TRADE BETWEEN DEVELOPED AND DEVELOPING COUNTRIES': THE DECADE AHEAD

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INTRODUCTION

Trade between developed and developing countries, and the trade policies of the two groups of countries, are matters of considerable interest. It has been suggested, for example, that this trade should have a central role in any "new round" of GATT negotiations. Yet, it is difficult to find a comprehenseive statement of what the interests of developed and developing countries in trade liberalisation actually are.

This paper aims to define the interests of the developed and developing countries in the liberalisation of their mutual trade. Possible approaches to harnessing these interests for promoting North-South trade in the decade ahead will also be analysed. The context for the discussion is the trade policies of developed and developing countries in the postwar period.

1 TRADE POLICIES AND INTERDEPENDENCE THROUGH TRADE IN MANUFACTURED GOODS

Trade policies of developed countries

In the years following the Second World War, the developed countries reduced their tariffs in the framework of successive rounds of trade negotiations on an item-by-item basis. The negotiations involved a compromise between the principles of reciprocity and of nondiscrimination. With the developing countries offering few tariff concessions, the developed countries exchanged such concessions on products of interest to them.

The developing countries nevertheless benefitted from the tariff reductions that were made under the most-favoured-nation clause. By the early 1960s, tariffs on manufactured goods imported from the developing countries had declined to a considerable extent, although remaining higher than the developed countries' overall tariff average on manufactured goods. (Balassa 1965, Table 2). At the same time, these tariffs showed a tendency towards escalation from lower to higher levels of fabrication, thereby discriminating against processing activities in the developing countries.

In the framework of the Kennedy and the Tokyo rounds of negotiations, tariffs have been reduced substantially across the board, with exceptions made for sensitive items that have included products of interest to developed (steel) as well as to developing countries (textiles). As tariff reductions have again been smaller on manufactured goods imported from the developing countries, post-Tokyo round tariffs on such goods remain somewhat higher than the overall average. The relevant figures are 9 and 7 per cent in the United States, 7 and 6 per cent in the European Economic Community, and 7 and 5 per cent in Japan[1].

There is also a greater frequency of relatively high tariffs on the developed countries' imports from the developing countries than on their overall manufactured imports. Thus, in the United States, tariffs of 10 per cent or higher apply to 20 per cent of imports from developing countries and 9 per cent of overall manufactured imports; comparable figures are 12 and 6 per cent for the EEC and 18 and 13 per cent for Japan. (Cline, 1984; Table 2.1).

Furthermore, although the extent of tariff escalation has been reduced, processing activities in the developing countries continue to suffer discrimination as tariffs are generally nil on unprocessed goods but rise with the degree of fabrication on processed goods. Since the effective rate of tariff on the output exceeds the nominal rate whenever the latter is higher than the tariff on the inputs, relatively low output tariffs may give rise to high effective rates of protection on the processing activity.

Much has been said in recent years about the proliferation of import restrictions that represent non-tariff barriers to trade in the developed countries. The long recession of the years 1980-82 has in fact led to the imposition of some protectionist measures in the United States and in the European Economic Community. However, the pervasive restrictions and the international cartels of the 1930s have not been repeated.

Also, the ire of protectionists has been largely directed against other developed countries and, apart from some tightening of the Multifiber Arrangement, few measures have been taken against developing countries during the recession. At the same time, in the United States, quantitative restrictions on footwear originating in developing countries have been abolished. (Balassa and Balassa 1984).

Thus, the deceleration of the growth of manufactured imports from the developing countries can be attributed to the decline in GNP growth rates in the developed countries rather than to increased protection. In fact, the apparent income elasticity of demand for manufactured goods imported from the developing countries (the ratio of the rate of growth of these imports to that of GNP) continued to increase (Table 1)[2]. Similar conclusions are reached if one considers the share of imports from the developing countries in the apparent consumption of manufactured goods (production plus imports minus exports) in the developed countries. This ratio increased from 0.9 per cent in 1973 to 1.5 per cent in 1978, and again to 2.0 per

Table 1. Changes in the volume of trade in manufactured goods between developed and developing countries, related to changes in GNP[a]

	Average annual rate of growth		Apparent income elasticity[b]
	Imports	GNP	
Industrial countries			
1963-73	6.5	4.6	3.6
1973-78	0.2	2.5	4.1
1978-81	8.4	2.0	4.2
1973-81	9.5	2.3	4.1
Developing countries			
1963-73	8.2	6.2	1.3
1973-78	12.5	5.3	2.4
1978-81	8.3	2.4	3.5
1973-81	11.7	4.2	2.8
Oil-importing developing countries			
1973-78	7.2	4.1	1.8
1978-81	9.5	4.3	2.2
1973-81	8.1	4.2	1.9
Oil-exporting developing countries			
1973-78	24.2	8.2	3.0
1978-81	6.9	−1.6	−4.3
1973-81	17.4	4.4	4.0

a) This table contains revised GNP growth rates for the developing countries.

b) The apparent income elasticity has been calculated with respect to GNP. rather than national income. Where terms of trade changes have been important, as for the oil-exporting countries in particular, these two measures can diverge substantially.

Source: Bela Balassa, "Trends in International Trade in Manufactured Goods and Structural Change in the Industrial Countries," invited paper prepared for the 7th World Congress of the International Economic Association on Structural Change, Economic Interdependence, and World Development, held in Madrid, Spain on September 5-9, 1983.

cent in 1981, with incremental shares (the ratio of increases in imports to increases in apparent consumption) rising from 2.4 per cent in 1973-78 to 3.8 per cent in 1978-81 (Table 2).

Notwithstanding some tightening of the Multifiber Arrangement, the developing countries also succeeded in raising their share in developed country markets for textiles and clothing. This result indicates the success of the developing countries in circumventing the restrictions imposed by the developed countries on textiles and clothing. This has occurred through upgrading as well as through the shift of exports to products, and the shift of the place of production to countries which are not subject to restrictions.

More generally, while the expansion of exports has been constrained by existing import restrictions as well as by the threat of the imposition of restrictions, the process of diversification in the developing countries has permitted them to increase their shares in developed country markets for manufactured goods in an unfavourable world environment. Thus, the success of the developing countries in exploiting the possibilities available in developed country markets has been determined to a great extent by the policies applied by the developing countries themselves.

The policies followed by the developing countries have also affected their ability to export primary commodities. But developed country policies have also had important effects. Foods produced in developing countries which compare with domestic production in the developed countries encounter barriers in these countries and often have to compete with their subsidised exports. The Common Agricultural Policy of the EEC as well as Japanese restrictions affect, in particular, sugar, cereals, vegetable oils and oilseed, beef and veal, wine, and tobacco; while the United States limits the importation of sugar and, to a lesser extent, oilseeds.

It has been estimated that a 50 per cent reduction in the developed countries' trade barriers on foods would lead to an 11 per cent increase in the exports of these commodities from the developing countries. (Valdez and Zietz, 1980). This figure understates, however, the impact of the developed countries' agricultural policies on developing country food exports by excluding the effects of export subsidies. Yet subsidies to food exports have increased over time, in particular in the European Economic Community, contributing to a decline in the world market shares of the developing countries.

Thus, the policies applied by the developed countries have retarded the growth of food exports from the developing countries, which did not surpass the 1973 level in 1981. In the same period the exports of raw materials declined slightly as the recession in the developed countries affected developing country exporters of these products more than proportionately[3].

But the policies applied in many developing countries have also discriminated against their own export of primary products. While an increasing number of developing countries have come to provide incentives to manufactured exports, such measures have rarely been used in favour of primary commodities.

Trade policies of developing countries

In the early postwar period, the dominant development strategy pursued by the developing countries involved import substitution in the manufacturing sector behind high protective barriers. This strategy favoured manufacturing activities producing for domestic markets and discriminated against manufactured as well as primary exports, and against primary production in general.

In the first half of the 1960s, Korea, Singapore, and Taiwan joined Hong Kong in pursuing an outward-oriented development strategy. Under this strategy, similar incentives are provided to exports and to import substitution as well as to primary and to manufacturing activities.

As the possibilities for import replacement in the narrow markets of developing countries were increasingly exhausted, and the high economic cost of continued import substitution came to be recognized, several large Latin American countries, including Argentina, Brazil, and Mexico, began to promote manufactured exports. Nevertheless, discrimination against primary activities was generally maintained and import substitution continued to be favoured, albeit to a lesser extent than beforehand, in these countries. Furthermore, several other countries, such as India, Chile, and Uruguay, continued to pursue an inward-oriented development strategy.

Available information for the decade prior to the quadrupling of oil prices in 1973-74 indicates the effects of alternative development strategies on exports and on economic performance in the countries under consideration. The first mentioned group of Far Eastern countries exhibited rapid growth in the exports of both primary and manufactured goods. Export expansion, together with low incremental capital-output ratios (ICORs) associated with efficient resource allocation, further led to rapid economic growth in these countries.

The second group of Latin American countries improved their export performance in manufactured, but generally not in primary, products; they were successful in reducing their ICORs, although these ratios remained above the levels observed in Far Eastern countries; and they accelerated their economic growth without, however, attaining the growth rates observed in the Far East. Finally, countries which continued to pursue import substitution oriented policies exhibited low export growth rates, low investment efficiency, and poor economic performance in general. (Balassa 1978).

The adverse effects of external shocks, in the form of the quadrupling of oil prices of 1973-74 and the world recession of 1974-75, were especially pronounced in the Far Eastern newly-industrialising countries that had higher than average export and import shares in national income. These countries nevertheless continued to apply outward-oriented policies and were able to surmount the effects of external shocks within a relatively short time. Thus, they increased their export market shares and reached economic growth rates even higher than in the period prior to 1973. The outward-oriented NICs also limited reliance on external borrowing, thereby avoiding excessive foreign indebtedness.

In an effort to maintain past economic growth rates, most other newly-industrialising countries relied greatly on external borrowing after 1973 while increasing the protection of their domestic industries. With higher protection leading to losses in export market shares and to a deterioration in the efficiency of investment, the borrowed funds were generally not used productively. Correspondingly, these inward-oriented NICs experienced a decline in GNP growth rates while their debt burden increased to a considerable extent (Balassa 1981a).

Similar conclusions apply to the oil-importing less developed countries. On the whole, countries following relatively outward-oriented development strategies relied to a lesser extent on foreign borrowing, put the borrowed funds to better use, and reached higher rates of export and GNP growth than countries pursuing an inward-oriented development strategy (Balassa 1984).

Various considerations explain these results. Given their high export and import shares, countries pursuing an outward-oriented development strategy had a greater latitude in reducing imports. By contrast, under inward orientation imports had already been limited to an absoluteiy necessary minimum, with further reductions leading to a decline in output.

The flexibility of the national economy is also greater under an outward-oriented, than under an inward-oriented, development strategy. In the former case, firms have been exposed to competition in world markets and have acquired experience in changing their product composition in response to shifts in foreign demand. By contrast, under inward orientation, there is generally limited competition in the confines of domestic markets and firms have little inducement to innovate, which is necessary under outward orientation in order to meet competition from abroad.

Finally, the low degree of discrimination against primary activities and cost reductions through the exploitation of economies of scale in export industries contribute to efficient exporting and import substitution in outward-oriented economies. By contrast, under inward-orientation, import substitution becomes increasingly costly, thereby lowering the efficiency of investment.

Preliminary results indicate that outward-oriented economies have also been better able to surmount the second oil shock of 1979-80 and the ensuing world recession than inward-oriented economies. The former group of countries has again gained export market shares and has succeeded in limiting the decline in rates of economic growth. in turn, the latter group has further lost market shares, experienced low economic growth rates, and suffered the effects of higher interest rates on their large external indebtedness. (Balassa 1984).

Trade in manufactured goods between developed and developing countries

Data on trade in manufactured goods between developed and developing countries provide an indication of growing interdependence between these groups of countries over the past two decades. Parallel with the increases in the imports of manufactured goods by developed countries from the developing countries, the developing countries expanded their imports of these products from the developed countries (Table 1). Increases in developing country imports were financed through higher export earnings, in particular through the growth of manufactured exports to the developed countries, as well as through foreign borrowing. In 1981, however, a slowdown occurred as several large oil-importing developing countries experienced

Table 2. **Trade in industrial commodity groups between developed and developing countries**

	1973		1978		1981		1973-78		1978-81	
	X_{LDC}/P	M_{LDC}/C	X_{LDC}/P	M_{LDC}/C	X_{LDC}/P	M_{LDC}/C	$\Delta X_{LDC}/\Delta P$	$\Delta M_{LDC}/\Delta C$	$\Delta X_{LDC}/\Delta P$	$\Delta M_{LDC}/\Delta C$
Developed Countries										
Iron and steel	3.5	0.4	5.0	0.5	6.5	1.0	7.3	0.7	17.5	4.8
Chemicals	3.4	0.4	4.6	0.6	4.9	0.7	5.9	0.7	5.8	1.0
Other semi manufactures	1.1	1.0	2.5	1.6	3.0	1.5	6.5	3.4	5.2	1.1
Engineering products	3.7	0.5	7.0	1.0	8.7	1.5	11.2	1.6	15.9	3.8
Textiles	2.8	1.3	3.6	2.7	5.0	3.0	5.6	6.1	17.2	6.3
Clothing	0.9	6.0	1.7	10.9	2.6	14.4	3.2	19.6	12.2	41.5
Other consumer goods	1.2	1.4	2.3	2.4	3.3	3.3	3.6	3.5	7.8	7.5
Total manufacturing	2.9	0.9	5.2	1.5	6.4	2.0	8.5	2.4	11.3	3.8
	1973		1978		1981		1973-78		1978-81	
	X_{DC}/P	M_{DC}/C	X_{DC}/P	M_{DC}/C	X_{DC}/P	M_{DC}/C	$\Delta X_{DC}/\Delta P$	$\Delta M_{DC}/\Delta C$	$\Delta X_{DC}/\Delta P$	$AM_{DC}/\Delta C$
Developing Countries										
Iron and steel	3.6	24.6	3.3	25.2	5.1	27.0	3.1	25.7	10.0	31.8
Chemicals	3.3	21.5	4.0	25.8	4.9	27.1	4.7	29.5	6.9	29.9
Other semi manufactures	7.4	8.0	10.3	15.1	8.0	14.9	**15.5**	26.4	3.1	14.6
Engineering products	6.1	34.7	8.6	43.0	13.7	51.1	10.4	47.9	46.1	80.9
Textiles	4.0	8.7	7.1	9.6	7.3	11.9	11.7	11.0	8.1	22.2
Clothing	36.8	7.4	55.9	14.6	58.3	17.6	78.0	32.2	63.5	24.6
Other consumer goods	12.1	10.1	17.9	16.9	20.1	19.7	22.8	22.6	24.6	25.4
Total manufacturing	7.3	21.3	10.4	29.6	12.5	33.3	13.3	36.5	19.5	44.0

Explanation of Symbols: X = exports, M = imports, **P** = production, C = consumption, DC = developed countries, LDC = developing countries.

Note: The production estimates for the developing countries are subject to considerable error possibilities. Also, the estimates for 1973 have been obtained through interpolation of the reported figures for 1970 and 1978 while the 1981 estimates have been derived through extrapolation by the use of production indices.

Source: Bela Balassa, "Trends in International Trade in Manufactured Goods and Structural Change in the Industrial Countries," invited paper prepared for the 7th World Congress of the International Economic Association on Structural Change, Economic Interdependence, and World Development, held in Madrid, Spain on September 5-9, 1983; and UNIDI, ***Handbook*** of ***Industrial Statistics,*** New York, United Nations, 1982.

growing difficulties in obtaining foreign loans. Following rapid increases in earlier years the rate of growth of manufactured imports by the oil-exporting developing countries also declined, reflecting a slowdown in the growth of their export earnings.

Nevertheless, the share of the developed countries in the apparent consumption of manufactured goods in the developing countries, taken together, continued to increase throughout the period under consideration. According to rough estimates made by the author that represent only general orders of magnitude, this ratio rose from 21.3 per cent in 1973 to 29.6 per cent in 1978 and to 33.3 per cent in 1981, with incremental shares increasing from 36.5 per cent in 1973-78 to 44.0 per cent in 1978-81 (Table 2). Not surprisingly, import shares are the highest for engineering products; in 1981, the developed countries provided slightly over one-half of the apparent consumption of the developing countries in these products.

With rapid increases in their imports, the developing countries assumed growing importance as markets for the manufacturing industries of the developed countries. Thus, the share of exports to the developing countries in the developed countries' production of manufactured goods increased from 2.9 per cent in 1973 to 5.2 per cent in 1978 and to 6.4 per cent in 1981. Incremental shares were even higher, 8.5 per cent in 1973-78 and 11.3 per cent in 1978-81 (Table 2).

Despite these increases, the ratio of manufacturing production in the developing countries to that in the developed countries remained relatively low; 13.9 per cent in 1973, 15.0 per cent in 1978, and 15.6 per cent in 1981[4]. Correspondingly, notwithstanding the continued imbalance of trade in manufactured goods between the two groups of countries, export-production ratios continued to be substantially higher in the developing than in the developed countries.

According to the author's rough estimates, the share of exports to developed countries in the production of manufactured goods in the developing countries increased from about 7.3 per cent in 1973 to 10.4 per cent in 1978 and to 12.5 per cent in 1981, with incremental shares of 13.3 per cent in 1973-78 and 19.5 per cent in 1978-81 (Table 2). In 1981, export shares were the highest in clothing, followed by the group of other consumer goods. Export shares were higher than average also for engineering products. This performance reflects in part the success of the developing countries in exporting labour-intensive engineering products, such as radios and television sets, and in part increased intra-industry specialisation, with the developing countries exporting labour-intensive, and importing capital-intensive, parts, components, and accessories.

II. MULTILATERAL TRADE LIBERALISATION AND THE INTERESTS OF DEVELOPED AND DEVELOPING COUNTRIES

Trade liberalisation in developing countries and developed country interests

in gauging the interests of the developed countries in trade liberalisation by the developing countries, it is necessary to assess how liberalisation would affect the volume and the pattern of developed country exports. This question will be considered in regard to trade with the newly-industrialising countries (NICs) which account for the overwhelming share of the developed countries' manufactured imports from the developing countries, which provide the largest markets for their manufacturing industries, and which have been exhorted by the developed countries to liberalise their trade.

The NICs protect their manufacturing industries by the use of tariffs and quantitative import restrictions. Quantitative restrictions came into greater use after 1973 in conjunction with the increased inward orientation of a number of the NICs and, again, after 1979 in attempting to cope with their increased debt burden. Import restrictions are applied even in outward-oriented NICs, with the exception of Hong Kong and Singapore, although these have much more limited scope and are administered in a more liberal fashion that in inward-oriented NICs.

Several years ago, an OECD report expressed the fear that a newly-industrialising country "may find itself moving into surplus on current account when in fact the availability of external capital and the possibilities for its profitable use would have permitted higher levels of domestic activity and consumption." (OECD, 1979, p.57). This fear has not been realised and no newly-industrialising country has accumulated excessive foreign exchange reserves. These countries have few possibilities, therefore, to draw on their foreign exchange reserves while, under present conditions, most NICs may not increase their foreign debt.

It follows that reductions in trade barriers by the NICs could not give rise to higher imports unless their exports are simultaneously increased. Excluding such a possibility for the time being, the relevant issue is how the composition of imports would be affected. This will be considered first for manufactured goods alone.

The NICs use import restrictions to save foreign exchange as well as to protect their domestic industry. They limit the imports of non-durable consumer goods that are produced locally, but demand for variety and for luxury goods creates demand for imports. The NICs also protect their incipient industries producing intermediate goods (iron and steel, chemicals, and other semimanufactures) and relatively simple engineering products (electrical and non-electrical machinery and transport equipment).

As a result of the application of protectionist measures, the share of consumer goods and intermediate products in the imports of the developing countries from the developed countries declined in recent years whereas the share of machinery and machine tools used in their manufacture, which dominate the engineering goods category, increased to a considerable extent. Correspondingly, the liberalisation of trade by the NICs would lead to increases in the imports of nondurable consumer goods, intermediate products, and simple engineering goods and to a decline in the imports of sophisticated machinery and machine tools necessary for their domestic production.

This conclusion needs to be qualified by reference to cases where NICs have made a push into technologically-advanced products. Examples are personal aircraft and simple computers in Brazil. It is such instances that have evoked the ire of U.S. exporters who have seen markets closing to them. But the vociferous complaints should not mask the fact that these commodities are few in number, so that their existence does not introduce a major modification in the argument.

One needs to consider, however, possible changes in the importation of primary commodities. Since these commodities are rarely protected by the NICs, their imports would decline, and the importation of manufactured goods – largely from the developed countries – correspondingly increase, following reductions in protection.

Reductions in primary product imports by the NICs would adversely affect the deveioped countries as well as the less developed countries (LDCs), since some of these commodities are exported by developed countries and others by LDCs. But, in the latter case, too, there would be a decline in the export earnings of the developed countries,, owing to reduced purchases of their products by the adversely-affected LDCs. Thus, ultimately, any increases in the manufactured exports of the developed countries to the NICs would be offset by reductions elsewhere, *so* long as the export receipts of the NICs remained unchanged.

Next, consider the case where the NICs expand their exports, so as to obtain foreign exchange for increasing their imports upon the liberalisation of trade. This is indeed the expected consequence of trade liberalisation that reduces the bias of the system of incentives against exports. For one thing, the cost of domestically-produced inputs will decline; for another thing, the exchange rate will tend to depreciate in order to equilibrate the balance of payments following the liberalisation of imports.

Part of the increase in the exports of a particular newly-industrialising country would find markets in other NICs as they liberalise their own trade. This will not improve, however, the net foreign exchange position of the developing countries, taken together. At the same time, increased imports from the developed countries will have to be paid for by higher exports to them.

Thus, while trade liberalisation will change the pattern of the NICs imports from the developed countries, increases in these imports would necessitate a corresponding rise in exports. The same result may be achieved if the developed countries liberalise their imports, since the NICs – and developing countries in general – use their increased foreign exchange earnings to buy goods from the developed countries.

It follows that many of the economic benefits the developed countries may derive from trade liberalisation by the NICs can also be obtained if the developed countries liberalise their own trade. The question arises, then, why the developed countries demand that the NICs liberalise their imports.

Part of the answer lies in the desire for stability, i.e. the wish to avoid sudden interruptions in exports due to the unanticipated imposition of restrictions by the NICs. Similar considerations explain opposition on the part of developed countries to the provision of export subsides by the NICs, which lead to encroachment on developed country markets and disturb existing trade patterns in third countries.

A more general consideration is the national power of decision-making. The developed countries wish to influence the composition of their manufactured imports, rather than being subject to decisions taken by the NICs. A related issue is the popular belief that reductions in foreign trade barriers represent a "benefit" and reductions in the country's own trade barriers a "cost" to the country concerned. Finally, there is the equally popular "fairness" argument, according to which benefits should not be provided unilaterally to countries that are able to "carry their own weight".

These considerations indicate the importance of domestic political factors in motivating demands in the developed countries for trade liberalisation by the NICs. In this connection, it has been claimed that the NICs could obtain better conditions of market access in the developed countries if they liberalised their own trade. But this argument should not be carried too far, since it would imply that Hong Kong, with its free trade policies, would receive the most favourable treatment among developing countries. In fact, Hong Kong's exports suffer more discrimination than those of perhaps any other NIC[5]. Nor does Singapore receive special treatment by reason of its liberal trade policy.

It may be suggested, however, that it is in the interest of the developed countries that the NICs participate in the GATT process and operate within the GATT rules of conduct. This would, however, require some reconsideration of present GATT procedures – as suggested below.

An additional consideration is that trade liberalisation by the NICs is in the interest of the LDCs. This is the case because the LDCs are evolving a comparative advantage in simple nondurable consumer goods, such as clothing and shoes, and should be able increasingly to enter the markets of NICs, just as the NICs have earlier done in the markets of Japan.

Trade liberalisation by the NICs would thus contribute to the industrialisation of the LDCs, in line with the stages approach to comparative advantage. (Balassa 1979). This is indeed a desirable objective, although it should not be forgotten that the markets for nondurable consumer goods are many times larger in the developed countries than in the NICs. Thus, "second tier" exporters would derive considerable benefit from trade liberalisation by the developed countries.

But the principal argument for reductions in trade barriers by the NICs lies in their own self-interest. This is because, as we have seen, the adoption of an outward-oriented development strategy leads to improvements in the efficiency of resource allocation and rapid economic growth. Economic growth, in turn, will eventually make the NICs full-fledged partners of the developed countries. At the same time, providing secure access to developed country markets will increase incentives, and reduce domestic opposition, to liberalising trade in the NICs.

The discussion has centered on the newly-industrialising countries, in regard to which demands for trade liberalisation and "graduation" have been made. This is not to say that the less developed countries would not benefit from liberalising their own trade. In fact, as noted above, outward-oriented less developed countries showed a much better performance than inward-oriented LDCs during the 1973-78 period of external shocks. Still, infant industry arguments provide more of a rationale for protection in the LDCs than in the NICs.

Trade liberalisation in developed countries and developing country interests

At the GATT Ministerial meeting in November **1982,** proposals were made for a North-South round of trade negotiations, under which developed countries would make tariff concessions to the developing countries on a preferential basis in exchange for the developing countries' liberalising their imports on a most-favoured-nation basis. The emphasis was on trade liberalisation by the NICs, which would, however, enjoy only temporary preferences that would cease upon "graduation".

The proposal evoked little interest on the part of the NICs, and understandably so. In the language of trade negotiations, these countries were asked to offer concessions to reduce their tariff and nontariff barriers in exchange for temporary tariff preferences, losing their GSP status in the process, while the developed countries liberalised their own non-tariff barriers. In order to discern the elements of an equitable bargain between the two groups of countries, the interests of the NICs in the liberalisation of trade by the developed countries need to be examined.

Tariff reductions by the developed countries would bring benefits to the LDCs, which are major producers of foods and raw materials they could increasingly export in a processed form once the escalation of tariffs is removed. The benefits would be smaller for the NICs that tend to export the products of "footloose" industries (e.g. relatively simple engineering products), and products made of imported materials (e.g. textiles and clothing), so that they suffer little discrimination due to the escalation of tariffs.

For the NICs, existing and potential non-tariff barriers in the developed countries represent the most important obstacles to trade. Notwithstanding the efforts made by the NICs to evade the MFA, the expansion of their textiles and clothing exports is constrained by the provisions of the 1981 Agreement, and they are subject to the limitations introduced subsequently on the importation of these products in the United States. Also, the NICs generally are adversely affected by restrictions on steel imports imposed by the EEC, and Brazil by U.S. limitations on steel imports from that country.

At the same time, the danger of the imposition of restrictions, whether in the form of quantitative import restrictions, export limitations, and countervailing or antidumping duties of a protective intent, creates a risk for the NICs and discourages investment in their export industries. In fact, in the United States, demands for the imposition of restrictions have reportedly been made in large part for their nuisance value, i.e. to discourage developing countries from exporting.

It may be added that the developed countries would also derive benefits from the liberalisation of their own trade. Such benefits stem from the upgrading of the labour force, the exchange of high-skill for low-skill products in trade with the developing countries, the spreading of research and development expenditures over a larger output, and the anti-inflationary effects of imports.

Trade negotiations between the developed countries and the newly industrialising developing countries

The above discussion concerning the interests of the developed countries and the NICs in trade liberalisation leads to a possible policy package that would combine the perceived objectives of the two groups of countries. Such a package would include lowering tariffs, reducing export subsidies, dismantling quantitative import restrictions, establishing an effective safeguard code, reforming the GATT review mechanisms and, more generally, giving a greater role to the developing countries in the GATT.

The last point underlies the importance of GATT, which provides the only appropriate venue for negotiating the liberalisation of trade. Negotiations would need to be carried out on a multilateral basis as bilateral approaches would be counterproductive by leading to charges of ***divide et impera.*** Nor would it be appropriate to provide special privileges, as has been suggested, to countries with high indebtedness.

There is a further argument for multilateral negotiations that transcends North-South relationships. This is the need to avoid the backsliding that is likely to occur in the absence of a new round of multilateral negotiations. As first stated sixteen years ago:

> "It would ... appear that if no efforts are made to liberalise trade, the alternative is likely to be increased protectionism rather than the maintenance of the status

quo. For lack of a better expression, we may speak of an "instability effect", according to which economic and political relationships are hardly ever in a position of stable equilibrium but have the tendency to move in one direction or andother. Thus, in the absence of pressures for the liberalisation of trade, protectionist counterpressures may gain force in the United States as well as abroad." (Balassa, 1967, p. 15).

Backsliding has in fact occurred in recent years, particularly insofar as trade among the developed countries is concerned. Thus, these countries would derive additional benefits from a new round of multilateral trade negotiations. Nevertheless, the negotiations may appropriately focus on North-South relationships. This would represent a change from the past pattern, when the developed countries negotiated among themselves and the developing countries were the passive observers.

The principal participants in the negotiation would be the OECD countries and the NICs. Using per capita incomes and the share of industry in national income as classification criteria, the NICs may be defined to include Argentina, Brazil, Mexico, Uruguay, Israel, Yugoslavia, Hong Kong, Korea, Singapore, and Taiwan. Issues related to negotiations with Mexico and Taiwan, which are not members of GATT, will be taken up below.

III. MODALITIES FOR NORTH-SOUTH TRADE NEGOTIATIONS

Steps towards a North-South round of trade negotiations

Trade liberalisation would create adjustment problems in the NICs as well as in the developed countries. But the time involved in the negotiations would ease the process of adjustment. Experience indicates that multilateral trade negotiations take several years following the completion of the preparatory phase. Also, the implementation of the agreement customarily involves a period of four or five years.

Nor should the difficulties several of the NICs presently experience in servicing their external debt be used as arguments against undertaking the negotiations. Considering the length of the preparatory period, it can be safely said that by the time the liberalisation of trade begins not only will these problems be overcome but the NICs will have proceeded to higher levels of economic development.

According to estimates published by the World Bank, the Gross Domestic Product of the middle-income oil importing countries will rise at an average annual rate of 4.5 per cent between 1982 and 1985 and by 4.4 to 6.9 per cent between 1985 and 1995, with a central value of 5.7 per cent. The corresponding per capita income growth rates can be derived by adjusting for expected population growth rates of 2.2 per cent. (World Bank, 1983, p.27).

However, during the 1960s and the 1970s, most of the NICs were growing at rates much in excess of the average for the middle-income oil importing developing countries. For these countries, 1990 per capita incomes have been estimated by assuming that, after stagnation in 1982-83, they would regain their past growth rates. In turn, it has been assumed that the NICs which had below-average growth rates in the 1960-81 period (Argentina, 1.9 per cent; Chile 0.7 per cent; Israel, 3.6 per cent; and Uruguay 1.6 per cent) would reach the central variant growth rate projected for the middle-income oil importing countries.

Under the stated assumptions, by 1990 the Latin American newly industrialising countries, Korea, and Yugoslavia would approximately reach Italy's 1960 and Japan's 1963 per capita incomes. In the same year, Hong Kong, Israel, and Singapore would surpass Italy's 1980 and Japan's 1975 incomes per head.

Two observations may be made in regard to these estimates. First, the per capita income levels the NICs are expected to reach towards the end of the decade would impose certain obligations on them in regard to their trade policy vis-a-vis developed as well as less developed countries. Second, and more important, these countries could accelerate their economic growth if they reformed their trade policies.

The content of the negotiations

As far as the obligations to be taken in the course of the negotiations are concerned, it would be desirable, first of all, that the developed countries reduce their overall tariff level and lessen the extent of tariff discrimination against the processing of primary commodities by the developing countries. In turn, the NICs should lower the level, and rationalise the structure, of their tariffs.

There is further need to reduce export subsidies. In the developed countries, subsidies are provided mainly to agricultural exports while in the NICs industrial exporters are the main beneficiaries. In inward-oriented NICs, export subsidies are designed to reduce the bias against exports associated with industrial protection. With reform of the system of protection, this rationale would largely disappear.

More important than tariff reductions is the liberalisation of quantitative import restrictions. It would be desirable that the developed countries gradually phase out the MFA as well as their restrictions on steel imports. Also, agricultural policies would need to be reformed, involving reductions in the protection afforded to agriculture. In turn, the NICs would take the obligation to phase out their own import restrictions. As a result of these changes, the developed countries as well as the NICs would place exclusive reliance on tariffs as measures of protection.

The proposed reforms would need to be accompanied by the establishment of an effective system of safeguards. The principal requirement for such a system is the assurance that safeguards are of a temporary character. This would necessitate setting time limits for the unilateral application of safeguards, with any further extension requiring the consent of a multilateral forum associated with the GATT. Extensions would be countenanced only in exceptional circumstances and made dependent on a plan for domestic adjustment.

An important part of the proposed safeguard mechanism would be the role assigned to the multilateral review process. More generally, the dispute settlement mechanism in the GATT would need to be strengthened and rendered more effective. The developed countries have special responsibility both to initiate cases before the GATT, when they consider that they have been injured by actions taken abroad, and to accept the conclusions of the review process, when their actions are found to have caused injury elsewhere.

In the review process, a greater role would need to be given to the NICs and to the developing countries in general. But this will depend to a considerable extent on the developing countries themselves; in particular, subscribing to the codes established in the framework of the Tokyo Round negotiations is a precondition for participation in the dispute settlement mechanism in regard to these codes.

Giving a greater role to the developing countries in the GATT also presupposes their willingness to participate in GATT affairs. The NICs could also caucus together, with a view to developing common positions in the GATT, in general, and for a North-South round of negotiations in particular.

The adjustment problem

It has been noted that the time involved for the preparation of the negotiations, the negotiations themselves, and the gradual liberalisation of trade barriers would provide considerable opportunity for adjustment. But, for adjustment to be successful, it would be desirable for the countries involved to begin taking appropriate measures in advance of the negotiations.

In the developed countries, the adjustment measures should be part of a long-term policy towards declining industries – in particular agriculture, clothing, shoes, and steel – aimed at encouraging the movement of resources from these industries to modern sectors. Thus, adjustment assistance to workers should focus on retraining and relocation while compensation for income losses would be made under regular social security provisions. In turn, firms that reduce their productive capacity in the industries in question might receive credits for purposes of establishment in other industries.

In some highly-protected NICs, the adjustment effort could be greater than in the developed countries. But the character of adjustment will not necessarily be the same. Thus, firms might receive assistance to improve their technology, to increase specialisation, and to adopt large-scale production methods while remaining in the same industry.

The World Bank and the IMF might play a role in promoting adjustment in the newly-industrialising countries. This is done to a certain extent today and could be stepped up in the future. The IMF, and the World Bank in its programme lending, **also** often include import liberalisation as a loan condition. Again, a further extension of this practice would be desirable, so that the process of liberalisation begins prior to the North-South negotiating round.

CONCLUDING REMARKS

Having reviewed changes over time in international trade between developed and developing countries, this paper has considered the interests of the two groups of countries in the liberalisation of their mutual trade. Proposals have further been put forward for a strategy that may be followed in regard to the modalities and the content of trade negotiations. No attempt has been made, however, to provide detailed recommendations on 'the conduct of the negotiations or to examine the impact of trade liberalisation on individual countries within the two groups.

While the paper has concentrated on the gains developed and developing countries may derive from reciprocal trade liberalisation, one should emphasise the interests of the developed countries and of the newly industrialising countries in liberalising their own imports. In fact, the governments of these countries could utilise the opportunity provided by the proposed North-South trade negotiations to overcome domestic protectionist pressures. This is analogous to the case where reformers in developing countries rely on the World Bank and the **IMF** to demand the implementation of policies they favour.

At the same time, the existence of an asymmetry between the developed and the developing countries should be noted. As the developing countries spend all of their foreign exchange earnings on goods imported from the developed countries, trade liberalisation by the latter group of countries would not adversely affect their payments balances. In turn, in liberalising their trade, the developing countries would have to find markets for their exports so as to pay for the increased imports.

Correspondingly, while their national interest, as well as the interests of the world economy, demand that the NICs reduce their trade barriers, they would have to be provided with security of market access in the developed countries. This fact, then, puts a particular responsibility on the developed countries to take adjustment measures that would permit liberalising their trade.

NOTES

1. Balassa and Balassa (1984) Table 1 – Isaiah Frank suggests however that these figures are misleading as average tariffs on imports from the developing countries are raised by the large imports of textiles and clothing that are subject to relatively high tariffs but are effectively limited by quantitative restrictions rather than by tariffs.
2. Manufactured industries are defined according to the convention used in trade statistics, i.e. excluding food, beverages, tobacco, petroleum products, and nonferrous metals.
3. The data refer to the volume of exports of the developing countries to the developed countries. They derive from United Nations, ***Monthly Bulletin of Statistics.***
4. The data have been adjusted according to the definition of the maufaturing sector used here. They originate in UNIDO, ***Handbook of Industrial Statistics.***
5. In an article entitled "America Needles Hong Kong", ***The Economist*** (17th December 1983) reports that the United States issued fourteen suspensions against Hong Kong goods under the MFA in 1983.
6. For a more detailed discussion, see Balassa (1980).

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