturing and other industries would require a skilled labour force with higher productive capabilities. Such countries would be seriously constrained by a limited supply of educated and skilled labour for a considerable time to come. Progress towards enhancing the skills of the labour force through expansion and improvement of education through to the secondary and higher levels will itself be slow owing to persistent high fertility, the increasing number of school-age children in the coming decades and currently high illiteracy rates.

However, their efforts towards greater openness to foreign trade and investment will continue to have other direct and indirect demographic implications. The most significant direct impact would be felt in rural-to-urban migration arising from increasing differentials in employment opportunities and wages between rural and urban areas, and facilitated by improved transport and communications. A significant indirect impact will be the moderation in fertility occurring as a result of increased female employment and migration to urban areas, where export-processing industries are likely to be located and in which female employment is likely to be disproportionately larger. That would cause the reduction in the population growth rates which most of these countries urgently seek. The speed at which the change can occur would depend, however, on the pace of industrialization and urbanization that the countries can generate and sustain.

Countries such as Indonesia, Malaysia and Thailand could be grouped into a category where GDP growth is high but there are manifest problems related to the educational and skill levels of the labour force in relation to emerging needs. In these countries, expanding access to and improving the quality of education at the secondary and higher levels is a high priority. As a result of the emerging imbalance in the labour market, these countries could witness a steady outflow and an inflow of labour with varying skills. Moreover, their greater openness to and links with the global economy also set in motion an accelerated pace of rural-to-urban migration, urbanization and metropolitanization for reasons mentioned above. These countries may also find themselves eventually having to continue large investments to improve the education and skills of an increasing number of school-age people, while at the same time meeting the needs of an elderly population.

China's position is unique in that the school-age population started to decline nearly 10 years ago. Entry to the labour force will also start declining soon. These transformations are occurring at a time when the economy is growing at more than 10 per cent per annum. Greater investment in education at the secondary and higher levels, which is feasible with a declining school-age population, could improve the skill levels of the domestic workforce. The consequences of an ageing population with a significantly reduced labour force will, however, need to be addressed during the initial decades of the next century. Differential opportunities would further reinforce migration towards the coastal areas, where economic growth has been concentrated, giving rise to growing regional income disparities within the country.

In the South Asian subregion, unemployment and underemployment will remain significant. Most countries in this subregion are likely to face continuing imbalances between the emerging pattern of demand for labour and supply of skills. Such imbalances can be expected to boost both rural-urban and cross-border migration. India could possibly supply the needed skills suitable for expanding investments. With its current industrial base, diversification and technological advancement, India could accelerate its economic and industrial growth considerably with the support of an expanding domestic market. Migration will be inevitable both within India's borders and outside them, and rural-to-urban migration is likely to increase considerably. Pakistan and Nepal, with persistent high fertility, population growth and low levels of education, could face serious challenges to their development efforts for reasons similar to those of India.

In the Central Asian countries, a further decline in fertility may occur because of the higher

levels of education and higher numbers of women in paid employment. They are likely to face problems in meeting the needs of the elderly and of women who may be pushed out of employment. In addition, rural-urban disparities, accentuated by the process of structural reform that is necessary if they are to join the global market economy, would result in a rapid flow of rural-urban migration.

The impact of globalization and regionalization on the role and status of women will also have to be dealt with. To the extent that they generate employment opportunities for women, globalization and regionalization will result in migration and employment of women, with favourable implications for mortality and fertility. However, it could also have some adverse social effects.

CHAPTER III

FOREIGN TRADE

III

Trade, the export and import of goods and services, has always been viewed as the primary force behind the integration of economies. Trade allowed countries to participate in the international division of labour and thereby to increase their efficiency, productivity and general welfare. However, it is not only the exchange of products that is important but also the associated exchanges of know-how, technology and skills. Trade has been a leading promoter of contacts between economic actors in different parts of the world and a prime facilitator of increased awareness among populations of economic conditions and events outside their own country. In the last couple of decades, rapid growth in trade, particularly exports, was also viewed as closely associated with, if not the engine of, rapid domestic economic growth in selected countries located mainly in the Asian region.[1]

In fact, it is the expressed intention of all countries in the Asian and Pacific region to participate more actively in the international market for goods and services, with an explicit policy objective of increasing exports and export earnings. The motivation for this policy, while indirectly connected with the desire for closer integration with the world economy, is also directly related to the perception of the role of exports in stimulating economic growth. There are several reasons why trade is a necessary condition for economic growth and why it can be an efficient engine of such growth.[2] Trade enables exploitation of a country's comparative advantage in production, and helps overcome the constraints posed by the limited size of the domestic market by providing a vent for surplus production. It also allows exploitation of economies of scale at the firm and industry levels and, where appropriate, the use of mass production techniques. Trade exposes domestic industries, both export industries and import-competing ones, to the rigours of external competition. This should lead to a more dynamic economy, capable of further growth, through improvements in both efficiency in the allocation of resources and cost efficiency at the level of the firm. Another benefit of trade is to secure expansion of output through the import of capital and intermediate goods required for augmenting domestic production. Establishing or further developing industries behind high protection barriers can lead to serious inefficiency and a lack of innovation. Thus, as investment grows in an economy in both absolute terms and as a proportion of GDP, it is likely that imports will need to grow faster than GDP and the financing of imports will be constrained without growth of exports and export revenues.[3]

In addition, as economies are progressively opened to world markets, trade can augment FDI. There is considerable evidence on a trade/FDI nexus.[4]

---

1 See, for example, World Bank, *The East Asian Miracle: Economic Growth and Public Policy* (New York, Oxford University Press, 1993), and UNCTAD, *Trade and Development Report, 1996* (United Nations publication, Sales No. E.96.II.D.6), part two, "Rethinking development strategies: some lessons from East Asian experience".

2 In fact it is important to keep in mind that the word "trade" has two components, exports and imports, and that "The more outputs you want, the more inputs you need, which is why the top 15 exporters are also the top 15 importers – and in virtually the same order", in "The cult of the export: there's more to life – and growth – than just exports", *Far Eastern Economic Review*, 10 October 1996, p. 7.

3 It has been claimed that there are three main channels through which international trade affects economic growth: the import of materials and capital equipment which are not available domestically; cross-border learning of organizational technology and product design; and imitation of production technology. All three basically involve import, rather than export, activities. For the arguments see, for example, Frank Hsiao and Mei-Chu Hsiao, "Diminishing returns and Asian NICs – how they overcome the iron law", in "Technology and development", paper presented at the Fifth Convention of the East Asian Economic Association, Bangkok, 25-26 October 1996.

4 Thus the unidimensional approach to analysing the effects of trade reform on trade performance and output is incorrect as it misses the significant effects that changes in a trade regime may have on FDI, for example, by lowering the transaction costs of doing business and generating greater confidence in the economic future of the country, and also the FDI-generated effects on trade. The latter was the basic purpose behind the development of the ASEAN free trade area. For discussion of this issue, see UNCTAD, op. cit., and M. Plummer, "Policy reform in Asia and trade-investment links", paper presented at the Fifth Convention of the East Asian Economic Association, Bangkok, 25-26 October 1996.

For example, a major link in the "flying geese" model of development is the export-related FDI flows from the leading or secondary geese to the followers which are used to develop the next generation of productive capacity. However, this process is only possible with dynamic trade flows in both directions, exports of products to the leading geese and imports of capital goods and more sophisticated products by the followers. Thus the "flying geese" model is to a great extent a trade-based model of development. Involvement in international trade also has a positive influence on economic growth through widening of the scope for reaping benefits from dynamic and shifting comparative advantage, increase in the robustness and flexibility of an economy, including through diversification in products and markets, and the development of transport and communication networks between economies. An active and large trade sector acts as a natural check on the economic governance of a country. A country's ability to be viewed as a reliable counterpart in international trade is directly related to the quality of its governance in terms of reliability of contract performance, and credibility of macroeconomic policy stances.

There are risks in relying on trade as a force for integration and an engine of growth. The classic caveat is the infant industry argument for protection. Further, if the external economy is primarily characterized by oligopolistic competition, small domestic firms may not be able to be competitive, and the local economy will be supplied only through imports (or by subsidiaries of the oligopolies) and so will be vulnerable to changes in the strategies and interests of these firms. In addition, foreign domination of certain sensitive areas such as food or services (banks, insurance, provision of infrastructure etc.) may not be an acceptable choice.

Exposure to trade implies a certain degree of international competitiveness for all sectors of the economy, tradables and non-tradables, for their efficient operation. Many goods or services that were thought of as non-tradable become tradable and subject to import competition. This may cause changes in the structure of production, with undesirable social repercussions.

Proportionately more trade also increases the exposure of an economy to events beyond its control, for example, fluctuations in international commodity prices, devaluation of the currency of a major trading partner or competitor, changes in the investment strategy of a major transnational corporation, or rapid shifts in consumer tastes in major markets. This exposure then needs to be recognized and managed to the degree possible using hedging techniques, modern communications, and maintaining the confidence and credibility of the economy as a whole. The need to be aggressive and dynamic in a fast-changing world puts pressure on countries and firms to adapt more frequently and more rapidly than in the past. This may be difficult for countries unaccustomed to such practices and may call for a greater role for the private sector, which is usually able to cope with rapid changes in market conditions better than the public sector.

Dependence for foreign exchange earnings on undiversified exports and/or export markets increases significantly the risks associated with market changes beyond one's control. In parallel, a high reliance on one partner for the import of any one product or basket of products is risky. Therefore an increased reliance on trade carries with it a need for diversification in products and partners which is more difficult to achieve in countries with a limited natural resource base or small industrial sector. Also, it is harder for countries that are small and isolated like the Pacific islands, or those with a small traditional trade sector, to compete and conform to the same standards of economic behaviour as the larger ones having more developed fiscal, financial, accounting and legal systems.

There is no fundamental economic reason why trade within any geographic region or subregion should be preferred to trade outside that region, as long as both are competitive. Rather trade within a region may confer some additional benefits and so lead to trade creation rather than trade diversion. There are three such benefits which seem to apply to the Asian and Pacific region. First, there may be considerable reductions in the costs of trade because the "economic distance" between countries, that is, the transaction costs associated with cultural differences, country image, state control, transparency of legal and administrative regimes, local distribution systems, communications, technological infrastructure etc. are reduced by cultural similarities, ethnic ties and intraregional networking. Second, trade relations among countries within a region seem to develop faster when they are at differing stages of development, such as is implicit in the "flying geese" pattern described above. It appears that there is a wider range of stages of development among countries in Asia and the Pacific than in Africa or Latin America, which may at least partially account for the more dynamic growth of

intraregional trade in this region. Trade relations also develop faster when countries are involved in producing different stages of the same final product. This feature, which is often referred to as "componentization", is increasingly widespread in the Asian and Pacific region with different components of industries such as electronics, textiles or automobiles being produced in different countries by transnational corporations, and the trade in intermediate products between them is being stimulated in the process. There are also some new joint ventures among small and medium-sized enterprises which feel more comfortable entering the regional market before venturing further abroad. The third benefit is the positive stimulation of trade-creating possibilities involved in the opening up of areas previously isolated from much external economic contact, such as the Mekong region, where local partners are more familiar with firms from their neighbouring countries than with those from further afield. A related trade creation pattern is emerging from the development of growth areas. The Asian and Pacific region, especially East and South-East Asia, can be distinguished from other regions by the substantial movement towards free trade on a local or subregional basis outside of conventional customs unions and free trade areas. It is likely that the agglomeration effects, regional spillovers and other complementarities observed in the Asian growth areas will become relatively more important in determining the location of production and direction of trade flows in the future.[5]

TRADE PERFORMANCE

This section provides a brief review of the evolution of trade of countries of the Asian and Pacific region in an attempt to identify to what extent the countries have succeeded in using trade as a source of integration into the world or regional economy. Much has been written in recent years about the trade performance of countries in the region. However, these analyses have tended to concentrate on the dynamic economies in East and South-East Asia or on individual countries. This section presents some summary statistics for as many countries of the region as have consistent data, and examines their trends and characteristics.

A regional overview

As shown in figure III.1,[6] the economies of the Asian and Pacific region as a group have increased their share of world exports of goods and services from about 19 per cent in the early 1980s to approximately 26 per cent in the early 1990s, and within this increasing share, the developing economies (which account for 60 per cent of the region's trade) recorded growth rates significantly higher than those of the world average for the entire period 1980-1994. They also outperformed their developed partners in the region. Whether their current growth rate of about 13 per cent can be maintained indefinitely is questionable, but the Asian and Pacific region is likely to continue to increase its share of world exports (see table III.1). The region has also shown higher than average rates of growth of imports of goods and services, and concomitantly is absorbing an increasing share of the world imports, up from about 20 per cent in 1980-1984 to over 25 per cent in the 1990s.

Exports of merchandise goods

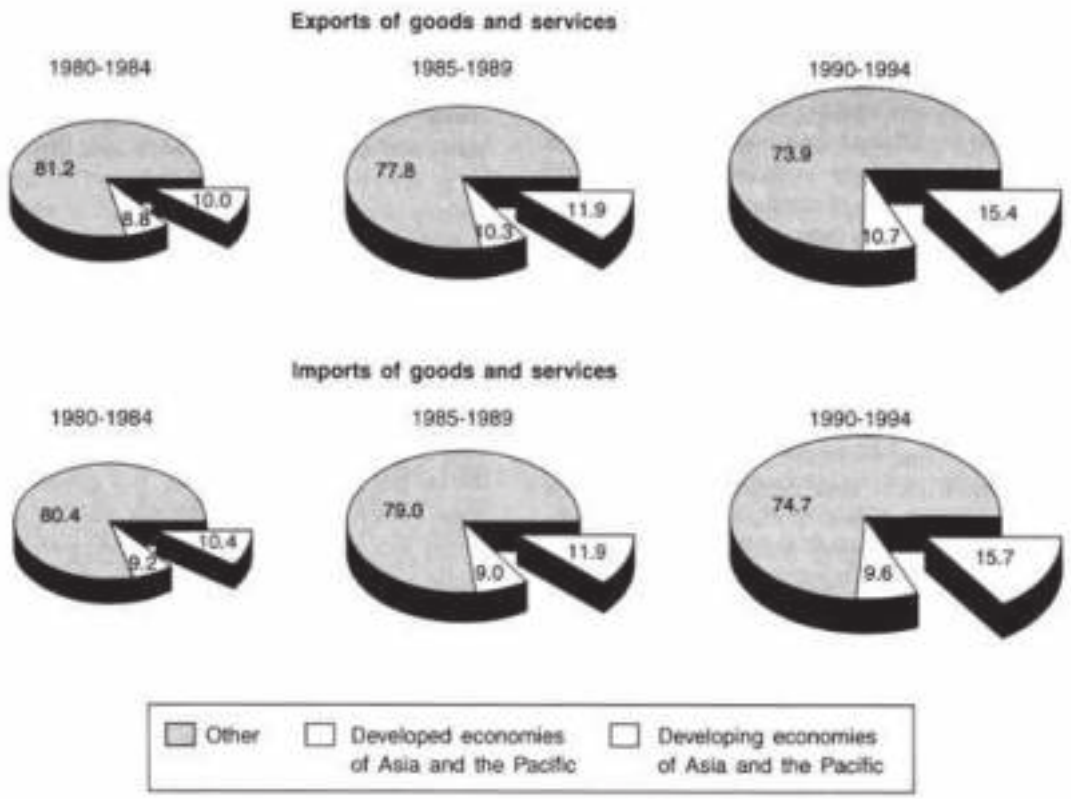
The analysis of the trade data presented below, which is based on period averages, does not take into account the very recent sharp decline in export earnings experienced by several countries including Malaysia, the Republic of Korea and Thailand. The sudden drops have been at least partially attributed to increased competition in export markets and a lag in the upgrading of skills and so of export products. The challenges posed by these declines are discussed later in the chapter under the heading "Adaptation of policies for national development".

---

[5] Beyond the three growth triangles within East and South-East Asia, initiatives to set up similar types of arrangements are under discussion between Bangladesh and India, among Australia, Indonesia and Papua New Guinea, and among the countries of North-East Asia. Thus the nation State, which has been the unit of analysis for international trade theory, may not be appropriate in the future as economic areas are increasingly unlikely to match the boundaries of nation States. For more on this, see Kenichi Ohmae, *The End of the Nation State: The Rise of Regional Economies* (New York, The Free Press, 1995).

[6] The calculations in this chapter have been based on current dollar values, owing to the lack of appropriate deflators for the various components reported.

Figure III.1. Share of world exports and imports of goods and services



Sources: ESCAP secretariat calculations based on GATT, *International Trade: Trends and Statistics*, various issues and WTO, *International Trade: Trends and Statistics 1995*.

Table III.1. Asia and the Pacific in world trade: growth rates of exports and imports of goods and services

	Exports			*Imports*		
	1980-1984	*1985-1989*	*1990-1994*	*1980-1984*	*1985-1989*	*1990-1994*
World	**-0.8**	**10.1**	**7.1**	**-0.5**	**10.1**	**6.9**
Economies of Asia and the Pacific	6.9	12.1	11.8	3.4	12.6	10.9
Developing economies of Asia and the Pacific	7.6	13.3	13.8	5.7	13.4	13.6

Sources: ESCAP secretariat calulations based on GATT, *International Trade: Trends and Statistics*, various issues and WTO *International Trade: Trends and Statistics 1995*.

Table III.2, which reports the growth rates for exports and imports of merchandise goods for the individual developing economies of the region, illustrates the variable performance both between economies and over time for individual economies. Twenty-six of the 39 economies listed from all over the region, or two thirds had growth rates in the early 1990s that were larger than the world average.

Table III.2. Rate of change of values of exports and imports of goods, ranked on 1990-1995 average

	Exports, f.o.b.			Imports, c.i.f.		
	1980-1984	1985-1989	1990-1995	1980-1984	1985-1989	1990-1995
World	**-0.9**	**9.3**	**6.8**	**-0.7**	**9.4**	**6.5**
Developing economies of the ESCAP region	**5.9**	**13.7**	**14.6**	**5.2**	**13.5**	**15.0**
Marshall Islands	29.2	-3.3	69.7	-7.5	-3.3	44.4
Cambodia	6.9	37.9	60.4	17.9	1.4	41.1
Lao People's Democratic Republic	14.5	7.8	34.5	6.8	11.8	23.2
Myanmar	-10.2	-5.2	27.2	15.3	3.4	23.1
Malaysia	7.0	9.8	19.8	7.8	8.4	20.9
Viet Nam	3.5	31.2	19.2	3.8	22.6	18.6
China	8.6	16.3	19.2	8.6	20.5	17.9
Thailand	3.7	23.0	18.9	-5.8	13.3	17.2
Singapore	5.7	14.2	17.9	7.9	5.0	17.0
French Polynesia	2.4	27.8	16.9	5.2	12.9	16.7
Bangladesh	6.8	7.6	16.3	-1.3	16.4	16.0
Sri Lanka	9.5	2.0	16.1	17.8	20.3	15.8
Solomon Islands	8.8	-3.1	16.0	5.5	7.9	15.8
Hong Kong	9.9	21.3	15.6	3.1	6.8	15.6[a]
Nepal	20.2	6.0	15.5	-2.0	3.8	15.1
Philippines	-2.0	8.8	14.9	7.8	19.7	14.6
Cook Islands	2.1	2.8	14.2	8.7	15.6	14.5
Papua New Guinea	-2.9	8.4	13.8	3.1	20.4	12.1
Indonesia	-2.1	0.9	12.7	2.7	6.4	11.1
Republic of Korea	13.9	17.1	12.6	11.7	5.8	11.0
India	4.5	10.6	11.8	0.9	6.2	9.9
Tonga	17.3	4.3	10.6	9.6	14.4	9.7
Pakistan	1.2	13.3	9.6	2.4	4.4	8.8
Taiwan Province of China	11.7	19.5	9.3	-4.7	6.2	7.7
Kiribati	74.2	7.6	8.6	1.2	9.7	6.4[a]
Iran (Islamic Republic of)	9.4	0.6	7.8[a]	2.2	6.0	6.4
Fiji	-7.7	8.7	6.1	-0.4	1.3	6.0
Vanuatu	10.1	-9.5	5.2	10.8	9.3	5.3[a]
Brunei Darussalam	-8.2	-8.2	4.9[a]	-5.4	9.5	5.2
Samoa	8.1	-6.1	4.6	-0.5	9.0	4.7
Maldives	23.0	20.4	3.5	-8.9	20.7	0.9
Bhutan	2.3	41.7	0.4[a]	-1.3	7.5	0.8
Mongolia	8.1	5.9	-0.5	9.6	-1.7	0.7[a]
New Caledonia	-12.0	34.2	-5.0	9.7	4.9	-4.4
Nauru	-6.8	4.7	..	16.9	-1.0	..
Guam	17.3	0.8	..	-8.3	10.0	..
Afghanistan	-1.2	-16.7	..	42.7	60.0	..
American Samoa	16.3	9.2	..	-3.2	9.7	..
Tuvalu	38.3	1.0	..	2.1	4.3	..
				13.8	-8.8	..
Other members of ESCAP in Asia and the Pacific	**6.7**	**10.2**	**10.8**	**0.5**	**9.8**	**10.2**
Russian Federation	..	..	11.9	8.2	8.5	17.5
Turkey	27.0	11.2	11.0	3.5	7.8	8.6
Japan	7.3	10.2	8.4	-0.7	9.6	8.5
New Zealand	0.5	10.5	7.7	..	..	6.1
Australia	1.6	10.4	6.2	5.0	12.1	5.3

Sources: ESCAP secretariat calculations based on United Nations, *Monthly Bulletin of Statistics*, vol. L, No. 10 (October 1996); IMF, *International Financial Statistics Yearbook, 1995* and *International Financial Statistics*, vol. XLIX, No. 11 (November 1996); and ADB, *Key Indicators of Developing Asian and Pacific Countries, 1996* (Oxford University Press, 1996).

[a] 1990-1994.

This shows that they are being integrated rapidly into world markets. In the period 1985-1989, there were 15 such economies, not necessarily the same ones, in a similar position and 12 economies have maintained a rate of growth of exports consistently higher than the world average over the last two and a half decades. These include, as expected, the newly industrializing economies (Hong Kong, Republic of Korea, Singapore, and Taiwan Province of China), China, Malaysia, and Thailand as well as Cambodia, French Polynesia, India, Pakistan and Viet Nam. Thus the experience of rapidly growing exports has been a very recent phenomenon in a significant number of the economies of the region. Very few economies have experienced a contraction in their exports over the last few years. In general, it has been the least developed countries and the Pacific island economies that exhibit low or negative growth rates in exports. These economies are thus the ones for which the risks of marginalization are very real.

It is also important to consider whether the export earnings performance has been accompanied by a significant degree of export earnings instability. Such instability can be very disruptive of development programmes, especially in small economies where the export intensity is rather high. As can be seen from table III.3, the economies of the region with relatively high instability in earnings are either Pacific islands, least developed countries or petroleum exporters. It can be considered

Table III.3. Instability in export earnings of merchandise goods, 1985-1995

Instability less than 10 per cent		*Instability between 10 and 20 per cent*		*Instability between 20 and 30 per cent*		*Instability more than 30 per cent*	
China	3.2	Tonga	10.6	Mongolia	20.7	Bhutan[a]	30.9
Malaysia	4.7	Taiwan Province of China	11.2	Lao People's Democratic Republic	21.7	Tuvalu[a]	35.2
India	5.3	Nepal	12.3	Cook Islands	22.0	Afghanistan[b]	39.6
Bangladesh	5.5	Viet Nam	13.1	Myanmar	22.4	American Samoa[c]	46.2
Sri Lanka	5.7	Solomon Islands[a]	13.2	Samoa	22.5	Nauru[b]	46.3
Philippines	5.9	Vanuatu	14.0	Guam[b]	23.3	Marshall Islands	48.9
Indonesia	6.0	French Polynesia	14.4	Brunei Darussalam[a]	23.3		
Singapore	6.2	Cambodia	17.3	New Caledonia[a]	26.0		
Hong Kong	6.3	Maldives	17.5	Kiribati	27.4		
Thailand	6.8			Iran (Islamic Republic of)	28.5		
Pakistan	7.6						
Fiji	8.5						
Republic of Korea	8.8						
Papua New Guinea	9.8						

Sources: ESCAP secretariat calculations based on United Nations, *Monthly Bulletin of Statistics*, vol. L, No. 9, (September 1996); IMF, *International Financial Statistics*, vol. XLIX, No. 11 (November 1996), and ADB, *Key Indicators of Developing Asian and Pacific Countries, 1996* (Oxford University Press, 1996).

Notes: The measure of instability is $1/n\sum_{t=1}^{n} [|(X_t - \hat{X}_t)/\hat{X}_t|] * 100$ where X_t is the oberved magnitude of export earnings; $\hat{X}_t$ is the magnitude estimated by fitting an exponential trend to the observed values and n is the number of observations. The vertical bar indicates the absolute value (i.e. disregarding signs). Accordingly, instability is measured as the percentage deviation of export earnings from the exponential trend levels for the given period.

[a] 1985-1994.

[b] 1985-1993.

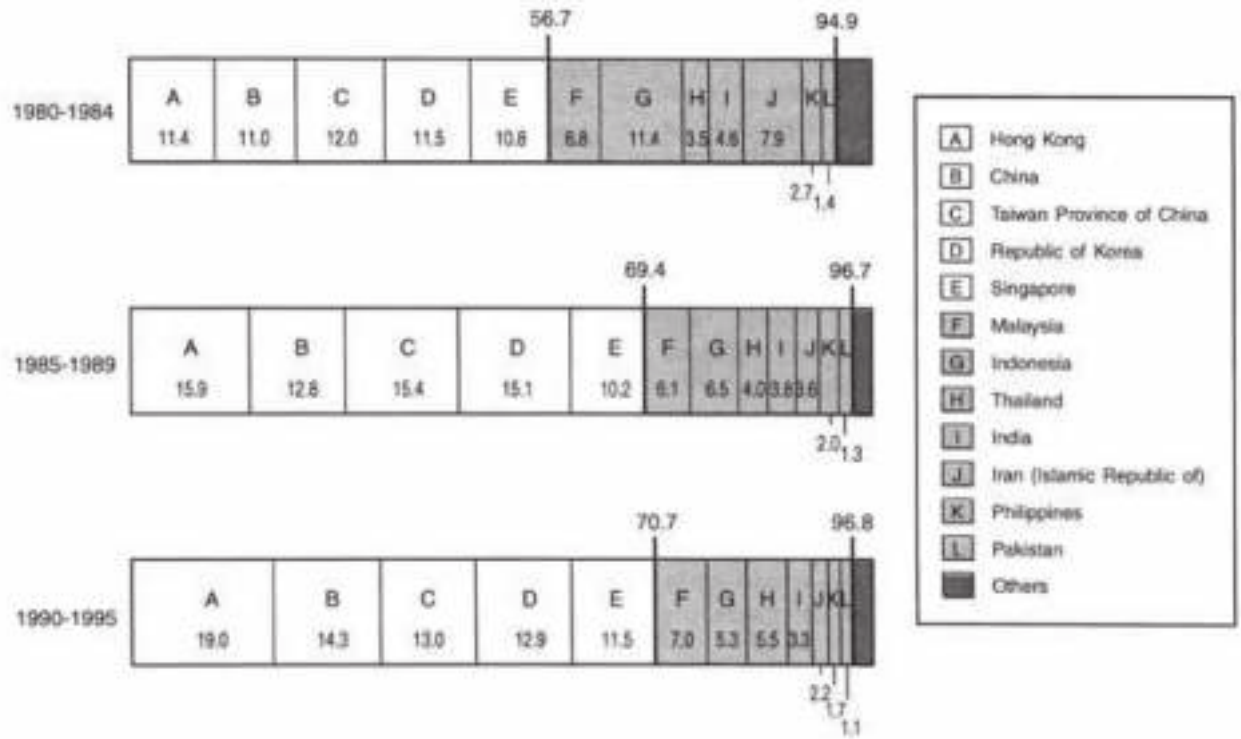
[c] 1985-1992.

that those with instability of under 10 per cent have not faced serious disruptions, whereas the development efforts in those with instability of over 20 per cent are very vulnerable to export performance.

Figure III.2 presents a picture of increasing export concentration in the region. The high percentage of exports (97 per cent in the period 1990-1995) originating in the 12 economies listed, which also account for 93 per cent of the GDP of the developing economies of the region and 83 per cent of the population, is not unexpected. It is interesting to note that the percentage of exports accounted for by just five economies (four economies in East Asia plus Singapore) rose from 57 per cent in 1980-1984 to 70 per cent in 1985-1989, but remained almost stable over the next period. This implies that the decline in the share of the other seven (from 38 to 26 per cent) was arrested, but the fact remains that these seven account for 45 per cent of the GDP and 43 per cent of the population of the region but have a much smaller share in trade. While some of the difference in performance can be accounted for by the transit trade of Hong Kong and Singapore, it is clear that the much better performance

Figure III.2. Share of major countries in merchandise exports of developing economies of the ESCAP region

(Percentage)



Sources: ESCAP secretariat calculations based on United Nations, *Monthly Bulletin of Statistics*, vol. L, No. 9 (September 1996); and IMF, *International Financial Statistics*, vol. XIIX, No. 11 (November 1996).

of a very few economies of the region has implications for the degree and speed of integration of many other economies into world and regional economy.

Table III.4 presents the export intensity indices[7] for the economies of the Asian and Pacific region. Increasing intensity of exports in a growing economy shows that this sector is driving the economy; however, an export intensity index may increase when there is negative GDP growth and the domestic economy is contracting faster than the export sector. A "high" export intensity index reflects the importance of the export sector of the economy in comparison with domestic demand; usually small economies such as Hong Kong, Singapore or most of the Pacific island countries have relatively high indices, especially in comparison with large economies such as China or India. Therefore, there is a need to look not only at the level of the index but also at the direction of change.

There are 10 out of the 31 economies listed with indices above 30 per cent and another 7 with indices above 20 per cent. The medium index is about 24 per cent, compared with a ratio of world trade to GDP of about 17 per cent, which can be interpreted to mean that in global terms the region is relatively trade-dependent. It is important to note that 14 of the economies reported in the table, or about half, have rising export intensity indices over the whole period, with 8 of these (Bhutan, China, Hong Kong, Malaysia, Mongolia, Papua New Guinea, Thailand and Viet Nam) recording increases of over 10 percentage points.[8] Eight economies recorded a significant decline in their export intensity indices (Brunei Darussalam, Iran (Islamic Republic of), Kiribati, Myanmar, Samoa, Taiwan Province of China, Tuvalu and Vanuatu), for reasons connected with maturing economies, natural disasters, depletion of natural resources, severe drops in the price of a major export, political events or, as seems to be the case for Vanuatu, because of a rapid growth in service exports, which are not included here.

To evaluate the move towards export expansion for future linkages, it is important to take into account the structure of markets for the exports of the economies in the region. This analysis has two dimensions; first, the general pattern of market concentration or dispersion, and second, changes in this pattern over time. From table III.5, which presents the overall world trade matrix, it is obvious that the economies in the region are a growing market for themselves; intra-developing country trade in the region grew from about 24 per cent of total exports in 1980 to 39 per cent in 1995. While, as expected, the developed economies still absorb a little over half of the exports from the developing economies of Asia and the Pacific, this percentage has been shrinking slowly (in 1980 it was 60 per cent) and regional intra-developing country trade is now significantly larger than the trade of the developing economies with the European Union (15 per cent) or North America (23 per cent) or Japan (12 per cent). These economies also constitute an important growing market for Japan, with their share of Japanese exports increasing from 28 per cent in 1980 to 38 per cent in 1995, and now accounting for a larger share than do the European Union or North America. A similar evolution can be seen for Australia and New Zealand; together these developed countries sent 22 per cent of their exports to the developing economies in the region in 1980 and 36 per cent in 1995, a significantly larger share than those to the European Union or North America, or even to Japan. However, Australia and New Zealand are very small markets for developing economies (about 2 per cent of the total exports of the region).

There are several conclusions that can be drawn from data on the pattern of trade separated between commodities and manufactured goods. First, the share of the intraregional developing country trade in commodities including fuels is slightly higher than that in manufactured goods (41 per cent as compared with 37 per cent in 1993) although both shares are rising slowly. However, when fuels are excluded from commodity trade, the percentages are almost identical (36 per cent for primary commodities and also rising). Second, for Australia and New

7 Defined as the exports of merchandise goods as a percentage of GDP.

8 The other seven are Bangladesh, India, Lao People's Democratic Republic, Nepal, Pakistan, Philippines and Sri Lanka.

Table III.4. Exports and imports of goods as a percentage of GDP

(Ranked on the ratio of exports to GDP, 1990-1995 average)

	Exports, f.o.b			Imports, c.i.f		
	1980-1984	1985-1989	1990-1995	1980-1984	1985-1989	1990-1995
Developing economies of the ESCAP region						
Singapore	139.0	141.5	134.5	176.8	159.0	148.2
Hong Kong	74.4	100.5	116.5	84.0	98.3	122.5
Malaysia	48.1	57.1	77.4	44.2	45.8	78.6
Brunei Darussalam	87.9	66.9	58.0	17.6	22.9	31.0
Papua New Guinea	33.5	41.3	47.3	45.0	44.9	32.6
Solomon Islands	46.0	44.9	43.3	52.1	56.7	49.8
Taiwan Province of China	48.0	47.2	40.3	40.9	34.9	35.8
Mongolia	20.1	21.6	36.7	29.1	34.0	37.5
Thailand	18.5	23.9	30.5	26.1	29.1	38.7
Fiji	31.8	29.6	30.1	44.4	38.5	45.1
Bhutan	10.8	22.3	28.6	40.6	41.5	42.5
Sri Lanka	23.3	21.0	26.3	38.5	30.9	37.6
Viet Nam	..	10.7	25.6	..	23.4	29.4
Republic of Korea	30.0	31.6	25.5	34.0	29.2	27.4
Indonesia	25.8	22.7	23.9	16.5	15.0	20.0
Maldives	21.7	33.1	22.3	79.5	77.0	93.7
Philippines	15.6	17.1	20.4	23.2	21.7	33.1
China	7.6	11.8	19.8	7.5	14.5	18.4
Lao People's Democratic Republic	7.3	6.0	15.6	25.9	19.5	29.3
Pakistan	9.9	11.6	14.4	20.2	18.3	19.1
Cambodia	..	..	14.4	..	9.5	21.8
Vanuatu	32.1	19.7	12.6	63.8	62.1	49.2
Bangladesh	6.2	6.4	9.3	18.9	16.7	17.8
Tonga	9.2	7.9	9.2	55.2	55.8	43.7
Nepal	4.7	5.5	8.8	17.7	18.7	25.7
India	4.7	4.6	7.6	7.8	6.9	8.7
Kiribati	15.0	7.3	6.4	50.2	36.8	52.4
Samoa	16.7	13.3	3.7	48.5	61.9	78.0
Iran (Islamic Republic of)	12.2	3.7	3.2	11.3	3.9	3.5
Tuvalu	31.0	6.2	2.4	77.4	62.3	51.4
Myanmar	6.6	2.1	1.0	5.4	2.3	1.3
Other members of ESCAP in Asia and the Pacific						
Russian Federation	..	..	26.6	..	..	17.0
New Zealand	23.7	20.8	23.4	24.5	20.0	22.0
Australia	12.9	13.9	14.9	14.6	15.8	16.0
Turkey	9.8	12.4	9.7	17.0	17.0	15.4
Japan	12.8	10.1	9.0	11.8	7.0	6.5

Sources: ESCAP secretariat calculations based on United Nations, *Monthly Bulletin of Statistics*, vol. L, No. 10 (October 1996); IMF, *International Financial Statistics Yearbook, 1995* and *International Financial Statistics*, vol. XLIX, No. 11 (November 1996); ADB, *Key Indicators of Developing Asian and Pacific Countries, 1996* (Oxford University Press, 1996); and World Bank, *World Tables 1995* (Baltimore, Maryland, John Hopkins University Press, 1995).

Table III.5. Percentage share of total merchandise exports by region and destination, Asian and Pacific region

(Selected years)

Origin	Destination		World	Developed market economy countries					Developing economies of the ESCAP region
				Total	European Union	North America	Japan	Australia, New Zealand	
World	1980	100		66.8	37.2	14.5	6.2	1.2	8.8
	1985	100		66.3	30.7	20.1	5.8	1.5	8.7
	1990	100		71.5	39.7	17.6	5.6	1.3	12.8
	1993	100		67.4	35.0	19.4	5.4	1.3	17.3
	1995	100		67.4	37.6	19.6	5.7	1.4	17.7
Developed market economy countries	1980	100		70.8	43.1	13.2	3.2	1.4	7.9
	1985	100		74.0	37.2	21.6	3.5	1.8	7.2
	1990	100		77.3	46.2	16.7	4.2	1.4	9.9
	1993	100		71.6	40.8	17.8	3.8	1.3	13.3
	1995	100		72.0	44.6	18.2	3.9	1.4	13.5
Japan	1980	100		47.5	14.0	26.3		3.1	28.4
	1985	100		58.6	11.4	40.1		3.7	19.3
	1990	100		59.3	18.8	34.0		2.8	31.4
	1993	100		52.3	15.8	31.2		2.5	37.7
	1995	100		52.3	16.7	31.2		2.5	37.7
Australia, New Zealand	1980	100		58.2	15.6	12.5	22.7	6.1	21.5
	1985	100		55.4	13.5	10.2	24.1	6.0	18.9
	1990	100		61.8	14.3	13.1	24.9	7.0	28.4
	1993	100		55.7	12.2	10.3	23.6	7.9	36.1
	1995	100		56.0	12.9	10.2	23.8	8.1	36.2
Developing economies of the ESCAP region	1980	100		60.2	15.6	19.9	20.2	2.5	24.1
	1985	100		63.5	11.5	31.1	16.3	2.3	20.8
	1990	100		57.2	15.4	23.5	14.4	1.9	33.3
	1993	100		53.4	14.6	22.9	12.1	1.9	37.3
	1995	100		52.4	15.0	22.5	12.0	1.9	38.8

Sources: ESCAP secretariat calculations based on UNCTAD, *Handbook of International Trade and Development Statistics*, 1989 and 1994; and United Nations, *Monthly Bulletin of Statistics*, vol. L, No. 6 (June 1996), special table D.

Zealand, the developing economies are more important markets for manufactured goods than they are for commodities, despite the relatively heavy concentration on commodity trade in the export basket of these countries (see table III.6). The developing economies in the region absorb about one third of Japanese manufactured exports, a larger proportion than either the European Union or North America. Third, the proportion of manufactured exports from the developing economies going to Japan is only about half of that to the European Union or North America, and the share has not been growing. However, Japan is clearly a very important market for commodities from the developing economies of the region, absorbing about one third of the total, the second largest share after exports among the developing economies themselves (40 per cent).[9] Box III.1 provides further details on the changing pattern of Japanese imports.

[9] A recent study of 16 major trading countries in the region reached the following conclusion on the composition of intraregional trade. "While the share of manufactures is increasing, its share in intraregional trade is significantly less than it is for interregional trade. Nearly 70 per cent of the exports of primary commodities of Asian and Pacific developing economies are consumed within the region (one third to Japan alone) while Europe and North America account for less than 20 per cent. With regard to manufactured goods, intraregional trade accounts for about only 40 per cent, and the United States and Europe absorb almost 50 per cent of the exports of the developing Asian and Pacific economies. (ESCAP, *Review and Analysis of Intraregional Trade Flows in Asia and the Pacific*, Studies in Trade and Investment, No. 6 (ST/ESCAP/1506).

Box III.1. The flying geese paradigm: the changing pattern of Japanese imports from East and South-East Asia

Japan is acknowledged as the lead economy in the flying geese pattern of industrial development in Asia, particularly East and South-East Asia. This pattern envisages that production is relocated from one economy (the lead economy) to other countries within the flying geese pattern in search of lower costs and much of the output is exported back to the lead economy. It is thus relevant to examine the changes in the structure of Japanese imports from its Asian neighbours. If the spread of industrial capacity is in line with this pattern, there should be a rising percentage of manufactured imports of various sorts from countries within the flying geese pattern that "inherited" industries from Japan.

Some evidence on this can be found in the table, which shows that there has, in fact, been a marked change in the structure of Japanese imports, with the share of manufacturing products increasing by 10 per cent in only five years, from about one half in 1990 to almost 60 per cent in 1995. Engineering products showed the most dramatic increase, the combined shares of machinery and metal products having increased from about one fifth to almost one third of the total imports. The table also shows that the Japanese manufacturing imports were increasingly sourced from East and South-East Asian economies; the combined market share of four ASEAN countries (Indonesia,

Percentage shares of East and South-East Asian economies in Japanese imports, 1990 and 1995

	Chemicals	*Machinery*	*Metals*	*Non-ferrous metals*	*Textiles*	*Miscellaneous*	*All manufactures*	*Non manufactures*	*Total value (millions of US dollars)*
1990									
China	**4**	**1**	**8**	**2**	**25**	**4**	**5**	**5**	**11 532**
Newly industrializing economies	**9**	**13**	**38**	**3**	**34**	**17**	**16**	**6**	**24 984**
Hong Kong	0	1	0	0	5	2	2	0	2 097
Republic of Korea	4	5	30	1	23	7	8	2	11 264
Singapore	3	2	0	0	0	1	2	1	3 413
Taiwan Province of China	2	5	7	2	6	7	5	2	8 210
ASEAN	**2**	**4**	**5**	**6**	**5**	**8**	**5**	**16**	**23 414**
Indonesia	0	0	3	3	1	4	2	9	12 138
Malaysia	1	1	1	1	1	1	1	4	5 197
Philippines	0	1	0	2	1	1	1	1	2 084
Thailand	1	2	1	0	2	3	2	2	3 995
Others	**85**	**82**	**50**	**90**	**37**	**71**	**74**	**73**	**165 771**
World	100	100	100	100	100	100	100	100	
Total value (millions of US dollars)	**15 472**	**39 355**	**4 514**	**9 502**	**12 362**	**32 564**	**113 769**	**111 933**	**225 701**
Percentage of total value	**7**	**17**	**2**	**4**	**5**	**14**	**50**	**50**	**100**
1995									
China	**5**	**6**	**11**	**12**	**51**	**16**	**14**	**6**	**36 354**
Newly industrializing economies	**8**	**17**	**18**	**9**	**14**	**15**	**15**	**9**	**41 619**
Hong Kong	0	1	0	3	2	2	1	0	2 764
Republic of Korea	4	3	12	4	10	5	5	5	17 443
Singapore	2	6	0	0	0	1	3	1	6 928
Taiwan Province of China	2	7	6	2	2	6	5	3	14 484
ASEAN	**3**	**10**	**5**	**7**	**7**	**14**	**9**	**15**	**38 745**
Indonesia	1	1	3	1	3	6	2	7	14 359
Malaysia	1	4	1	1	1	4	3	3	10 663
Philippines	0	2	1	0	1	1	1	1	3 509
Thailand	1	4	1	4	3	4	3	3	10 214
Others	**83**	**67**	**65**	**71**	**28**	**55**	**62**	**71**	**222 516**
World	100	100	100	100	100	100	100	100	
Total value (millions of US dollars)	**24 830**	**85 990**	**20 044**	**6 286**	**24 869**	**38 602**	**200 621**	**138 613**	**339 234**
Percentage of total value	**7**	**25**	**6**	**2**	**7**	**11**	**59**	**41**	**100**

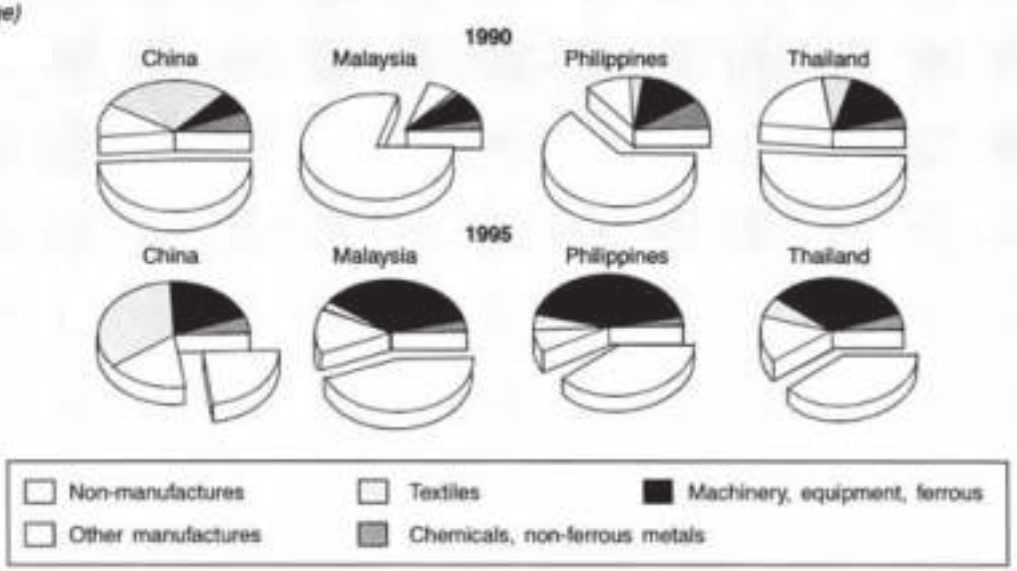
Source: ESCAP secretariat calculations based on Government of Japan, *Japan Statistical Yearbook, 1991*, table 10-9 and ibid., 1997, table 12-9.

(Continued overleaf)

(Continued from preceding page)

Changing export structure of East and South-East Asia to Japan, 1990 and 1995

(Percentage)



Source: ESCAP secretariat calculations based on Government of Japan, *Japan Statistical Yearbook, 1991*, table 10-9, and ibid., 1997, table 12-9.

Malaysia, the Philippines and Thailand), China and the NIEs (Hong Kong, Republic of Korea, Singapore and Taiwan Province of China) jumped from one quarter to almost 40 per cent of Japan's total imports of manufacturing products.

The increasing competitiveness of China and the group of four ASEAN economies, partly enhanced by Japanese FDI, is striking.[a] They have respectively increased their market share in machinery from 1 and 4 per cent in 1990 to 6 and 10 per cent in 1995. Among the ASEAN countries, Malaysia and Thailand are noted for the substantial increase in their market shares for these "highly dynamic products" (see also box III.2). It is worth noting that their gains in the Japanese import market share included not only skilled engineering products such as machinery and metals but also lower skilled products. About 60 per cent of textile imports to Japan originated from China and the four ASEAN countries in 1995 as compared with about 30 per cent in 1990, with the NIEs and the rest of the world losing their market shares. A similar pattern was apparent in miscellaneous manufactured products.

The flexibility of the Asian economies in responding to changes in market opportunities in Japan was remarkable.[b] During the past 15 years or so, there have been major structural changes in their exports to Japan, which have been increasingly dominated by manufacturing products. During the first half of the 1990s, the change in the composition of their exports to Japan became dramatic. As shown in the figure, about half of China's exports to Japan in 1990 were still non-manufactured products, but this proportion dropped to below one fourth in 1995. The percentage decline in non-manufactured exports from Malaysia was also very large: within the same period it dropped from as high as 80 per cent to about 45 per cent. Further, it is noted that among the ASEAN economies, Malaysia, the Philippines and Thailand have recently demonstrated enhanced technological capability: in 1995, a sizeable portion of their exports to Japan was in highly skilled engineering products. As shown in the figure, the combined shares of machinery, equipment and metal products have increased dramatically within a five-year time-span.

Thus there is considerable evidence of the successful implementation of the flying geese pattern among these countries. Nevertheless, the pattern of Japanese imports from many other developing economies in the Asian and Pacific economies remains dominated by non-manufactured goods, mainly foods and raw materials.

[a] The strategy of the Japanese transnational companies, in contrast to that of the American ones has been such that a growing proportion of their overseas output was exported to Japan. See, for example, "Balancing act", *The Economist*, 4-10 January 1997, p. 73.

[b] N. Fujita, "Growth factors of the Japanese imports from East Asian countries: a breakdown of trade matrices" and "Revised memo for the EAEA conference", table 2, presented at the Fifth Convention of the East Asian Economic Association, Bangkok, 25-26 October 1996.

A disaggregation of trade by product or product groups illustrates whether countries have succeeded in diversifying their export package or whether they are still vulnerable to events in specific products markets. Table III.6 shows the dependence of the economies of the ESCAP region on the

Table III.6. Percentage share of primary commodities in all merchandise trade values, ranked on 1993 data

	Exports of primary commodities, including fuels, as a percentage of total exports				
	1980	*A 1985*	*1990*	*B 1993*	*B-A*
Developing economies of the ESCAP region					
Myanmar	93.5	93.9	99.0	99.0	5.1
Solomon Islands	93.4	100.0	99.0	99.0	-1
Afghanistan	81.9	94.1	99.0	97.2	3.1
Brunei Darussalam	97.3	98.7	97.5	96.2	-2.5
New Caledonia	95.9	87.6	99.0	94.7	7.1
Samoa	92.5	89.0	90.0	93.9	4.9
Iran (Islamic Republic of)	91.3	100.0	98.6	87.3	-12.7
Tonga	99.0	89.0	78.5	85.7	-3.3
Maldives	89.5	67.3	72.6	83.0	15.7
Mongolia	-	20.1	72.4	67.6	47.5
Fiji	69.6	54.7	59.0	66.6	11.9
Vanuatu	82.0	82.5	69.4	63.1	-19.4
Viet Nam	42.1	91.7	54.6	60.3	-31.4
Papua New Guinea	90.4	97.1	83.7	47.5	-49.6
Indonesia	97.6	87.4	63.9	46.7	-40.7
Lao People's Democratic Republic	44.5	36.3	89.8	45.7	9.400
Kiribati	10.9	84.9	71.4	45.4	-39.5
Cambodia	99.0	62.7	99.0	42.1	-20.6
Cook Islands	66.2	55.7	34.8	38.1	-17.6
Malaysia	80.5	72.0	45.1	28.6	-43.4
Thailand	70.3	60.3	35.3	27.4	-32.9
India	39.2	44.1	28.5	25.3	-18.8
Philippines	64.2	44.3	31.1	23.8	-20.5
Singapore	41.7	38.5	25.9	19.3	-19.2
China	47.5	48.3	26.7	19.1	-29.2
Guam	99.0	2.8	22.2	18.8	16
Sri Lanka	81.9	72.4	41.6	18.0	-54.4
Pakistan	45.1	30.4	20.9	17.0	-13.4
Nepal	63.2	51.2	23.6	15.1	-36.1
Bangladesh	28.6	36.7	20.7	14.1	-22.6
Taiwan Province of China	12.1	..	6.9	7.2	7.2
Republic of Korea	9.4	8.1	5.8	6.0	-2.1
Hong Kong	5.9	6.7	5.8	4.3	-2.4
French Polynesia	26.8	15.2	6.5	4.0	-11.2
American Samoa	2.9	7.9	3.0	3.8	-4.1
Nauru	99.0	45.3	-	-	..
Other members of ESCAP in Asia and the Pacific					
New Zealand	74.7	71.1	70.0	68.8	-2.3
Australia	77.0	84.7	68.6	62.0	-22.7
Turkey	73.2	38.0	31.5	27.7	-10.3
Russian Federation	-	-	-	7.4	7.4
Japan	3.5	2.2	2.1	2.1	-0.1

Sources: ESCAP secretariat calculations based on UNCTAD *Commodity Yearbook*, 1989 and 1995.

export of primary commodities, including fuels. High dependence on commodities can be taken as a signal of both vulnerability to the excessive price fluctuations that have plagued commodity markets and lack of progress in industrial development. It is interesting to note that six economies remain dependent on commodities for over 90 per cent of their export earnings, and another three for over 80 per cent. These are either fuel exporters (Brunei Darussalam and the Islamic Republic of Iran), Pacific islands (New Caledonia and Tonga) or least developed countries (Afghanistan, Maldives, Myanmar, Samoa and Solomon Islands). Australia and New Zealand have about the same dependence as several other economies (between 60 and 70 per cent). It can be hypothesized that the 13 economies with dependence on commodities, including fuels, of over 50 per cent remain vulnerable to events in commodity markets. It should be noted that the fast-growing economies of East and South-East Asia, except Indonesia, all have commodity dependence of less than 30 per cent.

A decline of over 10 percentage points in commodity dependence during a decade is a significant indicator of the rising importance of manufactured exports. The economies which have succeeded in doing this include Bangladesh, Cambodia, China, Cook Islands, French Polynesia, India, Indonesia, Iran (Islamic Republic of), Kiribati, Malaysia, Nepal, Pakistan, Papua New Guinea, Philippines, Singapore, Sri Lanka, Thailand, Vanuatu and Viet Nam (19 out of 36 developing economies listed in table III.6). This is a very impressive performance. However, these results then have to be compared with the growth rates of exports to see if the decline is due to export expansion in other products or a faltering of exports generally. By referring to table III.2 it is clear that these are all success stories, with the exception of Vanuatu.[10]

Another way of evaluating the export vulnerability of countries is to calculate the dependence on a limited number of products; the lower this dependence, the more diversified and so robust is the export basket of a country. Unless there is a generalized world recession, the markets for different products do not move in parallel and so decline in one export is compensated by an increase in others. A high export dependence on a limited number of products is a signal of vulnerability to significant variations in export earnings and economic performance, independently of whether these are commodity or manufactured products. Annex table III.1 lists the two or three major export products in 1981-1982 and 1991-1992 of the 25 developing countries for which consistent date are available. From this table, it can be seen whether the important individual products have remained the same, as for example, for Brunei Darussalam, Indonesia or Solomon Islands, although with a different order of importance, or changed dramatically, as, for example, for the Philippines, Thailand or Tonga. The picture is one of considerable change in export structures, although for most countries one or two products, commonly commodities, have remained in the top three exports.

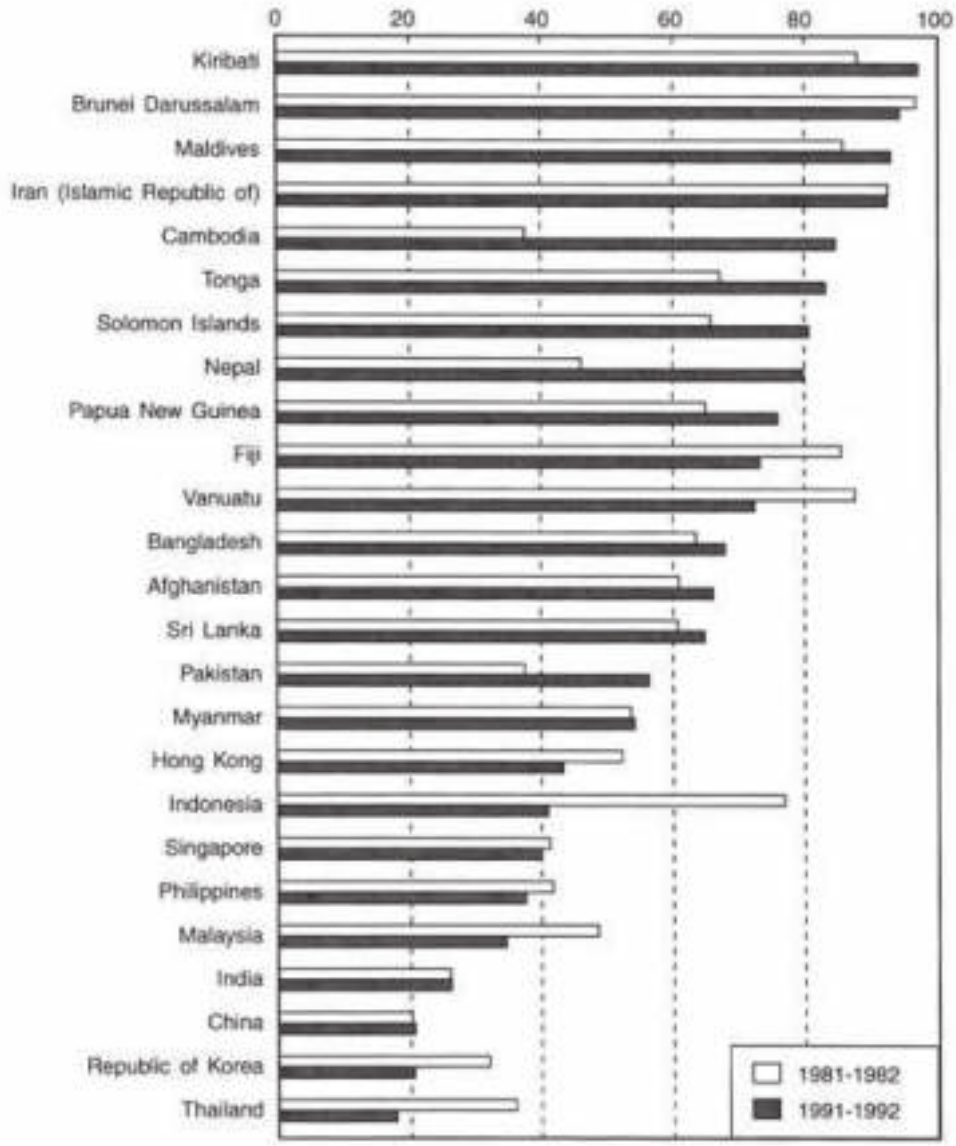
Figure III.3 presents a summary of this information in the form of an index of dependence on three most important export products ranked in descending order.[11] For 11 countries, this index was above 70 per cent in 1991-1992, signalling a high degree of concentration of exports. Six of these countries are least developed, two are petroleum exporters and the others are Pacific islands. Out of these 11, for 3 economies, the index remained almost stable and for 6 it increased. These are the only economies other than Pakistan registering a significantly increasing index. It can be hypothesized that a rising index is not a positive sign in terms of exposure to risk and sustainability of export earnings. Overall, 7 out of 26 countries had significantly declining indices, with that for Indonesia being the largest. These were mainly, as expected, the ASEAN and East Asian economies, but also Fiji and Vanuatu.

It is important to note that in terms of the composition of trade, electronic product exports originated mainly in the newly industrializing economies and the ASEAN-4 (Indonesia, Malaysia, the Philippines and Thailand) and China. The main manufactured exports of the region were textiles, electronics and miscellaneous items (toys, sporting goods, footwear, watches and clocks, travel goods, plastic articles and jewellery).

[10] Vanuatu has diversified into services.

[11] This index is independent of the composition of the three products and therefore measures the degree of concentration rather than the diversification from traditional export bundles.

Figure III.3. Percentage of total exports accounted for by three major products



Source: ESCAP secretariat calculations based on UNCTAD, *Handbook of International Trade and Development Statistics*, 1984, 1985, 1993 and 1994.

The export situation of the Central Asian republics was not included above as data only exist for the last few years. Table III.7 presents a summary picture for these economies. Their total exports in 1995 were around $12 billion, or about 2 per cent of the regional exports. These exports have been growing rapidly with rates of change of over 50 per cent for all economies in 1994, but much more slowly in 1995. The export intensity of these countries remains rather low, all indices being below 20 per cent, except for Turkmenistan, even though these indices have been increasing rapidly.

Table III.7. Merchandise trade of the Central Asian republics

	Value (millions of US dollars)		*Annual percentage change*		*Percentage of GDP*		*Commodity dependence*
	1994	*1995*	*1994*	*1995*	*1993*	*1994*	*1995*
Merchandise exports							
Armenia	232	248	673.3	6.9	1.4	8.9	..
Azerbaijan	637	550	81.5	-13.7	7.0	18.0	56.6
Kazakstan	3 231	5 064	111.3	56.7	14.2	17.8	81.8
Kyrgyzstan	340	380	203.6	11.8	2.9	12.8	57.9
Tajikistan	413	707	57.0	71.2	10.4	20.6	..
Turkmenistan	2 010	1 939	91.6	-3.5	20.3	39.0	72.3
Uzbekistan	3 044	3 100	322.2	1.8	3.5	14.2	24.7
Total	**9 907**	**11 988**	**144.3**	**21.0**	**8.1**	**17.8**	
Merchandise imports							
Armenia	415	661	382.6	59.3	3.9	15.9	..
Azerbaijan	791	681	228.2	-13.9	4.8	22.3	65.8
Kazakstan	4 499	3 882	810.7	-13.7	4.6	24.8	50.3
Kyrgyzstan	369	439	229.5	19.0	2.9	13.8	63.3
Tajikistan	899	690	140.4	-23.2	14.8	44.7	..
Turkmenistan	894	777	78.4	-13.1	9.7	17.3	33.9
Uzbekistan	2 479	2 900	158.8	17.0	4.7	11.5	40.8
Total	**10 346**	**10 030**	**274.0**	**-3.1**	**5.5**	**18.6**	

Sources: ESCAP secretariat calculations based on United Nations, *Monthly Bulletin of Statistics*, vol. L, No. 10 (October 1996) and World Bank, *World Development Report*, 1995 and 1996.

This shows that they have quite a long way to go before being able to participate effectively in the global economy. The exports of these economies have been quite concentrated in terms of products, with commodity exports still largely dominating in all countries except Uzbekistan.

Exports of services

Disaggregated data on services trade have been collected only for certain countries and only for the recent past. Total services trade was estimated to be $1,099 billion in 1994 and growing at the rate of over 9 per cent a year, or significantly faster than global trade in merchandise goods. The share of Asia and the Pacific in this total is estimated at about 20 per cent, a ratio smaller than the region's share in merchandise trade but one which is increasing rapidly. Table III.8 provides a listing of the values in 1994 and growth rates of service exports between 1990 and 1994 for the major exporters of the region; the Asian and Pacific region contained 6 of the top 20 exporters and 9 out of the 10 fastest growing exporters of services.

About 40 per cent of the world trade in services is business services (telecommunications, financial services, construction etc.), 30 per cent is related to travel (including travel for leisure, education, health and business) and the balance to transport, freight and insurance. In general, Asian and Pacific economies have relatively low net export ratios in absolute terms. This indicates a high degree of two-way trade in services, though not necessarily in the same ones. In terms of export intensity, service exports are very significant for six economies with the average ratio of service exports to GDP in 1990-1993 exceeding 20 per cent: four island countries with important tourist industries, and Hong Kong and Singapore which provide a range of services. For six other economies, the ratio of

Table III.8. Service exports from selected economies of Asia and the Pacific

	Value (millions of US dollars) 1994	*Percentage share of world 1994*	*Growth rate 1990-1994*
Developing economies of the ESCAP region	**149 242**	**13.6**	**16.5**
Hong Kong	32 538	3.0	15.0
Singapore	23 366[a]	2.1	15.2
Republic of Korea	18 816	1.7	15.4
China	16 503[a]	1.5	30.7
Taiwan Province of China	13 458	1.2	13.5
Thailand	11 822	1.1	17.3
Philippines	6 768[a]	0.6	21.6
Malaysia	6 546[a]	0.6	18.0
Indonesia	4 797[a]	0.4	20.8
Total	134 614	12.2	16.9
Developed economies of the ESCAP region	**75 845**	**6.9**	**8.4**
Australia	13 526	1.2	9.1
Japan	57 230	5.2	7.9

Source: ESCAP secretariat calculations based on WTO, *International Trade: Trends and Statistics 1995.*

[a] Data from IMF, *Balance of Payments Statistics Yearbook*, 1996, part 2.

service exports to GDP is over 6 per cent: three South-East Asian countries and three others where tourism is important. In 1993 and 1994, Asia was the region with the most dynamic trade in commercial services.

Imports of goods and services

As every export from one country is another country's import, an important part of the linkages being built in the region will depend on the pattern of imports. At the global level, trade has to balance, but this is not true at the country or regional level. Nevertheless, large bilateral trade imbalances are a source of friction between countries. It is interesting to observe from figure III.1 that the share of the developing economies in Asia and the Pacific in world imports of goods and services is a little higher than its share of world exports, with that for the developing economies of the region being just over 15 per cent. Twenty-four developing countries in the region exceeded the world average growth rate of imports of merchandise goods, having a large overlap in the list with those experiencing rapid export growth (see table III.2). The same 12 countries that account for almost all of the exports account for almost all of the imports – over 96 per cent in the period 1990-1995.

It is relevant to consider the import intensity indices of countries as another measure of their openness to the rest of the world. Whereas many researchers use total trade (exports plus imports) to GDP ratio to measure trade exposure or openness, the results are difficult to interpret for countries such as those in the Pacific subregion, where imports are often several times larger than exports. While these countries may be open to imports, they are not necessarily able to develop exports to match, or lack a very conducive policy for export development and often run very large current account deficits year after year, supported by aid flows and remittances. Their trade exposure figures have a very different meaning from those in most other countries, where exports and imports are of the same order of magnitude most of the time.

In this regard, several observations can be made from table III.4. First, for many economies the average import intensity index is larger than the average export intensity index, or imports constitute a larger percentage of GDP than exports. For the period 1990-1995, for only five economies was the import intensity index lower than the export intensity index (Brunei Darussalam, China, Indonesia, Papua New Guinea and Taiwan Province of China). For another 13 economies, the difference was less than 10 percentage points, whereas in 5 Pacific island countries the import intensity index was more than 30 percentage larger than the export intensity index.

Most imports of the developing countries of the region are manufactured goods, either final consumer goods, intermediate products or capital goods. For all but a handful, imports of primary commodities (excluding fuels) constitute between 10 and 20 per cent of total imports. This is much lower than the proportion in Japan (over 30 per cent). For some individual countries a significant proportion of their imports came from the region. This proportion exceeded 50 per cent for 12 economies, Bangladesh, China, Fiji, Hong Kong, Indonesia, Malaysia, Papua New Guinea, Philippines, Republic of Korea, Singapore, Sri Lanka and Taiwan Province of China.[12]

Imports into the Central Asian economies have been very variable, with a significant decline in four countries in 1995. Import intensity is generally higher than export intensity, reflecting the difficult economic situation of these economies.

POLICY INFLUENCES ON TRADE PERFORMANCE

The above pattern of increasing trade intensity and increasing diversification in products and markets in many countries of the region has its roots in several types of policy initiatives. In the following sections an attempt is made to bring together the major trends in policy stances relevant to increasing linkages and integration, classified for convenience under four headings: liberalization of trade regimes at the national level, trade-related domestic policy liberation, regional trade arrangements, and trade liberalization at the global level.

Liberalization of trade regimes at the national level

While practically all countries in the region had highly protected domestic economies a couple of decades ago, most have liberalized their frontier barriers considerably. The moves toward a more open economy have been a deliberate change in policy in line with the desire to use trade as an engine of growth. As such it is quite distinct from earlier policy stances on trade barriers which were focused on reducing barriers in export markets, mainly in OECD countries, while maintaining and legitimizing protective regimes in developing countries. Many of these changes were made independently of the GATT rounds of multilateral trade negotiations. The result had been to help integrate developing countries into the negotiating process, as evidenced by the participation of a significant number of them in the Uruguay Round.

Annex table III.2 provides a summary picture of the trade barriers currently existing in a selection of countries of the region. There is evidence of at least four distinct types of trade regime. First, Japan has a distinctive type of trade regime in Asia. In terms of official trade barriers, the Japanese market is as open as the other G7 countries; there are very few quantitative restrictions and tariffs are very low. Yet, the import-GDP ratio is substantially lower in Japan than in other OECD countries. The existence of a specific type of corporate network among Japanese firms and significant price wedges between domestic and imported goods of comparable quality leads many trade analysts to believe that the Japanese market is not as open to foreign competition as might otherwise be expected from a very low level of official trade barriers. Hong Kong and Singapore represent a second type, which is, essentially, an open free-trade regime with practically no official barriers. A third group includes Indonesia, Malaysia, Philippines, Republic of Korea, Sri Lanka, Taiwan Province of China and Thailand, where tariffs have been reduced to moderate levels and quantitative restrictions are the exception rather than the rule. A fourth group includes Bangladesh, China, India, Pakistan and Viet Nam, as well as most Pacific island countries, where, despite some reductions, tariff rates remain relatively high and, in many instances, quantitative restrictions still constitute important barriers to trade.

12 ESCAP, *Review and Analysis...*

GATT/WTO provided a list of 63 countries or areas that have undertaken unilateral reductions in protection vis-à-vis all trading partners since the start of the Uruguay Round, 9 of these being in East and South-East Asia,[13] namely, China, Indonesia, Japan, Macau, Malaysia, Philippines, Republic of Korea, Singapore and Thailand, and 4 in South Asia, namely, Bangladesh, India, Pakistan and Sri Lanka. In addition, Japan has taken measures to free trade in certain commodities after bilateral negotiations with the United States of America; for example, the 1988 negotiations on beef between the United States, Australia and Japan, and the 1990 Structural Impediments Initiative. Many of the reductions in Asian countries have been substantial and comprehensive in comparison with those in Europe and the United States. In some developing countries, such as Indonesia, Sri Lanka and Thailand, the average tariff rates currently applied are already lower than the post-Uruguay Round average bound tariff rates. In East and South-East Asia (except the Philippines), average tariff rates had come down to relatively low levels, 10 to 15 per cent, by the early 1990s. Yet, there remain significant "peaks" in tariff structures and the dispersion of tariff rates are large as well.[14] Moreover, in the case of primary and processed commodities, most Asian countries (including Japan) tend to set higher tariffs according to stages of processing and such tariff escalation is often reinforced by the use of non-tariff barriers on processed goods; food and energy products are cases in point.[15] Similar patterns of tariff escalation are found in most developed countries, and have been a source of grievance for developing countries that are making efforts to process their commodities before export. Most countries in South Asia have only recently begun to liberalize their trade policies and it will take some time before the structure of trade regimes for this subregion resembles those of the rest of Asia.

Measures to reduce tariffs have done a great deal to decrease the transaction costs of international trade and thus constitute a necessary step in closer integration with the regional and the global economy. The focus of attention is now shifting to non-tariff barriers. In many ways, such barriers create far greater transaction costs than tariff barriers because in the case of non-tariff barriers the market mechanism is completely circumvented, whereas in the case of tariff barriers it is merely distorted. Since the mid-1980s, the incidence of quantitative restrictions has gone down to less than 5 per cent in major East and South-East Asian economies, except Viet Nam, where the two-tier system of permits and licences constitutes an important non-tariff barrier.[16] Non-tariff barriers in ASEAN fell even faster than tariffs over the period 1984-1987 to 1991-1993, from 93 to 7 per cent in Indonesia, from 8 to 5 per cent in Malaysia and from 20 to 8 per cent in Thailand, on a coverage basis.[17] In South Asia, too, major progress was made in the dismantling of quantitative restrictions during the same period. In India, however, licensing restrictions remain extensive and significant on imports of final consumer goods.[18] In China, the scope of mandatory import planning had been cut back to less than 20 per cent of total imports by 1993, but import licensing was still imposed on some 53 product categories, accounting for 30 per cent of total imports in 1993.[19]

The movement towards liberalization at the national level of trade barriers of various sorts which has progressed at a varying pace in the region is a clear demonstration of the commitment of countries

---

13 GATT, *International Trade 1991-92, Trends and Statistics* (Sales No: GATT/1992-6), appendix table.

14 J.M. Dean, S. Desai and J. Riedel, *Trade Policy Reform in Developing Countries since 1985: Review of the Evidence*, World Bank Discussion Paper No. 267 (Washington DC, 1994).

15 R. Safadi and A. Yeats, "The escalation of Asian trade barriers", *Asian Economic Journal*, vol. 8, No. 2 (July 1994).

16 I. Probert, *Viet Nam: Open for Business*, Euro-Asia Centre Research Series, No. 32, European Institute of Business Administration, Fontainebleau, 1994.

17 P. Petri and M. Plummer, *The Multilateralization of Regional Preferences. Evidence from the Asia-Pacific*, Brandeis University Working Paper (Waltham, Mass.), March 1996.

18 I.J. Ahluwalia, "India's opening up to trade and investment", paper presented at an informal policy-dialogue meeting on India's policy reforms for structural adjustment and competitiveness, organized jointly by the OECD Development Centre and the Centre for Policy Research, New Delhi, 6-7 March 1995.

19 W. Tseng and others, *Economic Reform in China: A New Phase*, IMF Occasional Paper No. 114 (Washington DC, 1994), pp. 4-5.

to participating in the global trading market place. This liberalization has almost always been accompanied by moves towards realistic exchange rate policies. In most countries, exchange rates under flexible pegged regimes have been depreciating mildly, in concert with moves towards export stimulation. In those with relatively open capital accounts where inflows of foreign funds have led to appreciation in the exchange rate, measures have been taken to stem the degree of appreciation. Thus, exchange rate policies have been kept more or less consistent with trade policies.

There have also been efforts to devise ways of providing trade finance (pre-export credits etc.) for the private sector operators.[20] In most of the more advanced developing countries, commercial banks were the major providers of export finance. (The range of credits offered by a commercial bank network is generally a reflection of the level of development of the economy.) Refinance facilities were generally available to commercial banks from central banks. Some economies have specialized export credit agencies or export-import banks; for example, India, Republic of Korea, Taiwan Province of China and Thailand, and at least three others, Indonesia, Malaysia and Philippines are considering setting up such banks.

It should be noted that there are few private sector financial entities willing to take up this challenge of supplying export finance for small and medium-sized enterprises even in developed countries, and governments have been obliged to be the main suppliers. In most countries it is the availability rather than the cost of export finance that has been a barrier to further expansion of exports, especially for small and medium-sized trading firms, mainly owing to fund constraints and their lack of the physical collateral demanded by banks. Many financial intermediaries are unwilling to assume the risk of providing export credit, owing *inter alia*, to inadequate refinance facilities and the absence of guarantee mechanisms. There are also problems associated with delays and inflexibility in the provision of export finance by banks, and a lack of information available to those interested on where and how to obtain credit.

The increasing availability of modern telecommunications, and risk management tools, facilitates access to credit information and enables trade financiers to tailor their transactions to the specific needs of the trading counterparts. The possible combinations of funding and risk management techniques available today number in the thousands. Some financing techniques involve funding only, while others, such as factoring, incorporate both financing and credit intermediation. There is thus need in the developing economies of and the Pacific Asia to increase access to these new forms of financing and so improve the delivery mechanisms for pre-shipment export financing, short-term, post-shipment export financing, as well as structured finance techniques used in medium- and long-term financing, in order that the lack of these does not become a severe impediment to increased trade.

Trade-related domestic policy liberalization

Practically all domestic policy reforms undertaken in countries of the region have a direct or indirect bearing on their trade. For example, financial sector reform and liberalization, a review of which was featured in the 1995 *Survey*, is important because of the need for investors to raise finance to build up export capacity (for more on this issue, see chap IV) for producers to borrow to finance (imported) inputs, for exporters and importers to have easy access to short-term finance to conduct trade deals etc. Reforms undertaken to promote the role of the private sector (for a review of measures taken in this regard, see the 1996 *Survey*) are crucial as it is usually the private sector that is able to take advantage of new export opportunities. Policies of reform and/or privatization of state enterprises involved in productive activities are in general trade-stimulating through effects on improved efficiency and productivity. Reforms of state trading agencies help to reduce their monopoly controls over exports and imports of many goods and so also have a positive effect on trade flows. Reform of the education system is vital to improve the skill package of those involved in production for export; liberalization of the domestic prices and pricing system allows producers of exports to acquire inputs on a competitive basis etc. Most crucially, following conducive macroeconomic policies to maintain low inflation and a competitive exchange rate allows the export sector to perform according to its comparative advantage.

---

20 See ESCAP, *Regional Cooperation in Export Credit and Export Credit Guarantees*, Studies in Trade and Investment, No.2 (ST/ESCAP/1438). This study surveys 13 countries in Asia.

Furthermore, besides liberalization measures, many governments introduced selected policy measures to support their export industries in their efforts to diversify markets, develop competitive products and meet international standards of various sorts. Such measures, which create an enabling environment, have included the delivery of services by export promotion agencies, fielding trade missions overseas, particularly in new markets, attaching of commercial counsellors to diplomatic missions, undertaking market surveys, instituting incentives for firms to qualify for ISO certification, establishing quarantine and other inspection facilities which meet international standards, sponsoring research and testing for the development of new technologies, new products and so on.

Governments have also reformed and liberalized investment regimes, particularly their trade-related measures, in order to attract FDI in export industries. For example, many have permitted duty drawbacks on imports which are inputs to exports, and exempted such inputs, from both local or imported sources, from various domestic excise taxes. Export-related investments have been granted tax holidays and preferential access to domestic credit, especially short-term credits such as pre-shipment loans, often at subsidized interest rates. While the effectiveness of some of these measures has been questioned, there was a clear bias in the investment regimes towards export-oriented investment from any source.

The varying policy strategies followed in the East and South-East Asian economies have been analysed in depth in many research works, including the UNCTAD *Trade and Development Report 1996*[21] and do not need to be repeated here. The conclusion of the report was that "At the core of East Asian success lies a set of institutions which keep policy makers connected to business while still enabling governments to propose and implement appropriate measures directed at tackling a series of interrelated institutional and structural obstacles that can seriously hold back the process of investment, technological progress and exporting in a late-industrializing country".[22] Thus, the whole gamut of reforms have been accompanied by adequate and appropriate institutional development to facilitate the implementation of policies in an effective manner.[23]

It has been claimed that there are three major strategies to help an economy to be dynamic and delay the onset of diminishing returns: (i) improvement in education, (ii) expansion in domestic research and development, and (iii) an increase in the openness of the economy, including promotion of exports, imports and FDI.[24] It would appear to date that most countries in East and South-East Asia have relied on the first and the third but are currently moving towards the second. However, the progress of similar types of reforms in other parts of the region is somewhat slow. While many of such reforms are in progress in South Asia and some countries such as China and Viet Nam, others among the least developed and Pacific islands and in Central Asia, for example, have yet to realize sufficient progress. It should be recognized that liberalization, institutional development and the undertaking of initiatives to support trade are much more difficult and costly in terms of human resources in small countries. Nevertheless, they are all making moves in the same direction and deserve continued support in the process.

Arrangements affecting regional trade

The formula of a subregional customs union or free trade area, or a looser arrangement, has often been postulated as a precursor to more global integration, a tactical negotiation stance or as a form of survival in a competitive trading environment. The

21 UNCTAD, op. cit., pp. 72-158.

22 Ibid, p. 128.

23 One point of view is that these domestic reforms to facilitate taking advantage of trade and investment opportunities have "energized Asian development by providing a critical interface with the global economy, allowing regional economies to profit from static and dynamic growth catalysts, from a more efficient allocation of resources, directed by international prices, technology transfer, economies of scale and other sources of greater efficiency and productivity. And the policy transition in Asian developing countries has been extremely rapid, surprisingly comprehensive and abrupt, particularly in comparison to the historical experience of developed OECD countries", Plummer, op. cit., pp. 2-4.

24 Hsiao and Hsiao, op. cit. p. 5.

existing regional arrangements in the region are AFTA, CER, SAPTA, the ECO Protocol on Preferential Tariffs and the Melanesian Spearhead Group. There are also other less formal trade-related arrangements, including APEC and the various Asian growth areas in which there is cross-frontier co-operation between governments. All these arrangements differ substantially in terms of membership, coverage as regards goods, services and factors, instrument coverage, depth of cuts in barriers and other impediments to trade in goods and services, factor movement and relationships to non-members.

While considerable attention has been paid to these regional arrangements, a very revealing characteristic of the current trade patterns in Asia and the Pacific is the low degree of intra-subregional trade. Intra-SAARC exports comprise about 4 per cent of total exports of SAARC members, intra-ECO exports about 5 per cent, and intra-Pacific exports are almost as insignificant (see table III.9). Intra-ASEAN trade amounts to about 22 per cent of total exports. Intra-CER trade accounts for less than 5 per cent of the trade of Australia and about 20 per cent of that of New Zealand. There are three basic reasons for this; the package of export products offered by members of the regional trade agreements are similar; their import demand patterns are for capital goods and finished products most often not produced by any member of the region trade agreement; and the actual degree of meaningful trade liberalization among themselves is low, with the very recent exception of ASEAN. Trade between the regional groupings has also been dominated by certain bilateral flows. For instance, India accounts for most of the SAARC trade with ASEAN, while Singapore accounts for most of the ASEAN trade with SAARC. Some limited trade (and investment) links exist between ASEAN and the Pacific. Trade between ECO and SAARC is minimal. At the same time, the trade of all these subregions with East Asia (China, Hong Kong, Republic of Korea and Taiwan Province of China) is larger than their intra-trade, except for ASEAN. Thus it can be hypothesized that the developing economies in East Asia are offering the types of products desired by these other countries and tend to demand the sorts of products produced by them.

Table III.9. Inter-subregional merchandise trade flow matrix, 1995

(Millions of US dollars)

From \ To	ASEAN	SAARC	ECO	South Pacific Forum[a]	East Asia[b]	Total Asia and the Pacific[c]	Total exports
ASEAN	68 470	6 847	2 431	397	48 415	182 054	311 489
	(22.0)	(2.2)	(0.8)	(0.1)	(15.5)	(58.4)	(100)
SAARC	2 728	2 020	905	5	3 945	13 218	45 739
	(6.0)	(4.4)	(2.0)	(0.01)	(8.6)	(28.9)	(100)
ECO	1 703	1 241	2 525	1	3 682	12 584	56 293
	(3.0)	(2.2)	(4.5)	(0.01)	(6.5)	(22.4)	(100)
South Pacific Forum[a]	218	9	1	12	357	2 540	3 494
	(6.2)	(0.3)	(0.03)	(0.34)	(10.2)	(72.7)	(100)
East Asia[b]	50 676	6 692	3 826	99	163 473	305 240	559 325
	(9.1)	(1.2)	(0.7)	(0.03)	(29.2)	(54.6)	(100)

Sources: ESCAP secretariat calculations based on IMF, *Direction of Trade Statistics Yearbook, 1996* (Washington DC, 1996); and *Monthly Bulletin of Statistics of the Republic of China*, vol. XXII, No. 7 (September 1996).

Notes: The figures in parentheses show the percentage.

[a] Developing economy members only.
[b] China, Hong Kong, Republic of Korea, Taiwan Province of China.
[c] Including all developing economies and Australia, Japan and New Zealand.

In the light of this situation, it appears that the Asian economies are becoming integrated through intraregional trade irrespective of regional trade arrangements. The intraregional trade in Asia is, as expected, dominated by the effects of differing import demand structures which are closely related to the level and pace of economic development, rather than membership of a regional trade arrangement. Thus, relatively fast economic growth in Asia and the Pacific would in itself lead to a rise in intraregional trade. Consequently, growth in Asian intraregional trade in the next century will probably not be directly attributable only to progress in the functioning of regional trade areas, though this may also become important.

A large number and variety of partial equilibrium and general equilibrium models have been used to gauge the economic effects of various existing and proposed regional trading arrangements, including those in Asia.[25] The conclusions reached can be summed up as follows: (a) the net effect on the integrating countries is positive, with some exceptions in the cases of trade groupings composed of countries at very divergent levels of economic development; (b) the net impact of these regional trade arrangements tends to be quite small, usually less than 1 per cent of GDP (in absolute value) and sometimes dramatically less; and (c) the wider the trade grouping, the greater are the positive benefits reaped in terms of economic efficiency, with global liberalization offering the largest gains.[26] Within the Asian region it appears that it is the accompanying non-discriminatory liberalization, rather than the preferential trade liberalization itself, that holds the key to realizing the benefits potentially available from regional trade arrangements.

However, a comprehensive analysis of regional trade arrangements should go beyond the question of trade creation or trade diversion to include any progress in market integration within the trading area. Available evidence indicates that Asian markets are substantially segregated from one another. For example, there are few clear signs of movement towards declining price spreads.[27] There is also little policy coordination in the area of exchange rates.[28] However, some of the regional trade arrangements in Asia and the Pacific (for example, AFTA and CER) have progressed beyond the removal of border-trade restrictions (trade liberalization) to cover some non-border restrictions or distortions which affect trade (trade facilitation).[29] Trade

---

25 Computable general equilibrium models with economies of scale and imperfect competition have now been adapted to measure *ex ante* the effects of prospective or proposed regional trade arrangements. These recent models have generally predicted larger gains to the member countries than were obtained from traditional competitive industry versions of the general equilibrium models. Regional trade liberalization in these models leads to gains in the form of increased competition, reduced unit costs, and greater product variety, which are additional to those quantified in the traditional models. See, for example, P.J. Lloyd, "Regionalization and world trade", *OECD Economic Studies*, No. 18, Spring 1992, pp. 7-43; J.A. Frankel, *Trading Blocks: The Natural, the Unnatural and the Supernatural*, CIDER Working Paper No. C94-034, 1994, University of California, Berkley; G. Saxonhouse, "Trading blocks in East Asia", in J. Melo and A. Panagariya, eds., *New Dimensions in Regional Integration* (Melbourne, Cambridge University Press, 1993).

26 The question of why the effects of regional trade arrangements are so small is puzzling, especially since it is often believed that they are key determinants of a country's economic future. An important reason for this result is that they usually ignore the dynamic effects of regional economic integration, such as changes in X-efficiency, economies of scale, investment flows, business confidence, and other areas of economic liberalization which are difficult to quantity and which constitute integral components of modern regional trade arrangements.

27 Price spreads arise from differing tax structures and other such market interventions. There eventually needs to be some harmonization among these if trade is to be truly free from restrictions.

28 Saxonhouse, op. cit. There are, however, some recent agreements among a selected number of central banks to support any one of their currencies against short-term attacks in foreign exchange markets.

29 Regional trade arrangements have generally had no provisions, or weak ones, relating to factor trade. In Asia and the Pacific, CER is the only arrangement that has provided for national treatment of foreign capital. There is free movement of citizens and residents between Australia and New Zealand, which is guaranteed under a different agreement, known as the Trans-Tasman Travel Arrangements; it was adopted formally in the 1920s, long before the formation of CER. Trans-Tasman Travel Arrangements and CER are unique in having achieved free trade in goods, services and labour, but not in capital, within the area. (R. Scollay, "Australia-New Zealand Closer Economic Relations Agreement", in B. Bora, and C. Findley, eds., *Regional Integration and the Asia-Pacific* (Melbourne, Oxford University Press, 1996).

facilitation implies conformity to common product standards, investment principles, administrative polices and business practices. Thus, both trade liberalization and trade facilitation are geared towards reducing the transaction costs of doing business within the area or region in question.[30]

ASEAN Free Trade Area

The main mechanisms for the actualization of AFTA, which was started in 1993, are the Common Effective Preferential Tariff scheme and the "AFTA-plus" programme.[31] The design of the scheme is basically sectoral, and thus provides for more comprehensive product coverage than the liberalization by SAPTA and the ECO Protocol on Preferential Tariffs, which have employed an item-by-item approach. There are two main tariff reduction programmes under the scheme: the fast track and the normal track. The fast track will apply in the first instance to the 15 manufactured product groups agreed to at the Fourth ASEAN Summit for larger tariff reductions.[32] The reductions envisaged would bring ASEAN well ahead of the free trade arrangements envisaged by WTO and APEC.

Following the Fifth ASEAN Summit in December 1995 and the Ninth AFTA Council in April 1996, the time-frame has been shortened with an agreement to reduce tariffs on 98 per cent of trade items to a maximum of 5 per cent by 2003, that is, several years sooner than was originally envisioned and in a shorter time-span than allowed for implementation of the North American Free Trade Agreement.[33] The tariff reduction programmes have been supplemented by provisions for the removal of quantitative restrictions such as prohibitions, quotas and restrictive licensing, once the Common Effective Preferential Tariff concessions for the product set in, and the elimination of other non-tariff barriers gradually within five years from the commencement of such concessions. Thus, quantitative restrictions are to be removed when the intra-ASEAN tariffs fall to 20 per cent; that is, not until 2001 for high-tariff products.[34] In addition, the scheme envisages the harmonization of tariff lines to the 8-digit level of HS as well as the harmonization of standards and reciprocal recognition of tests and certification of products.

The Fifth AFTA Council decided to transfer items on the Temporary Exclusion List of the Common Effective Preferential Tariff to the Inclusion List with five equal instalments, starting on 1 January 1996 and ending by 1 January 2000.[35] Another agreement was to include unprocessed agricultural products in the common tariff scheme. This is a landmark reversal: only processed agricultural products were originally included, in recognition of the sensitivity of the large agricultural populations in most ASEAN countries. An agreement on services has been formulated which will provide for cooperation and liberalization in service trade with the aim of realizing a free trade area in services in the long run. The Council set up an AFTA unit within the ASEAN Secretariat, which collects information about

---

30 See M. Plummer, "Trade facilitation and liberalization in inter-American economic integration: a transactions-costs approach", paper presented to the Second APEC Roundtable: Facilitating Interdependence in the Asia-Pacific, Singapore, 23-24 June 1995; see also R.Z. Lawrence, "Regionalism, multilateralism and deeper integration", draft monograph for the Brookings Institution project, "Integrating the world economy, 1993", and Bora and Findlay, op. cit., pp. 7 and 50-51.

31 See J. Tan, ed., *AFTA in the Changing International Economy* (Singapore, Institute of Southeast Asian Studies, 1996).

32 Fertilizers, textiles, pulp, jewellery and gems, electronics, plastics, vegetable oils, rubber products, copper cathodes, pharmaceutical items, leather products, wooden and rattan furniture, and ceramic and glass products.

33 In order to simplify tariff reductions under AFTA, the Tenth AFTA Council (September 1996) mandated that one legal enactment for these reductions be prepared to cover the entire period up to 2003 (or 2006 in the case of Viet Nam). This would also create greater confidence on the part of the private sector on tariff reductions of member countries.

34 In some of these areas the dialogue has already started. For example, products beyond the HS 6-digit level are being reviewed to ensure a unified approach to the harmonization of standards, testing and accreditation of laboratories, conformity assessments and technical information.

35 A total of 682 tariff lines were transferred from the Temporary Exclusion List into the Inclusion List. Some of the products in the first instalment included inorganic and organic chemicals, and plastics, which are among the fastest growing traded products in ASEAN. The Seventh AFTA Council noted that the inclusion of Temporary Exclusion List products was bound to further accelerate the growth of intraregional trade.

the Common Effective Preferential Tariff as well as monitoring its implementation. Each country will also set up a national AFTA unit to tighten the implementation of the common tariff.

The Tenth AFTA Council agreed that textiles and textile products can be subjected to alternative rules of origin in order to qualify for concessions under the scheme. This would provide greater flexibility in the rules of origin of the scheme and enable textiles and textile products also to benefit from the concessions offered under AFTA. Currently, all products in the scheme must be subjected to a 40 per cent ASEAN content in value requirement. In the case of textiles and textile products, the Council mandated that these can alternatively be subjected to the substantial transformation process criterion in which products that are "substantially transformed" through a number of specified processes would be accorded Common Effective Preferential Tariff status and hence be eligible for lower tariffs. The effect of this is to enable an exporter to select the existing 40 per cent criterion of the scheme or the process criterion when applying for the ASEAN Common Effective Preferential Tariff certificate of origin.

Additional measures contained in "AFTA-plus" include the harmonization of customs procedures, an accelerated Green Lane System for products under the scheme, harmonization of tariff nomenclature at the HS 8-digit level by 1997 instead of 2000, implementation of the GATT Customs Valuation Agreement by 1997 instead of 2000 (Uruguay Round commitment), implementation of the ASEAN common customs form, elimination of customs surcharges by 31 December 1996, removal of barriers to foreign investment and the development of an ASEAN Dispute Settlement Mechanism. It is also expected that "AFTA-plus" will be dealing with TRIMs. All these agreements will mould AFTA into an impressive free trade agreement even by developed country standards.

In March 1995, some existing arrangements in ASEAN, for example, the brand-to-brand complementation scheme, the ASEAN industrial joint-venture programme and the Preferential Trading Arrangement, were phased out, as they offered preferential treatment to certain member countries on a partial or bilateral basis. In place of these three arrangements, a new framework was created for ASEAN cooperation in the manufacture of high-technology, high-value-added products called the ASEAN Industrial Cooperation scheme. It was also decided to establish an ASEAN patent and trademark system to ensure intellectual property rights.

In joining ASEAN, Viet Nam was accorded a different time schedule under AFTA. In acceding to the Common Effective Preferential Tariff scheme, Viet Nam agreed, on a reciprocal basis, to grant MFN and national treatment to ASEAN, and to promote transparency in its trade regime. It also agreed to an initial package of tariff reductions starting on 1 January 1996 and ending in 2006. It should be noted that in 1996 there was an agreement in principle to expand ASEAN (and AFTA) to include Cambodia, Lao People's Democratic Republic and Myanmar. These three countries are currently trying to restructure their trade regimes and practices in line with those of AFTA and are receiving considerable technical assistance for this purpose from various ASEAN members.

Much of the concern about the realization of AFTA boils down to uncertainty regarding the contributions of net and intra-industry trade to the expected growth in intra-ASEAN trade following liberalization. Reducing protection leads to a reallocation of resources from import-competing to export sectors, and is usually associated with diversification in export patterns through the process of horizontal specialization. This tends to increase the importance of intra-industry trade in the total multilateral trade of the liberalizing countries. The simultaneous reduction in both tariff and non-tariff barriers that is occurring in AFTA should thus boost intraregional intra-industry trade.[36] Further, the relocation of production activities of transnational corporations to third countries as part of their process of international vertical integration will be reflected in the growing magnitude of intra-firm trade.[37]

---

36 Some of the increase in the importance of intra-industry trade may simply reflect trade diversion as a result of preferential tariffs. Thus, an ASEAN country could be a net importer with respect to extraregional trade, but a net exporter when it comes to intraregional or intra-ASEAN trade. In this case, these exports will show up as contributing to an increase in the country's total multilateral intra-industry trade. Given that the preference margins that will exist following the implementation of AFTA are quite high, it can be expected that intra-industry trade resulting from trade diversion will also increase over time.

37 For discussion, see J. Menon, *Adjusting Towards AFTA: The Dynamics of Trade in ASEAN* (Singapore, Institute of Southeast Asian Studies, 1996).

There are a number of factors that augur well for the progress of AFTA. First of all, it has been launched in an overall economic and political environment conducive to regional cooperation. Second, there is strong political will in the wake of growing economic regionalism worldwide and in the face of the structural transformation in the ASEAN economies. In this respect, some have argued that AFTA would serve primarily as a means to hedge against "regional" efforts elsewhere in the world, or as a safety net in case the multilateral trading system falters temporarily. It would thus provide the requisite motivation for a group of countries to stick together to increase their collective bargaining position. Third, the *raison d'être* for the formation of AFTA has sprung from the recent closer economic ties among the member countries, in particular, the strengthening of trade-FDI links within the region. Fourth, tariffs in ASEAN countries are already relatively low by developing country standards, and further tariff cuts and removal of non-tariff barriers on a unilateral basis have become an integral part of the market-oriented policy stance of all member countries. Fifth, as a result of economic integration and the formation of intraregional company networks, most of the existing non-tariff barriers have become less binding (porous) and therefore their removal is unlikely to generate strong opposition.

It is important to note that AFTA has always been considered as much an investment agreement as a trade agreement. Free trade in ASEAN is unfolding at the same time as external barriers on non-member countries are being liberalized rapidly, with some countries considering to multilateralize Common Effective Preferential Tariff cuts under AFTA.[38] ASEAN is obviously not trying to create an inward-looking, trade-diverting bloc but rather a highly integrated production base that should be extremely attractive to transnational corporations. In this way, the subregion's economic disparities could turn out to be a great asset, as companies can benefit from a vertical division of labour within the subregion.

Australia-New Zealand Closer Economic Relations Agreement

This Agreement is very comprehensive by the general standards of free trade agreements. It embraces services as well as goods, both being included on a "negative list" basis, that is, everything is to be traded freely unless specifically exempted. Anti-dumping procedures have been abolished for trade between the two parties; each country applies its domestic competition laws to its trade with the other. Each has agreed not to subsidize exports into the other and any national preferences in government procurement are to include the other country within the preference. There has been free movement of people (including labour) between the countries for many years. A number of regulatory and business practices, including customs and business law, are to be harmonized.

In most regards, CER goes a long way towards economic integration. The legal systems and environmental and labour laws and conditions vary little between Australia and New Zealand. The structures of the economies are quite similar, reflecting high ratios of land to labour endowments and dependence on exports of primary products. This compatibility highlights the problems of new countries associating with CER; it would prove very difficult for any other country to enter into the existing agreement, for no other country is as similar to Australia or New Zealand as they are to each other. Paradoxically, while the economic gains from integration are greatest when the structures of economies are different, the process of integration is easiest when they are similar.

The rapid progress towards more complete bilateral integration has not undermined the commitment to unilateral trade liberalization in either country, and is not likely to do so. The reason is simply that CER-related trade still accounts for too small a proportion of either country's trade for it to contemplate sacrificing its wider economic interests for the sake of the trans-Tasman trade arrangement. Although CER can confidently be expected to yield significant further benefits as the objective of a single market is progressively realized, developments in trading relations among the wider circle of APEC members will inevitably carry much greater significance for both countries.

---

38 Singapore has offered to multilateralize the cuts, Indonesia has indicated that it would like to do so, and the Philippines has recently tabled a proposal to this effect.

For example, there has been a significant increase in trade and investment between ASEAN and CER (an increase of 30.8 per cent between 1993 and 1994; two-way trade between the two regions approached $12.5 billion in 1994) which has prompted a move to establish ASEAN-CER linkages. At this stage it is not clear what form the link might take. It has been agreed that, in the initial stages, the discussions will be limited to trade facilitation rather than trade liberalization. The areas for cooperation that have been agreed to so far include exchange of information, human resources development, customs matters, standards and conformance, trade and investment facilitation and promotion, competition policy and industrial cooperation.[39]

ECO Protocol on Preferential Tariffs

The ECO Protocol was signed in May 1991 to enable the steady expansion of trade within the ECO subregion on an overall reciprocal and mutually advantageous basis, employing an item-by-item approach. The agreement was concluded between the three founding members, the Islamic Republic of Iran, Pakistan and Turkey, but other members of ECO can join. The Protocol was initially for a four-year period but provides for automatic renewal every two years. The basic feature of the agreement is a mutual 10 per cent tariff reduction. The Islamic Republic of Iran and Pakistan have offered 15 products at the 4-digit level for preferential treatment, and Turkey has offered about 100 commodities at the 8-digit level. The rules of origin require that at least 50 per cent of the value of goods should originate in the exporting country in order to qualify for preferential treatment. A Committee on Preferential Tariffs consisting of the representatives of the three countries has been constituted to supervise the implementation of the agreement.[40]

The Protocol has been ratified by all three countries; the lists were drawn up and implementation began in May 1993. However, it has not been sufficiently developed to lead to visible benefits. ECO intra-trade in 1992 (among the three members of the Protocol) constituted only 3 per cent of their total trade volume. Furthermore, the margins of preference are quite insignificant and cover less than 5 per cent of the countries' bilateral trade volumes. Many of the items were narrowly defined (for example, paper bags for cement, bentonite, leg protectors used in sports – to quote one item from each country's list). After the Protocol became operational, some uncertainty remained as to whether the preferences were actually being applied.

Although the Committee has encouraged the submission of longer lists, widening of preference margins to 20 per cent, and the participation of the seven new members[41] in the preferential trading arrangement, little progress has been made on any of these fronts. At the 1995 Summit, the Heads of State signed the ECO Transit Trade Agreement and an Agreement on the Simplification of Visa Procedures for the Businessmen in the ECO Region. Such trade facilitation measures are important steps towards promoting regional trade. Eight ECO members signed the Transit Trade Agreement. While all these issues remain on the agenda, the ECO Secretariat is also encouraging discussion of the implications of the Uruguay Round and WTO for the ECO region, with a view to adopting open regionalism rather than preferential tariffs as a route to closer regional economic integration.

South Asian Preferential Trading Arrangement

The seven member countries of SAARC have 20 per cent of the world's population but only 2 per cent of the world's GDP, and together account for only 0.8 per cent of world exports. In April 1993, SAARC members agreed in principle to SAPTA. That Arrangement, like the ECO Protocol, provides for liberalization with product-by-product coverage, the reduction of tariffs in several successive rounds and periodic reviews. It also provides for special and differential treatment of the least developed

39 Chee Peng Lim and Robert R. Teh, Jr., "Linkages between AFTA and other regional trading arrangements such as CER", in Chia Siow Yue and Joseph L.H. Tan, eds., *ASEAN in the WTO: Challenges and Responses* (Singapore, Institute of Southeastern Studies and ASEAN Secretariat, 1996).

40 The Committee has held four meetings so far (Tehran, April 1993; Islamabad, September 1993; and Tehran, January 1995 and February 1996).

41 Afghanistan and Central Asian republics.

countries (Bangladesh, Bhutan, Maldives and Nepal). It contains safeguard measures and rules of origin, which state that the total value of the materials or parts originating from non-contracting States should not exceed 50 per cent of the f.o.b. value of the products for these to be eligible for preferential treatment.

A total of 226 items were covered by concessions exchanged by SAPTA members in 1993, of which 100 items were targeted exclusively in favour of least developed countries. The maximum number of concessions was made by India – nearly half of the total number of items, with 62 items offered in favour of least developed countries. All the other SAPTA members combined offered concessions in respect of 120 items, of which 38 were in favour of those countries. Under SAPTA, tariff concessions are expressed as a percentage of MFN rates, which means that as member States bring down their MFN rates, they must bring down their preferential rates accordingly so as to maintain the margin of preference.[42] In 1994, trade covered by SAPTA preferences amounted to $72.5 million, or only about 6 per cent of the intraregional trade. This share would be even less if account were taken of common products covered by concessions offered under other arrangements.

In 1996, the SAPTA members undertook a second round of trade negotiations. These negotiations, which were completed in December 1996, have resulted in a significantly larger number of concessions under two modalities: bilateral exchanges of tariff concessions among member countries of SAARC, and concessions applicable to all member countries. In the bilateral exchanges, which in total affect 1972 HS tariff lines, the largest number of concessions were made by India to Bangladesh (513), India to Pakistan (375), Pakistan to India (230), and Bangladesh to India (204). Most overall concessions are equivalent to 10 per cent of existing MFN rates, whereas those for least developed countries are 15 per cent or more. The schedule for implementation is short: all concessions are to enter into force by 1 March 1997 at the latest.

It is clearly too early to assess the impact of the second round on SAARC intra-trade. The fact that it has shown little progress to date has been attributed to the product-by-product approach being used, which is cumbersome to negotiate. Nevertheless, progress is being made and the governments have agreed that the ultimate aim is to permit duty-free trade in all tradable products and to convert SAPTA into a South Asian Free Trade Area by the next decade.

Bangkok Agreement

The First Agreement on Trade Negotiations among Developing Member Countries of the Economic and Social Commission for Asia and the Pacific Bangkok Agreement, established under the auspices of ESCAP, is a preferential trading arrangement designed to liberalize and expand trade among the developing countries in the ESCAP region through such measures as the reduction of tariffs and non-tariff barriers. The Agreement became operational in July 1976. Its current membership includes Bangladesh, India, Lao People's Democratic Republic, Papua New Guinea, Republic of Korea, and Sri Lanka, although the accession of Papua New Guinea to the Agreement at the fourteenth session of the Standing Committee, held in December 1993, has not yet been ratified. A recent significant development has been the submission of a formal application for accession by China in 1994. China and the other member countries are in the process of exchange of their request and offer lists. To capitalize on the momentum created by this development, the ESCAP secretariat is making efforts to further increase the membership of the Bangkok Agreement by offering technical assistance and advice on accession to the Agreement.

A total of 747 items are currently covered under the Agreement, with tariff cuts ranging from 10 to 50 per cent. However, the total trade value of the covered items remains very low. Further, it would appear that the Agreement needs to be reoriented to take into account the Uruguay Round agreements and regional trade liberalization movements. Considering the fact that very significant

---

42 The list of concessions offered by Pakistan is drawn from the same list of 578 products which the country permits to be imported from India. As is well known, Pakistan does not maintain MFN status in its trade relations with India. SAPTA, however, stipulates the MFN principle, which implies that any concession given by one member to another has to be extended unconditionally to all other members (except those preferences extended to least developed countries). In order to meet both conditions, Pakistan chose to offer concessions in respect of mainly those products listed for import from India.

developments have taken place since the conclusion of the second round of negotiations in May 1990, the Standing Committee of the Bangkok Agreement, at its fifteenth session held at in Bangkok February 1995, decided to launch a third round of negotiations with a view to making the Agreement a more viable regional mechanism for trade expansion.

Melanesian Spearhead Group

This grouping of the Melanesian Pacific island countries of Fiji, Papua New Guinea, Solomon Islands and Vanuatu contains 95 per cent of the land area of the Pacific and 80 per cent of the population. It was started in 1991 among the last three; Fiji joined as a full member in 1996 and New Caledonia as an observer. Steps have been taken since 1993 to promote the free flow of specified goods and services among the concerned countries under the Melanesian Spearhead Group trade agreement. Traditionally, there has been very little trade among the islands, with most exports going to developed country markets. Tariffs have been reduced to zero on an expanding list of items, documentation is being exchanged, procedures are being streamlined, and definitions on rules of origin etc. agreed. Further expansion of the zero-rated list is expected soon. While the volume of traded goods among these countries is not likely to be large, the experience with operationalizing the Melanesian Spearhead Group is seen as a useful learning exercise to support the efforts of these countries to be better integrated into the world trading system.

Promotion of integration among Central Asian republic

An agreement on the promotion of integration in economic and humanitarian areas was reached by Belarus, Kazakstan, Kyrgyzstan and the Russian Federation in 1996.[43] In accordance with this agreement, the four countries formed a customs union which is expected to play a leading role in expanding trade and economic links and in promoting the economic integration of the participating countries. The main objectives of the union are to remove artificial barriers hampering the movement of goods, services and capital, and to provide conditions for free interplay between economic entities and shaping common economic space on the basis of a common customs territory and uniform mechanism of economic regulation. Unified rules with regard to re-export and modalities of trade with third countries have been adopted by the countries concerned, and a common system of preferences for developing countries has been introduced. Alongside the establishment of the customs union, these countries are working on a payment and settlement facility within the framework of an agreement with a view to forming a payment union eventually.

Asia-Pacific Economic Cooperation

APEC is not a regional trade arrangement; rather its main objective is to coordinate and marshal regional forces for the maintenance and improvement of a multilateral trading framework. As such, APEC is a new exercise in economic cooperation that has developed on the North-South pattern rather than on the traditional South-South or North-North lines. Early decisions on economic cooperation by APEC governments dealt with issues of structure and participation, as well as with drawing up the guiding principles of APEC. Once this foundation was laid, the attention shifted to substantive economic issues, leading to the ambitious "Bogor Declaration", the APEC Economic Leader's Declaration of Common Resolve, adopted at Bogor, Indonesia, in November 1994, to dismantle all barriers to trade and investment by no later than 2020 (2010 for developed members).[44]

---

[43] The treaty between the Russian Federation, Belarus, Kazakstan and Kyrgyzstan on the promotion of integration in economic and humanitarian areas was signed in Moscow on 29 March 1996 by the respective Heads of State.

[44] APEC has three dimensions: liberalization, facilitation (of trade and investment) and cooperation. Cooperation programmes include databases, information exchange on policies and regulations and work on standards and other technical issues in telecommunications, fisheries and other sectors. They also include the networking of educational institutions and private sector bodies. So far, the results in cooperation have been modest. Only a compendium of telecommunication regimes in APEC countries is cited as an achievement.

The implementation of the Bogor "vision" was spelled out in the Osaka Action Agenda adopted at the APEC Ministerial Meeting in 1995. The Osaka Action Agenda has been translated into 18 national action plans, which were meant as voluntary and non-negotiable and were submitted to the APEC Ministerial Meeting in November 1996. In principle, each country's action plan must state its commitments for certain periods: 1997-2000 and 2001-2010 for developed members, and 2011-2020 for developing members. According to some preliminary assessments, only nine countries are proposing to reduce their tariffs beyond the levels already committed in WTO. All countries have submitted drafts on investment liberalization. However, the drafts are quite vague on the measures to give foreign investors national treatment. Proposals for liberalizing services vary, with only eight members opening their goods distribution markets. Only in the telecommunications sector are there substantial proposals for reducing restrictions on market access and there is still much room for improvement in these proposals in terms of specifying time-frames and clarifying current regulatory regimes and specific action to be taken.

APEC has a major role in the promotion of a "meta-regime"[45] which is manifested in open regionalism. The concept of "open regionalism" changes the interpretation of MFN from "exclusive MFN" (required for members only), which is the WTO norm, to "inclusive MFN" (also for non-members). However, inclusive MFN gives rise to a free rider problem. There is a point of view that the inclusive MFN should be replaced by a temporary conditional MFN, which would allow large regional groups, such as APEC, to use their leverage to achieve maximum liberalization around the world.[46]

APEC members do not hold the view that the implementation of the Bogor Declaration should be carried out by resorting to a negotiated outcome with legally binding rules. Instead, APEC has adopted an approach that favours concerted unilateral liberalization. All APEC agreements to date have been set out in declarations or codes endorsed jointly by either ministers or heads of APEC governments; none of these agreements can be defined as a law or treaty. APEC has no structure for legal enforcement and is not expected to have one.

One major role for APEC is mediating trade disputes, based on the view that the dispute settlement procedures of WTO are limited. The WTO processes do not address commercial disputes as WTO, properly, addresses only disputes between governments. There is a growing perception that in Asia and the Pacific it would be highly desirable to have a less formal kind of mechanism, based on mediation rather than arbitration, that would complement the WTO dispute settlement mechanism.

Trade liberalization at the global level

There are two distinct aspects to the international agreements on trade liberalization under the Uruguay Round that are important from the perspective of the region and trade expansion in the future: the commitments made by countries of the region, and the benefits or losses that are likely to occur as a result of implementation of the global accord.[47] For many of the developing countries of the region participating in the multilateral trade negotiations, it was the first time they had taken an active part in global trade negotiations; 22 of them are members of WTO and 11 more have applied for membership. This imposes a degree of international discipline on the region but also makes it possible for countries of the region to avail themselves of the benefits of membership.

---

45 "Meta-regimes" in trade are distinguished from international regimes in the sense that "meta-regimes" represent the principles and norms underlying international arrangements, whereas international regimes refer specifically to rules and procedures.

46 See H. Soesastro, "The institutional framework for APEC: an ASEAN perspective", in Chia Siow Yue, ed., *APEC: Challenges and Opportunities* (Singapore, Institute of Southeast Asian Studies, 1994).

47 For a discussion on the implications, see ESCAP, *Implications of the Uruguay Round Agreements for the Asian and Pacific region*, Studies in Trade and Investment, No. 15 (ST/ESCAP/1535).

Tariff bindings and reductions

According to the Uruguay Round agreements, liberalization of market access for most manufactured goods will be achieved within a five-year period, agriculture within a six-year period, and textiles and clothing over 10 years, all starting from 1995. During the Round, Asian countries as a group bound the least in terms of tariff lines or imports. However, careful interpretation of these results is needed because they are affected by the fact that Hong Kong did not make an offer on a substantial number of tariff lines on which the unbound applied tariff is zero. In fact, many of the Asian developing economies have bound a significant proportion of their tariff lines, for example, Indonesia at 90 per cent, and China, India, Malaysia, Philippines, Republic of Korea, Singapore and Thailand at between 60 and 89 per cent.[48] Some countries opted for binding without reductions, that is they bound their tariffs at rates above the currently applied rates. About 9 per cent of developed country lines, primarily those of developed countries in Asia, fall into this category.[49]

Most least developed countries in Asia bound their tariffs at a maximum ceiling level or reduced already bound rates which were above the rates currently applied. The ceiling bindings for most commodities were set at very high levels in Bangladesh (200 per cent) and Myanmar (168 per cent). In contrast, some South-East Asian countries committed themselves to uniform tariff bindings at relatively low levels, including Brunei Darussalam (20 per cent) and Singapore (3-10 per cent).

In all developing economies of the region, except Hong Kong and Singapore, the average post-Uruguay Round tariff level is still higher than that of developed countries. In East and South-East Asia, the average post-Uruguay Round tariffs for Malaysia and the Republic of Korea are in the 9-10 per cent range, with other ASEAN members (Indonesia, the Philippines and Thailand) having higher averages. Post-Uruguay Round tariffs in Indonesia are higher than pre-Round tariffs because Indonesia chose not to bind at its applied rates.[50] In all of these countries there are sectors that are still more protected. In the Republic of Korea, for example, tariffs in the 10-15 per cent range are applied in fisheries, processed food, textiles and apparel and fabricated metal products (steel). In Malaysia, the sectors receiving more protection are textiles, apparel and transport equipment. In the Philippines, the sectors are textiles, apparel, fabricated metal products, lumber, pulp and paper and processed foods. In Thailand, they are transport equipment, fabricated metal products, chemicals and petroleum. These countries thus continue to provide on a selective basis a margin of extra protection to sectors involving commodity processing or infrastructure and transport development.

In South Asia, India and Sri Lanka have made a big effort to reduce tariffs. However, tariff reductions have led to some anomalies in the incentive regimes, including higher protection for final than for intermediate and capital goods. There is still in the Asian and Pacific region widespread use of tariffs for revenue purposes, particularly in the Pacific subregion and the least developed countries, where the domestic tax base is small. Overall, there has been significant improvement in access to developing country markets in Asia under the Uruguay Round. Comparative data show that the developed countries and the East Asian region provide the least tariff protection. Protection in South Asia has also fallen, but remains more than double that prevailing in East Asia.

With regard to the agriculture sectors, most countries used tariffication procedures that resulted in base tariffs considerably above the estimated tariff equivalents for 1986-1988 ("dirty tariffication"). However, Japan has offered base tariff equivalents which are considerably below the actual nominal rate of protection in 1986-1988 in the case of all products with the exception of rice.[51] The largest tariff

---

48 M. Pangestu and S. Stephenson, "Evaluation of the Uruguay Round commitments by APEC members", in B. Bora and M. Pangestu, eds., *Priority Issues in Trade and Investment Liberalization: Implications for the Asia Pacific Region* (Singapore, Pacific Economic Cooperation Council, 1996).

49 Ibid. See also W. Martin and L.A. Winters, eds., *The Uruguay Round and the Developing Economies*, World Bank Discussion Paper No. 307 (Washington DC, 1995).

50 Pangestu and Stephenson, op. cit., p. 56.

51 See M.D. Ingco, *Agricultural Trade Liberalization in the Uruguay Round: One Step Forward, One Step Back?* World Bank Policy Research Working Paper No. 1500 (Washington DC, 1995).

reduction in agriculture was made by the Republic of Korea and the lowest average post-Uruguay Round tariff reduction by Australia. South Asian countries have mostly taken the option of binding tariffs at ceilings higher than actual levels for most commodities.

In terms of the number of specific commitments made under GATS, four East and South-East Asian economies (China, Malaysia, the Republic of Korea and Thailand) made some commitments in the areas of banking, insurance and securities-related services which will imply further liberalization of these sectors. India and Pakistan offered a number of commitments, whereas Bangladesh and Sri Lanka made very few. Thus the potential benefit of GATS to most of the countries in the region is still unclear.

A number of Pacific island economies are dependent on services, particularly tourism. Air transport services in the subregion are heavily protected, reflecting both the economic and the sovereignty concerns of several of the island States. Given that GATS contains the obligation to treat foreign service suppliers and domestic suppliers in the same manner, it may become increasingly difficult for the Pacific island countries to exclude foreign competition in these services, whether they are members of WTO or not.

The TRIPs agreement will require significant changes in intellectual property laws and regulations in developing countries of the region, and initially might increase some of the costs of using information and knowledge. However, it is expected that increased protection of intellectual property rights will induce greater inflows of foreign investment. This view has been questioned in some theoretical and empirical literature. The broad conclusion is that developing countries are unlikely to benefit from stronger intellectual property rights regimes unless they are in a position to engage in research and development at the frontiers of knowledge.[52] The concern of some developing countries that certain patented products, such as pharmaceutical products, will have higher prices should be somewhat allayed by the fact that the TRIPs agreement will not have its full impact until 2015. The fact that Asian developing countries will make a serious attempt to protect intellectual property rights does not imply that it is going to be easy; law enforcement in quite a number of countries is rather weak and it could take several years before it can be strengthened adequately.

The TRIMs agreement envisages that certain disciplines will apply to investment policies as far as they affect international trade. In particular, the discipline of national treatment would apply. The agreement confirms that the use of local content and trade balancing requirements on foreign investment are GATT-inconsistent. In theory, this should help to encourage FDI flows to the developing countries. However, several countries in the region see a restrictive side to these disciplines in terms of not being able to use TRIMs as part of their policy package to stimulate the domestic economy.

Global tariff liberalization

The global tariff reduction decisions important for Asian and Pacific exports concern mainly the textile and agriculture sectors. The phasing out of MFA is very important as textiles account for 25-30 per cent of manufactured exports for many countries in the region. Of these exports, United States and European markets constitute nearly 50 per cent of the total, while intraregional trade accounts for slightly over 35 per cent. Despite the Agreement, the average level of tariffs on textiles and clothing remains high in the developed economies, with the highest tariffs in Australia and New Zealand, especially with regard to clothing. The use of MFA quotas in the 10-year transition period is also still permitted.

The initial assessments of the MFA phase-out indicate that the most seriously restricted textile and clothing exporters, such as China and South Asian countries, are likely to be the major beneficiaries of the Agreement on Textiles and Clothing.[53] For China, Indonesia and countries of South Asia, their

[52] See, for example, E. Helpman, "Innovation, imitation and intellectual property rights", *Econometrica*, vol. 61, No. 6 (November 1993).

[53] For an analysis of the potential winners and losers in the textile trade in Asia, see Madhavi Majmudar, "Trade liberalization in clothing: the MFA phase-out and the developing countries", *Development Policy Review*, vol. 14, No. 1 (March 1996).

comparative advantage in clothing is so strong that increased sales will be likely to more than compensate for the loss of rents (which will be "transferred" to consumers in developed countries). Malaysia and the Philippines will probably lose from MFA, while Thailand should gain.[54]

For agriculture, it may very well be the case that the high levels of tariff bindings in that sector will never be applied by either developed or developing countries. Nonetheless, their existence may undermine the initial objective, to remove non-tariff barriers such as variable levies. Countries will still be able to impose tariffs at varying rates below the binding limit, and this could be tied to a domestically controlled price and therefore equivalent to a variable levy. Moreover, state trading enterprises have remained largely untouched by the Uruguay Round new rules for agriculture, which has not strengthened the provisions governing the actions of these monopolies. No additional provisions serve to enhance the transparency of these enterprises or to restrain their potentially restrictive impact on domestic markets. Overall, it appears that very little or no liberalization has been achieved for most agricultural commodities in terms of market access for the majority of Asian exporters. The largest increase in access opportunities is likely to be found in rice, beef, maize and poultry. However, the minimum access commitments and reduction of export subsidies should serve to improve somewhat the distortions currently present in agricultural trade.

Given the relatively small volumes of trade from Pacific island countries, these countries are unlikely to benefit as much as many other trading nations. Considering that their exports are predominantly tropical agricultural products, the way multilateral trade rules for these sectors develop is of significant importance. For instance, sugar, a major export commodity for Fiji, is currently sold at the European Union intervention price, which is around two to three times higher than the world price. It is expected at this stage that the price for sugar may decline by 12 per cent by 2000. Another example is tuna: a 24 per cent margin of preference is received by Pacific island exporters of tuna. While the European Union has not offered to lower this rate of import duty in the interests of sustaining its domestic canning operations, pressure from other tuna-exporting nations for a reduction in rates is bound to increase.[55] If prices for temperate food crops increase and prices for some tree crops decline as a result of the Round, countries such as Papua New Guinea and Solomon Islands, which are exporters of coffee and cocoa, and at the same time substantial importers of food items, are likely to be at a disadvantage.

Global liberalization of non-tariff barriers

The non-tariff barrier problem is a primary concern of the region's exporters. Of the 75 measures surveyed in mid-1992 (not including restraints applying to textile and clothing items under MFA), 93 per cent of non-tariff barriers affected exports from China, Japan, Republic of Korea, and Taiwan Province of China combined. The sectors most affected were travel goods, electrical equipment and appliances, footwear, machine tools and television sets.[56] However, the shares of East Asian and Chinese exports facing developed country non-tariff barriers were around 19 and 17 per cent, respectively.

While South Asian countries face lower tariffs on their exports to the industrial countries than do East Asian countries, these exports have higher non-tariff barriers coverage. Prior to the Uruguay Round, almost 37 per cent of the South Asian exports to the developed countries faced non-tariff barriers, with the share for Bangladesh being more than 48 per

---

54 L.A. Winters, "Implications of the Uruguay Round agreements: critical issues and adjustment requirements", in ESCAP, *Implications of the Uruguay Round Agreements for the Asian and Pacific Region*, Studies in Trade and Investment, No. 15 (ST/ESCAP/1535).

55 R. Grynberg, University of the South Pacific, Suva, "The closure of the Uruguay Round and its impact on the South Pacific Forum Island Countries", paper presented at the ESCAP Expert Group Meeting on Inter-subregional Cooperation in Trade and Investment, Bangkok, 26 September 1994.

56 Pangestu and Stephenson, op. cit., p.59; see also P. Low, and A. Yeats, *Non-tariff Measures and Developing Countries: Has the Uruguay Round Leveled the Playing Field?*, World Bank Policy Research Working Paper No. 1353 (Washington DC, 1994).

cent. India appears to have been the only country with a non-tariff barrier coverage ratio more or less the same as that for East and South-East Asia.[57] On the other hand, the region's exports to Japan were treated more favourably than similar exports from East Asia and China.[58] This may be viewed as primarily reflecting the commodity composition of the South Asian exports rather than explicit discriminatory measures. Therefore, the removal of non-tariff barriers on the region's exports to the rest of the world is likely to be the Uruguay Round's most important benefit for South Asia: the proportion of South Asian exports to the developed countries under non-tariff barrier coverage will be reduced drastically to only 6 per cent.

PROSPECTS AND CHALLENGES

Prospects

International trading environment

There is a relatively strong probability that the international trading environment will remain favourable. The moves towards global integration in the developed countries seem likely to continue, spurred on by trade and financial integration and the presence of transnational corporations as major actors in economic decisions. However, there is always the risk of a return to protectionism in the major developed country blocs, which remain very important outlets for exports of the region. Many developing countries fear that their very success will lead to some new, and sometimes hidden, non-tariff barriers being applied to their exports which compete with domestic products in these markets.

The spread of industry and specialization in the world is likely to be heavily influenced by two crucial factors; the degree of economic and social stability as viewed by investors and the degree of componentization of industrial processes that these investors find acceptable and efficient. A significant and growing proportion of trade in industrial products will be intra-industry or intra-firm trade, with the location of factories being more or less footloose throughout the world. There will be a natural tendency to locate factories within agglomerations that offer economies of scale in infrastructure, labour markets and services, and to service geographic areas from one or a few locations rather than have a spread of factories within various national borders. Thus transnational firms will push to maintain open markets. The one dark side to this picture will be the pressure resulting from continued high unemployment in the developed countries, which may lead governments to blame the South, particularly the successful trading nations of Asia, for their social problems, despite evidence to the contrary.[59] The ensuing tensions could be manifested in the use of barriers to trade inconsistent with existing international obligations.

The impact of the implementation of the liberalization agreements under the Uruguay Round is likely to continue to have a positive stimulus on trade flows. Several of the agreements, such as those on textiles and agriculture, will take a number of years to be implemented. For others, such as on services, the negotiations are still under way and their significant liberalizing influence on trade flows is still some time away. On balance, the effects of the Round should be positive for the region.

Regional trading environment

All the recent forecasts for economic growth in the Asia and Pacific region are highly optimistic. The predictions reported in table I.1 indicate continued fairly rapid growth in developing economy members of the Asian and Pacific region, at rates of between 5.1and 7.2 per cent for the period up to 2005. These are two or three times larger than the

---

57 N. Majd, *The Uruguay Round and South Asia: An Overview of the Impact and Opportunities*, World Bank Policy Research Working Paper No. 1484 (Washington DC, 1995), p. 18.

58 Ibid., p. 4.

59 See, for example, the discussions on the role of trade and of technology as causes of unemployment in the developed countries in UNCTAD, *Trade and Development Report, 1995*, United Nations publication, Sales No. E.95.II.D.16, part three: *Unemployment and Interdependence*, pp. 119-212.

rates of growth predicted for other developed or developing regions. However, most predictions of continued strong growth in GDP and trade are focused on the economies of East and South-East Asia, as these are the ones that have succeeded in harnessing the advantages of cooperation while retaining the advantages of competition. These predictions may be viewed as overly optimistic in the light of very recent falls in export earnings in several strongly expanding economies, but growth in the region is still likely to outpace that in other regions of the world. Further, it is likely that the expanding trade flows will occur mainly in countries with better developed infrastructure and service facilities, and in those that succeed in maintaining competitiveness, including through the progressive upgrading of the quality and technology context of their products.

One very positive sign in the region is the increasing numbers of middle- to upper-income consumers in the developing economies who are forming a growing market for modern consumer goods and services. For example, there are now more than 21 million persons in five developing economies (Hong Kong, Malaysia, Republic of Korea, Singapore and Thailand) whose per capita income is greater than the average per capita income of a person in Australia and New Zealand (total population of 21 million). These consumers tend to have a relatively high propensity to import and be at the forefront of the spread of the integration of economies into global and regional markets.

Thus it is relatively easy to predict that reform and liberalization of both domestic and external policies will continue in most if not all countries in the region. The examples of recent successes in East and South-East Asia are so visible that countries are most likely to continue striving to use trade as an engine of growth, in terms of both stimulating exports and relying on imports for infrastructure development, capital goods and their associated technological content, and selected consumer goods. This means that their economies will be relatively open, with few border restrictions, and so provide a conducive environment for continued expansion of trade, including intraregional trade. The one large unknown in this equation is the degree of political stability that will exist in the region. Even the more developed economies will be affected if political instability increases. To quote from a recent assessment on the future of Singapore, "the missing piece beyond its control is regional economic growth and political stability which underpin prosperity for the whole region".[60]

Trade liberalization efforts within subregional groupings such as ASEAN, SAARC, ECO and the South Pacific Forum are also likely to continue. The question is whether some of the regional groupings which are just starting the process of offering preferences to each other will follow the example of ASEAN and realize that such subregional liberalization is more effective when it starts from a negative list concept than when it uses a product-by-product approach, and when it is extended beyond the countries within the group. From the trade patterns observed in the Asian and Pacific region it would appear that open regionalism in trade relations is preferable to more closed groupings and that trade creation through open extension of preferences is likely to be more dynamic than trade creation within the group.[61] Thus "intraregional trade expansion must therefore occur without any neglect of interregional markets, which will require intraregional trade cooperation being pursued in a global context with market access being offered in one's own market in order to secure market access in other countries."[62]

In fact, it may be preferable for countries with relatively small domestic markets to view attracting investment as a regional rather than a national priority. This would also provide an added incentive for maintaining open trading regimes in subregional areas such as the Central Asian republics, the Pacific island countries or the Mekong region.[63]

---

60 Goh Keng Swee and Linda Low, "Beyond 'miracles' and total factor productivity: the Singapore experience," *ASEAN Economic Bulletin*, vol. 13, No. 1 (July 1996) p. 11.

61 "The bottom line is that regional initiatives do not aim to create trading blocs, but rather to harness synergy between economies – viewing the whole as clearly greater than the sum of its parts", address by Staporn Kavitanon, Secretary-General, Board of Investment of Thailand, on "Thailand's engine of growth for the 21st century", to the East Asian Economic Association at Bangkok on 26 October 1996.

62 ESCAP, *Review and Analysis*..., p. 57.

63 This argument would appear, prima facia, to have less relevance for countries with large domestic markets such as China or India.

The ASEAN countries seem to have set an interesting example to follow: by cutting regional tariffs, by reducing non-tariff barriers and promoting transparency in operations, the entire ASEAN region is becoming more attractive to foreign investors. This makes it easier for companies to establish one production facility for the region and set one regional marketing strategy rather than have to formulate different plans for each country. However, the ASEAN region has an added advantage: when it becomes a community of 10, it will represent a market of more than 450 million people and so an attractive market in itself.

By all accounts, intraregional trade in Asia and the Pacific is likely to gain further momentum in the coming years owing to the continued rapid economic growth and expanding markets of the developing countries of the region; the increasing outward orientation in the trade policies of the developing economies of the ESCAP region, including the countries of South Asia which have large markets; and intraregional investment and relocation of production facilities from Japan as well as the dynamic developing economies of Asia and the Pacific. On current trends, it is likely that intraregional exports may just about equal interregional exports by the turn of the century, while intraregional imports may continue to stay ahead of interregional exports. In the future, a significant amount of the intraregional trade will be generated in response to a growing urban middle-class society so that this trade will not be confined mainly to intermediate and capital goods but will also comprise consumer goods catering to varied tastes.[64] However, because growth in the region has not been and is likely not to be uniform, intraregional trade expansion in Asia and the Pacific will continue to be dominated by a relatively small number of countries. For example, the growing importance of China and India in this trade has been predicted by many economists. This situation will nevertheless open up opportunities for other countries to find regional export niches. However, both the volume and the composition of their exports will remain vulnerable to the economic performance of these few countries.

The process of spread of industries, such as those which are relatively labour-intensive (textiles and electronics), within the region is likely to continue, with the consequent creation of new trade flows. The increasing importance of new technologies as a determinant of industrial specialization will also promote the componentization and dispersal of production among countries,[65] and so influence the composition, size and direction of intraregional trade. However, the ability of individual countries to benefit from these opportunities is likely to be more determined by investors' ratings of their economic performance and potential than by any significant differences in trade or domestic policy regimes.

One of the dilemmas facing the region's developing countries is that not all of them can have export sectors that grow at well over 10 per cent a year when world trade is expanding much more slowly, at around 5-8 per cent; such rapid rates of growth are only possible for a few countries at a time or for countries that are unimportant in trade (those starting from a small export base). Not all countries can export the same products or move into the same potential export sectors without causing an aggregation problem, that is, creating a supply much larger than the demand and so causing prices to fall and some businesses to fail. In addition, for a growing number of products, there is a high rate of obsolescence associated with rapidly evolving technologies and changing tastes. Therefore, it is essential that firms pay sufficient attention to monitoring market trends and adapting to changes in demand (see box III.2). While trade will continue to act as an important modality for cementing regional linkages, the risks of marginalization for those who do not aggressively act to stay competitive are significant.

64 ESCAP, *Review and Analysis...*, pp. 3, 27 and 59.

65 See the arguments developed by E. Chen and C. Titherington, "The changing patterns of trade and industrial development in China and Asian NIEs", in Syed Abdus Samad and Somsak Tambunlertchai, eds., *Flying Wild Geese Pattern of Development: Changing Comparative Advantage in Asia and the Pacific* (Kuala Lumpur, APDC and ESCAP, 1996), p. 119.

Box III.2. Participation in dynamic markets

To an important extent, the long-term health of any country's export sector is determined by its capability to take advantage of market changes in importing countries. For most developing countries, this translates into their success in penetrating the expanding segments of OECD markets. From this perspective, the contrast between the East and South-East Asian and Latin American economies is striking: in 1990 about three quarters of exports from the former countries were in goods for which the share in total OECD imports had been expanding, whereas for the latter countries this category only amounted to 38 per cent of their exports. Furthermore, during the period 1963-1993, the Latin American share in OECD total imports of the 20 most dynamic products dropped from 15 to 2.5 per cent, whereas that of East and South-East Asia rose from 1 to over 10 per cent. Thus, the dominant position of Latin America among developing country exporters in the 1960s (when they accounted for about 60 per cent of total developing country exports) had been replaced in the 1990s by East and South-East Asian economies, which accounted for around 64 per cent in 1993.[a]

However, some caution is needed in using these results in discussions of future trends. The use of a long time period limits its relevance for projecting the future because various major structural breaks have occurred in the past 30 years or so, including the breakdown of the fixed exchange rate system, two oil and other commodity shocks, and massive capital transaction liberalization. An expansion in the number of countries included in the analysis might produce some interesting but different results. The use of the OECD import penetration as a benchmark for developing country's export performance could also be of limited relevance as it ignores the importance of trade among the developing countries, which has been growing rapidly in the Asian and Pacific region.[b] There remains ample opportunity for countries in the region to expand their exports even if they may not be capable of participating in the dynamic OECD market segments.

By examining the export trends of the developing economies in the ESCAP region, one can identify the fastest-growing export products and assess which of the economies experienced significant changes in their global market shares for these products. A sample of four export products of the ESCAP region is listed in the table. These products were selected among the 10 export products of developing economies of the ESCAP region which had the highest growth rates for the period 1981-1994. The first two listed in the table represent export products with a high skill content, and the other two, those with a low skill content. As shown in the table (overleaf), in the past five years developing country exporters of the ESCAP region experienced enormous gains in global market shares for these dynamic products. The increase in global market shares of the first-generation NIEs in modern office equipment and accessories is particularly striking. Their combined share jumped from below 1 per cent in the early 1980s to more than one fifth of the total world trade in these products in the early 1990s. As well, some relatively low-skill products, such as footwear and special textile fabrics, experienced reasonably rapid rates of growth in trade, implying that there is ample room for trade expansion in labour-intensive products. It is within this category of dynamic products that China, Indonesia and other countries in the region have excelled in the global market.

The above evidence further underscores the success of Asian economies in capturing a growing portion of the dynamic segments of world trade. This notwithstanding, some caveats apply. First, it is not only the high rate of growth or income elasticity of demand for imports that matters, but also the volume of trade. This is particularly true for resource-based and low-skill export products, which, despite their slower rates of growth, tend to have a sizeable trade value. For instance, the table shows that the total value of footwear exports from developing economies of the ESCAP region in 1994 was not too different from that of either automatic data processing equipment or office machines and accessories. Second, as markets change rapidly, it is always dangerous to project the future course of trade solely from its past trend. The sudden drop in semi-conductor exports from the same successful economies in 1996 illustrates this point well.

However, it would be useful to extend this illustrative analysis to include more products and countries. The question of whether a country has opportunities to expand its trade is a complex one and may not be satisfactorily answered by any single measure, no matter how useful it is as a first approximation. It is incumbent on each country in the region to evaluate its position in the trade of a particular product carefully by taking into account the various factors that affect its relative competitiveness as well as by paying due attention to the patterns and changes in the demand for imports worldwide.

(Continued overleaf)

---

[a] UNCTAD, *Trade and Development Report, 1996*, (United Nations publication, Sales No. E.96.II.D.6), pp. 124-127.

[b] By focusing on global exports, the figures in the table actually capture this idea, albeit implicitly. Further decomposition in terms of regional export destinations of countries are needed if the feature of growing intraregional trade among the developing countries is to be made more explicit.

(Continued from preceding page)

Selected world export products and major developing country exporters of the ESCAP region

Products/markets and five major developing economy exporters of the ESCAP region (ranked)	*Average 1981-1982*		*Average 1993-1994*	
	Value (millions of US dollars)	*Percentage of world trade*	*Value (millions of US dollars)*	*Percentage of world trade*
1. Automatic data processing equipment (SITC=752)				
Singapore	46	0.3	13 304	14.6
Republic of Korea	24	0.2	2 692	3.0
Hong Kong	42	0.3	1 250	1.4
Thailand	..	..	1 531	1.7
Malaysia	2	0.0	954	1.0
Others	4	0.1	322	1.1
Total developing economies of the ESCAP region	116	0.9	20 053	22.9
Total world trade	13 849	100.0	91 102	100.0
Growth rates of world trade (1982-1994)	–	–	–	17.0
2. Office machines and accessories (SITC=759)				
Singapore	59	0.6	5 725	8.7
Hong Kong	419	4.1	4 213	6.4
Malaysia	1	0.0	3 012	4.6
Thailand	..	..	1 573	2.4
China	..	..	682	1.4
Others	69	0.7	947	1.3
Total developing economies of the ESCAP region	548	5.4	16 352	24.8
Total world trade	10 324	100.0	66 022	100.0
Growth rates of world trade (1982-1994)	–	–	–	16.7
3. Footwear (SITC=851)				
Hong Kong	207	13.6	6 161	17.6
China	..	..	5 380	15.3
Republic of Korea	1 089	11.7	1 842	5.2
Indonesia	..	..	1 738	5.0
Thailand	51	0.5	1 259	3.6
Others	178	1.5	934	2.7
Total developing economies of the ESCAP region	1 525	16.0	17 314	49.0
Total world trade	9 289	100.0	35 093	100.0
Growth rates of world trade (1982-1994)	–	–	–	11.7
4. Special textile fibres and products (SITC=657)				
Republic of Korea	134	3.2	1 019	7.7
Hong Kong	80	1.9	938	7.1
China	..	..	236	1.8
Thailand	17	0.4	120	0.9
Indonesia	..	..	94	0.7
Others	62	1.5	238	1.8
Total developing economies of the ESCAP region	293	7.0	2 645	20.0
Total world trade	4 204	100.0	13 224	100.0
Growth rates of world trade (1982-1994)	–	–	–	10.0

Source: ESCAP secretariat calculations based on United Nations, *International Trade Statistics Yearbook*, 1984 and 1994, vol. II.

Prospects by product categories

Many studies have been carried out for individual countries on possible expansion of exports.[66] Some have been based on production or market surveys and others on the revealed comparative advantage approach. The former are basically impressionistic whereas the latter cannot capture potential comparative advantage as they are based on actual existing data, nor can they cope with intra-industry trade when there are exports and imports in same product lines. Nevertheless, these are all based on the premise that markets will be open and accessible and that a country can develop the wherewithal to meet the market requirements. However, history has shown that frequently the products that are predicted to be important today are not those of major importance tomorrow.[67] Therefore, rather than predict particular products for particular countries, it may be preferable to consider the prospects for broad product types. These can be separated into high-tech products, capital-intensive products and land/labour-intensive products.

It is likely that the newly industrializing economies in East and South-East Asia will be more specialized in high-tech goods and business services, that the other ASEAN members will have a larger emphasis on capital-intensive ones, and that China and South-Asia will have a stronger comparative advantage in land/labour-intensive goods. Of course, the degree of specialization will vary significantly between countries, and there is room for many types of industries within the categories listed above. There will also be an increasing proportion of consumer goods of all types, especially consumer durables, produced in the larger economies of the region.

The pattern of natural resource trade is likely to favour those countries which develop their mineral resources and agricultural and forestry raw materials within a configuration of industries able to use their inputs in an environmentally friendly manner. There will be an increasing proportion of regional trade in such natural resources as industry locates nearer to the market it is serving. However, when trade is intra-firm or of an enclave nature within economies, countries are going to have to be careful to maximize the rents they obtain from it on an ongoing, sustainable basis.

There is likely to be a significant and prolonged increase in regional trade in food products of various sorts. This will be stimulated by the growing numbers of consumers who can afford to purchase the foods they wish as well as the uneven pattern of production possibilities in the region. For example, with the population of South-East Asia expected to increase from 450 million to 615 million, its food and agriculture business market has the potential to triple to $60 billion annually by 2010. This market was $19 billion in 1992, with annual growth rates in the early 1990s in the range of 5 to 12 per cent in different countries, compared with a range of 0 to 3 per cent in the United States and Europe.[68] If producers and exporters are willing to be environmentally friendly, and careful about quarantine and other health controls, many of the smaller countries in the region may find that they are able to exploit niche food markets in their larger neighbours to great effect. Thus the production and export of food commodities should be a growth area in which the historical problems of price volatility and potential oversupply could be tackled through product differentiation and quality control.

There will also be increased trade in basic foods, grains, legumes, vegetable oils etc. along with the growing populations in the region. This is an area for increased regional trade for the efficient producers of these commodities, especially to satisfy

---

66 A selection of such studies includes Andrew Maule, "Some implications of AFTA for Thailand: a revealed comparative advantage approach", *ASEAN Economic Bulletin*, vol. 13, No. 1 (July 1996); Paul Yip, and others "The Asian consumer durable market: with special reference to China", ibid, vol. 12, No. 3 (March 1996); ESCAP, *Expansion of Manufactured Exports by Small and Medium Enterprises (SMEs) in ESCAP region*, Studies in Trade and Investment, No. 3, vol. I, Regional Study (ST/ESCAP/1457); ESCAP, *Myanmar, Trade and Investment Potential in Asia*, Studies in Trade and Investment, No. 19 (ST/ESCAP/1671); and ESCAP, *Promoting Exports of Fish and Fishery Products in Selected Island Developing Countries of the ESCAP Region*, Studies in Trade and Investment, No. 20 (ST/ESCAP/1677).

67 For example, in 1971 it was predicted that the product of growing importance for Thailand would be jute bags.

68 *Bangkok Post*, 17 and 18 October 1996. It is interesting to note that imported food accounted for about a quarter of Malaysia's trade deficit of $334.2 million for the first eight months of 1996.

basic need requirements. There are some indications that the traditionally more or less self-sufficient food producers such as China and India may need imports in the near future, and these demands could be at least partially met from within the region. The progressive implementation of the agreements on agriculture under the Uruguay Round which limit subsidies and other supports to agriculture should assist the price-competitive basic food producers of the region.

Another area for increased trade is the energy sector. At present intraregional trade is growing in petroleum products, natural gas and electricity. It has been estimated that regional crude petroleum production (excluding the Islamic Republic of Iran) is about 7 million barrels a day, with over 90 per cent of production in Australia, China, India, Indonesia and Malaysia, and it is expected to remain at about the same level for the next 20 years. Current exports of about 2.2 million barrels a day are predicted to decline to 1.6 million in 2000 as local demand in producing and exporting countries grows. The major exporters of crude are Australia, Brunei Darussalam, China, Indonesia, Malaysia, Papua New Guinea and Viet Nam. Thus, dependence on imports of crude petroleum from outside the region is expected to rise to 66 per cent in 2000, 72 per cent in 2005 and 77 per cent by 2010.[69] New supplies of natural gas and electricity are coming on stream and an increasing proportion of these outputs are being traded. Irrespective of the energy type, there will be need, particularly in net importing countries, to increase the efficiency of energy use, especially in energy-intensive industries and consumer uses.

It has often been claimed that the most likely area for rapid growth for trade in the region will be in various types of services. These claims are based on the low existing level of such trade and the fact that many of the more advanced developing countries in the region have either started to liberalize significant subsectors in the services areas or have signalled their intention of doing so over the next several years. However, these predictions may prove to be over-optimistic. Trade in business services, such as financial services, banking and insurance, may increase among selected countries of the region, say within ASEAN, in order to provide the same quality of services available to investors and business. However, many countries are not likely to give up their preference for national firms in certain areas such as insurance for some time to come as easily as they did in their reduction of trade barriers, mainly because of lags in the development of their own national firms which could conceivably compete with transnational firms, and a continued desire to have national savings intermediated by nationals. More trade in the transport area is likely as there are serious economies of scale in the provision of transport services; many publicly owned national enterprises in this area are currently a significant drain on national budgets and so are ripe candidates for privatization, which may involve foreign participation. Tourism will continue to be a viable source of export earnings for most countries, especially as the better-off consumers in the region start to explore new destinations.

Challenges

The future of external trade for countries in the region faces several challenges which, if they are not met, may jeopardize the generally bright scenario outlined above. These can be classified into four main groups: those connected with export structure and dependency; with loss of preference; with ongoing global trade liberalization; and with the adaptation of policies in national development strategies.

Export diversification

One of the looming problems is the need to integrate the smaller and weaker members of the region into the regional trade dynamics. There is a serious risk that these countries will be excluded from the export trade in manufactured products, both intermediate and final goods, a risk that they will have to continue to rely on commodity exports of various sorts and a risk that they will be unable to avail themselves of the benefits of an open and competitive trading environment because of structural deficiencies. The need to diversify their sources of export earnings, including within the areas of commodities and services, to diversify markets and to differentiate one country's products from those of others, is particularly urgent.

[69] Kang Wu, analyst from the East-West Center, Hawaii quoted in "Booming local demand eats into Asian crude oil exports", *Bangkok Post*, 30 October 1996, p. 5.

The challenge created by this situation has several dimensions. First, there are several economies in the region, including those in Central Asia and the Mekong region, where efforts towards integration through trade are just starting. Neglecting these economies runs the risk of increased spillovers to the more dynamic ones in the forms of legal and illegal migration, illegal trade and political instability. As has been started for the Mekong region, some degree of conscious fostering of increased trade relations with these economies by other countries in the region can have salutary effects and improve the economic climate for all.

As was pointed out earlier, several countries in the region, particularly some of the least developed and Pacific island countries, still have very concentrated export packages, with more than 60-80 per cent of their export earnings coming from a very limited number of products. Therefore these countries remain very vulnerable to events in these product markets. Often, as they are small suppliers of the products, they have little or no influence on the product markets and so have no control over the evolution of the market or its price trends. Sometimes this risk can be alleviated by differentiating their product from that of other suppliers in terms of quality, such as has been done by some coffee producers, or by meeting environmental or health considerations, such as organic fruits and vegetables, and thus creating a niche market. However this type of action is often copied by others and the advantage gained by the early starters are short-lived. The fast rise and then flattening off of Tongan squash exports to Japan as other Pacific countries expanded into the same market is a classic example. Thus, the vulnerability of the export earnings of these countries requires action to diversify products and markets on a competitive and sustainable basis. This challenge is very daunting in small countries with a limited natural resource base.[70] One feasible way forward appears to be to find opportunities to exploit the growing consumer market for speciality products in the region in a dynamic and innovative way, perhaps in joint ventures with small and medium-sized enterprises from the importing country. This solution would require a host of government and private sector actions which are often difficult to implement in these countries.[71] It would appear that national, regional or international development agencies have a role to play in providing intermediation between the enterprises in the host and home countries, as these firms are often unaware of the possibilities for joint ventures and those which might consider investing abroad are often quite averse to taking risks.

The problem of coping with severely fluctuating export earnings and the effects of sudden sharp shortfalls on the domestic economy remains a challenge for many countries in the region. The situation in South-East Asia, in 1996, with a sudden dramatic drop in export growth, is one example; the sharp reversal of export earnings in Papua New Guinea in 1995 and 1996 compared with earlier years is another; and the effects of devastating cyclones in Samoa which wiped out its copra earnings for several years in a row is a third. The traditional solutions of price or income stabilization measures at the international level, such as commodity price agreements or compensatory financing, have not functioned well. Therefore countries are left to cope with the domestic consequences of such shortfalls themselves. Even at the country level, the earlier approaches to domestic price stabilization for commodity production through marketing boards are out of vogue and most countries are having to learn to live with a greater degree of variability in prices and volumes of export products. One solution is greater use of risk management instruments, but these require a degree of financial sophistication on the part of producers, traders and governments which is still beyond the capacity of a number of countries. Another is to increase the diversity of export products within and outside the sectors suffering from instability in the hope that the downturn in one product will be matched by an upturn in another. Or again, exporters can be left exposed to variations in the hope that they will learn how to remain competitive and deal with market variations on their own.

---

70 For the least developed countries, early operationalization of the draft comprehensive and integrated WTO Plan of Action for the Least Developed Countries (WT/MIN(96)/W/2 of 18 November 1996) would assist, as one of its main aims is export diversification.

71 See, for example, the list of recommendations in ESCAP, *Enhancing Cooperation in Trade and Investment between Pacific Island Countries and Economies of East and South-East Asia in the 1990s*, vol. I, *Issues* (ST/ESCAP/1728) (forthcoming).

Whatever approach is taken to tackle the problems of excessive dependence and export earnings instability, there will be need to find ways of building up or maintaining the competitiveness of products. These efforts include modernizing business processes, particularly in the areas of quality control, productivity, management and marketing, areas which are primarily the responsibility of the private sector. There will also be a concomitant responsibility placed on governments to support the required human resources development, to assist with quality and quarantine control and inspection procedures and to implement up-to-date trade facilitation procedures.

Changes in preference margins

There have been several international trade-related arrangements developed to afford preferential market access to the exports of certain groups of countries because of their relatively low level of economic development. For the Asian and Pacific region, the important schemes were GSP, SPARTECA and the Lomé Conventions. However, the future of such arrangements is now in doubt given the overall low level of tariffs, which make preferential treatment almost unnecessary, and an increasing emphasis on reciprocity.

The evaluation of the impact of reductions in preferences will vary with the existing degree of utilization. The major GSP schemes of the European Union, Japan and the United States have been an important tool for trade creation for many Asian developing economies. They attach significant importance to the continuation of these schemes despite the Uruguay Round as they still provide some, though declining, margin of preference over suppliers from developed countries. The most important beneficiaries in Asia under the various GSP schemes to date have been China and the ASEAN-6 (Brunei Darussalam, Indonesia, Malaysia, Philippines, Singapore and Thailand).[72] However, during recent years, the schemes have been modified to favour imports from least developed countries as their export performance continued to be rather weak in comparison with that of the more advanced GSP beneficiaries. For example, the new GSP scheme of the European Union, which entered into force in 1995, has two major components, the graduation mechanism, and the tariff modulation mechanism which replaces the system of quotas and ceilings. A combination between the development index and the specialization index will determine whether a good from a particular source is entitled to GSP preferences.[73] This will favour countries that diversify their exports and those with low per capita incomes.

The impact of the graduation mechanism on Asia as a whole is likely to be trade-redistributive. The phasing-out of the GSP benefits of well-advanced Asian developing countries will reduce their export volumes under the various GSP schemes and allow others, less advanced countries, to expand trade under preferential conditions.[74] However, trade-reducing effects might occur even for some least developed countries owing to the graduation of certain products, especially traditionally sensitive products in which these countries have a comparative advantage.

The beneficiaries of the other two schemes, mainly selected Pacific islands, have not taken any real advantage of the preferences except in specific cases (for example, Fiji, for garments and Samoa,

---

72 For the European Community, China and the ASEAN-6 each accounted for about 30 per cent of the total value of GSP-related trade to date. The members of SAARC accounted for another 12 per cent.

73 The graduation mechanism is applied progressively and follows a schedule determined by the beneficiary country's specialization (the ratio between the beneficiary's global share in European Union imports and the beneficiary's sectoral share in European Union imports) as well as its development index, calculated on the basis of the country's relative per capita income and its relative exports. Based on index values provided by the European Commission, Hong Kong, Singapore and the Republic of Korea are among the most developed under the GSP scheme, Malaysia and Thailand are in the second most developed group, China, India and Indonesia in the third group, Pakistan and the Philippines in the fourth, and Sri Lanka in the fifth.

74 Asian countries affected by partial graduation of certain products are the Republic of Korea for cars, rubber, plastics, leather, consumer electronics, steel, textiles, clothing and miscellaneous goods; Hong Kong for clothing, leather, jewellery, certain consumer electronics, clocks, and miscellaneous goods; Brunei Darussalam for jewellery and precious metals; and Singapore for certain consumer electronics. For other countries, partial graduation is scheduled to take place on 1 January 1997 and 1 January 1998.

for automobile parts under SPARTECA, and Fiji for sugar and several countries for tuna under the Lomé Conventions).[75] Therefore in many countries the erosion of preferential access is likely to go virtually unnoticed. However, in the others certain sectors will be under considerable pressure either to improve productivity or diversify products and markets.

Ongoing global trade liberalization

Much has been said and written in the period since the end of the Uruguay Round and the establishment of WTO about the issues which remain unresolved and the implications and risks arising from the implementation and interpretation of existing agreements.[76] In the following paragraphs a few of these outstanding concerns are highlighted.

One of the challenges for Asia and the Pacific is the tendency, now that tariffs have been significantly reduced, for the governments of major developed countries to use non-tariff measures to block or reduce imports which are seen as threatening to local producers. In this regard, the major WTO-consistent instruments are anti-dumping and countervailing duty actions, that is, actions which can be taken when it appears that the exporter is charging less than a fair price for his product. In one year, between 1 July 1994 and 30 June 1995, about half of the 153 anti-dumping and countervailing investigations initiated and reported to WTO were targeted at Asian developing countries.[77] Anti-dumping actions are difficult to contest as there is often no world comparator reference price and, by the time legal action is completed, the market niche may be occupied by another supplier. This is especially true when the cases involve small or medium-sized firms, because of the complexities of the system and the cost of compliance in investigation proceedings. Thus there is some evidence that the percentage of cases with restrictive outcomes is higher for Asian developing countries. These countries also have a more difficult time in protecting their own industries against injury through using the anti-dumping and countervailing duty provisions, because of a lack of adequate expertise, personnel and financial resources to undertake such action.

One of the challenges to the maintenance of an open world trading system is to have a dispute settlement mechanism which functions efficiently and whose outcome is accepted as fair by all parties. The mechanisms agreed to during the Uruguay Round are a considerable improvement on the previous ones and to date seem to have been working better in terms of both time taken to reach a settlement (much shorter) and the acceptance of the result by the country whose actions were contested. There also appears to be more of a willingness to have disputes settled through WTO than before, when there was more frequent recourse to unilateral action, or sometimes bilateral negotiations and settlement. However, there is still concern that it would only take a couple of unresolved cases or disputed outcomes to destroy this image of fairness and resort to other means to settle problems might become more frequent.

The trend towards increased liberalization of trade in services and increases in the volume of this trade poses several risks for the region. The risks vary significantly between the types of services being liberalized. For example, increased trade in financial services reduces the impact of actions by national monetary authorities on money supply or interest rates and so increases the risk of transmission of financial sector problems from one country to another. It also increases prudential risks and hence the need for prudential regulatory functions to be carried out at a level of efficiency and sophistication comparable with that in more advanced countries. If a bank or other financial intermediary fails in one country, its activities in other countries will also be affected. There is a risk of significant

---

75 The limited use which the majority of Pacific islands have made of the preferential access provisions is a reflection of the fundamental difficulties faced by many of them in diversifying their product base and their markets beyond their exports of primary commodities to traditional importers.

76 See, for example, the series of background studies presented at the ESCAP/UNCTAD/UNDP Meeting of Senior Officials to Assist in Preparation for the First WTO Ministerial Conference, Jakarta, 4-6 September 1996, reproduced in ESCAP, *Asian and Pacific Developing Economies and the First WTO Ministerial Conference: Issues of Concern*, Studies in Trade and Investment, No. 22 (ST/ESCAP/1705), as well as those prepared for ADB, Study of the Emerging Trading Environment and Developing Asia, Conference on Country Studies, Manila, 29-30 August 1996.

77 See WTO, Trade Policy Review document No. 22 (WT/TPR/OV/1), December 1995, appendix tables 4 and 6.

concentration in the number of firms providing financial services and so magnifying the impact of problems with any one of them. It is also likely that the major providers of financial services are firms headquartered outside the region, and so beyond the direct influence the regional users of the services provided. The need for better transparency of operations and sharing of information among regulatory agencies, not to speak of harmonization of regulations, assumes greater urgency. Having different rules on transparency and different regulations will allow firms to move between markets at will to avoid reporting or sanctions.

For trade in professional, construction and other business services, increased trade implies increased freedom of movement of persons and this presents a challenge in terms of immigration rules and developing a better understanding of cross-cultural differences. Increased trade in telecommunication services has implications for the pricing of such services, which have been subsidized in many countries of the region, for the collection of revenues from their provision and for the maintenance of control over coverage, quality and content. These are areas of concern, for example, to developing countries wishing to maintain a cultural identity.

The balance-of-payments impacts of freeing trade in travel-related services, including for leisure, education, health and business, are highly uncertain, especially for less developed countries unable to compete in supplying these services. The liberalization of trade in services related to transport, freight and insurance should help improve efficiency and productivity but is likely to cause sizeable challenges for small suppliers of these services, including those where national airlines or shipping lines are considered as an important national symbol.

In all, while GATS explicitly recognizes the development dimension in the services field and has allowed for considerable flexibility in making offers for liberalization in different subsectors, there will be pressure to speed up the liberalization of services as this appears to be a growth area and so offers considerable financial returns. In this regard, the first WTO Ministerial Conference in Singapore declared: "we are determined to obtain a progressively higher level of liberalization in services on a mutually advantageous basis with appropriate flexibility for individual developing country members",[78] with immediate negotiations focusing on basic telecommunication and financial services and then maritime transport services and accountancy. The other areas presenting challenges to the countries of the region include emergency safeguard measures, government procurement services and subsidies. To remain outside the negotiations is really not an option if the points of view of Asian and Pacific countries are to be taken into account; rather, active engagement is needed.

Another related challenge is the new limits put on the use of TRIMs under the TRIMs agreement. While most countries have already, and on an autonomous basis, reduced the use of export requirements, trade-balancing requirements and other instruments related to trade, their desire to use FDI as an instrument for trade enhancement and economic growth may run counter to the intentions of foreign investors; there is always the possibility of the transnational corporations and the host government having very different objectives. "While recognizing that the links between trade and investment are likely to become stronger as liberalization and globalization trends become more pervasive, governments continue to feel the need to apply measures designed specifically both to attract and to regulate FDI. Many developing countries use investment incentives and performance requirements to pursue a variety of development objectives: to orient resource allocation to sectors considered to have particular growth potential; to build up a viable domestic private sector; to promote vertical integration; to attract foreign technologies or export-oriented investments; or to improve access to major markets and export marketing capacities. In many cases, moreover, since policy instruments to ensure free domestic competition are not sufficiently effective or enforceable vis-à-vis large foreign enterprises, investment measures are relied upon to correct market distortion created by these enterprises."[79] Thus

---

78 WTO, *Singapore Ministerial Declaration* (WT/MIN(96)/DEC), document presented at the Ministerial Conference held in Singapore, from 9 to 13 December 1996.

79 UNCTAD, "The General Agreement on Trade in Services follow-up negotiations", paper presented at the ESCAP/UNCTAD/UNDP Meeting of Senior Officials to Assist in Preparation for the First WTO Ministerial Conference, Jakarta, 4-6 September 1996 and reproduced in ESCAP, *Asian and Pacific Developing Economies...*, chap. 3.

there is a delicate balancing act to be conducted in keeping a favourable environment for foreign investment and strengthening the TRIMs agreement and its implementation. Probably the most conducive approach would be to strengthen competition policy at the national, and perhaps subregional level through regional trade arrangements, and to try to introduce at the global level a symmetry between the elimination of TRIMs and the introduction of norms of competition policy. However, as competition policy is a relatively new topic at the national level in practically all countries of the region, more work is needed to consider the appropriate types of national rules and, equally or more importantly, to develop a national regulatory capacity.[80]

One area of serious contention, particularly for Asian developing countries which are viewed as low-wage economies with liberal laws on wages and labour conditions, is the tying of trade to the respect of certain labour standards. "Since the end of the Uruguay Round, the issue of trade and labour standards has come to the forefront of the policy agenda. The protracted rise in unemployment in many OECD countries and in wage inequality in some countries has led some observers to look for external explanations, including claims of unfair trade practices associated with competition from firms that allegedly base their comparative advantage on low labour standards."[81] Given that there is no universal agreement on a minimum labour standard beyond the internationally recognized core standards of ILO, the imposition of externally decided standards is viewed legitimately by developing country exporters as unfair. They have very different standards of living and there are serious difficulties in enforcing compliance in economies with a large informal sector. The latest decision on this issue at the WTO Ministerial Conference states "we reject the use of labour standards for protectionist purposes, and agree that the comparative advantage of countries, particularly low-wage developing countries, must in no way be put into question".[82] The countries of Asia and the Pacific now have to be prepared to meet the challenges posed in any future discussions in this area.

The discussions on environmental standards for traded goods have been quite contentious and these standards have been viewed as another non-tariff barrier, especially when they are unilaterally or solely applied to developing country exports. They are also seen as placing an unfair financial burden on developing countries which cannot afford to implement developed country standards. However, these standards can also be used for the benefit of developing countries. For example, the certification of the environmental advantages of some products, such as organic coffee or fresh fruits and vegetables meeting quarantine regulations, could increase the demand for these products. It is very likely that many more environment-related standards will be developed over the next few decades as the international community becomes more sensitized to the environmental hazards of certain production methods and certain products. There will thus be a need for Asian and Pacific countries to be aware of the issues under debate, to take an active part in the discussions to ensure fairness and to turn the issue to their favour. It is likely that the growing groups of consumers and non-governmental organizations in these countries themselves will also be lobbying for certain standards to be met domestically, and the lobbies can assist in the international arena.

One of the greatest challenges to an open world trading system is the position taken on the supremacy of national laws and the use of these laws to justify overriding or negating international obligations. This challenge faces all governments of the world, but the consequences of such actions are more serious for the trading system in general and for exporting developing countries in particular when a major trading partner favours its national laws. When a major power goes its own way without regard for international obligations, there are repercussions for many countries and little leverage to enforce compliance with these obligations. Therefore the health of the international trading system depends to a large extent on the respect for its agreed rules accorded by major trading parties.

Adaptation of policies for national development

For most of the post-Second World War period, developing countries have used a range of instruments, some of which can be considered trade-restricting and discriminatory, to meet their national development concerns. These took the form of

---

80 For a discussion of this issue, see UNCTAD, "Competition policy and its interface with trade and investment", ibid, chap. 7.

81 OECD, *Trade, Employment and Labor Standards: Summary of a Study of Core Workers' Rights and International Trade* (Paris, 1996), p. 3.

82 WTO, *Singapore Ministerial Declaration...*, para. 4.

infant industry protection through tariff and non-tariff barriers to local industry, trade-related subsidies and performance standards etc. Many countries in the region have relaxed most of these barriers autonomously in recent years in order to avail themselves of the benefits of greater participation in the international trading system. Thus, the fact that many of the past policies are now WTO-incompatible may not be very restrictive of national development strategies. It also appears that there is still room for selected interventions. There is considerable room for flexibility for the least developed and selected other low-income countries,[83] and in two key sectors, agriculture and textiles, there is still scope for selective government interventions by all developing countries. Nevertheless, devising WTO-consistent trade strategies to promote long-term development will be a challenge in most countries in the Asian and Pacific region.

Many of the countries in the region, including the first- and second-generation newly industrializing countries, recognize the urgent need for upgrading and modernizing their industrial sectors in line with changing comparative advantage, whereas others, as noted earlier, have a need for diversification of their export base. To meet these challenges, governments need to review their policy packages, monitor their implementation and make adaptations as and when required. There will be a need almost universally for enhancing the role of the private sector to undertake productive activities and for changing the role of the government towards facilitation, supervision and regulation. The improvement of trade facilitation and efficiency is also a high priority, through modernizing and standardizing customs procedures, upgrading packaging and transport modes, upgrading and extending knowledge of modern marketing modalities and increasing the use of electronic communications systems, risk management markets etc. While these are useful undertakings in themselves and may help to improve the competitiveness of certain exports, they will not necessarily lead to upgrading or diversification of production per se. The enabling policies of the government for skills development, research and development, access to and absorption of technology, and the like are crucial for continuing to exploit dynamic comparative advantage in trade. Policies by governments to support small and medium-sized enterprises and small-scale producers of exported agricultural or fisheries products are also essential, but not easy to devise in a market-friendly way. Increased government and private sector cooperation within a framework of agreed sharing of responsibilities would be of considerable assistance in facing this challenge.

Governments also face serious challenges in the area of employment as their economies adapt to changing comparative advantage. Some mismatches between the skill composition of the labour structure and the production structure may lead to pressure for migration and tensions with the local population. This issue may be especially difficult to manage in countries with growing unskilled or semi-skilled labour surpluses, unless sufficient attention is paid to the upgrading of skills. Temporary migration of unskilled or semi-skilled labour to labour-deficit countries may also raise tensions between countries, especially when demand for these workers decline.

Countries also have non-economic objectives which may justify selective interventions, particularly in the food and energy sectors. The risks of too high a degree of import dependency for these sectors is recognized by almost every country from Europe to the South Pacific, although the definition of "too high a degree" varies considerably. The challenges for the region will be how to balance these legitimate concerns with market forces and efficiency considerations and how to cope with increased competition for access to and control over strategic natural resources. Minimizing regional conflicts would appear to be one way of minimizing the dangers from a high degree of food or energy dependence, but countries are still likely to wish to preserve a certain domestic capacity in these areas. There is also likely to be a rise in tension among countries over, for example, underwater petroleum and gas reserves or fish stocks, unless some common understandings can be reached.

Another difficult challenge for many countries is generating enough financial resources to carry out all the above (see chap IV). Ensuring access to adequate credit to finance trade, both export and import, remains an important problem in most countries of the region, in particular for their small and medium-sized private sector enterprises. The development of trade-financing institutions, either nationally or subregionally, is still in its infancy.

---

83 See UNCTAD, *Trade and Development Report, 1996* (United Nations publication, Sales No. E.96.II.D.6), part II, chap. III, pp. 156-157.

ANNEX

Annex table III.1. Three major exports of selected economies in the Asian and Pacific region (at the SITC Revision 2 group level, average 1981-1982 and 1991-1992)

	As percentage of country merchandise exports	
	1981-1982	1991-1992
Bangladesh	**63.5**	**67.9**
Make-up articles, wholly or chiefly of textile materials n.e.s.	25.3	
Textile fabrics, woven, other than cotton fabrics	22.9	
Jute	15.2	
Clothing accessories		51.0
Other woven textile fabric		8.6
Shellfish fresh, frozen		8.4
Brunei Darussalam	**96.7**	**94.2**
Crude petroleum	56.4	49.1
Gas, natural and manufactured	40.3	41.3
Petroleum products, refined		3.8
Cambodia	**37.6**	**84.6**
Ores and concentrates of non-ferrous base metals	25.1	
Structures and parts nes	12.5	
Wood		45.5
Clothing accessories		28.1
Natural rubber, gums		10.9
China[a]	**19.8**	**20.7**
Clothing accessories	9.8	12.5
Crude petroleum	5.3	
Parts and accessories of road motor vehicles, passenger motor cars, motor vehicles for transport of goods, materials and electrical apparatus such as switches, relays, fuses and plugs	4.7	
Footwear		4.4
Toys, sporting goods, etc.		3.8
Fiji	**85.4**	**73.2**
Sugar and honey	76.1	44.7
Fish, crustacea and molluscs tinned, prepared	7.2	
Clothing accessories		21.4
Gold, non-monetary		7.0
Hong Kong	**52.4**	**43.4**
Clothing not of fur	33.5	31.1
Perambulators, toys, games and sporting goods	10.1	
Watches and clocks	8.7	6.4
Parts of and accessories suitable for office machines and automatic data processing machines and units thereof		5.9
India	**26.1**	**26.2**
Clothing not of fur	10.1	8.3
Pearls and precious and semi-precious stones, unworked and worked	9.3	14.5
Iron ore, concentrates	6.7	
Cotton fabrics, woven		3.4
Indonesia	**76.9**	**41.0**
Crude petroleum	62.9	17.6
Gas, natural and manufactured	14.1	13.0
Veneers, plywood, improved or reconstituted wood		10.3
Iran (Islamic Republic of)	**92.5**	**92.4**
Crude petroleum	81.0	88.7
Petroleum products	11.5	
Floor coverings		3.7
Kiribati	**87.8**	**97.0**
Oil seeds, nuts, kernels	67.6	70.8
Wood rough	10.2	
Cotton	10.0	
Fish, fresh, chilled or frozen and fish, dried, salted or in brine; smoked fish		15.3
Crude vegetable meterials, n.e.s.		10.9
Malaysia	**48.6**	**34.6**
Crude petroleum	26.5	
Wood rough	10.6	
Rubber crude, synthetic	11.6	
Thermionic, cold and photo-cathode values, tubes and parts		13.8
Crude petroleum, gas, natural and manufactured		12.9
Other wood in the rough or roughly squared and wood, simply worked, and railway sleepers of wood		7.8
Maldives	**85.7**	**92.9**
Fish, fresh and simply preserved and fish, crustacea and molluscs tinned, prepared	80.3	49.4
Tea and mate	5.4	
Clothing accessories		43.5

(Continued on next page)

Annex table III.1 *(continued)*

	As percentage of country merchandise exports	
	1981-1982	1991-1992
Myanmar	**53.7**	**54.2**
Rice	28.3	
Wood	25.5	22.1
Vegetables, fresh, chilled, frozen or simply preserved; roots, tubers		16.2
Special transactions		15.9
Nepal	**46.2**	**79.8**
Leather	18.9	
Floor coverings, tapesteries, etc	16.2	51.9
Rice	11.0	
Clothing accessories		21.2
Vegetables, fresh, chilled, frozen or simply preserved; roots, tubers		6.6
Pakistan	**37.5**	**56.4**
Rice	15.2	
Cotton	11.5	8.2
Cotton fabrics, woven	10.8	
Textile yarn; cotton fabrics woven; fabrics, woven, of man-made fibres		35.8
Made-up articles wholly or chiefly of textile materials and floor coverings		12.4
Papua New Guinea	**65.0**	**75.9**
Ores and concentrates of non-ferrous base metals	49.9	
Coffee	13.1	
Gold, non monetary		34.7
Ores and concentrates of base metals, n.e.s.		34.0
Other wood rough, squared		7.2
Philippines	**41.8**	**37.6**
Special transactions	23.8	16.6
Sugar and honey	9.7	
Ores and concentrates of non-ferrous base metals	8.3	
Transistors, valves, etc		10.6
Clothing accessories		10.4
Republic of Korea	**32.0**	**20.6**
Clothing not of fur	17.1	
Ships and boats	9.8	5.6
Footwear	5.1	
Thermionic, cold and photo-cathode valves, tubes and parts		9.7
Fabrics, woven, of man-made fibres		5.3
Singapore	**41.3**	**40.0**
Petroleum products	26.8	14.6
Special transactions	7.9	
Electrical machinery n.e.s.	6.6	
Automatic data processing machines and units thereof; parts of and accessories suitable for office machines		18.3
Television receivers, radio broadcast receivers, sound records, broadcast receivers, sound recorders, gramophones, dictating and sound recorders		7.1
Solomon Islands	**65.8**	**80.6**
Wood rough and wood shaped	34.2	39.2
Fish, fresh, chilled or frozen and fish, dried, salted or in brine; smoked fish	31.7	32.8
Other fixed vegetable oils		8.6
Sri Lanka	**60.8**	**64.8**
Tea and mate	31.9	17.3
Clothing not of fur	15.9	41.1
Petroleum products	13.0	
Pearls, precious and semi-precious stones, unworked or worked		6.3
Thailand	**36.1**	**17.9**
Rice	16.1	4.3
Vegetable, fresh, chilled, frozen, simply perserved;roots, tubers	12.2	
Sugar and honey	7.9	
Fish, crustaceans and molluscs fresh, chilled, frozen, salted prepared or preserved, n.e.s.		8.7
Part of and accessories suitable for office machines and automatic data processting machines and units thereof		4.9
Tonga	**67.2**	**83.1**
Other fixed vegetable oil non-soft	26.6	
Oil seeds, nuts kernels	21.2	
Fruit fresh, and nuts fresh or dry	19.4	
Vegetable, fresh, chilled, frozen, simply perserved; roots, tubers and other edible vegetable products, n.e.s., fresh or dried		60.1
Spices		13.3
Fish, crustaceans and molluscs, fresh, chilled, frozen, salted prepared or preserved, n.e.s.		9.7
Vanuatu	**87.5**	**72.4**
Oil seeds, nuts kernels	72.7	33.3
Meat fresh, chilled, frozen and meat dried, salted, smoked	14.7	15.6
Special transactions		23.5

Source: ESCAP secretariat calculations based on UNCTAD, *Handbook of International Trade and Development Statistics*, 1984, 1985, 1991 and 1994.

[a] 1988-1989.

Annex table III.2. Trade regimes in selected Asian and Pacific economies

Trade regime / Country	Tariff assistance (applied tariff levels)	Non-tariff barriers	Tariff predictability (WTO bindings)	Time-bound schedules/plans of trade liberalization	Membership in regional arrangements affecting trade
AUSTRALIA	Close to 50% of imports enter free of duty and an additional 20% qualify for free entry under system of tariff concessions for specified industries or purposes. Most tariffs have ceilings of 10 or 15%, with exceptions mainly for passenger motor vehicles and textiles, clothing and footwear products. Overall unweighted tariff average around 12% (1992); weighted average tariff was 4.1% in 1993/94; a projected 2.8% in 1996/97; and a projected 2.2% in 2000/01.	Restrictive technical requirements and design rules for automobiles, certain automobile parts, electronic equipment, medical and telecommunications equipment, and machinery parts and equipment.	94% tariff lines are bound. Tariffs on non-agricultural products remain at a high level. Products have tariffs much higher than those of other developed economies,[a] such as certain clothing (maximum 55%), motor vehicles (maximum 40%), electrical machinery (maximum 23%) and glass (maximum 23%).	White Paper (May 1994): with the exception of certain automotive products, all other tariffs are to be reduced in stages to 5% by 1 July 1996; the tariff rate on passenger motor vehicles and their original equipment components, currently 25%, will be reduced in stages to 15% by 1 January 2000; tariffs on light commercial and four-wheel drive vehicles and components to 5% by 1 July 1996; replacement components for passenger vehicles will remain at 15% from 1 July 1996 until 2000. By 1 July 2000, Australia will reduce tariffs on carpets to 15% (currently as high as 25%), on textile, clothing and footwear items to a maximum of 25%; on cotton sheeting and woven fabrics, tariffs will fall to 15% from the current maximum rate of 28%; on apparel and certain finished textiles, to 25% (now up to 40%); on footwear, to 15% (now up to 30%) and on footwear parts, to 10% (now up to 17%).	APEC, CER, SPARTECA
BANGLADESH	Customs duties vary between 7.5% and 50%; levied on all imports except raw cotton, textile machinery, machinery for irrigation and agriculture, animal feeds used by the poultry and dairy industries, drugs and medical equipment. The average trade-weighted import tariff rate has been brought down to around 21% (1994/95).		Commitments in its WTO tariff schedule are negligible. A small number of agricultural and machinery items are bound at 50%, with a 30% surcharge. All other products are bound at the prohibitive rate of 200%.		SAARC (SAPTA)

(Continued on next page)

Annex table III.2 *(continued)*

Trade regime / *Country*	*Tariff assistance (applied tariff levels)*	*Non-tariff barriers*	*Tariff predictability (WTO bindings)*	*Time-bound schedules/plans of trade liberalization*	*Membership in regional arrangements affecting trade*
CHINA	Nominal MFN tariffs range from 3% on promoted imports to over 150% on discouraged imports, such as automobiles. Average nominal tariff exceeded 35% (1995) trade-weighted average tariff 43% (1994), with finished goods more heavily protected than upstream inputs.[b]	Multiple, overlapping non-tariff barriers that restrict imports (mainly import licenses and import quotas). Non-trade barriers restrict the types and numbers of entities that have the legal right to engage in international trade. Foreign exchange balancing regulations.	Offer made in WTO accession negotiations would lead to a 17% simple average industrial tariff. China's present tariff offer, apart from applying a high simple average tariff, includes almost prohibitive rates on many specific products (i.e. 50% for consumer electronics).	In November 1995, announced tariff reductions on more than 4,000 tariff line items in 1996, and second-phase reductions planned for 1997. China's stated goal is to bring average nominal tariff down to 23% in 1996, and to make further reductions to about 15% in 1997. China agreed to undertake further eliminations of non-tariff import barriers in 1996 and 1997.	APEC, EAEC
JAPAN	Generally low (exceptions: agar-agar, sugar, confectionery, chocolate, cheese and dairy products, jam, smoked salmon, winter sport goods) Unweighted average 3.91 (7.2 for industrial goods) (1994)	Tariff quotas; import licences; global and MFA quotas; variable levies; state import monopoly; sole importing agency.	99% of tariff lines bound.		APEC, EAEC
HONG KONG	No customs duties on imports	No quantitative restrictions for considerations other than health, safety or the environment.	Tariffs are bound on only 23% of industrial products (29% by value).		APEC
INDIA	Effective customs duties are high. Peak tariff rates 50% (1996); import-weighted average 30-33%.	Import licensing regime. Ban on mainly consumer goods imports. Other quantitative restrictions under the negative imports list.	India undertook a two-tier offer on industrial products, binding tariffs in excess of 40% at 40% and binding tariffs below 40% at 25%.	Goal of a 25% import-weighted average by fiscal year 1996/97.	SAARC (SAPTA)

(Continued on next page)

Annex table III.2 *(continued)*

Trade regime / *Country*	*Tariff assistance (applied tariff levels)*	*Non-tariff barriers*	*Tariff predictability (WTO bindings)*	*Time-bound schedules/plans of trade liberalization*	*Membership in regional arrangements affecting trade*
	Especially high tariffs on agricultural and consumer items. Some telecommunications projects granted a special 25% rate. Exorbitant effective rates of 290% assessed on distilled spirits.	Countervailing duties raise effective tariff rates significantly. Encourages counter trade.	Some industrial goods, e.g. automobiles and all consumer products were excluded from the offer. Scope of bindings on industrial goods increased substantially from 12% of imports to 68% once all reductions are staged in; however, the overwhelming majority of these bindings exceed current Indian applied rates of duty. In agriculture, tariff bindings are higher than actual rates in important sectors, ranging from 100 to 200%.		
INDONESIA	Applied tariff rates range from 5 to 30% A number of products are subject to import surcharges. Simple average tariff, including surcharges, is 20%; average (unweighted) tariff is 14.2% (1996). Significant tariff dispersion; the average tariff rate on final goods is double that for unprocessed products. Substantial tariff escalation exists in industries such as transport equipment, textiles and paper products. The manufacturing sector is the most highly assisted, with average effective assistance over 50%.	Many major bulk food commodities, such as wheat, rice, sugar and soybeans, are subject to non-tariff barriers. Sole importer is the National Logistics Agency. Prices of these commodities are often higher than world market prices (sugar and soybean prices are about 40% higher than import parity prices). All processed goods are subject to a 10% value-added tax. A luxury tax ranging from 20 to 35% is also levied on certain products.	Tariff bindings to increase from under 10% to 95% of its tariff lines (8,877 items, of which 7,536 on industrial products), at ceiling rates of 40%. Exceptions are automotive equipment, iron and steel, chemical, plastic and rubber products, and agricultural equipment. Agreed to tariff its non-tariff barriers on agricultural products.	Surcharges and non-tariff measures on bound items to be removed within 10 years, i.e. by 2005. The January 1996 package continued the reduction in the number of import surcharges to 77; 27 of those will be phased out in line with WTO commitments.	ASEAN (AFTA), EAEC, APEC

(Continued on next page)

Annex table III.2 *(continued)*

Trade regime / *Country*	*Tariff assistance (applied tariff levels)*	*Non-tariff barriers*	*Tariff predictability (WTO bindings)*	*Time-bound schedules/plans of trade liberalization*	*Membership in regional arrangements affecting trade*
MALAYSIA	In 1994, tariffs were reduced or eliminated on 600 items, including machines and machinery parts, refrigerators and freezers, and electrical and electronic equipment. Tariff reductions agreed to in the Uruguay Round trade negotiations include reductions or outright elimination on 1,400 industrial raw materials, 600 food items, cars (but with a top rate of 200%), textiles and consumer durables.	Licences for normally prohibited goods. Short list of prohibited manufactured imports to protect pioneer industries. System of licensing on built-up automobiles. Strict controls on imports of whole chickens and chicken parts. Passenger cars are subjected to specified local-content requirements.	Average bound duty 15%, with higher rates on industrial products. Peak tariffs of over 50% affect some industrial sectors.		ASEAN (AFTA), EAEC, APEC
NEW ZEALAND	Tariffs on most goods manufactured in New Zealand fall within the range of 5-15% (1996). Tariff average around 6%, and no *ad valorem* tariff exceeds 30%. Rates in some sectors remain relatively high (motor vehicles, tires, textiles (except yarns), curtains, carpets, clothing and footwear range from 20 to 30%; passenger vehicles and original equipment tires, 25%; replacement tires, 15%; clothing and adult shoes, 30%; children's shoes, 25%; and carpets, 20%; distilled spirits, 13 to 20%). 49% of the tariff lines are duty-free. The average rate for tariff lines actually subject to duty was equal to 14.6% (1996). Great unevenness in the tariff structure; tariffs are higher on fully processed goods.	Strict regime of sanitary and phytosanitary control for all imports of agricultural products.	Coverage of its tariff bindings increased from 55% to over 99% of lines. All tariffs on agricultural products have been bound. The only remaining unbound tariffs are on 10 lines concerning used clothing, used footwear and used motor vehicles. The implementation period for most products ends in 1999, the exceptions being pulp, paper and printed material. The average bound rate will be 7.1 % for agricultural products and 12.8% for other products.	Tariff rates on "sensitive" products scheduled to be reduced to 5% by 2000. Tariffs on pharmaceuticals will be eliminated by 1 July 1997, on beer by 1 July 2002, and on pulp and paper by 1 July 2004. Unilateral tariff reduction plan for 1 July 1997 through 1 July 2000 which will reduce all tariffs to no more than 15%; goods with a tariff rate over 20% in 1996 will have a rate of 15% in 2000; goods at 15-20% in 1996 will have rate of 10% in 2000; goods at rates below 15% in 1996 will have rate of 5% in 2000 (with the exception of car parts, which will carry a tariff of 10%). Goods with a tariff of 5% in 1996 will enter duty-free after 1 July 1998.	APEC, CER, SPARTECA

(Continued on next page)

Annex table III.2 *(continued)*

Trade regime / Country	Tariff assistance (applied tariff levels)	Non-tariff barriers	Tariff predictability (WTO bindings)	Time-bound schedules/plans of trade liberalization	Membership in regional arrangements affecting trade
PAKISTAN	Tariff regime is characterized by complexity, broad discretionary powers, and lack of transparency. Arbitrary and inconsistent customs valuations and frequent changes in rates. Maximum tariffs are at 65%. The average tariff rate (exclusive of the temporary duty) is about 45%. Some imports can be exempt from any duties for a specific period of time (plants and machinery for the power sector).[c]	The negative list of items banned for religious, health security or other reasons comprises 75 items.	Only 40% of the 2,128 Pakistani tariff items are bound. Primary products and agricultural products are bound at prohibitive levels (100 to 150%), while in the industrial sector bindings have been made at 65%.	Under the Uruguay Round commitments, Pakistan had announced plans to reduce the tariff structure from about 150-200% to about 50% by 2004.	SAARC (SAPTA), ECO
PHILIPPINES	Four-tier rate structure: 3% for basic raw materials; 10% for raw materials, capital equipment for which no locally produced substitutes are available and spare parts; 20% for intermediate and semi-processed goods and capital equipment for which there are locally produced substitutes; 30% for finished goods. The progressive nature of duties provides a high degree of effective protection for the manufacturing industry.	Expanded value-added tax law effective since 2 January 1996 contains a discriminatory provision against imported meat by subjecting the latter to the 10% VAT, while exempting domestic meat. Discriminatory excise tax on spirits; specific import restrictions on some 100 agricultural and industrial products. Ban on imports of many agricultural products,[d] e.g. corn and corn substitutes (including wheat for feed), poultry and poultry products, and meat and meat	Only 37% of tariffs lines are bound. Has yet to implement its WTO agricultural commitments though it had promised to do so by July 1995 (only ASEAN member of WTO that has not done so).	Executive Orders No. 264 of 28 August 1995 (covers chiefly industrial goods) and No. 288 of 15 January 1996 (covers agricultural commodities, excluding "sensitive" products) established a four-tier tariff structure with rates of 3, 10, 20 and a maximum 30%,[e] through phased reductions. Average unweighted tariff levels will decline between now and the year 2000, from 13.47 to 7.46% for manufactured goods; from 5.73 to 3.90% for mining sector goods; and from 20.76 to 13.08% for agricultural goods. The programme excludes certain "sensitive" agricultural products, whose current quantitative bans or restrictions are required under WTO commitments to be tariff equivalents, with minimum imports quotas at much lower tariffs.	ASEAN (AFTA), EAEC, APEC

(Continued on next page)

Annex table III.2 *(continued)*

Trade regime / Country	Tariff assistance (applied tariff levels)	Non-tariff barriers	Tariff predictability (WTO bindings)	Time-bound schedules/plans of trade liberalization	Membership in regional arrangements affecting trade
	The average of effective duties was 10.7% on raw materials; 19.7% on semi-finished products; and 26.5% on finished products; average duty, 20% (1995).	products (except beef and beef products). The National Food Authority remains the sole authorized importer of rice and corn. Standards compliance is required for imports of 30 specific products, including lighting fixtures, electrical wires and cables, portland cement		The overall unweighted average tariff level will decline from 14.28 to 8.16% by 2000.	
REPUBLIC OF KOREA	Average tariff rate, 7.9%; products subject to a tariff rate of at least 30% or higher include certain meat, poultry, offal, most fruits and nuts, many fresh and processed vegetables, all flour and starches, peanuts, various vegetable oils, juices, jams, peanut butter, soups, beer and distilled spirits and dairy products. Foreign passenger vehicles are subject to an applied rate of 8%; cascade system of high taxes on top of the 8% tariff, three of which are based on engine size. Emergency tariffs to respond to import surges. Duties still remain very high on a large number of high-value agricultural and fisheries products. Tariff rates above 45% on most horticultural products, such as shelled walnuts, table grapes and citrus. Most tariffs on textile and apparel products: 7.5% for man-made fibres, 15% for yarns, 30% for fabrics and made-up goods and 35% for apparel.	import licensing system. Tariff-rate quotas. Within-quota tariff rates are to be maintained at zero or low levels. Over-quota tariff rates on some products are quite high, e.g. a number of agricultural products have out-of-quota tariff rates of over 200%. Agricultural and fishery products are restricted or prohibited, i.e. subject to quotas or tariff-rate quotas with prohibitively high rates which can range up to 900%. Select products for "national promotion" are routinely denied an import licence. Discriminatory value-added taxes for imported agricultural and manufactured products. Lifted import ban on rice in 1995 and established a quota for 51,307 tons (to increase to 205,228 tons by 2004).	Approximately 90% tariff lines are bound (almost all agricultural tariffs and 90% of tariffs on industrial products). The explicit reason involved for non-binding the remaining 10% is protection either to new industries or industries in difficulty. The average bound rate for industrial products will be 8.2% once the commitments are fully implemented. Except for rice, all agricultural products are bound.	In the process of phasing in tariff reductions to zero tariffs on most of all products in the following sectors: paper, toys, steel, semiconductors, and farm equipment. Tariffs on chemicals will be harmonized to final rates 0, 5.5 or 6.5% depending on the product. Reducing tariffs on scientific equipment by 65% from pre-Uruguay Round levels. Duties on agricultural products will be reduced by 40% from the 1993 applied levels in 10 equal instalments between 1995 and 2004.	APEC, EAEC

(Continued on next page)

Annex table III.2 *(continued)*

Trade regime / *Country*	*Tariff assistance (applied tariff levels)*	*Non-tariff barriers*	*Tariff predictability (WTO bindings)*	*Time-bound schedules/plans of trade liberalization*	*Membership in regional arrangements affecting trade*
SINGAPORE	99% of imports enter duty-free. Insignificant tariffs (5%) on some categories of goods, including chemicals and pharmaceuticals, ceramics and glass, iron and steel, machinery and equipment, automobiles and shipbuilding. Certain automobile and cosmetic products are, however, subject to excise duties. Significant tariffs on a few products, including cigarettes, alcoholic beverages, automobiles and gasoline.	Prohibitions mainly for health and sanitary reasons.	Singapore bound only 60% (according to some sources, 70%) of its tariff lines. Before the Uruguay Round, only 5% of the tariff lines were bound.		ASEAN (AFTA), EAEC, APEC
TAIWAN PROVINCE OF CHINA	Basic duty formula is as follows: raw materials, 0-2.5% (with a few as high as 25.5%); semi-processed goods, 0-10% (some 15-20%); and finished goods, 5-15% (some 50%). Areas with high tariffs include fresh fruits, including grapes, pears, apples, citrus, peaches, and kiwi fruit (40-42% tariff), avocados (28%), and cranberries (23%); processed fruit, including fruit juices (40-50%), figs (35%), canned peaches (20%), fruit cocktail (34%), and raisins processed vegetables, including vegetable juices (35-40%), frozen peas and corn (25-27%), frozen french fries and hash brown potatoes (17 and 32%); soups and broths (25%); breakfast cereals (25%); sunflower seeds and oil (21-24%); chocolate (15%); non-chocolate confectionery (30-32%); processed popcorn (25%); and ice cream (22.5%).	Import licences ("negative list"); 828 categories require approval; another 425 items are imported under special conditions: 138 require pro-forma notarization from local banks and 287 require import permits from the Board of Foreign Trade. A de facto ban on imports of another 239 items, including chicken (fresh and frozen), certain cuts of pork, peanuts, live dairy cattle vaccinated against brucellosis, and adzuki beans; rice and rice products; animal offal (beef, pork, and poultry), sugar, and selected dairy products; fishing boats (including sport fishing boats).	Offered to bind 94% of its tariff lines at a maximum rate of 30%. The tariff rates on the remaining items are not to exceed 50%.	Plans call for a reduction by 5% in car import duties by 1999.	APEC

(Continued on next page)

Annex table III.2 *(continued)*

Trade regime / *Country*	*Tariff assistance (applied tariff levels)*	*Non-tariff barriers*	*Tariff predictability (WTO bindings)*	*Time-bound schedules/plans of trade liberalization*	*Membership in regional arrangements affecting trade*
	Certain industrial products are also subject to high tariffs; average nominal duty on automotive parts is 20%, while the effective duty and tax rates for passenger cars and trucks range from 60-100%; actual duty rate for passenger cars is now 30%; 35-42% for commercial vehicles.	Licences are not granted to generic drugs. Restrictive standards and testing requirement.			
THAILAND	Selective, resulting in high rate dispersion; the duties ranged from 0 to 100% with a simple average of 23.1% (22.6% for manufactured products). Average trade-weighted tariff for dutiable items was 21.26% (1995). Figures do not include the effects of specific tariffs which are levied on some 161 items (1995). Arbitrary customs valuation procedures. In the case of new investment projects, import of machinery and raw or essential materials may benefit from tariff reductions ranging from 50 to 100%, for a period of up to five years.	Licences from the Ministry of Commerce in order to import items such as food products, raw materials, and industrial products. Strict import licensing requirements for agricultural items, such as soybean products, powdered milk, and coffee.	The number of bound tariffs on industrial products increased from only 2% to 68% and the trade-weighted average tariff on these products is to be reduced from 37.3 to 28%. In 1995, Thailand began the process of converting licensing restrictions (excluding industrial products) to tariff-rate quotas and tariffs.	At the end of 1994, Thailand commenced a major reform of tariff schedules to be completely phased in by 1 January 1997.	ASEAN (AFTA), APEC, EAEC
TURKEY	High protection on many agricultural and food products. In conjunction with its accession to a customs union with the European Union (effective 1 January 1996), Turkey adopted a new import regime, which applies the European Union common external customs tariff for third country imports and provides zero duty rates for non-agricultural items of European Union/EFTA origin.	Import licenses for certain goods, including telecommunications equipment, some agricultural products, chemicals, pharmaceutical products, vehicles and coal.			EU, ECO Protocal on Preferential Tariff

(Continued on next page)

Annex table III.2 *(continued)*

Trade regime / *Country*	*Tariff assistance (applied tariff levels)*	*Non-tariff barriers*	*Tariff predictability (WTO bindings)*	*Time-bound schedules/plans of trade liberalization*	*Membership in regional arrangements affecting trade*
VIET NAM	Tariff structure has undergone dramatic changes but remains the central element for fiscal (23% of government fiscal revenue) as well as industrial policy. Medium rate between 2 and 5%; non-weighted duty rate, 10.7%. Tariffs are subject to frequent adjustments and the adoption of a minimum price list for imports is perceived by importers as a major obstacle to transparent and unhindered trade, particularly for consumer goods, where the non-weighted average is 14.7% with 21.3% of tariff lines above the 30% rate.		Tariffs are not bound. In the discussions for WTO membership, Viet Nam has not yet made any offer for tariff binding.		ASEAN (AFTA)

Sources: European Commission, *Market Access: Sectoral and Trade Barriers Database* (Brussels, 1996); and Office of the United States Trade Representative and Related Entities, *National Trade Estimate: Report on Foreign Trade Barriers, 1996* (Washington DC, 1996).

Notes:

a At the APEC 1995 Ministerial Meeting, Australia committed itself to bringing forward by one year the date on which its final Uruguay Round tariff bindings would be phasing down – some 2,800 tariff lines in total. For industrial products where bindings are accelerated in this way, final bound rates will be achieved on 1 January 1998. For agricultural products, they will be achieved on 1 January 1999.

b Special tariff preferences are established for five Special Economic Zones: Shenzhen, Zhuhai and Shantou in Guangdong province, Xiamen in Fujian province and Haianan Island; there are three free trade areas and 2 export processing zones located in Shanghai's Pudong development district, in Tianjin and in Shenzhen. The free trade areas are fenced-off areas where importing can be conducted with no tariffs, duties or taxes imposed as long as no products made within the zone are sold into the domestic market. 14 open coastal cities and regions have authority to approve foreign investment projects, to offer investment incentives and to import specified equipment and technology on a duty-free basis. Furthermore, there are about 200 economic and technological development zones in the 14 coastal cities and in 16 locations along the rivers as well as in inland provincial capitals offering preferential arrangements to foreign investors in technologically advanced industries. There are also the so-called science parks or high technology development zones offering privileges to enterprises concentrating on specified high-technology activities.

c The duty-free import of plant and machinery for export processing zones has been cancelled as of 31 January 1996.

d "Sensitive" agricultural products consist of some 90 tariff lines and represent 11 per cent of all agricultural items; while virtually all of these have nominal rates of 30 per cent at present, most of their imports can generally be banned under the provision of the "Magna Carta for Small Farmers", which provides for banning imports of farm products deemed to be produced locally in sufficient quantity.

e Several important exceptions to the 30 per cent tariff rate, in addition to the anticipated tariff conversions for currently banned agricultural products; rice will continue to carry a 50 per cent tariff and remain under import controls; tariffs on soya sauce powder and chocolate dragees will remain at 50 per cent before declining in January 1998; in lieu of previous quota restrictions, a 40 per cent tariff will apply until 1999 for import of new automobiles, jeeps, station wagons and motorcycles.

CHAPTER IV

EXTERNAL FINANCIAL AND INVESTMENT INFLOWS

IV

FINANCIAL AND INVESTMENT INFLOWS AND GROWTH

The close interrelationship between international trade, financial and investment inflows and economic growth is being increasingly recognized. Its essence can be attributed to the three explanatory factors explained below.

First, products developed in the more advanced countries eventually become standardized to the extent that their production can be shifted, often *in toto*, to the less developed countries via capital flow, and the products are then exported back to the country where they were originally developed or to third countries. Recent experience in Asia with the flying geese paradigm is the best illustration of this process.

Second, growth, trade and financial and investment flows are closely linked through the transfer of technology. Financial flows facilitate the import of new technology in the form of new products and new production processes. Technology transfers benefit not only the recipient firms but also others in both the traded and the non-traded sectors of the economy through externalities and spillovers, thus improving the international competitiveness of an economy and contributing to the process of economic development.

Third, financial and investment flows essentially play two roles in improving the macroeconomic situation of a country: they supplement domestic savings and investment and they assist in overcoming the foreign exchange constraint imposed by the imbalance between foreign exchange earnings and import needs. In other words, these flows play an integrating role between countries with surplus savings and countries with deficits. This transfer of savings makes available a higher volume of imports, including capital goods, to the lower-savings countries, thus enabling the two sets of countries to improve their structures of output and growth.[1]

In the context of financial and investment inflows and economic growth, the role of transnational corporations deserves particular mention. Transnational corporations can promote economic growth in host countries by providing capital, technology and management skills. With their well-established market contacts, they also play an important role in the expansion of exports. It is noteworthy that, whereas in 1990 there were 37,000 companies with 170,000 foreign subsidiaries and affiliates, by 1995 these numbers had grown to 39,000 companies and 270,000 foreign subsidiaries and affiliates controlling an FDI stock of $2.7 trillion, equivalent to 10 per cent of world GDP.[2] Furthermore, companies trading with themselves, through their subsidiaries and affiliates, accounted for as much as 40 per cent of world trade in industrial goods.[3] By 1992, worldwide sales of transnational corporations had exceeded the global exports of goods and services.[4]

This process is not exclusively confined to transnational corporations from developed countries. Developing countries, notably China, the Republic of Korea and Singapore have succeeded in developing their own transnational corporations as they exploit the trade-investment nexus. The average annual outflows from developing economies have risen from 6 per cent of total worldwide FDI outflows during the period 1985-1989 to 10 per cent during the period 1990-1994. Although transnational corporations based in developing countries do not as yet figure in the world's 100 largest transnational corporations, they are catching up quickly. From an ESCAP perspective, it is striking to note that the majority of transnational corporations in developing countries are based in Asia.[5]

---

[1] For a discussion of the macroeconomic impact of FDI flows, see Maxwell Fry, *Foreign Direct Investment in Southeast Asia: Differential Impacts* (ASEAN Economic Research Unit, Institute of Southeast Asian Studies, 1993).

[2] UNCTAD, *World Investment Report 1993: Transnational Corporations and Integrated International Production* (United Nations publication, Sales No. E.93.II.A.14), p. 19 and *World Investment Report, 1996: Investment, Trade and International Policy Arrangements* (United Nations publication, Sales No. E.96.II.A.14), p. xiv.

[3] Stefan Wagstyl, "Global manufacturing," *Financial Times*, London, 27 September 1996.

[4] World Bank, *Global Economic Prospects and the Developing Countries* (Washington DC, 1996), p. 12.

[5] UNCTAD, *World Investment Report 1996*... p. 33.

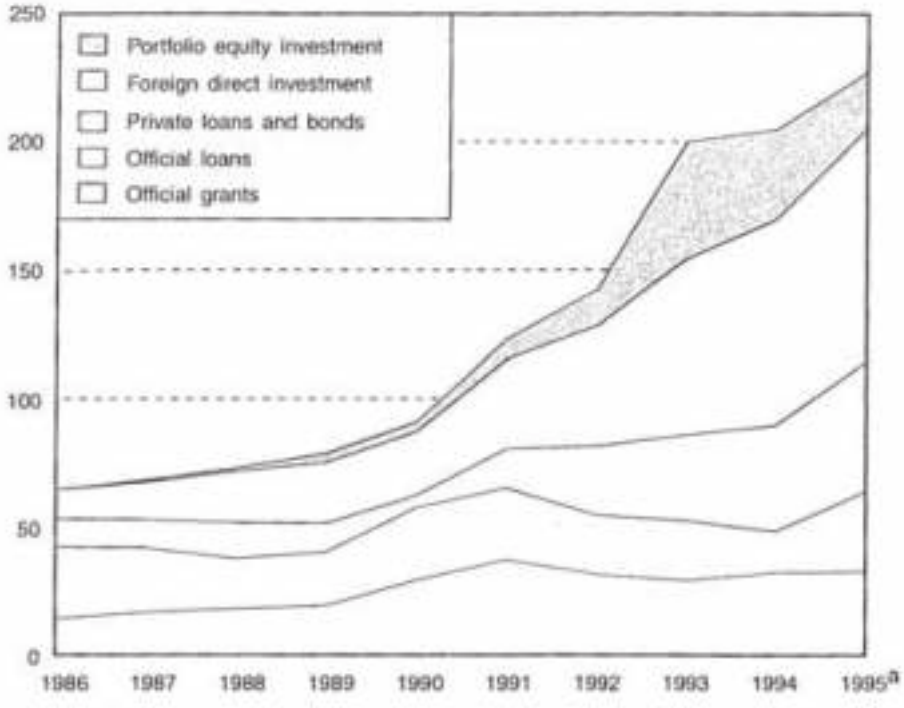
RECENT EXPERIENCE

Consistent data are available for four main categories of financial flows to developing countries: (a) long-term debt; (b) FDI; (c) portfolio investments; and (d) grants. Long-term debt is defined as debt with a maturity of one year or more and is composed of public debt (loans from official bilateral or multilateral sources), publicly guaranteed debt (loans from a private source whose repayment has been guaranteed by an official body in the recipient country) and private debt. Private debt, in turn, is composed of bonds, bank loans and other credits issued or acquired by private sector enterprises in a country without any public guarantee. FDI, portfolio investments and grants are non-debt-creating flows. FDI is the sum of equity capital, reinvestment of earnings and inter-company loans between parent and subsidiary or affiliate. Portfolio investments are the total of country funds placed in foreign stock markets and direct purchases of equity in local stock markets by foreigners, while grants are transfers from official or non-official sources involving no repayment obligation.

One of the more striking developments of the 1990s has been the rapid and steady recovery of long-term financial flows to developing countries (figure IV.1). The recovery can be almost entirely attributed to the growth in private capital flows, which nearly quadrupled between 1990 and 1995, with their share of aggregate resource flows increasing from around 40 to 70 per cent during the

Figure IV.1. Aggregate net resource flows to developing countries, 1986-1995

(Value in billion US Dollars)



Sources: Reproduced from World Bank, *World Debt Tables 1996: External finance for developing countries*, vol. 1: Analysis and summary tables, p. 3.

[a] Preliminary.

same this period. Within the global package of private capital flows, it is useful to distinguish between FDI, portfolio flows, syndicated loans and bond issues. All four, while interrelated, have displayed somewhat divergent trends in the recent past. FDI flows have continued the steady upward trend begun in the late 1980s, and developing countries have boosted their share of global FDI to 32 per cent in 1995 from 16 per cent in 1990.[6] In contrast, portfolio flows to developing countries, after rising slowly in the late 1980s and much more rapidly in the early 1990s, declined dramatically in 1994 and 1995. This decline began in the second half of 1994, when American monetary policy was first tightened, and became dramatic with the onset of the Mexican crisis. Bank lending, which had declined during and after the debt crisis, started increasing again between 1993 and 1995. This recovery in bank lending had been mirrored earlier by a rise in international bond issues by developing countries in the early 1990s.

As shown in table IV.1, total net resource flows to all developing countries more than doubled in value in the 1990s; FDI and portfolio investment, accounted for the largest increases, the former increasing by a factor of 3 and the latter by a factor of 6. The share of developing countries in the ESCAP region in total net flows increased significantly, from 38 to 52 per cent, between 1990 and 1995, as did their shares of FDI (from 46 to 62 per cent) and long-term debt (from 45 to 53 per cent). With a rapid rise in total portfolio investments in all developing countries, the share of the ESCAP member countries grew strongly as the emerging and increasingly liberalized markets of East and South-East Asia attracted many overseas investors.

Table IV.1. Aggregate net resource flows to developing countries and the share of developing economies in the ESCAP region

(Value in billions of US dollars, figures in brackets are percentages)

	1990	*1991*	*1992*	*1993*	*1994*	*1995*
Aggregate flows	101.9	127.1	155.3	207.2	207.4	231.3
of which ESCAP region	(37.6)	(35.8)	(40.4)	(40.2)	(47.8)	(52.2)
Net flow of long-term debt	43.8	47.0	62.7	64.1	60.0	86.2
of which ESCAP region	(45.0)	(52.1)	(47.8)	(31.0)	(50.8)	(52.9)
Foreign direct investment	25.0	35.0	46.6	68.3	80.1	90.3
of which ESCAP region	(46.0)	(41.1)	(47.9)	(56.8)	(55.2)	(61.7)
Portfolio investment	3.7	7.6	14.1	45.6	34.9	22.0
of which ESCAP region	(64.9)	(13.2)	(39.0)	(44.1)	(53.9)	(61.8)
Grants	29.4	37.5	32.0	29.4	32.5	32.9
of which ESCAP region	(16.0)	(14.7)	(15.3)	(15.3)	(16.9)	(17.6)

Source: ESCAP secretariat calculations based on World Bank, *World Debt Tables 1996: External Finance for Developing Countries*, vol. 1: Analysis and summary tables (Washington DC, 1996), pp. 192, 196 and 212.

Note: Figures include all developing economies for which consistent data exist; but exclude the Central Asian republics.

From table IV.2, it can be seen that the total flows to the region have increased threefold between 1990 and 1995, but there has been a significant shift in the composition of flows. In particular, the shares of long-term debt and grants have been declining, the former by 30 per cent and the latter by 70 per cent. The shares of FDI and portfolio flows have both been growing at such a rate that currently the most important source of external finance is not long-term debt, as it was in the early 1990s, but FDI. In fact, FDI now accounts for almost half of all inflows.

[6] Ibid., table I.1.

Table IV.2. Percentage distribution by type of financial flow, developing economies in the ESCAP region, 1990-1995

	1990	1991	1992	1993	1994	1995
			(Millions of US dollars)			
Aggregate net resource flows	38 238	45 471	62 694	83 269	99 067	120 782
			(Percentage)			
Net flow of long-term debt (excluding IMF)	51.5	53.9	47.9	23.9	30.7	37.7
Foreign direct investment (net)	29.9	31.5	35.6	46.5	44.7	46.2
Portfolio equity flows	6.2	2.4	8.7	24.2	19.0	11.3
Grants (excluding technical cooperation)	12.4	12.2	7.8	5.4	5.6	4.8

Source: ESCAP secretariat calculations based on World Bank, *World Debt Tables 1996: External Finance for Developing Countries*, vol. 1: Analysis and summary tables (Washington DC, 1996), pp. 192, 196 and 212.

Note: Figures include all developing economies for which consistent data exist; but exclude the Central Asian republics.

These overall favourable trends, however, reveal themselves very unevenly in terms of individual economies (table IV.3). Of the main categories of resource flows, the net flow of public and private long-term debt during the 1990s has been important nearly everywhere, accounting for over half of the total inflows in many economies (notable exceptions being Fiji and Malaysia). While its share of total inflows has declined between the two periods for quite a number of economies including 6 least developed countries, the net flow has remained above 40 per cent in 19 out of the 32 countries listed, and above 30 per cent in another 4. While not shown in the table, it is clear that the proportion of private debt in this category has a tendency to increase with the level of development of the country concerned. Thus, public debt is proportionately more important in the least developed countries, in South Asia and in the Central Asian republics than in East and South-East Asia.

FDI flows are important primarily in East Asia, particularly China, and in South-East Asia, but they are also important as a share of total resource flows in Cambodia, Fiji, the Lao People's Democratic Republic, Kazakstan, Maldives, Myanmar, Nepal, Papua New Guinea, Solomon Islands and Vanuatu, where they amount to around one fifth or more of the total foreign flows received by these countries. Portfolio flows to ESCAP member countries have naturally been confined to economies with functioning equity markets.[7] As a consequence they are very concentrated, exceeding one fifth of total resource flows in only five countries (India, Malaysia, the Philippines, Republic of Korea and Viet Nam) and they exceed 10 per cent in another three (Indonesia, Pakistan and Thailand). In the rest of the ESCAP region, they are effectively non-existent. As could be expected, grants have remained important as a source of foreign inflows in the least developed countries and the Pacific islands, accounting for over half of the inflows in 10 out of the 13 such countries listed in table IV.3. They are also very significant in several of the Central Asian republics.

[7] There are a number of economies in the region where such markets have reached a ratio of market capitalization to GDP that is broadly comparable to those of the developed countries. On the whole, however, these markets remain thin and narrow. See Bank of International Settlements, *66th Annual Report* (Basle, 1996), chapter VII, pp. 120-123.

Table IV.3. Aggregate net resource flows

(Annual average value in millions of US dollars)

	1985-1989					1990-1994				
	Total	*a*	*b*	*c*	*d*	*Total*	*a*	*b*	*c*	*d*
ESCAP developing economies										
Least developed countries										
Bangladesh	1 414.2	781.0	1.4	0.0	631.4	1 470.8	626.6	6.6	9.4	828.6
Bhutan	28.3	13.5	0.0	0.0	14.8	34.9	2.1	0.0	0.0	32.7
Cambodia	..	..	..	..	..	142.4	11.0	31.2	0.0	100.2
Lao People's Democratic Republic	175.8	145.4	1.2	0.0	29.4	172.2	78.6	28.6	0.0	65.0
Maldives	15.6	0.2	3.0	0.0	12.4	33.1	13.1	7.0	0.0	13.0
Myanmar	273.8	197.2	1.2	0.0	75.6	108.8	41.2	3.2	5.8	58.2
Nepal	289.4	159.4	1.0	0.0	128.6	289.4	132.4	5.0	0.0	152.0
Samoa	16.1	0.8	0.2	0.0	15.1	40.9	14.0	4.6	0.0	22.3
Solomon Islands	33.5	10.6	4.7	0.0	18.1	29.1	–0.2	14.2	0.0	16.6
Vanuatu	27.3	2.7	7.9	0.0	16.8	44.3	5.2	24.2	0.0	14.9
East and North-East Asia										
China	8 253.8	5 560.6	2 487.0	0.0	206.0	27 285.4	9 395.2	16 062.2	1 608.0	219.8
Mongolia	..	..	..	..	..	84.8	45.3	7.0	0.0	32.0
Republic of Korea	–2 043.0	–2 667.0	579.8	42.0	2.2	6 018.6	2 704.6	818.4	2 492.4	3.2
South-East Asia										
Indonesia	3 001.4	2 343.0	442.2	39.8	176.4	6 653.6	3 516.8	1 693.0	1 187.8	255.8
Malaysia	–74.4	–963.0	798.8	56.4	33.4	5 544.4	185.2	4 173.6	1 139.6	46.4
Philippines	1 219.0	486.0	389.0	50.6	294.0	2 506.2	1 044.0	613.0	564.4	285.2
Thailand	1 885.6	598.2	731.8	420.6	135.0	4 752.0	2 206.2	1 788.0	614.6	143.4
Viet Nam	..	..	..	..	..	323.2	26.0	39.4	89.5	186.2
South and South-West Asia										
India	5 314.0	4 480.0	155.8	83.2	595.0	5 449.2	3 243.2	269.4	1 381.2	554.0
Iran (Islamic Republic of)	–285.0	–210.2	–83.2	0.0	8.4	199.0	249.0	–113.8	0.0	63.6
Pakistan	1 102.6	615.2	152.2	0.0	335.6	2 139.0	1 177.8	322.4	336.4	302.4
Sri Lanka	482.0	264.4	36.4	0.0	181.6	603.0	287.0	115.0	22.4	178.6
North and Central Asia										
Armenia	..	..	..	..		122.9	50.2	0.0	0.0	72.7
Azerbaijan	..	..	..	..		72.2	33.7	0.0	0.0	27.4
Kazakstan	..	..	..	..		461.3	305.0	145.0	0.0	11.3
Kyrgyzstan	..	..	..	..		106.2	63.8	3.3	0.0	39.1
Tajikistan	..	..	..	..		111.9	90.1	3.3	0.0	18.5
Turkmenistan	..	..	..	..		96.1	110.0	0.0	0.0	3.2
Uzbekistan	..	..	..	..		231.0	181.0	45.0	0.0	7.0
Pacific island economies										
Fiji	24.6	–8.8	16.3	0.0	17.2	28.5	–28.2	39.8	0.0	16.8
Papua New Guinea	567.4	181.2	124.8	0.0	261.2	442.8	46.0	130.8	0.0	266.2
Tonga	11.1	1.7	0.1	0.0	9.4	16.0	2.4	1.0	0.0	12.6

Source: ESCAP secretariat calculations based on World Bank, *World Debt Tables 1994-1995 and 1996: External Finance for Developing Countries*, vol. 2: Country tables (Washington DC, 1996).

a = Net flow of public and private long-term debt (excluding IMF).

b = Foreign direct investment (net).

c = Portfolio equity flows.

d = Grants (excluding technical cooperation).

Long-term debt

The relatively high credit standing of many of the economies in the region has meant that many countries have continued to enjoy more than adequate access to long-term debt, whether in the form of bank loans or bonds. In 1990, the region raised roughly half its external resources in the form of long-term debt; by 1995, the proportion had fallen to just over one third, reflecting the rise of FDI. The breakdown of long-term debt between bonds and bank syndications indicates that, for the region as a whole, bonds predominate. In addition, bond maturities have lengthened and spreads have narrowed, and this is perhaps a better measure of creditworthiness than the actual volume of bond issues.[8]

The region's credit standing is based on the fact that, with the exception of the Philippines, it has never had to restructure its debt with commercial banks.[9] Capitalizing on this, some countries have also acquired a considerable volume of short-term debt over the last few years.[10] When short-term debts are regularly rolled over, as they frequently are, they acquire the characteristics of long-term debt. Functionally, short-term debts play the role that working capital does for an individual company; they enable an economy to maintain a higher level of liquidity and thus allow spending and investment plans to be maintained. At the same time, however short-term debts can be highly volatile (indeed, just as volatile as portfolio flows), and their sudden reversibility can create severe risks for the receiving or intermediating entities.

Bonds can be official or private in origin. They are normally classified under private debt as, regardless of origin, they are bought by private investors. In the ESCAP region, the practice of raising bond finance in foreign markets is of recent origin. The principal reason for this has been the weakness of expertise on bonds, and there are few domestic bond markets of any size, with the exception of Hong Kong, Malaysia, the Republic of Korea and Singapore.[11] However, enterprises from a growing number of economies in the ESCAP region have begun, especially over the last three years, to raise bond finance on the international markets, the Republic of Korea being a prominent case in point (table IV.4).

Portfolio investments

One of the more significant developments in the evolution of external resource flows to the region recently has been the rise of portfolio investments into the region's equity markets, an indication of the increasing integration of the region with respect to cross-border investment flows. In earlier years, a few ESCAP member countries had floated country funds on foreign equity markets. This practice continues with added strength, and several companies from the region are raising equity in this manner (table IV. 4).

In the late 1980s, and early 1990s, as capital market restrictions began to be eased, portfolio investment flows into equity markets in the region grew rapidly to nearly 25 per cent of aggregate resource flows to the region in 1993. Apart from East and South-East Asia, India and Pakistan were the largest beneficiaries of this development. Portfolio flows, however, declined sharply to just over 10 per cent of total flows by 1995. This abrupt reversal was clearly related to the 1994 Mexican crisis, which adversely affected foreign investor confidence in nearly all developing country equity markets, although not as much in East and South-East Asia as in other parts of the world. It is, however, indicative of the volatility inherent in these flows, with short-term funds moving in and out, more or less oblivious to the fundamental economic conditions prevailing in the countries.

---

[8] World Bank, *World Debt Tables 1996, External Finance for Developing Countries*, vol. 2: Country tables (Washington DC, 1996), pp. 4-5 and 8.

[9] A number of countries in the region have rescheduled their official debt with international financial institutions and bilateral donors.

[10] Thailand's short-term debt was half of its total external debt at the end of 1995. See "Hint of greater stability", *Bangkok Post*, 27 January 1997.

[11] Efficient bond markets can relieve the volatility of equity markets by providing alternative investment outlets with less risk on the downside.

Table IV.4. International equity and bond issues of selected economies in Asia and the Pacific

(Millions of US dollars)

	International equity issues			*International bond issues*		
	1993	*1994*	*1995*	*1993*	*1994*	*1995*
China	1 901	2 594	666	2 852	3 652	1 433
Hong Kong	837	320	1 206	7 472	6 796	2 935
India	340	3 029	274	556	891	800
Indonesia	299	1 359	1 112	510	2 246	2 299
Malaysia	–	–	1 294	958	2 345	2 594
Pakistan	–	1 183	–	–	195	–
Philippines	126	1 059	886	1 274	1 307	1 059
Republic of Korea	328	1 168	1 310	5 962	6 483	11 037
Sri Lanka	–	33	–	..	..	..
Singapore	564	301	475	..	..	..
Taiwan Province of China	35	437	719	78	1 964	541
Thailand	725	2 256	531	2 335	3 527	2 265

Source: ESCAP secretariat calculations based on IMF, *International Capital Markets: Developments, Prospects and Key Policy Issues*, tables 24 and 30 (Washington DC, 1996).

Foreign direct investment

FDI flows signify a long-term commitment on the part of the investor and are thus far more stable than other flows. Moreover, once established on the ground, they can generate the interest of other foreign investors, such as suppliers of components or of supporting services, to join the pioneers and start virtuous circles of foreign investor interest. However, perhaps for this very reason, FDI flows have been highly concentrated, the overwhelming bulk going to just a few countries in the region. The pattern of FDI flows over time can also be quite uneven for an individual country. For example, the remarkable change in the share of China in 1994 and 1995 is clearly evident in table IV.5. Nevertheless, East and South-East Asia's general dominance in the 1990s as a recipient of FDI persists. In this context, the changing role of Hong Kong, the Republic of Korea and Taiwan Province of China is worthy of note. For these economies, the proportion of resources originating in FDI has declined, principally because these economies have become net exporters of capital. For instance, Hong Kong became a very large source of outward FDI (around $20 billion annually over the last three years) while the Republic of Korea, Singapore and Taiwan Province of China have had annual outflows of about $3 billion over the same period. China and Malaysia joined the ranks of FDI providers in 1992 (see box IV.1).

Taking FDI flows as a ratio of GDP (table IV.6), Singapore and Malaysia stand out, with FDI amounting to 10 and 8 per cent of these countries' GDP respectively; the average for even the relatively high recipients is 2 to 4 per cent, the only exceptions being small economies such as Solomon Islands and Vanuatu. Similarly, the ratio of FDI to gross fixed capital formation is the highest in Singapore and Malaysia (well over one quarter) while the average for East and South-East Asia is around 5 to 6 per cent. Since 1992, China has been the biggest recipient of FDI among developing countries in the world, and FDI now finances almost an eighth of China's gross fixed capital formation. A number of other economies, including some least developed and Pacific island countries, have also increased their share of gross fixed capital formation financed by inflows of FDI.

Given the importance of FDI in the region, it would be useful to examine the sources and uses of this resource flow. Most of the long-term flows of finance currently have their origin in the developed countries, which remain the main exporters of capital via their transnational corporations, banks, institutional funds, bond markets and export credit facilities. Some of the Asian NIEs, as noted, are now emerging as sources of outward FDI. Exact data on uses are not available. The available information for a few select countries (Indonesia, the Republic of Korea and Thailand) indicates that the manufacturing

Table IV.5. Foreign direct investment inflows, 1984-1995

(Value in millions of US dollars)

	Average		1990	1991	1992	1993	1994	1995[a]
	1984-1989	1990-1994						
ESCAP developing economies								
Least developed countries								
Afghanistan								
Bangladesh	1	7	3	1	4	14	11	125
Cambodia	..	31	..	..	33	54	69	80
Lao People's Democratic Republic	1	29	6	8	9	60	60	75
Maldives	3	7	6	7	7	7	8	9
Myanmar	1	3	5	–	3	4	4	0
Nepal	1	5	6	2	4	6	7	8
Samoa	–	5	7	3	5	5	3	3
Solomon Islands	5	14	10	15	14	15	17	17
Vanuatu	8	24	13	25	26	27	30	25
East and North-East Asia								
China	2 282	16 062	3 487	4 366	11 156	27 515	33 787	37 500
Democratic People's Republic of Korea	106	0	–	–	–	–	–	1
Hong Kong	1 422	1 597	1 728	538	2 051	1 667	-2 000	2 100
Mongolia	..	6	..	2	8	8	10	10
Republic of Korea	592	818	788	1 180	727	588	809	1 500
Taiwan Province of China	691	1 154	1 330	1 271	879	917	1 375	1 470
South-East Asia								
Brunei Darussalam	–	6	3	1	4	14	6	7
Indonesia	406	1 693	1 093	1 482	1 777	2 004	2 109	4 500
Malaysia	798	4 174	2 333	3 998	5 183	5 006	4 348	5 800
Philippines	326	757	530	544	228	1 025	1 457	1 500
Singapore	2 239	4 682	5 575	4 879	2 351	5 016	5 588	5 302
Thailand	676	1 788	2 444	2 014	2 116	1 726	640	2 300
Viet Nam	2	39	16	32	24	25	100	150
South and South-West Asia								
India	133	269	162	141	151	273	620	1 750
Iran (Islamic Republic of)	-62	-114	-362	23	-170	-50	-10	-30
Pakistan	136	322	244	257	335	354	422	639
Sri Lanka	36	115	43	48	123	195	166	195
North and Central Asia								
Armenia	..	2	..	..	..	..	8	10
Azerbaijan	..	0	..	..	..	..	..	110
Kazakstan	..	87	..	..	100	150	185	284
Kyrgyzstan	..	2	..	..	..	..	10	15
Tajikistan	..	2	..	..	..	..	10	15
Uzbekistan	..	27	..	..	40	45	50	115
Pacific island economies								
Fiji	17	46	80	15	50	49	35	35
New Caledonia	2	16	31	3	17	20	10	10
Papua New Guinea	123	131	155	203	291	1	4	15
Tonga	–	1	–	–	1	2	2	2
Other members of ESCAP in Asia and the Pacific								
Australia	4 306	4 800	7 077	4 903	4 912	2 687	4 423	13 094
Japan	81	1 623	1 753	1 730	3 490	234	908	39
New Zealand	176	1 894	1 686	1 698	1 090	2 200	2 796	2 483
Russian Federation	..	127	..	..	..	..	637	2 017
Turkey	245	716	684	810	844	636	608	1 037

Source: ESCAP secretariat calculations based on United Nations, *World Investment Report 1996: Investment, Trade and International Policy Arrangements* (United Nations publication, Sales No.E.96.II.A.14), annex table 1, pp. 227-231.

[a] Estimated.

Box IV.1. Foreign direct investment outflows from developing economies of the region

Usually, FDI inflows and not outflows are the policy objective in developing economies in order to enhance the pace of their economic growth. However, FDI outflows have become a prominent feature of certain developing economies of the region. The rationale for FDI outflows from developing economies has several components.[a] A persistent build-up of foreign exchange reserves permits countries to invest abroad and recycle their surplus capital. However, a favourable balance-of-payments situation is not a necessary condition. Outward FDI is undertaken by countries with the objective of gaining or improving access to markets for their goods and services. FDI is also used to secure a stable supply of imported raw material. For example, in 1970, the Republic of Korea began investing in the lumber industry in Indonesia to provide resources for its plywood industry. Similarly, overseas investment is undertaken to gain access to cheaper labour, or access to modern technology and skills, and research and development programmes.

A select number of developing economies in the region have significant FDI outflows. In 1995, China, Hong Kong, Malaysia, the Republic of Korea, Singapore, Taiwan Province of China and Thailand accounted for almost 100 per cent of the total outflows from developing economies of the region and 88 per cent of the outflows of all developing countries. Foreign investment from these economies grew by 238 per cent between 1990 and 1995, with FDI from China, Malaysia and Thailand having grown very rapidly in the last few years. Each of these seven economies had over $2.5 billion of FDI outflows in 1995, except Thailand, which had around $900 million. In Hong Kong, the Republic of Korea and Taiwan Province of China, FDI outflows now exceed inflows. FDI outflows from Malaysia, Singapore and Thailand were 40 per cent or more of their FDI inflows in 1995 whereas China's FDI outflow was 9 per cent of its FDI inflows.

FDI outflows from the above economies have gone to different parts of the world. However, in each case a few economies were the major destinations, with a significant share going to developed countries.[b] In 1993, whereas Asian countries accounted for 54 per cent of outflows from Singapore, the United States was also a significant destination. With regard to Malaysian FDI, in 1995 Singapore was the destination for 30 per cent and the other top six destinations were the United States, Hong Kong, the United Kingdom, China, Indonesia and Australia. China's investments are in some 130 countries. However, at the end of 1995, 61 per cent of its total investment stock was in Hong Kong and Macau, followed by 15 per cent in North America. A large share of investment from Hong Kong and Taiwan Province of China goes to China. Investment from some of the countries has started to go to new destinations. For example, of total FDI from the Republic of Korea in 1991-1995, 4 per cent went to Latin American countries and 3 per cent to African countries. Sizeable amounts of investment from Malaysia have gone to South Africa in recent years.

The limited information available on the composition of FDI outflows shows that most have gone into manufacturing and services, especially in recent years. For example, in 1993, 32 per cent of Singapore's investment was in manufacturing and 68 per cent in non-manufacturing, with a major part of the latter in financial services and real estate. The composition of investment from Malaysia changed over the years from a heavy involvement in real estate to businesses. In the case of the Republic of Korea in 1990-1995, around 60 per cent of its investment went to manufacturing and 23 per cent to services. Some two thirds of China's overseas investment is in service industries, much of it servicing China's own exports.

The need for capital in developing countries often led to restrictions on capital outflows. Most of the countries which now have major FDI outflows liberalized

---

[a] FDI outflows and policies affecting them have been analysed in detail in UNCTAD, *World Investment Report 1995: Transnational Corporations and Competitiveness* (United Nations publication, Sales No. E.95.II.A.9).

[b] Within the developed world, North America still remains the major destination. However, FDI outflows to the European Union have started gaining momentum, with average annual FDI outflows increasing from $100 million in 1989-1991 to $860 million in 1992-1994. Within the European Union, the United Kingdom, Germany and the Netherlands have so far been the main locations. (For more details on Asian investment in Europe, see UNCTAD, *Sharing Asia's Dynamism: Asian Direct Investment in the European Union*, (United Nations publication, Sales No. E.97.II.D.1).

(Continued overleaf)

(Continued from preceding page)

their regulatory regimes gradually. For example, the Republic of Korea first permitted overseas investment in 1968 but the policy regime remained quite restrictive and an extensive capital control system was maintained until the mid-1980s. In 1987, a major liberalization regarding outward FDI was carried out; the government reduced its role in approval of investment, with only very large projects continuing to need approval. Presently, smaller projects (under $10 million) need to obtain validation from foreign exchange banks only, while outward FDI valued at up to $50 million (roughly 99 per cent of all projects) only requires notification to the Bank of Korea. In 1994, the country adopted a negative list system under which only a few areas specifically listed by the government are not permitted for outward FDI. In the case of Thailand, in 1994 the limit on outward investment requiring government approval was changed from $5 million to $10 million and there is no industry-specific restriction.

Countries encouraging FDI outflows have also adopted promotional measures. To facilitate outflows, they collect information on investment opportunities abroad and provide advisory services to prospective investors. They are signing an increasing number of bilateral investment treaties and double taxation agreements. Besides, some countries either have or are planning to have investment guarantee schemes to cover non-commercial risks. Many countries provide fiscal, financial and other incentives. For example, most types of investment income remitted from abroad, as well as expenses on feasibility studies for overseas investment, are tax-exempt in Malaysia. The Republic of Korea has established special funds from which long-term loans are provided for overseas investment. In 1994, China started providing training for managers on matters related to establishing and operating foreign affiliates. Singapore provides training for workers of its foreign affiliates. In 1995, Singapore started a programme called "Promising Local Enterprises 2000" aimed at nurturing 100 promising local enterprises to reach S$100 million sales in the following 10 years and then to become Asian transnational corporations. To encourage outward FDI, Thailand in 1996 established the Thailand Overseas Investment Promotion Board, chaired by the Prime Minister.

Future prospects for FDI from developing economies are quite promising. As the existing firms gain more experience and confidence, they will enhance their overseas investment, whereas inward FDI liberalization policies in many countries will continue to remain active on the demand side. At the same time, more developing countries will be providing outward FDI flows as they grow and restrictions on outward capital flows are liberalized. However, as a major part of the very large outward FDI from Hong Kong and China is between these two economies, these investment flows will disappear from statistics after the merger in 1997, and there will be a sudden significant drop in total FDI outflow from developing economies.

sector received over 50 per cent of the FDI flows between 1989 and 1994, with the services sector accounting for most of the rest. Despite this overall pattern, many countries in the region, particularly the Pacific islands, least developed countries and the economies in transition, have received investment primarily in either commodity production or tourism, with the occasional investment in commodity processing or in manufacturing, mainly to take advantage of preferential market access (textiles in Fiji, automotive parts in Samoa, for example).

The economic importance of FDI is clearly an evolving one, moving from the exploitation of natural resources to manufacturing and to services. Within manufacturing, a large volume of labour-intensive activities are in the process of shifting from the industrially more advanced economies in the ESCAP region to the less advanced ones, evidence of the flying geese pattern. The more advanced economies are now beginning to attract FDI in capital- and skill-intensive industries. As part of this evolution, Singapore and Malaysia, for instance, have instituted more selective criteria for the kind of FDI that they wish to have, favouring higher value added and a higher technological content in the output that FDI will generate. The Republic of Korea and Taiwan Province of China appear to be traversing the route followed by Hong Kong and Singapore in attracting FDI in knowledge- and skill-intensive services, as in both the Republic of Korea and Taiwan Province of China, services are estimated to account for over one third of new FDI flows, compared with around 20 to 25 per cent in the early 1980s.[12]

---

12 UNCTAD, *World Investment Report 1995, Transnational Corporations and Competitiveness* (United Nations publication, Sales No. E.95.II.A.9), pp. 60-63.

Table IV.6. Rate of foreign direct investment inflows to gross domestic product and to gross fixed capital formation

	Percentage share of inward FDI flows			
	to GDP		*to gross fixed capital formation*	
	1984-1989	*1990-1994*	*1984-1989*	*1990-1994*
ESCAP developing economies				
Least developed countries				
Bangladesh	0.01	0.03	0.1	0.2
Cambodia	..	1.7	..	..
Lao People's Democratic Republic	0.1	2.6	..	..
Maldives	3.2	4.4	7.7	9.4
Myanmar	0.01	0.01	0.1	0.1
Nepal	0.04	0.1	0.2	1.0
Samoa	–	4.0	..	..
Solomon Islands	3.1	8.7	12.6	..
Vanuatu	7.4	14.4	25.9	48.4
East and North-East Asia				
China	0.7	3.6	1.8	11.6
Hong Kong	3.0	1.7	12.2	6.8
Mongolia	..	0.3	..	..
Republic of Korea	0.4	0.3	1.4	0.7
Taiwan Province of China	0.7	0.6	3.3	3.0
South-East Asia				
Brunei Darussala	–	0.1	..	..
Indonesia	0.5	1.3	1.6	3.5
Malaysia	2.4	7.8	8.8	22.4
Philippines	1.0	1.5	5.1	6.2
Singapore	10.3	9.7	28.3	28.4
Thailand	1.3	1.7	4.4	4.3
Viet Nam	0.02	0.5	..	..
South and South-West Asia				
India	0.1	0.1	0.2	0.5
Iran (Islamic Republic of)	-0.02	-0.02	-0.1	-0.2
Pakistan	0.4	0.7	2.0	3.6
Sri Lanka	0.6	1.2	2.3	4.6
North and Central Asia				
Armenia		0.03		
Kazakstan		0.3		
Kyrgyzstan		0.04		
Tajikistan		0.1		
Uzbekistan		0.1		
Pacific island economies				
Fiji	1.4	3.0	9.7	15.8
Papua New Guinea	4.4	3.9	20.0	13.4
Tonga	–	0.7	..	..
Other members of ESCAP in Asia and the Pacific				
Australia	2.1	1.7	8.6	7.6
Japan	0.004	0.05	–	0.2
New Zealand	0.5	4.3	2.5	24.2
Russian Federation	–	0.1	..	0.02
Turkey	0.3	0.5	1.4	1.9

Source: ESCAP secretariat calculations based on United Nations, *World Investment Report 1996: Investment, Trade and International Policy Arrangements* (United Nations publication, Sales No.E.96.II.A.14), Annex table 1, pp. 227-231, and IMF Tape No. 993023 F.

Official development assistance

Grants form part of ODA along with long-term concessional debt finance and these are provided by both bilateral and multilateral sources. Most economies in East and South-East Asia ceased long ago to be reliant, or indeed eligible, for ODA, particularly in the form of grants. South Asia remains dependent on ODA while also attracting private finance. However, many economies in the region continue to rely on ODA for their balance-of-payments and investment needs. For example, the least developed countries and the Pacific island countries have been the smallest recipients of private external finance in absolute terms; despite their attempts to become more open and attractive to foreign investors, they have attracted only limited private finance. The Central Asian republics and Mongolia are in broadly comparable circumstances. These economies in transition are currently in the process of developing the required legal and other institutional structures capable of attracting private financial flows on a sustained basis. However, the countries within the Mekong area are taking advantage of their geographical location and benefiting from the resiting of production facilities by investors from East and South-East Asia in search of lower-cost manufacturing bases. In Central Asia, Kazakstan and Uzbekistan have attracted natural-resource-seeking FDI in oil and gas, and some investors from Japan and the Republic of Korea are begining to show interest in manufacturing. Lack of familiarity with international business and slow progress in developing the required institutions have also undoubtedly affected flows of private capital into these economies in more significant amounts.

The international community appears to be increasingly leaning towards the perception that ODA resources for public spending programmes are no longer needed and that all countries should endeavour to raise capital from private market sources. However, the above groups of countries, by and large, lack access to private capital markets and will continue to lack it for some years to come. They are thus dependent on ODA flows to meet their needs for external funds. In the 1990s, owing to budgetary constraints in donor countries, ODA from bilateral sources has been on a declining trend.

ODA from multilateral sources (international development banks) on non-concessional terms has also been declining, although the reasons are different. As the more creditworthy countries that traditionally borrowed from multilateral financial institutions have gained easier access to private funds, they have not been borrowing as much from these institutions. Concomitantly, balanced portfolio considerations limit the lending of these institutions to less creditworthy countries. Thus, overall lending by multilateral institutions is not rising. By the same token, export credit commitments from the developed countries have become heavily weighted by a preference for higher quality borrowers; less creditworthy countries find it difficult to obtain export cover in the developed countries and thus to import capital goods. The result is that the least developed countries are finding access to finance progressively more, rather than less, difficult than in the past.

POLICY DEVELOPMENTS

Policy frameworks in developing countries of the region dealing with private financial and investment inflows have evolved considerably over the years. In particular, liberalization of the restrictive policies affecting external inflows in many countries gained momentum in the 1990s. Policy initiatives at the regional and international levels to encourage financial flows and investment are also being developed, and some are already in place. These policy initiatives are discussed below under three broad groupings: national, bilateral and regional, and international levels.

National level

Realizing the important contribution that private financial flows can make to economic development, countries, on their own initiative, have introduced many policy reforms to attract them. Restrictive investment regimes have been liberalized. In addition, various types of incentives are being offered to attract FDI. Greater attention is also being paid to making the macroeconomic environment more conducive to foreign investors. Provision of infrastructure and other support services is being targeted. Financial sector reforms are being undertaken to facilitate financial flows of various forms. All these measures are discussed briefly here.

Liberalization of investment regimes

Various forms of restrictions were applied in the past to FDI in the developing countries of the region. These relate to admission and establishment, ownership and control, and operational and other measures. Under admission and establishment, measures included closing certain sectors, industries or activities to FDI; quantitative restrictions on the number of foreign companies admitted in specific sectors, industries or activities; and screening, authorization and registration of investment and minimum capital requirements. Ownership and control restrictions existed in various forms, among which were: allowing only a fixed percentage of foreign-owned capital in an enterprise; compulsory joint ventures, either with state participation or with local private investors; mandatory transfer of ownership to local firms, usually over a period of time; restrictions on ownership and transfer of land or immovable property; and restrictions on payment of dividends and reimbursement of capital upon liquidation. Even after entry, foreign firms could face certain restrictions on their operations, such as restrictions on employment of foreign key professional or technical personnel and performance requirements such as sourcing or local content requirements, technology-transfer requirements, training requirements and export targets.

As is evident from table IV.7, the types of restrictions relating to FDI have been greatly liberalized in a large number of countries of the region. Many of them now do not require investment approval or licensing, close few sectors to FDI (mainly for national security reasons) and allow repatriation of profits and capital. Several countries, including Indonesia, Malaysia, the Republic of Korea, Singapore and Thailand, liberalized their investment regimes significantly in the 1980s or even earlier. The speed of liberalization gained momentum in the 1990s in most of the countries of South Asia. Liberalization of investment regimes in Pacific island countries and economies in transition has been gradual. For example, China allowed joint ventures beginning only in 1979, and in 1986 wholly foreign-owned enterprises were admitted. On the whole, the policies of countries in the region are increasingly converging towards a highly liberalized regime.

Having sufficiently liberal policies towards FDI is important, but their effective implementation is equally, if not more, important. Bureaucratic hurdles and hassles can create long delays in approval of investment projects, which discourages foreign investors. Even where formal approval is no longer required, other aspects, such as obtaining access to utilities such as electricity, water and telephone service, remain time-consuming. Foreign investors in South Asian countries often complain about bureaucratic hassles.[13] Such problems are also common in Pacific island countries. In ASEAN countries, they are generally a much less important factor, which partly explains the success of these countries in securing foreign investment.

Investment promotion through incentives

Not only have investment regimes been liberalized, but countries have begun offering various incentives to attract foreign investment. Whereas deregulation of investment regimes has reduced government control over the decisions of foreign investors, in some cases these incentives have been used to achieve specific development objectives by directing investment to specified activities and certain geographical areas of the country. Another rationale for investment incentives is to correct for the failure of markets to reflect the wider benefits arising from externalities in production, resulting from such factors as transfer of technology, the spread of knowledge and the upgrading of skills of workers who are mobile. Therefore, the social return to FDI can be higher than the private return, justifying the need for incentives. Provision of incentives is also justified on the grounds that investors should be compensated for domestic market imperfections.

These incentives can be broadly grouped into three categories: fiscal, financial and other incentives. Fiscal incentives usually include a reduction of the standard corporate income-tax rate, tax holidays, accelerated depreciation allowances on capital taxes, exemption from import duties and duty drawbacks on exports. Financial incentives include

---

13 Charan D. Wadhva, "Foreign direct investment policies and related institution-building: the experience of India", paper presented at the Seminar on Promotion of Regional Economic Cooperation in Foreign Direct Investment Policies and related Institution-building among Asian and Pacific Developing countries, 3-5 September 1996, Bangkok.

Table IV.7. Recent changes in investment regimes and incentives in selected developing economies of the ESCAP region

Investment regime	*Fiscal/financial conditions*
Bangladesh	
Restricted sectors for foreign direct investment (FDI) Four local industries are restricted: arms, nuclear energy, forestry and railways; and regulations on drug manufacturing effectively bar foreign corporations from the industry. *Foreign ownership restrictions* 1991: foreign private investment could be undertaken either independently or as a joint venture. 1991: 100 per cent foreign equity was allowed on all investments, not only those in special zones. *Licensing/approvals, rules and procedures* 1991: no formal permission was required to set up a company with foreign investment. *Performance requirements* For all export items, the prior permission of the Bangladesh Bank to open back-to-back letters of credit has been waived as long as such exports conform to guidelines for adding domestic value.	*Foreign incentives for FDI* Tax holidays, accelerated depreciation allowance, and duty-free importation of capital goods for export-oriented industries. *Foreign-exchange repatriation* Full repatriation of invested capital, profits and dividends. *Access to domestic finance* 1992: foreign investment companies could borrow working capital from commercial banks as term loans.
China	
Opening-up to foreign investment 1979: foreign investment allowed in the form of joint ventures. 1986: the law of China on wholly foreign owned-enterprises promulgated. Various activities and sectors have been opened to FDI gradually. The same is true for opening up of various areas and cities. 1994: latest industrial policy authorized. Foreign investment projects for approval have been grouped into four types: encouraged, promised, restricted and prohibited. The list of industrial sectors as regards foreign investment contains only the items of encouraged, restricted and prohibited projects. Projects not listed belong to promised group. *Licensing/approvals, rules and procedures* Approval is required. Increasingly lower levels of governments in China are being delegated powers of approval.	*Fiscal incentives for FDI* Incentives are provided in special economic zones and other open cities. Incentives include reduced income tax rates, tax holidays for projects involving advanced technology, accelerated depreciation allowance and zero import duty on capital goods and raw material.
Fiji	
Restricted sectors for FDI The milling of all sugarcane is handled by the public sector and is closed to private enterprises.	*Incentives for FDI* Incentives provided under tax-free zone/tax-free scheme include tax holidays, accelerated depreciation and import-duty exemptions. Special industry-related incentives exist. Carrying forward of losses is allowed.

(Continued on next page)

Table IV.7 *(continued)*

Investment regime	*Fiscal/financial conditions*
Licensing/approvals, rules and procedures All proposals from foreign investors must be approved by the government. The applications must be submitted through the Fiji Trade and Investment Board, which now acts as a "one-stop shop" for all necessary approvals.	*Foreign-exchange repatriation* Exchange control permission is required for remittances in and out of the country. *Bona fide* applications for foreign currencies for repatriation of capital and profit are generally approved after income tax clearance. *Access to domestic finance* Local borrowing by non-residents is limited.
India	
Restricted sectors for FDI There has been a substantial cutback in areas reserved for public undertakings since 1991. *Foreign ownership restrictions/approvals* Automatic approval for majority foreign investment (5 per cent) permitted in 35 sectors; 100 per cent equity ownership in export-oriented industries; up to 50 per cent in the mining sector and case-by-case approval in all other cases. *Performance requirements* 1991: the government dispensed with local-content requirements.	*Fiscal incentives for FDI* Various tax incentives, including tax holidays, are provided. *Foreign-exchange repatriation* 1992: foreign investors in the stock exchange were allowed to repatriate profits and exchange money at market rates. Full convertibility of the rupee on current accounts. *Access to domestic finance* 1991: foreign companies had (unconditional) access to credit.
Malaysia	
Restricted sectors for FDI Some states prevent any landholding by foreign companies. All sectors are open to foreign investment. *Foreign ownership restrictions* 1988: 100 per cent equity was allowed in projects catering for the domestic market but only for a period of five years. A 25 per cent foreign participation ceiling on privatization has been set. Foreign equity of 100 per cent is allowed in projects exporting 80 per cent of goods producted; up to 79 per cent foreign equity is allowed if exports equal 51-79 per cent of goods produced; 30-51 per cent foreign equity is allowed for exports of 20-50 per cent of goods produced; up to 30 per cent foreign equity for projects exporting less than 20 per cent of production. *Licensing/approvals, rules and procedures* 1988: the approval process for foreign investment and manufacturing enterprises was simplified. A coordination centre on investment has been set up and bureaucratic procedures have been streamlined. *Performance requirements* No local-content conditions apply, although manufactured products should meet local content guidelines to qualify for extended incentives.	*Fiscal incentives for FDI* "Pioneer status" companies are fully exempt from the company profit tax for a period of five years. As an alternative to pioneer status, there is the "investment tax allowance", along with a variety of other incentives, such as deduction of research and development expenditure and allowances for training, exports, reinvestment and buildings. *Foreign-exchange repatriation* Removal of all current account and most capital account controls. Repatriation of capital, profits and dividends, fees, royalties and proceeds from the sale of assets in Malaysia by foreign investors is freely permitted. *Access to domestic finance* Foreign investors are allowed to avail themselves of domestic credit facilities to finance their businesses in the country.

(Continued on next page)

Table IV.7 *(continued)*

Investment regime	*Fiscal/financial conditions*
Pakistan	
Restricted sectors for FDI 1990: the government cut the number of sectors closed to foreign participation to two: defence and items subject to religious bans. *Foreign ownership restrictions* Foreigners can now own up to 100 per cent of the equity in a business. *Licensing/approvals, rules and procedures* 1990: licensing was eliminated. *Performance requirements* No formal local content requirements apply.	*Fiscal incentives for FDI* Tax holidays for longer periods in less leveloped areas of the country; concessional rates of duties for import of plant and machinery and capital gains tax exemption on investment in listed companies. *Foreign-exchange repatriation* 1991: permission was no longer needed to remit dividends and disinvestment proceeds. The government has lifted virtually all foreign exchange controls. *Access to domestic finance* All restrictions on domestic borrowing for fixed investment were removed. For working capital, restrictions were greatly liberalized.
Papua New Guinea	
Restricted sectors for FDI A reserved activities list exist, mainly consisting of small-scale activities. The list is being gradually phased out. *Licensing/approvals, rules and procedures* Foreign investment in mining and petroleum sectors is overseen by Department of Mining and Petroleum. All other proposals are handled by Investment Promotion Authority.	*Incentives for FDI* Exemption from company income tax for various purposes (e.g. export income exemption). Special depreciation allowances. Wage subsidies aimed at promoting employment. Staff training, double tax deduction against company taxation. *Foreign-exchange repatriation* Repatriation of profits, principal, interest and services charges allowed. Payments for the costs of other foreign obligations approved by State are permitted. The country has recently adopted a flexible exchange rate system. *Access to domestic finance* Limited facilities for domestic borrowing available.
Philippines	
Restricted sectors for FDI Foreign companies/residents are unable to own land under the 1987 constitution but can lease the land for long periods. The sectors of mass media, retail trade, rural banks and marine resources, except deep-sea fishing are restricted. *Foreign ownership restrictions* 1991: the government allowed 100 per cent foreign equity in most industries. *Licensing/approvals, rules and procedures* Only those enterprises who wish to avail themselves of incentives need approval from the Board of Investment. 1987: a One-Stop Action Centre was established where representatives from eight government agencies are housed together. *Performance requirements* There are no local content requirements except for car manufacturers, where 40 per cent local content is required.	*Fiscal incentives for FDI* 1987: the "tax holiday" incentive was introduced. 1989: the promotion of industrial estates and infrastructure projects began. 1994, 1995: incentives to export-oriented industries in the form of zero duty on imported capital equipment and spare parts, and tax credits for five years on imported raw materials for production and packaging. Tax holidays in special economic zones. *Foreign-exchange repatriation* 1992: all restrictions were removed. Some remittances are subject to tax.

(Continued on next page)

Table IV.7 *(continued)*

Investment regime	*Fiscal/financial conditions*
Sri Lanka	
Restricted sectors for FDI Five sectors are reserved: pawnbroking, moneylending, retail trade with capital less than $1 million, personal services other than tourism, and coastal fishing. *Foreign ownership restrictions* 1991: 100 per cent foreign equity was allowed. *Licensing/approval, rules and procedures* 1989: the government abolished all industrial licensing requirements, quotas and controls, except in areas such as manufacturing ammunition, explosives, military vehicles and hardware, poisons, narcotics, alcohol, toxic and hazardous materials and printing of currency. 1991: the free and automatic approval of FDI was introduced.	*Fiscal incentives for FDI* Incentives are available for investment in export-oriented projects, in backward areas, in infrastructure and tourism related projects. Incentives include tax holidays, accelerated depreciation allowances and concessional import duties. *Foreign-exchange repatriation* Most types of transactions can be remitted freely.
Thailand	
Foreign ownership restrictions 1991: joint venture criteria were relaxed. 1991: foreign ownership in agriculture, livestock, fisheries, mining and services was increased to a maximum of 49 per cent. 1992: 100 per cent foreign ownership for firms exporting 80 per cent of goods produced was planned. Some sectors require majority Thai ownership. *Licensing/approval, rules and procedures* 1991: the criteria for approving projects were revised to increase transparency. 1992: legislation was enacted to reduce administrative procedures. *Performance requirements* 1993: local content requirement has been removed on many products. No other performance requirements are in place except for firms applying for promotional privileges.	*Fiscal incentives for FDI* Major tax incentives include tax holidays, exemption or reduction of import duties on capital goods and machinery. Greater incentives are granted to export-oriented enterprises and those established in remote areas. *Foreign-exchange repatriation* 1990-1992: exchange regulations were relaxed and mostly abolished. *Access to domestic finance* Foreign investors have full access to sources of domestic finance.
Viet Nam	
Restricted sectors for FDI Land remains the property of the State but can be leased to foreigners. *Foreign ownership restrictions* 1987: foreign firms were free to invest up to 100 per cent equity in almost any field. *Licensing/approvals, rules and procedures* 1996: new investment policy simplified the investment approval procedures.	*Foreign-exchange repatriation* Repatriation of capital is only possible after an enterprise is terminated or dissolved.

Sources: European Round Table of Industrialists, *Survey on Improvements of Conditions for Investment in the Developing World* (Brussels, 1993); and *World Investment Report 1992: Transnational Corporations as Engines of Growth* (United Nations publication, Sales No. E.92.II.A.19); APEC, *Guide to the Investment Regimes of the APEC Member Economies 1996* (Singapore, APEC Secretariat, 1996); and country studies on Bangladesh, China and India presented at the Seminar on the Promotion of Regional Economic Cooperation in Foreign Direct Investment Policies and Related Institution-Building among Asian and Pacific Developing Countries, Bangkok 3-5 September 1996.

grants, subsidized loans and loan guarantees, publicly funded venture capital participating in investment involving high commercial risks and government insurance at preferential rates. Other incentives include a subsidized dedicated infrastructure (for example, industrial estates), subsidized technical assistance and preferential government contracts. Usually, all these incentives are general in nature and are available to all types of foreign investment. However, these incentives have also been used to attract investment in designated industries or in specified areas of the country, particularly export processing zones. Sometimes these incentives are conditional and linked to performance requirements, such as export, local content and technology-transfer requirements.

Table IV.7 includes an overview of various incentives in selected countries of the region. These incentives are widespread as almost all the countries listed in the table have incentive schemes. Moreover, developing countries generally prefer fiscal incentives, partly because fiscal incentives can easily be granted without incurring any financial costs at the time of their provision. These incentives lead to loss of government revenue in the future when the enterprises are actually established and become operational. Non-fiscal incentives usually require allocation of resources. For example, subsidized loans and infrastructure require funds, and developing countries find it difficult to offer such incentives in the face of growing budgetary constraints. Popular fiscal incentives include tax holidays or reduced income tax rates, accelerated depreciation allowances and duty-free imports of capital goods and machinery. Export-oriented industries are accorded preference in regard to incentives. Similarly, investment in less developed areas of a country qualifies for more incentives lasting for longer periods. For example, Pakistan, the Philippines, Sri Lanka and Thailand offer special incentives for less developed areas. Competition among developing countries in provision of incentives has increased over time: a recent study by UNCTAD reports an expansion of incentives in most countries between the 1980s and the 1990s.[14]

The role of incentives in attracting FDI has been questioned on theoretical as well as empirical grounds. Various empirical studies show that incentives play a minor role in attracting FDI.[15] Moreover, these incentives create distortions in the economy, especially those linked to performance requirements. At best, investors find ways to circumvent those requirements or invest real resources to attenuate the adverse effects on their investment decisions. In ASEAN countries, incentives linked to performance requirements have virtually been eliminated.[16] In some cases, such incentives simply result in the transfer of resources from the host developing country to foreign treasuries without any special benefit being provided to foreign investors. If the host country does not tax the investment income owing to a tax incentive, the home country tax regime may be such that the income may end up being taxed there.[17] Thus, the taxation of transnational corporations by a developing country cannot be examined in isolation from the tax regime of the home country. Moreover, these incentives result in financial losses to governments in developing countries in the form of cash outlays and lost tax revenue which are badly needed for development. Most countries eventually offer identical or similar incentives as competition for external resources intensifies. As a result, investors have become less sensitive to these measures in their decisions to locate their investments.

If it is accepted that incentives are not so important, then what other factors have more influence on the inflows of FDI? Some of the important determinants of FDI coming out of the empirical studies are growth prospects, market size, profitability, quality of economic management, few trade barriers, freedom from burdensome regulations on ownership, management and organization, non-discrimination against foreign-controlled enterprises, commitment to economic development, political stability and a favourable government attitude

14 UNCTAD, *Incentives and Foreign Direct Investment* (United Nations publication, Sales No. E.96.II.A.6).

15 Ibid.

16 Denise E. Konan, "The need for common investment measures within ASEAN", *ASEAN Economic Bulletin*, vol. 12, No. 3, March 1996, p. 339.

17 Anwar Shah, ed., *Fiscal Incentives for Investment and Innovation* (New York, Oxford University Press, 1996).

towards private enterprise.[18] From this, it can be concluded that other policy and non-policy variables are more important determinants than incentives in investment-location decisions. As other policy and non-policy conditions converge, the role of incentives gains importance at the margin.

Macroeconomic policy setting and availability of support services

A stable macroeconomic environment is a critical prerequisite for maintaining the confidence of both domestic and foreign investors and achieving steady long-term growth. Large budget deficits, excessive monetary expansion and repressed financial systems are symptoms of chronic instability, almost certainly indicating future problems with inflation, exchange rate weakness and a poor environment for taking long-term investment decisions.

In the ESCAP region, the adverse macroeconomic conditions of the 1970s and 1980s caused by exogenous factors, led to significant declines in growth rates in several countries. However, the economies that adjusted quickly to the shocks of that period, or did not allow their macroeconomic aggregates to get seriously out of balance in the first place, achieved by far the best record of economic growth and rapidly became the most attractive destinations for external capital. It is worth emphasizing that countries in the ESCAP region have, on the whole, compiled a much better macroeconomic record over the years compared with most other developing countries. The more open economies in the region have always been judged to be good country risks, with relatively low risk premiums, by foreign investors and have been able to raise external finance with relative ease. This has had the effect not only of increasing the ESCAP region's share of the resources flowing to developing countries but also of altering their composition in favour of FDI and portfolio investments. These changes are particularly evident in the East and South-East Asian subregions, which are clearly distinguishable by their exemplary macroeconomic, savings and investments records.

In addition to macroeconomic stability, the availability of a physical infrastructure plays a key role in attracting foreign investment. For example, a foreign investor interested in the manufacturing sector will be reluctant to come to a country facing serious electricity shortages. Road, transport and telecommunications facilities significantly contribute to lowering the cost of production. Similarly, an educated and skilled workforce is essential in order to use increasingly sophisticated technology. Countries in the region have started paying greater attention to the provision of infrastructural facilities and other support services. In fact, many countries have started encouraging a greater role for the private sector, including FDI, in the provision of an infrastructure.[19]

Financial sector liberalization and development

Countries in the region have been liberalizing their financial sectors over the years, which has helped to enhance financial flows to these countries. The financial sector reforms have been discussed in detail in the 1995 issue of the *Survey*. Some of the major reforms and developments in the financial sector directly related to private financial flows are reviewed below. These include reduction of barriers to entry for banks and other financial institutions, promotion of new financial markets and external financial liberalization.

In the banking sector, barriers to entry have been reduced in order to increase competition in providing services to customers. This reduction in barriers relates to both domestic and foreign banks. In addition, state-owned banks have been privatized to enhance the role of the private sector and improve competition within the banking sector. Partly helped by financial liberalization, there has been rapid development of non-bank financial institutions and other financial markets and instruments (for example, leasing companies, insurance firms, securities companies, pension funds and mutual funds). The distinctions between various types of financial institutions are disappearing as their services are becoming more diversified and similar services are being provided by more than one type of institution.

---

[18] For a detailed review of relevant empirical studies, see UNCTAD, *Incentives and Foreign Direct Investment*...

[19] For details, see chapter V.

While most countries have introduced improvements in prudential regulations to ensure that banks follow sound business practices and do not jeopardize the stability of the financial system through imprudence and malpractice, the failure of some major financial institutions, such as the Bangkok Bank of Commerce in Thailand recently, highlight the need for further reforms in this area. The situation regarding non-bank financial institutions is generally worse. For example, a large number of people in Pakistan lost their savings with finance companies and cooperatives in the early 1990s. There is a greater need for regulation of non-bank financial institutions.[20]

With deregulation and liberalization in both the financial and the real sectors of the economy, enterprises have started to use equity and bond finance in addition to bank loans. This has led to the establishment or strengthening of stock markets in many countries of the region.[21] Growth in capitalization of these stock markets has been phenomenal (table IV.8). Various types of funds (for example, mutual funds and pension funds) at the national level are increasingly investing in these markets. Similar funds at the international level, mainly based in industrialized countries, are also active and many are investing in stock markets in the ESCAP region. Some of the funds established at the international level are meant solely for investing in a particular country. On the Kuala Lumpur Stock Exchange, for instance, 79 funds were active at the end of 1993; most of these funds invested a certain proportion of their portfolios in Malaysian stocks, while 11 had been created solely for investment in Malaysia.

In many countries, more than one agency has been responsible for the development and regulation of the capital market, which has created conflicts and problems of coordination, a situation not conducive to the development of capital markets. A major reform in this respect was the establishment of a single agency to develop and administer the set of rules and regulations governing stock market activities (table IV.8). Legislation has also been enacted in a number of countries to close loopholes and to set standards aimed at eliminating or minimizing malpractice, and to ensure fuller disclosure of information and a stable trading environment. There is a great deal of cooperation among financial institutions in the region with regard to the sharing of experiences and information. For example, the first meeting to exchange experiences among regulatory agencies of stock markets in the Asian region was held in August 1994. The Central Bankers of the Pacific Island Countries hold annual meetings. In November 1995, the Hong Kong Monetary Authority and the central banks of Malaysia, Indonesia and Thailand reached an agreement under which they could borrow United States dollars from each other, enabling them to raise extra liquidity at short notice and to counter speculative runs on their currencies.

To meet ever-rising finance needs, private debt securities markets are growing. While the corporate bond markets in India, Malaysia, the Republic of Korea and Thailand have grown to moderate sizes, such markets are in the initial stages of development in many countries of the region. One of the most important factors hindering the growth of corporate bond markets in this region is their high credit risk, which implies the possibility that coupon payments and/or principal repayments may not be made on time or at all. There is a need for independent and reliable information on the riskiness of corporate bonds to enable an investor to make an informed decision. Independent credit-rating agencies for corporate bonds have been established in recent years in several countries, including India, Indonesia, Malaysia, the Philippines and Thailand. A common critical challenge faced by these agencies relates to building or improving the capacity to conduct internationally acceptable credit analysis, despite the presence of lower standards of accounting and disclosure in this region compared with those in developed economies. In addition, these agencies can take a relatively long time to rate bond issues. In Malaysia, the government is considering establishing a second credit-rating agency to overcome this problem.

An obstacle related to the development of bond markets in some economies with surplus government budgets is the non-existence of a market for government securities. As a result, there

---

[20] For a detailed discussion of this point, see ESCAP, "Institutional development for macroeconomic policy management and coordination" (E/ESCAP/SB/LDC(3)/1).

[21] The World Bank has recently started placing greater stress on the development of capital markets in general and stock markets in particular. The May 1996 issue of *The World Bank Economic Review* is a symposium issue, which seeks to boost knowledge of the relationship between stock markets and economic development.

Table IV.8. Development of equity markets

Country	Year of establishment of stock exchange(s)	Growth of capitalization (billions of US dollars)		Status of foreign participation	Regulatory agency
		1987	1996		
Bangladesh	Dhaka Stock Exchange revitalized in mid-1970s	–	–	Since 1992, 100 per cent equity participation by foreigners allowed; some registration procedures required to ensure repatriation rights	In 1994, a Security Exchange Commission was constituted
China	Shanghai and Shenzen Stock Exchanges established in late 1980s	–	42	As of March 1993, special classes of shares (B-shares) are available to foreign investors	China Securities Regulatory Commission established in 1992
India	Several local stock exchanges exist. A National Stock Exchange is under establishment	12	144	Only listed foreign institutional investors permitted to invest in capital market	Securities and Exchange Board of India established in 1988
Indonesia	Jakarta Stock Exchange revived in 1977	1	75	Since 1989, foreigners have been permitted to invest in Indonesian public companies with a 49 per cent limit	Bapepam (the Capital Market Supervisory Agency) established in 1976
Malaysia	Kuala Lumpur Stock Exchange established in 1960	10	240	Listed stocks freely available to foreign investors since 1989	The Security Exchange Commission set up in March 1993
Pakistan	Karachi Stock Exchange established in 1948, Lahore Stock Exchange in 1970 and Islamabad Stock Exchange in 1992	–	11	Listed stocks freely available to foreign investors as of March 1993	The Corporate Law Authority regulates and supervises the capital market
Philippines	The Manila Stock Exchange and the Makati Stock Exchange merged in 1993 to form the Philippine Stock Exchange	3	66	Special classes of shares (B-shares) available to foreign investors as of March 1993	The Securities and Exchange Commission has undergone a total reorganization since August 1995
Republic of Korea	Seoul Stock Exchange established in early 1970s	30	175	Beginning in 1992, foreign investors were allowed to buy Korean stocks subject to a 12 per cent ceiling, with share restrictions to be removed gradually	The Security Exchange Commission established in 1977
Singapore	The Stock Exchange of Singapore was formally separated from the Kuala Lumpur Stock Exchange in 1989	15	176	Foreign investors are allowed to buy stocks of local companies and float their securities on the Singapore stock exchange	The Monetary Authority of Singapore has extensive regulatory and supervisory responsibilities

(Continued on next page)

Table IV.8 *(continued)*

Country	Year of establishment of stock exchange(s)	Growth of capitalization (billions of US dollars)		Status of foreign participation	Regulatory agency
		1987	1996		
Thailand	Stock Exchange of Thailand in its current form has existed since 1975	5	149	Since 1993, stocks of domestic companies available to foreign investors are subject to a 49 per cent ceiling. Some registration procedures are required to ensure repatriation rights	In 1992, the Security Exchange Commission was established

Sources: S. Gooptu, "Portfolio investment flows to emerging markets", in S. Claessens and S. Gooptu, *Portfolio Investment in Developing Countries*, World Bank Discussion Papers No. 228 (Washington DC, 1993), pp. 72-73; "Asian finance survey", *The Economist* (12 November 1994), p. 9; M. Goldstein and others, *International Capital Markets, Developments, Prospects, and Policy Issues* (Washington DC, International Monetary Fund, September 1994), pp. 126-127, Business Monitor International Ltd., *Thailand 1996-1998* (London, June 1996) and national sources.

is no benchmark risk-free rate, which obliges the market to determine both the risk-free rate and the risk premium associated with a specific corporate bond. Hong Kong has started auctioning government bonds to supply a benchmark risk-free rate, even though it does not need the financing.[22] Malaysia and Singapore are planning the same in the near future. The countries with budget deficits can also auction their public debt in order to provide a benchmark risk-free rate, which, in turn, would help in the emergence of bond markets in those countries. In addition, governments can issue guarantees for private bonds as a means to develop and strengthen bond markets; this is already being done in the Republic of Korea, which has the region's most rapidly expanding bond market.

The liberalization of financial flows has involved reforms of both the domestic as well as the external financial markets. The liberalization of the external financial markets is expected to be one of the most important parts of this general movement towards greater openness to international capital flows. The main elements of external financial liberalization policies include decontrol of foreign exchange transactions on current accounts, making exchange rates flexible and removing or easing restrictions on capital flows between countries. Aspects of capital account liberalization include granting permission to domestic banks and corporate businesses to borrow offshore in foreign currencies, allowing foreign participation in domestic financial market institutions and instruments, and allowing domestic financial institutions to set up foreign branches or affiliates (some of the above-mentioned reforms are included in table IV.7 for selected countries). Because many countries around the world have adopted such policies, the provision of investment finance is increasingly becoming an integrated global industry.

Bilateral and regional levels

In contrast with the number of regional trading arrangements in this region, there are very few investment arrangements. This is partly due to the fact that developed countries are the major source of investment resources, which reduces the need to have investment arrangements at the regional level among developing countries. Strong competition among developing countries to secure a larger share of the limited resources available in the form of foreign investment is another factor. In addition, developing countries can have divergent needs and development strategies and may not be willing to lose control over resource inflows. However, a large number of bilateral investment treaties have been signed, again

22 Joseph E. Stiglitz and Marilou Uy, "Financial markets, public policy and the East Asian miracle", *The World Bank Research Observer*, vol. 11, No. 2, August 1996, p. 249.

mainly between developed and developing countries.[23] The signing of these treaties among developing countries has also started to increase.

Usually, bilateral investment treaties deal exclusively with investment and lay down specific standards of investment protection and transfer of funds. They contain provisions for the settlement of disputes both between the treaty partners and between investors and the host State. They generally recognize the effect of national law on FDI and accept the right of governments to regulate entry of FDI. They can contain exceptions or qualifications to some general principles (for example, exceptions for balance-of-payments considerations in relation to the principle of free transfer of funds). By providing protection, bilateral investment treaties help in promoting FDI. At the bilateral level, separate from bilateral investment treaties, a large number of treaties for avoidance of double taxation have been concluded.

At the regional level, there have been two major initiatives by ASEAN and APEC dealing with investment. A brief analytical description of them is provided below.

Investment agreement between the ASEAN countries and the ASEAN Investment Area

In 1987, Governments of ASEAN member countries signed an agreement for the protection and promotion of investment.[24] It is a legally binding intra-ASEAN agreement. The agreement obligates each contracting party to encourage and create favourable conditions in its territory for investment from other contracting parties. The agreement applies only to investments specifically approved in writing and registered and which are in accordance with conditions prescribed by the host countries. However, this agreement does not affect the rights and obligations of the contracting parties with respect to investments which, under the previous stipulation, do not fall within the scope of the agreement. The agreement provides most-favoured-nation treatment to investors. National treatment is not granted, but countries may negotiate it separately. The agreement has clauses dealing with protection of investment and provides for adequate compensation in case of expropriation of investment under special circumstances. Regarding protection standards, treatment according to international law is granted. Free transfer of funds and repatriation of investment are provided. The agreement also provides a mechanism for solving disputes between the contracting parties.

While the above-mentioned agreement deals with promotion and protection of investment between ASEAN member countries, the decision of the Fifth ASEAN Summit, held in Bangkok on 14 and 15 December 1995 on an ASEAN Investment Area[25] represents an important step toward establishing the whole ASEAN region as a host to inward FDI by promoting ASEAN as a single, diverse but increasingly integrated area, rather than seven alternative investment locations.

> "The basic concept of the ASEAN Investment Area is to substantially increase the flow of investment into ASEAN from both ASEAN and non-ASEAN sources by enhancing ASEAN's attractiveness and competitiveness for investments. This would be done by jointly promoting ASEAN as the most attractive investment area and by strengthening and increasing the competitiveness of ASEAN's economic sectors through greater ASEAN cooperation and progressively reducing and eliminating impediments to investment. The scope of investments covers manufacturing and non-manufacturing sectors, with emphasis in the initial stages on the manufacturing sector."[26]

The features and measures of the ASEAN Investment Area are being developed, and it is expected to be in place within 10 to 15 years. Measures to establish the investment area are to be divided into three segments: a facilitation and cooperation programme, a promotion and awareness programme and a liberalization programme. The liberalization programme is expected to be

---

23 According to the UNCTAD, *World Investment Report 1996*, roughly 1,160 treaties involving 158 countries were concluded up to June 1996, approximately two thirds of which were concluded in the 1990s.

24 A revised agreement which includes Viet Nam is ready in draft form. Once signed, it will supersede the current agreement. The draft revised agreement contains additional articles on the simplification of investment procedures and the approval process, transparency and predictability, sojourn of personnel and accession of new members.

25 The name proposed originally was the ASEAN free investment area.

26 ASEAN Secretariat, *Recommendations of the ASEAN Heads of Investment Agencies on the ASEAN Investment Area*, Jakarta, 1996, p. 1.

implemented at a pace commensurate with each ASEAN member economy's ability to implement it without destabilizing the economy.

A number of growth triangles have been set up in the ASEAN region to promote FDI and investment from within the region. These are mainly loose and informal arrangements emerging largely out of existing complementarities. A joint and coordinated effort by the private sector and governments has been made to create the necessary infrastructure and other policy conditions for manufacturing ventures and service units to be established in the triangles. The Singapore-Riau-Johor growth triangle is probably the oldest, and it has achieved significant success. Among the new ones are the East ASEAN growth area comprising, parts of Brunei Darussalam, Indonesia, Malaysia and the Philippines, and the ASEAN northern growth triangle, comprising parts of Indonesia, Malaysia and Thailand.

Growth triangles can be interpreted as an attempt to achieve at the microlevel what the ASEAN Investment Area may eventually do on a larger scale. Their rationale is to facilitate productive efficiency by allowing enterprises to combine labour supplied by the less developed regions (for example, Batam as part of the Riau islands, Indonesia) and capital and skills from the more developed partner (Singapore). As these growth triangles are generally led by the private sector and set up to attract foreign investment from within and outside the region, they represent a positive, although relatively limited, approach. Growth triangles may thus be seen as offering a scope for geographically restricted but earlier implementation of measures that may be applied regionwide as the ASEAN Investment Area concept matures.

APEC non-binding investment principles

The importance of FDI to economic development in the Pacific region led APEC to establishing common non-binding investment principles. They are meant to be a facilitation device and not a means to force members to liberalize their investment regimes. They only require best efforts. Endorsed by APEC ministers in 1994, these principles take into account the growing number of bilateral investment agreements and the common elements between existing subregional arrangements relevant to investment.

APEC non-binding investment principles require transparency in all laws, regulations, administrative guidelines and policies pertaining to investment. Member economies are to follow the principles of MFN and national treatment in relation to the establishment, expansion, operation and protection of foreign investment. These principles basically require equal treatment of foreign and domestic entities and no discrimination between foreign entities. The latter principle is important because it forbids discrimination between APEC and non-APEC members, in line with the open regionalism concept.

Member economies are not to relax health, safety or environmental regulations as an incentive to foreign investment. Use of performance requirements that distort or limit expansion of trade and investment is discouraged. Expropriation of foreign investment is forbidden, but, if it becomes unavoidable, prompt payment and effective compensation are to be made. Prompt and free repatriation of profits, dividends, royalties, loan payments and liquidations in freely convertible currency is the goal for the member economies. In addition, regulatory and institutional barriers to the outflow of investment are to be minimized. Temporary entry and sojourn of key foreign technical and managerial personnel connected with foreign investment is to be permitted, subject to the relevant laws and regulations. Double taxation related to foreign investment is to be avoided, and foreign investors are to abide by the host economy's laws, regulations, administrative guidelines and policies.

Disputes are to be settled through consultations and negotiations between the disputing parties. These provisions, in a legal sense, provide no protection. However, the principles are valuable since they contribute to the understanding of what is "fair" and "not fair" in treating FDI. Such an understanding is very important for dispute settlement through an informal process, so that both parties are satisfied and convinced of the fairness of settlement. While these principles are voluntary in nature, they could form the basis for more formal cooperation at the regional level.

International level

There are already some agreements at the international level related to sectoral or specific issues in the area of foreign investment, notably GATS and the agreements on TRIMs and TRIPs. These agreements were discussed in the previous chapter in the context of foreign trade and are reviewed here briefly.

Foreign investment in the services sector is regulated by GATS, since it covers the supply of markets through the presence of foreign service suppliers. A limited number of countries from the region made some commitments regarding market access and national treatment. The intention is for these commitments to be progressively enlarged in coverage and depth through further negotiation. The process of liberalization envisaged in the agreement takes into account the level of development of individual countries and their national policy objectives. As a result, the developing countries have the flexibility to strengthen their domestic services sector first and then gradually open it to foreign competition.

The performance requirements of FDI are dealt with in the TRIMs Agreement. The agreement covers only investment measures related to merchandise trade. It restricts the use of the following three TRIMs: local content requirements, trade balancing requirements and foreign exchange balancing requirements. It gives a two-year period to developed countries to implement its provisions, five years to developing countries and seven years to least developed countries. More time can be granted upon the consent of all contracting parties. Some developing countries are reluctant to give up TRIMs because they consider them a part of their broader development strategy. However, many developing countries, including those in ASEAN, have already phased these measures out or are in the process of so doing.

The TRIPs Agreement deals with the protection of intellectual property rights in trade and investment. It specifies general provisions and basic principles regarding the protection of intellectual property rights, including national treatment and MFN requirements, as well as rules on substantive standards for the protection of specific categories of intellectual property rights, domestic enforcement procedures and international dispute settlement. The full implementation of the agreement is to be completed by 2015.

Private capital flows to developing countries in general have been on the rise. However, all countries have not equally benefited, often because perceived political and commercial risks restrict the entry of foreign investors. Therefore, the wider availability of investment guarantees through insurance coverage can potentially enhance flows of FDI to a wider range of developing countries. Already, the Multilateral Investment Guarantee Agency (MIGA) of the World Bank provides insurance coverage to foreign investors for political risks in developing countries. Before issuing a guarantee, the agency must be satisfied that the laws of the host countries meet basic standards and that the investor complies with these laws. Its membership is open to all members of the World Bank, and it had 128 members as of July 1995. The demand for the insurance services of MIGA has rapidly increased in recent years, and by 1995 it had facilitated over $6 billion in FDI in its developing member countries, including China.[27] With the rise in private capital flows, multilateral lending institutions may consider taking a larger role in guaranteeing private investment, for which there will be growing demand.

Some reflections

The adoption of outward-looking development strategies by an increasingly large number of developing countries has contributed to the rapid liberalization of foreign investment regimes in the region, mainly in the form of unilateral actions at the national level. A large number of bilateral investment treaties and some initiatives at the subregional level have also helped in shaping the increasingly open FDI regimes. Moreover, some FDI-related issues have been included in the Uruguay Round agreements. As a result of and parallel to these initiatives, developed countries have started calling for a multilateral agreement on investment. OECD countries have already started negotiations on such an agreement at their level.[28] A global agreement is needed, it is argued, because existing policies and arrangements at the national, regional and international levels, covering a widening set of issues, contain overlaps, gaps and inconsistencies and, when taken together, do not constitute a coherent and complete international FDI framework. Therefore, the feeling is increasing that a multilateral investment framework would create a stable, predictable and transparent enabling environment, which would help to enhance FDI flows and to promote the development of countries.

While developing countries are willing to enter into bilateral investment treaties and regional agreements and some sectoral and issues-specific multilateral agreements, many of them are not yet willing to have a comprehensive multilateral agreement on investment. One reason for this is that most

[27] UNCTAD, *World Investment Report 1995*....

[28] UNCTAD, *World Investment Report 1996*....

developing countries are only recipients of FDI, whereas developed countries are both sources and recipients. This asymmetry in the relationship between developed and developing countries is one factor which is not present in the case of foreign trade, where all the countries, irrespective of their development status, are both exporters and importers. As the developing countries become exporters of capital, their reluctance to have an investment framework at the international level will perhaps diminish.

More importantly, many developing countries consider investment measures important policy tools for development. Investment measures are usually designed with the objective of promoting broad goals, including economic development, import substitution and export promotion, employment growth, technology transfer and easing of balance-of-payments pressure. Therefore, a change in the investment policy would require changes in the broader policy regime. These implicit linkages make the task complicated and add to the reluctance of developing countries to dismantle investment measures fully. In addition, there are significant differences in national characteristics and conditions, making the achievement of a uniform global investment policy a difficult task. Moreover, in a very open environment some countries may fear losing control over their resources and may prefer an approach in which the starting point is not the foreign investor's right to invest but the host country's permission to allow them to do so.[29] GATS takes this point into account while addressing the issue of establishment; the agreement does not create a "right of establishment" but rather a "permission of establishment".

Some countries may fear that allowing foreign investors unrestricted access may result in their acquiring substantial power in some product markets and then abuse their dominant position in the market. Given their financial resources and access to technology, foreign firms would find it generally easier to indulge in restrictive business practices. The need for a competition policy at the national level is obvious. Moreover, the need for safeguard mechanisms at the international level to deal with restrictive business practices has also been argued.[30]

A consensus is emerging among countries of the world on greater cooperation with regard to FDI, but there are differences on how to achieve it. The countries wishing to continue with the current evolving arrangements do not rule out a comprehensive agreement at some later stage. Moreover, rapidly converging development and investment policies among countries are going to make the achievement of this goal easy. It seems that a gradual approach would gain broader acceptance among developing countries. The recent establishment of the APEC non-binding investment principles and the success of their implementation over time will provide useful lessons for a global agreement. A similar set of non-binding principles can be formulated at the international level as a preliminary step, and they could be converted at a later stage into a formal agreement, which could meet the varying needs of certain groups of countries through exceptions and qualifications and by giving a longer time period to developing countries for implementation of the provisions of the agreement.

PROSPECTS AND CHALLENGES

While the developing economies of the ESCAP region, almost without exception, are in the process of adjusting their policy stances towards encouraging more integration with global markets for finance and investment, this process is not without problems. This section outlines some of the challenges associated with greater efforts towards such integration as well as the prospects in the light of developments in the 1990s. However, new and unforeseen difficulties are likely to arise, especially for the countries in the region which have had limited access to and experience with international financial flows to date, as financial engineering is rapidly changing the world of finance.

Prospects

Trade and financial flows are closely interrelated and, as indicated in Chapter III, prospects for trade in the region over the next 5 to 10 years are highly optimistic. As trade increases, output becomes more specialized; this process is then built upon and reinforced by larger flows of finance between countries. Within this broad framework, prospects for financial flows for economies in

---

29 Ibid.

30 This issue is discussed in detail in chapter 7 of ESCAP, *Asian and Pacific Developing Economies and the First WTO Ministerial Conference: Issues of Concern*, Studies in Trade and Investment No. 22 (ST/ESCAP/1705).

the region need to be evaluated with respect to the following: (a) sustainability from the point of view of both the providers and the recipients; (b) flows from within the region; (c) implications arising from the increasing variety of private international finance; (d) the limited access to private finance for many countries in the region, and (e) prospects for ODA.

Sustainability

This discussion starts from the assumption that the openness, outward orientation and commitment to the macroeconomic balance of the economies in the region will, by and large, be maintained and that there will be no significant policy slippage in these areas. On that assumption and other things being equal, financial capital should flow from capital-rich economies, with relatively low rates of return, to capital-poor economies, with relatively higher rates of return on a risk-adjusted basis. However, investors' perceptions of capital-importing countries can change in ways that are unrelated to changes in the fundamental economic conditions prevailing in these economies. There is ample evidence of many investors being simultaneously influenced by changes in sentiment (the so-called "herd instinct"). In addition, if one country in a subregion has macroeconomic problems, then the perception of the attractiveness of neighbouring countries to investors may be negatively affected.

Furthermore, there is at all times a juxtapositioning of cyclical and secular forces at work in capital-exporting countries that can affect sustainability from the providers' side. For instance, in times of recession, capital-exporting countries generally provide poor returns on investment, and resources tend to flow from them. Over the long term, however, these lower returns are offset by higher returns when such economies turn around and profitability improves. So financial flows from these countries tend to be cyclical. Thus, while the overall trends in the size of financial flows from developed to developing countries and in the integration between them are increasing, predicting the amplitude of the fluctuations around this trend is uncertain.

Another consideration in this context is that the current attractiveness of emerging markets as alternative destinations for investment funds could be a one-off phenomenon based on the transitory enthusiasm generated by the process of reform and liberalization recently initiated in these economies. It is conceivable that some of these flows of capital could taper off significantly in the years ahead and capital-importing countries would have to offer substantially more competitive returns in order to continue receiving financial flows. In addition, capital-importing countries would need to show evidence of improvement in the supervision, administration and regulation of their financial markets and of both bank and non-bank financial institutions, most of which are currently considered less well supervised than markets and financial institutions in capital-exporting countries, and so less secure for investors.

There is some merit to the argument that as fiscal consolidation takes firm root in the industrialized countries, their interest rates should drop further or at least should not increase. This offers the opportunity for an increasing interest rate differential between these mature markets and those in developing countries. Such a situation should induce increased flows of finance, particularly debt and portfolio finance, from developed to developing countries, including those in the Asian and Pacific region. However, once the interest rate differential narrows as a result of the flows, they could taper off again.

These factors are not necessarily applicable to FDI. However, even with such long-term flows, problems could arise. From the point of view of providers, FDI flows are sustainable as long as they generate the expected rates of return on capital and/or fit in with the overall production strategy of the investor. In the 1990s, there has been a rapid growth of FDI as transnational corporations have shifted production of labour-intensive items to lower-cost locations or have segmented the production process itself. Clearly, such trends are likely to continue for some time to come and to vary in both time and space between types of industries. One positive element in this picture is that as more countries of the region undertake greater liberalization of their FDI policy regimes, the geographical scope for relocating production will expand.

From the point of view of recipient countries, all large inflows of foreign capital bring in their wake a potential balance-of-payments problem associated with the return flow of resources. Current financial flows, with their preponderance of non-debt-creating forms such as FDI, will generate return flows

through the profits and dividends that the investments yield. The question that arises is whether the countries in the region have the capacity to continue to absorb these flows effectively and generate a stream of foreign exchange earnings. Moreover, it should be noted that, in the long run, the cost of servicing FDI can be higher than the cost of servicing debt.[31]

In this regard, the ESCAP region is much better situated than other parts of the developing world. With its high rates of trade and GDP growth, it should be able to profit from its own dynamism as well as from the contribution of regional trading arrangements and other economic cooperation arrangements established or being established in the region. A very significant proportion of trade now occurs within the region and, as intraregional trade grows, financial flows should grow in tandem. In addition, as economic cooperation arrangements begin to function as one investment space, inflows of finance and capital from within and from outside the space will increase. However, it should be stressed that, for the time being, the countries benefiting from this dynamic remain concentrated in the East and South-East Asian subregions. In other parts of the ESCAP region, the impediments to financial flows discussed above are unlikely to be overcome in the immediate future, and the access of these countries to private sources of finance will remain constrained.

Finance from within the region

The prospects of increasing financial flows from within the region are bound up, ultimately, with the same considerations that apply to financial flows from the rest of the world. The attractive destinations in the region, such as East and South-East Asia, with their greater range of opportunities and better rewards, will be able to draw in finance from within the region, especially now that an increasing number of economies have become capital exporters. China, for example, is now both a large importer of capital and a significant exporter of capital, as, are Hong Kong, Malaysia, the Republic of Korea, Singapore and Taiwan Province of China to varying degrees. Financial flows originating from within the region can end up outside the region when the objective being pursued relates to the strategic acquisition of technology (Malaysia's acquisition of Lotus), or inside it, when some segment of domestic production is being shifted to a lower-cost location (Singapore's investments in Indonesia). While there are no a priori grounds for regional investors to prefer investing within the region, there may be practical reasons for them to do so. The interest of ASEAN countries in investing in the Mekong area illustrates this point.

The situation becomes blurred when portfolio flows or bank loans are considered, as once an asset has been acquired by an institution or investor from within the region, it can be traded and end up anywhere in the world. However, it is the initial acquisition that is important. Intraregional financial flows could expand as knowledge and familiarity with capital markets increase and intraregional financial linkages develop. This could happen partly as a market response and partly through active, official promotion. In either case, the prospects for increasing intraregional financial flows would appear to be encouraging over the long term. In this context, it is worth mentioning that developing economies in the region hold foreign exchange reserves amounting to about $400 billion as of June 1996. The exact disposition of these reserves is not known, but a large part is probably held outside the region. It is possible that a significant proportion of these reserves may eventually be held within the region.

Increased variety of finance

One positive prospect for the region is the increasing diversity of sources of finance both in terms of a spread of origins and in terms of the forms available, that is, equity, bonds, bank loans and FDI. For non-FDI flows, international markets now function more or less as an integrated whole, and the country of origin of the financial flow is not only unimportant but often diverse and unknown. Equities and bonds issued by the same entity are traded in more than one location, and bank syndicates can be regional or international in terms of

31 Stijn Claessens, "Alternative forms of external finance: a survey", *The World Bank Research Observer*, vol. 8, No. 1, January 1993, p. 91.

membership and participation. The legal domicile of the lead-manager financial institution is usually no more than an academic curiosity. As far as FDI is concerned, origin is important to the extent that a particular transnational corporation has the technology as well as the marketing networks which are to be accessed in order to make the investment profitable. The increasing spread of transnational corporations beyond those whose head office is in one of a limited number of developed countries and the widening spread of their international production and marketing networks bring an increasing choice to host countries and should benefit the region. This is particularly so as many of the new transnational corporations have their headquarters within the region.

The prospects for countries to access the increasingly wide range of instruments appear more restricted. Portfolio equity flows are naturally confined to economies either with functioning stock markets or with a sufficient mix of company stock that can be marketed as a country fund abroad. There are already a number of stock markets in the region, and several countries which do not have them are making efforts to start their own or have such plans on the drawing boards. However, caution should be exercised in setting up many small national stock markets as these markets are likely to remain thin and volatile, with too few companies listed and too few players to be able to attract much participation either domestically or from international investors (see box IV.2). The use of country funds marketed through other capital markets within the region seems to be an attractive option which has yet to be sufficiently exploited.

Despite their inherent volatility, inflows into existing stock markets in the region provide a useful adjunct to the sources of finance available to a country, with positive effects on the costs and availability of funds. As developing countries, taken together, still account for a very small proportion of the aggregate cross-border portfolio flows from the developed countries, there is scope for such flows into the ESCAP region to increase on balanced portfolio considerations. This will happen if recipient country stock markets can maintain a combination of stability and growth comparable to their developed country counterparts and improve the levels of supervision and regulation and of efficiency in settlement procedures. There is also the likelihood that a larger volume of institutional finance, such as pension funds (including those from domestic sources), as distinct from the more speculative short-term flows, will be drawn into these stock markets. These increased flows should provide an incentive for an increasing number of companies from a wider range of productive sectors to raise investment finance through these markets by establishing good track records of profits and dividends.

A related consideration in increasing the diversity of sources is the ongoing efforts to widen investment outlets and develop more active corporate bond markets in recipient countries. Investments in bonds can dampen volatility in the equity markets by providing a balanced mix of stock and fixed rate instruments, thus reducing downside risks. However, the development of active bond markets requires the availability of fixed (or floating) rate instruments issued by the government or central bank along the full range of the maturity spectrum so as to have benchmarks against which similar securities issued by the private sector can be priced. The pricing function also needs to be credible, and independent bond rating agencies may play an important role in this respect. These conditions may place a limit on the number of viable bond markets in the region but should not stop enterprises from other countries from issuing bonds on credible markets.

Many of the governments of the region have rarely issued bonds on international markets; they have preferred, instead, to tap international bank syndicates when external funds have been needed. There is little qualitative difference between bonds and bank loans, except possibly in issuance costs and the risk of embarrassment if a particular bond issue evokes a poor response. However, bank finance is likely to remain the main option available to many countries in the region, on the grounds of familiarity if nothing else. Access to international bond markets will remain limited for some time to come for governments unless they overcome their reluctance to tap this source of finance. In order to do so, they will have to be willing to accept maturities and spreads in line with market conditions.

Box IV.2. Institutional prerequisites for capital market development

As incomes and savings rise, most developing countries have exerted efforts into expanding and improving the banking infrastructure so that individuals feel secure keeping their savings in monetized form, usually as deposits with banks. When use of the banking system for facilitating savings is quite widespread and savings rates are moderate to high, the need is increasingly felt that savings outlets should be diversified, in particular for the purpose of providing a better intermediation between savings and investment. This has certainly been true in East and South-East Asia, where savings rates are exceptionally high. Capital markets have been viewed as a principal means to this end and several governments have undertaken efforts to educate their populations about the benefits of savings through share and bond ownership. More emphasis has been placed in this regard on the trading of stocks than on trading bonds, with bond markets still in their infancy in most countries. Stock markets have also been considered as vehicles to promote widespread public ownership during the privatization of state enterprises.[a]

However, capital markets can become an effective means of facilitating savings and investment only when they attain a certain critical mass in terms of both the number of companies and the number of active players and when they can offer an appropriate mix of investment instruments, including equities and bonds. In addition, they need to be able to attract participation from a reasonably wide spread of enterprises from different economic sectors to provide a broad-based range of investment options to savers. By these criteria, several of the smaller economies in the region are almost automatically disqualified from having viable capital markets for the time being. Such economies, including some of the least developed countries, the economies in transition and the Pacific islands, might therefore be better off using the services of other more established financial markets in the region through, for instance, cross-listings, or by forming joint, subregional capital markets. Hong Kong and Singapore, for instance, can offer the full range of capital market services to savers and investors comparable to those available in the developed countries.

Growth in market capitalization, the availability of shares or bonds issued for an increasing diversity of companies and low day-to-day volatility are important manifestations of efficient capital markets. Underpinning the strength of these phenomena, whether in the region or elsewhere, is the quality of the related infrastructure, such as the effectiveness and credibility of the market intermediaries and the soundness of the regulatory regime overseeing them.[b]

Capital market intermediaries essentially consist of underwriters and brokers. Underwriters are responsible for new share or debt issues, while brokers, who are usually members of stock exchanges, buy and sell securities (shares and bonds) on behalf of clients, including underwriters. In most capital markets in the region, there is a degree of relationship between and, indeed, some overlapping of functions between the underwriters and brokers as underwriters rely on the expertise of brokers for a considerable part of their operations. A sufficient degree of competition among intermediaries is an important prerequisite for efficient capital markets. This is partly to reduce the likelihood of collusion and of market manipulation and also to provide an efficient pricing service for investors. Efficient pricing is important as the entities trading on capital markets normally issue audited financial reports only at fixed intervals, generally once a year (although many companies now also issue interim, usually unaudited, reports more frequently). The intermediaries provide the varying analyses and assessments of the performance of companies between the financial reports for the benefit of the capital market and also perform the pricing function and help to create a secondary market in which the securities can be traded at the prices so determined.

Carrying out the pricing function efficiently depends on a number of other factors as well: the timeliness and reliability of the financial information provided by the entities whose securities are being traded on the stock market, the professional standards and expertise of the accounting function in the country concerned, the quality of information and research on the companies and the market information made available to the public by the intermediaries. It also depends

---

[a] Asli Demirgüç-Kunt and Ross Levine, "Stock markets, corporate finance, and economic growth: an overview", *The World Bank Economic Review*, vol. 10, No. 2, 1996.

[b] World Bank, *The Emerging Asian Bond Market* (Washington DC, 1995).

on the credibility and independence of the rating services available, if any. In addition, efficient pricing also requires the existence and observance of rules regarding the timely disclosure of price-sensitive information by companies so as to prevent or lessen abuses such as insider trading. On all these matters, standards vary widely across the region.

Both the entities whose shares or bonds are trading on the capital markets and the intermediaries acting on their behalf need to be governed by an effective regulatory regime. In most of the region, firms have been under the ambit of a body of company law that goes back many years, whereas the situation with regard to underwriters and brokerage firms is somewhat ambiguous. In the past, most of their functions were not independently overseen by any regulatory body or authority in many countries. While banking operations were regulated by the central banks, other activities, such as underwriting or project financing that formed an important component of the financial system, were carried out by specialized, state-owned institutions that were directly supervised by the government itself. Most stock exchanges were, by and large, under self-regulatory regimes.

As the capital markets have become more important, developing economies have been placing more emphasis on strengthening the regulatory side. Indonesia and the Republic of Korea established capital market supervisory agencies relatively early, in 1976 and 1977 respectively, and India did so in 1988. Most of the other economies with important capital markets established unified overseeing agencies in the 1990s. These bodies not only regulate the underwriting activities of investment houses or merchant banks but also oversee the stock exchanges and bond markets.

As far as the underwriters are concerned, the overseeing role is essentially concerned with protecting the potential investor from the dangers of fraudulent misrepresentation. Fairly strict rules now exist about what may or may not be said in prospectuses or information memoranda when share or debt issues are being planned. Brokerage houses have rules against insider trading or against the formation of groups to influence a share price artificially. Takeover bids have to be disclosed. In most countries, these intermediaries have to be licensed and the staff have to pass examinations to obtain the right to trade. Nevertheless, fly-by-night brokers are not uncommon, causing harm to the credibility of the markets and loss of savings to investors.

The stock exchanges and bond markets, for their part, have to ensure that their listing rules are properly observed, that companies file properly audited accounts as and when required and that members, or their agents, settle transactions, such as transfer of share ownership, within stipulated time periods. As these functions come under the umbrella of special regulatory agencies, many countries have also carried out changes in the applicable legal arrangements. These include strengthening the power of overseeing institutions to carry out investigations into alleged malpractice and levy penalties on the offending parties. Indeed, some forms of malpractice, such as the deliberate concealment of information by companies or underwriters, have been converted into criminal offences in some countries in the region.

Overall, the ambit of the regulatory regimes is very similar to the standards prevailing in the developed countries, and developing countries, by and large, have made good progress in strengthening their capital markets compared with, say, the mid-1980s. Market capitalization has risen and the variety of companies and instruments traded has expanded. There has been a process of institutional development in developing country capital markets, particularly in the Asian region, to attract both domestic and foreign investors.[c] However, much still remains to be done.

It is clear that the prerequisites for the institutional development of capital markets as described above can be met by only a small number of economies in the region. Also important are related developments in at least three areas. First, it is self-evident that setting up the institutional infrastructure for the supervision of capital markets is one thing; ensuring that the function is performed with an acceptable degree of effectiveness is another. Many developing countries in the region do not as yet have the required depth of well-informed investors, underwriters, market professionals and regulators to do the job. Hence, a considerable effort in the area of training personnel, and building and nurturing adequately manned independent institutions, for the purposes of supervision is still needed.

Second, supervision of capital market operations depends upon the deregulation of financial markets, in particular the freeing of interest rates so that market-based benchmark rates can be determined and risks can be properly differentiated between various types of issuers. Many countries in the region have still to free interest rates completely. This applies particularly to South Asia but also elsewhere to varying degrees.

---

[c] ESCAP/UNCTAD, *Foreign Investment in Asian Stock Markets*, Monograph No. 6 (ST/ESCAP/1699).

(Continued overleaf)

(Continued from preceding page)

Third, there has to be commensurate development in the relevant legal fields, not just in the general statutes covering capital markets but also in the development of case law and precedent. Very often, regulators think it sufficient to draw attention to the governing statutes and regulations affecting the capital markets as an indication of security. For most investors, this is usually not enough; it is the actual rulings by the relevant courts or other authorities that are important.

It is self-evident that progress in the three areas listed above, as well as the development of highly skilled professional expertise for intermediation, cannot be achieved overnight. However, recent experience suggests, and the exchanges in South Asia are a good example, that investors are generally satisfied with the direction in which change is taking place. In this regard, the increasing depth of capital markets as demonstrated by the entry of overseas institutional investors, such as mutual funds, is an encouraging sign, indicative of a growing level of maturity in these markets. An important additional element is the overall fiscal milieu, particularly the tax treatment of capital gains on securities and reducing the differences in treatment between resident and non-resident investors. The owners and operators of capital markets in the region are aware of what constitutes best practice from an international perspective and are creating the institutions and policy frameworks required.

It should also be noted that, while further effort is needed in the region towards adequate supervision and regulation, no market in the world is totally free from abuse. The large number of cases lodged with and rulings made by the Securities and Exchange Commission in the United States in any one year is illustrative of the difficulties involved in operating capital markets. However, there is a good case to be made for the regulators and operators of the capital markets in the region to learn from each others' experience and to share information on cases of violations of rules of conduct.

Access conditions

Access to finance, beyond FDI in natural resources or tourism and very limited bank finance, has so far been confined in the region to a restricted number of countries, mainly in East and South-East Asia. These countries are likely to continue to have access to the increasingly rich variety of financial flows available. However, many of the other countries face the prospect of continued marginalization from international financial flows. Part of this is almost inevitable as it requires a good deal of sophistication in both the government regulatory authority and the financial community to either develop one's own capital markets to the stage of international acceptance, or to engage in trading on someone else's. For many of the least developed countries, the economies in transition and the Pacific island economies, the best prospect would appear to be to develop a sound and expanded banking system first and to make efforts to increase access to FDI and public debt. The increased mobilization of domestic savings through the domestic financial system, mainly the banks, would appear to be a prerequisite for expanding access to other forms of finance later on.

Official development assistance

Outside East and South-East Asia, much of the rest of the region remains dependent on ODA to a significant degree. In the 1990s, ODA for long-term development has decreased as disaster relief and peace-keeping operations have taken up a larger share, and there is increasing skepticism regarding ODA as an instrument for development. Moreover, for a number of such countries, government-backed export credit guarantees in the developed countries, which previously facilitated the import of capital goods (usually on a deferred-payment basis through suppliers' credits), have ceased to enjoy any form of public subsidy. These are, hence, either not forthcoming at all or, if available, at a drastically higher cost. As imports of capital goods often require such guarantees to be issued in the exporting country, this has serious implications for the ability of many countries in the region to maintain a sustained programme of capital goods imports. If current trends are projected into the next 5 to 10 years, the prospects for those countries of the region dependent on long-term ODA for their development needs or on export guarantees to finance capital equipment are quite bleak.

The problem is not only that a resource constraint will make it more difficult to sustain the process of economic reform, especially import liberalization, but that for many countries making the transition to acquiring finance on market-based criteria, the flow of ODA from bodies such as the World Bank is regarded as a seal of approval by private providers of finance. A diminution of ODA could have the perverse effect of reducing private finance as well.

Some level of ODA will, however, probably continue to be provided for the least developed countries, the Central Asian republics and the Pacific island economies. Nevertheless, there is likely to be increased conditionality attached to aid flows in terms of their uses and in terms of the socio-economic policies being pursued. For the others, there will inevitably have to be a transition towards private sources of finance and all that such a change entails in terms of the cost and availability of private finance.

Overall, therefore, prospects for the region are mixed. Those economies that have already succeeded in attracting significant volumes of FDI or have developed strong capital market institutions (and they remain few in number) will continue to attract private finance in a variety of forms and from a diversity of sources, combining it or substituting between its various components according to their requirements. At the same time, however, those countries that are still primarily dependent on ODA and/or are still in the process of developing their financial sectors, especially their capital markets, are likely to face a significant external resource constraint at the very time that they are striving to institute measures of trade and investment liberalization and thus need larger resources to meet a larger current account deficit than in the past. South Asian economies stand somewhere between these two stylized extremes. They may be able to attract increasing quantities of both FDI and portfolio flows, given their market size and relative institutional development. However, until there is evidence of more durable improvement in the macroeconomic fundamentals and greater investment in physical and market infrastructure, private financial flows, such as FDI and portfolio investments, are likely to remain restricted for these countries as well.

Challenges

Private financial flows have certainly brought benefits to the recipient countries. Moreover, it appears that developing countries will have to increasingly depend on them in the coming years, since ODA is not expected to be as easily available as in the past. Therefore, countries that have been less successful in securing private financial flows face the challenge of how to attract them. Countries that have been more successful in the past will have to compete to sustain these flows as well. All countries will have to learn to minimize the adverse consequences of such flows, especially of short-term flows, which can exhibit high volatility. The challenges to be faced can be grouped into four areas: (a) adapting or maintaining appropriate development policies; (b) developing viable financial markets; (c) dealing with the consequences of increased financial flows; and (d) promoting regional/sub-regional approaches to investment.

Implications for development policies

The sustainability of financial flows at the country level hinges directly on the need to implement or continue to implement sound macroeconomic policies. Macroeconomic stability is essential for attracting and retaining private financial flows because it gives confidence to foreign investors in a competitive rate of return on their investments and repatriation of profit and capital whenever they wish. Therefore, countries with serious problems of macroeconomic balances will have to deal with them on a priority basis in order to achieve more success in attracting foreign investment. Similarly, countries that have been more successful in securing foreign investment will have to struggle constantly to maintain the macroeconomic stability to sustain such flows. And yet, these flows themselves add to the difficulties in maintaining macroeconomic balance because of their unpredictable size and their rapid volatility. For example, the several ASEAN countries which have been the recipients of large capital inflows have had inflation rates below 5 per cent for a number of years. A slight increase in the inflation rate in these countries becomes a cause of great concern simply because they realize that a higher inflation rate will erode their competitiveness in the international market. However, some of these

countries have developed large current account deficits on the balance of payments which cannot be sustained over the long run. These countries realize this and have already started taking measures to contain their current account deficits. In sum, achieving and maintaining macroeconomic stability will remain a major challenge for all the developing countries in the region.

The question of sustainability of financial flows is also bound up with a range of complex development issues. In the first place, there is the question of absorptive capacity, with infrastructure and human resource skills being the most important considerations in enabling economies to translate investments into profits and into foreign exchange earnings. For the latter, export markets will need to be found and exploited. Sustainability thus requires that an individual economy become more competitive and better integrated into the multilateral trading system.

A major challenge lies in extending the advantages of integration to those economies in the region that remain poorly integrated. There are two subregions where the challenge is especially daunting: the Pacific island economies and the Central Asian republics. The former have physical limits to their absorptive capacity as they are very geographically dispersed, while the latter are still in the throes of the transition to, and are developing the institutions for, participation in the multilateral trading and financial systems. The ability of these two groups of countries to integrate is thus structurally constrained, for the present, at any rate. This leaves two important groups of economies in the region, South Asia and the least developed countries, where the process of integration has been relatively slow. Over the years, these economies have not been able to invest adequate resources to upgrade their physical infrastructures, traditionally a public sector preserve, because of budgetary constraints. For the same reason, public investment in the development of technical education and skills has been inadequate. Yet, without these, their attractiveness to private international investors will remain limited.

In the years ahead, developing countries will be under increasing pressure to liberalize their investment regimes further and to have more open policies towards private financial flows. As discussed above, countries have been using investment measures as a part of their broader development strategy and for balance-of-payments considerations. They will have to weigh the benefits and costs of more liberal policies. By keeping restrictive measures, countries cannot enjoy the full benefits of a more liberal regime. At the same time, if they open up their economies fully to private financial flows, this will probably require changes in the overall domestic economic policies for which they may not be prepared. They will lose the freedom to pursue independent macroeconomic policies and will have to pay more attention to the consistency of their policies with those of other countries as well as to the sentiments of private investors abroad. These countries will thus have to decide the appropriate speed for further liberalization of policy regimes related to foreign private financial flows. For example, after the Mexican peso crisis, some developing countries have been reconsidering the extent to which they should rely on the highly liquid investments that stock markets typically attract.

Development of financial markets

Adequate regulation and supervision of financial markets is very important for the growth and stability of non-FDI financial flows. Countries generally recognize that closer links with international markets require that domestic financial markets meet international standards. For this it is important to learn the complex functioning of financial markets of more advanced countries, for which highly skilled human resources are needed. Once domestic intermediating entities become involved in international capital market operations as participants, be they for equities, bonds or bank loans, along with their supporting paraphernalia of hedging, swaps, options and futures trading, good central banking supervision of international operations, supported by strong oversight institutions for trading in equities and bonds, is needed. This is important to maintain foreign investors' confidence and to minimize the chances of malpractice. Such institutional development needs to be further strengthened in practically all the countries of the region. Given their state of unpreparedness and scarce appropriately skilled human capital, the integration of the institutionally less developed

economies in the international financial markets and thus their access to certain types of foreign resources are therefore going to remain problematic for some time to come.

Developing countries will have to develop greater transparency in the operations of their businesses. Mandatory disclosure of reliable information about firms and financial intermediaries is required to enhance investor participation in equity markets. It is also needed to foster joint venture arrangements of various sorts. Foreign investors interested in making non-FDI investment in a particular country will be encouraged by the presence of institutions that can help them to provide reliable assessment about the performance of the enterprises of their choice. The existence of capable and trusted accounting firms that can certify the accuracy and authenticity of business accounts of the firms increases the investor's confidence. Allowing foreign firms in this field could improve the situation. Similarly, investors will be more willing to invest in corporate bonds if they have been rated for risk by reputable independent rating agencies. Countries will need to establish and strengthen such institutions to be more successful in attracting non-FDI financial flows.

Dealing with increased risks

One of the consequences of greater integration in the world's financial markets already witnessed in the last few years has been a visible increase in short-term volatility of financial flows, against which many governments of developing countries appear to stand powerless. It is argued that financial markets, often divorced from economic fundamentals and seemingly indifferent to the broader social responsibilities of governments, have created a new and complex dimension of policy for developing countries, viz. how to deal with short-term volatility and the tendency of markets to overshoot. Although it might be felt that this volatility is restricted to and affects only short-term investment flows into the stock and the bond markets, it can have an adverse impact on other financial flows including FDI as well through contagion effects and by generating an overall aura of uncertainty. Hence, uncertainty can have wide-ranging consequences. The concerns for those developing countries with significant capital markets revolve around three policy concerns: one, the sheer volume of foreign exchange and capital market transactions that often leave governments little leeway to influence exchange and interest rates; two, the huge array of financial instruments used for hedging purposes by the financial markets that have blunted the effectiveness of monetary and fiscal policies; and three, governments are often having to try harder to please financial markets and rating agencies.

Several countries in the region which have well developed financial sectors have recently experienced considerable volatility in short-term capital flows. Central banks in these countries have used open market operations to mop up excess liquidity created by these short-term capital flows. Central banks have also used other discretionary regulatory measures, including raising reserve requirements on the foreign liabilities of banks, putting a ceiling on their net external liability position and prohibiting the sale of monetary instruments of less than one-year maturity to non-residents as well as some administrative measures to limit the growth of short-term liabilities. Such measures have often resulted in unexpected costs to the central banks and to the economy as a whole.[32] However, no matter what measures are undertaken, this volatility of short-term capital will remain, and countries will have to learn to minimize its adverse consequences on their economies.

While countries of the region have primarily been guided in their liberalization of investment regimes by a desire to have a larger share of international private capital flows, greater attention needs to be paid to the composition and maturity structure of these flows. External flows dominated by short maturities can cause a serious liquidity crisis, even for countries with sound economic fundamentals. This is likely to become particularly important when a country attempts to finance its infrastructure projects through portfolio investments. These types of projects, in contrast with export-oriented FDI,

---

32 For example, in 1993 Malaysia received strong inflows of speculative capital in anticipation of gains from interest rate and exchange rate differentials, and Bank Negara Malaysia, in its efforts to stabilize the domestic money and foreign exchange markets, incurred significant losses. See Bank Negara Malaysia, *Annual Report 1993* (Kuala Lumpur, 1994), p. 38.

generally have long gestation periods and do not directly contribute to foreign exchange earnings. This aspect, combined with the observed higher volatility of portfolio equity investments in comparison with FDI, also indicates that a proper balance would be have to be struck between FDI and portfolio investments. Increased attention would also have to be paid to the basket of currencies in which these flows are denominated as an over-concentration in one currency could easily trigger a crisis if that currency suddenly appreciated in value relative to the domestic currency.

Many countries in the region prefer FDI to debt because, with the former, repayment is in the form of profits, and these only arise when the project succeeds. Moreover, there is no requirement of full value maintenance as in the case of debt. However, many, if not all, FDI projects also create certain financial obligations apart from the profits that the foreign investor will wish to remit to its parent company. FDI projects can create copyright, patent and royalty fees that can add up to a significant amount.[33] Thus, sustainability of repayment obligations can be quite large, and it puts a premium on FDI projects being successful in generating a sufficient flow of earnings to service the foreign exchange obligations that they will generate. Therefore, all the countries of the region will face the challenge of improving the efficiency of FDI.

Regional/subregional initiatives

The above challenges are couched in terms of individual economies, and perforce, will vary in significance and solution between the different economies of the region. There are some challenges, though, that may be best faced through the consolidation of efforts among countries, at least at the subregional level. For example, efforts are needed towards further developing the concept of single investment zones, such as is currently being done in the ASEAN Investment Area for other groupings of countries. There is, for instance, a good opportunity to develop such an area in the Mekong region, or in the Melanesian Spearhead Group of Pacific islands, or in East Asia. Single investment zones, however, are difficult as they require the standardization, or at least the harmonization, of many domestic policies in the fiscal and monetary area as well as in the trade regimes, and so they pose a considerable challenge to countries.

Another area for action is joint liberalization of trade in services, especially financial sector services, and the development of subregional institutions for trading in exchange rates, equities and bonds in different parts of the region. The former would facilitate subregional financial flows of various sorts and the latter are needed to overcome problems of thin and volatile markets which are not attractive to either international participants or domestic ones. Again, while some appreciation of these requirements may exist, the restrictions that they would put on domestic policy freedom and the necessity to think "regional" rather than "national" tend to limit the interest of policy makers at present.

The countries of the region will also have to face up to pressures to participate in negotiations on a multilateral investment arrangement, presumably under APEC or under WTO, and to be party to such an agreement. In doing so, they need to face up to the challenges of evolving a common position so as not to permit non-economic considerations from influencing the direction of financial flows, and of developing their own competition laws so as to counter the potential abuses of market power of both domestic firms and transnational corporations. These laws are becoming increasingly important as freedom to invest anywhere in the world grows.

* * *

With the increasing sophistication of financial engineering, many countries of the region will face the difficult challenge of developing sufficient expertise and robust financial institutions so as not to be overwhelmed by the vacillating interests of investors, and yet to attract the finance they need. The lagging countries will have to leapfrog their way into uncharted territory or risk being marginalized.

---

[33] Thailand's outward remittances for copyrights, patents, royalties and technical fees amounted to over $8 billion in 1995. See "How to protect that bright idea", *Bangkok Post*, 10 February 1997.

CHAPTER V

TRANSPORT AND COMMUNICATIONS

V

INTRODUCTION

An efficient transport and communication system is indispensable both for national development and for integration with global and regional economies. Internal and external transport and communication links facilitate movements of goods, services and production factors, enabling producers to produce at low-cost locations nationally and internationally and to exploit the advantages of economies of scale and scope. An efficient transportation and communication system reduces the cost of distribution and thus helps to expand internal and external markets. Economic growth, participation in international trade and capacity to attract FDI may be seriously constrained in a country with inadequate expansion in coverage or poor quality of the transport and communication facilities.

The growth of intraregional and interregional transport and communication linkages permits economies to share and develop geographical and economic complementarities for mutual benefit. Historically, developments in transport and communications have been crucial in opening opportunities for mass production and market expansion to spread the impulse of industrialization globally. In order for countries to compete in the global market place, they must raise the efficiency and quality of their transport and communication infrastructure and services. The efficiency of infrastructural services, in which transport and communications play a very important role, is a major consideration in the decisions of transnational corporations with regard to investment location. The participation of developing countries in the globalization process thus crucially depends on the efficiency and reliability of their transport and communication services.

The developing countries of the ESCAP region have made substantial investments to develop their national transport and communication systems. This has included the expansion and improvement not only of various transport and communication infrastructures but also of service facilities by utilizing available modern technologies. Modern technologies are increasingly being used, particularly in the telecommunications sector. In transport, the priorities attached to the development of roads, railways, inland waterways, and coastal and ocean shipping have varied from country to country. Most countries, however, seem to have placed more importance on the expansion of the road system as the principal means of land transportation, though the advantages of railways as a means of bulk transportation have not been overlooked. Recent improvements in railway technologies, which have enhanced the fuel efficiency, speed and environmental advantages of the railway, particularly through electrification, have made railway transport a more viable alternative.

Despite many achievements over the years, serious lags still remain in the development of the transport and communication sectors of the developing countries in the region. The rapidly growing economies of the region are currently facing rising demand for infrastructure with which supply has not been keeping up. Congestion and bottlenecks have emerged as serious problems in many countries. The public sector, which has traditionally undertaken most of the investment in the transport and communication infrastructure and managed and operated systems, has been facing financial and managerial problems limiting its ability to undertake further expansion and efficient operation. Countries will nevertheless continue to face rising demand for infrastructure to be able to sustain or further expand their economic and commercial activities. The limitations on the financial and managerial capacity of the public sector have been affecting the quantity, quality, timeliness and cost-effectiveness of the services that are provided. Countries of the region have therefore increasingly been turning to collaboration with the private sector to assist in the process of developing the infrastructure facilities and services.

A review of the trends in transport and communications in the region and of future needs and prospects for the purposes of national development is undertaken in this chapter.

DEVELOPMENTS IN NATIONAL TRANSPORT AND COMMUNICATIONS

Transport

Road transport

The establishment of a national road network provides the easiest channel through which production can be moved to markets. Most countries have therefore looked upon the development of a reliable road network as a crucial requirement for long-term economic growth. Road transport has thus been emerging as the predominant mode of transport for both passengers and freight within the ESCAP region. In many economies in the region, the share of road transport in freight movement exceeds 50 per cent. In passenger movement, however, the share of road transport is generally less than that of rail transport.

The current stock of roads in the ESCAP region has been estimated at about 6 million km, of which motorway and national highway networks account for approximately 1 million km. Significant expansion in the road network has taken place in countries such as Bangladesh, Brunei Darussalam, Indonesia, Malaysia, Nepal and Pakistan over the past decade. The length of the road network has increased at an average annual rate in excess of 4 per cent per year in these countries. Road density[1] within the region suggests, however, that wide variations exist among countries in national road infrastructure development. Hong Kong and Singapore have the highest densities reflecting both their small geographical size and their more advanced development status. In large countries, not only size but also varied topography influences the extent and density of roads. Larger countries can thus be expected to have lower road densities but some of the relatively small countries, such as the Lao People's Democratic Republic, Myanmar and Nepal have the lowest density of road networks, reflecting both their topographic problems and their relatively low stage of economic development (table V.1).

Table V.1. Road network density in selected ESCAP member countries or areas

	Year	*Km road length per sq km*
Singapore	1994	4.78
Hong Kong	1994	1.60
Republic of Korea	1994	0.73
Samoa	1989	0.73
Tuvalu	1989	0.58
India	1992	0.56
Philippines	1991	0.54
Brunei Darussalam	1993	0.42
Sri Lanka	1993	0.40
Viet Nam	1992	0.32
Azerbaijan	1994	0.28
Armenia	1994	0.26
Pakistan	1993	0.23
Malaysia	1993	0.18
Indonesia	1991	0.16
Vanuatu	1988	0.12
Thailand	1994	0.12
China	1994	0.12
Uzbekistan	1994	0.10
Bangladesh	1990	0.10
Kyrgzstan	1994	0.09
Tajikistan	1994	0.09
Nepal	1991	0.06
Lao People's Democratic Republic	1993	0.06
Papua New Guinea	1989	0.05
Kazakstan	1994	0.03
Turkmenistan	1994	0.03
Mongolia	1992	–

Source: ESCAP, *Review of Developments in Transport, Communications and Tourism in the ESCAP Region, 1995* (ST/ESCAP/1620), p. 34.

The share of paved roads, which is indicative of the quality of the various national road networks, also suggests wide variations. Upgrading roads and maintaining them properly are as important as extending the length of the network. The upgrading of unpaved surfaces and proper maintenance will ensure quality of road services in terms of increased average speed, better safety and reduced transportation costs. Many countries still have major proportions of their road network unpaved. In China, the Lao People's Democratic Republic, Mongolia and Myanmar, a third or less of the stock of road is paved. Indonesia, Malaysia, Pakistan and

[1] The measure of road density used is road length per sq km of land area.

the Republic of Korea have achieved substantial improvements in road quality by expanding paved length at a rate of more than 6 per cent a year over the past decade.

Despite the importance of the road sector, many of the region's roads are poorly managed and suffer from large backlogs of deferred maintenance. While during the past several years many countries have attempted to address the issue of road maintenance, sufficient importance has not been given to the subject in the ESCAP region.

The growth in the number of motorized road vehicles has been spectacular in most countries. Such vehicles, by and large, have displaced the slow-moving, mostly animal-driven transport vehicles. In fact, the growth in vehicle numbers and varieties has outpaced the growth in road space, creating the now common scenes of crowding and congestion, especially in urban and suburban areas in the region. The total number of registered vehicles in the region in 1994 (excluding the Central Asian republics) was more than 150 million and this figure is growing at the rate of 3 to 4 per cent annually. The number of vehicles has increased most rapidly in China, India, the Republic of Korea and Thailand. Rising per capita incomes, expansion of economic activities and the relaxation of import restrictions in many countries have contributed to the growth in vehicle fleets. In Hong Kong, the Republic of Korea and Singapore, passenger cars account for more than 50 per cent of the total number of cars. Other countries have more complex mixtures of four-wheeler passenger cars, commercial vehicles and two- and three-wheeler passenger carriers.

The rise in the total number of registered motor vehicles also reflects the growth of local assembly and production plants by both domestic and foreign manufacturers in countries as diverse as China, India, Malaysia, the Republic of Korea and Thailand. The growth of registered vehicles largely reflects the rise of first-time motor vehicle purchases in the developing countries. This stands in contrast to the saturation of the vehicle market and the predominance of replacement purchases in many developed countries, including Australia, Japan and New Zealand in the ESCAP region.

The rising number of motor vehicles in most countries in the region has given rise to a number of concerns. These include congestion and environmental pollution, particularly in urban areas. In Thailand, for example, road traffic congestion has contributed to significant cost increases in extra fuel burnt and time lost, and has lowered air quality in Bangkok. A similar situation is arising in many other major urban centres in the region.

Rail transport

The expansion in railway route length in the region has been slower than the expansion in road length. This is because road rather than railway construction has received more emphasis in national development plans, reflecting considerations of comparative advantage of the two alternative systems, but also because of the initial existence of sizeable lengths of railway track in many countries and the virtual non-existence of motorworthy roads. Between 1986 and 1994, the combined length of the railway networks in the region increased from about 246,100 route-km to 248,700 route-km, an average annual rate of growth of only 1.1 per cent (table V.2). The developing countries, however, have added a little more to their existing railway track. This is reflected in a higher growth rate of 2.1 per cent between 1986 and 1994.

China has undertaken the largest new railway construction in the region. India, the Islamic Republic of Iran and Myanmar have also extended their railway networks. The three developed countries of the region have reduced their route length by almost 2 per cent by closing loss-making segments.

Maintenance and technological upgrading rather than track expansion have been emphasized in railway development in most countries and railway route electrification has made strong headway in most countries. China added 4,556 km of electrified track to its railway network and, in the process, doubled the share of electrified route from 8.4 per cent of the total track route to 16.5 per cent over the period from 1986 to 1994. India, during the same period, increased the share of electrified route in its railway network from 10.5 to 18.5 per cent. However, almost one third of the total electrified route length in the ESCAP region is located in the three developed countries in the ESCAP region.

The trends in railway passenger and freight traffic are mixed. Just under half of the 24 railway systems for which data are available experienced a

Table V.2. Growth of railway route length in the ESCAP region, 1986 and 1994

(Thousands of kms)

	1986	*1994*	*Percentage increase*
ESCAP region	246.1	248.7	1.1
ESCAP developing countries	183.4	187.2	2.1
Central Asia	79.6	80.7	1.4
South Asia	22.7	22.8	0.4
East Asia	62.1	64.0	3.1
South-East Asia	19.0	19.7	3.7
ESCAP developed countries	62.7	61.5	−1.9

Source: ESCAP, *Review of Developments in Transport, Communications and Tourism in the ESCAP Region, 1995* (ST/ESCAP/1620), p. 23.

decline in the volume of passenger traffic (measured in terms of passenger-km) during the period 1986-1994. In Viet Nam, the decline in passenger traffic of more than 10 per cent per year was largely influenced by the deteriorating state of the track and bridges on the Hanoi-Ho Chi Minh City trunk line, resulting in the imposition of speed restrictions and the loss of traffic to road transport. Of the 14 countries that increased their passenger traffic, China, Indonesia, the Islamic Republic of Iran, Myanmar and Thailand had passenger traffic growth of more than 4 per cent per year.

Freight traffic (measured in net tonne-km), on the other hand, grew for most countries in the region. As in the case of passenger traffic, the fastest rate of growth in rail freight traffic was achieved by Indonesia and the Islamic Republic of Iran at more than 8 per cent each year during the period 1986-1994. Although rail freight traffic increased in most countries, it appears that the rate of increase failed to keep pace with growth in GDP, suggesting a possible loss of market share to other transport modes, especially road transport. Among the handful of countries that experienced a sustained reduction in railway freight traffic, Mongolia stands out. The annual 12.6 per cent decline in freight traffic per year on Mongolian Railways largely reflects the reduction in traffic to and from the Russian Federation following the dissolution of the former Union of Soviet Socialist Republics in 1991. The Russian Federation and the Central Asian republics also experienced significant freight traffic reductions on their railways for similar reasons.

Inland water transport

The ESCAP region has a combined river basin of over 19,106 sq km. For the millions of inhabitants of these riverine areas, inland water transport is a traditional means of transportation. It plays a vital role in the economic development of remote rural areas and the welfare of the people who live there and who are generally less well off. These underprivileged communities would often be inaccessible or too costly to service by other means. However, in the last two decades, most countries in the ESCAP region have emphasized the development of speedier modes of transport, such as roads and railways, with the result that there has been relative underinvestment in inland water transport.

In addition, the large extraction of water to meet the spiralling needs of irrigation and other uses, the deforestation of river basins leading to erosion and siltation and the lack of sustained effort to maintain and improve waterways have gradually reduced navigability. These factors, together with the lack of a coordinated and integrated approach to overall transport development, have contributed to the gradual decline in the condition of inland water transport infrastructure and the standard of inland water transport services in the ESCAP region, even in countries where inland water transport is extensively used.

The present level of inland water transport usage varies widely throughout the ESCAP region. In Bangladesh, Cambodia, the Lao People's Democratic Republic, Myanmar, Thailand and Viet Nam, it accounts for between 18 and 44 per cent of the national freight transport while in China, India,

Indonesia and Malaysia it represents only 3 to 10 per cent of the total tonne-km of the freight transport sector.

Cargo container traffic has been growing in importance in the region. The carriage of containers by inland waterways in the region is in its nascent stage and can expand considerably. The inland waterways of China carry an estimated container volume of 300,000 20-ft equivalent units (TEUs) annually, a volume that is comparable with that of some European countries that make extensive use of inland water transport. By contrast, in India and Thailand, the volumes carried by container on inland water ways are 6,300 and 3,000 TEUs respectively. The other riverine countries of the region have very little and irregular movement of containers by inland water transport.

Air transport

The ESCAP region has witnessed the fastest growth in air traffic in the world, measured in number of flights, number of passengers and volume of cargo carried. Between 1982 and 1992, the region's scheduled airline passenger traffic, measured in passenger-km, grew at an average annual rate of 8.1 per cent while the corresponding global traffic grew at the average annual rate of about 5.6 per cent. In 1992, the region recorded 406.7 billion scheduled air passenger-km. The region is set to overtake Europe to become, after North America, the second largest market for airline passengers in the world.

Forecasts of the future trend in air passenger traffic suggest that, by the year 2003, the region will account for nearly 29 per cent of the world's scheduled air passenger traffic, compared with 21 per cent in 1992. Air passenger traffic in the region is expected to grow by an average of 8.3 per cent per year up to the year 2003, compared with the forecast growth rate of 5.2 per cent for the world.

During the period 1982-1992, the rate of growth of air cargo traffic, measured in tonne-km, averaged 10.2 per cent a year, well above the annual rates of 7.1 per cent for the world and 6.8 per cent for North America. In 1992, the air cargo traffic within the Asian and Pacific region reached 18,430 million tonne-km, second only to the level of air cargo traffic within Europe of 19,830 million tonne-km. In 1993, air cargo traffic in the Asian and Pacific region grew by another 20 per cent. The countries in the region with the fastest growth in air cargo included Malaysia, the Republic of Korea, Singapore and Thailand.

Air cargo traffic in the Asian and Pacific region is forecast to grow at an annual rate averaging 9.3 per cent during the period 1992-2003 as against a 6.6 per cent growth forecast for the world. As a consequence, the region's share of worldwide air cargo traffic will increase from 29.7 per cent in 1992 to 39.2 per cent in 2003.

Shipping and ports

International trade in merchandise depends overwhelmingly on ocean shipping and its corresponding port facilities. In the 1950s and 1960s, developing countries in the region operated with virtually no merchant fleet of their own. Port facilities were also grossly inadequate. The growing participation of countries in international trade has required expansion and upgrading of both shipping and port facilities.

Shipping capacities have grown in most countries over the past few decades and many developing countries now have their own national shipping lines. During the period 1985 to 1995, the merchant fleet capacity of developing countries in the ESCAP region grew at a rate of 4.3 per cent per annum, which was higher than the 1.7 per cent world capacity growth (table V.3). In 1995, the developing countries of the ESCAP region, including Turkey, had a share of 17.2 per cent of the world total tonnage capacity of 490.7 million. These figures had risen from 13.2 per cent and 416.3 million tons in 1985. The total tonnage share of the ESCAP region as a whole decreased by 1.4 percentage point from 23.4 per cent of the world total to 22 per cent in 1995. This reflected the continued decrease in Japanese-owned fleets from 39.9 million gross tons in 1985 to 19.9 million gross tons in 1995.

Over the last two to three decades, some major interlinked issues of concern to developing countries in international shipping have been participation of national lines in the carriage of their own foreign trade, liner conferences and the development of mainline and feeder route structures by the large international consortia. The issue of participation of national lines was addressed in the United Nations Liner Code, which was adopted in April 1974 and came into force in October 1983. Under the code, the national lines of the two countries served had equal rights to participate in a

Table V.3. Growth of merchant fleets in the ESCAP region, 1985-1995*

(Thousands of gross tons, as of 31 December)

	1985[a]	1993	1994	1995	Percentage change per annum[b] 1985-1995	1994-1995
Developing countries or areas	**54 971**	**76 656**	**80 154**	**84 666**	**4.4**	**5.6**
Bangladesh	358	388	380	379	0.6	-0.2
Brunei Darussalam	1	365	366	366	77.2	0.1
Cambodia	4	6	6	60	32.5	934.5
China	10 568	14 945	15 827	16 943	4.8	7.1
Democratic People's Republic of Korea		671	696	715		2.7
Fiji	31	39	31	32	0.4	2.2
Hong Kong	6 858	7 664	7 703	8 795	2.5	14.2
India	6 605	6 575	6 485	7 127	0.8	9.9
Indonesia	1 936	2 441	2 678	2 771	3.6	3.4
Iran (Islamic Republic of)	2 380	4 444	3 803	2 902	2.0	-23.7
Kiribati	2	5	5	6	11.8	18.5
Lao People's Democratic Republic		3	3	3		0.0
Malaysia	1 773	2 166	2 728	3 283	6.4	20.4
Maldives	133	55	68	85	-4.5	24.4
Myanmar	117	711	683	523	16.2	-23.5
Nauru	67	1				
Pakistan	451	360	375	398	-1.2	6.1
Papua New Guinea	29	48	47	49	5.5	4.7
Philippines	4 594	8 466	9 413	8 744	6.6	-7.1
Republic of Korea	7 169	7 047	7 004	6 972	-0.3	-0.5
Samoa	26	6	6	6	-13.2	0.0
Singapore	6 505	11 035	11 895	13 611	7.7	14.4
Solomon Islands	6	7	8	8	3.3	0.0
Sri Lanka	635	294	294	227	-9.8	-22.8
Thailand	586	1 117	1 374	1 743	11.5	26.9
Tonga	17	11	1	12	-3.8	972.7
Turkey	3 684	5 044	5 453	6 268	5.5	14.9
Tuvalu	1	70	51	64	62.5	25.1
Vanuatu	138	1 946	1 998	1 874	29.8	-6.2
Viet Nam	299	728	773	700	8.9	-9.4
Developed countries	**42 324**	**27 327**	**25 360**	**23 194**	**-5.8**	**-8.5**
Australia	2 088	2 862	3 012	2 884	3.3	-4.3
Japan	39 940	24 248	22 102	19 913	-6.7	-9.9
New Zealand	296	218	246	397	3.0	61.2
ESCAP region total	**97 296**	**103 983**	**105 515**	**107 860**	**1.0**	**2.2**
World total	**416 269**	**457 915**	**475 895**	**490 662**	**1.7**	**3.1**
Developing ESCAP region/world	13.2	16.7	16.8	17.3	..	..
ESCAP region/world	23.4	22.7	22.2	22.0	..	..

Source: Lloyd's Register of Shipping, *Statistical Tables 1985* and *World Fleet Statistics*, various issues.

* Including merchant ships of 100 tonnes gross and above, excluding wooden and non-propelled craft.

[a] Data for 1985 as at 30 June.

[b] Reflecting compounded annual growth for the period 1985-1995.

liner conference trade while third countries were entitled to a significant share "such as 20 per cent". This provision subsequently came to be known as the 40/40/20 rule. The new mood of private sector participation and the adoption of free market principles which began to emerge in the late 1980s has however largely overtaken the Liner Code with many countries dismantling cargo reservation provisions in their own trade. The liner conference system as an institution has also been in a state of decline over the past two decades basically for the failure of the conferences to meet the objectives and aspirations of their members.

Another major issue of concern to developing countries, which emerged in the late 1970s and early 1980s, was a change in operating practices and route structures of the large international consortia. Prior to the advent of the container, the major ports of most countries received direct calls from vessels operating on the major trade routes. Following the introduction of the container, the consortia commenced deploying large mainline vessels on routes which only called at a small number of large transhipment ports, with services being provided to neighbouring countries by smaller feeder vessels. This practice raised two issues. Firstly, the issue of participation in international shipping by countries which had been relegated to feeder status and secondly, the issue concerning the type and size of container port facilities which the feeder ports should provide. The rapid growth in the liner trades of many ESCAP member countries has, however, contributed towards reducing the level of concern with these operating practices. The ports of Thailand, for example, at the beginning of these changes were relegated to feeder status on not only the European and North American trades but also in the trades to East Asia. With the growth in Thailand's container trade and the building of the deep-sea port of Laem Chabang, direct services are now available to most of the country's East Asian and some of the North American trade. Before the year 2000 it is likely that direct services to Europe will also become available.

A significant recent development in the liner shipping sector is the formation of global alliances between major container shipping lines, with names such as the Grand Alliance and the Global Alliance. The major reason for the formation of these alliances is to improve operational efficiency and logistics services globally to key customers without the constraints of rigid route specifications that liner conferences used to lay down. The shipping lines within these alliances, *inter alia*, cooperate to provide common terminals or terminal contracts; joint feeder services; joint purchase of containers; joint purchase or ownership of ships; interchange of empty containers; jointly managed pools of containers; joint intermodal, rail or trucking operations; joint container depots; and to a degree, joint EDI systems.

During the period 1985 to 1993, the cargo throughput of the region's ports grew very rapidly. The total cargo loaded and unloaded in the ESCAP region in 1994 was 2,596 million tons which accounted for 28.7 per cent of the world total of 9,058 million tons. The developing countries of the region handled 1,401 million tons of sea borne cargoes representing 15.5 per cent of the world total. The use of mechanization and containerization and the increasing commercial orientation of port operations have contributed to an expansion in their cargo-handling capacities. Ports in Hong Kong, Indonesia, the Islamic Republic of Iran, Malaysia, Myanmar, the Republic of Korea, Singapore and Viet Nam have reported significant growth in cargo traffic exceeding 10 per cent per year over the period. To keep pace with this growth, many countries in the region have planned major investments to expand their port infrastructure. Container traffic for the region has been rising fast to account for half of the total world container throughput by 1996. The developing countries of the region accounted for 35.6 per cent of the world total of container traffic in 1993.

Multimodal transport

The expansion of both the internal and the external trade of the region's developing countries has been placing a growing demand on the systems and procedures whereby the whole transport chain is managed. In this respect, the advantages of multimodal transport are now widely recognized. The development of free trade areas, economic zones and growth triangles which straddle country borders has further pressed home the urgency of the establishment of a freer environment for transport operations. The importance of multimodal transport is thus widely acknowledged, but institutional constraints still limit its application in many countries. Multimodal transport covering air, land and sea transport places the responsibility for these activities on one operator, who then manages and coordinates the total task from the shipper's door to the consignee's door, ensuring the continuous movement of goods along the best route and by the most efficient and cost-effective means.

Documentary and procedural requirements are being amended to allow containers to move more rapidly through seaport terminals to their hinterlands. Customs authorities are developing computerized systems in most of the developing countries. Once these can be linked into shipping and trading community networks, the potential for greatly increased efficiency through the use of modern information technology may be realized.

Governments are also reviewing existing bilateral agreements for cross-border traffic and considering the adoption of international conventions relating to the movement of containers, goods and vehicles. Countries are also addressing the need for more effective transport connections to inland locations by providing inland container depots (ICDs) with appropriate handling equipment to transfer containers from one mode of transport to another and both on and off-site container freight stations (CFSs) to enable multimodal transport operators (MTOs)/ forwarders to consolidate/break cargoes of individual shippers. The introduction of block container trains between various inland locations and ports, with road links over short distances of the ICDs to satellite CFSs, is greatly facilitating efficient door-to-door transport.

Several freight forwarding and shipping companies now meet the need for increased efficiency of transport services to enable the traders of the region to remain competitive in world markets and facilitate growing trade with their regional neighbours. They have adapted or are in the process of adapting their operations to provide full multimodal transport services. However, in some countries, the progress towards the introduction of full door-to-door transport has been slow, owing to inadequate road access to premises, restrictive regulations and cumbersome clearance procedures. The need for appropriate regulatory environment for multimodal operations is however being increasingly recognized. Some countries are in the process of enacting multimodal transport legislations, in line with international conventions and the UNCTAD/ICC Rules for Multimodal Transport.

Freight forwarding associations are also assisting the development of multimodal transport by establishing criteria and standards of operation and performance. Association members are encouraged to apply for registration as multimodal transport operators authorized to issue the International Federation of Freight Forwarders Associations multimodal transport Bill of Lading and to accept responsibility and liability for the total transport operation. The growing acceptance by banks of that Bill of Lading is assisting the process.

Telecommunications

Telecommunications technology has evolved rapidly over the past decades making it possible to establish and expand faster, cheaper and more reliable lines of communications nationally and internationally. The countries of the region have adopted digital electronic systems controlled by computer processors, which are able to provide more reliable, high-quality service, with a wider range of service options. The change from electromechanical and semi-electronic switching systems has thus tremendously improved the quality of telecommunication services.

On the transmission side, digital microwave radio systems and optical fibre cables have dramatically increased system capacity, reliability and quality, and reduced the unit cost of transmission. A very high percentage of traffic is now carried in the form of facsimile and data transmissions for commerce and industry.

One significant development is the introduction and rapid acceptance throughout the region of the Internet. This system has been facilitated by the rapid upgrading and expansion of telecommunications infrastructure, as well as the application of state-of-the-art technologies for routing data communication within the region. The focus of Internet system application has now shifted from the academic and research world to business.

Fixed telephone network

Between 1984 and 1994, the number of installed telephone main lines in the region grew by 7.6 per cent per year, roughly comparable with the region's rate of growth of GDP over the same period. Over this period, the region's telephone density increased from 2.8 to 4.9 telephone main lines per 100 head of population. The telephone networks of the region's developing countries grew nearly twice as fast as the region as a whole. This almost trebled telephone density for the developing countries from 0.98 to 2.9 main lines per 100 head of population.

The strongest growth took place in the East Asian subregion where the number of telephone main lines increased from 14,630,000 to 59,160,000. China's 26.4 per cent growth per year accounted for most of the increase. With an estimated 28.8 million telephone main lines installed by the end of 1994, China achieved a telephone density of 2.42 main lines per 100 head of population.

South-East Asia achieved the second fastest rate of growth in telephone installations within the region, with an average annual rate of increase of 12.1 per cent in the period 1984-1994. Within this subregion, the fastest growth was recorded by Viet Nam (with 20.2 per cent a year, albeit from a very low base), and Indonesia and Thailand (each with 16.7 per cent a year).

South Asia's telephone coverage was poor, with 1.17 telephone main lines per 100 head of population in 1994. The number of telephone main lines in this subregion increased by an annual average of 12.1 per cent, from 4.8 million main lines in 1984 to 15 million in 1994. However, only the Islamic Republic of Iran (with 6.57 main lines per 100 persons) and Maldives (with 5.95 main lines per 100 persons) had telephone densities that were above the average for the region's developing countries. Densities in other countries were far below that average.

Mobile telephone services

The adoption of cellular telephone technology in the region has advanced rapidly over the past three to four years. In 1994, there were about 9.2 million cellular telephone subscribers in the region. More than one third of them were located in East Asia. The number of subscribers in the region grew at an average 78.2 per cent a year between 1990 and 1994, more than 10 times higher than the growth rate for the fixed line network. The fastest annual rates of growth in the number of cellular telephone subscribers were in China (203.6 per cent), Sri Lanka (133.5 per cent) and Thailand (107.7 per cent).

The spectacular growth of cellular telephones in the developing countries owes much to the growing affluence of a large segment of the population of the region. Young and affluent consumers, captivated by the latest electronic gadgetry, are spurring new demand not only for cellular telephones, but for other mobile technologies such as radio-paging, mobile data and public access cordless telephone (CT2) systems. The demand for cellular telephones has been influenced by other factors such as the underdeveloped state of the fixed line network. Long waiting times for connection have compelled users to seek substitutes in the form of mobile cellular telephones.

Cambodia provides the most striking example of a country where subscribers have been forced to adopt cellular telephones because of deficiencies in the conventional network. The wireline network in the country was devastated by 20 years of civil war and, even now, in some parts of the country, the presence of landmines has made it dangerous to lay cables. Starting in 1992, the Ministry of Posts and Telecommunications established four cellular joint ventures with foreign partners and, by the beginning of 1995, these joint ventures had some 13,500 subscribers, so that the ratio of cellular to fixed line subscribers is now about 2 to 1. In Thailand, that ratio currently stands at 0.5 to 1. The traffic gridlock within Bangkok has been an important factor in the rapid growth of cellular phone acquisitions.

Telecommunications traffic

ITU estimated that the international call traffic of the region increased from 870 million minutes in 1984 to 7.5 billion minutes in 1994. With a growth rate of 23.4 per cent per year in traffic, the region's share of global international traffic rose from 7 to 15 per cent during the course of a decade. It is estimated that about 59 per cent of the international call traffic originating in the region is attributable to intraregional calls.

Outgoing international call traffic of the developing countries, however, also grew rapidly during the period. Starting from a base of 480 million minutes in 1984, traffic volume grew at roughly 27 per cent per year to 1994. The developing countries of the region accounted for more than two thirds of the total international calls in 1994 compared with just over half in 1984, the rest of it being accounted for by Australia, Japan and New Zealand.

Emerging needs and current efforts

In the face of rising demand for transport and communication services, most governments have embarked upon plans to expand and upgrade the infrastructure and services across all modes of transport.

Easing of urban transport congestion has been a priority area for further investment. Within the

region, 48 major urban public transport investment projects, valued at an estimated $75 billion, will either be in progress or planned for commencement during the period 1995-2000. An estimated $34 billion is committed to the extension of 14 existing mass rapid transit railway or metropolitan railway systems; some $25 billion is committed to the construction of 13 new systems. More than three-quarters of the estimated total investment in urban transport systems in the region is meant for urban public transport system development in East Asia. Nearly 41 per cent will be accounted for by the construction of three new metropolitan railway systems and the extension of two existing ones in the Republic of Korea alone.

Economic expansion and growing private vehicle ownership have been placing pressure on the road networks in most countries, leading to emphasis on the expansion and upgrading of the network. Indications of the major road and highway projects that are being built, or will be undertaken, in selected countries in the ESCAP region in the near future are summarized in table V.4.

Major railway development projects, valued at more than $100 billion, are planned for implementation in the region by the year 2000. China and India together account for more than half of the estimated value. The estimate is conservative and does not include, for example, the gauge conversion project in India. India plans to complete the conversion of an additional 7,000 route-km from metre to broad gauge by 2000. Even the $100 billion estimate serves to illustrate the magnitude of investment that is expected to be committed to individual major railway development projects up to the end of the century (table V.5).

A number of development projects and initiatives aimed at improving inland water transport infrastructure and operations are also under way throughout the region. Both economic and environmental considerations justify inland water transport developments in the region. Inland water transport has been found to be the most energy-efficient of the transport modes.[2] Many countries of the region need an efficient inland water transport system to serve remote or low-income areas.

In order to accommodate the rapid expansion in air passenger and cargo traffic, major efforts have been exerted to develop airports and related infrastructure. Available information indicates that some 73 major airport development projects, costing more than $40 billion, are under way or will commence during the five-year period from 1995 to 2000. More than 80 per cent of this planned investment will involve the construction of new airports. The balance of investment is earmarked for capacity expansion, in the form of passenger and freight terminal expansion, runway extension and duplication, and the installation of more advanced air traffic control and communications systems.

Nearly two thirds of the estimated investment is expected to take place in East Asia. China will account for roughly 50 per cent of air transport investment largely because of investments for the updating of outmoded navigational and landing aids, as well as for runway extensions to handle larger wide-bodied aircraft at many secondary international airports.

Among the major airport development projects planned or under construction are the new Chek Lap Kok Airport for Hong Kong with an estimated cost of $6,460 million (excluding the cost of a linking bridge costing $1,820 million and a 34-km mass transit railway costing $4,360 million); the new Kuala Lumpur International Airport at Sepang with an estimated cost of $5 billion (including the cost of a road and high-speed railway link); the second Bangkok International Airport at Nong Ngu Hao with an estimated ultimate cost of $4,960 million or an expansion of the Bangkok International Airport; the new Seoul Metropolitan International Airport with an estimated cost of $4,250 million; and the new Macau International Airport with an estimated cost of $912 million.

One concern is that the additional capacity being developed by some of these projects may prove inadequate by the time they come into service. The new Hong Kong International Airport is frequently quoted as a case in point. There are differing views about the level of investment which will be required by the year 2010 to relieve the serious airport congestion in the region. ICAO has forecast a requirement of $70-100 billion for airport

[2] In Europe, recent research has shown that energy consumption for the transportation of goods by the various modes is as follows: for inland waterway navigation, 10 kwh/100 tonne-km; for rail transport, 15 kwh/100 tonne-km; for road transport, 29 kwh/100 tonne-km; and for air transport, 360 kwh/100 tonne-km. See Permanent International Association of Navigation Congresses, *Bulletin No.64*, 1989.

Table V.4. A selection of road network development plans and projects in selected ESCAP member countries

Country/area	*Estimated cost*	*Development/project plans*
Afghanistan	$2 million	Construction of transit route from Ashkhabad, Turkmenistan, to Chaman-Quetta, Pakistan, through Torghundi, Herat and Kandahar.
Bangladesh	$156,250,000	To build 1,330 km of regional highways and feeder roads. Scheduled for completion in 2001.
	$252.4 million	Second road rehabilitation and maintenance project to rehabilitate national highways, widen narrow roads and overlay a total of 1,800 km in a four-year period.
	$600 million	Construction of 4.8-km multi-purpose, four-lane, 47-span Jamuna Bridge, scheduled for completion in 1997. ODA is funding the second phase of the four-year bridge improvement and maintenance project.
Cambodia	$85 million	First phase of emergency road recovery programme, 1,000 km of asphalted national roads will be rehabilitated.
	$21 million	A road construction centre will be constructed with aid from Japan.
	$8 million	A replacement programme for bridges.
	$18 million	Ferry facilities to be rehabilitated.
Hong Kong	$925 million	2.16 km-long Tsing Ma suspension bridge to be completed by mid-1997.
India	$245 million	ADB loan to improve five national highway sections totalling 333 km in Andhra Pradesh, Bihar, Haryana, Rajasthan and West Bengal. Completion scheduled for 1998.
Indonesia	$2 740 million	Construction of 770 km of toll roads. Scheduled completion between 2000 and 2004.
Kazakstan	–	Danish Road Directorate to prepare a road sector survey of Kazakstan.
Lao People's Democratic Republic		The Government has prioritized the building of the road network in its development plan. By 2000, it is expected that 50 per cent of the public investment budget will be devoted to road network investment.
Mongolia	$427 million	Implementation of the Mongolian road master plan and feasibility study, funded by ADB and incorporating the Asian Highway and Tumen River projects, would involve construction of a network of 5,362 km. Transport rehabilitation project, funded by a loan credit from the World Bank.
Pakistan	$500 million	Construction of bypass roads and flyovers in Karachi to ease congestion and to connect the port to the superhighway via Mauripur.
Philippines		The 19-km six-lane elevated Manila South Tollway from Manila to Muntinlupa will be completed in 1999 under a BOT scheme.
Republic of Korea	$9.5 billion	Expressway construction or widening in the Seoul metropolitan area.
Sri Lanka	$57 million	Loan and technical assistance grants from ADB for the third road improvement project.
Thailand	–	The Government, ADB and the Overseas Economic Cooperation Fund of Japan are financing the Outer Ring Road, the Bangkok-Chonburi Highway, and the Rangsit-Saraburi Highway. Preparation of detailed engineering design and tender documents for toll motorway TM-3 between Pattaya and Mabtaput, with financing from the ADB fifth highway sector loan.
Viet Nam	–	The State Planning Committee to evaluate 134 bridges on a 300-km stretch of National Highway 1 between Hanoi and Ho Chi Minh City, and to link the highway to those of neighbouring countries. Technical support and consultancy for the project funded by ODA.

Source: Based on ESCAP, *Review of Developments in Transport, Communications and Tourism in the ESCAP Region, 1996* (ST/ESCAP/1620), pp. 37-40.

Table V.5. Major railway infrastructure development projects, 1995-2000

Country or area/ project description	*Estimated cost (millions of US dollars)*	*Schedule*
India: various capital works, including electrification of 500 km, re-gauging of 1,600 km, double tracking of 250 km and track renewal of 2,400 km	20 865	In progress
Taiwan Province of China: high-speed line, Taipei-Kao-hsiung (345 km)	16 925	Not yet started
Republic of Korea: high-speed line, Seoul-Pusan (411 km)	15 000	Under way Planned completion 2001
China: high-speed line, Beijing-Shanghai (1,300 km)	12 195	Not yet started Planned completion 2000
Hong Kong: construction of second main line for Kowloon-Canton Railway Company (34 km)	2 979	At the planning stage
Taiwan Province of China: upgrading (electrification/track doubling/resignalling) of east coast trunk line (337 km)	1 600	At the planning stage
China: construction of new, electrified line, Zhuhai-Guangzhou (173 km); private sector involved	800	At the planning stage
India: construction of new line on the west coast (Konkan Railway of 760 km)	673	In progress
Islamic Republic of Iran: construction of new rail line to the port of Bandar Abbas	..	Complete March 1995
Construction of new line Tedzhen-Sarak Mashhad between the Islamic Republic of Iran and Turkmenistan (Completes the new Silk Railway China-Central Asia-Islamic Republic of Iran-Turkey-Europe)	..	Inaugurated in May 1996

Source: ESCAP, *Review of Developments in Transport, Communications and Tourism in the ESCAP Region, 1995* (ST/ESCAP/1620), table 5, p. 30.

Note: In addition, the ADB has proposed a number of new railway projects for the Greater Mekong subregion involving links between China, Cambodia, the Lao People's Democratic Republic, Myanmar, Thailand and Viet Nam.

development over the next 15 years. According to other industry observers, who are predicting almost a quadrupling of passenger numbers within this time-frame (from 122 million passengers in 1994 to nearly 400 million passengers by 2010), this estimate is conservative. Their expectation is that the amount of investment required over the next 15 years will be closer to $200 billion.[3]

The telecommunications subsector will also require sizeable investment expenditure. However, unlike many other areas of infrastructural investment, a sizeable part of the telecommunications investment can be generated by the operating agencies. More than 50 per cent of such investments worldwide is found to be financed from the financial surpluses of telecommunications operating agencies. According to ITU, the Asian and Pacific region as a whole achieved a 49 per cent reinvestment of telecommunications revenue in recent years. Despite the limitations of data, it is estimated that investment in telecommunications for the region as

[3] Report of the Air Transport Action Group of the Pacific Economic Cooperation Council, *Bangkok Post*, 11 July 1995.

a whole currently averages about $38.5 billion a year.[4]

Notwithstanding recent heavy investment in telecommunications infrastructure in China and India, the future investment needs of these two countries during the remainder of this decade are huge. For example, in China, a total of 450 billion yuan ($55 billion) will have to be expended between now and the year 2000 if the Government's target of 114 million installed telephone lines, or 8 lines per 100 persons, is to be achieved. In the case of India, the required investment by the year 2000 to provide the 50 million new lines needed to increase telephone density from less than one line per 100 persons currently to 5 lines per 100 persons (the average for the region's developing countries) has been estimated at $75 billion.[5]

In fact, mobilization of finance for the development and improvement of transport and communications infrastructure will be a formidable task for most countries in the region. Based on the incremental needs in selected physical transport and communications infrastructure (telecommunications, railways, roads, seaports, airports and urban transport), it is estimated that the required increase in selected physical facilities up to the year 2000 would need incremental investment to the tune of over $500 billion.[6] Investment resources currently available or foreseen for the necessary investment leave a gap of over $300 billion. It is unlikely that governments will be able to raise a sum of this magnitude from traditional sources of funding such as the government budget and foreign aid and loans, and alternative sources of finance will have to be explored. Enhancing the role of the private sector in infrastructure financing, management, operations and risk-sharing holds the promise of efficient delivery of infrastructure under arrangements such as BOT and BOO schemes. The involvement of transnational corporations in infrastructure development has been increasing. Their growing involvement in the region is reflected in the annual inflow of about $2.3 billion of FDI into infrastructure-related industries in selected South, East and South-East Asian countries during the late 1980s and early 1990s.[7] There are however a number of important issues that arise in the process of involvement of the private sector through privatization of existing state-owned enterprises and/or participation in new ventures. Those issues need to be carefully considered for their best possible solution (box V.1).

The importance attached to private sector participation in infrastructure development was reflected in the decision of the Commission at its fifty-first session to convene a Ministerial Conference on Infrastructure concurrently with the private sector-oriented World Infrastructure Forum – Asia, 1996. The Ministerial Conference launched the New Delhi Action Plan for Infrastructure Development in Asia and the Pacific, 1997-2006 and the Asia Infrastructure Development Alliance (AIDA). AIDA, a tripartite alliance between government, the private sector and multilateral and intergovernmental agencies, has as its principal aim the accelerated development of infrastructure through public-private partnerships.

Special problems confront the least developed, landlocked and island developing countries and economies in transition in their efforts to develop adequate and efficient infrastructure. These problems arise from inadequacies in strategic planning of infrastructure development as well as related institutional capacity-building. In some of them, special efforts are needed to restore the damage resulting from decades of war. The traditional dependence of these countries on ODA whose volume has been shrinking, puts further strain on their capacity to finance the required infrastructure development. Their need for a better and more efficient transport and communications infrastructure will nevertheless be greater in order for them to join the mainstream of globalization and regionalization. In this respect there is an urgent need to address specific transport related issues including availability and choice of alternative transit routes; minimization of transit cost and time on these routes; and cooperation among the Governments and organizations concerned.

---

4 ITU, *Asia-Pacific Telecommunication Indicators 1995*.

5 Asia-Pacific Telecoms Supplement, *Bangkok Post*, 22 May 1995.

6 *ESCAP, Infrastructure Development as Key to Economic Growth and Regional Economic Cooperation* (ST/ESCAP/1364).

7 UNCTAD, *World Investment Report 1996: Investment, Trade and International Policy Arrangements* (United Nations publication, Sales No. E.96.II.A.14), annex tables 10 and 11, pp. 285-295.

Box V.1. Issues and implications of private sector involvement in infrastructure

Until just about a decade ago, the provision of infrastructure in nearly all countries was almost entirely a public sector responsibility. The assumption of virtually exclusive responsibilities by the public sector was motivated by a number of considerations. The provision of infrastructure was considered far too important and strategic to be left to the private sector to supply. It was presumed that the technology and economics precluded any substantial role for the private sector. Specifically, it was felt that decreasing unit costs in the production and distribution of infrastructure services would give rise to a natural monopoly, with attendant misuse of market power by private sector providers. Because infrastructure services often resembled "pure public goods" or "merit goods" they were regarded as unattractive to private investment. There was also the practical reality that in many countries the private sector was simply unwilling or unable to undertake lumpy investments with the long gestation periods typical of many infrastructures.

However, for over a decade, economists and many governments have begun to question the true extent of "market failure". Furthermore, the many examples of "government failure", particularly the indifferent performance of state-owned enterprises, have contributed to a reappraisal of the appropriate roles for the public and private sectors in infrastructure development. The governments of many developing countries are facing severe resource constraints which are compelling them to look to the private sector to finance a portion of their physical infrastructure development.

Privatization of existing state-owned enterprises is one way of bringing in the private sector for infrastructure development and the provision of the relevant services. Many countries in the region have sought to privatize their existing infrastructures and service facilities while also seeking private investment in new ventures. Privatization can be effected by divestiture and non-divestiture options. Corporatization, an example of the latter approach, is being frequently employed in the privatization of state-owned enterprises in infrastructure sectors. The state-owned enterprise is transformed from a government department or statutory body into a limited company to free it from bureaucratic and political interference and constraints and thus provide it with greater flexibility than a government enterprise to respond to market forces. The government remains the owner of the corporatized company. Corporatization is often the precursor to the eventual divestment of the shares in the state-owned enterprise. Malaysia, one of the first countries in the region to initiate the privatization of state-owned enterprises in infrastructures, has used this technique in a number of instances, including the corporatization of the airports and the Malayan Railway.

In contrast, divestiture involves the partial or complete transfer of ownership to private shareholders. The sale of government equity in state-owned enterprises may not, however, translate into a sale in perpetuity of shares in the government enterprises concerned. The privatized companies in Malaysia, for example, operate under a licence from the government for a specific time period.

BOT is a common technique employed for bringing in private sector investment to develop new infrastructure facilities. Each BOT project involves a concession agreement between the government and a private company under which the latter finances the construction of a facility and operates it for a specified period. The private company, in turn, is allowed to retain the income generated over the concession period. At the end of the concession period, the facility reverts to public sector ownership. A variation of BOT is the BOO scheme, where the final ownership remains with the private sector company.

There are many examples of provision of infrastructure: an additional 2 million telephone lines in Bangkok and 1 million provincial telephone lines in Thailand ($2.8 billion and $1,250 million respectively); the North-South Expressway in Malaysia ($2.4 billion); construction of power plants in the Philippines ($2 billion); a mass-transit system in Guangzhou, China ($1.2 billion); and a national sewage system in Malaysia ($2.5 billion).

The following are some of the pros and cons of involvement of the private sector in infrastructure development that need to be carefully weighed. It is not always easy to reconcile the often conflicting demands on policy to serve diverse objectives such as wider geographical coverage, affordability for all sections of the population, financial viability and ensuring reliable services.

There are several obvious benefits that emanate from private sector involvement:

(a) A reduction in both the administrative and the financial burdens on the public sector can be achieved through the transfer of public sector activities and employees to the private sector;

(b) Financial gains could accrue from the sale of infrastructure assets, savings on investment and operating expenditure, revenue from lease payments from private entities, and the transfer of the government's outstanding debt to private operators;

(c) Private sector involvement could enhance the dynamism of the economy in the long run through improved efficiency, a favourable impact on the international perception of the country's investment climate and a strengthening of the local capital market.

The following considerations, however, must be weighed while moving towards privatization of existing state-owned enterprises or inducting the private sector into new ventures:

(a) Unprofitable state-owned enterprises are often unsuitable for privatization. If however, only unprofitable entities are left in the public sector, the sector's financial position could worsen and become unsustainable;

(b) Efficiency gains may not be achieved if public monopolies are simply converted into private monopolies. In addition, if privileged shareholding allows the government to retain effective control and influence over the firm's behaviour, the efficiency gains associated with flexibility may be compromised;

(c) The infrastructure services provided by private companies often have to be regulated to counteract the market power of private monopolies and oligopolies and to protect consumer welfare and employee interests. Institutions must be created to perform supervisory and regulatory functions, not only to enforce minimum safety, quality and environmental standards but also to take into account broader socio-economic objectives, where necessary. Social goals, however, must be balanced with the aim of enhancing efficiency;

(d) The way in which the policy is implemented, whether it concerns privatizing an existing state-owned enterprise or building a new project, should be transparent and above board to retain public confidence that vital infrastructure service facilities will not be misused or exploited for private gain. The award of projects on a "first-come, first-served" basis or the use of a closed tendering system could encourage rent-seeking activities by individuals and firms.

INTERNATIONAL AND REGIONAL LINKAGES

Transport infrastructure

As the preceding review has shown, the development of transport linkages in the Asian and Pacific region has been given high priority by the member countries of ESCAP. The strengthening of intraregional and interregional transport and communications linkages has also received considerable attention. This was emphasized in the Transport and Communications Decade for Asia and the Pacific, 1985-1994, and reemphasized in the New Delhi Action Plan. An integrated Asian land transport infrastructure development (ALTID) project, comprising the Asian Highway, the Trans-Asian Railway and land transport facilitation measures, was adopted in 1992 for implementation over the years.

The major objective of the ALTID project is to provide reliable and efficient land transport linkages within the ESCAP region and between this and other regions, as part of an integrated sea, land and air transport system, in order to facilitate regional and international trade and tourism.

Although new in its present form, the ALTID project represents a continuation of a process dating back to the launching of the Asian Highway project in 1959 and the Trans-Asian Railway project in the 1960s by ESCAP. Since the provision of land transport infrastructure is a necessary but not sufficient condition for promoting freer movement of freight and passenger traffic, the ALTID project envisages greater cooperation among countries in facilitating land transport at border crossings through their accession to various international conventions and multilateral and bilateral agreements in the field of transport facilitation.

ALTID is an important symbol of the increasing integration of the economies of Asia. Countries in the region gave their fullest support at the fifty-second session of the Commission to include ALTID as a priority project in the New Delhi Action Plan. The Ministerial Declaration in New Delhi in 1996 reaffirmed that support. Convinced that efficient transport linkages among countries in the region can be an important catalyst for economic transformation in individual countries, many countries are endeavouring to forge new cross-border linkages or to re-establish old ones. This is perhaps exemplified by the reopening of the rail link between Viet Nam and

China and the inauguration in May 1996 of a new rail link between the Islamic Republic of Iran and Turkmenistan, creating a "new silk railway" from China to Central Asia and then to the Islamic Republic of Iran, Turkey and Europe.

Both the Asian Highway and the Trans-Asian Railway projects have not only been reactivated but revised and expanded recently. The Asian Highway currently consists of a network of international roads approximately 90,000 km in length. It was to extend originally from Afghanistan and the Islamic Republic of Iran in the west to Thailand, Viet Nam, Indonesia and the Philippines in South-East Asia. It also provided for a connection to Sri Lanka while passing through South Asia. The ESCAP secretariat carried out fresh studies on the Asian Highway networks to identify its current status and shortcomings. The Asian Highway network has now been revised to include highway networks in the Central Asian republics. The revised version provides for a southern corridor from the Islamic Republic of Iran to South and South-East Asia; a new network for a corridor from South-East Asia to China and Mongolia, and one in the Central Asian republics of Armenia, Azerbaijan, Kazakstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan.

The road networks are built by the individual nations concerned according to standard international specifications. Currently, approximately three-quarters of the Asian Highway is two lanes wide and efforts are being made in participating countries to widen the one-lane sections to two lanes. Roughly 75 per cent of the two-lane roads has been paved. However, the missing links still amount to a total of 2,200 km, or 3.4 per cent of the total length of the network.

The Trans-Asian Railway is also an extensive network. There are five major land bridges for the Trans-Asian Railway. Their connecting links and the current status of development are as follows. First, the Trans-Asian Railway northern corridor runs from Europe to the Korean peninsula via the Russian Federation, or the Russian Federation and China. The minimum required infrastructure for this corridor currently exists in the rail networks of China, Mongolia, Kazakstan, the Russian Federation or the Russian Federation and the Korean Peninsula. Second, the Trans-Asian Railway southern corridor runs from Europe (and Central Asia) to South Asia and then to South-East Asia. A portion of this corridor would run from the Islamic Republic of Iran to Bangladesh. The missing links in this corridor are a major problem for further progress. Third, the "new silk railway" extends from Europe and Turkey to the Islamic Republic of Iran, Central Asia and China.

In May 1996, the inauguration of a link between the Islamic Republic of Iran and Turkmenistan put in place the minimum required infrastructure for this land bridge also. Fourth, the Trans-Asian Railway South-East Asia/North-East Asia corridor was initiated by the ASEM summit in 1996. Missing links are a major problem with this land bridge too. The fifth land bridge is the Trans-Asian Railway linking northern and north-western Europe with the port of Bandar Abbas in the Islamic Republic of Iran, via the Russian Federation and Central Asia.

International transport facilitation

The provision of transport infrastructure is a necessary but not a sufficient condition for the efficient movement of international transport. The lack of efficient transport facilitation can lead, for example, to the delay of vehicles at border-crossing points, resulting in material and time losses. An important aspect of efficiency is therefore transport facilitation.

The purpose of facilitation is to optimize the utilization of transport linkages between countries and subregions by allowing complex operations to be performed as rationally as possible. The achievement of such facilitation goals is not easy. The need to adhere to government regulations with regard to issues such as national health, security, customs and taxes, may continue to remain major constraints on cross-border traffic facilitation. However, several important initiatives have been undertaken in the region in this regard in recent years and these are briefly reviewed below.

Land traffic

As part of the implementation strategy of the ALTID project, the Commission has recommended that countries in the regions, if they have not already done so, consider the possibility of acceding to

seven major international conventions in the field of land transport facilitation. The status of accession of countries and areas of the ESCAP region to these international conventions is shown in table V.6. Creating a minimum legal basis for cross-border road and rail traffic is still a major task to be accomplished to facilitate international and bilateral trade and tourism in Asia.

In the field of railways, many countries in Europe and some in Asia (for example, the Islamic Republic of Iran) are a party to the Convention Concerning International Carriage by Rail (COTIF), Berne, 1980, which replaces the traditional national customs document by the International Consignment Note (CIM). However, the member countries of the Organization of Railways Cooperation (OSShD), including China, the Democratic ople's Republic of Korea, Kazakstan, Mongolia, the Russian Federation and Viet Nam, have developed and are using the system of the Agreement on International Railway Freight Communications (SMGS system) for the same purpose. A draft convention on international customs transit procedures for the carriage of goods by rail has been developed by ECE and this is being finalized in consultation with OSShD and other organizations to harmonize the approaches to customs requirements.

Transit transport plays a particularly important role in the development of landlocked countries. There are 12 such countries in the region. Two current international transit conventions pertain to the facilitation of transit transport of landlocked countries: the Convention and Statute on Freedom of Transit, Barcelona, April 1921 (commonly known as the Barcelona Transit Convention), and the Convention on Transit Trade of Landlocked States, New York, 1965 (commonly known as the New York Transit Convention). Unfortunately, to date, only 13 countries of the region are contracting parties of these conventions. There is good potential to improve transit transport in the region if the landlocked countries in Asia and those countries that border them accede to the Barcelona and New York transit conventions.

Maritime traffic

In addition to land transport facilitation, the facilitation of maritime traffic plays an increasingly important role in the movement of freight and passengers. Efficient cargo operations should require very short stays in port even for modern large carriers. The delays caused by the adherence to documentary requirements often become very expensive. To improve the situation, countries in the region are adopting the amended Convention on Facilitation of International Maritime Traffic, 1965 (FAL Convention). The objective of the FAL Convention is to simplify procedures for the inward clearance of ships, cargoes, passengers and crew on arrival in a port during the course of an international voyage. This can be achieved by the utilization of six standard declaration forms and the adoption of common standards for processing documentation.

At this time, only Australia, China, the Democratic People's Republic of Korea, Hong Kong, Fiji, India, the Islamic Republic of Iran, the Marshall Islands, New Zealand, the Russian Federation, Singapore, Thailand and Vanuatu are parties to the FAL Convention. The countries which have not yet joined the Convention may wish to do so as an important step in harmonizing standards for processing documentation.

International inland water transport facilitation is another area of importance. There are several rivers which run across international borders in Asia such as the Ganga Jumuna-Padma-Bhramaputra network and the Mekong River system. To make use of these waterways of international importance, agreements and protocols between interested countries have been or are in the process of being developed. The Protocol on Inland Water Transit and Trade between Bangladesh and India, and the recent Mekong River agreements are cases in point. These protocols and agreements can facilitate the smooth and efficient movement of cargoes and passengers on international inland waterways within the ESCAP region. The experience with such agreements in Europe is positive. For example, the countries on the Rhine River basin ratified the so-called Act of Mannheim of 1868 as one of the international treaties governing navigation on the Rhine River which is implemented through the Rhine River Commission. The arrangement proved very effective for facilitating inland water transport development in Europe even when countries had differences on other matters. Similar arrangements could be of great practical value in facilitating international inland water transport in the region.

Table V.6. Accession status of countries and areas of the ESCAP region to international conventions, as at November 1996

Country or area	*Convention on Road Traffic (1968)*	*Convention on Road Signs and Signals (1968)*	*Customs Convention on the International Transport of Goods under Cover of TIR Carnets (1975)*	*Customs Convention on the Temporary Importation of Commercial Road Vehicles (1956)*	*Customs Convention on Containers (1972)*	*International Convention on the Harmonization of Frontier Control of Goods (1982)*	*Convention on the Contract for the International Carriage of Goods by Road (CMR) (1956)*
Group I: Mainland Asia							
Afghanistan			x	x			
Armenia			x			x	
Azerbaijan			x				
Bangladesh							
Bhutan							
Cambodia				x			
China					x		
Democratic People's Republic of Korea							
Hong Kong				x			
India		x					
Islamic Republic of Iran	x	x	x				
Kazakstan	x	x	x				x
Kyrgyzstan	x	x					
Lao People's Democratic Republic							
Malaysia							
Mongolia							
Myanmar							
Nepal							
Pakistan	x	x					
Republic of Korea	x	x	x		x		
Russian Federation	x	x	x		x	x	x
Singapore				x			
Tajikistan	x	x	x				x
Thailand	x	x					
Turkey	x	x	x	x	x		x
Turkmenistan	x	x	x				x
Uzbekistan	x	x	x		x	x	x
Viet Nam							
Group II: Island countries							
Brunei Darussalam				x		..	..
Indonesia	x	x	x		x	..	..
Japan						..	..
Maldives						..	..
Philippines	x	x				..	..
Sri Lanka						..	..

Source: ESCAP secretariat.

Note: x = acceded.

Multimodal transport and freight forwarding

Just-in-time delivery is becoming a prerequisite for competitive international trading. Instead of piecemeal, fragmented, unimodal systems of transport, with differing laws, regulations, procedures, customs and practices for each mode, traders require comprehensive distribution logistics requiring an integrated system of despatch, transport and delivery.

An inadequate transport infrastructure, lack of appropriate legislation governing the entry of foreign licensed vehicles and containers into national territories, and the absence of harmonized customs procedures are major constraints for the development of multimodal transport. Availability of electronic data interchange (EDI) in the developing countries of the region could considerably facilitate the process. Many of the countries, however, do not yet have EDI arrangements.

Multimodal transport can be usefully promoted through the development of uniform multimodal agreements at the subregional level. The success of this approach has been demonstrated in Latin America, where Bolivia, Colombia, Ecuador, Peru and Venezuela have reached agreement on uniform rules which govern the operation of multimodal transport, including standards and criteria for multimodal transport operators, the provision of contracts and the use of multimodal transport documents. A similar approach has been proposed for the ASEAN countries. A draft working document for the development of a multimodal agreement for the ASEAN subregion is under consideration by ASEAN governments. A similar approach could also benefit the other subregions.

Electronic data interchange

As a result of changes in global manufacturing, the sourcing of products and the relocation of industries, it is likely that the focus in future will be on making logistics systems as flexible as possible. This means that logistics systems will be driven by the need to customize and satisfy the exact requirements of the customer in terms of both product configuration and service quality. This also means that EDI will constitute the main means of data and information interchange.

It is therefore becoming apparent that in the not-too-distant future, the development of EDI will be an unavoidable requirement for effective participation in international trade. The further introduction and development of EDI in the region could have an appreciable impact on trade as well as the development of multimodal transport operations and freight forwarding.

CONCLUDING OBSERVATIONS

In view of the rapid expansion in trade, investment and economic activities generally in the region, further extension and upgrading of the transport and communication infrastructure in the region are urgently needed. Disparities in levels of development of transport and communications infrastructure in different economies are a major constraint on the regional and global integration of these economies in the region. Accelerated development of national, subregional and regional transportation and communication networks is clearly needed to keep pace with the demands of economic expansion in the region. In this context, the development of urban transport systems is also an area that requires greater attention, particularly in view of the growing pressure of population and industry in the increasingly congested urban centres of many countries in the region.

While physical infrastructure forms the foundation for forging internal and external linkages, the quality, efficiency and cost-effectiveness of the services that these infrastructures deliver to users is equally important. The efficiency and cost-effectiveness of external transport and communications linkages are crucial in the development and maintenance of export markets while speedy, efficient and cost-effective information flows enhance the development of financial markets which rely greatly on such information flows. Proper maintenance of infrastructure assumes significance in this text. Substandard conditions of transport networks add to freight transport costs and introduce inefficiency into production and distribution systems.

There is a growing recognition that the solution to the problem of traffic gridlock in urban centres and cities in the region may not be achieved simply by providing more or better infrastructure. The need for demand management or traffic-restraining measures is increasingly recognized. The rapid increase in the number of road vehicles in the region's larger cities is not sustainable over the long term. The existing land-use patterns suggest paucity of land for extra road space to accommodate persistent growth in vehicle numbers. Area restrictions, road pricing, reserved bus lanes and better overall traffic management are needed. The integration of the plans for all urban transport infrastructure and services within a comprehensive land-use planning framework is required for the purpose. Strict enforcement of landuse zoning and building density (or plot ratio) regulations will be also needed. The extension and improved management and organization of mass public transport systems could be an important element in the solution of urban congestion.

The financial performance of the railways in the region needs to be improved. Many countries in the region have been making efforts to transform their railway organizations into unambiguous commercial entities. In reality, few railways in the region have been able to generate sufficient revenue to cover their operating costs. Restructuring and reorganization should encourage stronger efforts towards the achievement of financial solvency.

Improved systems of costing should allow management to monitor the financial performance of individual traffic segments and permit the identification of those traffic segments or services which have no prospect of generating sufficient revenue to cover their costs. Railway organizations in Indonesia, Malaysia and Thailand have recently made considerable progress both in the improvement of their management and cost-control processes and in securing the agreement of their Governments to compensate them for running unprofitable segments to meet community and social service obligations. Other countries could adopt similar policies and measures to make their railways operate profitably.

Industrial expansion in the region has been placing rising demand for freight transport on the rail and road systems. Inland shipping could provide a substitute or supplementary mode for movement of domestic cargoes and relieve pressures on the roads and railways. The advent of containerized transport has enhanced the potential use of inland shipping. The full realization of this potential has been frustrated by the application of traditional protectionist laws and regulations (called cabotage laws), which exclude foreign flag ships from carrying domestic cargo between two or more ports in the same country. In order to provide domestic cargo customers with choices in the selection of transport modes, removal of such restrictive laws may be necessary. New Zealand's example in dismantling restrictive cabotage legislation and in ensuring equity in the competition between the various transport modes for domestic freight volumes could be considered by other countries. Malaysia has also recently liberalized its cabotage restrictions. These newly liberalized laws provide domestic cargo forwarders with greater flexibility in the choice of mode and advantage in rate negotiations with competing modes.

In the international container shipping sector, the cargo reservation policies of past decades have given way to more market oriented policies, and the liner conference system has been in a state of decline. Along with these changes container shipping alliances are emerging which are offering much more efficient and cost effective systems, through the use of larger vessels, rationalization of route structures and cooperative arrangements for joint operations.

In the field of regulation of liner shipping, some countries or groupings of countries have unilaterally developed policy and legal instruments for controlling the sector. This in turn has created a complex and uncertain business environment. To the extent that regulation is deemed necessary there would appear to be a strong case for the development of regulations on an internationally agreed basis. International container shipping by its very nature has always been global. The globalization process is demanding, however that shipowners provide a wider range of services to multinational customers. In this context, developments in the international liner shipping market need to be closely monitored because of the growing possibilities of horizontal and vertical integration of shipping assets and land-based facilities through acquisition, contractural agreements, and concentration into global alliances.

In the field of air transport, the administration and management of airports and maintanance of safety standards are crucial tasks. Throughout the region, airports are usually managed by national civil aviation administrations. In the 1980s, there was a move towards the establishment of autonomous airport or civil aviation

authorities. They were given a corporate structure where traffic volumes and the possibility of financial self-sufficiency justified such autonomy. More recently, some governments adopted policies aimed at transferring ownership or control of airports to the private sector. Provided that such privatization can meet the requirements for safety and security, investment and management needs can perhaps be better met from private sector financial and managerial resources. Many countries are also inducing the private sector to provide air transport services with private ownership of aeroplane fleets. Australia, China, Indonesia, Japan and the Republic of Korea have allowed their domestic private carriers to enter regional or international markets, while others, notably India, Nepal, Pakistan and the Philippines, have opened up their domestic markets to new private carriers.

In the field of telecommunications, a wide variety of management and regulatory structures and practices exist in the region. State-run post and telegraph agencies have traditionally provided telecommunications services in the region. The current trend is towards liberalization, opening up the hitherto monopolized telecommunications services to private participation and market competition. Privatization in the telecommunications subsector is generally more easily achieved than in other transport and communications subsectors. The advent of digital telephone technology has lowered the barriers to market entry by avoiding the need for potential entrants to undertake large investments in fixed-link telephone infrastructure. Private investors may, however, opt for fast profits to be made in the lucrative "high tech" end of the market, even in countries where only a small percentage of the population has access to basic fixed-line telephone services. Expansion of service facilities to people at large may suffer as a result. Community welfare could suffer if private monopoly (or duopoly) is allowed to develop. Appropriate regulatory frameworks need to be developed to avoid such potentially adverse consequences. In Australia, an independent regulatory authority has been using price caps and interconnection agreements as its main instruments of regulation since 1992.

The recent Ministerial Meeting of WTO produced the basis for an information technology agreement which would aim to abolish tariffs on information technology products by the year 2000. This was followed by an agreement on telecommunications signed by 68 countries in February 1997 under the auspices of WTO. These developments will have important implications for the adoption and spread of information technology in the region in the area of communications in particular. The growth of the Internet within the region is as yet undocumented but is considerable. The Internet is still in its infancy and the potential that it offers for education, business and research is enormous. However, because of the borderless nature of the Internet and the World Wide Web, major stumbling blocks to their further development in the future involve issues of intellectual property rights protection and censorship. The issue of intellectual property rights arises because the open nature of the Internet makes it difficult for owners of copyright to limit the reproduction and spread of information. National governments are also concerned that an expansion of Internet usage and linkages to the rest of the world could encourage a flood of pornography, and unbridled political comment and discussion could undermine order and stability.

National transport and communications infrastructure development need to take into account the prospects of intraregional and interregional linkages. Development of regional road and rail networks under the Asian Highway and the Trans-Asian Railway as part of the ALTID project requires commitment of financial and human resources. The adoption of recommended standards and the filling in of the missing links in the networks would provide important intraregional linkages.

However, building of the network infrastructure at standards set for reliability and efficiency will not be sufficient for reliable and efficient international land transport movement. The development of the intraregional road and rail linkages also requires adequate facilitation measures and agreements at border crossings. Such facilitation can take place through accession to related international conventions and bilateral agreements. In the area of transport facilitation, a harmonized legal system for international transport by road and rail should be developed and introduced in the region. In parallel, there is a need for regional cooperation in developing and enforcing harmonized laws and regulation governing transportation of hazardous goods (box V.2).

Box V.2. The need for regional cooperation in the transportation of hazardous goods across borders

As the countries of the ESCAP region become more industrially oriented, larger quantities of complex, dangerous goods, such as chemicals and a variety of combustibles, are being transported across national borders and through inland networks, creating an increased risk to the population and the environment. The transportation of dangerous goods often poses a greater threat to the community and the environment than when the goods are stored at their eventual industrial destination, even though the quantities may be smaller. The reason is that the problems are magnified when a whole range of goods, sometimes in one shipment, has to transit corridors which often pass through population centres. Throughout the transport process, a number of different government ministries and agencies (sometimes more than 20) have varying levels of responsibility, thus splitting the line of command and bringing into play a number of legislative regulations, not all of which are complementary.

The related administrative procedures in terms of documentation, information transfer between agencies, and coordination are also overly complex. Importantly, the transport sector, by its nature, is not specially geared to the handling of hazardous cargoes in the same way as specialized processing plants. The basic procedures and skills required in handling these cargoes are therefore largely absent in the transport sector. Owing to the above-mentioned limitations and the absence of a harmonized approach, incidents and accidents involving hazardous cargoes occur all too frequently.

European countries have made considerable progress in harmonizing legislation and regulations relating to the international carriage of dangerous goods. These initiatives include the European Agreement Concerning the International Carriage of Dangerous Goods by Road, annex I of the Convention Concerning International Carriage by Rail (COTIF) (Berne 1980) and appendix B of COTIF on uniform rules concerning the contract for international carriage of goods by rail. In addition, the United Nations Committee of Experts on the Transport of Dangerous Goods has developed recommendations on the transport of dangerous goods.[a]

To date, however, no international provisions or agreements for the over land transport of dangerous goods exist in Asia. From a commercial point of view, harmonization of classification and listing of dangerous goods, as well as their terminologies, reduces the need for and cost of complying with different national and modal requirements. From the point of view of safety, such harmonization facilitates the identification of appropriate transport precautions and an appropriate response in case of an accident. There is clearly a need for urgent regional and subregional initiatives to be taken in this regard.

---

[a] *Recommendations on the Transport of Dangerous Goods*, 9th rev. ed. (United Nations publication, Sales No. E.95.VIII.1).

The multimodal transport concept directly supports efficient management of the supply chain. Consequently, the development of multimodal transport across the ESCAP region will provide the opportunity to reduce costs, increase competitiveness and improve quality, thereby placing Asia in a strong position to meet growing trade competition from the rest of the world. A legal framework is also required to provide the basis for the eventual unhindered access to the routes. The example of the European Union is instructive in this regard. In the interest of compatibility of inter-country transport infrastructure, four major all-European agreements have been negotiated. Similar legal frameworks could be developed for Asia covering at least the Asian Highway and the Trans-Asian Railway networks.

CHAPTER VI

CONCLUSIONS AND POLICY IMPLICATIONS

VII

THE CONTEXT

The basic objectives of development are relatively invariant over time and space. These are promotion of economic growth, equity in income distribution and employment. Environmental sustainability is a more recent addition. The relative emphasis placed upon each of these objectives may, of course, differ among countries, depending on the stage of development and the socio-political ethos. A major challenge that developing countries in the region now face and will have to confront in the twenty-first century is that the above objectives have to be pursued in an environment characterized by intensified globalization and regionalization.

Globalization and regionalization are ongoing processes driven by a host of technology-, market- and policy-related factors. Among these are increased competition in the international economy; push and pull factors prodding transnational corporations to locate production abroad; developments in information technology, financial markets, services sectors, transport and communications; greater liberalization and openness of trade, FDI and financial sector policy regimes in developing countries; and international measures aimed at securing multilateral agreements on cross-border transactions and increasing their transparency. The most important among international measures is the Uruguay Round.

Globalization and regionalization have become intensified in recent years, and the momentum is likely to continue into the next millennium. While the more open policy stance adopted by developing countries in the region attests to their voluntary participation, many of the factors driving these processes are beyond the control of individual developing countries. They have little choice other than to participate in these processes since an insular approach is likely to marginalize them further. As the preceding chapters have shown, the developing ESCAP region as a whole has been an active participant in these processes, though there are major differences among various groups of countries in the extent of their participation. Therefore, the key policy question that developing countries in the region will have to address is how to optimize the benefits of participation in the emerging international division of labour while promoting their national development objectives.

The integration of individual economies with the international and regional economies widens the opportunities for national development but also poses some risks. The benefits and costs are not uniform for all countries, especially because of wide variations in initial conditions reviewed in chapter II, and may also differ for a particular country over time. This creates the need to monitor and analyse the impacts continually and to fine-tune the policy instruments to deal with them. Nevertheless, certain generalizations can be made both about the benefits and costs and the contours of policy imperatives. The following sections are an effort in this direction.

BENEFITS AND RISKS OF GLOBALIZATION AND REGIONALIZATION

The benefits and risks of integration with the international and regional economies have been dealt with at some length in the previous chapters, especially under chapters III and IV, which deal respectively with international trade and financial flows (including foreign direct investment), the two main planks of globalization and regionalization. Nonetheless, it is useful to recapitulate some key points.

Foreign trade

In the context of the benefits, development literature until recently focused largely on international trade. The static gains of trade stem mainly from greater specialization, higher allocative efficiency, wider access to production factors (such as capital equipment) as well as to intermediate and consumer goods at lower prices, and greater opportunities to exploit the economies of scale. It is

being increasingly recognized that the dynamic gains are no less significant. These arise from, *inter alia*, increased competition, stepped-up technological improvements, enhanced acquisition of knowledge either through imports or learning on the job, and reduced incidence of rent-seeking activities. These gains contribute to accelerated growth.

Trade stimulates economic growth through several other channels. There is often a positive relationship between a country's trade intensity and its attractiveness for inflow of FDI. Trade necessitates the development of transport and communications networks which accelerate the growth of traded as well as non-traded output. Furthermore, greater involvement in trade induces the pursuit of macroeconomic stability and improved economic governance, which are increasingly acknowledged as the basic prerequisites for growth.

Similar comments also apply to intraregional trade, which has the additional advantage that the "psychic distance" between countries located within a region may be shorter because of similarities in, *inter alia*, culture, legal codes, ethnic ties, distribution systems. Thus, new trading opportunities can be created. In addition, regional cooperation may induce faster liberalization of trade policies.

That participation in international trade has been an important contributory factor to accelerated growth of several economies in the Asian and Pacific region, especially those in East and South-East Asia, can be hardly questioned. It is pertinent to note that China, Hong Kong, Malaysia, the Republic of Korea, Singapore, Thailand and Viet Nam achieved export growth rates well above the world average during the period 1980-1995 (chapter III). From the perspective of the trade-growth nexus, a particular concern relates to the performance of the least developed countries and the Pacific island economies, many of which exhibit low or negative growth rates in exports. In some of the cases, the apparently high growth rates observed during some periods are due to a low base.

While the positive impact of trade on growth is widely accepted, there exists a divergence of views regarding its impact on equity in income distribution. However, there is a certain degree of consensus that trade is likely to alleviate absolute poverty through a rapid expansion in output and employment in labour-intensive export industries and related activities, as well as through an increase in real wages for labour, which is the primary asset that poor households possess. The success of several East and South-East Asian economies in greatly reducing absolute poverty is, to a significant extent, attributable to their trade performance.

The analysis of the relationship between international trade and environmentally sustainable development is of relatively recent origin. There are several views in this respect. It is argued that, in countries with a comparative advantage in production requiring large amounts of natural resources excessive reliance on exports may cause severe environmental degradation unless carefully planned conservation and regeneration measures are implemented. In pursuing export orientation, the countries may relax environmental standards with a view to reducing production costs and thereby maintaining thier competitive edge. The counter-argument is that the cost of compliance with environmental norms typically constitutes a small proportion of the total cost. It should not be a significant deterrent to exports. A country's export performance is determined to a much greater extent by such factors as resource endowments, technology, labour and productivity. It is also argued that trade may make a positive contribution to the environment as rising per capita incomes brought about by trade raise the demand for a better environment. While the need for more in-depth research on the interface between trade and environmental sustainability is recognized, it is probably a fair assertion that there is nothing intrinsic to trade that militates against environmental sustainability.

In the light of the above, it appears that trade can contribute to faster growth and greater alleviation of poverty. The development experience of several economies in the region also bears this out. However, due cognizance should be taken of some of the risks associated with international trade. There is the risk that the economy may become subject to greater instability, particularly in situations where exports are concentrated in a few products or countries. In such circumstances, a slump in the demand for a country's major export items or a recession in major partner countries can cause a substantial deceleration in the entire economy. Greater participation in trade also inevitably entails greater liberalization of the trade policy regime. It is therefore possible that some of the industries which grew up under protective trade regime may collapse.

Although it may be desirable to let highly inefficient industries die a natural death under the liberalized policy regime, there is a cost associated with the process. For example, workers employed in those industries may have to be retrained in order to enable them to find employment in other expanding industries. Moreover, potentially viable industries may need some time to adjust. Another problem is that participation in international trade would require adherence to international policy norms, especially those envisaged under the Uruguay Round. That imposes a measure of constraint on national policy choices. Furthermore, there arises the need to develop the ability to identify new areas of production and trade in a world of shifting comparative advantage. Otherwise, a country may run the risk of becoming locked into areas of trade with slow growth potential in the long run. In the case of trade promoted under regional cooperation initiatives, there is an additional risk of loss due to trade diversion.

External financial and investment inflows

A major pillar of globalization and regionalization is international financial and capital flows. It is obvious that access to these flows relieves a country's foreign exchange constraint and thereby expands its capacity to import. In most developing countries, the ability to produce intermediate and capital goods is relatively weak. Domestic investment and production levels are therefore substantially dependent on import capacity. A major problem that is associated with such flows is their volatility, which, in turn, may cause instability in macroeconomic parameters such as the exchange rate, the price level and the interest rate. The benefits of access to international financial flows are therefore largely conditioned by a country's ability to deal with such negative impacts.

Most developing countries, including those in the ESCAP region, are clearly demonstrating a much more positive attitude towards FDI. FDI adds to a country's capital stock, and there is a growing appreciation that the more important benefits of FDI lie in its potential to contribute to faster growth through spillover effects. Foreign investors typically use modern production technology. Faced with tougher competition, domestic producers may be encouraged to adopt similar technological standards. Better management practices usually employed by foreign investors may be emulated by domestic producers. Furthermore, foreign investors often have better market connections either through intra-firm channels or arms-length contacts. They can thus improve a country's export performance by developing and marketing new export products as well as by increasing the exports of traditional products.

In several East Asian and South-East Asian countries, FDI has been an important factor in promoting exports and accelerating growth. In countries such as Malaysia, Singapore and Thailand, foreign investors have played a large, if not dominant, role in exports of manufactured products either through wholly-owned investments or joint ventures. China, which has emerged as the largest recipient of FDI among developing countries, has also benefited substantially from it. In contrast, the least developed and Pacific island countries and the economies in transition have not generally been able to attract much FDI or other private financial flows (chapter IV).

FDI may make a significant contribution to employment. An increasingly important feature of FDI is the relocation of production of the labour-intensive components of the value-added chain to developing countries. In so far as such investments cause a net increase in the employment of unskilled and semi-skilled labour, they may have contributed to poverty alleviation as well.

As regards the question of the effect of FDI on the environment, there is the point of view that transnational corporations may shift their pollution-intensive production to developing countries as they come under pressure in their home countries to comply with higher environmental standards. The counter-argument is that the cost of adopting anti-pollution measures is not usually a significant part of total cost of production. Therefore, differences in environmental standards do not in themselves constitute a sufficient incentive to relocate. Moreover, the environmental standards usually adopted by transnational corporations are higher than those of domestic producers as the former are more sensitive to the cultivation of a favourable image in the host countries. Empirical evidence does not seem to bear out the notion that the locational decisions of transnational corporations are greatly influenced by differences in environmental standards.

As with the case of trade, there are some risks associated with FDI. It generates a stream of outflows of profits and other payments and may thus exacerbate foreign exchange constraints, especially when foreign investments are not in export-oriented sectors. In some situations foreign investments may be of an enclave nature with few forward or backward linkages and, hence, few spillover benefits in terms of diffusion of production, management and marketing technologies. In addition, unrestricted access to FDI may subject domestic producers to premature competition. Local production capacity may thus be impaired. This consideration is particularly important because transnational corporations frequently enjoy certain assets which make it easy for them to undermine local firms or to prevent entry of new ones. For example, transnational corporations often have ready access to international capital markets at lower cost and also to worldwide production and distribution networks. In addition, transnational corporations may evade payment of taxes to the host country through transfer-pricing mechanisms.

Transport and communications

There is increasing recognition of the importance of an infrastructure, particularly for transport and communications, for sustained economic growth. The mounting concerns that growth rates in some of the fast-growing economies of East and South-East Asia may slow down owing to infrastructural bottlenecks have added weight to this perception, even though the state of development of their infrastructures is generally much better than those of the least developed and Pacific island countries and of the economies in transition (see chapter V). Transport and communications contribute to growth as facilitators of trade and investment, both domestic and foreign. Transport cost has long been acknowledged as a natural barrier to foreign trade. Improved access to transport facilities and reduced transport costs would relax this barrier and have a positive impact on trade. Foreign investors take the development of transport facilities into account as a major element in their decisions regarding locations. This factor is becoming more important with the increasing trade orientation of transnational corporations. Similarly, the availability of dependable communications facilities at reasonable prices is assuming greater importance as a determinant of a country's competitiveness. The rapidity with which information on production capacity, product quality and suppliers' capability can be transmitted to prospective buyers abroad is a crucial element in striking trade deals. Foreign investors especially value communications facilities in order to be able to maintain close contacts with their affiliates elsewhere or their parent offices. The introduction of practices such as just-in-time delivery has added to the importance of transport and communications for both domestic producers and transnational corporations. Investment in transport and communications spurs the growth of non-traded sectors by increasing the flexibility in the pattern of production, distribution and consumption of goods and services within the domestic economy and by developing forward and backward linkages among various sectors.

It is evident that investment in transport and communications directly creates new employment opportunities during the process of construction as well as for maintenance. A great deal of such employment involves unskilled and semi-skilled labour. Additional employment opportunities are created through the growth-propelling impact of transport and communications. Absolute poverty may thus be alleviated.

The relationship between transport and communications and the environment is less clear. In particular, some modes of transport can cause environmental damage in the event of use of environmentally unfriendly technology (for example, coal-operated railways) or an inappropriate choice of project location (for example, a road may cause disruptions in human settlements or damage forest areas). Large cities are particularly vulnerable to environmental problems associated with transport. For example, accidents, air pollution due to vehicle exhaust emissions and noise pollution are common in large Asian cities. Those adverse consequences can be minimized with proper planning, regulatory measures and choice of technologies.

POLICY DIRECTIONS

As noted above, globalization and regionalization are largely an exogenous reality over which individual developing countries can exercise little control. Any attempt at insulation is likely to be fraught with the risk of greater marginalization.

Although there are some risks associated with participation in these processes, the policy direction should be one of minimizing potential negative impacts and not isolation. The implementation of such an approach requires action at the national, regional/subregional and international levels. The contours of the required action are indicated below.

National level

Effective participation in the globalization process requires a certain degree of stability in the basic macroeconomic parameters of price level, exchange rate and interest rate. It is well known that high and variable inflation rates deter economic growth and accentuate distributional inequities. These also affect a country's ability to participate in international trade or to attract FDI. For example, high inflation rates would cause an increase in production cost. That would erode a country's competitive advantage and undermine incentives to export. Similarly, wide fluctuations in exchange rates adversely affect export performance. The volatility of financial flows is often aggravated by variations in the domestic interest rate. Macroeconomic instability generates uncertainties with respect to returns on investment and thus adversely affects both domestic and foreign investment.

At the same time, the task of macroeconomic management is rendered more complicated by exposure to the global economy. For example, an increase in the interest rate to contain inflation may induce large inflows of short-term funds, causing an appreciation in the exchange rate and an adverse effect on exports. Furthermore, these inflows can aggravate the very inflationary pressure the containment of which had provided the initial justification to increase the interest rate. Thus, it would be increasingly important to monitor the behaviour of macroeconomic parameters and fine-tune the combination of monetary, fiscal and exchange rate policy instruments to achieve the desired stability. At times, it is even necessary to adopt administrative measures, at least temporarily, without eroding the confidence in fundamental orientation to openness.

An important requirement for ensuring macroeconomic stability is to maintain a healthy fiscal balance. Fiscal deficits are often a major source of macroeconomic instability. Developing countries in the region face a dilemma in respect of fiscal balance. On the one hand, they have to reduce the rates of taxes, particularly those on business income and imports, in order to improve their competitiveness. On the other hand, large public investments are required for the provision of goods and services which are characterized by externalities or other market failures. Among these are health, educational and infrastructural services. In order to address this dilemma, these countries will have to pay greater attention to better tax collection and improved tax administration. It will be necessary to widen the tax base, particularly by focusing on consumption taxes. Many countries in the region have taken measures along these lines by introducing reforms in tax administration and adopting value-added taxes.[1] In this context, the need for reform of public enterprises, which in many countries are a major source of fiscal drain, deserves emphasis. Consideration should be given to accelerated corporatization or privatization in a systematic and well-planned manner. A stricter application of the criterion of social rate of return will have to be applied to government expenditure, including expenditure on defence, which has risen significantly in several countries.

Reforms and liberalization associated with globalization and regionalization may worsen the current account deficit. Liberalization of import policies eases the accessibility of imported consumer goods and reduces their relative prices. Import bills may thus rise. Such liberalization can increase the overall propensity to consume and slow down the accumulation of domestic savings. Easier access to foreign savings may temporarily finance the resultant savings-investment gap, which has a mirror image in the current account deficit, but the rising current account deficit may not be sustainable in the long run. It is therefore important to adopt countervailing measures to ensure that domestic savings are not adversely affected. This possibility appears to be a matter of concern for some countries in the region. In Thailand, for example, the Government recently announced introduction of a civil service pension fund and state enterprise provident funds to increase domestic savings.

[1] For a more detailed discussion of changes in tax policies and efforts towards improved tax administration, see ESCAP, *Issues and Experiences in Tax System Reforms in Selected Countries of the ESCAP Region* (ST/ESCAP/1564).

Participation in the globalization and regionalization processes necessarily implies greater liberalization of trade, investment and financial sector policy regimes, with the potential threat of disrupting domestic enterprises. The speed and sequencing of liberalization measures should be carefully chosen in the light of the unique conditions obtaining in individual countries without compromising compliance with international obligations. Among some key questions are: should liberalization be implemented across the board simultaneously or should there be some sequencing with, for example, the liberalization of trade policies preceding that of financial sector policies? Should current and capital account transactions be liberalized at the same time? Should there be a differential speed of liberalization in different sectors?

The viability and the stability of the financial sector are crucial for effective intermediation of international finance. Therefore, it becomes increasingly important to ensure a healthy financial system. In particular, the banking system has to be strengthened through appropriate capital adequacy requirements, loan-loss provisions and improved prudential supervision. This assumes greater urgency because, under liberalized financial sector policy regimes, commercial banks may become more vulnerable owing to several factors. Among these are the increasing importance of market-based securities in their portfolios and easier entry of new banks.

The relationship between the private and the public sectors needs to be fundamentally redefined. In an open and liberal environment, the government's role becomes primarily one of creating enabling conditions for the private sector to play the leading role in production and marketing. In some instances, of course, governments may have to take proactive measures for the development of the nascent private sector. Thus, new institutional relationships between the private and the public sectors have to be put in place. The private sector has to be given a greater role in policy design, but at the same time it must not be allowed to capture the regulatory authority of the government to the detriment of public interest.

Governments will have to pay greater attention to a more efficient and transparent administrative and institutional set-up for effective economic governance. It is necessary to establish the appropriate legal framework and enforcement mechanisms to prevent predatory practices and anti-competitive behaviour by both domestic and foreign producers. At the same time, efforts must be made to ensure that red tape and stifling regulations do not hamper private sector initiatives.

Effective participation in the integration process requires a healthy and educated workforce. The acquisition, absorption, diffusion and development of technologies essential to the maintenance of competitiveness would not be feasible without appropriately educated farmers, industrial workers and managers. The need to staff new institutions of various sorts arises. Higher priority will therefore have to be given to human resources development. Improvement in the quality of health and educational services and an extension of their coverage will assume greater importance. In countries with low primary school enrolment ratios and large masses of illiterate adult populations, such as in South Asia, the extension of quality basic education has to receive higher priority. In other cases, where basic education has been available universally for some time, greater attention has to be paid to secondary, tertiary, vocational and technical education. In view of the budgetary implications of expanded public expenditure on human resources development, the scope for recovery of costs, wherever possible, should be explored.

Greater flexibility in labour markets is required in order for entrepreneurs to respond to emerging changes in the trading and investment environment. However, there exists a dilemma in ensuring flexibility in labour markets. The wider access to information strengthens the demand for security of employment, higher wages and other standards of labour welfare applied in developed countries. Thus, countries will have to find ways to strike a balance between the need for flexibility and the avoidance of industrial disputes which policies to introduce flexibility might induce. One measure which could possibly moderate potential disputes is the provision of adequate compensation to displaced workers.

The maintenance of competitiveness in trade necessitates continuous monitoring of international trading conditions and finding niches for the development of new products. It also requires application of improved technologies to reduce production costs and improve the quality of existing export products. Hence, there is a need for training and retraining of labour, research and development

(R & D) and enhancement of institutional capacity within the government machinery to design and implement a system to encourage the private sector to respond to emerging changes. The latter would include the capacity to collect and disseminate relevant information on changes in international demand and supply conditions, technological developments and quality standards. The governments would also need to strengthen their own capacity to formulate and enforce quality standards.

Many developing countries in the region have traditionally used measures such as subsidies, tax breaks, support for R & D, and directed credit as well as tariff and non-tariff protection to diversify production and eventually exports. The obligations under the Uruguay Round impose a degree of constraint on the application of some of these measures. It is important to understand fully the implications of the Uruguay Round with a view to determining the extent and nature of the flexibility available to national governments and design policy regimes accordingly.

The widening and deepening of financial and capital markets is also an important requirement for mobilizing both domestic and international financial resources. In this context, it is worth noting that bond markets in the region remain extremely underdeveloped. Although some countries have experienced rapid growth in stock markets, many of these markets do not have adequate depth or breadth. The thinness of these markets, coupled with substantial foreign participation, makes them more vulnerable to fluctuations in international financial flows. Therefore, attention has to be paid to increasing the depth and breadth of these markets while ensuring that confidence in these markets is retained through appropriate regulatory frameworks and institutional set-ups for monitoring and effective enforcement.

One of the risks associated with FDI is that it involves future payment obligations to outside entities, thus exerting pressure on the balance of payments. It is therefore necessary to adopt policies that encourage reinvestment of profits and investment in export-oriented sectors. The maintenance of macroeconomic stability and the design of an incentive structure consistent with international obligations may help in these respects to some extent. Additionally, these considerations could be built into agreements with transnational corporations, especially in the case of large projects. The implementation of such projects is usually contingent on substantial negotiations between host countries and transnational corporations.

Host countries have to adopt policies that encourage forward and backward linkages between FDI and the rest of the economy in order to maximize the spillover benefits, including technology transfer. The whole range of incentive and performance requirements traditionally employed by many developing countries to achieve this has to be carefully reviewed in the light of developments in the international arena, particularly with respect to TRIPs and TRIMs. The necessary adjustments have to be made in such a way as to allow spillover benefits to be maximized without violating WTO obligations or creating impediments to the inflow of FDI. To deal with some of the other negative consequences of FDI mentioned above, an appropriate legal and regulatory framework has to be established or strengthened with respect to such matters as competition, safety in workplaces, environmental standards and transfer pricing. In cases of investment in sectors with tendencies to give rise to natural monopolies, some regulatory authority may have to be maintained over output volume, quality and pricing decisions. In parallel, enforcement mechanisms have to be strengthened.

A major new development under the Uruguay Round has been GATS. Many elements of the agreement are still under negotiation. The agreement is limited in scope, does not automatically extend national treatment and permits temporary exemptions from MFN obligations. The agreement thus leaves considerable room for flexibility in national policy-making. The countries in the region would need to examine in detail the implications of GATS and formulate appropriate policies for their service industries, some of which are rapidly globalizing.

The extension, maintenance and technological upgrading of the transport and communications infrastructure, so vital to integration with the international and regional economies, will require substantial resources. The countries in the region will therefore have to adopt alternative financing strategies since the traditional reliance on public sector funding will no longer be adequate. Those strategies should include private sector provision of these facilities through such mechanisms as BOT and BOO. Some countries in the region have already made substantial progress in this respect.

The transport and communications sectors are often characterized by externalities and economies of scale and have a tendency to give rise to monopolies. Governments, therefore, will have to strengthen their regulatory capacity to ensure the fulfilment of such objectives as expanded coverage, improved quality and reasonable prices.

Regional/subregional levels

The measures needed at the national level have to be complemented by many actions at the regional/subregional levels, some of which are listed below.

It was observed in chapter III that regional cooperation arrangements, other than ASEAN, do not seem to have made much progress in trade liberalization. The efforts in this direction need to be further intensified while ensuring that the measures adopted would lead to net trade creation. From this perspective, regional cooperation arrangements may wish to consider how they can practise open regionalism to minimize trade diversion. Furthermore, regional cooperation initiatives should strive towards a reasonable degree of equity in the distribution of gains among participating countries to maintain cohesiveness among partner countries.

In order to complement trade liberalization efforts, greater attention has to be paid to trade facilitation through such measures as harmonization of customs classifications, documentation requirements, product standards and environmental and health regulations.

Regional/subregional cooperation arrangements could view respective regions/subregions as a single market space for investment. That would require, in addition to trade liberalization and facilitation measures, greater convergence among participating countries in inflation rates, interest rates and tax levels. A more frequent dialogue among finance ministries and central banks could facilitate such convergence.

The provision of fiscal, financial and other incentives to attract foreign investment is common among developing countries in the region. Sometimes, these are tantamount to "beggar-my-neighbour" policies. Closer collaboration among countries at the regional/subregional levels with a view to harmonizing such incentives could help to avoid revenue losses and other types of losses.

Economic cooperation in the Asian and Pacific region is being stimulated by subregional development zones in various permutations such as growth triangles, quadrangles or polygons. Typically, these zones are informal arrangements covering parts of participating countries and aim at exploiting the complementarities of contiguous areas with the strong involvement of the private sector. To some extent, these operate as multi-country export processing zones and are thus attractive to transnational corporations from outside the participating countries. A few zones are already functioning successfully, and several more are at various stages of implementation. Regional/subregional cooperation could give a boost to such zones.

There could be greater collaboration in providing mutual defence when the exchange rate of a participating country is under strain or when there is a run on the foreign exchange reserve. An initiative towards these ends has been recently launched by a few central banks in East and South-East Asia following the Mexican crisis.

In the area of commodity trading, a number of countries in the region have established or are considering setting up their own futures markets, mainly for major export products to cater for their producers, processors and traders for hedging price risks. However, there is often a lack of sufficient liquidity at the national level to trade commodity contracts efficiently enough for these purposes, and potential international users are attracted only to the most liquid markets. As many of the commodities considered possible candidates for commodity futures contracts are common among groups of countries in the region, some consideration should be given to the possible ways of combining efforts. There are basically two options. One is for those wishing to make use of futures contracts for trade-related purposes to be permitted to trade on the markets of another country where an exchange exists. This is already happening to a limited degree on the Kuala Lumpur Commodity Exchange. The other is to establish a multi-country (electronic) exchange with common contract terms and clearing facilities. While such a move has been initiated for a black pepper contract between India and Malaysia, there are other commodities for which this would appear possible, involving a larger number of countries. There are various modalities for ownership as well as trading methods and clearing procedures which are now feasible using modern electronic communications.

Similar arguments apply in the area of bond and stock markets. Many countries in the region have small stock markets and fledgling bond markets or are in the process of establishing them, including as a complement to their programmes for privatization of public enterprises. However, many of these markets are not functioning well owing, *inter alia*, to lack of depth in terms of the number of firms listed, the value or number of transactions per day, or the persons active in trading. There are also problems of instability in performance, lack of credible rating agencies and underdeveloped accountancy and reporting systems. It would seem appropriate to investigate the feasibility for a small country to list those of its firms that offer stocks or bonds on the market of another country. This has started to a certain extent, mainly on the markets in Hong Kong and Singapore. Alternatively, the idea of a joint stock or bond market set up by a few countries under agreed rules, as has already been done in Central America, should be evaluated. The larger or more established markets in the region which have domestic and international credibility will, of course, continue to be viable and could take the lead in assisting with the above-mentioned proposal.

In addition, for many countries in the region national efforts to establish trade finance (export credit) or investment guarantee schemes run up against the constraint of having limited opportunities to diversify the financial risks involved in the schemes, and so the schemes become nonviable. Joint efforts to develop these facilities by several countries, perhaps on a subregional basis, would increase the probability of their viability. However, the conditions for the success of multi-country efforts are quite stringent and need to be well understood by all parties, particularly in terms of access conditions, codes of behaviour and financial or other rules.

As countries increasingly integrate with the global and the regional economies, the need arises for frequent travels by prospective buyers, sellers, investors, joint venture partners and others in connection with trade and investment. Efforts should therefore be made towards easing visa requirements for business travel. Some countries have already initiated measures in this respect. ASEAN countries allow the entry of visitors from each other without a visa for varying periods of time. Most recently, India announced that Sri Lankan academics, intellectuals and businessmen would qualify for five-year multiple journey visas.

R & D is becoming increasingly characterized by economy of scale. There is thus a need for greater regional/subregional cooperation in R & D by pooling financial, human and technical resources to promote products of interest to participating countries as either exports or imports.

Regional/subregional arrangements should explore ways to fill up missing linkages in transport and communications, as explained in chapter V. They should also produce initiatives to harmonize systems and procedures for cross-border movements of cargo and fleets and to facilitate accession to various international conventions and agreements.

Finally, regional/subregional arrangements should contribute to the maintenance of peace and harmonious political relationships among countries. In recent years, the Asian and Pacific region has been mostly free from armed conflicts between countries. However, there are certain flashpoints. Economic cooperation requires that no conflagration take place.

International level

The international community will have to preserve and improve the environment for developing countries to participate in the globalization/regionalization processes effectively. Some of the ways in which this can be done are suggested below.

The analysis in the preceding chapters has clearly shown that the majority of the least developed and Pacific island countries and the economies in transition have not yet been able to participate meaningfully in the globalization/regionalization processes. This is, in part, because a minimum threshold of development is required before a country can actively partake of the opportunities in international trade or flows of capital. The initial conditions in these countries, characterized by a low level of per capita income, domestic savings and investment make it unlikely that these countries will be able to reach that threshold on their own or to avail themselves of the benefits of globalization/

regionalization. They will continue to need strong support in terms of ODA for the forseeable future. The declining trend in ODA should be urgently reversed.

The above-mentioned groups of countries as well as some of the other developing countries will require considerable technical assistance with training, the establishment of a regulatory framework and the development of institutional set-ups. There is thus a great need for stepped-up technical assistance to those countries, including assistance from developing countries that are in a position to provide it.

A major way in which the international community can assist developing countries' integration into the global economy is to ensure full implementation of the Uruguay Round in respect of market access for developing countries' export products. In this context, particular mention should be made of textiles and clothing. The Asian and Pacific region accounts for more than 40 per cent of world exports of clothing, and for many individual countries in the region, textiles and clothing represent as much as a quarter of manufactured exports. Another matter of concern for some developing countries in the region is that agricultural trade liberalization as a result of the Agreement is likely to be minimal.[2]

There is a growing tendency to link issues such as labour welfare, environment and human rights to trade policies. Such issues should not be misused as non-tariff barriers against developing countries.

Several Asian countries, such as China, India, Indonesia, Malaysia, the Republic of Korea and Thailand, have been targeted for anti-dumping actions by developed countries at one time or the other. Although the Uruguay Round has introduced several features to reduce the protectionist elements of anti-dumping, these have been diluted by other provisions. The use of anti-dumping measures as a protective device should be strongly discouraged, particularly because many developing countries may find it difficult to seek relief through costly dispute settlement procedures. In some instances, some developed countries use their national laws to practise, in effect, managed trade in order to secure a bilateral trade balance. Such practices should be avoided.

The implementation of the Uruguay Round would cause erosion in margins of preferences under GSP, the Lomé Convention or other arrangements. This reinforces the need for avoidance of any non-price restrictions on market access for the exports of developing countries.

At the same time, consideration should be given to improvement of GSP and other preferential market access schemes for products of particular interest to the least developed countries, the Pacific island countries and the economies in transition through the widening of product coverage, the reduction of procedural complexities and the avoidance of frequent changes in schemes.

Concerned by the problems faced by least developed countries, the WTO Ministerial Conference held in Singapore from 9 to 13 December 1996 agreed to a Plan of Action for their benefit. The Plan recognizes the need for diversification of least developed countries' exports and provides for, *inter alia*, duty-free access to their exports on an autonomous basis. The Plan of Action should be implemented urgently.

Home countries of transnational corporations could play a role in encouraging foreign investment in developing countries, particularly on behalf of those that have failed in the past to attract such investment. They could, for example, help to correct misconceptions by disseminating information on the fundamental economic conditions of the host countries, organize investment forums and trade fairs and provide insurance cover for non-commercial risks. They could also assist by actively pursuing bilateral investment treaties and agreements to avoid double taxation.

---

[2] Arvind Panagariya, M.G. Quibria and Narhari Rao, *The Emerging Global Trading Environment and Developing Asia* (Manila, Asian Development Bank, 1996).

Since the 1957 issue, the *Economic and Social Survey of Asia and the Pacific* has, in addition to a review of the current situation of the region, contained a study or studies of some major aspect or problem of the economies of the Asian and Pacific region, as specified below:

1957: Postwar problems of economic development
1958: Review of postwar industrialization
1959: Foreign trade of ECAFE primary exporting countries
1960: Public finance in the postwar period
1961: Economic growth of ECAFE countries
1962: Asia's trade with western Europe
1963: Imports substitution and export diversification
1964: Economic development and the role of the agricultural sector
1965: Economic development and human resources
1966: Aspects of the finance of development
1967: Policies and planning for export
1968: Economic problems of export-dependent countries. Implications of economic controls and liberalization
1969: Strategies for agricultural development. Intraregional trade as a growth strategy
1970: The role of foreign private investment in economic development and cooperation in the ECAFE region. Problems and prospects of the ECAFE region in the Second Development Decade
1971: Economic growth and social justice. Economic growth and employment. Economic growth and income distribution
1972: First biennial review of social and economic developments in ECAFE developing countries during the Second United Nations Development Dacade
1973: Education and employment
1974: Mid-term review and appraisal of the International Development Strategy for the Second United Nations Development Decade in the ESCAP region, 1974
1975: Rural development, the small farmer and institutional reform
1976: Biennial review and appraisal of the International Development Strategy at the regional level for the Second United Nations Development Decade in the ESCAP region, 1976
1977: The international economic crises and developing Asia and the Pacific
1978: Biennial review and appraisal at the regional level of the International Development Strategy for the Second United Nations Development Decade
1979: Regional development strategy for the 1980s
1980: Short-term economic policy aspects of the energy situation in the ESCAP region
1981: Recent economic developments in major subregions of the ESCAP region
1982: Fiscal policy for development in the ESCAP region
1983: Implementing the International Development Strategy: major issues facing the developing ESCAP region
1984: Financing development
1985: Trade, trade policies and development
1986: Human resources development in Asia and the Pacific: problems, policies and perspectives
1987: International trade in primary commodities
1988: Recent economic and social developments
1989: Patterns of economic growth and structural transformation in the least developed and Pacific island countries of the ESCAP region: implications for development policy and planning for the 1990s
1990: Infrastructure development in the developing ESCAP region: needs, issues and policy options
1991: Challenges of macroeconomic management in the developing ESCAP region
1992: Expansion of investment and intraregional trade as a vehicle for enhancing regional economic cooperation and development in Asia and the Pacific
1993: Fiscal reform. Economic transformation and social development. Population dynamics: implications for development
1995: Reform and liberalization of the financial sector. Social security
1996: Enhancing the role of the private sector in development. The role of public expenditure in the provision of social services.

This publication may be obtained from bookstores and distributors throughout the world. Please consult your bookstore or write to any of the following:

1. Sales Section
   Room DC2-0853
   United Nations Secretariat
   New York, N.Y. 10017
   USA

   Tel: (212) 963-8302
   Fax: (212) 963-4116
   Telex: 422311 UN UI

2. Sales Section
   United Nations Office at Geneva
   Palais des Nations
   CH-1211 Geneva 10
   Switzerland

   Tel: (41) (22) 917-1234
   Fax (41) (22) 917-0123
   Telex: 23711 ONU CH

3. Chief
   Conference and General Services Section
   Division of Administration
   Economic and Social Commission for
   Asia and the Pacific (ESCAP)
   United Nations Building
   Rajadamnern Avenue
   Bangkok 10200, Thailand

   Tel: (662) 288-1234
   Fax: (662) 288-1000
   Telex: 82392 ESCAP TH

For further information on publications under this series, please address your inquiries to:

Director
Development Research and Policy Analysis Division
Economic and Social Commission for
Asia and the Pacific (ESCAP)
Rajadamnern Avenue
Bangkok 10200, Thailand

Tel: (662) 288-1610
Fax: (662) 288-1000, 288-3007
Telex: 82392 ESCAP TH, 82315 ESCAP TH
Cable: ESCAP BANGKOK

كيفية الحصول على منشورات الامم المتحدة

يمكن الحصول على منشورات الامم المتحدة من المكتبات ودور التوزيع في جميع انحاء العالم . استعلم عنها من المكتبة التي تتعامل معها أو اكتب الى : الامم المتحدة ،قسم البيع في نيويورك او في جنيف .

如何购取联合国出版物

联合国出版物在全世界各地的书店和分销处均有发售。请向书店询问或写信到纽约或日内瓦的联合国销售组。

HOW TO OBTAIN UNITED NATIONS PUBLICATIONS

United Nations publications may be obtained from bookstores and distributors throughout the world. Consult your bookstore or write to: United Nations, Sales Section, New York or Geneva.

COMMENT SE PROCURER LES PUBLICATIONS DES NATIONS UNIES

Les publications des Nations Unies sont en vente dans les librairies et les agences dépositaires du monde entier. Informez-vous auprès de votre libraire ou adressez-vous à : Nations Unies, Section des ventes, New York ou Genève.

КАК ПОЛУЧИТЬ ИЗДАНИЯ ОРГАНИЗАЦИИ ОБЪЕДИНЕННЫХ НАЦИЙ

Издания Организации Объединенных Наций можно купить в книжных магазинах и агентствах во всех районах мира. Наводите справки об изданиях в вашем книжном магазине или пишите по адресу: Организация Объединенных Наций, Секция по продаже изданий, Нью-Йорк или Женева.

COMO CONSEGUIR PUBLICACIONES DE LAS NACIONES UNIDAS

Las publicaciones de las Naciones Unidas están en venta en librerías y casas distribuidoras en todas partes del mundo. Consulte a su librero o diríjase a: Naciones Unidas, Sección de Ventas, Nueva York o Ginebra.

Printed in Thailand
March 1997 – 2,800

United Nations Publication

ISBN: 92-1-119739-2
ISSN: 0252-5704
ST/ESCAP/1727

- The world economy is experiencing rapid globalization. This is clearly reflected in sharp increases in world trade in goods and services, foreign direct investment and private financial flows as a proportion of world GDP.

- Developing countries in the ESCAP region have become much more integrated with the globalization process. There has been a remarkable increase in their shares in world trade and financial and investment inflows. This has been paralleled by a significant upsurge in intraregional trade and investment flows.

- The process of integration has been uneven. For example, just 12 economies account for 97 per cent of the exports of developing economies of the region and 98 per cent of foreign direct investment inflows. In general, the disadvantaged economies – the least developed, landlocked and Pacific island countries and the economies in transition – remain poorly integrated with the global and regional economies.

- Greater integration offers opportunities for national development through enhanced access to capital, technology and markets for exports, but it also exposes the domestic economies to external shocks such as fluctuation in exchange rates among major currencies, sudden decline in demand for exports and unanticipated reversal of investment and financial flows.

- Policy responses to deal with the challenges have to suit the unique conditions of individual countries. In general, the imperatives at the national level are improved balance in government budgets and the current accounts of balance of payments, appropriately sequenced liberalization of trade, investment and financial sector policies, and upgrading of human resources and institutional capacity. Regional cooperation in trade, investment, finance and transport and communications linkages has to be strengthened. Fair and full implementation of the Uruguay Round agreements is required.

- The structural conditions of the disadvantaged economies pose formidable problems for integration. These economies have to depend heavily on official development assistance to improve their initial conditions. It is disconcerting that ODA as a proportion of GNP of developed countries has been declining: the proportion was 0.27 per cent in 1995, the lowest figure since 1950 and a far cry from the internationally agreed target of 0.7 per cent.