

Trade and Development in Advanced Developing Countries and Least Developed Countries: Empirical Patterns and Policy Implications

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Abstract

This article looks at the role of international trade in the process of economic development in some of the world's most advanced developing countries (the MDT countries) on the one side, and the world's least developed countries (LDCs) on the other. The comparison of trade patterns of these two country groups highlights the strong influence that trade may have on the development process. The influence can be a negative one, as is highlighted by the example of the average LDC. In order for the LDCs to size the opportunities that trade may provide them with, the article proceeds to develop recommendations for future trade policies.

Key Words: trade, export competitiveness, import capacities, LDCs, specialization

I. Introduction

The passed decades have witnessed a series of United Nations Systems conferences on distinct aspects of the United Nation's development agenda. These conferences have helped to identify core areas of development cooperation and to better coordinate the activities of development partners. In addition, these conferences have lead to a broad consensus on the core priorities of development activities and the identification of international development goals. At the center of these international development goals stands the objective of halving extreme poverty by the target year 2015 against the base year 1990²⁾.

The achievement of these development objectives, and especially the objective of poverty reduction, requires the attainment of significant economic growth (Karshenas, 2001; UNCTAD, 2002a). Such growth, in turn, depends on a variety of complementary factors

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that are influenced by national and international policies. Amongst these, international trade assumes a key role. This is because trade—export competitiveness and import capacities—can be an important facilitator for capital accumulation and technology transfers. In short, trade is vital for the stimulation of economic growth, the achievement of overall development and the reduction of poverty³.

This paper looks at the role of international trade in the process of economic development in some of the world's most advanced developing countries on the one side, and the world's least developed countries on the other. The advanced developing countries correspond with the countries that are the focus of the MDT project, while the least developed countries are a country group that was identified by the United Nations⁴. The former will be referred to as MDTCs and the latter as LDCs (for a comprehensive categorization of MDTCs and LDCs see annex table 1). The MDTCs and the LDCs are subgroups of the broader developing countries group, which will be contrasted with a developed countries group. The MDTCs and the LDCs are outstanding subgroups of the developing countries group as they represent the two extremes of the development spectrum. With respect to various development indicators, ranging from economic indicators to human development indicators, the MDTCs tend to persistently outperform the broader developing countries group, and the LDCs tend to fall further behind this group (UNCTAD, 2000, 2002a).

The different country groups include very diverse countries, however. The MDTC group for example encompasses the most successful transition economies of Eastern Europe, large

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- 2) The OECD (OECD, 1996) was the first organization to provide a comprehensive list of the different development goals, later other organizations (IMF/OECD/UN/World Bank, 2000) have built on this list. International development goals also entered in the concluding document of the United Nations Millennium Summit, namely the United Nations Millennium Declaration (UN, 2000; UN, 2001a), as well as the final document of the Third United Nations Conference in Least Developed Countries, namely the Third Programme of Action for Least Developed Countries (UN 2001b). There are strong similarities between the development goals cited in the different documents, but there are important differences between them as well. These differences concern the goals themselves, their indicators and base years (for a discussion, see UNCTAD, 2001a, and Herrmann, 2003 forthcoming). But despite these differences there is agreement on one central development objective, namely the development objective to reduce extreme poverty by half by the year 2015 vis-à-vis the base year 1990. Extreme poverty is identified by an international poverty line set at Dollar 1 per day and person in 1985 purchasing power parities (PPP). For a discussion of other development goals see the contribution by Mr. Kawai in this volume.
 - 3) For selected contributions to the debate on trade, poverty and growth, see Birdsall and Hamoudi (2002), Dollar and Kraay (2001), Karshenas (2001), Mayer (2000, 2001), UNCTAD (2000a), Winters (1999, 2001), World Bank (2002a, 2002b).
 - 4) The United Nations identifies the least developed countries on the basis of three core criteria: Low income (measured by GDP per capita), weak human resources (measured by the Augmented Physical Quality of Life Index) and economic vulnerability (measured by the Economic Vulnerability Index). For a detailed discussion of the methodology that is used to identify the least developed countries of the world, see for example UNCTAD (2001a).

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Table 1: Map of MDT project countries and the UN's least developed countries, 2001

	Development level (United Nations)			Income and debt (World Bank)				Industrial development (Amsden 2001)	Trade integration (World Bank 2002b)
	Developing countries (DCs)	Transition economies (TCs)	Least developed countries (LDCs)	Upper-Middle income countries (U-MICs)	Lower-middle income countries (L-MICs)	Low- income countries (LICs)	Highly indebted poor countries (HIPC)	Newly industrialized countries (NIEs)	Countries w/ strong trade integration (Globalizers)
MDT project countries (MDTCs)									
Argentina	DC	..	..	U-MIC	..	..	..	NIE	Globalizer
Brazil	DC	..	..	U-MIC	..	..	..	NIE	Globalizer
Chile	DC	..	..	U-MIC	..	..	..	NIE	..
China	DC	..	..	..	L-MIC	..	..	NIE	Globalizer
Czech Republic	..	TC	..	U-MIC	..	..	..	..	..
Hungary	..	TC	..	U-MIC	..	..	..	..	Globalizer
Indonesia	DC	..	..	..	..	LIC	..	NIE	..
Korea, Rep.	DC	..	..	U-MIC	..	..	..	NIE	..
Malaysia	DC	..	..	U-MIC	..	..	..	NIE	Globalizer
Mexico	DC	..	..	U-MIC	..	..	..	NIE	Globalizer
Poland	..	TC	..	U-MIC	..	..	..	..	..
Russian Federation	..	TC	..	..	L-MIC	..	..	..	..
Thailand	DC	..	..	..	L-MIC	..	..	NIE	Globalizer
13 MDTCs	9 DCs	4 TCs	0 LDCs	9 U-MIC	3 L-MIC	1 LIC	0 HIPC	9 NIEs	7 Globalizers
UN's Least Developed Countries (LDCs)									
Afghanistan	DC	..	LDC	..	..	LIC	..	..	..
Angola	DC	..	LDC	..	..	LIC	HIPC	..	..
Bangladesh	DC	..	LDC	..	..	LIC	..	..	Globalizer
Benin	DC	..	LDC	..	..	LIC	HIPC	..	..
Bhutan	DC	..	LDC	..	..	LIC	..	..	..
Burkina Faso	DC	..	LDC	..	..	LIC	HIPC	..	..
Burundi	DC	..	LDC	..	..	LIC	HIPC	..	..
Cambodia	DC	..	LDC	..	..	LIC	..	..	..
Cape Verde	DC	..	LDC	..	L-MIC	..	..	..	..
Central African Rep.	DC	..	LDC	..	..	LIC	HIPC	..	..
Chad	DC	..	LDC	..	..	LIC	HIPC	..	..
Comoros	DC	..	LDC	..	..	LIC	..	..	..
Congo, Dem. Rep.	DC	..	LDC	..	..	LIC	HIPC	..	..
Djibouti	DC	..	LDC	..	L-MIC	..	..	..	..
Equatorial Guinea	DC	..	LDC	..	L-MIC	..	..	..	..
Eritrea	DC	..	LDC	..	..	LIC	..	..	..
Ethiopia	DC	..	LDC	..	..	LIC	HIPC	..	..
Gambia, The	DC	..	LDC	..	..	LIC	HIPC	..	..
Guinea	DC	..	LDC	..	..	LIC	HIPC	..	..
Guinea-Bissau	DC	..	LDC	..	..	LIC	HIPC	..	..
Haiti	DC	..	LDC	..	..	LIC	..	..	Globalizer
Kiribati	DC	..	LDC	..	L-MIC	..	..	..	..
Lao PDR	DC	..	LDC	..	..	LIC	HIPC	..	..
Lesotho	DC	..	LDC	..	..	LIC	..	..	..
Liberia	DC	..	LDC	..	..	LIC	HIPC	..	..
Madagascar	DC	..	LDC	..	..	LIC	HIPC	..	..
Malawi	DC	..	LDC	..	..	LIC	HIPC	..	..
Maldives	DC	..	LDC	..	L-MIC	..	..	..	..
Mali	DC	..	LDC	..	..	LIC	HIPC	..	Globalizer
Mauritania	DC	..	LDC	..	..	LIC	HIPC	..	..
Mozambique	DC	..	LDC	..	..	LIC	HIPC	..	..
Myanmar	DC	..	LDC	..	..	LIC	HIPC	..	..
Nepal	DC	..	LDC	..	..	LIC	..	..	Globalizer
Niger	DC	..	LDC	..	..	LIC	HIPC	..	..
Rwanda	DC	..	LDC	..	..	LIC	HIPC	..	Globalizer
Samoa	DC	..	LDC	..	L-MIC	..	..	..	..
Sao Tome & Principe	DC	..	LDC	..	..	LIC	HIPC	..	..
Senegal	DC	..	LDC	..	..	LIC	HIPC	..	..
Sierra Leone	DC	..	LDC	..	..	LIC	HIPC	..	..
Solomon Islands	DC	..	LDC	..	..	LIC	..	..	..
Somalia	DC	..	LDC	..	..	LIC	HIPC	..	..
Sudan	DC	..	LDC	..	..	LIC	HIPC	..	..
Tanzania	DC	..	LDC	..	..	LIC	HIPC	..	..
Togo	DC	..	LDC	..	..	LIC	HIPC	..	..
Tuvalu	DC	..	LDC	..	..	..	..	..	..
Uganda	DC	..	LDC	..	..	LIC	HIPC	..	..
Vanuatu	DC	..	LDC	..	L-MIC	..	..	..	..
Yemen, Rep.	DC	..	LDC	..	..	LIC	HIPC	..	..
Zambia	DC	..	LDC	..	..	LIC	HIPC	..	..
49 LDCs	49 DCs	0 TCs	49 LDCs	0 U-MIC	7 L-MIC	42 LIC	31 HIPC	0 NIEs	5 Globalizers

Note: The complete list of newly industrialized countries includes those listed in the table plus India, Taiwan and Turkey (Amsden, 2001); the complete list of "more globalized developing countries" includes those listed in the table plus Colombia, Costa Rica, Dominican Republic, India, Cote d'Ivoire, Jamaica, Jordan, Nicaragua, Paraguay, Philippines, Uruguay and Zimbabwe (World Bank 2002b).

developing economies of Latin America and developing economies of Southeast Asia. But despite differences amongst individual countries within the groups, there are very strong similarities between the countries in each group as well. These similarities concern their development status. The MDTCs—which include many newly industrialized countries—belong to the world's most advanced developing countries, and the LDCs—which mainly include non-oil commodity dependent countries—belong to its most underdeveloped countries (Amsden, 2001; UNCTAD, 2002a).

The developmental success of the most advanced developing countries is associated with manifold factors, including their respective trade policies. But it is not the purpose of this paper to review the trade policies that were pursued by different successful developing countries. By contrast, the paper instead looks at trade patterns that characterized the most successful developing countries. The trade patterns that are characteristic for the most advanced developing countries are then compared with the trade patterns that characterize the least developed countries. The comparison of trade patterns of these distinct country groups highlights the strong influence that trade may have on the development process. This influence can be a positive one, as is shown by the example of the MDTCs, but it can be a negative one as well, as is highlighted by the example of the average LDC. In order for the MDTCs to further strengthen the positive influence that trade has on their development, and in order for the LDCs to seize the opportunities that trade may provide them with, the paper proceeds to develop recommendations for future trade policies. These recommendations are based on trade theories, but they also take account of today's global economic environment, namely the pressures exerted by the processes of economic privatization and economic liberalization.

In short, the first section of the paper reviews trade data in order to identify trade patterns for the most advanced developing countries and the least developed countries, and in its second section the paper uses trade theory to identify trade policies that could help the most advanced developing countries and the least developed countries alike to increase the positive developmental impact of international trade.

II. Trade patterns: An empirical analysis

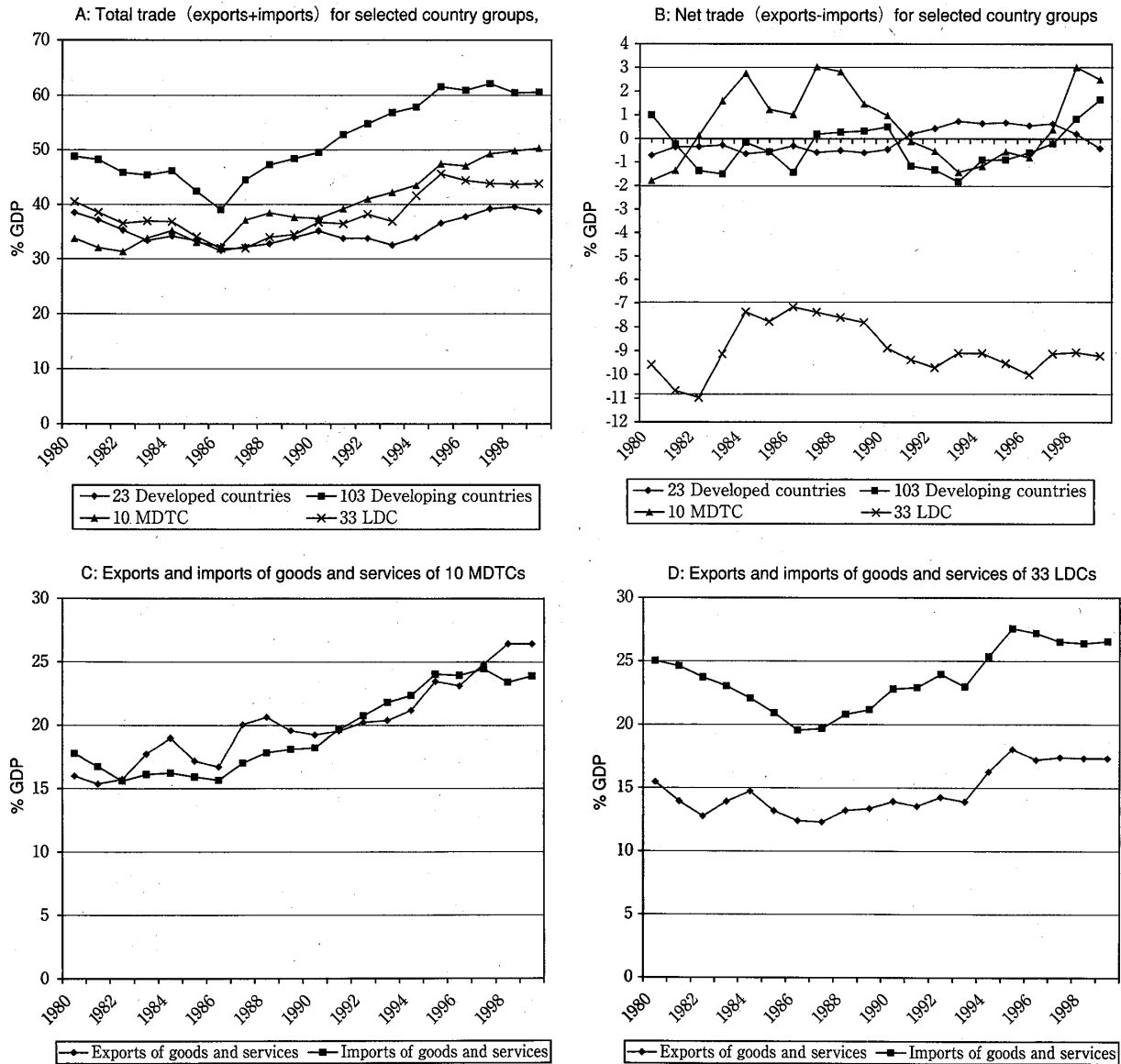
It is sometimes suggested that the gains that countries derive from international trade depend on the level of their integration in international trade; and that their level of integration in international trade depends on the openness of countries to international trade⁵. While this line of argument is plausible, this paper argues that the argument is not universally true. This is because the underlying relations are not necessary relations; they are contingent upon context. They differ with the development status of countries and correspondingly they can be said to differ across time and space.

It can for example be found that the most advanced developing countries have a level of trade integration that is lower than the level of trade integration for the broader developing countries group, and it can also be found that the level of trade integration of the least developed countries is even higher than the level of trade integration of the developed countries group. Chart 1A provides a more detailed picture of the level of trade integration of different groups of countries. Accordingly, developed countries as well as LDCs have seen only a small change of their trade integration between 1980 and 1999. During this time, the trade integration for developed countries increased from 38.5 to 38.7 percent of their GDP, while the trade integration of the LDCs increased from 41 to 44 percent of GDP. But the developing countries and the MDTCs saw a significant change of their trade integration over the same period. Between 1980 and 1999, the trade integration of developing countries increased from 49 to 61 percent of their GDP, and the trade integration of the MDTCs increased from 34 to 50 percent of their GDP. In sum, the 1999 level of trade integration shows that the trade integration for developed countries remains lowest and that the level of trade integration for developing countries is highest. The trade integration of both MDTCs and LDCs, by contrast, falls in-between these extremes. A comparison between the LDCs and the MDTCs also shows that for the largest part of the 1980s the LDCs have been more integrated in world trade than the MDTCs, and that the MDTCs have increased their trade-GDP ratios only in the 1990s.

Chart 1B provides a glance behind the level of trade integration at the form of trade inte-

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- 5) Please note that sometimes the level of integration in international trade and the openness of countries to international trade are both measured by an identical indicator, namely the ratio of trade to GDP (for a more detailed discussion, see for example Birdsall and Hamoudi, 2002 and UNCTAD, 2002a). Correspondingly, the trade-GDP ratio is sometimes utilized to express the level of integration in international trade and it is sometimes also utilized to express the openness of countries to international trade. But this is wrong, because the level of international trade integration and the openness of countries to international trade can only be equated on the basis of various ad-hoc auxiliary assumptions, none of which necessarily reflect reality. These assumptions, for example, entail the assumption that countries which pursue external liberalization, decrease trade barriers and open up to international trade automatically see an increase of their trade. But the capacity to trade is not only associated with the level of trade barriers, but also with domestic supply capacities and productive potentials. Correspondingly, trade integration and trade openness should not be confused as identical factors and should not be measured by an identical indicator. The level of integration in international trade is most appropriately measured by the ratio of total trade to GDP; the openness of countries to international trade is most appropriately measured by their effective rate of protection, tariff rates, tariff peaks and non-tariff barriers. Finally, the ratio of exports or imports to GDP is also sometimes equated with inward-orientated policies or outward-orientated policies of countries. But this is misleading as well, as the level of exports or imports is not necessarily positively associated with the pursuit of export promotion policies or import substitution policies. Instead, the ratio of exports and imports to GDP should merely be taken as an indication for the form of international trade integration, while outward or inward orientations should be associated with nothing else than two distinct types of trade policies. It is these definitions that are used in this paper.

Chart 1: Level and form of international trade integration for selected country groups, 1980-1999



Source: Calculations, based on World Bank, World Development Indicators, 2001, CD-Rom.

Note: (1) The group of MDTCs excludes the Czech Republic, Poland, and the Russian Federation for a lack of complete data series. (2) Values for all country groups, with the exception of the MDTC group, correspond with aggregates provided by UN Comtrade.

gration. The chart shows that the net trade for all country groups, with the exception of the least developed countries, varies in a band between +3 and -2 percent of GDP over the 1980-1999 period. For the least developed countries, by contrast, it varies between -7 and -11 percent of GDP. In 1999 the net trade for the developing countries group and for MDTCs is positive (1.7% GDP and 2.6% GDP respectively), while the net trade for developed countries and LDCs was negative (-0.4 and -9.2% GDP respectively). But the chart not only shows that the LDCs are the only country group that had a negative trade balance in excess of -2 percent of their GDP, it also shows that the LDCs are the only country group which did not have a positive trade balance over the entire period 1980-1999.

Charts 1C and 1D show the level of exports and imports for MDTCs and LDCs. The difference between the two country groups with respect to these trade patterns is stark: The MDTCs witnessed an increase of total goods and service exports and imports over the 1980-1999 period. The exports grew by about 10 percent from 16 to 26 percent of GDP, and imports grew by about 6 percent from 18 to 24 percent of GDP. The LDCs saw initially a decrease of total goods and service exports and imports that was reversed only in 1994. Over the entire period their exports grew by about 2 percent from 15 to 17 percent of their GDP and their imports grew by only 2 percent from 25 to 27 percent of GDP.

While the level of trade integration appears disassociated from the development status of different country groups, the form of trade integration does not. This is particularly apparent in the comparison between the MDTCs on the one side, and the LDCs on the other. The MDTCs have benefited from a positive trade integration over the past years as the growth of both exports and imports of goods and services as a percentage of GDP was significant and balanced. But the LDCs are characterized by a negative trade integration over the past decades. This is because the growth of their exports and imports of goods and services as a percentage of GDP was neither significant nor balanced. The MDTCs' integration in world trade displays a harmonized increase of exports and imports, whereas the LDCs' integration in world trade was dominated by high levels of imports throughout the entire period 1980 - 1999. An increase of imports however must not have negative implications for economic development. By contrast, large imports in the present may help countries to increase their exports in the future. This is the case, if the imported goods are capital goods that are used for investments rather than consumer goods that are eaten up by the population. But in LDCs the high levels of imports are—as will be shown below—associated with declining imports of investment goods (i. e., machinery) and increasing imports of consumption goods (i. e., foods).

In sum, the form of integration in international trade is closely associated with developments in exports and imports of the different countries. It is on the developments in the export sectors and their implications for import capacities that the following sections will concentrate on.

a. Export performance

Table 2 shows exports of goods and services for the different groups of countries in values and shares. The table illustrates a remarkable growth of all export categories, but it also highlights an uneven distribution of export shares. The growth of total world exports far outpaced the growth of world GDP in the period 1980-1999. During this period, world GDP increased by about 69 percent while total world exports grew by 135 percent. A disaggregation by export categories shows the following increases vis-à-vis the 1980 base: total world exports 135 percent; world service exports 309 percent; world merchandise exports 222 percent; world manufactures exports 314 percent; and world non-fuel primary commodity exports 46 percent⁶). These trends show two extremes: On the one side, non-primary commodity exports (services and manufactures) have seen an increase that exceeds the growth of world income and the growth of total world trade; on the other side, primary commodity exports (excluding fuels) fell short of the increase of world income and total world trade. In accordance with this difference it can be suggested that the world demand for the former type of exports is relatively dynamic and that the world demand for the latter type is rather unfavorable.

Table 2 also shows the specialization of country groups in the different exports categories, and it highlights how the shares of these country groups developed over time. Between 1980 and 1999 the development of the export shares of developed countries, on the one side, and developing countries, on the other, were mirror images of each other. The developed countries lost export shares in all export market segments with the exception of total merchandise exports, and the developing countries gained market shares in all export market segments with the same exception: total merchandise exports. The final aggregate changes in export shares for the two country groups were—with the exception of service exports for the developing countries group—relatively small.

But within the developing countries group there are noteworthy differences. The MDTCs outperformed the developing countries group in all export market segments, while the LDCs fell further behind other developing countries in all export markets. Indeed, while all developing countries saw an increase of their shares in world exports, with the exception of aggregate merchandise exports, the LDCs saw a decrease of their share in world exports with the exception of manufactures exports. Between 1980 and 1999 the LDCs' share in world exports of non-fuel commodities decreased by more than 50 percent, the MDTCs' share in the same group increased by 14 percent; the LDCs' share in world exports of manufactures climbed by 10 percent, but the MDTCs' share in this category increased by more than 47

6) Calculations based on World Bank, World Development Indicators 2001, CD-Rom and UN Comtrade database.

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Table 2: Trends in goods and service exports for selected country groups, 1980-99

	1980 (a)	1989	1999 (b)	Actual gain/loss over period (b-a)	Hypothetical ^a 1999 (c)	Hypothetical gain/loss over period (c-a)	Difference: Actual & hypothet- ical gain/loss (c-b)
Goods and service exports							
Value, billion 1995 USD							
World	3345	4358	7865	4520	-	-	-
Developed countries	2304	3205	5462	3158	5417	3113	-45
Developing countries	928	933	2095	1167	2181	1254	86
10 MDTC	215	318	827	612	506	291	-321
LDC	25	21	34	9	58	34	24
Share in world, %							
Developed countries	68.9	73.5	69.5	0.6	68.9	0.0	-0.6
Developing countries	27.7	21.4	26.6	-1.1	27.7	0.0	1.1
10 MDTC	6.4	7.3	10.5	4.1	6.4	0.0	-4.1
LDC	0.7	0.5	0.4	-0.3	0.7	0.0	0.3
Share, index 1980=100							
Developed countries	100.0	106.8	100.8	0.8	100.0	0.0	-0.8
Developing countries	100.0	77.2	96.0	-4.0	100.0	0.0	4.0
10 MDTC	100.0	113.6	163.5	63.5	100.0	0.0	-63.5
LDC	100.0	65.8	58.2	-41.8	100.0	0.0	41.8
Service exports							
Value, billion 1995 USD							
World	503	788	1554	1052	-	-	-
Developed countries	412	621	1163	751	1275	862	112
Developing countries	84	156	341	257	260	176	-81
10 MDTC	25	44	113	89	77	52	-37
LDC	3	4	6	3	10	7	4
Share in world, %							
Developed countries	82.0	78.8	74.8	-7.2	82.0	0.0	7.2
Developing countries	16.7	19.8	21.9	5.2	16.7	0.0	-5.2
10 MDTC	4.9	5.5	7.3	2.4	4.9	0.0	-2.4
LDC	0.6	0.5	0.4	-0.2	0.6	0.0	0.2
Share, index 1980=100							
Developed countries	100.0	96.1	91.2	-8.8	100.0	0.0	8.8
Developing countries	100.0	118.2	131.2	31.2	100.0	0.0	-31.2
10 MDTC	100.0	112.0	147.7	47.7	100.0	0.0	-47.7
LDC	100.0	74.3	64.1	-35.9	100.0	0.0	35.9
Merchandise exports							
Value, billion 1995 USD							
World	2842	3570	6310	3468	-	-	-
Developed countries	1892	2584	4299	2408	4200	2308	100
Developing countries	844	777	1754	910	1873	1029	119
10 MDTC	190	275	714	523	423	232	-291
LDC	22	18	28	6	48	26	20
Share in world, %							
Developed countries	66.6	72.4	68.1	1.6	66.6	0.0	-1.6
Developing countries	29.7	21.8	27.8	-1.9	29.7	0.0	1.9
10 MDTC	6.7	7.7	11.3	4.6	6.7	0.0	-4.6
LDC	0.8	0.5	0.4	-0.3	0.8	0.0	0.3
Share, index 1980=100							
Developed countries	100.0	108.7	102.4	2.4	100.0	0.0	-2.4
Developing countries	100.0	73.3	93.6	-6.4	100.0	0.0	6.4
10 MDTC	100.0	114.9	168.9	68.9	100.0	0.0	-68.9
LDC	100.0	64.6	57.5	-42.5	100.0	0.0	42.5
Manufactures exports							
Value, billion 1995 USD							
World	1524	2483	4790	3266	-	-	-
Developed countries	1328	1977	3478	2150	4173	2846	695
Developing countries	156	419	1154	999	490	334	-665
10 MDTC	69	164	537	468	217	148	-320
LDC	3	3	10	7	9	6	-1
Share in world, %							
Developed countries	87.1	79.6	72.6	-14.5	87.1	0.0	14.5
Developing countries	10.2	16.9	24.1	13.9	10.2	0.0	-13.9
10 MDTC	4.5	6.6	11.2	6.7	4.5	0.0	-6.7
LDC	0.2	0.1	0.2	0.0	0.2	0.0	0.0
Share, index 1980=100							
Developed countries	100.0	91.4	83.3	-16.7	100.0	0.0	16.7
Developing countries	100.0	164.9	235.7	135.7	100.0	0.0	-135.7
10 MDTC	100.0	145.5	247.4	147.4	100.0	0.0	-147.4
LDC	100.0	59.3	110.2	10.2	100.0	0.0	-10.2
Non-fuel primary commodity exports							
Value, billion 1995 USD							
World	545	621	798	253	-	-	-
Developed countries	370	409	517	147	542	172	26
Developing countries	163	174	243	80	239	76	-4
10 MDTC	71	79	119	48	104	33	-15
LDC	15	10	11	-4	22	7	11
Share in world, %							
Developed countries	67.9	65.8	64.7	-3.2	67.9	0.0	3.2
Developing countries	29.9	28.1	30.4	0.6	29.9	0.0	-0.6
10 MDTC	13.1	12.7	14.9	1.8	13.1	0.0	-1.8
LDC	2.7	1.6	1.3	-1.4	2.7	0.0	1.4
Share, index 1980=100							
Developed countries	100.0	96.9	95.3	-4.7	100.0	0.0	4.7
Developing countries	100.0	93.9	101.9	1.9	100.0	0.0	-1.9
10 MDTC	100.0	97.2	114.1	14.1	100.0	0.0	-14.1
LDC	100.0	61.0	49.2	-50.8	100.0	0.0	50.8

Source: Calculations based on UN Comtrade and UNCTAD service data.

Note: (1) Note that the sum of non-fuel primary commodity exports and manufactures does not add-up to total merchandise exports as the categories of fuels (SITC 3) and non-classified goods (SITC 9) are not listed here. (2) Values are deflated by UNCTAD's unit value of manufactures exports of developed countries.

^a Hypothetical values and gains/losses assume that the country groups' base year shares (i. e., 1980 shares) remained unchanged throughout the period 1980-1999.

percent; the LDCs' share in world exports of merchandise decline by about 43 percent, while MDTCs' share in this category increased by 69 percent; and the LDCs' share in world service exports deteriorated by 36 percent, while the MDTCs' share in this category increased by 48 percent⁷⁾. The cumulative effects of these changes are reflected in the developments with respect to aggregate goods and service exports. The MDTCs' share in world exports of goods and services has increased by about 64 percent against the 1980 base, while the LDCs' share in world exports of goods and services has tumbled by about 42 percent to 58 percent of the 1980 level.

Furthermore, it is noteworthy that the large increase in manufactures exports for the MDTCs is mainly due to an increase of high-tech/high-skill manufactures exports, while the increase in manufactures exports for the LDCs was driven by an increase of low-tech/low-skill manufactures exports. Between 1980-1984 and 1995-1999 the following developments can be detected: In the MDTCs, the share of high-tech/high-skill manufactures in total merchandise exports increased from 10.3 percent to 45.6 percent, while the share of low-tech/low-skill manufactures in total merchandise exports increase from 14.1 to 27.2 percent. The LDCs' share of high-tech/high-skill manufactures in their total merchandise exports increased from only 1.4 to a mere 2.8 percent, but their share of low-tech/low-skill manufactures in their total merchandise exports increased from 8.4 percent to 25.8 percent⁸⁾.

Table 2 also estimates gains and losses of the different groups of countries that are due to changes of their shares in world exports in selected export categories. If the MDTCs had not managed to increase their share in world exports of goods and services between 1980 and 1999, the MDTCs would have been US-Dollar 321 billion poorer in 1999. On the other side, if the LDCs had managed to prevent a decrease of their share in world exports of goods and services over the same period, the LDCs would have been US-Dollar 24 billion wealthier in 1999. For the LDC group US-Dollar 24 billion is more than twice the net ODA disbursements of OECD/DAC donor countries to LDCs in 1999 and only a little more than net ODA disbursements of the OECD/DAC donors to LDCs in 2000⁹⁾. This difference is im-

7) The categorization of export items into non-fuel primary commodities and manufactures corresponds with the Standard International Trade Classification (SITC), revision 3. According to it non-fuel primary commodities are defined as all food items (sections 0 plus 1, 22, 4), agricultural raw materials (section 2, minus 22, 27, 28), and minerals, ores and metals (sections 27 plus 28, 68). Manufactures include sections 5, 6, 7 and 8 minus 68. Please note, however, that the totals of non-fuel primary commodities and manufactures do not add-up to total merchandise, as fuel items (section 3) and non-classified goods (section 9) are excluded from this analysis.

8) The increase of manufactures in total merchandise exports of the LDCs is largely due to an increase of manufactures exports of a group of only eight LDCs. These are Bangladesh, Cambodia, Haiti, Lao PDR, Lesotho, Madagascar, Myanmar and Nepal. For a detailed classification of LDCs based on export specialization, see UNCTAD (2002a) and International Trade Centre UNCTAD/WTO (2001a, 200b) For a classification of manufactures exports based on technology and skill intensity see Wood and Mayer (1999).

portant and it underlines that the achievement of export competitiveness and the increase of export shares is a vital precondition for developing countries to raise resources for development financing.

The loss in export revenues is due to a combination of two factors: a decrease of export volumes and a decrease of export values. The former is associated with low productive capacities in the least developed countries, while the latter is associated with low prices for their main export items. Chart 2 shows trends in real world market prices from 1960 to the first quarter of 2002. The chart shows both a strong short-term volatility of non-fuel primary commodity prices and a long-term decline of these prices. By 2001, the deflated world market prices of non-fuel primary commodities stood at only 54 percent of their average 1979-1981 level. During the same period, the following world market price declines can be observed: foods 47 percent; tropical beverages 68 percent; agricultural raw materials 35 percent; and minerals, ores and metals 33 percent. Furthermore, since the Asian financial crisis of 1997 non-fuel primary commodity prices saw a further rapid decline, and since 2001 fuel prices witnessed a large increase. Between 1997 and 2001, coffee prices declined by 66 percent, cotton prices fell by 39 percent and copper prices fell by 27 percent, but crude oil price rose by 24 percent, to name just a few commodities. Due to the structure of their trade, the group of LDCs is particularly hard hit by these opposed developments in commodity prices. This is because the majority of LDCs are net-exporters of non-oil primary commodities and net-importers of oil. Consequently, these price developments cause a further deterioration of their trade balances and a significant loss of their incomes (Herrmann and David, 2001)¹⁰.

In combination with declining market shares, the declining world market prices cause a fall of the LDCs' income terms of trade. Furthermore, the combination of deteriorating non-fuel primary commodity prices and relatively stable manufactures prices also causes a fall of the commodity terms of trade. Finally, a look at the barter terms of trade for the 1990s shows that the LDCs' barter terms of trade declined by about 20 percent vis-à-vis the 1990 base, and that the MDTCs' barter terms of trade declined by only 1 percent against the same base year¹¹.

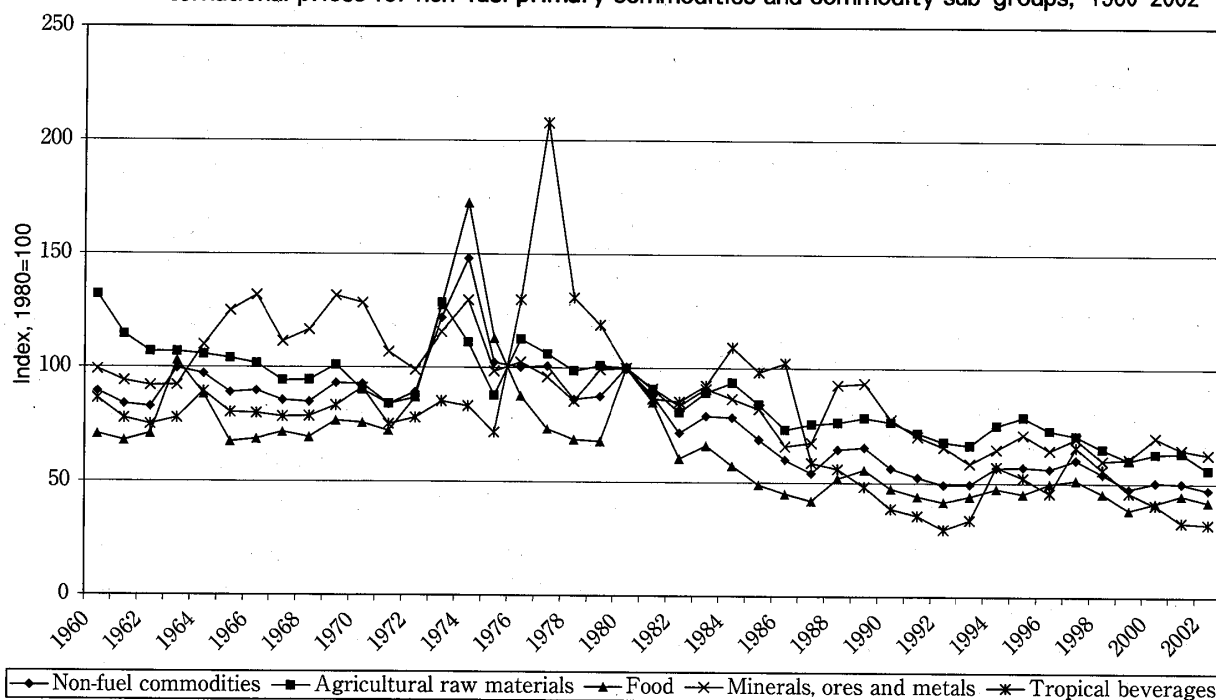
In sum, there is a remarkable difference between the MDTCs and the LDCs. Aggregate data for the 1980-1999 shows that the MDTCs, which specialize in manufactures exports, gain market shares in dynamic markets, while the LDCs, which largely specialize in non-fuel primary commodity exports, lose market shares in sluggish markets. But the LDCs

9) ODA stands for official development assistance; OECD/DAC countries are those OECD countries that are members of OECD's Development Assistance Committee (DAC). The OECD provides the value of net ODA disbursements.

10) Calculations based on UN Commodity Price Bulletin.

11) Calculations based on UNCTAD data. The calculations are based on simple averages of unit value ratios, weighted averages can be expected to provide starker results.

Chart 2: International prices for non-fuel primary commodities and commodity sub-groups, 1960-2002



Source: Calculations based on UNCTAD Commodity Price Bulletin.

Note: Figures for 2002 are based on first quarter only.

not only loose export shares in sluggish world markets, they also loose export revenues due to deteriorating world market prices. In combination these two processes lead to a shortage of foreign exchange and contribute to the accumulation of large external debt. UNCTAD shows that in the LDCs there is a strong link between the dependency on non-fuel primary commodity exports and the accumulation of unsustainable external debt, according to the debt sustainability criteria of the HIPC Initiative¹²⁾. The fact that these countries have limited foreign exchange revenues and that large international debt burdens further subtract from the foreign exchange earnings places a significant limitation on the capacity of these countries to import goods.

b. Import capacities

The capacity of countries to import goods depends solely on the capacity of countries to access foreign exchange. Since export revenues are only one amongst many sources of for-

12) The Highly Indebted Poor Country (HIPC) Initiative is an initiative of the International Monetary Fund (IMF) and the World Bank. The initiative provides debt relief to countries that are acknowledged to have an unsustainable debt burden and that have completed so called Poverty Reduction Strategy Papers. In these papers—the PRSPs—the developing countries are supposed to outline how they intend to achieve development objective of poverty reduction and how they intend to use their resources towards this end, including the resources generated through debt relief and aid.

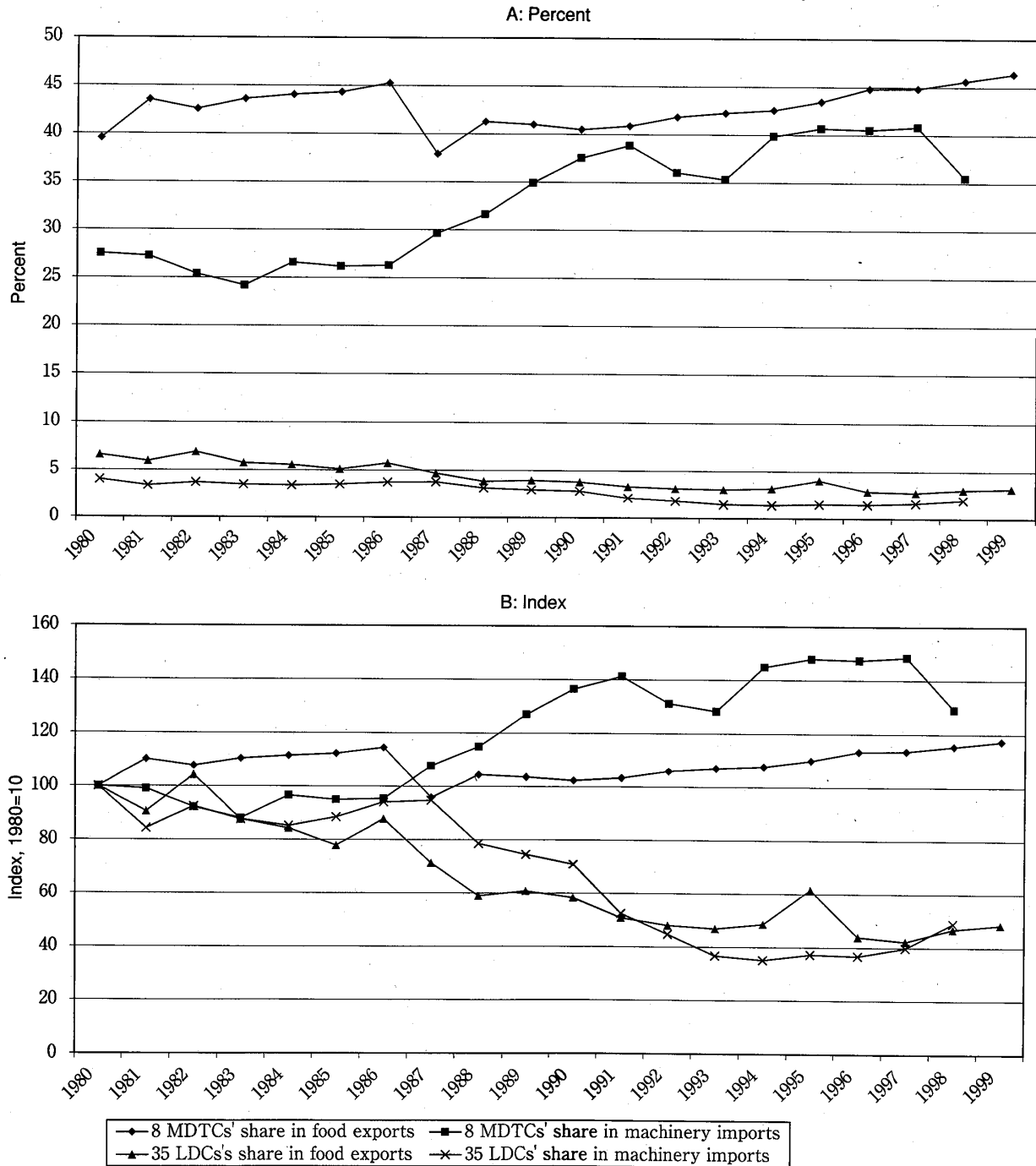
foreign exchange earnings, export revenues are only one amongst many factors that influence import capacities. But the influence of export earnings on import capacities of countries differs with the development status of countries and the size of their economies. Developed countries with a large domestic economy (e. g., USA) have manifold means to access foreign exchange and to maintain high import capacities, even in the absence of significant export revenues. But poor developing countries with small domestic economies (e. g., LDCs) frequently have very limited means to access foreign exchange. Therefore, their import capacities more strongly depend on their ability to generate export revenues. In short, the influence of export revenues on import capacities is negatively associated with development status and economic size.

Chart 3 shows developments in two very important trade sectors for developing countries, namely food exports and machinery imports. The chart contrasts the shares of MDTCs and LDCs in the food exports of developing countries and in addition it contrasts the shares of MDTCs and LDCs in machinery imports of developing countries¹³⁾. The MDTCs' share in both categories increased: food exports increased by 17 percent by 1999, and machinery imports increased by around 49 percent by 1997, the year before the Asian financial crisis triggered through. The LDCs' share, by contrast, decreased. Food exports declined by 52 percent by 1999, and machinery imports fell by 51 percent by 1998, the last year for which this data series is available.

In sum, the MDTCs, which have managed to diversify into manufactures exports, have benefited from increasing market shares in relatively dynamic markets and they have also benefited from relatively stable international prices for their export items. Correspondingly, the MDTCs have increased their export revenues and their import capacities which positively influenced their ability to upgrade their domestic production structures and to further increase their export competitiveness. By contrast, the LDCs, which strongly specialize in non-oil primary commodities, have witnessed declining market shares in sluggish markets and they have also been hit by declining international prices for their exported goods. Consequently, they have witnessed deteriorating export revenues and deteriorating import capacities which negatively effected their ability to upgrade domestic production structures and to support their export competitiveness. Negative terms of trade for LDCs and high levels of subsidies in the OECD countries have further worsened the situation of the least developed countries: They saw a collapse of processed commodities in their export baskets and in addition they saw a decline of food items in their exports (UNCTAD, 2002 a). Neither would be problematic if they had managed to balance the decrease in selected

13) Both commodity groups are defined on the level of SITC 2. But while the category of food exports that is used here corresponds with the category of foods that is provided by SITC, the category of machinery imports that is used here is distinct from the category of manufactures that is provided by SITC. The category of machinery is based on a definition by Jörg Mayer (2000, 2001) and it is his dataset on machinery imports that was used for the corresponding calculations in the analysis.

Chart 3: Share of MDTCs and LDCs in total machinery imports and total food exports of developing countries, 1980-1998 and 1980-1999 respectively



Source: Calculations based on UN Comtrade database and Mayer (2000, 2001).

Note: (2) The two country groups exclude all countries for which data for either series was missing. The group of MDTCs excludes China and all countries with economies in transition (Czech Republic, Hungary, Poland and the Russian Federation). (2) The values underlying the index are deflated by UNCTAD's unit value of manufactures exports of developed countries.

export items through an increase in other export items, but they did not.

The cumulative developments have led to a raising level of exports combined with a raising level of imports in the MDTCs, but they have caused the level of exports to fall short of the levels of imports in the LDCs. These distinct developments in the two country groups imply distinct forms of international trade integration. The form of trade integration that characterizes the MDTCs is positive, but the form of trade integration that is characteristic for the LDCs is negative. This is because in poor developing countries with small economies, persistent and large net trade deficits have a negative impact on foreign exchange earnings and subsequently on investment, consumption and overall economic activities.

c. Policy challenge

The different performances in international trade are sometimes linked to different types of domestic trade policies. It is suggested that countries, which have a rather positive trade performance, pursue sound trade policies, while those that have a weak trade performance pursue weak trade policies. In accordance with structural adjustment policies sound trade policies are typically associated with liberal trade policies and weak trade policies are typically associated with strategic/managerial/interventionist trade policies. But the relation between trade performance and trade policies is challenged on empirical grounds. Many MDTCs that display a rather positive trade performance have long pursued strategic trade policies, especially in the early stages of their development. By contrast, most LDCs that display a very weak trade performance have pursued liberal trade policies from early stages of their development onward. This is because the majority of LDCs has participated in structural adjustment programmes and, subsequently, the majority of them have engaged in external economic liberalization. Indeed, while many of the MDTCs have been criticized for interventionist trade policies, many of the LDCs are now recognized for their liberal trade policies.

A recent study of the World Bank (2002b) finds that the majority of low-income countries, including the majority of LDCs, now has sound economic policies in place. UNCTAD data show that many LDCs have gone further in liberalizing their financial markets than other developing countries, and IMF data show that many LDCs have also made substantial progress in liberalizing their trade regimes (UNCTAD, 2000). If anything this mixed experience with respect to trade performance and trade policies suggests that it is not so much the type of trade policies that influences trade performance than the sequencing of trade policies that makes the difference. This is because both the MDTCs and the LDCs have pursued liberal trade policies, but at different times. Many of the MDTCs, especially the Southeast Asian ones, have long pursued interventionist trade policies and they have switched towards more liberal trade policies only in a more advanced develop-

mental stage. By contrast, many of the LDCs, especially those that participated in structural adjustment programmes, have departed from interventionist trade policies and have instead instituted relatively liberal trade regimes, despite their relatively backward developmental stage.

The difference between the two developing country groups with respect to trade performance begs the question whether the least developed countries cannot follow the example of the more advanced developing countries and pursue similar trade policies. This question is essentially the question of the transferability of the development model of successful developing countries to less successful developing countries. A similar question is the question of the transferability of the Southeast Asian development model from the Southeast Asian economies to African countries¹⁴). There is no straightforward answer to this question. As development models function in a specific societal and international context, the models cannot easily be transplanted in the time or space dimension. But even though entire development models cannot be transplanted, individual elements may be. The objective of the subsequent section is to identify elements of successful development strategies that equally apply to more advanced developing countries and least developed developing countries, to newly industrialized countries and commodity-dependent countries, to Southeast Asian economies and African countries.

III. Trade policies: A theoretical approach

It is a stylized fact that today's economy was shaped by technological change. But it often remains a neglected fact that this economy was quite simply shaped by political decisions as well. Indeed, today's economy would not be the same if it were not for two political decisions with far-reaching implications. These are the decision to privatize scarce and essential resources, and the decision to liberalize internal and external markets. The former enabled individuals to control scarce resources that are essential for human survival, and the latter enabled these individuals to freely transfer these resources between different economic entities, be they companies or countries. In short, it is the combination of (1) the scarcity of resources, (2) the essential function of resources, (3) the privatization of resources, and (4) the liberalization of markets that is necessary for an understanding of economic dynamics. If only one of these elements were missing, it would be difficult to explain the competition over resources and subsequently it would be difficult to explain

14) With the financial support of the Government of Japan, UNCTAD has conducted research on African development in a comparative perspective. This research partially addresses the question of what African countries may learn from the development experiences of countries outside the region. The research output—a series of papers—can be ordered through UNCTAD's publications department.

ambitions to raise competitiveness.

This paper argues that the goal of building trade capacities is closely related with the goal of raising (export) competitiveness. But, furthermore, the paper argues that the goal of raising competitiveness is a difficult challenge under the outlined conditions. This is because the combination of economic privatization and economic liberalization have increased two opposed pressures: On the one side, economic liberalization promotes and increase of international competition and raises concerns about national competitiveness, but on the other side economic liberalization also limits the use of macroeconomic policies that were traditionally important for the management of national competitiveness. Thus, while countries have the need to increase their competitiveness, they increasingly lack the means to that end. This is, the paper argues, because economic liberalization increases international interdependencies and decreases policy autonomy. While this is generally true for all open economies, it is especially so in small countries and it is even more so in small developing countries. For all small countries it is difficult to act autonomous of large countries, but for small developing countries it is particularly difficult "to blow against the wind". This is because they often lack credibility and, furthermore, they generally are strongly dependent on external assistance.

a. Theoretical considerations

The need to successfully compete for essential resources raises the question of how to successfully increase competitiveness, whereby competitiveness is defined by relative price levels. This subsequently raises the question of what determines price levels. Trade theories hint at answers. The classical theory of comparative advantage stresses that comparative advantage is dependent on the price of the product (P), which in turn is determined by wages (w) over productivity levels (Y):

$$P = w / Y \quad (1)$$

This formula can be modified to better reflect the multiple factors that determine product prices:

$$P = (oc / Y) - QUAL + pi \quad (2)$$

Accordingly, the wage "w" as the only costs of production is replaced by total operation costs "oc". In accordance with the modified formula, the product price is determined by total operation costs (oc) over productivities (Y). But in addition, the product price is also determined by the profit rate (pi) and the product quality (QUAL). In accordance with this formula competitiveness is defined by the inverse relation between the price of the product, on the side, and the quality of the product, on the other. This relation effectively lowers the price of products, which have a high quality, and it increases the price of those that have a lower quality. This implies that a product with a higher quality may have a higher price and still be considered competitive, while one with a lower quality needs to

have a lower price in order to be competitive.

The total operation costs can be further subdivided into costs that are associated with macroeconomic policies (pc), with utilized resources (rc) and with transactions (tc):

$$oc = pc + rc + tc \quad (2.1.)$$

The policy costs "pc", the resource costs "rc", and the transaction cost "tc" maybe further distinguished into different categories of costs:

Policy costs:

$$pc = (ag - dwl) + (ir + xr) + (tp - sp) \quad (2.1.1)$$

The policy costs can be distinguished in costs that are associated with trade policies (ag - dwl), with monetary policies (ir + xr), and with fiscal policies (tp - sp). Here "ag" are the aggregate gains of strategic trade policies; "dwl" are the deadweight losses of such trade policies¹⁵⁾; "ir" are interest rates; "xr" are exchange rates; "tp" are tax payments of enterprises; and "sp" are various subsidy payments to enterprises.

Resource costs:

$$rc = hrc + pcc + (lc + onc) \quad (2.1.2)$$

Here "hrc" stands for costs associated with human resources (e.g., wages and payroll fringe costs); "pcc" stands for the costs of physical capital (i.e., the rental rate); "lc" represents the costs of land; and "onc" represents costs of other natural resources, many of which are currently free of charge, but proper accounting mechanisms would need to internalize these costs.

Transaction costs:

$$tc = I + f + dlc \quad (2.1.3.)$$

Here "i" represents the costs of insurance and "f" the cost of freight. Furthermore, "dlc" represents a cost item that can be associated with a delivery lag. The delivery lag represents the time lag between the placement of an order and the delivery of the product.

It is this modified formula that guides the subsequent analysis. The formula also illustrates that product price depends on various operation costs which can be classified in three categories: (1) The category of policy costs (i.e., costs that are associated with influences of macroeconomic policies); (2) the category of resource costs (i.e., costs that are associated with the factors of production); and (3) transaction costs (i.e., costs that are especially associated with insurance and transport). Furthermore, the product price depends on the productivity, the product quality and profit rates. In theory, the price of a product can be influenced through manipulations of all these components, but in practice, alterations of these components face significant restrictions. These restrictions will be

15) Orthodox theories of optimal tariffs suggest that only large countries may have positive net gains from strategic trade policies, but in accordance with new trade theories it may be suggested that other countries may derive positive net gains from such trade policies as well. This is because new trade theories, in contrast to "old" trade theories, do not only emphasize static trade gains, but also dynamic trade gains.

elaborated in the subsequent sections.

b. Practical limitations

In theory, the international competitiveness of domestic producers could be achieved through a variety of economic policies and policy mixes including mercantilist trade policies and exchange rate manipulations as well as interest rate manipulations and fiscal policies. But the paper argues that these economic policies are constrained by the global economic environment. The paper argues that the pursuit of mercantilist trade policies is limited by the rules of the international trading system¹⁶). Furthermore, the paper argues that manipulations of monetary policies are discouraged by the danger of strong negative feedback effects. Misaligned exchange rates and unreasonable interest rates may for example create opportunities for arbitrage profits and encourage financial speculations. Furthermore, unreasonable interest rates can give wrong price signals to the real sector economy and misguide investment decisions. As either outcome would harm sustainable economic developments, it can be expected that countries with relatively open economies will pursue

16) While the international trading system cannot entirely preclude unilateral actions, it can significantly constrain these actions. The system, however, opens up space for a special and differential treatment of developing countries and particularly least developed countries. Under WTO rules, LDCs have limited possibilities to sue import restrictions and they are granted the right to use export subsidies. But the effectiveness of export subsidies is ambiguous. This is because many poor countries such as the least developed countries have significant resource constraints that preclude large subsidy payments. But there are other reasons why subsidies may not be the first choice of least developed countries. Export subsidies may make sense for goods that cannot be easily substituted, but they make less sense for normal goods characterized by fairly normal demand conditions. Most exports of least developed countries, be they agricultural goods (foods and raw materials) or low-tech manufactures (especially no-name clothing and accessories), fall in the latter category of goods. Foreign consumers will purchase these goods when they are subsidized, but they are likely to switch to competing goods when the relative prices change accordingly. Whether export subsidies are reasonable instruments to encourage domestic production and domestic exports essentially depends on whether the benefits for domestic entrepreneurs exceed the income transfer to foreign consumers. As it is difficult to quantify both direct and indirect benefits of the entrepreneurs, it is pretty much impossible to answer this question objectively. But it is probable that a temporary expansion of production in a low-tech sector brings about only limited benefits to this sector. This is because low-tech sectors are typically characterized by a relatively low potential for innovations and inventions. In sum, the use of export subsidies for the promotion of export competitiveness appears to have limited utility in the context of poor developing countries such as the least developed countries. This is because such countries typically specialize in normal low-tech goods, which probably yield only small dynamic gains, and because such countries typically have relatively small economies and cannot influence world market prices. De jure, WTO rules also allow for selected import restrictions, but de facto countries are largely unable to use import restrictions. The use of import restrictions with respect to manufactures is limited by various conditionalities, and the use of import restrictions with respect to agricultural goods is for example limited by the so-called Peace Clause.

similar monetary policies with similar aims, namely the aim to avoid exchange rate misalignments and the aim to avoid inflationary pressures.

In short, economic liberalization is associated with the manifestation of relatively liberal trade and a convergence of monetary policies around the practices described above. The relative paralysis of these two policy instruments implies that countries are increasingly unable to positively distinguish themselves from others through the use of trade or monetary policies. Countries are therefore encouraged to positively distinguish themselves from others through the pursuit of alternative economic policies. The limitations of trade and monetary policies subsequently increase the pressures on fiscal and wage policies. But both of these policy instruments face important constraints as well: Limited budgetary resources, especially in poor developing countries, limit the possibility of these countries to increase the competitiveness of local companies through various direct and indirect subsidies. In addition, already low effective labor costs in many developing countries preclude the possibility that these countries increase the competitiveness of local companies by offering even lower wage rates and payroll fringe costs¹⁷⁾.

Finally, the limitations of these classical types of economic policies may increase pressures on other policy areas. Correspondingly, it is possible that countries attempt to increase their competitiveness by offering low levels of environmental protection, which may significantly lower the costs of natural-resource-intensive productions. But what is true for the level of labor standards and the costs associated with labor is also true for the level of environmental standards and the costs associated with natural-resource usage: They are already very low and they should not be lowered any further. An increase of economic competitiveness and economic growth on the basis of low social standards or low environmental standards actually lead to market distortions and unsustainable economic practices. This is because low labor and environmental standards and artificially low labor and environmental costs effectively lead to an externalization of costs from the balance

17) In developing countries, especially the least developed countries, labor costs associated with wage rates, payroll fringe costs and labor standards are already at minimal levels. It is not in the interest of developing countries to encourage a further decrease of these costs, by contrast. But an increase of labor costs in developing countries is frequently impeded by three types of labor-cost ceilings: One, low levels of productivity in the primary commodity sector of the developing countries often fix the labor costs in the developing countries at a minimal level. Second, high levels of subsidies for low-tech sectors in the industrialized countries also fix wages in developing countries at a minimal level. Third, a high effective rate of protection against imports in the industrialized countries also fix wages in the developing countries at very low levels. Contrary the first type of labor-cost ceiling, the second and third types receive only little attention, but they are no less important. It must be recognized that industrialized countries that provide large subsidies or maintain high import barriers, essentially enforce developing countries to maintain low levels of labor costs. Otherwise developing countries, especially the least competitive ones, will see a further decline of their agricultural exports as well as their low-tech manufactures exports.

sheets and national accounts and to an inflated face value of national income. The false benefit - cost analysis misguides economic agents and causes unsustainable economic practices with potentially devastating future effects. This is because externalized costs do not disappear for all times as they are merely converted into future debt that becomes payable when the social or environmental exploitation cause social or environmental disruptions. To prevent misguided economic activities and unsustainable economic production processes, it is essential that environmental costs be internalized in balance sheets. Accordingly, economic agents should not rely on low environmental costs, and should instead expect higher environmental costs in the future¹⁸⁾.

In sum, economic agents face an increasing pressure to raise their economic competitiveness, but they also increasingly lack the means to these ends. This is because the liberalization of economies has led to important limitations on economic policies. Indeed, most constraints on economic policies are negatively correlated with the development level so that the constraints increase as the development level decreases. In correspondence with the presented line of argument, the paper makes the following assumptions: (1) the countries pursue liberal trade policies; (2) the countries pursue non-interventionist monetary policies as defined above; (3) the countries cannot significantly expand fiscal expenditures; (4) the countries cannot significantly reduce labor-related costs; (5) and the countries cannot reduce environmental costs. But the paper makes an additional assumption: (6) the profit rates offered by companies are fixed at an internationally acceptable level and therefore profit rates are assumed to be invariable. This assumption is based on the fact that the international liberalization of capital markets has established the international mobility of capital. Capital can essentially flow to all companies around the world and therefore the different companies must essentially compete for capital out of the same pot. This requires that all companies offer internationally competitive returns and this demands that they offer internationally expected profit rates. In other words, the effective profit rate that is offered (after risk adjustments) tends to correspond with the profit rate that is expected by international investors. If it does not, companies may not be able to attract investment capital, may not be able to prevent capital flight and may ultimately witness a credit crunch.

18) The internalization of environmental costs in the balance sheets is a difficult challenge, of course, as it must overcome the assignment problem with respect to natural resources and must identify the right price for these resources. Ideally, the laws of thermodynamics should guide the pricing of resources. Correspondingly, two types of prices should be calculated: One price would take account of the value that is associated with the resource in its original form. This price would need to take account of the availability and importance of the resource itself. The second price would take account of the damage that can be caused by the resource through its alteration. This price would need to take account of the capacity and importance of sinks. Whatever price is higher should be the minimal price that is assigned. The final market price could be determined in trading of pollution permits, for example.

These assumptions significantly limit possibilities to manipulate the costs that influence the product price. The assumptions regarding trade policies essentially preclude the possibility to influence the product price through a strategic management of trade policies. Similarly, the assumption regarding monetary policies essentially precludes the possibility to influence the product price through interest rate and/or exchange rate manipulations, and the assumption regarding fiscal policies implies rather limited possibilities to influence the product price through lower tax rates and/or higher subsidies. The command of overall sustainability also restricts labor policies as well as environmental policies as means to lower product prices. Finally, the paper assumes fixed levels of profit rates. The strong restrictions with respect to these possibilities to decrease product prices increases the pressure on alternative means to decrease product prices. These include especially a focus on the cost of capital and the costs associated with transactions. But some of these possibilities are also limited.

The development of better financial institutions, including development banks, may for example contribute to a reduction of the cost of capital. But while a reduction of the cost of capital is possible, it is not very flexible either. This is because rental rates are, at least partially, endogenous to the development process. In early stages of development capital is typically scarce and rental rates are relatively high, and in later stages of development the capital stock increases and the rental rate decreases. In sum, the limited possibilities to reduce the different costs associated with macroeconomic policies and resources increases the pressure to reduce costs that are associated with insurance and transport.

In countries where infrastructures are underdeveloped, the cost of freight is very high, and in countries that are exposed to high operation risks, the cost of insurance is very high as well. High operation risks are for example associated with the absence of clear legal systems, including the absence of clear property rights. Unclear property right with respect to land can for example significantly increase the operation risk for land-intensive investments. In sum, it must be realized that developing countries have a great potential for large reductions of transaction costs, but at the same time it is also important to realize that developing countries may not derive the expected benefits from a reduction of transaction costs alone. In other words, while a reduction of transaction costs can make an important contribution to export competitiveness, it will probably not be able to ensure the attainment of export competitiveness itself.

c. Policy implications

Drawing on classical trade theory, the previous section outlines three theoretical possibilities to increase export competitiveness: (1) a decrease of operation cost, (2) an increase of productivity levels, and (3) an improvement of the product quality. But while classical trade theory helps to identify these possibilities, classical trade theory cannot ex-

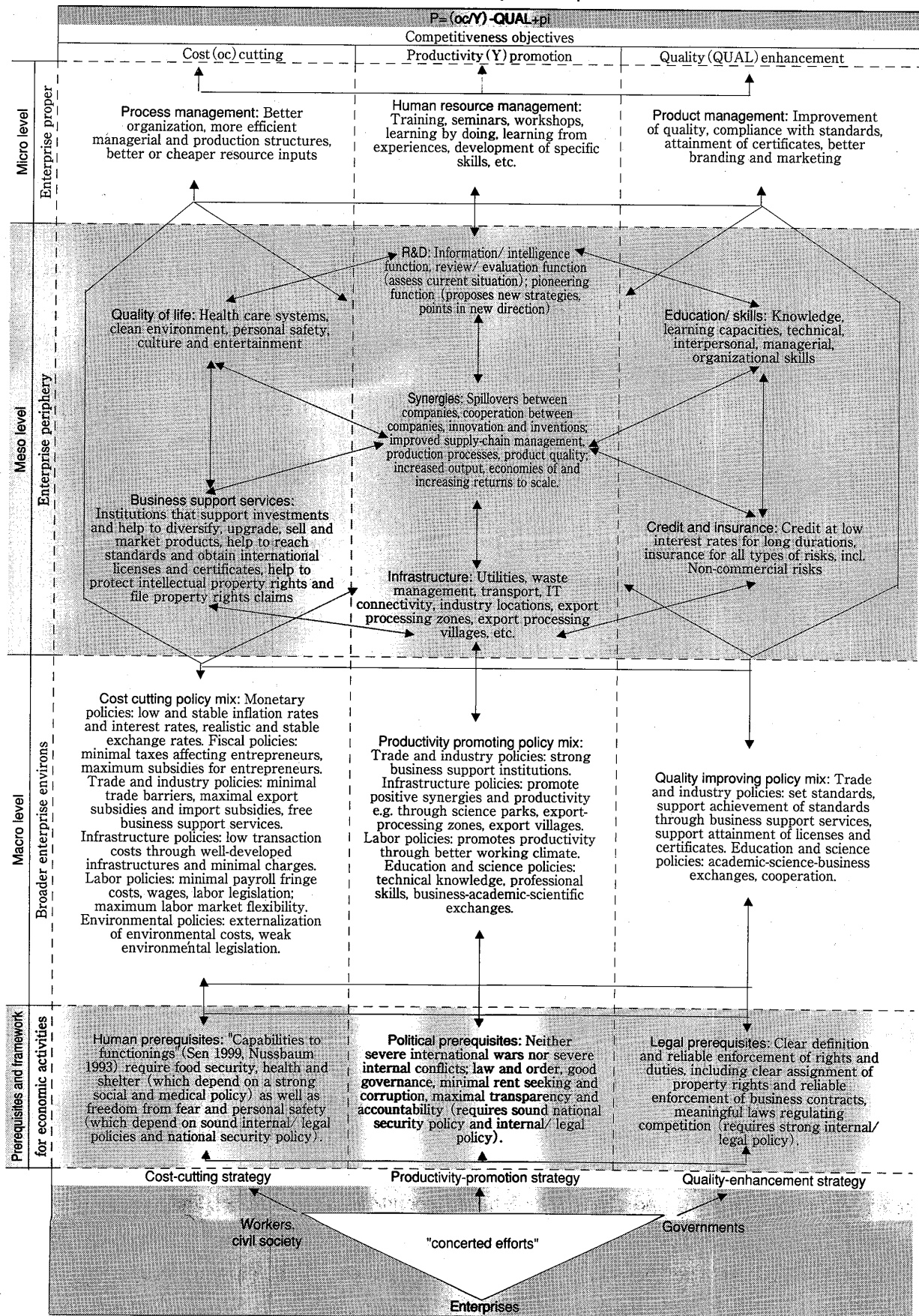
plain how to actually achieve these objectives. For answers to this question it is necessary to turn to new theories on trade. Unlike the classical trade theory, which acknowledges the importance of productivity differences but fails to give reasons for these differences, new trade theories not only acknowledge the influence of productivity differences but also provide explanations for these differences. The differences in productivities are attributed to a long list of factors, including positive externalities and technological dynamics that encourage innovations and inventions and economies of scale. In addition, new trade theories emphasize the influence of transaction cost (including transport cost), which traditional trade theories typically ignore, as well as the influence of taste differences and product differentiation, which traditional theories neglect as well.

Inspired by new trade theories and endogenous growth theories, chart 4 tries to systematically sketch out two types of factors that influence the level of international export competitiveness. The first type of factors has a direct influence on export competitiveness. These factors include operation costs, productivity levels and product quality. The second type of factors has only an indirect influence on export competitiveness as these factors firstly influence the operation costs, the productivity levels and/or the product quality. The former type of factors is here referred to as "direct determinants", while the latter type of factors is referred to as "indirect determinants". It is important to note that the qualifications "direct" and "indirect" do not imply a ranking. Direct determinants are as important as indirect determinants and in order for countries to enhance their trade capacities and export competitiveness countries are best advised to concentrate on both direct determinants and indirect determinants. By doing so countries have different options. They may focus on factors that decrease total operation costs, on factors that increase factor productivities or on factors that improve the product quality. But instead of placing their focus on only one of these clusters, countries may also decide to concentrate on all three clusters together. Indeed, the latter strategy certainly is the most comprehensive strategy and it is the most promising one as well. This is because a simultaneous decrease of production costs, increase of productivity levels and increase of the product quality will allow for a maximal decrease of the product prices or a maximal increase of the profit rate or a combination of these two possibilities.

The direct determinants combined with the indirect determinants for capacity-building strategies define an area for strategic policy interventions by developing countries as well as their development partners. The chart associates the direct determinants with indirect determinants and it associated the indirect determinants with different analytical levels, encapsulating the level of the enterprise, the level of the enterprise periphery, the level of macroeconomic policies and the level of broad societal prerequisites. The degree to which these different determinants of domestic productive capacities and international export competitiveness are developed in the different groups of developing countries differs significantly. Other contributions to the MDT project show that many of these determi-

Part I: Globalization and the Transformation of Governance

Chart 4: Determinants of export competitiveness



nants are already highly developed in the majority of the advanced developing countries, but most of the determinants remain woefully underdeveloped in the majority of the least developed countries¹⁹⁾. Correspondingly, it follows that in the advanced developing countries, where these determinants are already comparably well developed, more attention needs to be paid to the maintenance of these determinants, while in the least developed countries, where these determinants are extremely weak, much more attention needs to be paid to their development.

But while the different determinants for productive capacities and export competitiveness are essentially the same in the different countries, the potential of the individual determinants to raise productive capacities and export competitiveness can significantly differ amongst countries. This is because the potential of these determinants stands in an over-determined relation with the overall economic environment. Countries for example that have a strong specialization in manufactures goods, which is typically characterized by a capital-intensive production and a high technology content, have a relatively large potential to increase their productivity levels. The MDTCs belong to this group of countries. Countries, on the other side, that have a strong specialization in agricultural goods, which is typically associated with a labor and land-intensive production and a low technology content, have a comparably low potential to increase their productivity levels. The average LDC fits this case. In other words, capital intensity is typically positively associated with technology intensity and technology intensity is typically positively associated with a relatively high propensity to increase productivity levels. For this reason, it can be expected that the MDTCs, which increasingly specialize in manufactures and particularly in high-tech manufactures, have a relatively large propensity to increase their productivity levels, while the LDCs that specialize in primary commodities and especially non-mineral primary commodities have a comparably low propensity to increase productivity.

But the technology intensity not only has implications for the propensity to increase productivity levels, it may also influence the type of productivity increases. The former—the propensity to raise productivities—and the latter—the type of productivity increases—are interrelated, however. In capital-intensive industrial sectors, where the production is characterized by a relatively high technology intensity, productivity increases are primarily based on technological learning and technological improvements; in labor-intensive primary commodity sectors, which are characterized by a comparably low technology intensity, they are rather based on a rationalization of work. Unlike the former type of productivity increase, which appears essentially unlimited and dynamic, the latter type of productivity increase is much more limited and static.

19) The contributions to this volume show that both the financial sectors and the real sectors in the majority of MDTCs are relatively developed. This contrasts starkly with the LDC case. In the LDCs financial markets are virtually non-existing and the real sector economy remains extremely weak.

The distinct propensities to raise productivity levels have far-reaching implications for the overall development strategy. This is because countries, including the MDTCs that have a large propensity to raise productivity levels do not so strongly depend on alternative means to increase their overall export competitiveness. Fairly underdeveloped countries such as the LDCs, however, have a rather limited possibility to increase productivity levels and therefore they more strongly depend on alternative measures to raise their export performance. In accordance with the conceptual framework used here, these alternative means include means to reduce operation costs and to raise the product quality. But these two possibilities are also rather restricted in the least developed countries case. This is because already low levels of resource costs make it difficult to further reduce these costs, and rather low levels of technological know-how make it difficult to increase product quality. The combination of these factors suggests a very strong focus on transaction costs, including insurance and freight.

In other words, the least developed countries, which have the greatest need to increase domestic productive capacities and international export competitiveness, also face the greatest challenges to achieve these objectives. This is because the least developed countries, compared with more advanced developing countries, are confronted with rather limited possibilities to decrease operation costs, limited propensities to increase productivity levels and a limited potential to improve product quality. It is important that the development community recognizes these specific challenges confronting the least developed countries and increases its efforts in accordance.

IV. Summary and conclusion

The comparison between MDTCs and LDCs highlights the strong influence of trade on development. This influence can be a positive one, as highlighted by the experience of the MDTCs, or it can be a negative one, as highlighted by the experience of many LDCs. While both country groups display a comparable level of integration in international trade, they display a rather distinct form of integration in international trade. A positive form of integration in international trade is characteristic for the MDTCs and a negative form of integration in international trade is characteristic for the LDCs. The form of integration in international trade is influenced by the level of exports in relation to the level of imports, which in turn is influenced by the specialization of countries in international trade.

Between 1980 and 1999, the MDTCs have persistently increased their export concentration in manufactures exports, especially high-tech manufactures exports, while the LDCs have maintained a strong concentration in primary commodity exports, especially non-fuel primary commodity exports. The different forms of export specialization have important implications for export performance. This is because world market prices of high-tech

manufactures exports are relatively stable, while the world market prices for non-fuel primary commodities are both unstable and typically declining. Furthermore, the world demand for high-tech manufactures exports is relatively dynamic, while the world demand for non-fuel primary commodities is rather static and increasingly saturated. But the MDTCs have not only managed to successfully diversify their export baskets and expand in more dynamic export markets, they have also managed to increase their share in total world exports. The LDCs, by contrast, continue to have a rather homogenous export basket and specialize in rather sluggish export markets. Furthermore, they were confronted with a decreasing share in total world exports.

In correspondence, between 1980 and 1999 the MDTCs have significantly increased their levels of both exports and imports and have benefited from a positive integration in international trade, but the LDCs have maintained a rather low level of exports compared to imports and have therefore seen a more negative integration in international trade. The rather low levels of exports combined with relatively high level of imports cause a large net trade deficit in the least developed countries. In poor developing countries such a trade deficit causes a shortage of foreign exchange, which necessitates either a contraction of imports or an accumulation of external debt. Neither outcome is desirable. The former will cause a contraction of domestic investments and/or a contraction of domestic consumption, and the latter will cause an increase of external debt service obligations and further exacerbate the shortage of foreign exchange. Such outcomes constitute and reinforce a cycle of underdevelopment in which a weak export performance, weak import capacities, low investments, low savings, low consumption and increasing poverty reinforce each other.

In short, the influence of trade on development can be positive or negative. Whether it is one or the other, does not so much depend on the level of integration in international trade than the form of integration in world trade, and the form of integration in international trade is not so much dependent on the openness to international trade than the specialization of countries in export markets. Finally, whether countries are able to diversify their export baskets and push into more dynamic export markets, or whether they continue to specialize in unfavorable export items and operate in sluggish export markets, depends on whether the countries can improve the international export competitiveness of their products, which in turn depends on their domestic productive capacities.

But the specialization in manufactures, compared with the specialization in agricultural goods, is not only beneficial because it is typically associated with larger gains from international trade, but also because it is associated with a higher propensity to increase domestic productivity levels. The different propensities to increase productivity levels in turn have implications for the type of strategies that more industrialized countries can pursue in order to increase their productive potentials and their export performance, and the types of strategies that the least developed countries can pursue to achieve these ends. In sum, the least developed countries face the largest challenges. This is because they not only have

limited possibilities to reduce production costs and increase product quality; they also have relatively limited possibilities to increase productivity levels. As a result, the corresponding development strategies necessarily have a strong focus on transaction costs.

In conclusion, the production and trade of manufactures and primary commodities have different developmental implications. But while it is important to take note of this difference, it is equally important to not overemphasize them. This is because the specialization in manufactures is not necessarily a blessing and the specialization in non-fuel commodity exports is not necessarily a curse. The former does not automatically lead to a virtuous cycle of development, nor does the latter automatically cause a vicious trap of underdevelopment to persist. It can be observed that the world market for many low-tech manufactures increasingly resembles the world market for many non-fuel primary commodities (adding-up problems and declining prices), and that the world market for selected primary commodities resembles more closely the world market for more sophisticated manufactures (strong demand and remunerative prices)²⁰. This implies that the growth path of many countries that specialize in low-tech manufactures is highly fragile and that the development prospects of countries that specialize in primary commodities are not necessarily gloomy²¹. In fact, a comparison between farm-gate prices and retail prices of many commodities shows a large increase of the price spread. These price trends suggest that countries, which manage to upgrade their commodities and move-up in the value added chain, can size substantial gains. It is this where the least developed countries should aspire to and what their development partners should actively support. And in accordance it is important that developing countries better mainstream trade in their development strategies, including their poverty reduction strategies, and that their development partners more actively support strategies to develop productive capacities and export competitiveness²². In small and poor developing countries, such as the least developed countries, the development of export competitiveness is a precondition for import capacities and the combination of both is a precondition for these countries to better integrate in international trade, to gain from trade and to reverse their marginalization.

In correspondence, the development of productive capacities and export competitiveness

20) For a discussion of the difficulties associated with trade in low-tech manufactures, see UNCTAD (2002b).

21) In its contribution to the Third United Nations Conference on LDCs, the International Trade Centre UNCTAD/WTO has introduced a number of entrepreneurs from least developed countries that have managed to overcome various export hurdles and have successfully diversified into dynamic export markets (International Trade Centre UNCTAD/WTO, 2001c; von Kirchbach, 2001). But so far these are only islands of success.

22) One important venue through which development partners could deliver aid in this area is through the Integrated Framework for Trade-related Technical Assistance, especially if the stakeholders in the Integrated Framework—which include the IMF, ITC, UNCTAD, UNDP, WTO and World Bank—pool their respective competencies and engage in concrete capacity-building projects.

should be a core objective of development strategies. But while the main responsibility for such development strategies naturally rests with the developing countries themselves, the final success of these development strategies also strongly depends on their development partners. The development partners must increase the level of debt relief and the level of aid. Furthermore, the development partners must increase the effectiveness of their aid. For the latter purpose the donor countries need to untie their aid to the developing countries, eliminate their subsidies for their agricultural sectors, eliminate their subsidies for their low-tech manufactures sectors, and provide meaningful market access for developing countries. While developed countries make progress in some of these areas, many developed countries increase wage subsidies which benefit primarily their low-tech manufactures sectors and virtually all developed countries maintain very high aggregate support to their agricultural sector.

The subsidies that are poured into uncompetitive sectors in industrialized countries decrease the effectiveness of the aid that is spend on productive sector development in developing countries. This is because the subsidies make it impossible for entrepreneurs in developing countries to compete with their counterparts from developed countries on an equal footing. The imbalance between subsidies and development aid highlights the extent and severity of the situation. For comparison, in 2000 alone the aggregate support measures of OECD countries for their domestic agricultural sectors were worth US-Dollar 327 billion, and the total net aid disbursements of OECD countries to all 49 least developed countries were worth only US-Dollar 12.5 billion. In other words, total aid was worth less than two weeks of aggregate agricultural support²³⁾. The agricultural subsidies of OECD countries certainly contributed to the fact that many LDCs, which used to be net-exporters of food items until the late 1980s, are net-importers of food items since then.

But these policies of the industrialized countries not only have a direct negative impact on the LDCs; they have an indirect negative impact on the LDCs as well. This is because subsidies in the industrialized countries also impede the development prospects of more advanced developing countries, which in turn impedes the development prospects of the least developed countries. In other words, if more advanced developing countries face a glass ceiling and get stuck on the ladder of development, the least developed countries cannot, despite increased development assistance, move up on the ladder of development. This is because the more advanced countries will continue to compete against the least developed countries in a market for agricultural goods and basic manufactures and, subsequently, the more advanced countries will prevent the least developed countries to significantly increase their share in both agricultural exports and basic manufactures exports. This has negative implications for their export revenues, their income levels and ultimately their poverty reduction efforts.

23) Calculations based on OECD/DAC electronic database and OECD (2001).

Finally, the elimination of subsidies is itself an insufficient condition to actually boost exports of LDCs. Another important condition to support the exports of LDCs is the provision of meaningful market access. To this end, industrialized countries—which already dismantled many quantitative import restrictions²⁴⁾—now need to also dismantle non-tariff barriers. By contrast, the more advanced developing countries must reduce both their quantitative import barriers and their non-tariff barriers. So far too many countries maintain too many tariff peaks, which essentially impede horizontal diversification into non-traditional goods, and too many countries use tariff escalations, which significantly limit vertical diversification into higher value-added goods.

In sum, all efforts of least developed countries to develop their export competitiveness will be futile if more advanced countries do not pursue complementary policies. The developed countries must provide sufficient financial resources so that the least developed countries can effectively develop their export sectors. But furthermore they must quite simply provide export opportunities so that the least developed countries can actually increase their export volumes. Both developed countries and more advanced developing countries should concentrate on developing new and dynamic industries rather than subsidizing old and uncompetitive ones. This is because industries that are considered “sunset industries” in the more advanced countries, are actually potential “sunrise industries” in the less developed countries, according to the theories of dynamic comparative advantage. Finally, the developed countries and the advanced developing countries should further dismantle their quantitative import restrictions and they should also eliminate non-tariff barriers. In order for the Doha Round to truly be a development round, it is essential that all these challenges be addressed in tandem.

Considering the positive influence that trade may have on the development process, the improvement of trade capacities in developing countries should become a core concern of the development activities of the entire development community. In correspondence, the guiding slogan for development assistance should not be “more trade instead of aid”, but “more aid for trade”.

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24) Examples for which are recent initiatives of the QUAD countries for LDC exports, including the initiative by Canada, the EBA initiative by the EU, the 99 Percent Initiative by Japan, and the AGAO by the USA. For a discussion of these initiatives and their expected impact see Hoekman, Ng and Olarreaga (2001), Oxfam/IDS (2001), UNCTAD (2001b) and UNCTAD/Commonwealth Secretariat (2001). It is interesting to note that the different analyses derive at vastly different conclusions about the benefits of these initiatives.

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