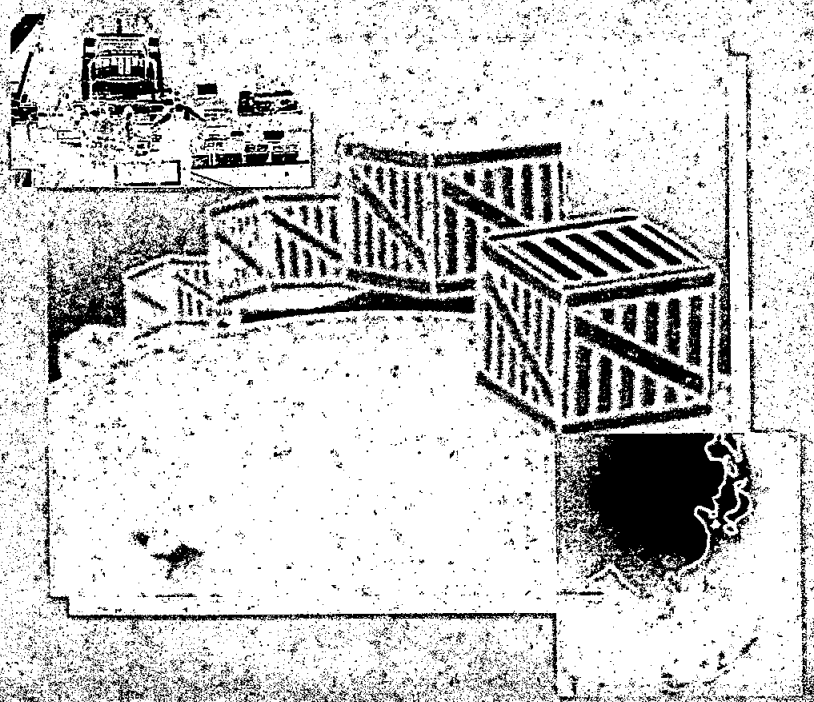
EXPORT PROMOTION STRATEGIES *of the* SEACEN COUNTRIES

Edited by
Danda Pani Paudel



THE SEACEN CENTRE

EXPORT PROMOTION STRATEGIES OF THE SEACEN COUNTRIES

by

Danda Pani Paudel

The South East Asian Central Banks (SEACEN)
Research and Training Centre
Kuala Lumpur, Malaysia

EXPORT PROMOTION STRATEGIES OF THE SEACEN COUNTRIES

© 1994 The SEACEN Centre

Published by The South East Asian Central Banks (SEACEN)
Research and Training Centre
Lorong Universiti A,
59100 Kuala Lumpur, Malaysia.
Tel No: 03-7585600
Fax No: 603-7574616
Telex: MA 30201
Cable: SEACEN KUALA LUMPUR

ISBN: 983-9553-46-1

All rights reserved. No part of this publication
may be reproduced, stored in a retrieval system,
or transmitted in any form by any system, electronic,
mechanical, photocopying, recording or otherwise,
without the prior permission of the copyright holder.

Printed in Malaysia by Graphic Stationers Sdn. Bhd.

FOREWORD

As is common for almost all developing countries, shifting emphasis away from import substitutes towards exportables has been a key goal of all the SEACEN countries at certain points in their economic histories. Towards this, and in response to the various international developments including the successive oil shocks, the collapse of the Bretton-Woods System, persistently high global inflation, widespread recession and on top of all these, the successful experience of Korea, Singapore and the Republic of China, Taipei should impress upon the rest of the SEACEN countries the need to start significant efforts in the promotion of exports. In addition, some of the SEACEN countries which have adopted structural adjustment programs should favor export promotion strategies along the policy of the World Bank and International Monetary Fund. But for the SEACEN countries which have pursued various export promotion measures, the implementation and hence the resulting trade performance have not been simply linear. Their respective success and failure points are divergent while time horizons stretch out differently.

This study attempts to assess the export performance of the SEACEN countries; their involvement in designing and implementing export promotion strategies; as well as the problems and issues faced by them. The study also examines empirically the export-led growth hypothesis as well as the major factors in determining export demand for the SEACEN countries. As shown in the study, the empirical tests are more significant in those country cases where the promotional activities have been undertaken earlier and hence, with a good track record of industrialization and higher per capita income.

The research project is a collaborative effort between The SEACEN Centre and its member banks. Nine member central banks participated in this project, namely, Bank Indonesia, the Bank of Korea, Bank Negara Malaysia, Nepal Rastra Bank, Bangko Sentral ng Pilipinas, the Monetary Authority of Singapore, the Central Bank of Sri Lanka, the Central Bank of China, Taipei, and the Bank of Thailand. Each member central bank made available at least one researcher in preparing the respective country studies which constitute Part II. The SEACEN Centre in this regard wishes to express its sincere gratitude to the participating member central banks for their kind cooperation and strong support in bringing forward this project to a successful completion.

The SEACEN Centre for its part coordinated the whole project. In this regard, Dr. Danda Pani Paudel, Senior Economist seconded from Nepal Rastra Bank to The SEACEN Centre, was responsible for the whole research design and the coordination among the country researchers. He edited the country chapters and also prepared the overview on the export promotion strategies of the SEACEN countries. The overview forms Part I of the study.

At the initial stage of the project, Dr. Paudel was kindly assisted by his research associate, Mr. Wong Chee Seng. Mrs. Jami'ah Jaffar took care of the proof-reading work, and the manuscript was typed by Miss Karen How. Dr. Paudel would also like to thank the Publications Unit for its assistance.

The views expressed in this volume, however, are those of the respective authors and do not necessarily reflect the views of the member central banks and monetary authorities or that of The SEACEN Centre.

Dr. Vicente B. Valdepeñas, Jr.
Director
The SEACEN Centre

Kuala Lumpur
May 1994

EXECUTIVE SUMMARY

Being a collaborative project, the report comprises two parts namely the overview on the export promotion strategies of the SEACEN countries prepared by the researcher in-charge of the project; and, country chapters contributed by country researcher(s). Most of the SEACEN countries have placed emphasis away from import substitutes towards exportables due mainly to the successive oil shocks, persistently high global inflation, the collapse of the Bretton-Woods System, widespread recession and on top of all these, the successful experience of Korea, Singapore and the Republic of China, Taipei. While the ultimate objective of export promotion is to promote the efficiency, capacity utilization and growth, the successful implementation of the export promotion police depends exactly on those factors that differ from country to country. This study aims at assessing the export performance of the SEACEN countries; their involvement in designing and implementing export promotion strategies as well as analysing empirically the export-led growth hypothesis for the SEACEN countries.

A brief review of the reform experiences sheds light on how and when the SEACEN countries started the overall trade liberalisation in general, and export-trade in particular. A careful examination of various liberalisation exercises finds that Korea, Singapore and ROC-Taipei experimented with the export promotion measures as early as the 1960s, while Malaysia and Thailand adopted such measures in the mid- 1970s. The rest of the SEACEN countries namely Indonesia, Nepal, the Philippines and Sri Lanka, starting from late 1970s, are still in the process of reform towards the adoption of a fully liberalised trade policy. The overall performance indicates that those countries which adopted the export promotion measures earlier have been more successful in maintaining an impressive growth in major sectors. Over time, there is a structural shift in the composition of exports, i.e., the manufacturing exports are replacing the primary commodity exports, although market concentration is still a great concern for most of the SEACEN countries.

In addition to the qualitative assessment of the export promotion measures, this study also identifies empirically the direction of relationship between exports and economic growth as well as the major factors affecting export demand for the SEACEN countries. Prior to the regression estimation, unit root test and cointegration test were conducted to test the stationarity of the time series used, and the Granger Causality Test was performed using Akaike's and Schwarz's optimal lag criteria. As such, causality tests were performed with and without

component effects of exports on economic growth to find which variable influences another. According to the results, there is a unidirectional causality from output growth to export growth in the cases of Korea and Malaysia which supports the export-reducing growth hypothesis. In contrast, the internally-generated-exports (IGE) hypothesis, i.e., growth-led exports, is supported in the case of Thailand. A negative feedback relationship, i.e., export-reducing growth and growth-reducing exports hypotheses, is found in the case of Singapore while a positive feedback relationship, i.e., IGE and export-promotion hypotheses are found in the case of ROC-Taipei. After suppressing the component effect of exports on GDP, there is either a change in the direction or the results are quite significant unlikely with component effect in the cases of Indonesia, Malaysia, Singapore, ROC-Taipei and Thailand. This means that the indirect effect of exports to growth and vice versa is a matter of concern in most of the SEACEN countries. In the cases of Nepal, the Philippines and Sri Lanka, the results are ambiguous at the 5-per cent level of significance in both situations. In sum, unlike the previous studies which assumed the export-led growth as *a priori* hypothesis for export promotion, the present causality test casts doubts on the so-called fashionable strategy of export-led growth.

Similarly, real exports from the SEACEN countries depend on individual SEACEN country's international competitiveness as proxied by real effective exchange rate as well as the income effect from the importing countries as represented by the export trade-weighted GDP of the top-fifteen major trade partners. Based on the empirical findings, the real effective exchange rate shows positive but statistically insignificant relation with the real export demand in the cases of the Philippines and Sri Lanka. For the rest of the countries, the real effective exchange rate is either highly significant or at least with the expected negative direction of relationship in explaining the real export demand. Similarly, except in the case of Nepal, for the rest of the SEACEN countries the export-weighted real GDP of importing countries explains positively and significantly the real export demand. Thus, one can suggest that the SEACEN countries should give due consideration to their real effective exchange rates and the export-weighted GDP of the importing countries in formulating and implementing export strategies.

Evidently, there are different problems and limitations among the SEACEN countries, although the SEACEN countries have experimented with various measures to promote exports through:

Fiscal incentives such as tax and duty concession, tariff and non-tariff measures;

Financial facilities such as credit, refinance, insurance and other related measures; and,

Institutional support such as central bank, commercial banks, export-import bank, specialised institutions for marketing information, trade fairs and missions.

Finally, the SEACEN countries, whether more successful or not, tend to further the scope for financing scheme, re-scheduling comparative advantage, diversifying their exports in view of the emerging trade blocks, etc., but not at the cost of efficiency to the whole economy.

TABLE OF CONTENTS

	Page
FOREWORD	iii
EXECUTIVE SUMMARY	v
LIST OF TABLES	xix
LIST OF CHARTS	xxii
LIST OF APPENDICES	xxiii

PART I
EXPORT PROMOTION STRATEGIES OF THE SEACEN COUNTRIES: AN OVERVIEW

Introduction	3
Significance	3
Objectives	4
Research Design	5
Methodology	5

Chapter 1: An Overview of Export Promotion Strategies of the SEACEN Countries

I. Introduction	6
II. The Salient Features of Export Trade in the SEACEN Countries	7
2.1 Review of Trade Policy Environment	7
2.2 Contribution of Export to the Economy	10
2.3 Growth Trend and Changing Patterns of Export	13
2.4 Exports and Growth: Some Empirical Evidence	20
2.4.1 Causality Test Between Exports and Economic Growth	20

Page

2.4.2 Unit Root Test 22
2.4.3 Cointegration Test 24
2.5 Demand for Exports 28
2.5.1 Unit Root Test 33
2.5.2 Cointegration Test 35

III. Export Promotion Policies in the SEACEN Countries 40

IV. Problems and Issues on Export Promotion 51

V. Policy Recommendations for Effective Export Promotion 54

VI. Summary and Conclusion 58

References 64

PART II
COUNTRY CHAPTERS

Chapter 2: Export Promotion Strategies: Indonesia

I. Introduction 81

II. Export Trade and Salient Features 82
2.1 Trade and Commerce Policy Environment 82
2.2 Contribution of Exports to the Economy 83
2.3 Growth Trend and Changing Patterns of Exports 84
2.4 Some Empirical Evidence 87
2.4.1 Findings 89
2.4.2 Export Demand 90
2.4.3 Methodology 91
2.4.4 Estimation Results 92

III. Export Promotion Policies 92
3.1 Monetary Policy Measures 92
3.2 Foreign Exchange System 94
3.3 Exchange Rate Policy 95

		Page
3.4	Financial Market Development	96
3.5	Fiscal Policy Measures	97
3.5.1	Tariff and Non-Tariff Barriers	99
3.5.2	Export Restrictions	100
3.6	Institutional Arrangements	103
3.6.1	Trade Mission and Trade Houses	103
3.6.2	Export Processing Zone	106
3.7	Export Finance Scheme	106
3.8	Export Infrastructure and Industrial Sites	109
3.9	Role of Central Bank in Export Promotion	111
IV.	Problems and Issues on Export Promotion	113
V.	Policy Recommendations	114

Chapter 3: Export Promotion Strategies: Korea

I.	Introduction	127
II.	Export Trade and Salient Features	128
2.1	Growth Trend and Changing Patterns of Exports	128
2.1.1	Growth Trend of Exports	128
2.1.2	Changing Patterns of Exports	129
2.1.2.1	Export Structure by Commodities	129
2.1.2.2	Export Structure by Region	130
2.2	Contribution of Exports to the Economy	131
2.2.1	Production	133
2.2.2	Employment	133
2.2.3	Imports	134
2.2.4	Other Macroeconomic Variables	134
2.3	Some Empirical Analyses	134
2.3.1	Function	135
2.3.2	Null Hypotheses	135
2.3.3	Results	135
III.	Export Promotion Policies	137
3.1	An Overview of Trade and Commercial Policy	137
3.2	Monetary Policy Measures and Exchange Rate Policy	139

Page

3.2.1 Export Financing System 139
3.2.2 Exchange Rate Policy 140
3.3 Fiscal Policy Measures 143
3.3.1 Tariff Incentives 143
3.3.2 Tax Incentives 143
3.3.3 Administrative Support 143
3.4 Institutions and Facilities for Export Promotion 144
3.4.1 Financial Institutions 144
3.4.1.1 EXIMBANK 144
3.4.1.2 Korea Development Bank 145
3.4.2 General Trading Companies 145
3.4.3 Other Institutions 146
3.4.3.1 Korea Trade Promotion Corporation 146
3.4.3.2 Korea Foreign Trade Association 146

IV. Problems and Issues on Export Promotion 147

V. Policy Recommendations 149

VI. Summary and Conclusion 150

References 151

Chapter 4: Export Promotion Strategies: Malaysia

I. Introduction 161

II. Export Trade and Salient Features 163
2.1 Industrialization and Trade Strategies 163
2.2 Contribution of Exports to the Economy 165
2.3 Growth Trend and Changing Patterns of Exports 166
2.4 Direction of Exports 172
2.5 Implications on Balance of Payments 175
2.6 Export and Growth: Some Empirical Evidence 180
2.6.1 Some Recent Studies 180
2.6.2 The Model and Method of Specification 181
2.6.3 Estimation Results 182
2.6.4 Estimation of Export Demand Function 183

	Page
2.6.4.1 Theoretical Framework	183
2.6.4.2 Export Function	184
2.6.4.3 Estimation Results	184
III. Export Promotion Policies	185
3.1 Finance and Credit Facilities	185
3.1.1 Export Credit Refinancing	186
3.1.2 Malaysian Export Credit Insurance Berhad	187
3.2 Fiscal Incentives	188
3.3 Institutional Arrangement	190
3.3.1 Free Trade Zones	190
3.3.2 Licensed Manufacturing Warehouses	191
3.3.3 Services of Trade Commissioners	191
3.3.4 Malaysian Export Trade Centre	191
3.3.5 Missions and Fairs Programs	192
3.3.6 Countertrade	192
3.3.7 Bilateral and Multilateral Negotiations for Better Accessibility of Malaysia's Exports	192
3.4 Foreign Direct Investment	193
3.5 Small- and Medium-Scale Industries	194
3.5.1 Incentives	195
3.5.2 Financial Assistance	195
IV. Problems and Issues on Export Promotion	196
4.1 Structural Weaknesses in the Export Sector	197
4.1.1 Export Concentration	197
4.1.2 Export Market Concentration	198
4.1.3 Export Volatility	198
4.2 International Comparison of Malaysia's Position in Terms of Export Diversification and Concentration Index	199
4.3 Issues and Implications	200
4.3.1 Niche Strategies	200
4.3.2 Incentive System	202
4.3.3 Human Resource Development	202
4.3.4 Technology Development	203
4.3.5 Trade Barriers	203

Page

V. Policy Recommendations 204

5.1 Revising the Current Incentive System 204
5.2 Identification and Creation of New Market Niche 205
5.2.1 Expanding Intra-ASEAN Trade Opportunities 205
5.2.2 The Generalised System of Preferences 205
5.2.3 Intensifying South-South Trade 206
5.2.4 Revitalizing the Export Targeting System 207
5.3 Production Standards and Quality 207
5.4 Effective Human Resource Development 207
5.5 Institutional Support to Enhance Export 208

VI. Summary and Conclusion 208

References 210

Chapter 5: Export Promotion Strategies: Nepal

I. Introduction 217

II. Export Trade and Salient Features 217

III. Export Promotion Policies 221
3.1 Review of Export Policy 221
3.2 Recent Policy 223

IV. Problems and Issues on Export Promotion 225

V. Policy Recommendations 226

VI. Summary and Conclusion 227

Chapter 6: Export Promotion Strategies: The Philippines

I. Introduction 229

II. Export Trade and Salient Features 230
2.1 Export Growth 230
2.2 Structure of Merchandise Exports 231

Page

2.3 Direction of Trade 236
2.4 Empirical Evidence on the Determinants of Exports 238

III. Export Promotion Policies 239
3.1 Review of Trade, Industrial and Monetary Policy 239
3.2 Recent Developments in Monetary Policy 240
3.2.1 Foreign Exchange Policy 240
3.2.2 Foreign Currency Loans 241
3.2.3 Rediscounting Policy 242
3.3 Other Financial Assistance to Exporters: Export Insurance and Guarantees 242
3.4 Fiscal Policy 243
3.4.1 Fiscal Incentives 243
3.4.2 Duty and Tax Concessions 243
3.5 Institutional Measures for Export-Oriented Industries 244
3.5.1 Bonded Manufacturing Warehouses 244
3.5.2 Export Processing Zone Authority 245
3.5.3 Incentives 245

IV. Problems and Issues on Export Promotion 246

V. Policy Recommendations 248

VI. Summary and Conclusion 249

References 251

Chapter 7: Export Promotion Strategies: Singapore

I. Introduction 255

II. Export Trade and Salient Features 255
2.1 Contribution of Exports to the Economy 255
2.2 Growth Trend and Changing Patterns of Exports 258
2.3 Markets 261
2.4 Composition of Exports 263

		Page
III.	Export Promotion Policies	264
	3.1 Trade and Commerce Policy Environment	264
	3.2 Exchange Rate Policy	264
	3.3 Fiscal Policy	264
	3.4 Export Finance	265
	3.4.1 MAS Rediscounting Scheme	265
	3.4.2 The Export Credit Insurance Scheme	265
	3.5 Institutional Arrangements	266
	3.6 Export Information System	267
	3.7 Schemes of Trade Preferences	267
IV.	Problems and Issues on Export Promotion	267
	4.1 Persistent Trade Deficit	267
	4.2 Labor Shortage	267
	4.3 Dependence on Performance of External Economies	268
	4.4 Trade Actions	268
V.	Policy Recommendations	268

Chapter 8: Export Promotion Strategies: Sri Lanka

I.	Introduction	285
II.	Export Trade and Salient Features	286
	2.1 Contribution of Exports to the Economy	286
	2.2 Growth Trends and Changing Patterns of Exports	288
	2.3 Structure of Exports on Country-wise Basis	291
	2.4 Causality Between Exports and Economic Growth	294
	2.4.1 Estimated Results	295
	2.5 Export Demand Function	296
	2.5.1 Estimated Results	297
III.	Export Promotion Policies	297
	3.1 Review of Trade and Commerce Policy Environment	297
	3.2 Role of the Central Bank of Sri Lanka	300
	3.2.1 Monetary Policy Measures	300
	3.2.2 Short-Term Refinance Schemes	300

Page

3.2.3 Refinance Under the Medium- and Long-Term Credit Fund 301
3.2.4 Exchange Rate Policy 303

3.3 Fiscal Incentives 304
3.4 Banks and Financial Institutions 313
3.4.1 Commercial Banks 313
3.4.2 Development Banks 313
3.4.3 Other Institutions 315

IV. Problems and Issues on Export Promotion 321

V. Policy Recommendations 324

Chapter 9: Export Promotion Strategies: The Republic of China (ROC), Tapei

I. Introduction 327

II. Export Trade and Salient Features 328
2.1 Contribution of Exports to the ROC's Economy 328
2.2 Growth Trend and Changing Patterns of Exports 328
2.3 Empirical Analyses 335

III. Export Promotion Policies 339
3.1 Review of Trade and Commerce Policy Environment 339
3.2 The Role of the Central Bank of China 341
3.2.1 Monetary Policy Measures 341
3.2.2 Exchange Rate Policy 342
3.3 Nineteen-Point Economic and Financial Reform 343
3.4 The Export-Import Bank of the ROC 343
3.5 Fiscal Policy Measures 344
3.5.1 Regulations for Rebate of Taxes on Export Products 344
3.5.2 Investment Incentives 344
3.6 Institutional Arrangements 345
3.6.1 Export Processing Zone 345
3.6.2 Bureau of Commodity Inspection and Quarantine 346

Page

3.6.3 China External Trade Development Council 346
3.6.4 Hsinchu Science-Based Industrial Park 348
3.6.5 Vocational Training Centers 348

3.7 Other Incentives 348

IV. Problems and Issues on Export Promotion 348

V. Policy Recommendations 349
5.1 Continuous Expansion of Foreign Trade 349
5.2 Upgrading the Industrial Structure 350
5.3 Promoting Big Trading Companies 350
5.4 Joining Important International Economic Organizations 350

VI. Summary and Conclusion 351

References 353

Chapter 10: Export Promotion Strategies: Thailand

I. Introduction 363

II. Export Trade and Salient Features 363
2.1 Contribution of Exports to the Economy 363
2.1.1 Contribution of Exports to Gross Domestic Product 364
2.1.2 Contribution of Exports to Employment 366
2.1.3 Contribution of Exports to Imports 367
2.2 Growth Trend and Changing Patterns of Exports 368
2.2.1 Structural Change in Type of Exports 368
2.2.2 Direction of Export Market 371
2.2.3 Trends in Imports 372
2.2.4 Foreign Direct Investment 372

III. Export Promotion Policies 376
3.1 Review of Trade and Commerce Policy Environment 376
3.2 Role of Central Banks 379

Page

3.2.1 Export Credit 380
3.2.2 Exchange Rate Policy to Promote Exports 381
3.3 Fiscal Policy 383
3.3.1 BOI Incentives 383
3.3.2 Import Duty and Tax Refund 385
3.3.2.1 Customs Department 388
3.3.2.2 Fiscal Policy Office 388
3.3.2.3 Bonded Factories and Export 389
3.3.2.4 Non-Tariff Measures 390
3.4 Banks and Financial Institutions for Export Finance 391
3.4.1 Commercial Banks 391
3.4.2 The Industrial Finance Corporation of Thailand 393
3.5 Supporting Services 393
3.5.1 Department of Export Promotion 393
3.5.2 Commercial Counselors 393
3.5.3 Export Development Fund 394
3.5.4 Export Development Committee 394

IV. Problems and Issues on Export Promotion 394

V. Policy Recommendations 396

VI. Summary and Conclusion 397

References 399

LIST OF TABLES

Table **Page**

Chapter 1: An Overview of Export Promotion of the SEACEN Countries

1.1 Exports by 0-9 SITC Section 15
1.2 Exports by Principal Commodity 16
1.3 Imports by Commodity Group 17
1.4 Unit Root Test Results 23
1.5 Cointegration Test Results 26
1.6 Granger Causality Test Results 27
1.7 Direction of Causality 29
1.8 Unit Root Test Results 34
1.9 Cointegration Test Results 35
1.10 Regression Results 37

Chapter 2: Export Promotion Strategies: Indonesia

2.1 Causality Test for Indonesia's Exports and GDP 89
2.2 Structure of Export Duty Tariffs 102
2.3 Structure of Import Duty Tariffs for Industrial Goods 103

Chapter 3: Export Promotion Strategies: Korea

3.1 Export Structure by Commodities by Industry 129
3.2 Export Structure by Region 131
3.3 Major Incentives for Export Promotion 138
3.4 Major Steps in Relaxing Foreign Exchange Control 141
3.5 Credit Commitments and Loan Disbursement by EXIM Bank 144
3.6 Exports to the Advanced Countries 147

Table **Page**

Chapter 4: Export Promotion Strategies: Malaysia

4.1 Malaysia: Exports of Primary Commodities 168
4.2 Causality Tests with Malaysian Exports and Economic Growth 183
4.3 Utilization of Export Credit Refinancing Facilities by Industrial Sector 186
4.4 Exports Declared by Markets and by Products 187
4.5 Export Diversification and Export Concentration Index 201

Chapter 5: Export Promotion Strategies: Nepal

5.1 Nepal: Economic Indicators 219
5.2 Nepal: Direction of Foreign Trade 220

Chapter 6: Export Promotion Strategies: The Philippines

6.1 Philippines: Selected Indicators, 1970-1991 232
6.2 Exports by Major Commodity Group, 1970-1991 233
6.3 Philippines: Composition of Exports 234
6.4 Exports of Electronics and Garments (Regular and Consigned), 1980-1991 235
6.5 Direction of Exports, 1970-1991 237

Chapter 7: Export Promotion Strategies: Singapore

7.1 Share of Exports in GDP 257
7.2 Granger Causality Tests 258
7.3 Singapore: Total Trade 259
7.4 Annual Growth Rate of Exports 260
7.5 Export/Import, Export/GDP Ratio 261
7.6 Singapore: Domestic Exports by Selected Countries 262
7.7 Composition of Exports 263

Table **Page**

Chapter 8: Export Promotion Strategies: Sri Lanka

8.1 Sri Lanka: Composition of Exports 287
8.2 Sri Lanka: Merchandise Exports 292
8.3 Sri Lanka: Merchandise Imports 293

Chapter 9: Export Promotion Strategies: The Republic of China (ROC), Taipei

9.1 Average Growth Rate of Foreign Trade 330
9.2 Export Structure 332
9.3 Structure of Exports by Destination 333
9.4 Major Items in Balance of Payments 335
9.5 Results of Causality Test Between Exports and Economic Growth 336

Chapter 10: Export Promotion Strategies: Thailand

10.1 Contribution of Exports to GDP Growth 365
10.2 Supply Structure of GDP Growth 365
10.3 Employment Distributed by Sector 366
10.4 Proportion of Trade in GDP 367
10.5 Structure of Exports 369
10.6 Structural Changes in Exports 370
10.7 Direction of Export Market 371
10.8 Structure of Imports 373
10.9 Net Inward Foreign Direct Investment 374
10.10 Net Flows of Foreign Direct Investment by Countries 375
10.11 BOT Rediscounts of Promissory Notes for Export Activities by Commodity 382
10.12 Number of BOI-Approved Investment Projects With Export Requirement by Type of Activity 386
10.13 Export Sales and Export Propensities of Promoted Firms by Nationality 387
10.14 Form of Export Credit Extended by Commercial Banks 392

LIST OF CHARTS

Chart		Page
Chapter 1: An Overview of Export Promotion of the SEACEN Countries		
1.1	Export as Percentage of Gross Domestic Product	12
1.2	Manufacturing Export as Percent of Total Export	12
1.3	Export/Import Ratio	12
1.4	Average Export Growth in Percent	12
1.5	Exports in US$ Million	18
	1.5.1 U.S.A. as an Export Destination	19
	1.5.2 Japan as an Export Destination	19
	1.5.3 EEC as an Export Estination	19
	1.5.4 ASEAN Nations and NIEs as an Export Destination	19
Chapter 2: Export Promotion Strategies: Indonesia		
2.1	Export/Import Ratio	85
2.2	Indonesia: Trade Balance and Current Account	88
Chapter 3: Export Promotion Strategies: Korea		
3.1	Export Structure by Commodities	130
3.2	Korea: Exports and GNP Growth	132
3.3	Proportion of Exports to GNP	132
Chapter 4: Export Promotion Strategies: Malaysia		
4.1	Structure of Exports	169
4.2	Malaysia: Principal Markets of Exports	173
4.3	Balance of Payments	176
4.4	Trade Account	177
4.5	Exports/Imports and Exports/GDP Ratio	178
Chapter 9: Export Promotion Strategies: The Republic of China (ROC), Taipei		
9.1	The Ratio of Trade to GNP	329
9.2	Export Structure	331

LIST OF APPENDICES

Appendix **Page**

Chapter 1: An Overview of Export Promotion of the SEACEN Countries

1.1 SEACEN Countries: Selected Economic Indicators 70
1.2 SEACEN Countries: Export Destination by Country and Region 71
1.3 Lag Length Test for Causality Test 72
1.4 SEACEN Countries: Total Exports and Share of Export Partners 73
1.5 Selected SEACEN Countries: Error Correction Equations 74
1.6 SEACEN Countries: Nominal and Real Effective Exchange Rates (1985 = 100) 75
1.7 SEACEN Countries: Export-Weighted Real GDP Index of Export Partners 76
1.8 SEACEN Countries: Real Gross Domestic Products and Real Exports 77
1.9 SEACEN Countries: Export Growth and Sectoral Share of GDP 78

Chapter 2: Export Promotion Strategies: Indonesia

2.1 Indonesia: Balance of Payments (Million U.S. $) 116
2.2 Export by SITC Commodity Groups 118
2.3 Import by SITC Commodity Groups 119
2.4 Value of Non-Oil/LNG Exports 120
2.5 Indonesia: Destination of Exports 122
2.6 Indonesia: Employment by Sector, 1971-1991 124
2.7 Indonesia: Gross Domestic Product, 1975-1991 125

Chapter 3: Export Promotion Strategies: Korea

3.1 Korea: Export Financing System 152
3.2 Statistical Table 155
3.3 Export by Country 157
3.4 Import by Country 159

Appendix **Page**

Chapter 4: Export Promotion Strategies: Malaysia

4.1 Malaysia: Composition of Exports 212
4.2 Malaysia: Gross Exports by Major Countries 213
4.3 Malaysia: Gross Imports by Major Countries 214
4.4 Empirical Test of Granger Causality 215

Chapter 6: Export Promotion Strategies: The Philippines

6.1 Data Used in Regression Analysis 253
6.2 Estimation Results 254

Chapter 7: Export Promotion Strategies: Singapore

7.1 Contribution of NODX to GDP Growth 269
7.2 Equations Used in Granger Causality Tests 270
7.3 Singapore: Exports by Level Terms 271
7.4 Singapore: Re-Exports by Selected Countries (in US$) 272
7.5 Singapore: Re-Exports by Selected Countries (Percent Share) 273
7.6 Singapore: Annual Growth of Re-Exports by Selected Countries 274
7.7 Singapore: Domestic Exports by Selected Countries 275
7.8 Singapore: Annual Growth of Domestic Exports by Selected Countries 276
7.9 Singapore: Non-Oil Domestic Exports by Selected Countries (in US$) 277
7.10 Singapore: Annual Growth of Non-Oil Domestic Exports by Selected Countries 278
7.11 Singapore: Non-Oil Domestic Exports by Selected Countries (Percent Share) 279
7.12 Domestic Exports to Other Countries by Commodity Section 280
7.13 Re-Exports to Other Countries by Commodity Section (in US$) 282
7.14 Re-Exports to Other Countries by Commodity Section (Percent Share) 284

Appendix **Page**

Chapter 9: Export Promotion Strategies: The Republic of China (ROC), Taipei

9.1 ROC, Taipei: Composition of Exports 354
9.2 ROC, Taipei: Selected Indicators 356
9.3 ROC, Taipei: Merchandise Export by Country 358
9.4 ROC, Taipei: Merchandise Import by Country 360

PART I

EXPORT PROMOTION STRATEGIES OF THE SEACEN COUNTRIES: AN OVERVIEW

Part I

EXPORT PROMOTION STRATEGIES OF THE SEACEN COUNTRIES

by
Danda Pani Paudel

Introduction

This chapter presents an overview of the export promotion policies and the export performance of SEACEN countries based on the information provided in the country chapters prepared by the respective country researchers. It should be pointed out that international trade in general was facilitated with the beginning of General Agreement on Tariffs and Trade (GATT) in the late 1940s. The eight multilateral trade negotiating rounds organized under the auspices of GATT in Geneva (1947) (1956), Annecy (1949), Torquay (1951), Dillon (1962), Kennedy (1968), Tokyo (1979) and Uruguay Rounds (1994) led to the liberalization of trade barriers; and, along with this an unprecedented expansion of the world trade. Despite these efforts, the liberalization of trade since then has been focused on regional blocks like NAFTA, EC, EFTA, SAARC, etc., putting a low profile to multilateral trade and further delaying the integration of the world economy.

The SEACEN countries also pursued import substitution policies in the post-war period, but the inward-looking strategies created a lot of problems. Therefore, the outward-looking policy or at least a balanced export/import development strategy became a pressing need for all the countries during the 1970s and 1980s. As a result, most of the SEACEN countries have benefitted from the export-oriented policies and all of them are now re-emphasizing the role of exports in their economies. With this perspective, the main objective of the study is to assess the export performance with regard to the export promotion strategies of the SEACEN countries.

Significance

External shocks as well as domestic macroeconomic instability during the 1970s and early 1980s induced most of the SEACEN countries to

liberalize their trade policies. Thus, during the late 1970s and the early 1980s with a view to accelerating export promotion, the SEACEN countries have initiated various policy measures including export credit refinance and insurance schemes. As a result of the export promotion efforts, the SEACEN countries have recorded significant changes in country and commodity-wise diversification as well as in the growth of the manufacturing sector and hence, in the level of exports. Despite a significant growth in exports, most of the SEACEN countries continued to face imbalances in their trade account and in the overall balance of payments for the last twelve years. The SEACEN countries still have much to do to promote their exports.

The growth and changing patterns in exports have further enhanced the role of the export sector in the SEACEN economies. But in most cases, the export sector is affected adversely by domestic factors such as the increasing trend of budgetary deficits; and, hence, a higher inflation, insufficient infrastructural support, the shortage of inputs for manufacturing sector, lack of financing, unstable exchange rates and other fiscal and institutional inefficiencies. The protectionist attitude of developed economies, despite some significant change, poses a serious threat to the promotion of exports in the SEACEN countries. Nevertheless, the SEACEN economies have been increasingly opening up. In this regard, a study of export promotion strategies with a view to assessing the export performance of the SEACEN countries is most timely and relevant.

Objectives

This study, as approved in the Board of Governors' Conference in Colombo, Sri Lanka, in January 1991, was conducted with the following objectives:

(1) To review the export performance of the SEACEN countries with reference to the relative significance of exports, pre- and post-refinancing schemes in the SEACEN economies, export structure, export growth and the direction of trade;

(2) To examine the problems and issues faced by the SEACEN countries that serve to impede their promotion of exports;

(3) To evaluate the effectiveness of export promotion strategies presently adopted by the SEACEN countries;

(4) To explore the possibility of new approaches in export promotion strategies; and,

(5) To examine the present role of the central bank and monetary authority in the export promotion as well as the potential for a further evolution of this role.

Research Design

This study was approved as a collaborative research project between The SEACEN Centre and the member central banks and monetary authorities. The report is divided into two parts. The first part is an overview of the country studies and it presents comparative and regional analyses; while the second part consists of the country chapters prepared by researchers designated by the member central banks and monetary authorities.

Methodology

The study makes use of both qualitative and quantitative analyses. The methodology proposed for the empirical investigation includes: (i) causality tests between export and economic growth; and, (ii) the demand for exports from the SEACEN countries. Prior to the estimation of both functions, both unit root test for stationarity in individual time series and cointegration test for stationarity of a linear combination of selected variables are applied in the first part of the study. Lack of access to econometric software might hinder country researchers from performing these stationarity tests. Therefore, the empirical results of the overview and country chapters may not necessarily converge. Some parts of the study relied heavily on qualitative analysis supported by appropriate statistical data series.

Chapter 1

AN OVERVIEW OF EXPORT PROMOTION STRATEGIES OF THE SEACEN COUNTRIES

I. Introduction

Exports have always played a crucial role in the process of economic development. For many reasons, including the increased trade and balance of payments deficits, deteriorating reserve position, and as a whole, their macroeconomic imbalances, many developing countries have relied on export promotion as a path to economic development. Specialization in the production of manufactures based on comparative advantage is thus a possible development route to industrialization, which is essential for the promotion of exports and in resolving growth problems.

Traditionally, most of the SEACEN countries were considered export/import economies. At the time, they used to export a few primary products and import consumer goods. Since World War II, most of the SEACEN countries considered import substitution as the best policy for economic development. But the vicious circle of low efficiency, low capacity utilization and slow growth caused by strict protection of the less efficient domestic industries caused the economy to stagnate. Thus, the SEACEN countries recognized that the promotion of exports provided advantages over import substitution by way of resource allocation, capacity utilization, economies of scale, improvement in technology, greater employment opportunities and output growth. Besides, in response to international changes including the first oil shock, collapse of the Bretton-Woods System, high global inflation, and on top of these the successful experience of Korea, Singapore and the Republic of China impressed upon the rest of the SEACEN countries the need to mount significant efforts at the promotion of exports. In addition, some of the SEACEN countries which have adopted structural adjustment programs have been observed to favor export promotion strategies in tune with the policy of the World Bank and the IMF.

Nevertheless, most of the SEACEN countries have experimented with various export promotion measures, but the implementation and hence

their outcomes depend upon country-specific factors. It is, therefore, important to assess the impact of various export incentives on the export performance and then on the national economies of the SEACEN countries.

In this regard, this chapter presents an overview of the export promotion strategies of the nine SEACEN member countries namely Indonesia, Korea, Malaysia, Nepal, the Philippines, Singapore, Sri Lanka, the Republic of China and Thailand based on the information provided in the country chapters prepared by country researchers.[1] Moreover, this chapter presents a comparative country analysis on the export promotion policies and their implication on export performance for the last two decades.

II. The Salient Features of Export Trade in the SEACEN Countries

2.1 Review of Trade Policy Environment

After World War II, most of the SEACEN countries adopted the import substitution policy with a view to protecting infant domestic industries. During this time, the inward-looking strategy became popular especially for the developing countries. At that time, most of the SEACEN countries were mainly agricultural-based. Prior to 1970, the SEACEN countries were over-dependent on the export of a few primary commodities demand for which were virtually inelastic. On the other hand, these countries imported basically consumer goods which did not help in the growth-promoting role of imports. In order to meet the pressing need, most of the SEACEN countries placed emphasis on agricultural diversification and industrialization through non-traditional and manufactured export production. This section briefly reviews the export trade policy environment in the SEACEN countries.

With a view to promoting the non-traditional export (non-oil/gas), **Indonesia** initiated the outward-looking policy through financial facilities for the exporters in 1982. Since Indonesian exports relied heavily on oil/gas and traditional commodities, in the mid-1980s, it shifted its trade policy regime from the use of quantitative restrictions to the use

1. Myanmar did not participate in this collaborative project; therefore in what follows, 'SEACEN' refers to the above nine member countries.

of tariffs. In the meantime, it also acceded to the GATT code on subsidies and countervailing duties. Thus, from an inward-oriented trade policy, Indonesia has shifted its attention to export promotion with a view to upgrading industrial efficiency and international competitiveness and in the process, minimize the inefficiencies of import substitution.

In the early 1960s, **Korea** introduced various incentives in the areas of financing, taxation and tariffs with a view to promoting exports. In addition, the monthly sessions of the Expanded Meeting for Export Promotion were held to identify the obstacles to export expansion and to provide workable solutions. In the mid-1970s, Korea introduced the Japanese type of specialized general trading companies to overcome the problem of inefficiency of small-scale individual sales techniques in the international markets. It also reconstituted the "Expanded Meeting of the Trade Promotion Committee" including trade experts and policy-makers in order to look into the import policy as well. The merit medals for the best performer in export trade exerted an immense psychological impact on Korean traders. As such, the foreign trade policy of Korea can be considered as a combination of export promotion and import management, even though more emphasis is given to export promotion as the engine of growth.

Malaysia used to depend on only a few commodities exports, namely rubber and tin prior to 1970s. However, it introduced the basic strategy of industrialization in the 1960s, placing emphasis on import substitution. Throughout the 1970s and 1980s, Malaysia aggressively pursued the outward-oriented strategy with a generous incentive system through the Investment Incentive Act of 1968. As a result, the domestic market began to show signs of saturation after a rapid industrialization from 1970 onwards. During the 1980s, a number of reforms and structural changes were undertaken in order to develop capital goods. They have undertaken heavy industrial projects as well as medium- and long-term policy strategies to spur an outward-oriented manufacturing growth.

Faced with declining trend of the major traditional products such as rice and forest products over the time period due mainly to population growth and deforestation as well as the lack of light manufactured products to this day, **Nepal** had to rely for a long time on India for her international trade. However, from 1980 onwards,

Nepal has expanded the third markets especially for export trade. The Nepalese trade policy includes both import substitution and export promotion as basic policy framework. However, due consideration is given to export trade as a way of expanding manufactured products with the introduction of a number of incentives and facilities. As a result, carpets, garments and handicrafts have been developed substantially as manufactured products.

The preferential trade with the United States in the 1950s and the import control and tariff protection system of the 1960s hampered industrial growth in the **Philippines** mainly because the industries were heavily dependent on imported materials and equipment. Similarly, the martial law regime of the 1970s held back a more rapid export expansion as it maintained a protectionist and inward-looking trade and industrial development strategy. Thus, the Philippines lagged behind in its export promotion activities.

Singapore has remained a virtual free port where trade liberalization programs were irrelevant because it has no trade and commercial restrictions. Free trade was believed to lead a long-term economic growth and the main focus then was to develop Singapore into an international trading center.

Together with the liberalization scheme of 1977, **Sri Lanka** has initiated various export promotion policies with a view to expanding the export base and diversifying export products and markets. However, in the face of social unrest and macroeconomic instability, it sought the market diversification benefit, rather than enlarge the manufactured export base.

In spite of the contrasting policy regime to export promotion, the **ROC-Taipei** has maintained an impressive growth in major sectors. The ROC-Taipei adopted import substitution strategy to control foreign exchange expenditure and develop domestic industry. However, when ROC's domestic market became saturated, the policy shifted in favor of export expansion with a view to further developing its industry and trade. Since the mid-1980s, the ROC-Taipei has liberalized and reformed its past experiment to overcome the rising trend of protectionism and stiff competition in the global markets. However, a balanced development of foreign trade remains the basic guideline of the trade policy.

In **Thailand**, the government turned to emphasize on manufactured export promotion policies especially in the Third Development Plan (1972-1976), with the confidence that exportation would be a major impetus in the expansion of production and national income. Accordingly, various incentives introduced for the promotion of exports included import duty/tax refunds, export credit, and the establishment of bonded factories, EPZ and the Board of Investment. The weak points of each export promotion policy have been revised and new appropriate measures have been introduced in order to promote the manufacturing sector as an engine of growth.

Despite the heterogeneous nature of their infrastructural setting and economic structure, as well as having different trade strategies and levels of industrialization, the SEACEN countries as a group initiated the export promotion programs or a balanced development of export/import either in the early 1970s or in 1980s. Evidently, they have further re-embarked on the liberalization exercise since the mid-1980s, placing emphasis this time on their competitiveness in export trade.

2.2 Contribution of Export to the Economy

The growth-promoting role of exports can be considered in several dimensions. Since exports are a component of national income, they can contribute directly to the national income. Similarly, exports can contribute to the economy through their capacity to break import bottlenecks if there is a foreign reserve constraint in the economy. Likewise, exports have a role of promoting backward integration to help in turn promote price stability and exchange rate stability. Finally, exports can also contribute to the economy by way of generating greater employment opportunities and better income distribution. It is not surprising then that most of the SEACEN countries are now placing emphasis on specialization along the production of manufactured exports as a possible development route to industrialization.

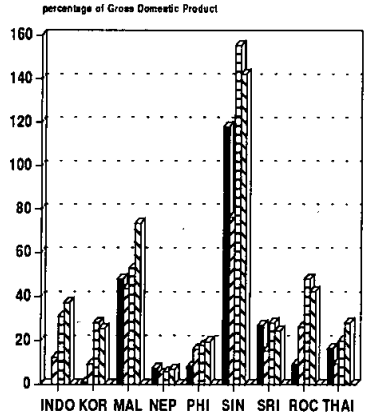
The degree of openness of an economy is measured in terms of the sum of exports and imports as ratio of either GNP or GDP while the ratio of exports to GDP can be used as a yardstick to measure the export-dependency ratio. Nepal and the Philippines have a very low (less than 20 percent) exports-dependency ratio followed by Korea, Sri Lanka and Thailand with a relatively greater degree of openness (24-28 percent) in their economies by the end of 1991. The degree of

exports-dependency ratio is very high (37-42 percent) in the economy of Indonesia and the ROC-Taipei followed by Malaysia where the export to GDP ratio was 44 percent in 1970 and reached more than 73 percent by the end of 1991. Among the SEACEN countries, Singapore as an entrepot trading centre is virtually the most open economy where even the non-oil domestic exports to GDP ratio is about 1.4:1. But because of the rapid growth in exports in the 1970s, the exports-dependency ratio was moderately higher in 1980 than in 1991 as in the cases of Korea, Singapore, Sri Lanka and the ROC-Taipei (see Chart 1.1).

As noted above, most of the SEACEN countries have been successful in maintaining a higher share of exports in GDP over the last two decades. Similarly, a look at the manufacturing exports as a percentage of total exports reveals interesting inter-country variations for the same period. Chart 1.2 shows that Korea and the ROC-Taipei recorded more than three-fourths of the total merchandise exports as manufactured exports as early as 1970 which further increased to about 90 percent by the end of 1991, followed by Singapore with a relatively smaller share of manufactured exports to total exports (28-63 percent) for the same period. But it is equally important to note that the share of manufactured exports to the total merchandise exports, as in the case of Singapore, refers to non-oil domestic exports due mainly to their higher value-added contribution to GDP. Nonetheless, all the SEACEN countries have significantly improved their manufacturing exports proportions during the 1980s with the exception of Indonesia where the non-oil/gas exports are still very low (less than 40 percent).

While exports can contribute to the economy by breaking import bottlenecks, it is also important to maintain a balanced current account too. Chart 1.3 shows that export/import ratios for the selected sample years are highly encouraging for Indonesia, Malaysia and the ROC-Taipei, whereas the trend has shown an improvement in the case of Singapore since the mid-1980s. Nepal, the Philippines and Sri Lanka have been facing difficulties managing the merchandise trade balance; and, hence, the overall current account deficits. Korea and Thailand are also facing the problem of marginal deficits. Trade in services has been recognized as an important part of the current account in the most recent years. Thus, Korea, the Philippines and Thailand have maintained a surplus in their non-factor services trade. Among the SEACEN countries, Singapore has maintained an impressive growth in services sector and hence, the largest surplus in trade in services. In sum, most of the SEACEN countries have still much more to go in the promotion of exports which should

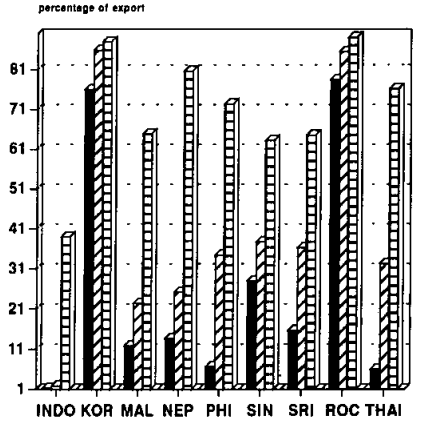
CHART 1.1: EXPORT AS PERCENTAGE OF GROSS DOMESTIC PRODUCT



1960		0.9	47.9	7.4	8.5	117.9	26.9	9.5	16.4
1970	12.5	9.4	43.6	4.9	16.2	76.3	15.4	26.2	9.7
1980	30.8	28	52.8	5.9	17.8	155.3	27.9	47.9	20.1
1991	37.2	25.4	73.4	7	19.5	142.1	24.3	42.3	28

1960 1970 1980 1991

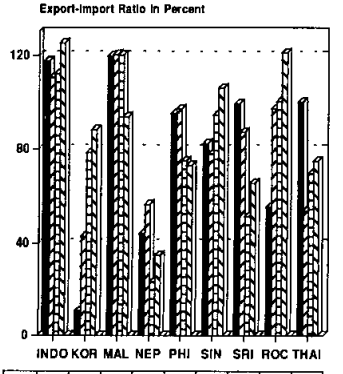
CHART 1.2: MANUFACTURING EXPORT AS PERCENTAGE OF TOTAL EXPORT



1970	1.4	76	11.9	13.7	6.8	28	15.7	78.5	6.1
1980	1.9	85.9	22.4	25.2	34.5	37.8	36.3	85.6	32.3
1991	39	88.1	64.9	80.7	72.4	63.3	64.6	89.2	76.2

1970 1980 1991

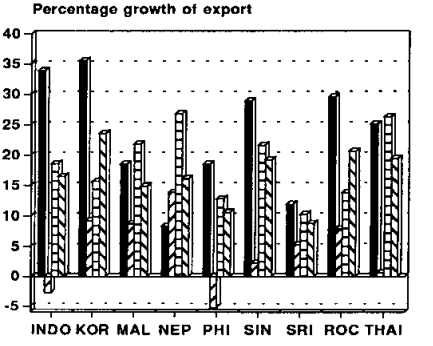
CHART 1.3: EXPORT-IMPORT RATIO



1960	117.6	10.8	119.8	44.1	95.2	82.4	99.4	55.2	100
1970	110.6	42.9	120.4	56.4	97	78	87.2	97.2	53.8
1980	112.1	78.5	120.1	23.5	75	94.5	51.3	100.4	69.5
1991	125.3	88.2	93.7	34.8	73	106.1	65.5	121.2	74.9

1960 1970 1980 1991

CHART 1.4: AVERAGE EXPORT GROWTH IN PERCENTAGE



1970-80	33.9	35.6	18.5	8.4	18.5	28.9	11.9	29.6	25.1
1981-85	-2.7	9.3	8.8	13.9	-5.2	2.3	5.3	7.9	0.6
1986-91	18.6	15.7	21.8	26.8	12.8	21.6	10.3	13.8	26.3
1970-91	16.5	23.6	14.9	16.1	10.6	19.2	8.8	20.6	19.4

1970-80 1981-85 1986-91 1970-91

Source: Appendix 1.1

be at least sufficient to cover the imports and hence manage a non-deficit current account. Nevertheless, a significant growth in the manufacturing sector and hence the level of exports has helped the SEACEN economies by generating greater employment opportunities and better income distribution.

2.3 Growth Trend and Changing Patterns of Exports

Some of the SEACEN countries had started export promotion measures as early as the 1960s. But, it was the first oil crisis which led most of the SEACEN countries to restructure their economies and exports as well. Despite the oil crisis, there were high inflation and volatile exchange rates during the 1970s, though most of the SEACEN countries had maintained spectacular growth in exports and imports. Chart 1.4 and Appendix 1.1 show that the average annual growth of exports in the 1970s was very high in the cases of Indonesia (34 percent), Korea (36 percent), Singapore (29 percent), the ROC-Taipei (30 percent) and Thailand (25 percent) followed by a similar or a slightly lower rate of growth in imports. With the exception of Nepal (8 percent) and Sri Lanka (12 percent) during the 1970's, Malaysia (19 percent) and the Philippines (19 percent) also saw a fairly high growth rate both in exports and imports.

Because of the prolonged recession in the industrial countries in the early 1980s and also the decline in economic activity among the SEACEN countries, there was a sharp downturn in export and import growth in the region for the first half of the 1980s. The average annual export growth for the period was even negative in the cases of Indonesia (-3 percent) and the Philippines (-5 percent) followed by a similar trend in import growth. Similarly, the import growth was also negative in Singapore (-1 percent), the ROC-Taipei (-11 percent) and Thailand (-2 percent). Moreover, a sharp decline in the oil and non-oil commodities prices in the international markets led to huge deficits in most of the SEACEN countries' current accounts in the first half of 1980s. But because of the structural reforms in general and the financial reforms in particular, almost all of the SEACEN countries have been able to restore their export and import growth in the second half of 1980s. A look at the overall period reveals that the average annual growth of exports was high in Korea (24 percent), Singapore (19 percent), the ROC-Taipei (21 percent) and Thailand (20 percent), followed by a significant growth (15-17 percent) in Indonesia, Malaysia and Nepal (Appendix 1.1). This overall average annual growth

of export was slightly lower (9-11 percent) in the Philippines and Sri Lanka.

Table 1.1 shows the share of 0-9 SITC commodity groups in the total exports. As mentioned earlier, some of the SEACEN countries especially Korea and the ROC-Taipei maintained a high share of manufactured sector as early as 1970 while Indonesia, Malaysia, the Philippines and Singapore were heavily dependent either on mineral fuels or on raw materials at that time. The overdependence on food and live animals was recorded in the cases of Nepal, Sri Lanka and Thailand for the year 1970. In 1980, there was a moderate progressive shift in exports from traditional to non-traditional products; while in 1991, almost all the SEACEN countries maintained a dominant presence of manufactured exports in their total exports. A similar picture can be observed from Table 1.2. With the exception of Korea and the ROC-Taipei, all the SEACEN countries showed a dominant role for a few selected principal commodities in their total exports in 1970; while in most countries' cases, they came down dramatically to a negligible share by the end of 1991.

However, it is also important to mention that all the SEACEN countries are not exporting similar manufactured products. For example, Nepal and Sri Lanka with a low industrial base have expanded their manufactured exports through ready-made garments, carpets and tea processing while Indonesia has still a low record of non-oil/gas exports. It is in the Philippines where garments and electronic products play a predominant role in manufactured exports. Similarly, textiles, integrated circuits, jewellery, canned fish and footwear are the major manufactured exports from Thailand. Among the SEACEN countries, Korea, Malaysia, Singapore and the ROC-Taipei have been generally successful in exporting heavy industries and/or high-tech products.

Looking at SEACEN imports by commodity group, one realizes that from the very beginning, almost all the SEACEN countries have been importing manufactured goods whether they have an early history of industrialization or not (see Table 1.3). From the composition of imports, it is hard to conclude anything regarding the growth-promoting role of imports. But because of the high content of imported materials in exports, the value-added contribution of such imports and the increasing trend of capital and intermediary goods, one can say that exports or their growth-promoting stimulus to imports is obvious since the manufacturing exports have gained ground.

Table 1.1

EXPORTS BY 0-9 SITC SECTION

Country	Exports in	1970 (% Share of the Total)										Exports in	1980 (% Share of the Total)										Exports in	1991 (% Share of the Total)									
	US$ M.	0	1	2	3	4	5	6	7	8	9	US$ M.	0	1	2	3	4	5	6	7	8	9	US$ M.	0	1	2	3	4	5	6	7	8	9
Indonesia	1173	11.1	0.5	47.0	31.2	3.3	0.4	1.0	0.4	-	5.1	21909	5.9	0.3	16.3	71.9	1.3	0.4	2.8	0.5	0.4	0.2	29142	8.7	0.5	8.1	38.3	1.9	2.9	22.3	2.3	14.4	0.6
Korea	835	7.9	1.7	12.0	1.1	-	1.3	26.5	7.3	42.2	-	17505	6.6	0.7	2.0	0.3	0.2	4.3	36.7	20.3	29.9	0.3	71870	2.9	0.2	1.4	2.1	-	4.4	22.0	41.6	24.5	0.9
Malaysia	1676	5.5	0.4	53.8	7.1	6.0	0.7	22.9	1.6	0.8	1.2	12941	3.6	0.1	32.3	24.5	11.1	0.6	13.1	11.5	2.6	0.6	34363	3.9	0.2	11.8	15.5	6.6	1.8	7.8	41.1	10.9	0.4
Nepal	42	60.7	0.4	24.6	-	0.4	0.2	9.8	-	3.9	-	135	37.0	0.7	34.8	-	2.3	-	16.3	-	8.9	-	326	15.0	-	3.4	-	0.9	-	54.9	-	25.8	-
Philippines	1062	25.7	1.4	53.9	1.6	9.0	0.6	6.5	0.1	0.8	0.5	5788	24.1	0.6	24.3	0.7	9.8	2.0	9.1	2.3	10.6	16.5	8840	13.9	1.0	5.5	2.4	3.5	3.4	8.0	13.9	16.3	32.1
Singapore	592	5.8	0.6	1.6	56.5	2.7	2.4	9.3	10.8	7.9	0.5	12052	2.3	0.4	0.6	55.0	1.5	2.2	5.1	25.4	7.3	0.1	36222	1.7	0.6	0.7	26.1	0.8	6.4	3.4	52.2	7.7	0.4
Sri Lanka	341	63.2	0.1	2.7	-	6.1	0.1	24.8	0.4	2.6	-	1052	45.3	0.2	19.7	15.3	0.3	3.0	4.3	0.4	10.8	0.7	1988	28.5	0.7	5.1	0.4	0.1	2.5	42.0	3.3	14.7	2.7
ROC-Taipei	2988*	15.5	0.1	2.9	1.3	-	1.6	25.0	20.9	32.6	-	19811	8.6	0.1	1.7	1.5	-	2.5	22.9	24.7	38.0	-	60667	* 4.9	0.1	1.7	0.6	-	3.5	20.6	35.2	33.4	-
Thailand	710	47.1	1.4	28.9	0	0.1	0.2	14.8	0.1	0.4	6.7	6504	44.5	1.0	14.3	0.1	0.2	0.7	22.1	5.7	6.4	4.9	28548	26.5	0.5	5.1	1.0	-	1.9	16.7	24.2	22.6	1.5

* Refers to 1972 and 1988 respectively.

Notes : Code numbers refer to:
0 = Food and live animals; 1 = Beverages and tobacco; 2 = Crude materials, excl. fuels; 3 = Mineral fuels, etc.; 4 = Animal vegetable oil and fats; 5 = Chemicals; 6 = Basic manufactures; 7 = Machines, transport equipment; 8 = Miscellaneous manufactured goods; and, 9 = Unclassified goods.

Sources: Country Chapters; *Key Indicators of Developing Asian and Pacific Countries,* various issues, ADB.

Table 1.2
EXPORTS BY PRINCIPAL COMMODITY
(Percent of Total Merchandise Exports)

	1970	1975	1980	1985	1991
INDONESIA					
Petroleum	40.0	74.8	65.1	57.1	23.8
Rubber	19.3	5.0	4.9	4.3	3.6
Wood	9.1	7.0	7.7	2.1	13.0
Total:	68.4	86.8	77.7	63.5	40.4
KOREA					
Woven fabrics	n/a	9.5	5.7	4.4	6.6
Ships & boats	n/a	2.7	3.5	16.6	5.7
Telecommunication equipment	n/a	1.1	1.4	1.7	2.9
Rubber tires & tubes	n/a	1.6	2.7	1.5	1.3
Total:	n/a	14.9	13.3	24.2	16.5
MALAYSIA					
Rubber	33.4	21.9	16.4	9.5	3.8 *
Palm oil	5.1	14.3	9.3	11.8	5.5
Petroleum	3.9	9.2	23.7	22.6	13.4
Tin	19.6	13.1	8.9	3.0	1.1
Timber	16.5	12.0	14.1	10.2	8.9
Total:	78.5	70.5	72.4	57.1	32.7
NEPAL					
Rice	n/a	31.8	3.1	9.1	-
Jute products	n/a	-	18.3	11.1	4.2
Timber	n/a	13.1	14.8	0.1	-
Total:	n/a	44.9	36.2	20.3	4.2
PHILIPPINES					
Coconut products	20.3	20.1	14.1	7.5	3.4
Copper concentrates	17.0	9.2	9.4	1.8	2.0
Logs & timber	23.9	9.0	7.0	2.8	0.5
Sugar	17.1	25.3	10.8	3.7	1.3
Total:	78.3	63.6	41.3	15.8	7.2
SINGAPORE					
Petroleum products	19.0	26.3	28.5	26.7	16.9
Rubber	14.0	10.2	7.9	3.0	1.1
Telecommunication	3.0	3.1	6.6	2.0	9.7
Total:	36.0	39.6	43.0	31.7	27.7
SRI LANKA					
Tea	55.0	48.7	34.7	34.0	22.1
Rubber	21.8	16.5	14.6	7.3	3.2
Coconut products	11.7	8.4	4.2	6.8	2.1
Total:	88.5	73.6	53.5	48.1	27.4
ROC-TAIPEI					
Outer garments	n/a	8.1	5.9	4.1	2.0
Footwear of plastic	n/a	3.9	4.2	3.2	1.1
Travel goods	n/a	1.6	3.2	2.7	1.1
Thermionic valves, tubes, etc.	n/a	1.5	2.5	2.8	3.7
Total:	n/a	15.1	15.8	12.8	7.9
THAILAND					
Rice	17.0	13.0	14.5	11.7	4.2
Corn	13.3	12.7	5.5	4.0	0.5
Tapioca products	8.3	10.2	11.2	7.7	3.4
Rubber	15.1	7.7	9.3	7.0	3.2
Total:	53.7	43.6	40.5	30.4	11.3

* Refers to 1990.

Sources: *Supplement on Trade Statistics*, Supplement Series No. 4, 1982, IMF.
Key Indicators of Developing Asian and Pacific Countries, various issues, ADB.

Table 1.3
IMPORTS BY COMMODITY GROUP
(Percent of Total Imports)

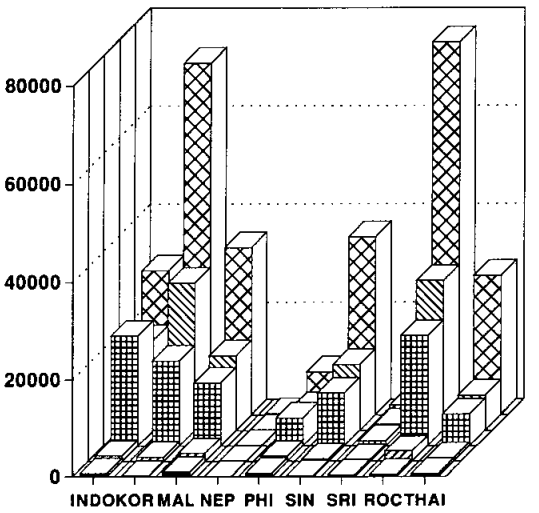
	1970	1975	1980	1985	1991
INDONESIA					
Food, beverages & tobacco	14.7	12.4	12.2	5.1	4.5
Raw materials	1.6	3.5	4.6	6.4	8.5
Fuels	1.6	5.4	16.2	19.5	8.2
Manufactured goods	82.1	78.7	66.7	69.0	78.8
KOREA					
Food, beverages & tobacco	n/a	13.9	8.9	5.1	5.2
Raw materials	n/a	15.4	16.3	12.4	10.9
Fuels	n/a	19.1	29.9	23.6	15.6
Manufactured goods	n/a	51.6	44.9	58.9	68.3
MALAYSIA					
Food, beverages & tobacco	20.5	17.5	11.3	10.4	6.4 *
Raw materials	8.1	6.9	4.6	3.5	3.2
Fuels	12.1	12.0	15.2	10.1	5.1
Manufactured goods	57.8	62.8	68.4	76.0	85.3
NEPAL					
Food, beverages & tobacco	17.2	14.4	12.6	11.1	15.9
Raw materials	4.3	3.5	2.9	5.5	9.9
Fuels	14.6	10.0	11.8	11.9	11.2
Manufactured goods	63.9	72.1	72.7	71.5	63.0
PHILIPPINES					
Food, beverages & tobacco	10.6	10.2	7.5	10.3	8.0
Raw materials	6.4	4.3	4.1	3.1	5.2
Fuels	12.0	21.2	28.4	27.8	14.9
Manufactured goods	70.6	58.2	48.8	41.2	71.9
SINGAPORE					
Food, beverages & tobacco	14.2	9.2	6.2	7.0	6.2
Raw materials	13.2	7.7	8.6	3.4	1.8
Fuels	13.5	24.6	28.7	29.5	14.1
Manufactured goods	57.0	57.1	55.2	60.1	77.9
SRI LANKA					
Food, beverages & tobacco	46.6	50.3	20.2	n/a	22.2
Raw materials	3.0	2.9	1.7	n/a	12.9
Fuels	2.7	16.7	24.3	n/a	13.9
Manufactured goods	47.7	29.5	53.4	n/a	51.0
ROC-TAIPEI					
Food, beverages & tobacco	n/a	10.3	6.9	7.5	4.9 **
Raw materials	n/a	15.6	13.7	13.0	9.9
Fuels	n/a	13.6	25.5	21.5	8.0
Manufactured goods	n/a	60.5	53.9	58.0	77.2
THAILAND					
Food, beverages & tobacco	5.2	4.2	4.3	4.7	5.0
Raw materials	5.3	6.0	5.9	6.3	6.1
Fuels	8.7	21.6	30.4	22.6	9.1
Manufactured goods	76.7	66.1	53.0	66.4	79.8

* Refers to 1990. ** Refers to 1988.

Sources: *Supplement on Trade Statistics*, Supplement Series No. 4, 1982, IMF.
Key Indicators of Developing Asian and Pacific Countries, various issues, ADB.

Charts 1.5.1 to 1.5.4 show the destination of exports by country and region. Taking into account the share of exports of the SEACEN countries, the classification covers four countries and regional groups. As such, from 1970 to 1991, the share of exports to USA and Japan from the SEACEN countries has been substantial at an average of 40.3-percent level. Among the SEACEN countries, Nepal and Sri Lanka had minimal (7.1 percent) exports to USA and Japan during the 1970s. But since the 1980's, they have also increased their exports to USA and Japan to a level of 32.7 percent. The EEC and ASEAN plus NIEs have sharply increased their share in the SEACEN countries' exports over the period. To sum up, the SEACEN countries' exports are increasingly concentrated in the USA, Japan, EEC and ASEAN plus NIEs over the period under study. In other words, such export concentration was less than three-fourths in 1970 and reached more than four-fifths by the end of 1991.

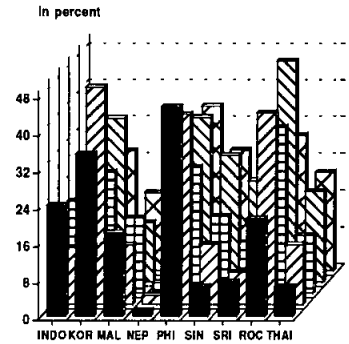
CHART 1.5: EXPORTS IN US$ MILLION



1991	29635	71870	34363	256	8840	36479	1988	76178	28546
1985	18527	30283	15317	153	4629	13508	1290	30726	7138
1980	22609	17505	12941	135	5788	10852	1052	22611	6504
1970	1173	835	1676	42	1062	502	341	2060	710
1965	687	175	971	23	767	236	410	450	623

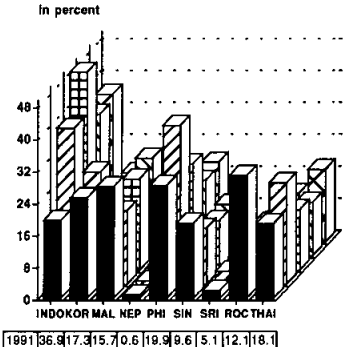
Source: Appendix 1.2

CHART 1.5.1: UNITED STATES OF AMERICA AS AN EXPORT DESTINATION



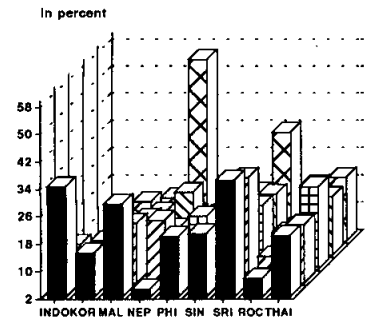
1991	12	25.9	16.9	23.7	35.7	26.1	28.1	29.3	21.3
1985	21.7	35.5	12.9	35.3	35.7	27.5	22	48.1	19.7
1980	20	26.3	16.4	2.4	27.4	16.8	11.1	36.1	12.6
1970	12.5	47.3	13	2	41.4	13.2	7.1	41.7	13.1
1965	24.1	35.2	18.2	1.3	45.5	6.5	7.5	21.3	6.5

CHART 1.5.2: JAPAN AS AN EXPORT DESTINATION



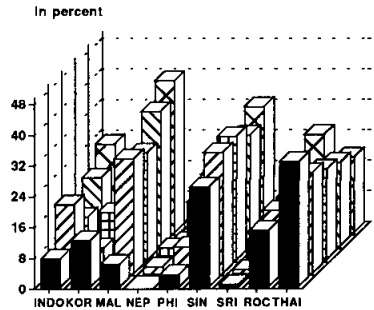
1991	36.9	17.3	15.7	0.6	19.9	9.6	5.1	12.1	18.1
1985	35.4	15	24.4	0.7	18.9	13	5.1	11.3	13.4
1980	49.4	17.4	22.8	1.4	26.5	12.4	3.2	11	15.1
1970	38.9	28	18.3	1	39.6	14	3.3	11.9	25.3
1965	19.5	25.1	27.9	0.9	28.2	18.8	2	30.6	18.6

CHART 1.5.3: EUROPEAN ECONOMIC COMMUNITY AS AN EXPORT DESTINATION



1991	12.8	13.6	14.8	55.4	18.6	16.5	33.9	18.4	20.7
1985	6.2	10.8	14.5	20.4	14	11.4	19.9	9.8	19.1
1980	5.9	15.5	16.9	14	17.5	14.3	20.6	12.8	26
1980	13.3	7.75	19.4	20.3	7.2	13.9	32.8	9.9	19
1965	34.2	14.9	29.1	4.43	19.6	20.5	36.1	7.5	19.9

CHART 1.5.4: ASEAN NATIONS AND NEWLY INDUSTRIALIZED ECONOMIES AS AN EXPORT DESTINATION



1991	23.3	18.9	39.6	2.9	16.4	33	7.9	25.7	19.6
1985	18	10.8	35.3	1.4	18.9	29.1	7.3	14.3	21.9
1980	11.2	12.4	28	3.2	15.1	32.3	4.9	16.3	23.6
1970	17.9	6.7	29.9	1.9	7.1	31.6	1.1	16.4	26.3
1965	7.5	12.1	6		3.3	26	0.7	14.7	32.6

From the above survey of the growth and changing patterns of exports as well as imports, it becomes clear that there is a structural shift in the composition of exports whereas market concentration is still a great concern. During the period under study, the SEACEN countries as a group have been successful in maintaining a spectacular growth in exports and imports except in the first half of the 1980s due to severe economic recession, rising trend of protectionism and downward pressure on commodity prices. Keeping in view the market concentration and, to some extent a similar composition of exports, the SEACEN countries are creating a mutual understanding for and competition in the international market.

2.4 Exports and Growth: Some Empirical Evidence

In addition to the review of growth trend and changing pattern of exports of the SEACEN countries, this section aims to identify empirically the direction of relationship between exports and economic growth. Similarly, an attempt has been made to establish an empirical assessment of the export performance of the SEACEN countries. So far, each SEACEN member country has: (i) a small or limited domestic market; (ii) good track record in export promotion; and, (iii) similar direction of export markets. The focus will be on the demand side of exports assuming the supply side is a function of effective export intervention of the government, i.e., domestic environment.

2.4.1 Causality Test Between Exports and Economic Growth

It is important to be able to determine the causality relationship between exports and economic growth. In the past, numerous studies had been done in determining the direction of causality between exports and economic growth.[2]

In dealing with the export promotion activities of the SEACEN countries, it is important to test the export-led or export-promotion hypotheses. For the present purpose, Granger's causality test seems to be more appropriate as it is bivariate. Granger causality posits the idea that X causes Y, if the coefficients on the lagged X help to predict Y more accurately and vice-versa. Although the study aims to assess the export promotion hypothesis which implies a prior expectation of the

2. See Jung and Marshall (1985), and Dodaro (1991) for an eloquent review of past studies.

direction of causation from export to GDP, the study is open to the idea of the possibility of a two-way relationship between exports and GDP with a view to comparing the direction of causality among the SEACEN countries.

As explained elsewhere, the growth-promoting role of exports is manifold. As such, the direct and indirect contribution of exports to economic growth are obvious. But in the past, no study attempted to separate the component effects of exports to GDP. Therefore, to suppress the component effect since exports are a component of GDP, exports can be subtracted from GDP and the relationship between exports and GDP (less exports) can be established with a view to comparing the component effect and indirect effect. Similarly, to normalize the inflationary effect, both the exports and GDP are used in real terms. That is, exports are deflated by the export price indices (1985=100), and CPI is used as a proxy in the case of Nepal where export prices are not available.[3] For comparison, the data on GDP are also based on 1985 prices. The variables are the growth rates of real exports and real GDP. The annual data used are from 1970 to 1991. The causality tests are performed on two combinations of: (i) growth rates of real exports and real GDP; and, (ii) growth rates of real exports and real GDP (less real exports).

Unlike the traditional regression analysis which shows only the dependence of one variable on the others, the causality test helps to determine which variable is causing the other. Thus, the basic hypothesis here is to test the direction of causality in the following order:

(a) Export to GDP;
(b) GDP to export;
(c) Both way; and,
(d) None.

Based on a simple two-variable model developed by Granger (1969), the following function can be formulated for the estimation of a causal relationship between exports and GDP:

3. See Cooper, S.A. (1988) for a detailed interpretation for the options for the choice of price deflator.

$$Y_t = a_0 + \sum_{i=1}^{m} a_i X_{t-i} + \sum_{j=1}^{n} b_j Y_{t-j} + U_t \quad (1)$$

$$X_t = c_0 + \sum_{i=1}^{r} c_i Y_{t-i} + \sum_{j=1}^{s} d_j X_{t-j} + V_t \quad (2)$$

Where, U_t and V_t are uncorrelated random error terms,
Y_t = Real GDP or real GDP (less real exports) growth,
X_t = Real exports growth,
a, b, c and d are parameters to be estimated.

The null hypotheses are: $\Sigma ai = 0$ and $\Sigma ci = 0$.

Thus, the causality test provides the direction of causal relation or the independent movement of the variables in the following conditions:

(a) Unidirectional causality from X to Y, if $\Sigma ai \neq 0$ and $\Sigma ci = 0$;
(b) Unidirectional causality from Y to X, if $\Sigma ai = 0$ and $\Sigma ci \neq 0$;
(c) Feedback relationship between X and Y, if $\Sigma ai \neq 0$ and $\Sigma ci \neq 0$; and,
(d) Independence is suggested, if Σai and Σci are not statistically significant, i.e., $\Sigma ai = 0$ and $\Sigma ci = 0$.

2.4.2 Unit Root Test

Prior to the estimation of causality, it is necessary to test the stationarity of the selected time series. This is done because the regression equations that relate non-stationary variables can give rise to the so-called spurious regression problem and lead to incorrect statistical inferences (Granger and Newbold, 1974). Therefore, the unit root test with a view to capturing the order of integration of the selected time series, i.e., growth rates of real exports, real GDP and real GDP (less exports), is performed. While doing so, the first step is to determine the stationarity in their level; otherwise, a first difference may be required to achieve stationarity. Tests for unit root are performed on all the selected time series using the augmented Dickey-Fuller (ADF) test. The Campbell and Perron (1991) procedure was used in deciding

the lag lengths followed by a sequential testing procedure of either a constant or a constant and trend.

Results of the ADF tests for unit roots are summarized in Table 1.4. According to the test results, the real GDP growth (RGDPG) series is stationary at the 1-percent level of significance in Indonesia, Korea, Nepal, Singapore, Sri Lanka and ROC-Taipei; while it is stationary at the 5- and 10-percent level of significance respectively in Malaysia, and the Philippines and Thailand. The real export growth (REXG) series is stationary at the 1-percent level of significance in all the SEACEN countries except in Korea where it is stationary at the 5-percent level of significance. Similarly, the real GDP (less export) growth (RGDPLXG) is also stationary at a different level of significance in all the SEACEN countries. To sum up, all the selected time series in all the SEACEN countries are stationary on growth rates; in other words, they are integrated at zero order, i.e., I(0).

Table 1.4

UNIT ROOT TEST RESULTS

	L E V E L							
	RGDPG		REXG		RGDPLXG			
	No. of Lags	Constant No Trend	No. of Lags	Constant No Trend	No. of Lags	Constant No Trend		Constant Trend
Indonesia	0	-4.3340 ***	0	-3.9811 ***	0	-2.6889 *		
Korea	0	-3.8610 ***	2	-3.2397 **	0	-3.5873 **		
Malaysia	0	-3.2359 **	0	-4.0139 ***	1			-4.3470 **
Nepal	0	-5.7326 ***	0	-5.8318 ***	0	-5.7582 ***		
Philippines	0	-1.6679 *	0	-4.1544 ***	1			-3.5584 *
Singapore 1/	1	-4.0118 ***	0	-3.9032 ***	0			-3.5724 *
Sri Lanka	0	-4.4888 ***	0	-6.6808 ***	0	-5.0435 ***		
ROC-Taipei	0	-3.9099 ***	0	-5.0216 ***	0	-3.3040 **		
Thailand	0	-2.6951 *	0	-4.6317 ***	0	-5.1246 ***		

*** Significant at 1-percent level.
** Significant at 5-percent level.
* Significant at 10-percent level.

Notes: RGDPG = Real GDP growth.
REXG = Real export growth.
RGDPLXG = Real GDP (less export) growth.

1/ Refers to non-oil domestic exports.

2.4.3 Cointegration Test

The long-run equilibrium relationship between variables is a core concern in economic theory. As mentioned earlier, a series is integrated of order d, or I(d), if it is stationary after being differenced d times. So an I(0) series is stationary and variables integrated of higher order are non-stationary. Stationarity of a variable implies that: variance and covariances are constant over time, Wong (1993). Before the concept of cointegration was introduced by Granger (1981, 1983), it was a standard practice to include a time trend in the regression or differenced data on the assumption that data are trend or difference-stationary. But this procedure was criticized by Nelson and Plosser (1982) when they proved that most of the macroeconomic series are not trend-stationary, and differencing them results in a loss of long-run information. Now it has become clear that cointegration is useful to determine stationarity out of a linear combination between selected time series which individually may be non-stationary. It is important here to note that cointegration does not necessarily mean that there is no relationship between variables; it only suggests that there is no long-run relationship between the variables which can be improved by some re-specification.

In the literature, there are several test methods for cointegration. The test for cointegration used in this study is the one proposed by Engle and Granger (1987). The first step is to find out whether each selected time series is stationary or not. This can be tested by using a unit root test on each time series. The second step test can be done on the residuals of the level regression estimated using non-stationary variables. If the residuals are stationary, then the non-stationary variables are cointegrated. The cointegration tests are, however, not necessary where the variables are of zero-order integration. In this study, even as the variables are of zero-order integration, we nevertheless pursued a cointegration test. After all, the causality tests are not bound with the cointegration status, if they are stationary on their growth rates. Cointegrating regressions were performed including a constant or a constant and trend. The cointegration test results are summarized in Table 1.5. The test results show that with the exception of Singapore where real GDP and exports as well as real exports and GDP are not cointegrated, all other combinations are cointegrated.

In the Granger Causality Test, the lag length (m, r in equations (1) and (2)) substantially influences the test results. Thus, the selection of

lag length is very important in the causality test. Too many lags may reduce the number of effective observations, while too few lags may affect the size of the test. Among the various criteria that can be used include the popular information criteria of Final Prediction Error (FPE) (Akaike, 1969) and Schwarz Criterion (SC) (Schwarz, 1978) to select the optimal lag length for causality tests. For this, the autoregressive least square estimation was carried out from lag length one to lag length five taking into consideration the smallness of the sample size. But so far as the sample size is concerned, the significance of the test depends very little on the number of observations per se but is rather influenced in an important way by the span of the data, Campbell and Perron (1991).

The selection of optimal lag length was based on the least FPE or SC statistics. Since the lag length based on FPE is normally longer than the lag length based on SC, the lag length used here is based on SC with a view to gaining the number of observations. As an efficient step-wise procedure, firstly, the lag length of the independent variable was determined. And on the condition of the given lag length of the independent variable, the lag length of the dependent variable was determined. The results of the optimal lag length tests are summarized in Appendix 1.3. As mentioned earlier, the empirical analysis of the overview chapter may not be consistent with the results of the country chapters mainly because, among other things, the overview chapter is subject to compliance with unit root and cointegration tests which are essential for the time series data to ensure non-spurious results.

The Granger causality test results are summarized in Table 1.6. As can be seen, a few time series are stationary and/or cointegrated with constant and trend. Due consideration has been given to include trend as an independent variable, but the test results are finally selected on the basis of their significance. According to the results, between the growth rates of real GDP and exports, there is a negative unidirectional causality from GDP to exports in the cases of Korea and Malaysia, whereas it is positive in the case of Thailand. There is a two-way or feedback negative relationship between the growth rate of real GDP and exports in Singapore followed by a positive bidirectional relationship in the case of ROC-Taipei. Based on the 5-percent level of significance, there is no causation from either side between the growth rates of real GDP and exports. In other words, there is an independent movement of the GDP and exports growth in the cases of Indonesia, Nepal, the Philippines and Sri Lanka.. However, with a weak database,

Table 1.5

COINTEGRATION TEST RESULTS

	RGDPG, REXG			REXG, RGDPG		RGDPLXG, REXG			REXG, RGDPLXG		
	No. of Lags	Constant No Trend	Constant Trend	No. of Lags	Constant No Trend	No. of Lags	Constant No Trend	Constant Trend	No. of Lags	Constant No Trend	Constant Trend
Indonesia	0	-4.3181 **		0	-3.9742 **	0	-3.5994 *		0	-5.2370 ***	
Korea	0	-4.0349 **		1	-3.3209 *	0	-3.8145 **		1		-4.0573 *
Malaysia	0	-3.3005 *		0	-3.8947 **	0	-3.4515 *		1	-5.0515 ***	
Nepal	0	-5.8903 ***		0	-6.0550 ***	0	-5.8241 ***		0	-5.9956 ***	
Philippines	1		-3.9207 *	0	-4.3088 **	1		-3.8980 *	0	-4.3406 **	
Singapore 1/		--			--	1		-4.4347 **	0		-4.1315 *
Sri Lanka	0	-4.6715 ***		0	-6.9364 ***	0	-4.7022 ***		0	-6.1106 ***	
ROC-Taipei	0	-3.7931 **		0	-4.7476 ***	1	-3.4170 *		0	-4.4297 **	
Thailand	0	-3.4195 *		0	-5.7800 ***	0	-3.7292 *		0	-3.4002 *	

*** Significant at 1-percent level.
** Significant at 5-percent level.
* Significant at 10-percent level.

1/ Refers to non-oil domestic exports.

Table 1.6
GRANGER CAUSALITY TEST RESULTS

	No. of Lags	RGDPC ==> REXC F-Value/(Prob.)	No. of Lags	REXC ==> RGDPC F-Value/(Prob.)	No. of Lags	RGDPLXC ==> REXC F-Value/(Prob.)	No. of Lags	REXC ==> RGDPLXC F-Value/(Prob.)
Indonesia	1/1	1.7984	1/1	0.0396	1/1	5.1906 * (-)	1/1	3.9553 * (-)
		(0.1975)		(0.9612)		(0.0183)		(0.0402)
Korea	1/2	4.3160 * (-)	3/1	0.8180	1/3	0.7466	3/1	0.3099
		(0.0347)		(0.5379)		(0.4948)		(0.8659)
Malaysia	1/1	4.1882 * (-)	1/1	0.7483	1/1	18.0300 ** (-)	1/1	12.0300 ** (-)
		(0.0345)		(0.4890)		(0.0001)		(0.0006)
Nepal	2/1	1.9947	1/1	3.1307	1/1	0.4994	1/1	0.6174
		(0.1611)		(0.0712)		(0.6160)		(0.5517)
Philippines	1/1	2.3183	1/2	2.3318	1/1	0.0475	1/1	0.3501
		(0.1306)		(0.1336)		(0.9538)		(0.7099)
Singapore	2/5	10.5670 ** (-)	1/5	10.4830 ** (-)	1/3	7.0545 ** (-)	1/1	2.8797
		(0.0054)		(0.0058)		(0.0094)		(0.0855)
Sri Lanka	1/2	0.9240	2/1	0.1674	1/2	1.9675	2/1	0.6549
		(0.4198)		(0.9166)		(0.1766)		(0.5931)
ROC-Taipei	1/2	26.0150 ** (+)	1/4	18.0870 ** (-)	1/1	1.2876	1/5	11.3100 ** (+)
		(0.0000)		(0.0005)		(0.3030)		(0.0047)
Thailand	1/3	5.5704 * (+)	1/1	2.1901	3/2	2.4359	1/2	6.6062 ** (+)
		(0.0194)		(0.1443)		(0.1094)		(0.0095)

** Significant at 1-percent level.

* Significant at 5-percent level.

Notes: (1) Figures in parentheses are probability values which show the chances for acceptance of null hypotheses, i.e., A is not
----- Granger-caused by B.

(2) + or - sign in parentheses indicates the sign of the sum of the coefficients of the significant (up to 5-% level) causal variables.

(3) A ==> B = Causality from A to B.

(4) Lag lengths of dependent variable are decided on the given lag lengths of independent variable.

a more liberal attitude to the level of significance is also equally necessary to understand the structural inefficiencies.

After suppressing the component effect of exports, there is unidirectional negative causality from GDP (less exports) to exports in the case of Singapore followed by a unidirectional positive causality from exports to GDP (less exports) in the cases of ROC-Taipei and Thailand. It is interesting to observe that after suppressing the component effect, in the case of Indonesia, there arose a two-way or feedback negative relationship between the growth rates of real GDP (less exports) and exports, which was not significant either way with the component effect. Similarly, after netting the component effect, there is a two-way or feedback negative relationship between the growth rates of real GDP (less exports) and exports in the case of Malaysia. Except in Korea where the share of exports to GDP is very low (25 percent), and in Singapore where even the non-oil domestic export alone is greater than GDP, the direction of causality is more significant and clear after relaxing the component effect. With the exception of Indonesia, the causal relation is still inconclusive between the growth rates of GDP (less exports) and exports in the cases of Nepal, the Philippines and Sri Lanka up to 5-percent level of significance. The direction of causality can be seen more clearly in Table 1.7.

According to the direction of causality, our results are either improved or at least equivalent to Jung and Marshal (1985) and Oskooee, et.al. (1991). It is, however, hard to make inferences from the test results to support the World Bank classification of trade orientation (1987), but there are ample evidences to support the view that the higher the per capita income and level of development, the greater the level of significance in explaining the relationship between exports and economic growth. In sum, the export-led growth hypotheses or the correlations between exports and output growth found in the previous studies seem to be spurious.

2.5 Demand for Exports

In addition to an empirical test of the export-led growth hypothesis, this section will assess empirically the export performance of the SEACEN countries by using the key variables which are, both in theory and practice, believed to determine the real demand for exports. As such, the competitiveness of the exporters of the SEACEN countries

Table 1.7

DIRECTION OF CAUSALITY

	RGDPG --> <-- REXG	RGDPLXG --> <-- REXG	RGDPG --> <-- REXG 1/	RGDPG --> <-- REXG 2/
Indonesia	n	- **	n	- **
	n	- **	+ **	+ **
Korea	- **	n	- *	+ *
	n	n	n	+ *
Malaysia	- **	- ***		
	n	- ***		
Nepal	n	n		
	n	n		
Philippine	n	n	n	n
	n	n	n	n
Singapore	- ***	- ***		
	- ***	n		
Sri Lanka	n	n	n	n
	n	n	n	n
ROC-Taipei	+ ***	n	+ *	n
	+ ***	+ ***	n	+ *
Thailand	+ **	n	+ **	+ **
	n	+ ***	n	+ *

1/ Results from Jung and Marshal (1985).
2/ Results from Oskooee, et.al. (1991).
*** Significant at 1-percent level.
** Significant at 5-percent level.
* Significant at 10-percent level.
n Indicates no causality.
For the period coverage, see the respective study.

is proxied by the respective SEACEN country's real effective exchange rates (REER). An increase in the real effective exchange rate means a real appreciation of the domestic currency which makes the exportable items more costly. In other words, if exports are costly, then there will be less demand for such exports, causing a fall in the export level, and the reverse is true if the real exhange rate declines/depreciates. Similarly, the world demand for merchandise exports from the SEACEN countries is represented by the growth in real GDP of major importing partners of the SEACEN countries. Thus, an increase in the importing countries' GDP is expected to lead to a positive impact on the demand for real exports from the SEACEN countries and vice-versa. For this, the export-weighted real GDP index of the export trade partners is used to measure the income effect on real export demand.

Among the various weighted indices, the bilateral export-weighted index seems to be a more appropriate measure in calculating the real effective exchange rate, considering the focus of the study on export trade. The same method is used in calculating the export-weighted real GDP of the export trade partners. The influence of import price or the impact of exchange rate on imported materials to be used in export production is assumed as a subject of adjustment by government intervention. Similarly, among the various price deflators in estimating real effective exchange rate indices, the consumer price index (CPI) is preferred because it is easily available and comparable for all the SEACEN member countries and their trade partners as well as it closely follows the GDP deflator. So far, the study is limited to looking at the aggregate export function rather than at the commodity level. The third- market competition is ignored on the assumption that each member country conducts its export business based on its existing labor skills, technological know-how and comparative advantage.

Nevertheless, the real effective exchange rate measures the changes in the cost of a country's exports to foreign countries. The study follows the geometric averaging, which is widely preferred to the arithmetic averaging, mainly because it does not suffer from the problems of time reversibility and weight bias. The prices of domestic currency with each partner country's currency in terms of US dollar weighted by export trade partners' share in total exports of each SEACEN member country are used taking into consideration the merits of appreciation and depreciation.

Altogether, the top fifteen export trade partners are selected based on their share in total exports during the base year. For this study, 1985 is selected as base year on account of the availability of data on real GDP, export price indices, CPI and the other variables. The total exports and percentage coverage for the base year are summarized in Appendix 1.4. Thus, the real effective exchange rate and export-weighted real GDP used in this study are based on the export weights of the top fifteen export partners. The nominal and real effective exchange rates and the export-weighted real GDP index are summarized, respectively, in Appendices 1.6 and 1.7. As mentioned earlier, the study is constrained in making a comparable analysis with other studies or even with the country chapters prepared by the country researchers where the stationarity and cointegration tests are ignored. Similarly, the study is also constrained in comparing countries with different trade weights and base year. But it is important to note that our calculation of the real effective exchange rate shows a similar trend with that of the Asian Development Bank (ADB).

Empirical attempts to capture the adjustment of export demand toward a desired equilibrium have often been employed within the framework of partial adjustment mechanism mainly because the behavior of export prices, income level of importing countries, etc., may prevent concerned parties from immediately adjusting their responses to desired levels. In other words, assuming the disequilibrium framework, the export demand normally adjusts to the difference between the desired and actual export demand in the previous period. However, in the recent past, this approach has been severely criticized especially when Granger (1983, 1987) introduced the concept of cointegration, and hence, the error correction model (ECM). The error correction specification can be thought as a more general, intertemporal version of partial adjustment in which expectations are based on available information (Nickell, 1985). Prior to these techniques, there was a practice to include the differences and the lagged levels of the variables in the same equation without the test of stationarity on the level of lagged variables to measure the short- and long-run relationships respectively. Since there is the presence of a lagged dependent variable in the estimation of an error correction model, we used the Durbin *m*-test which consists of calculating the least squares residuals and applying the least squares method to the error term as a dependent as well as lagged dependent variable in order to test the auto-regression. The Durbin *m*-test is intuitively superior to that of

that Durbin *h*-test which generally suffers from indeterminacy (Kmenta, 1986). As Table Appendix 1.5 indicates, the outcome of the Durbin *m*-test shows no autocorrelation.

Against this background, we attempted to estimate the error correction model with a view to capturing the short-run ability of competitiveness (REER) and export-weighted GDP (XWGDP) of major trade partners to explain the export demand function of the SEACEN countries. Prior to this, if a cointegrating relationship, i.e., the long-run relationship among the selected variables, exists, then the error correction model can be legitimately used. Therefore, the error correction model was estimated for those countries, namely, Nepal, the Philippines, Sri Lanka and ROC-Taipei where there was a cointegrating relationship among the selected variables. The results are summarized in Appendix 1.5. On the basis of these findings, one can safely say that the short-run predictability of the demand for export from the SEACEN countries is poor which may be due to the smallness of the sample size. In other words, a short-run real export demand model cannot be fitted to the levels of the given variables without re-specifying the model with additional variables and/or data periods.

Finally, in view of the nature of the study, i.e., comparative analysis, we estimated the simple function with a view to measuring the price and income effect on real exports demand from the respective SEACEN countries through the level of coefficients on real effective exchange rate and the export-weighted GDP of the importing countries. Dummy variables are used to capture the implication of policy changes wherever necessary.

The world demand for real exports from the individual SEACEN member country can be specified in log-linear form as follows:

$$LnREX_t = a + b\ LnREER_t + c\ LnXWGDP_t + Ut;\ b<o,\ c>o.$$

where, LnREX = The quantity of real export demand from trade partner in log,

LnLREER[3] = Real effective exchange rate in log,

LnLXWGDP[4] = Export-weighted real GDP of trade partners in log,

U is a random error term.

As mentioned above, the unit root and cointegration tests were performed with a view to ensuring the stationarity of the selected variables as well as to determine stationarity out of a linear combination among selected variables which individually may be non-stationary.

2.5.1 Unit Root Test

The unit root test results are summarized in Table 1.8. Tests for unit roots were performed on univariate time series on log forms with constant, and constant and trend. According to the test results, all variables used in the real exports demand functions are stationary on level in log forms in the cases of Korea, Sri Lanka and ROC-Taipei, while almost all the variables are stationary either on level in log or on log first-differences for the rest of the SEACEN countries.

---

3. The REER is calculated as follows:

$$REER_1 = \prod_{i=1}^{m} (eli\ pd1/pfli)^{wi}$$

Where, π = Product of elements eli times domestic/foreign consumer prices to the power export-weight,
eli = Nominal exchange rates in foreign currencies per unit of domestic currency during period 1. That is, the domestic exchange rate in terms of US dollars divided by the exchange rates of importing partners in terms of US dollars,
pd1 = Domestic consumer price index,
pf1i = Consumer price indices of foreign countries,
wi = Bilateral export trade weights,

$$\text{or, } wi = TEi / \sum_{i=1}^{m} TEi$$

where, TEi = Shares of each top fifteen export partners in total exports in the base year.

4. The XWGDP is calculated as follows:

$$XWGDPI = \prod_{i=1}^{m} (eli)\ wi$$

Where, π = Product of elements eli to the power export weight,
eli = Real GDP index of export trade partners during period 1,
wi = Bilateral export trade weights,

$$\text{or, } wi = TEi / \sum_{i=1}^{m} TEi$$

where, TEi = Shares of each top fifteen export partners in total exports in the base year.

Table 1.8
UNIT ROOT TEST RESULTS

	LEVEL IN LOG									LOG FIRST DIFFERENCE					
	LnREX			LnREER			LnXWGDP			Δ LnREX		Δ LnREER		Δ LnXWGDP	
	No.of Lags	Constant No Trend	Constant Trend	No.of Lags	Constant No Trend	Constant Trend	No.of Lags	Constant No Trend	Constant Trend	No.of Lags	Constant No Trend	No.of Lags	Constant No Trend	No.of Lags	Constant No Trend
Indonesia		--			--		1		-4.9998 ***	0	-4.0215 ***	0	-2.9118 *		--
Korea	0	-5.0453 ***		0	-2.6794 *		1		-3.9616 **		--		--		--
Malaysia		--			--		1		-4.0971 **	0	-3.7302 **	3	-2.7882 *		--
Nepal		--			--			--		0	-5.9548 ***	0	-3.8824 ***	0	-4.3386 ***
Philippines		--			--		1		-4.4582 **	0	-4.1496 ***	0	-5.1666 ***		--
Singapore		--		1	-4.8908 ***		1		-3.6148 *	0	-3.9116 ***		--		--
Sri Lanka	0		-3.3166 *	5	-2.7833 *		1		-3.8298 **		--		--		--
ROC-Taipei	5	-2.7635 *		3		-3.9825 **	1		-3.9299 **		--		--		--
Thailand		--			--			--		0	-4.6510 ***	0	-3.4027 **	1	-4.3386 ***

*** Significant at 1-percent level.
** Significant at 5-percent level.
* Significant at 10-percent level.
Notes: LnREX = Real exports in log.
---- LnREER = Real effective exchange rate in log.
LnXWGDP = Export-weighted real GDP of major export trade partners in log.
REER and XWGDP are also free from unit root on first-differences in the case of Malaysia.

2.5.2 Cointegration Test

Cointegration tests were also performed on the levels of selected variables to determine whether they are stationary on level in log or on log first-differences. If some variables are stationary on level in log and others are stationary on log first-differences, the cointegration tests are performed on level in log assuming that if a zero-order stationary variable is tested on difference term, it gives a stationary result. As such, the significant cointegration test results are reported in Table 1.9. The cointegration tests were performed with constant, or with constant and trend. The lag length in the cointegration tests was also determined following Campbell and Perron (ibid.). According to the results, the variables are cointegrated on level only in the cases of Nepal, the Philippines, Sri Lanka and ROC-Taipei, and for the rest of the SEACEN countries, the variables are not cointegrated.

Table 1.9

COINTEGRATION TEST RESULTS

Combination	Nepal	Philippines	Sri Lanka	ROC-Taipei
LnREX, LnREER, LnXWGDP (Constant, No Trend)	-4.4692*	-7.6094***	-4.3190**	-4.0154*

*** Significant at 1-percent level.
** Significant at 5-percent level.
* Significant at 10-percent level.

As discussed above, not one of the selected time series was stationary on level in log. The level non-stationary time series of the different variables are not cointegrated. But as a standard practice in testing for stationarity and cointegration, we followed the following process. First, the stationarity of the univariate series was checked by unit root test and hence, if the variables were integrated individually at zero order, i.e., I(0), regressions were run on a linear combination of those variables. Second, if some of the variables were integrated of order-zero, and the remaining variables were integrated of order-one, i.e., I(1), cointegration tests were performed on level assuming that the

variables which are stationary at zero order will likewise be stationary on first-differences. Third, regressions were run on level, if the variables were found stationary individually at zero order, or if all the variables in the model were cointegrated. And last, regressions were run at the highest order of integration, in other words at their first-differences, where both of the above conditions were not met. The regression results are summarized in Table 1.10.

The regressions were estimated on level in the cases of Korea, Nepal, the Philippines, Sri Lanka and ROC-Taipei, while the estimated regressions are on first-differences for the rest of the SEACEN countries. Dummy variables are used to capture the policy change especially in the case of Sri Lanka where there was a structural policy shift under the liberalization program in 1977. Similarly, dummy variables are used to capture the policy effect of exchange rate change from fixed to flexible regime in the cases of Indonesia (1982), Korea (1980), Thailand (1978) and ROC-Taipei (1979). So in these country cases, dummy variables are used as:

$$D = \begin{matrix} 1 & \text{under the new policy regime} \\ 0 & \text{otherwise} \end{matrix}$$

In those country cases where some of the variables were trend-stationary on level or on first differences, the trend variable was used as an independent variable in the regression equation. However, the results were even less encouraging, with the exception of Thailand. Finally, except in the case of Thailand, the trend variable was dropped to attain a good fit of the model.

In order to make the interpretation more consistent, the member countries are classified into two groups based on the estimated regression equation on level and first-differences. According to the regression results, except in the cases of the Philippines and Sri Lanka where the real effective exchange rate shows a positive but statistically insignificant relation with the real export demand, the real effective exchange rate is highly significant with the expected negative direction of relationship with the real export demand in the cases of Nepal and ROC-Taipei, followed by Korea with a negative but statistically insignificant direction of relationship (see Table 1.10).

In other words, the real effective exchange rate failed to explain the real export demand for the Philippines and Sri Lanka where the

Table 1.10
REGRESSION RESULTS
(LnREX = LnREER, LnXWGDP, DV/Trend)

	Dependent Variable	Constant	LnREER	ΔLnREER	LnXWGDP	ΔLnXWGDP	DV	Trend	R2	DW	F-Value	SE
Indonesia +#	^LnREX	-0.1451		-1.0026		5.6443	0.0039		78.73	2.2456	11.1051	0.0842
		(-1.9363)		(-5.7071)***		(3.4639)***	(0.0996)				(0.0005)	
Korea #	LnREX	1.4141	-0.3407		2.2981		-0.0618		98.21	1.3092	206.2909	0.1196
		(0.2851)	(-1.0248)		(2.5425)***		(-0.5822)				(0.0000)	
Malaysia +#	^LnREX	-0.0309		-0.0058		0.0258	--		40.56	1.8114	3.4118	0.0871
		(-0.6590)		(-1.3309)*		(2.2806)**					(0.0451)	
Nepal	LnREX	23.0804	-2.7892		-0.5423		--		72.37	2.0389	24.8786	0.1818
		(3.7505)***	(-3.3508)***		(-1.0201)						(0.0000)	
Philippines	LnREX	2.1977	0.1342		1.8986		--		96.39	1.6735	151.2108	0.0898
		(1.0701)	(0.4599)		(8.1827)***						(0.0000)	
Singapore +#	^LnREX	-0.1279		-0.5426		6.1018	--		70.70	2.0399	12.8713	0.0826
		(-2.3347)**		(-1.5116)*		(6.0889)***					(0.0002)	
Sri Lanka	LnREX	2.8593	0.0918		1.5642		-0.1356		91.93	1.2522	68.3564	0.0756
		(1.9495)**	(0.6692)		(8.0374)***		(-1.2405)				(0.0000)	
ROC-Taipei	LnREX	-6.4831	-0.6064		3.5545		0.0325		99.28	1.5559	821.7870	0.0729
		(-7.9600)***	(-2.6184)***		(21.2791)***		(0.5367)				(0.0000)	
Thailand +#	^LnREX	-0.0612		-0.0676		2.9941	-0.1267	0.0118	57.02	2.9239	3.1839	0.0733
		(-0.9643)		(-0.1888)		(2.3295)**	(-2.2392)**	(2.6903)**			(0.0465)	

* Significant at 1-percent level.
** Significant at 5-percent level.
*** Significant at 10-percent level.
Notes: (1) + Estimated regression equation on log first-difference.
----- # Estimated regression equation with Cochrane-Orcutt procedure [i.e., Indonesia (AR4), Korea (AR1), Malaysia (AR1), Singapore (AR1) and Thailand (AR3)].
(2) Figures in parentheses are 't'-ratios.
(3) Estimated regression equation on semi-log in favor of dependent variable in the case of Malaysia.

so-called competitiveness in the international market is found to be an unimportant variable in influencing exports. This is further supported by the trend of nominal and real effective exchange rate where, during the period under review, the average annual growth of exports was remarkably high in great contrast with very high nominal and real effective exchange rate indices especially before 1985 (see Appendix 1.6). It implies that the growth of exports in the Philippines and Sri Lanka is not influenced by the exchange rate. Besides, as is common to them, macroeconomic imbalances including high inflation could more probably distort the prospects for exports. In contrast, Nepal has maintained a comparatively lower or stable nominal and real effective exchange rate while ROC-Taipei is among the few countries in the region which have been successful in maintaining a more stable or appreciating exchange rate along with a robust growth in exports due mainly to the scale of economies involved and the high-end technology used for the period under study. Thus, while the exchange rate is also one of the major factors influencing the demand for real exports in Nepal and ROC-Taipei, the direction of relationship is validated, although this is not significant in the case of Korea.

Except for the case of Nepal where the export-weighted real GDP of the major importing countries unexpectedly shows a negative but statistically insignificant relation with the real export demand, the export-weighted real GDP explains positively and significantly the real export demand for Korea, the Philippines, Sri Lanka and ROC-Taipei. It shows that any change in real GDP of export partners leads to a positive and significant change in the real exports of Korea, the Philippines, Sri Lanka and ROC-Taipei. In the case of Nepal, the negative relationship between the foreign GDP and export demand, if judged from the size or volume of exports which is the lowest among the SEACEN countries, the level of foreign GDP has no influence on Nepalese exports. In other words, if Nepal could maintain a realistic exchange rate, her exports with a small volume can take advantage of the foreign markets, i.e., Nepal should still be concerned with the level of income of the importing countries. For the other countries, the real GDP of their export trade partners is highly significant in explaining the real demand for their exports. This means that the real exports of Korea, the Philippines, Sri Lanka and ROC-Taipei are substantially influenced by the income effect of their respective trading partners.

As mentioned above, dummy variables with a view to capturing the effects of policy changes are used in the cases of Korea, Sri Lanka

and ROC-Taipei where there were structural or policy changes involving trade promotion during the period under study. But contrary to expectations, the results show that the effect of policy changes is rather negative and insignificant in the cases of Korea and Sri Lanka, whereas it remains positive but insignificant in the case of ROC-Taipei. Given these results, the new exchange rate policy regime could not accelerate and instead reduced the export demand. Thus, the dummy variable reflects the failure to account for the positive and significant impact on exports through the change in exchange rate policy. The explanatory power of the regression is very high (99.28 percent) in ROC-Taipei, followed by the Philippines (96.39 percent), Sri Lanka (91.93 percent) and Nepal (72.3 percent) with a highly significant F-values for all the country cases.

The second group of countries with an estimated regression equation on log-first-difference form are Indonesia, Malaysia, Singapore and Thailand where none of the variables were stationary on level and none of them were cointegrated. But one cannot say definitely that in these specific-country cases, the selected time series cannot converge into stability over a period of time or cannot have a long-run equilibrium for the said function. Thus, our results are based on a few and primary exogenous variables where one may find a good fit subject to a change in the list of the exogenous variables and sample size. According to the results, the changes in the real effective exchange rate show an expected direction of relationship with the demand for real exports. However, the coefficient is not statistically significant in the case of Thailand while the coefficients are statistically significant in the cases of Indonesia, Malaysia and Singapore. Hence, a constant or a marginally changed exchange rate during the period under study could be considered as one of the main reasons for higher exports in Thailand. In other words, Thailand has been successful in maintaining a spectacular growth in exports since the second half of 1980's because the real effective exchange rate has been generally realistic. The demand for real exports is significantly explained by the changes in real effective exchange rate or their competitiveness, in the cases of Indonesia, Malaysia and Singapore.

Similarly, the changes in the export-weighted real GDP of the trading partners significantly influence the demand for real exports for Indonesia, Malaysia, Singapore and Thailand. This is shown by the coefficients of export-weighted foreign GDP which are highly significant (at 1-percent level) in Indonesia and Singapore followed by

Malaysia and Thailand (at 5-percent level). The dummy variable shows a positive but insignificant result in the case of Indonesia, whereas it is statistically significant with an unexpected negative sign in the case of Thailand. In the case of Thailand, the flexible exchange rate regime rather shows a negative impact on export sector. This is possible on the ground that the exchange rate itself is insignificant in explaining the demand for real exports. Similarly, in the case of Thailand, other things being equal, the demand for exports increases significantly over the time period as shown by the trend variable. The explanatory power of the model as shown by R^2 is highly significant in the cases of Indonesia (78.71 percent) and Singapore (70.70 percent), followed by a low level of R^2 in Malaysia (40.56 percent) and Thailand (57.02 percent). But the overall predictive power of the model based on F-values is very high in the cases of Indonesia and Singapore followed by a significant level of predictive power in the cases of Malaysia and Thailand. The model could be considered as generally successful in explaining the behavior of the selected variables consistent with economic theory.

III. Export Promotion Policies in the SEACEN Countries

As discussed earlier, almost all the SEACEN countries have embarked on trade liberalization in general, and export promotion in particular, during the last two decades. This section presents a brief overview of the export promotion policies of the SEACEN countries while a more detailed analysis is presented in the country chapters.

Indonesia shifted its policy towards export promotion with a view to boosting its non-oil/gas exports in 1982 when the oil/gas exports became vulnerable in the world market. Thus, Bank Indonesia started to provide export liquidity credit along with numerous credit-related facilities to exporters. But in 1990, the export credit facility was replaced by a drawback system which has been in effect since 1986. Bank EKSIM is a specialized bank for export/import financing in Indonesia. The foreign banks were also permitted to open their offices in Jakarta as well as in other six provincial cities in the late 1980s with a mandatory guideline of 50-percent portfolio loan to export activities. Apart from allowing freedom in the payments system, Bank Indonesia has extended the issuance draft maturity and rediscount period. Within a managed floating exchange rate system, exporters are free to use their foreign exchange earnings as well as to borrow off-shore loans. Thus, capital transactions are free from exchange controls.

The exchange rate has been based on a trade-weighted basket, but still many periodic devaluations had been instituted to maintain the competitiveness of exports. Among other things, the promotion of non-oil/gas exports was the core of financial reform of the late 1980s, since banks have to channel at least 80 percent of their total foreign borrowings to finance export activities.

During the 1980s, Indonesia introduced various fiscal policy measures including the provision of port facilities as well as duty drawback and exemptions to compensate anti-export bias, import duty exemptions for export production, preferential quota system over tariffs, abolition of non-tariff barriers in major items and liberalization in foreign investment for the promotion of non-traditional exports. There are various public and private organizations, including the National Agencies for Export Development, to help support the promotional activities in exports. Similarly, the Export Support Board is providing the consultancy services to exporters while Ansuransi Ekspor Indonesia (1985) has taken over the management of export credit insurance scheme from its sister institution. In the mid-1980s, bonded warehouses were converted into bonded zones. Together with the export financing scheme which facilitates export-oriented industries, pre-shipment export finance guarantee and post-shipment credit and insurance were made mandatory in 1990. In sum, Bank Indonesia has undertaken monetary policy measures including export finance and exchange rate management to promote exports in line with fiscal policy measures.

In ***Korea***, various incentives for export promotion in the area of financing, taxation and tariffs were introduced as early as the 1960s. In order to identify the obstacles to export expansion and to provide workable prescriptions, Korea, from the very beginning, has uniquely maintained the "Expanded Meeting for Export Promotion" which was renamed in 1977 as "Expanded Meeting of the Trade Promotion Committee" in order for the government emphasis to be given not only for the exports but also for the imports. Similarly, there has been a positive impact on the psychology of Korean exporters with the introduction of merit medals for the best performers in export activities. As a long-run strategy, Korea has been maintaining for the last one-and-a-half decades or so, the Japanese-type specialized trading companies in order to improve the efficiency of small-scale individual sales techniques in international markets. Korea introduced an automatic access to export financing as early as the mid-1960s including credit based on the master letter of credit (LC), as

well as local LCs known as domestic exports. The exchange rate was changed to multiple basket-pegged system in 1980 followed by a market average exchange rate system as a transitional stage towards the early adoption of a managed float system beginning 1990. All-out efforts in exchange rate policy were aimed at maintaining the competitiveness of Korean exports. The early tariff incentive system was changed into tariff drawbacks on imported raw materials to be used for export production under the GATT rules in the mid-1970s.

Nevertheless, the export finance and insurance schemes, direct and indirect tax incentives as well as the monthly meetings of the policy-makers, businessmen and economic experts have been considered more effective measures in Korean trade policy. Although nearly every banking institution takes part in export promotion, Export-Import Bank of Korea as a specialized institution deals with the medium- and long-term credits for export/import transactions and overseas investment whereas the Economic Development Corporation Fund deals with the export insurance business. The Korea Development Bank has also played an important role in financing the export-oriented heavy and chemical industries. As mentioned earlier, the Japanese-type general trading companies (GTCs) for the last fifteen years or so have played a crucial role in export expansion. A business firm should maintain a share of more than 2 percent of the total exports of Korea for each year to obtain or continue GTC status. On this basis, there were 13 GTCs in 1976, while 5 GTCs lost their status and the remaining 8 GTCs accounted for 43 percent of the total exports in 1991. The Korea Trade Promotion Corporation deals solely with the export marketing programs whereas the Korea Foreign Trade Association is known as the Korea World Trade Centre where each company or individual, who wants to engage in export-import business, is required to be a member to become a registered foreign trader.

In ***Malaysia***, various soft loan schemes have been launched to extend facilities to domestic exporters as well as to foreign buyers. The export credit refinancing facility (ECR), which was established in 1977, mainly comprises post-shipment refinancing and pre-shipment financing facility with a view to obtaining immediate funds upon shipment and meeting working capital needs of exporters and related manufacturers, respectively. The ECR scheme also covers the trading companies dealing with the raw materials and intermediate goods used in the manufacturing process. These schemes are aimed at promoting manufactured exports and agricultural products with a higher

value-added and local content. The success of this program is obvious as the level of annual utilization of the ECR facilities reached nearly RM 18 billion in 1991 from about a meager amount of RM 140 million in 1977. For this, Bank Negara Malaysia is the sole authority. Together, the Malaysia Export Credit Insurance Berhad (MECIB) has provided the insurance coverage in case of exporters' loss. The MECIB has also launched a bond indemnity support facility for the contractors-cum-exporters as well as an export credit insurance/ guarantee scheme to protect commercial banks and other financial institutions against non-payment by exporters.

Malaysia has also adhered faithfully to maintain a non-interventionist foreign exchange policy. Since the Plaza Accord of 1985, the ringgit has been depreciated against the major currencies of trading partners namely USA, Japan, Germany and Singapore which in turn has enhanced the competitiveness of Malaysian exports. The Promotion of Investment Act (PIA, 1986) which replaced the Investment Incentive Act (1968) has provided tax incentives for the export sector in the form of: (i) abatement of adjusted income for exporters; (ii) export allowance of 3 percent; (iii) double deduction of expenses for promotion of exports; (iv) double deduction of export credit insurance premium; and, (v) drawback of customs duties and exemption from import duties, excise and sales tax. At present, there are 12 free trade zones (FTZs) in Malaysia which have attracted large export-oriented industries in electronic and textile sectors. In case the FTZ is neither practised nor desirable, the licensed manufacturing warehouses are entitled to enjoy similar facilities as enjoyed by FTZs. The Trade Commissioners provide the market information to exporters whereas the Malaysian Export Trade Centre in close liaison with Trade Commissioners provides market information and arranges various meetings/ seminars for the foreign buyers and Malaysian exporters. The Ministry of Trade and Industry organizes trade fairs, trade missions, in-store promotions, fact-finding missions, overseas buyers' missions, etc. Similarly, Malaysia has already signed 15 bilateral payment arrangements so far. Malaysia has also been successful in attracting foreign direct investment which has helped promote technology transfer in the manufacturing sector. Besides various institutions in financing small- and medium-scale industries, Bank Negara has introduced very recently a New Investment Fund with a view to generating new productive capacity especially in supporting the export drive.

Prior to 1980, the main thrust of the ***Nepalese*** trade policy was market diversification with a view to reducing the dependency on India as well as to earning convertible foreign exchange. Unfortunately, the diversification drive created a side-effect in the economy under the lure of various incentives with the diversification of primary commodities to overseas markets although they could be exported more profitably to India. Additionally, this situation created big trade deficits with India and hence, payments difficulty. From the very beginning, Nepal has been using the exchange rate as a powerful instrument for the promotion of exports. As such, as early as the 1960s, Nepal adopted Exporters' Exchange Entitlement (EEE) scheme popularly known as 'Bonus Scheme' which lasted up to the late 1970s. But the EEE scheme created a lot of distortions, encouraging primary product exports as well as luxurious goods imports rather than the more needed capital and development goods. So in order to improve overseas exports, the EEE was replaced by a dual exchange rate system in the late 1970s. Various incentives such as duty drawback, warehouse facility, air transport, etc., were introduced in 1982, followed by a nine-point export promotion scheme including cash subsidy, export finance, etc. Similarly, for the easy access of rediscount and insurance facility, commercial banks have established an export unit in their branch offices. Together with the recent privatization program, a dynamic and transparent trade policy has been announced to develop new export bases through the promotion of backward linkages for making export trade competitive and sustainable. Among other things, the one-stop one-window system and the full convertibility of the Nepalese currency in current account are the major steps towards attracting foreign investment and hence the promotion of exports in the recent years.

In the case of the ***Philippines***, the export growth in US dollar values was recorded at a low level of 4-5 percent in the 1950s and 1960s mainly because of the bias against exports from the overvalued currency and import controls (Appendix 1.9). The Investment Incentives Act of 1967 and the Export Incentives Act of 1970 helped promote a robust growth of exports (20.3 percent) in the Philippines for the period 1970s, a historically high record during the past four decades or so. As a result, the semi-conductors and garments came up as non-traditional exports though with a relatively low value-added contribution. However, in the 1980s, the Philippines experienced a slow growth of exports in US-dollar terms although the currency was devalued dramatically in 1983-1984. In 1990, the terms of export

financing were made comparable to the international market along with rediscount facility and pre- and post-shipment loans. As such, the rediscount facility for the exporters was made available from the regional offices of the Central Bank and later on, this facility was also extended to the indirect exporters. At present, exporters are allowed to avail themselves of a US dollar-based working capital credit. Very recently, the Central Bank has fostered a market-oriented thrust in the determination of exchange rates making all foreign exchange trading activities to be dealt through the Philippine Dealing System. As a part of the liberalization package, among others: (i) the removal of the mandatory surrender requirement for export proceeds; and, (ii) the liberalization of payment modes for exports and imports.

Presently, imported inputs are allowed to enter free of duty under the bonded manufacturing warehouse and customs bonded warehouse for export production. In the case of garments and textiles, the Garment and Textile Export Board is the sole administering agency. The Philippine Export and Foreign Loan Guarantee Corporation deals with exporters and/or commercial banks against non-payment risks by foreign buyers. The small and medium industries must have: (i) a three-year track record of exporting priority non-traditional products; (ii) an average profit margin of 10 percent; (iii) an average return on equity of 15 percent; and, (iv) an average current ratio of 1.5:1 to qualify for the export credit guarantee program. Similarly, under the United States Agency for International Development (USAID) guarantee scheme, four major Philippine banks have provided 50 percent guarantee coverage on their loans to small and medium enterprises in exports. Since the main method of payment for the majority exporters has been the sight letters of credit, there seems no urgent need for an export credit insurance and guarantee scheme which covers basically non-payment risks. The export environmental development program, the export market development program and export enterprise development programs are the major branches of national export development program which ultimately decides on export policy. The Export Omnibus Bill is designed to remedy the shortcomings in the policy and institutional framework for export promotion. The recently established export processing zones are expected to contribute to the country's industrialization and export expansion by providing suitable sites for foreign investors through fully operational four zones, three industrial areas and separate self-contained enclaves for a variety of industries.

In the case of ***Singapore***, in which high import content in domestic exports exceeds 70 percent, its exchange rate policy is aimed at maintaining low inflation to ensure sustainable economic growth rather than making exports more price-competitive. Thus, any depreciation in the Singapore dollar makes imports more costly, and thus pushing up export prices. The main thrust of the Republic's trade policy is to develop Singapore into an international trading centre. As it is, Singapore has no trade restrictions. The Tradenet, a one-stop electronic data interchange system introduced in 1989, has helped the traders gain quick administrative clearance. The double tax deduction scheme and the international trading company scheme have provided a concessionary tax rate to the export-oriented units. The export finance rediscount/ refinance schemes which were introduced as early as the mid-1970s have recently been expanded to small- and medium-sized enterprises penetrating external markets. Similarly, since the mid-1970s, insurance has been provided to exporters against financial and/or non-financial risks of non-payment by buyers.

The Trade Development Board (TDB), while boosting the cost competitiveness of export companies, is also concerned with the quality of products and the skills of employees. Trade fairs and missions qualify for grants under the market development assistance scheme set up by the TDB while the Design Centre is a policy-making unit for the Design Council which offers grants for eligible costs of designed projects. In addition, the TDBs other schemes include: (i) the Certification Assistance Scheme to help obtain required international certification; (ii) the Approved International Fair Scheme to attract trade exhibitors and visitors to local trade shows; (iii) the Export Institute of Singapore to provide education and training up to Diploma in Export Marketing; and, (iv) the TDB-Globalink to offer a customized on-line information service regarding international business, trade, tenders, banking, finance, property, legislation, and so on. To sum, Singapore supports schemes of trade preferences which conforms to the GATT rules. As such, Singapore actively participates in the Asia-Pacific Trade Association (APTA), the Generalized System of Preferences and the Global System of Trade Preferences.

In ***Sri Lanka***, prior to the liberalized trade policy of 1977, there were also schemes such as Foreign Exchange Entitlement Certificate (FEEC) and Convertible Rupee Account (CRA) targeting to promote non-traditional exports. But because of the high tariffs, quantitative

restrictions, exchange control regulations, licensing system and public sector trade monopolies, the traditional export sector was rather distorted. In contrast, the liberalization scheme provided various facilities such as lowering export duties, easing of exchange control regulations, removing quantitative restrictions, etc., with a view to encouraging and diversifing the export sector. As such, the Central Bank included exports in the priority sector so that export sector would not starve for credit. As a result, the short-term export credit refinance for every exporter and the supplementary export credit refinance for non-traditional exporters were made available together with a refinance facility under the medium- and long-term credit fund for fixed capital requirements of export-oriented and agro-based industries. But over time, various types of refinance schemes with preferential interest rates distorted the overall interest rate structure and hence the competitiveness of financial reforms. Thus, the net result was an adverse impact on the efficiency of resource allocation. At present, refinance facilities are provided only for high value-added or pioneering industries with the objective of diversifying export structure.

In line with the liberalized trade and payment system, Sri Lanka adopted a flexible exchange rate system. During 1977-1991 period, the Sri Lankan currency was depreciated against the world major five currencies by about 69 percent. In contrast, because of the high domestic inflation, the real effective exchange rate adjusted for inflation differential continued to appreciate since the late 1980s which overshadowed the desired objective of maintaining international competitiveness. As mentioned above, with the removal of quantitative restrictions since the late 1970s, tax and tariff incentives have been provided especially for non-traditional exports through General Incentive Scheme as well as under the Greater Colombo Economic Commission which was later on renamed as the Board of Investment. All the commercial and development banks as well as the non-bank financial institutions are the major institutions providing different financial and non-financial facilities to direct and indirect exporters. Similarly, the Export Development Board (EDB), established in 1979, has provided financial as well as high potential exportable list of products and overall information about the markets. The EDB has also implemented Annual Award Scheme and Export Expansion Grant as an incentive to the exporters. The Sri Lanka Export Credit Insurance Corporation has provided various guarantee facilities such as: (i) pre- and post-shipment credit guarantee; (ii) export payment insurance; and, (iii) export

performance guarantee. In order to promote exports, the Board of Investment has established three export processing zones with well-developed industrial estates and improved infrastructural facilities. The Expo 1992, Sri Lanka's first export fair and the Export Decade 1992-2002 are the additional export promotion activities in Sri Lanka.

To initiate the early 1960s policy shift from import substitution towards export expansion, ***ROC-Taipei*** initiated various policy measures such as the Nineteen-Point Economic and Financial Reform, managed floating system, establishment of various specialized institutions and other related measures, either in the 1960s or the 1970s. As a result, ROC-Taipei experienced a rapid industrial growth during the 1960s and 1970s. From the very beginning of its resumption, the Central Bank of China, Taipei, introduced export credit refinancing in the early 1960s which was further reformed to upgrade the loanable ratio of export loans followed by a preferential interest rate in the early 1970s. In line with the export expansion policy, the Central Bank has further focused for technology-intensive as well as infrastructural projects such as electricity and telecommunication development. In 1978, the unitary exchange rate policy was replaced by a managed floating rate system with a view to helping export enterprises through stabilizing the foreign exchange rate and hence, increasing the competitiveness of export products.

Among other things, liberalization of trade control and encouragement of exporters were the major objectives of the Nineteen-Point Program which laid the foundations for ROC-Taipei's "take-off" in the 1960s and 1970s. The Export-Import-Bank has been actively involved in providing various types of export insurances such as: (i) D/P, D/A export insurance; (ii) export finance insurance; (iii) medium- and long-term export insurance; (iv) overseas investment insurance; (v) medium- and long-term export exchange risk insurance; (vi) export credit insurance; and, (vii) overseas construction insurance. Besides, this Bank has also provided a wide range of financial support such as loans and guarantees to supplement the functions of local commercial banks. From the early 1960s, various tax incentives, such as: (i) five-year income holiday; (ii) limit on income tax payable; (iii) tax exemption for undistributed profit; (iv) tax deduction of exports; (v) installment payments of import duties on industrial equipment; and, (vi) exemption of export sales from business tax, had been provided through the "Statute for Encouragement of Investment"

until it was replaced by the "Statute for Industrial Upgrading" (SIU) in 1990. Altogether, there are three export processing zones which were set up during the 1960s. Taking into account the sharply rising labor cost and hence the tendency of shifting towards capital and technology-intensive production, the Kaohsiung export processing zone, the oldest zone, is being transformed to a high-tech industrial park.

To ensure the quality of exportable products, the Bureau of Commodity Inspection is responsible for the inspection on a wide variety of products. The China External Trade Development Council (CETRA), established in 1970, acts as the centralized trade promotion agency. As such, the CETRA has coordinated with Government and private sector to break through the barriers and engender competition in the international trade by providing services and assistance, mainly on: (i) marketing; (ii) information; (iii) exhibitions; (iv) product design promotion; and, (v) training of talent. Since the late 1970s, the Hsinchu science-based industrial park has carried out various industrial research and development works. To upgrade labor quality as well as to boost productivity, ten vocational training centers were set up, followed by the establishment of a vocational training bureau to coordinate the supply and demand of technical labor force with a view to meeting the needs of high-tech industries. According to SIU the high-tech industries have a positive impact on high value-added, low energy consumption and least polluted environment. Similarly, businessmen are urged by the Government to form big trading companies to be able to compete with large manufacturers and large-scale traders in international markets.

Thailand had to face balance of payments deficits in the late 1960s due mainly to high level of imports of machinery and raw materials for import substitution industries, stagnation of primary exports and the decline in both US military spending and foreign investment. Thus, in the early 1970s, Thailand started focusing on the promotion of manufactured exports and this effort was stepped up further in the mid-1980s through 1990. Despite a spectacular growth in exports, Thailand has been facing the problems of infrastructural bottlenecks, shortage of skilled labor and inflation since the late 1980s. In response, the Bank of Thailand extended its rediscount facility for all types of exporters in 1960 which was initially introduced for the rice exporters. Maturity of the export refinancing both for the pre- and post-shipment was extended in 1983. A special rediscount facility was

also started much earlier for the small exporters. In the mid-1980s, the domestic letter of credit scheme was introduced for the manufacturing firms subject to promotion by the Board of Investment (BOI). Basically, the exchange rate was used as a tool to mitigate the effects on trade of foreign exchange volatility on several occasions since the late 1970s when Thailand adopted a more flexible exchange rate system. As the BOI is solely responsible in promoting export-oriented activities through fiscal incentives, it has introduced duty drawback and tax exemption schemes including the promotion of international companies with a fixed export targets. A 100-percent exemption on overall tax paid on imported raw materials as well as the rebates on all types of taxes such as excise, municipal, business, custom, etc., were also introduced in the early 1970s. Since the rebate rates were too aggregated, they were disaggregated in 1986 based on the four-digit Customs Cooperation Council Nomenclature (CCCN) codes.

The bonded factory system, which completely bypasses customs procedures while importing inputs to be used for manufactured exports, became very popular in Thailand in the first half of the 1980s. For administrative simplicity, the exporters are required to submit detailed input coefficients to customs officials for their inspection. At present, there are seven export processing zones in Thailand. For the sake of avoiding possible shortage of goods and "cultural preservation", still there are numbers of non-tariff measures in the cases of particular commodities. Commercial banks are a major source of export credit in Thailand. However, large and small commercial banks differ in their policy towards exports. The latter are less inclined to export finance. The Industrial Finance Corporation of Thailand also provides soft loans to export-oriented industries. The Department of Export Promotion, a government agency, deals with marketing information, trade fairs and trade missions. It has 17 overseas trade centers. Altogether, 45 commercial counselors abroad are involved in marketing, trade fairs, trade contracts and other related activities for the promotion of exports. The Export Development Committee has simplified export procedures although there are still nine channels to process export activity. The Export Development Fund created from the import charges is used for the promotional activities such as trade missions, fairs, negotiations, etc. In addition to government agencies, there are private organizations such as the Board of Trade, the Federation of Thai Industries and Foreign Chamber of Commerce which assist their members in the promotion of their exports.

IV. Problems and Issues on Export Promotion

As discussed earlier, some of the SEACEN countries have started export promotion activities quite early and over the years, they have developed into the stage of capital-intensive high-technology electronic policy framework. On the other hand, those member countries which have a low level of industrialization and export base have been catching up by placing similar emphasis on the promotion of manufactured exports. In any case, each SEACEN member country faces various types of problems in export promotion. Thus, this section highlights the major problem areas that the SEACEN member countries have faced in the process of export promotion.

In the case of ***Indonesia***, there has been a lot of investment in building export infrastructure. But in comparison to the progress of industrialization, the infrastructural facilities provided even with the additional efforts such as supply of electricity through new power plants, extended port facilities, well-established EPZs, etc., have also lagged far behind. Secondly, since the lifting of export financing from refinancing facilities, exporters have competed in the credit markets. So far, banks and financial institutions are free to charge market rate of interest for the export credit, it would be more costly as well as selective. In addition, indirect exporters who are crucial for backward linkages have starved for credit as well as for duty-free imports. As such, the net result has been the discouragement of Indonesian exporters. Finally, because of the lack of marketing information, economic situation and business trend in the international markets, Indonesian exporters have faced difficult business prospects.

Based on the recent past export performance, ***Korea*** has been facing the problem of imbalances in exports by industry. This is to say, the emerging industries such as textile fabrics and semi-conductors are leading over the traditional products of footwear, electric household appliances, etc., which show negative trends. Similarly, exports to advanced countries namely USA, Japan and EC have declined. All these call for a structural change in exports by destination and industry. The export promotion strategies including those technologies developed in Korea favor the assembling and processing of semi-finished goods with economies of scale, discouraging the development of small- and medium-sized firms. The export unit values remain stable in contrast to the increasing cost of production causing exports to be less profitable than domestic goods.

Since the electrical machinery and appliances, textiles and rubber-based products dominate the manufactured exports of ***Malaysia***, there is always a market risk because these products are subject to the vagaries of the business cycle like primary commodities. Moreover, the destination of exports, which is mainly to USA, Japan, EEC and Singapore, needs to be diversified to ensure less volatility in export market. The present need of Malaysia is to emphasize on export-oriented high value-added and high-technology industries to move towards capital-intensive products. Similarly, government intervention should be towards promoting a neutral effect so that the export-oriented and resilient private sector-led economy can be sustained. Finally, the manpower development in meeting the growing needs of high-tech and heavy industries should be pursued through education and training.

In ***Nepal***, because of the poor performance of the agricultural sector which has a dominant role in the economy, traditional products have no more role to play in export growth. Due to topographical hardships and landlocked position, Nepal has been facing the problem of infrastructural bottlenecks. The industrialization process is at an early stage and the so-called leading manufacturing products such as handicrafts, carpets and readymade garments are overdependent on imported raw materials as they also suffer from a lack of economies of scale. Moreover, lack of prior inspection of goods, certification of quality to acceptable standards, the value-added contribution is hard to upgrade. Because of the number of procedures and formalities of the trade treaty with India, exports to India entail the problem of value-addition as well.

The ***Philippines*** has been facing fluctuating trade balances over the past four decades or so. The bias against exports as well as the import controls in the 1950s and 1960s set back the growth of exports while the export-oriented policies in the late 1960s and early 1970s contributed a lot to the promotion of exports. However, the infrastructural bottlenecks such as electricity, transport and communication, the high interest rate regime, the absence of domestic letters of credit and the rigid exchange rate policy were the major constraints in the promotion of export-oriented industries in the past. Similarly, the fast growing manufacturing exports such as garments and semi-conductors based on a high import content have a relatively low value-addition. Nevertheless, with the announcement of exchange rate liberalization in 1992, there have been a lot of reforms towards privatization with a

view to enhancing the efficiency and competitiveness of the economy, which include deregulation in the financial sector, improvement in the infrastructural services and implementation of the tariff reduction program.

The persistent trade deficit, which has been declining, calls for raising the value-added of domestic exports in ***Singapore***. The shift from highly labor-intensive to skill and capital-intensive such as electronically controlled industrial process as robotics is needed to cope with the problem of labor shortage followed by further training and education for the indigenous skilled labor and professionals. Singapore's exports are highly vulnerable to economic downturns and protectionism in the major developed countries such as USA, Japan and EC and vice-versa. The protectionist measures taken against Singapore by Australia, USA and EC are quantitative restrictions, anti-dumping and countervailing duty actions.

Sri Lanka's trade deficit over the last twenty years was due mainly to a high growth of imports against exports. In turn, this is due to the fact that a large share of non-traditional exports depends heavily on imported inputs with low domestic value-added. In contrast, the traditional exports have a high value-added contribution though their expansion is limited by structural, institutional and technological constraints. Despite the significant depreciation of the Sri Lankan currency in nominal terms, the export sector is affected adversely by the increasing trend of budgetary deficits; and, hence by a very high inflation, causing appreciation of the Sri Lankan currency in real terms. Similarly, exporters are affected adversely by higher interest rates in the domestic front on top of a discriminatory tariff system in the external front. Some of the Sri Lankan products such as gerkins, spices and foliage plants have to compete in the EC markets with the African and Caribbean countries which are enjoying preferential market access under the Lomè Convention.

The accumulated foreign reserves in the course of a persistent trade surplus imposed pressure on the appreciation of ***ROC-Taipei*** currency which in turn intensified trade friction with USA. At present, ROC-Taipei is facing the problems of export promotion mainly because of: (i) protectionism in international market; (ii) predominance of small- and medium-scale industries and hence lack of own brand names; (iii) overdependence on foreign technologies, imported machinery and raw materials; and, (iv) increase in

production cost due to labor shortage, wage rise and soaring prices for plant sites.

In the last five years or so, ***Thailand*** has been facing the problem of trade deficits mainly because of the influx of foreign direct investment. Overheating of the economy, the upward pressure on prices, and the environmental degradation have accompanied the expansion of manufacturing sector. On the one hand, there is a cost burden to exporters by red-tape in the delay in tax refund system, Board of Investment's approval due mainly to the shortage of government personnel and on the other, small exporters have difficulty in enjoying preferential treatment in comparison to their big counterparts. Besides, the financial facilities are lagging behind in comparison with the expansion of exports due mainly to a shortage of funds from the Central Bank. The overall incentives have created overdependence on raw materials and intermediate products from abroad. The protectionist policies of the developed countries and the formation of regional trading blocs as single market would have limited the market access of Thai exports.

V. Policy Recommendations for Effective Export Promotion

Based on the diverse experiences in export promotion measures, level of export performance, export base, industrialization and on the whole, the economic perspective, each SEACEN member country faces different problems and issues related to the export development. However, the basic programs to stimulate export development are similar which include financial and fiscal incentives, maintenance of realistic exchange rate, macroeconomic stability and neutral treatment between exports and imports, diversification of country and commodity-wise exports, enlargement of export base. Thus, this section presents policies which could be considered towards enhancing the export performance of the SEACEN countries.

The use of existing domestic letter of credit should be modified in ***Indonesia*** so that the indirect as well as the final exporters can make use of it through the issue of certificate attesting to past performance of exporters by concerned banks which ultimately reduces the banks' losses stemming from exporters' deliberate default or non-performance. Secondly, the role of the National Agency for Export Promotion could be enhanced by privatizing its management. Thirdly, the establishment of general trading companies in private sector could be helpful to directly

market Indonesia's exports abroad and actively encourage alternative channels of marketing. In other words, public sector intervention should be minimized in export marketing. Finally, taking into account the role played by the agencies in the past, the credit goes to overseas buyers and joint-ventures which made it possible for Indonesian exports to be channeled into overseas markets. With this background, one can say that there is an urgent need to focus on target marketing with the support of strong private sector groups.

As ***Korea*** is well on the way towards becoming an industrial country, the trend of deregulation and liberalization in every sector of the economy shows the market mechanism as a first best policy. With the economic cooperation of its trading partners especially newly developed or developing countries, Korea will benefit a lot from the international division of labor or specialization rather than keeping artificial measures to promote exports. Nevertheless, Korea should start with structural change in favor of the newly emerged industries as long as the traditional products are losing comparative advantage in the international markets. Korea should expand the new commodities to its emerging trade partners to avoid the trade concentration risk with the developed countries which it has been facing for the last few years. Finally, in the Korean economic perspective, the public sector has to play a guiding role to minimize friction and the private sector should take a leading initiative for the promotion of exports.

After a long period of heavy protection, the time has come for the ***Malaysian*** industries to be more competitive with foreign counterparts. As such, Malaysia should gradually follow a low uniform tariff system to ensure greater competition and free trade. In line with the ASEAN Preferential Trading Arrangement and ASEAN Free Trade Area and, with the adoption of Common Effective Preferential Tariff Scheme, Malaysia would have a tremendous opportunity if it works with a comprehensive export-targeting program. Under the GSP scheme, Malaysia could benefit a lot by enhancing competitiveness, design and quality of products. A search for the non-traditional markets such as the Middle East, African and Latin American countries as well as the expansion of bilateral and multilateral payment arrangements should be a long-run strategy for Malaysia. With this perspective, the existing export-targeting system which is focused on Japan, USA and EC should be revitalized. Similarly, the Government needs to create a conducive environment to promote indigenous new technology-based firms. For

this, the recently introduced Human Resource Development Fund should be channeled to educate and train the technical manpower.

Since its industrial development is in the primitive stage, ***Nepal*** should emphasize on labor-intensive techniques with a view to providing employment opportunities. A balanced development of export/import is essential because even consumer goods are also imported to meet public demand. Because of the transit problem, Nepal should endeavor to promote light-weight and high value-added commodities. There should be a feasibility study in view of the topographical constraints prior to establishing the export-oriented industries to ensure the comparative advantage. The existing Trade Promotion Centre should be made responsible for the design, quality control and market information. The total efforts of the industrial policy should be to attract foreign investment so that the export base could be upgraded.

In the ***Philippines***, the recently liberalized foreign exchange system has increased the confidence of the foreign income earners such as exporters and overseas workers which ultimately encourage the potential exporters. Similarly, the deregulation of the banking system including branch expansion, free entry of foreign banks has created the competition in banking sector in providing better services at the lowest possible cost. The implementation of the tariff reduction program is expected to enhance foreign trade performance. The involvement of the private sector for the development of infrastructure is a good start in order to promote efficiency and competitiveness. Furthermore, with the coordination of the newly-created Department of Energy, the power outages which remained the main constraint of the industrial sector, in the recent past, has been eliminated significantly. Finally, the recently implemented overall policy package has encouraged the competitiveness of the Philippine manpower which is widely believed to be comparable with ASEAN members in terms of wage and productivity.

In ***Singapore***, the trade policies should be at promoting Singapore as an international trading and transportation hub. There should be a sustained upgrading of Singapore's trading infrastructure in order to attain world-class standards. In view of emerging trade blocs, Singapore should further endeavor to diversify and expand exports to other markets such as China, India, Eastern Europe and Latin America. Similarly, to

cope with the acute shortage of manpower, Singapore should focus on the development of automation which really can replace the manpower.

In ***Sri Lanka***, macroeconomic instability has been a cause for the low performance of export sector. In view of expanding more value-added industries, there is an urgent need for institutional and structural changes. As there is a high value-added in traditional products, the new type of products should be experimented in line with the changing international demand such as tea and rubber products. For the non-traditional products, expansion in the village level units, multi-cropping methods and on top of these, exporters are in need of a guideline based on the findings of market research from time to time. After the establishment of standardization and preferential treatments within the EEC, it is necessary to improve the quality as well as to identify new products with high value-added to enter into the duty-free EEC markets.

In the six-year National Development Plan started in 1991, ***ROC-Taipei*** has set targets for exports and imports with a view to maintaining a balanced development. To achieve the targets, the market should be diversified and promoted so that enterprises could expand their share in the world market. In the early stage, when the labor cost was comparatively low, the Government concentrated on labor-intensive light industries. But when labor cost raised sharply in recent years, the labor-intensive light industries have lost their comparative advantage. Moreover, the small enterprises also face the problem of own brand names. In order to enhance the competitiveness of ROC's products, the most important step is to move from labor-intensive, light-industries to technology and capital-intensive heavy industries. At present, the promotion of big trading companies is the main concern to upgrade international marketing capabilities and to decrease production cost. To be integrated into the world economy, ROC-Taipei must persist actively to develop bilateral and multilateral relations and hence to join more international economic organizations.

In the case of ***Thailand***, the infrastructural facilities particularly transportation and telecommunication, and supply of technical manpower are the major concerns to enhance production efficiency and hence, international competitiveness. To ease the problems faced by exporters, the Customs Department should reform the facilities of: (i) bonded packaging warehouses; (ii) manufacturing warehouse zones;

(iii) customs office in large industrial estates; and, (iv) computerization for the purpose of tax collection and goods release. Taking into account the congestion at the Bangkok Port as well as the door-to-door delivery system, the facility of inland container depots is urged to work out. The EXIM Bank established in September 1993 is a specialized financial institution which is to promote and support exports and investment for the development of the country by fulfilling the gap in credit, guarantee, insurance and other financial services which are deemed necessary. Rural industrialization should be a main thrust of the infrastructural policy to ensure the backward linkages. Needless to emphasis, the role of the Central Bank should focus on the stabilization of the economy.

VI. Summary and Conclusion

Given the first oil shock, the collapse of the Bretton Woods system as well as the successful experience of some of the SEACEN countries such as Korea, Singapore and ROC-Taipei in exports, the rest of the SEACEN countries recognized the importance of focusing on the export sector. Subsequently, the second oil shock, recession in OECD countries and rapidly growing debt service obligations due to rising interest rates gave rise to further liberalization in almost all the SEACEN economies.

During the period under study (1970-1993) with the exception of the first half of 1980s, exports in the SEACEN countries as a group have registered a robust growth. But imports have also increased rapidly. The net result, except in the cases of Indonesia, Singapore and ROC-Taipei, has been the less-than-satisfactory performance of the trade account. One interesting point here is that the average annual export growth has fairly exceeded the import growth in the cases of Korea, ROC-Taipei and Thailand, whereas import growth has exceeded export growth for the rest of the SEACEN countries. Despite the excess of export growth over import growth for twenty years, Korea and Thailand have faced the problem of trade (merchandise) account deficits. In contrast, Indonesia has recorded surpluses in trade account despite a fairly high import growth over export growth for the period under study.

In fact, most of the SEACEN countries have faced the problem of deficits in their trade account even as they are now sufficiently opening

up. If we look at the growth of export in US dollar values, except in the case of Nepal, all the SEACEN countries maintained a spectacular growth in the 1970s. In such a situation, one can easily say that the export growth in domestic currency values may be part of the devaluation gain in many SEACEN countries. In this context, a look at exports as percentage of GDP shows a direct growth promoting role of exports as well as the degree of openness of the economy. Exports are the single biggest sector and fulcrum of the economy of Singapore where the export/GDP ratio was 1.4:1 in 1991 which is uncommon for the rest of the SEACEN countries mainly because Singapore is an entrepot trading center where the trade sector dominates over the other sectors of the economy. The export/GDP ratio is very high (.73:1) in Malaysia. This external orientation ratio is still low for the rest of the SEACEN countries. The more remarkable feature of the export trade of the SEACEN countries is that the traditional exports have declined in importance tremendously, followed by a progressive advance for the manufacturing exports.

However, on the basis of the nature and scale of industrial sector, with the exception of ROC, Taipei where the manufacturing sector has a higher share, the SEACEN countries can be classified into three groups. The first group with a higher degree of industrialization measured by industry as a ratio of GDP includes Korea (42.9 percent), Malaysia (46.2 percent) and Singapore (42.8 percent), followed by the second group of countries which have a marginally lower level of industrialization namely Indonesia (37.8 percent), the Philippines (39.8 percent) and Thailand (39.3 percent) (Appendix 1.9). Except in the case of Indonesia where manufacturing as a ratio of GDP is very low (13.8 percent), all the first and second groups of countries namely Korea (30.4 percent), Malaysia (26.8 percent), the Philippines (28.6 percent), Singapore (31.8 percent), ROC, Taipei (34.9 percent) and Thailand (26.4 percent) have a higher proportion of manufacturing production. As such, most of these countries have a bigger base for manufacturing exports namely textiles, electronics, chemicals semi-conductors and electronic machinery. Moreover, most of them are now placing emphasis on capital-intensive heavy industries with a view to upgrading economies of scale on the one hand, and minimizing the cost of production due to labor shortage and wage hike on the other. In contrast, Nepal and Sri Lanka have a low level of industrialization, and hence a narrow manufacturing export base. As such, the major manufacturing exports for these countries include handicrafts, carpets, readymade

garments, wood products, etc. Moreover, these products are mostly dominated by quota system under MFN status. These products are also based on light and labor-intensive techniques which reflect the abundant supply of labor with a comparatively lower cost.

If one looks at the import composition, the manufactured goods have a dominant role over the total imports of all the SEACEN countries. Evidently, most of the SEACEN countries have maintained a mutually competitive rather than a complementary status. The major markets for the SEACEN countries exports which were recorded as early as 1970 have also remained the same until recently and they include USA, Japan, EC as well as the intra-SEACEN countries. But over time, the export intensity has moderately increased to the EC and intra-SEACEN countries. The total volume of exports of the SEACEN countries in US-dollar terms for the last two decades or so has increased by about 35 times.

As discussed earlier, the present study has also established some empirical facts regarding the export and economic growth and demand for export from the SEACEN countries. Although exports are a component of GDP, in the recent economic literature, there are either disputes among the economists or different findings regarding the causal relationship between export and economic growth. For this, we have attempted to measure the direction of causality between exports and economic growth. An additional argument has been pursued by eliminating the component effect of exports on GDP. According to the results, which are also comparable to the earlier findings, there is a unidirectional negative relation from economic growth to export growth in Korea and Malaysia followed by a positive relation in Thailand. Similarly, there is a bidirectional negative relationship between exports and economic growth in the case of Singapore followed by ROC-Taipei with a positive relation between exports and economic growth. After suppressing the component effect, the results are more significant in the cases of Indonesia and Malaysia. There is no causal relationship either way between exports and economic growth in the cases of Nepal, the Philippines and Sri Lanka which implies that there may be other factors which influence exports and economic growth. In sum, the SEACEN countries should have to consider a simultaneous action rather than a piecemeal approach to policy formulation and implementation. In other words, the export promotion policy could

not be effective in isolation; rather, it should be complementary to the whole macroeconomic policy.

Similarly, real exports from the SEACEN countries depend on individual SEACEN country's international competitiveness as proxied by real effective exchange rate as well as the income effect from the importing countries as represented by the export trade-weighted GDP of the major trade partners. According to the empirical findings, the real effective exchange rate shows positive but statistically insignificant relation with the real export demand in the cases of the Philippines and Sri Lanka. For this, one can argue that if the real effective exchange rate failed to explain the real export demand, the so-called competitiveness in the international market is found to be an unimportant variable in influencing exports. Further, this is supported by the trend analysis of nominal and real effective exchange rate where the average growth of exports, for the period under study, was remarkably high with a contrastingly high nominal and real effective exchange rate before the mid-1980s (Appendix 1.6). For the rest of the countries, the real effective exchange rate is highly significant with the expected negative direction of relationship in explaining the real export demand, except in the cases of Korea and Thailand where the relationship is as expected but not significant. Similarly, Malaysia, Singapore and ROC-Taipei are the few countries in the region which have been successful in maintaining a more stable or appreciating exchange rate along with a robust growth in exports due mainly to the scale of economies involved, high-end technology used and macroeconomic stability for the period under study.

Only in the case of Nepal does the export-weighted real GDP of the major importing countries unexpectedly show a negative but statistically insignificant relation with the real export demand. In this case, if one judges from the size or volume of exports which is the lowest among the SEACEN countries, the fact that the level of trade partners' GDP has no influence on Nepalese exports seems quite reasonable. In other words, Nepalese exports with a small volume can take advantage of the foreign markets. For the rest of the SEACEN countries, the export-weighted real GDP of importing countries explains positively and significantly the real export demand. In addition, the dummy variable, which is expected to capture the policy changes involving trade promotion during the period under study, is positive but insignificant in the cases of Indonesia and ROC-Taipei, while it shows that the effect of policy changes is rather negative but

insignificant in the cases of Korea and Sri Lanka followed by a significant negative relation in the case of Thailand. Therefore, the policy change reflects the failure to account for the positive and significant impact on exports. Similarly, based on the trend stationarity of the data, the trend variable is significant only in the case of Thailand indicating that, other things being equal, the demand for exports increases significantly over the time period. In sum, with the exception of a few cases, the SEACEN countries should give due consideration for their real effective exchange rates and the export-weighted GDP of the importing countries in formulating and implementing export strategies.

A common goal among the SEACEN countries is to promote exports. The evidence shows that the development of exports in the SEACEN countries is fast growing through the expansion of non-traditional exports. This growth in exports is equally supported by the growth in imports as most of the exportable products of the SEACEN countries have a high import content. Nonetheless, the SEACEN countries have been heading towards the outward-oriented strategy. In other words, almost all the SEACEN countries have introduced various fiscal incentives as a compensation to the anti-export bias. Some of the SEACEN countries such as Korea, Singapore and ROC-Taipei experimented with various policy measures as early as the 1960s or so. Now they are placing emphasis on the comparative advantage of their products. In this context, Singapore has focused more on the chemical and electronic products as well as on trade in services. Korea has recently experienced a declining competitiveness for its traditional manufacturing industries whereas the competitiveness is very high in the case of the emerging industries. On the other hand, capital-intensive heavy industrialization is being worked out in ROC-Taipei where the labor-intensive light industries are facing the problem of own brand names as well as labor scarcity and international financing to compete in the world markets.

Malaysia and Thailand have also started the promotional strategy since 1970s. Comparatively, Malaysia has been successful in maintaining macroeconomic stability as well as adequate infrastructural network and is now heading towards the high-technology heavy industries. But in Thailand, in spite of the promotional policies, the infrastructural bottlenecks including the institutional support and government agency services remain the major impediments to a more rapid expansion of exports. Indonesia and the Philippines virtually reformed their export promotion policies in the 1980s. Priority has been

given to the non-traditional products but very recently they have deregulated their financial sector, including the institutional support in marketing and new industrial facility, which may take some time to develop adequate network of manufactured exports as expected. Nepal and Sri Lanka have also been pursuing the promotion of manufactured export since the late 1970's. However, the low level of industrialization, high domestic inflation, lack of full-fledged institutional set-up and low value-added with high import-content are suppressing the manufactured exports.

Evidently, there are different problems and limitations among the SEACEN countries, although the SEACEN countries have experimented with various measures to promote exports through: (i) fiscal incentives such as tax and duty concession, tariff and non-tariff measures; (ii) financial facilities such as credit, refinance, insurance and other related measures; and, (iii) institutional support such as central bank, commercial banks, export-import bank, specialized institution for marketing information, trade fairs and missions. Similarly, there is a strong support among the SEACEN countries that backward integration, FTZs, one-window system, etc., could contribute a lot for improving potential exports. The implementation of all these export development policies has not yet materialized fully in the cases of Indonesia, Nepal, the Philippines and Sri Lanka, though they are also actively working to stimulate exports.

With the exception of Singapore, most of the SEACEN countries are trying to make a balanced development of export and import though the emphasis on the latter one is on a fairly declining trend. Finally, the SEACEN countries, whether more successful or not, tend to further the scope for financing scheme, rescheduling comparative advantage, diversifying their exports in view of the emergence of regional trading blocks, etc., but not at the cost of efficiency to the whole economy. It is also important to note that foreign investment in the region has played a significant role in the promotion of exports. For this, almost all the SEACEN countries have re-embarked on the liberalization exercise keeping an attractive corridor open for foreign investment.

REFERENCES

1. Akaike, H. (1969), *Statistical Predictor Identification*, ***Annuals of the Intitute of Statistical Mathematics***, 21, 203-217.

2. Alam, M.S. (1991), *Trade Orientation and Macroeconomic Performance in LDCs: An Empirical Study*, ***Economic Development and Cultural Change***, 840-848.

3. Anjaria, J., et.al. (1985), *Trade Policy Issues and Developments*, ***IMF Occasional Paper***, No. 38, IMF.

4. Ariff, M., and T.E. Chye (1992), *ASEAN-Pacific Trade Relations*, ***ASEAN Economic Bulletin***, Vol. 8, No. 3, 258-283.

5. Asian Development Bank (1990), ***Foreign Trade Barriers and Export Growth***, Economics and Development Resource Center.

6. _____ (1990), ***Export Finance: Some Asian Examples***.

7. _____, ***Key Indicators of Developing Asian and Pacific Countries***, various issues.

8. Balassa, Bela (1978), *Export Incentives and Export Performance in Developing Countries: A Comparative Analysis*, ***World Bank Reprint Series***, No. 59.

9. _____ (1985), *Exports, Policy Choices and Economic Growth in Developing Countries After the 1973 Oil Shock*, ***Journal of Development Economics***, 18, 23-35.

10. Bond, M.E. (1987), *An Econometric Study of Primary Commodity Exports from Developing Country Regions to the World*, ***IMF Staff Papers***, Vol. 34, No. 2, 191-227, IMF.

11. Campbell, J.Y., and P. Perron (1991), *Pitfalls and Opportunities: What Macroeconomists Should Know About Unit Roots*, ***Econometric Research Program***, Research Memorandum No. 360, Princeton, New Jersey.

12. Cooper, S.A. (1988), *Estimating New Zealand's Real Effective Exchange Rate*, ***Discussion Paper G88/7***, Reserve Bank of New Zealand.

13. Council for Economic Planning and Development (1992), ***Taiwan Statistical Data Book***, the Republic of China, Taipei.

14. Das, D.K. (1990), ***International Trade Policy: A Developing Country Perspective***, MacMillian Press Ltd.

15. de Vries, Barend A. (1979), *Export Promotion Policies*, ***World Bank Staff Working Paper***, No. 313, The World Bank.

16. Dicky, D.A., and W.A. Fuller (1979), *Distribution of the Estimators for Autoregressive Time Series With a Unit Root*, ***Journal of the American Statistical Association***, 84, 427-431.

17. _____, and S.G. Pantula (1988), *Determining the Order of Differencing in Autogressive Process*, ***Journal of Business and Economic Statistics***, 5, 456-461.

18. Dodaro, S. (1991), *Comparative Advantage, Trade and Growth: Export-Led Growth Revisited*, ***World Development***, Vol. 19, No. 9, 1153-1165.

19. Durand, Martine (1986), *Method of Calculating Effective Exchange Rates and Indicators of Competitiveness*, ***OECD Working Papers***, No. 29, OECD.

20. Engle, R.F., and C.W.J. Granger (1987), *Cointegration and Error Correction: Representation, Estimation and Testing*, ***Econometrica***, 55, 251-276.

21. Goncalves, R., and J. Richtering (1987), *Intercountry Comparison of Export Performance and Output Growth*, ***The Developing Economies***, XXV-1, 3-18.

22. Graboyes, R.F. (1991), *International Trade and Payments Data: An Introduction*, ***Economic Review***, Federal Reserve Bank of Richmond, 20-31.

23. Granger, C.W.J. (1969), *Investigating Causal Relations by Econometric Models and Cross Spectral Models*, ***Econometrica***, 37, 424-438.

24. _____ (1981), *Some Properties of Time Series Data and Their Use in Econometric Model Specification*, ***Journal of Econometrics***, 28, 121-130.

25. _____ (1983), *Cointegrated Variables and Error Correction Models*, ***Discussion Paper 83-13***, Department of Economics, University of California, San Diego.

26. _____ (1986), *Developments in the Study of Cointegrated Economic Variables*, ***Oxford Bulletin of Economics and Statistics***, 48, 3.

27. _____, and P. Newbold (1974), *Spurious Regression in Econometrics*, ***Journal of Econometrics***, 110-120.

28. Hiemenz, U. (1988), *Perspectives for ASEAN-EC Trade in Manufactures in the Late 1980s and Early 1990s*, ***Malaysian Journal of Economic Studies***, Vol. XXV, No. 1, 1-16.

29. Havrylyshyn , Oli, and Martin Wolf (1981), *Trade Among Developing Countries: Theory, Policy Issues and Principal Trends*, ***World Bank Staff Working Paper***, No. 479, The World Bank.

30. International Monetary Fund, ***International Financial Statistics***, various issues.

31. _____, ***Direction of Foreign Trade***, various issues.

32. Jung, W.S., and P.J. Marshall (1985), *Exports, Growth and Causality in Developing Countries*, ***Journal of Development Economics***, Vol. 18, No. 1, 1-12.

33. Keesing, Donal B. (1979), *Trade Policy for Developing Countries*, ***World Bank Staff Working Paper***, No. 353, The World Bank.

34. Kmenta, Jan (1986), ***Elements of Econometrics***, 2nd Edition, Mac Millan Publishing Company, New York.

35. Koch, E.B. (1984), *The Measurement of Effective Exchange Rates*, ***BIS Working Papers***, No. 10, Bank for International Settlements.

36. Krueger, A.D., et.al. (1983), ***Trade and Employment in Developing Countries: Synthesis and Conclusions***, University of Chicago.

37. Michaely, M. (1977), *Exports and Growth: An Empirical Investigation*, ***Journal of Development Economics***, 4, 49-53.

38. Moreno, R. (1989), *Exchange Rates and Trade Adjustment in Taiwan and Korea*, ***Economic Review***, Federal Reserve Bank of San Francisco, 30-48.

39. _____ (1990), *External Shocks and Adjustment in Four Asian Economies, 1978-87*, ***Economic Review***, Federal Reserve Bank of San Francisco, 27-41.

40. _____ (1991), *Explaining the U.S. Export Boom*, ***Economic Review***, Federal Reserve Bank of San Francisco, 39-52.

41. Morgan Guaranty Trust Company of New York (1978), ***Effective Exchange Rates: Nominal and Real in World Financial Markets***.

42. Nelson, C.R., and C.I. Plosser (1982), *Trends and Random Walks in Macroeconomic Time Series*, ***Journal of Monetary Economics***, 10, 139-162.

43. Nickell, Stephen (1985), *Error Correction, Partial Adjustment and All That: An Expository Note*, ***Oxford Bulletin of Economics and Statistics***, Oxford, Vol. 47, 119-129.

44. Ng, Boey Kui (1987), *Changing Trade Patterns in the SEACEN Countries*, ***SEACEN Staff Papers No. 22***, The SEACEN Research and Training Centre, Kuala Lumpur.

45. Oskooee, B.M., et.al. (1991), *Exports, Growth and Causality in LDCs: A Re-Examination*, ***The Journal of Development Economics***, Vol. 36, 405-415.

46. Phillips, P.C.B. (1987), *Time Series Regression With a Unit Root*, ***Econometrica***, Vol. 55, No. 2, 277-301.

47. Pindyck, R.S., and D.L. Rubinfeld (1991), ***Econometric Models and Economic Forecasts***, Third Edition, McGraw-Hill International.

48. Powell, A. (1991), *Commodity and Developing Country Terms of Trade: What Does the Long Run Show?*, ***The Economic Journal***, 101, 1485-1496.

49. Rhee, Y.W. (1984), *A Framework for Export Policy and Administration: Lessons from the East Asian Experience*, ***World Bank, Industry and Finance Series***, Vol. 10.

50. Rhomberg, R.R. (1976), *Indices of Effective Exchange Rates*, ***IMF Staff Papers***, Vol. 23, IMF.

51. Roy, D.K. (1991), *Determinants of Export Performance of Bangladesh*, ***The Bangladesh Development Studies***, Vol. XIX, No. 4, 27-48.

52. Schwarz, G. (1978), *Estimating the Dimension of a Model*, ***Annual of Statistics***, 6, 461-464.

53. The SEACEN Research and Training Centre (1987), ***SEACEN Seminar Report on Export Credit Refinancing and Insurance Schemes in the SEACEN Countries***, Kuala Lumpur.

54. Tamaschke, R. (1988), *Trade Growth and Policy Formulation in a Small Open Economy: Conceptual Framework and Statistical Analysis of Recent Australian Experience*, ***Malaysian Journal of Economic Studies***, Vol. XXV, No. 1, 73-89.

55. Tyler, W.G. (1981), *Growth and Export Expansion in Developing Countries: Some Empirical Evidence*, ***Journal of Development Economics***, 9, 121-130.

56. Vinod, Thomas, John Nash and Associates (1991), *Best Practices in Trade Policy Reform*, ***World Bank Publication***, Oxford University Press.

57. Weerasekera, Y.M.W.B. (1992), *Nominal and Real Effective Exchange Rates for the SEACEN Countries*, ***SEACEN Staff Paper No. 42***, The SEACEN Research and Training Centre, Kuala Lumpur.

58. Westphal, L.E. (1978), *The Republic of Korea's Experience with Export-Led Industrial Development*, ***World Development***, Vol. 6, No. 3, 347-382.

59. Winters, L.A. (1981), ***An Econometric Model of the Export Sector: U.K. Visible Exports and Their Prices, 1955-1973***, Cambridge University Press.

60. Wong, J.K. (1993), *Testing and Estimating Cointegrating Relation ships: A Survey*, ***Discussion Paper G93/1***, Reserve Bank of New Zealand.

61. World Bank (1987), ***World Development Report***, Oxford University Press.

62. Yeats, A.J. (1989), *Developing Countries' Exports of Manufactures: Past and Future Implications of Shifting Patterns of Comparative Advantage*, ***The Developing Economies***, XXVII-2, 109-145.

Appendix 1.1

SEACEN COUNTRIES: SELECTED ECONOMIC INDICATORS

Country	Export as % of GDP				Export/Import as % of GDP				Manuf. Export as % of Total Exports			Average Annual Export Growth (%)				Average Annual Import Growth (%)			
	1960	1970	1980	1991	1960	1970	1980	1991	1970	1980	1991	1970-1980	1981-1985	1986-1991	1970-1991	1970-1980	1981-1985	1986-1991	1970-1991
Indonesia		12.5	30.8	37.2	117.6	110.6	112.1	125.3	1.4	1.9	39.0	33.9	-2.7	18.6	16.5	33.9	-3.5	13.3	18.2
Korea	0.9	9.4	28.0	25.4	10.8	42.9	78.5	88.2	76.0	85.9	88.1	35.6	9.3	15.7	23.6	27.4	4.5	21.2	19.4
Malaysia	47.9	43.6	52.8	73.2	119.8	120.4	120.1	93.7	11.9	22.4	64.9	18.5	8.8	21.8	14.9	18.5	3.4	29.3	16.2
Nepal	7.4	4.9	5.9	7.0	44.1	56.3	23.5	34.8	13.7	25.2	80.7	8.4	13.9	26.8	16.1	18.3	16.1	23.6	18.8
Philippines	8.5	16.2	17.8	19.5	95.2	97.0	75.0	73.0	6.8	34.5	72.4	18.5	-5.2	12.8	10.6	21.2	-10.5	18.9	11.9
Singapore	117.9	76.3	155.3	142.1	82.4	78.0	94.5	106.1	28.0	37.8	63.3	28.9	2.3	21.6	19.2	25.6	-1.4	21.1	16.9
Sri Lanka	26.9	15.4	27.9	24.3	99.4	87.2	51.3	65.5	1.7	36.3	64.6	11.9	5.3	10.3	8.8	18.0	2.3	8.9	10.3
ROC-Taipei	9.5	26.2	47.9	42.3	55.2	97.2	100.4	121.2	78.5	85.6	89.2	29.6	7.9	13.8	20.6	29.2	-1.3	21.1	19.4
Thailand	16.4	9.7	20.1	28.0 *	100.0	53.8	69.5	74.9	6.1	32.3	76.2	25.1	0.6	26.3	19.4	21.9	-1.5	32.2	17.5

* Refers to 1990.

Notes: Manufactured Exports refer to: (i) Basic Manufactures; (ii) Machine, Transport and Equipment; and, (iii) Miscellaneous Manufactured Goods.

Sources: Country Chapters.
International Financial Statistics (IFS), 1992, IMF.
Key Indicators of Developing Asian and Pacific Countries, various issues, ADB.

SEACEN COUNTRIES: EXPORT DESTINATION BY COUNTRY AND REGION

Country	Exports in	1965 (% Share of the Total)					Exports in	1970 (% Share of the Total)					Exports in	1980 (% Share of the Total)					Exports in	1985 (% Share of the Total)					Exports in	1991 (% Share of the Total)				
	US$ M.	USA	JAPAN	EEC	ASEAN + NIEs	OTH.	US$ M.	USA	JAPAN	EEC	ASEAN + NIEs	OTH.	US$ M.	USA	JAPAN	EEC	ASEAN + NIEs	OTH.	US$ M.	USA	JAPAN	EEC	ASEAN + NIEs	OTH.	US$ M.	USA	JAPAN	EEC	ASEAN + NIEs	OTH.
Indonesia	687	24.1	19.5	34.2	7.5	14.7	1173	12.5	38.9	13.3	17.9	17.4	22609	20.0	49.4	5.9	11.2	13.5	18527	21.7	35.4	6.2	18.0	18.7	29635	12.0	36.9	12.8	23.3	15.0
Korea	175	35.2	25.1	14.9	12.1	12.7	835	47.3	28.0	7.7	6.7	10.3	17505	26.3	17.4	15.5	12.4	28.4	30283	35.5	15.0	10.8	10.8	27.9	71870	25.9	17.3	13.6	18.9	24.3
Malaysia 1/	971	18.2	27.9	29.1	6.0	18.8	1676	13.0	18.3	19.4	29.9	19.4	12941	16.4	22.8	16.9	28.0	15.9	15317	12.9	24.4	14.5	35.3	12.9	34363	16.9	15.7	14.8	39.8	12.8
Nepal 2/	23	1.3	0.9	4.4		93.4	42	2.0	1.0	20.3	1.9	74.8	135	2.4	1.4	14.0	3.2	79.0	153	35.3	0.7	20.4	1.4	42.2	256	23.7	0.6	55.4	2.9	17.4
Philippines	767	45.5	28.2	19.8	3.3	3.4	1062	41.4	39.6	7.2	7.1	4.7	5788	27.4	26.5	17.5	15.1	13.5	4629	35.7	18.9	14.0	18.9	12.5	8840	35.6	19.9	18.6	16.4	9.5
Singapore 1/	236	6.5	18.8	20.5	26.0	28.2	502	13.2	14.0	13.9	31.6	27.3	10852	16.8	12.4	14.3	32.3	24.2	13508	27.5	13.0	11.4	29.1	19.0	36479	26.1	9.6	16.5	33.0	14.8
Sri Lanka	410	7.5	2.0	36.1	0.7	46.3	341	7.1	3.3	32.8	1.1	55.7	1052	11.1	3.2	20.6	4.9	60.2	1290	22.0	5.1	19.0	7.3	46.6	1988	28.1	5.1	33.9	7.9	25.0
ROC-Taipei 3/	450	21.3	30.6	7.5	14.7	25.9	2060	41.7	11.9	9.9	16.4	20.1	22611	36.1	11.0	12.8	16.3	23.8	30726	48.1	11.3	9.8	14.5	16.3	76178	29.3	12.1	18.4	25.7	14.5
Thailand	623	6.5	18.6	19.9	32.6	22.4	710	13.1	25.3	19.0	26.3	16.3	6504	12.6	15.1	26.0	23.6	22.7	7138	19.7	13.4	19.1	21.9	25.9	28546	21.3	18.1	20.7	19.8	20.1
SEACEN TOTAL:	3268	18.5	19.1	20.7	11.4	30.3	8401	21.3	20.0	15.9	15.4	27.4	99997	18.8	17.7	15.9	16.3	31.3	99997	28.7	15.2	13.9	17.5	24.7	99997	24.3	15.0	22.7	20.9	17.1

1/ Refers to 1966.
2/ Exports to India included in 'Others' item.
3/ Refers to 1971 and 1981 respectively.

Sources: Country Chapters.
Direction of Trade Statistics, various issues, IMF.

LAG LENGTH TEST FOR CAUSALITY TEST

Country	Lags	RGDPG/REXG		REXG/RGDPG		RGDPLXG/REXG		REXG/RGDPLXG	
		FPE	SC	FPE	SC	FPE	SC	FPE	SC
Indonesia	1	10.0921	2.4588 *	329.7950 *	5.9456 *	48.1728 *	4.0219 *	364.3490 *	6.0452 *
	2	11.0779	2.5974	390.6040	6.1601	55.3290	4.2057	413.7910	6.2178
	3	9.9167 *	2.5266	453.5140	6.3494	55.9509	4.2568	461.6130	6.3671
	4	11.7462	2.7259	543.6350	6.5606	64.1061	4.4229	562.2920	6.5944
	5	14.7227	2.9641	636.7850	6.7312	81.4475	4.6747	637.7870	6.7327
Korea	1	18.1757 *	3.1324 *	253.5510	5.6759	28.6209 *	3.5865 *	259.6410	5.7064
	2	20.5296	3.2922	221.8950 *	5.5845 *	31.8682	3.7319	212.7830	5.5527
	3	21.8373	3.3867	246.0570	5.7254	36.0171	3.8871	65.9492 *	4.4212 *
	4	26.4708	3.5877	267.7700	5.8414	44.3891	4.1046	81.2569	4.6599
	5	33.3281	3.7930	264.7210	5.8534	51.2103	4.2226	102.6550	4.9061
Malaysia	1	11.8040 *	2.6155 *	100.5530 *	4.7578 *	133.9490 *	5.0445 *	84.4127 *	4.5828 *
	2	13.3350	2.7832	119.9420	4.9794	148.3270	5.1919	98.6682	4.7842
	3	14.3808	2.8982	139.6390	5.1714	157.0120	5.2887	119.3060	5.0140
	4	17.7545	3.1390	137.6070	5.1868	159.5670	5.3348	98.3952	4.8514
	5	17.2676	3.1236	168.2090	5.3999	174.1360	5.4346	123.1950	5.0885
Nepal	1	12.6988 *	2.6777 *	1014.420 *	7.0977 *	10.9069 *	2.5255 *	923.473 *	6.9643 *
	2	13.3711	2.7687	1132.870	7.2421	11.7353	2.6382	986.343	7.0696
	3	14.4119	2.8776	1319.310	7.4208	13.4594	2.8092	1136.920	7.2456
	4	15.2829	2.9627	1538.460	7.5907	15.3339	2.9659	1310.880	7.4144
	5	17.8692	3.1352	1661.610	7.6703	18.0386	3.1447	1405.720	7.5005
Philippines	1	16.0787 *	3.9246	145.4760 *	5.1271 *	19.0686	3.0951 *	145.5950 *	5.1279 *
	2	16.6504	3.0049 *	159.8060	5.2664	18.9596 *	3.1348	160.3390	5.2697
	3	17.5658	3.0983	184.0960	5.4478	20.2776	3.2419	184.5030	5.4500
	4	19.5945	3.2376	151.3230	5.2818	25.2016	3.4893	152.2510	5.2879
	5	16.5050	3.0784	190.7450	5.5257	23.7917	3.4441	191.9870	5.5322
Singapore	1	11.0259	2.5473	234.2270	5.6487	467.5220 *	6.2945 *	319.4200	5.9136
	2	9.1706	2.4084	249.8400	5.7567	553.8050	6.5093	316.7880	5.9475
	3	9.4338	2.4766	175.1850	5.4362	581.3980	6.5978	256.5790 *	5.7798 *
	4	5.2627	1.9230	139.8120	5.2314	693.9630	6.8048	295.1670	5.9499
	5	5.1058 *	1.9051 *	112.7160 *	5.0126 *	861.0000	7.0328	354.6840	6.1459
Sri Lanka	1	0.0033 *	-5.5209 *	0.0066	-4.8667	54.1301 *	4.1838 *	0.0066	-4.8755
	2	0.0037	-5.3719	0.0060 *	-4.9221 *	60.4778	4.3381	0.0059 *	-4.9256 *
	3	0.0043	-5.1844	0.0072	-4.6989	73.2661	4.5644	0.0072	-4.7036
	4	0.0049	-5.0328	0.0063	-4.8032	87.9019	4.7674	0.0063	-4.8057
	5	0.0063	-4.7733	0.0072	-4.6645	110.1970	4.9899	0.0072	-4.6639
ROC-Taipei	1	15.9897	2.9190	170.6190	5.4018	11.8960	2.6233	186.9050 *	5.3776 *
	2	16.6239	3.0033	151.3560 *	5.3108 *	13.8993	2.8243	207.7200	5.5286
	3	16.4011	3.0297	174.2680	5.4722	16.7369	3.0499	222.0450	5.6352
	4	13.1088 *	2.8356 *	200.0130	5.6196	16.8611	3.0874	244.8810	5.7631
	5	16.5148	3.0790	153.5270	5.3204	10.1747 *	2.5946 *	251.5950	5.8026
Thailand	1	7.8654 *	2.2096 *	162.3330	5.2367	11.8857	2.6224	127.2010	5.0781
	2	7.9112	2.2607	169.5930	5.3258	9.5249 *	2.4464 *	118.0740 *	5.0416 *
	3	8.6536	2.3903	146.9910 *	5.2227 *	9.7541	2.5100	133.1030	5.1942
	4	8.0349	2.3462	169.2720	5.3939	10.2761	2.5922	136.1470	5.2254
	5	8.3678	2.3991	200.7580	5.5768	10.0378	2.5811	159.4740	5.3585

Notes: A/B = Lag length of A on the given lag length of B; * = Least values.

SEACEN COUNTRIES: TOTAL EXPORTS AND SHARE OF EXPORT PARTNERS
(Base Year 1985)

	INDONESIA	KOREA	MALAYSIA	NEPAL	PHILIPPINES	SINGAPORE	SRI LANKA	ROC-TAIPEI	THAILAND
Total Exports (in Mn. US$)	18527	26442	15317	161	4629	21534	1316	30726	7078
% Share of Top 15 Export Partners	92.84	81.33	88.03	83.03	85.73	79.85	60.02	88.00	76.77
USA	21.61	35.10	12.87	29.77	35.73	22.43	21.86	48.00	19.82
Japan	46.39	15.00	24.39	0.57	18.90	9.97	5.07	11.00	13.46
Australia	0.80	1.22	1.71	0.08	1.73	3.46	1.23	2.00	1.75
Germany	1.38	3.23	2.64	8.93	3.78	2.38	5.42	3.00	3.77
United Kingdom	1.03	3.02	2.58	6.83	3.61	2.91	6.40	2.00	2.46
Netherlands	2.12	1.14	5.86	0.11	-	1.35	3.43	-	7.18
Italy	0.82	-	-	-	0.63	-	1.14	1.00	1.70
Singapore	8.78	1.62	19.35	1.28	5.40	-	3.39	3.00	8.01
Hong Kong	1.88	5.17	1.35	-	4.04	6.75	0.82	8.00	4.07
China	0.45	-	1.05	1.25	-	1.55	-	-	3.84
Malaysia	0.42	1.48	-	-	3.76	16.43	0.91	1.00	5.03
Thailand	0.44	-	3.41	-	1.90	4.41	-	1.00	-
Korea	3.54	-	5.91	-	1.56	1.30	-	1.00	1.86
ROC-Taipei	1.91	-	2.26	-	1.86	1.81	-	-	1.64
Philippines	1.07	-	2.40	-	-	-	-	1.00	-
Canada	-	4.06	-	0.46	1.60	-	1.26	3.00	-
Panama	-	2.46	-	-	-	-	-	-	-
Norway	-	1.60	-	-	-	-	-	-	-
Saudi Arabia	-	3.20	-	-	0.84	1.24	3.69	2.00	2.29
Liberia	-	1.49	-	-	-	-	-	-	-
India	-	1.54	2.82	27.99	-	2.25	-	-	-
Indonesia	-	-	0.43	-	0.39	1.61	-	1.00	-
France	-	-	-	1.08	-	-	1.91	-	1.88
Spain	-	-	-	0.09	-	-	-	-	-
Switzerland	-	-	-	0.97	-	-	-	-	-
Pakistan	-	-	-	1.13	-	-	2.14	-	-
Sri Lanka	-	-	-	2.49	-	-	-	-	-
Iran	-	-	-	-	-	-	1.25	-	-

Note: In the case of Sri Lanka, the coverage is little bit low mainly because the time series data of her export trade partners such as USSR, Iraq and United Arab Republic are not available.

Sources: Country Chapters.

International Financial Statistics, IMF, Yearbook 1992.

Taiwan Statistical Data Book, Council for Economic Planning and Development, Republic of China, 1992.

SELECTED SEACEN COUNTRIES: ERROR CORRECTION EQUATIONS
Demand for Exports

Country	Dependent Variable	Constant	Lagged Dependent Variable	Δ LREER Lagged Once	Δ LTWGDP Lagged Once	Error Correction Term	DV	$\bar{R}^2$	Durbin *m*-TEST	F-Value	S.E. (%)
Nepal	Δ LREX	-0.0168 (-0.1154)	-0.6228 (-0.0156)	0.3259 (0.2296)	2.2786 (0.5729)	-0.7283 (-1.2773)	-	0.03	0.5305 (0.5960)	1.1460 (0.3740)	26.83
Philippines	Δ LREX	0.0717 (1.2949)	0.3102 (1.0641)	-0.0768 (0.2873)	-0.6740 (-0.5258)	-0.6587 (-2.1355) **	-	0.04	-0.7036 (0.4820)	1.2001 (0.3510)	9.68
Sri Lanka	Δ LREX	0.0929 (1.7465) *	-0.0414 (-0.1474)	0.0327 (0.2444)	-1.6289 (-1.6387)	-0.6918 (-1.8088) *	-0.2501 (-0.0629)	0.23	-0.4764 (0.6340)	2.1566 (0.1180)	7.48
ROC-Taipei	Δ LREX	0.3144 (7.1381) ***	-0.4478 (-1.7078)	-1.1609 (-4.8416) ***	-1.8199 (-1.7288) *	0.5100 (1.5052)	-0.0936 (-2.8734) **	0.61	0.4349 (0.6640)	6.9855 (0.0020)	6.43

*** Significant at 1-percent level.
** Significant at 5-percent level.
* Significant at 10-percent level.

Figures in parentheses below the Durbin *m*-Test and F-Value denote the significance level.

SEACEN COUNTRIES: NOMINAL AND REAL EFFECTIVE EXCHANGE RATES (NEER AND REER)
(1985=100)

	Indonesia		Korea		Malaysia		Nepal		Philippines		Singapore		Sri Lanka		ROC-Taipei		Thailand	
	NEER	REER	NEER	REER	NEER	REER	NEER	REER	NEER	REER	NEER	REER	NEER	REER	NEER	REER	NEER	REER
1970	360.83	135.31	289.97	129.98	83.35	110.99	139.80	130.72	329.84	95.02	70.88	87.01	380.92	319.18	96.68	88.28	134.73	115.78
1971	329.96	121.51	256.35	124.81	84.71	108.83	138.65	121.87	298.61	100.29	70.44	84.62	381.67	312.81	96.84	86.89	133.29	110.11
1972	287.52	107.91	216.45	112.63	85.97	108.59	138.30	125.26	274.97	95.76	72.81	85.49	359.08	296.81	92.97	82.38	125.21	103.76
1973	265.99	117.70	203.53	100.12	91.19	112.58	130.97	119.75	257.16	95.00	77.44	104.46	333.19	271.94	93.45	81.87	116.29	100.95
1974	275.61	143.92	202.29	107.86	94.29	113.91	132.52	124.15	259.78	110.40	78.54	111.42	320.85	256.14	94.73	107.12	118.71	110.91
1975	278.69	157.03	169.33	102.18	95.30	109.99	127.94	118.51	244.61	101.10	81.04	108.53	306.84	231.29	95.21	103.20	117.76	105.82
1976	281.64	176.95	171.35	111.11	92.14	103.23	118.44	104.68	242.37	102.31	79.95	99.16	268.15	186.70	96.10	99.74	121.26	106.05
1977	266.98	173.60	167.82	112.08	91.74	100.79	116.82	105.87	237.70	103.02	79.11	94.79	250.92	162.28	94.84	98.34	117.59	103.68
1978	218.63	145.65	158.34	114.05	88.02	95.90	116.25	107.42	222.25	97.46	80.05	94.59	139.12	91.62	93.56	96.12	107.14	96.49
1979	156.93	113.66	158.60	124.52	92.55	97.44	114.48	100.89	222.08	105.20	82.45	93.98	135.96	91.00	97.11	99.76	106.14	97.93
1980	159.53	123.27	126.38	114.68	94.49	95.21	112.53	101.38	219.56	110.04	84.03	93.24	127.71	96.59	97.50	106.01	106.17	106.03
1981	159.27	127.99	115.61	116.87	92.29	93.48	118.28	106.74	213.34	110.66	89.47	97.72	118.01	95.28	97.45	112.13	105.82	109.30
1982	164.22	138.38	112.68	115.15	97.18	99.25	117.12	110.41	207.48	112.16	92.99	99.39	116.01	97.15	95.36	106.14	106.70	109.91
1983	118.25	108.52	107.92	110.03	99.22	101.93	110.94	110.28	161.30	92.74	97.06	100.59	107.15	97.81	95.49	103.47	109.44	113.02
1984	106.57	104.47	106.44	106.89	102.21	104.86	106.16	102.46	109.33	91.22	99.12	101.37	104.09	106.03	98.86	102.38	111.00	111.54
1985	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00
1986	71.73	75.21	90.75	91.64	84.86	84.52	82.38	94.01	82.95	82.32	95.39	92.19	88.25	93.47	99.79	98.57	92.81	93.15
1987	50.84	57.37	92.79	93.84	80.47	78.95	78.34	94.15	77.71	78.09	94.19	89.07	79.20	87.38	115.08	110.65	88.55	89.19
1988	46.03	54.88	101.22	106.05	73.03	71.36	74.49	91.98	72.71	77.01	96.97	89.57	71.69	86.38	124.58	116.81	86.81	87.65
1989	45.33	55.59	112.61	119.39	72.13	69.72	68.68	87.41	71.92	81.93	102.51	92.49	65.96	83.98	136.45	127.26	87.42	89.06
1990	44.16	55.82	96.86	106.23	71.70	67.89	63.89	82.29	64.07	79.44	110.51	98.34	57.51	83.87	133.73	122.66	86.40	89.41
1991	40.26	53.36	101.79	116.86	69.72	65.68	55.42	76.59	55.79	78.52	116.37	101.82	56.04	87.24	133.05	120.74	86.27	90.42

Appendix 1.7

SEACEN COUNTRIES : EXPORT-WEIGHTED REAL GDP INDEX OF EXPORT PARTNERS

	Indonesia	Korea	Malaysia	Nepal	Philippines	Singapore	Sri Lanka	ROC-Taipei	Thailand
1970	52.27	58.32	47.27	62.47	54.46	49.48	62.02	56.89	51.59
1971	54.98	61.05	50.29	64.31	57.11	52.05	64.96	59.41	54.53
1972	59.16	65.31	54.07	66.00	61.08	55.65	69.59	63.36	58.64
1973	63.79	69.70	58.64	69.27	65.64	60.25	74.49	67.79	63.28
1974	64.23	70.11	59.95	69.37	66.18	61.56	75.32	68.15	64.43
1975	65.60	70.60	61.69	71.47	66.87	62.41	75.90	68.53	65.43
1976	69.26	74.82	65.52	74.02	71.08	67.13	80.61	72.94	69.59
1977	72.95	78.35	69.41	77.89	74.85	71.25	83.89	76.78	73.35
1978	77.09	82.52	73.84	82.11	79.09	75.65	87.89	80.94	77.66
1979	81.21	85.78	77.91	82.49	82.92	79.84	90.90	84.57	81.93
1980	83.63	87.53	80.89	84.57	84.85	82.68	92.36	86.16	84.62
1981	86.74	90.02	84.60	87.33	87.69	86.10	94.45	88.83	87.58
1982	88.74	90.08	87.19	87.58	88.46	87.76	94.91	88.60	89.12
1983	92.34	92.81	91.66	91.93	92.08	91.71	97.62	91.85	92.64
1984	97.36	97.50	96.91	96.15	97.52	97.53	102.04	92.27	98.13
1985	100.93	100.46	99.54	100.05	100.46	100.00	104.71	100.00	100.93
1986	104.35	103.97	103.23	103.64	104.00	103.74	107.75	103.73	104.61
1987	109.69	108.14	109.53	107.61	109.09	109.41	111.44	108.56	109.89
1988	116.61	112.79	117.55	114.14	115.37	116.67	116.84	114.11	116.70
1989	122.15	116.27	124.32	118.78	120.19	122.52	120.86	117.94	121.93
1990	127.55	119.16	130.81	122.74	124.31	128.07	123.96	120.69	126.77
1991	131.72	120.70	135.79	125.39	126.89	131.84	124.98	121.83	129.76

Sources: Data computed from Country Chapters: *International Financial Statistics*, Yearbook 1992, IMF; *Direction of Foreign Trade*, various issues, IMF; *Key Indicators of Developing Asian and Pacific Countries*, various issues, ADB; *Taiwan Statistical Data Book*, Council for Economic Planning and Development, Republic of China, 1992.

SEACEN COUNTRIES : REAL GROSS DOMESTIC PRODUCT AND REAL EXPORTS

(1985=100)

	INDONESIA		KOREA		MALAYSIA		NEPAL		PHILIPPINES		SINGAPORE		SRI LANKA		ROC-TAIPEI**		THAILAND	
	GDP	Exports	GDP	Exports	GDP	Exports	GDP	Exports	GDP	Exports	GDP	Export*	GDP	Exports	GDP	Exports	GDP	Exports
	(Bn. Rupiah)		(Bn. Won)		(Mn. Ringgit)		(Mn. Rupees)		(Bn. Pesos)		(Mn. S$)		(Mn. Rupees)		(Bn. NT$)		(Bn. Baht)	
1970	35706	3084	24813	1617	28065	14751	28474	1383	338	38	12148	1925	104085	22503	729	154	401	44
1971	38208	3732	27113	1940	30054	14756	28134	1584	355	41	13668	2722	104021	21547	823	214	421	53
1972	41808	4393	28564	2874	32876	16180	29011	1773	372	41	15504	4002	107159	22041	933	261	438	67
1973	46537	5113	32432	4866	36722	17552	28872	1786	406	49	17291	5407	110936	24446	1052	315	481	62
1974	50089	5340	35117	6221	39777	14993	30701	1579	426	43	18389	5515	115320	21218	1065	301	502	66
1975	52583	5136	37621	7128	40096	15385	31148	2309	453	45	19140	4915	120732	25354	1117	301	526	68
1976	56206	6132	42471	9599	44732	19481	32519	2672	490	58	20571	6236	126089	26418	1272	452	576	95
1977	61128	6860	46749	11745	48200	19427	33500	1990	520	69	22166	7110	130907	22568	1402	487	633	108
1978	65921	7368	51289	13034	51408	22466	34975	2026	548	68	24071	8865	140604	24712	1592	606	699	115
1979	70045	10713	55182	13129	56214	24222	35804	2324	583	74	26313	10272	149150	26289	1722	645	736	125
1980	76965	10460	53989	14586	60398	23477	34973	1495	613	89	28863	10486	157642	26697	1848	719	711	130
1981	83066	11016	57615	17198	64591	22781	37891	2414	633	91	31636	11016	166384	28542	1962	775	820	145
1982	84932	9859	61821	18373	68429	25323	39323	1449	655	95	33808	10769	140189	30642	2032	817	853	162
1983	88493	14541	69101	21152	72706	31210	38152	1512	668	90	36576	13147	147141	28453	2203	968	915	148
1984	94656	18429	75606	24839	78349	38817	41846	2280	617	88	39615	16944	154644	32788	2437	1131	980	178
1985	96997	20695	80847	26363	77547	38017	44417	2915	571	86	38924	16735	162375	35083	2557	1200	1014	192
1986	102696	28004	90868	30326	78361	49053	46325	2525	591	102	39683	23406	169358	38196	2855	1508	1064	226
1987	113455	43459	101804	38122	82585	51983	48152	2496	620	109	43433	30786	171899	38490	3207	1753	1165	271
1988	113982	53045	113492	43050	89967	58787	51644	3087	659	122	48273	43571	176528	38976	3443	1783	1319	336
1989	122581	61699	120477	41423	97804	70650	53639	2753	698	138	52821	48191	180589	38933	3703	1846	1478	417
1990	311614	61594	131503	42818	107406	82109	55564	3641	715	149	57133	51943	191785	44358	3884	1901	1626	467
1991	141313	72024	142633	46662	118147	97924	57558	5029	708	181	60960	58023	200992	46698	4168	2117	1789	559

* Refers to non-oil domestic exports.

** Refers to base year 1986.

Sources: Country Chapters: *International Financial Statistics*, Yearbook 1992, IMF; *Key Indicators of Developing Asian and Pacific Countries*, various issues, ADB; *Taiwan Statistical Data Book*, Council for Economic Planning and Development, Republic of China, 1992.

SEACEN COUNTRIES: EXPORTS GROWTH AND SECTORAL SHARE OF GDP

	Indonesia	Korea	Malaysia	Nepal	Philippines	Singapore	Sri Lanka	ROC,Taipei	Thailand
Exports Growth									
1950-59	n.a.	9.36	n.a.	n.a.	3.78	n.a.	0.23	n.a.	0.58
1960-69	2.44	42.32	5.75	5.56	4.78	6.23	-1.34	23.69	7.15
1970-79	35.64	38.16	23.78	9.18	20.31	26.84	12.67	32.62	24.05
1980-89	5.89	15.97	9.31	6.48	6.26	13.37	5.12	15.73	15.23
1990-93	12.60	7.19	16.81	24.30	9.89	13.64	17.94	6.24	16.47
Overall Avg.	14.14	22.60	13.91	11.38	9.00	15.02	6.93	19.57	12.70
Industry as % of GDP									
1971-79	38.79	32.36	40.50	31.14	40.86	43.67	27.31	7.4	34.66
1980-89	36.11	45.39	46.14	37.74	41.02	42.64	26.76	8.05	38.39
1990-93	38.39	51.12	52.05	34.60	37.55	41.97	28.42	7.79	44.9
1971-92	37.76	42.96	46.23	34.16*	39.81	42.76	27.5	7.75	39.31
Manufacturing as % of GDP									
1971-79	7.78	21.88	20.5	n.a.	30.20	31.83	16.08	33.94	23.5
1980-89	14.43	32.76	25.96	n.a.	28.15	30.77	14.95	37.05	26.08
1990-93	19.32	36.51	33.84	n.a.	27.37	32.91	17.56	33.87	29.57
1971-92	13.84	30.38	26.77	n.a.	28.58	31.84	16.20	34.96	26.38

Note: Exports in US dollar values.
* Refers to non-agricultural sector.

Sources: *International Financial Statistics*, IMF, Yearbook, various issues.
World Tables, The World Bank, 1993.

PART II

COUNTRY CHAPTERS:

Indonesia
Korea
Malaysia
Nepal
Philippines
Singapore
Sri Lanka
Republic of China, Taipei
Thailand

Chapter 2

EXPORT PROMOTION STRATEGIES: INDONESIA

by
I Made Sudana and Andang Setyobudi

I. Introduction

Export activities are important in promoting the economic well-being of a nation. The arguments of specialization and comparative advantage notwithstanding, a nation has to generate sufficient export earnings to match its import requirements. In the medium- and long-run scenarios, the balance of payments position has to be maintained. In case of international payment deficits which are experienced by most of the developing countries, including Indonesia, capital transfer has to be tapped to finance such an imbalance. Such financing is only possible if foreign asset is available.

Before fiscal year 1987/1988, Indonesian exports relied heavily on oil/gas and traditional commodities. These commodities have very uncertain position in the world market. The prices of primary goods mostly fluctuate and usually move at the expense of exporting countries. At the same time, developing countries like Indonesia do need foreign exchange to finance imports comprising of capital goods and raw materials for the domestic industries.

Growth in the value of non-oil exports, comprising mainly of primary products, fluctuated during the last two decades due to the changes in commodity prices. Most of the fluctuations in the growth of non-oil export, particularly during 1986-1988, were because of the fluctuations in commodity prices, i.e., the agricultural products which comprised a large share of non-oil exports until recently. Prior to 1980, agricultural products accounted for about 90 percent of non-oil exports whereas it fell drastically to 44 percent, lower than the level of manufactured exports in 1988.

A sharp decline in the average annual growth from 7.5 percent during 1973-1981 to 3.3 percent during 1981-1988, and an increase in current account and budgetary deficits, required Indonesia to adopt a comprehensive stabilization and adjustment program. The past strategy of financing the twin-deficits by foreign borrowings proved to be

untenable. The debt service ratio has become unacceptably high because of limited ability of the economy to generate the requisite export and fiscal surpluses.

To finance the required investment to reach the 5-percent targeted annual rate of growth in the Fifth Five-Year Plan, Indonesia supplements its growth-cum-debt strategy with exports particularly non-oil exports, to increase the mobilization of domestic savings, and to promote greater participation of foreign private investment. The mobilization of domestic savings through the banking system has been motivated by deregulation of the financial sector.

The banking deregulation of October 1988 permits new banks to open by simplifying the authorization procedures. Foreign banks are allowed to establish under joint-venture within a maximum share limit of 85 percent. The existing foreign banks are also allowed to open branches in six other large cities outside Jakarta which are considered to have economic potential for exports. With the provision of one year of operation, 50 percent of the portfolio credits of the joint-venture banks, and branch offices of foreign banks outside Jakarta has to be earmarked for export credits. Exports are defined to include processing, manufacturing, and sales activities for all commodities that generate export value-added. This definition, therefore, encompasses the activities of indirect as well as direct exporters.

This export policy has played a dual role of: (ii) encouraging industrial efficiency by exploiting the externality of exporting and competing in world markets; and, (ii) laying the groundwork for the domestic producers and exporters on an equal footing with foreign competitors, and thereby, preventing the development of inefficient import substitution.

II. Export Trade and Salient Features

2.1 Trade and Commerce Policy Environment

Over the last five years, Indonesia has been quite successful in shifting its trade policy regime from the use of quantitative restrictions to the use of tariffs. The Indonesian Government has adopted this policy to enhance the efficiency and productivity of various business sectors as well as to improve the distribution of goods and services. The newly

introduced measures are related to: (i) the reduction of import duties and the surcharges on import duties; and, (ii) the simplification of trade licensing procedures.

Tariffs are now the main trade policy instruments. Existing quotas are continually being replaced with tariffs - generally termed surcharges, which are temporary in nature. Surcharges are designed to alleviate the adjustment burden on some industries following the removal of quantitative restrictions. Being temporary, the removal of surcharges will in future enable a gradual reduction in the overall level of tariff protection. Indonesia has GATT-bound some of its tariffs, and is actively considering binding additional tariff rates.

Import duties are applied on the c.i.f. value of imported goods. All import duties are now applied on an ad-valorem basis. Import values are determined by an independent surveyor assigned by the Government for all transactions greater than US$ 5000. The invoice price is used for transactions less than those amount. Furthermore, Indonesia has signed the GATT code on Subsidies and Countervailing Duties in 1985. Since Indonesia has replaced a system of export payments (the Export Certificate Program) with an import duty drawback and exemption scheme, this scheme allows Indonesian exporters to import their inputs at world prices. In the same year, Indonesia also replaced an ad-hoc and often protective import and domestic sales tax scheme with a trade-neutral value-added tax (VAT) system. Under the VAT, imported products are taxed at the same rate as similar domestic products, and the VAT is rebated for any product that is exported.

2.2 Contribution of Exports to the Economy

Indonesia's exports consists of two major commodity groups, i.e., oil/gas and non-oil/gas exports. Before 1987, Indonesia's exports was dominated by oil and gas exports which comprised more than half of the total exports. The Indonesian Government realised that overdependence on oil/gas export would not benefit the economy. Consequently, Indonesia has actively promoted non-oil/gas exports in the beginning of 1980s. The open door policy with a free flow of foreign exchange, coupled with a change in the export structure have partly aided Indonesia in evading the negative effects of commodity export prices, especially for oil and gas. It was evident that since 1987 non-oil/gas exports have exceeded those of oil/gas export. The

domination of agricultural products in non-oil/gas export has also been replaced by manufacture products.

In line with the fast growing non-oil/gas export revenue, the role of exports to the economy has been increasing as illustrated by the increasing trend in its exports to GDP ratio annually. The ratio of exports to GDP stood at 22.4 percent in 1975 has increased to 37.2 percent in 1991. It reflected mainly the good performance of non-oil exports.

The increase of non-oil exports has also brought about a growing need in imports of both capital goods and raw materials. This was mainly because part of the manufactured commodities for export have high import contents. It was indicated by the ratio of total export to total import ranging between 75.4 percent to 164.4 percent and on average was around 120 percent. The lowest ratio was recorded in 1983 while the highest was in 1979.

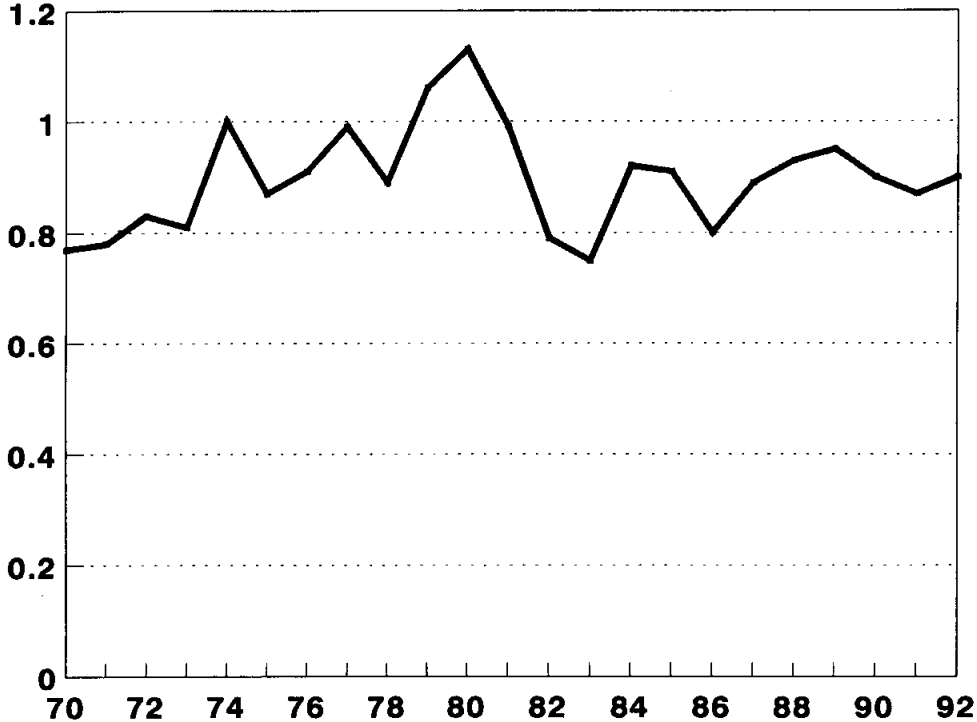
Even though Indonesia's export has performed remarkably during the last decade, the non-oil/gas current account deficit widen slightly but the foreign exchange reserves position strengthen to US$ 9.9 billions which is equivalent to five months of non-oil/gas imports. The improvement in the international reserve position was due to the increase in capital inflows in line with the conducive climate of investment condition.

The role of exports has increased significantly the rate of employment absorption due to the increasing role of manufacture in exports. The number of people employed in the industrial sector is growing significantly. In 1971, the share of labor force in the manufacturing sector was 6.84 percent while the agricultural sector was 66.27 percent. In 1991, agriculture's share decreased to 51.5 percent while that of manufacture increased to 11.4 percent. This development was in accordance with the government policy which has attempted to lower the role of agriculture and encourage the manufacturing sector.

2.3 Growth Trend and Changing Patterns of Exports

The growth of Indonesia's exports generally shows an upward trend, although it also experienced negative growth rate at times. Negative growth had occurred three times within the first-half of the 1980s. The biggest drop occurred in 1986 which posted a negative growth of 22.3

Chart 2.1: **EXPORT / IMPORT RATIO**
1970 - 1992



percent due to a sharp fall of world oil prices while the fastest growth stood at 44.3 percent in 1979. The average annual growth rate during the last 15 years was 12.4 percent.

As mentioned above, Indonesia's export can be generally divided into two commodity groups namely, oil/gas and non-oil/gas exports. The share of oil/gas export which stood at 73.5 percent in 1975, has increased to 81.2 percent in 1981. The growth rate of oil/gas export in 1980 was the highest (60 percent) and the oil price hike was attributable to this development. Thereafter, the growth rate declined steeply with the highest drop in 1986 (38.3 percent) and subsequently decreased to only 38.7 percent in 1991.

On the other hand, non-oil/gas export has become increasingly more important. Its value in 1975 was only US$ 1.817 million or 26.5 percent to total exports and this figure increased to US$ 18.180 million in 1991. From 1975 until 1991, its average growth rate was 17.3 percent with the largest growth rate of 35.2 percent in 1988 and a negative growth rate of 27.1 percent in 1981.

Within non-oil/gas export, manufacture products have shown an impressive development. It was US$ 40 million in 1975 and reached US$ 12.474 million in 1991, or the incremental rate was 49.3 percent per annum. With its rapid growth, its share has climbed from 2.2 percent in 1975 to 68.6 percent in 1991. Exports of manufacture goods, primarily textiles and textile products, rose by 40.4 percent to US$ 3667 million, to become the largest category of non-oil/gas exports in 1991 accounting for 20.2 percent of total non-oil/gas export. Wood products became Indonesia's second most important manufacture exports in 1991 with total value of US$ 3612 million or an increase of 9.9 percent from the previous year. In 1991, exports of mining products, including copper, nickel, tin and aluminium recorded US$ 1617 million, representing a 11.7-percent growth from the previous year.

Indonesia's principle export markets are Japan, European community (E.C.) and United States (U.S.). In 1991, total Indonesia's exports to Japan and EC mounted to US$ 10.767 million and US$ 3742 million or 37.0 percent and 13.0 percent respectively. And exports to the U.S. reached US$ 3509 million, accounting for 12.0 percent in total export. Oil/gas made up the majority of exports to Japan.

Indonesia's trade balance has always been in surplus. In 1991, its surplus amounted to US$ 4801 million as compared to US$ 5351 million in 1990. Non-oil/gas trade balance has been improving, showing a downward trend in its deficit. Meanwhile, its balance of services continued to experience a deficit, which has always been greater than the surplus in the trade balance. As a result, Indonesia's current account has always been in a deficit position following an uptrend movement.

The capital account shows that private capital inflow has been very dominant during the last two years. Total capital inflows, both Government and private sectors have always been positive and in 1991 it amounted to US$ 5829 million, of which the private sector accounted for 75.6 percent. This development led to a surplus in the overall balance of payments position amounting to US$ 1207 million in 1991.

2.4 Some Empirical Evidence

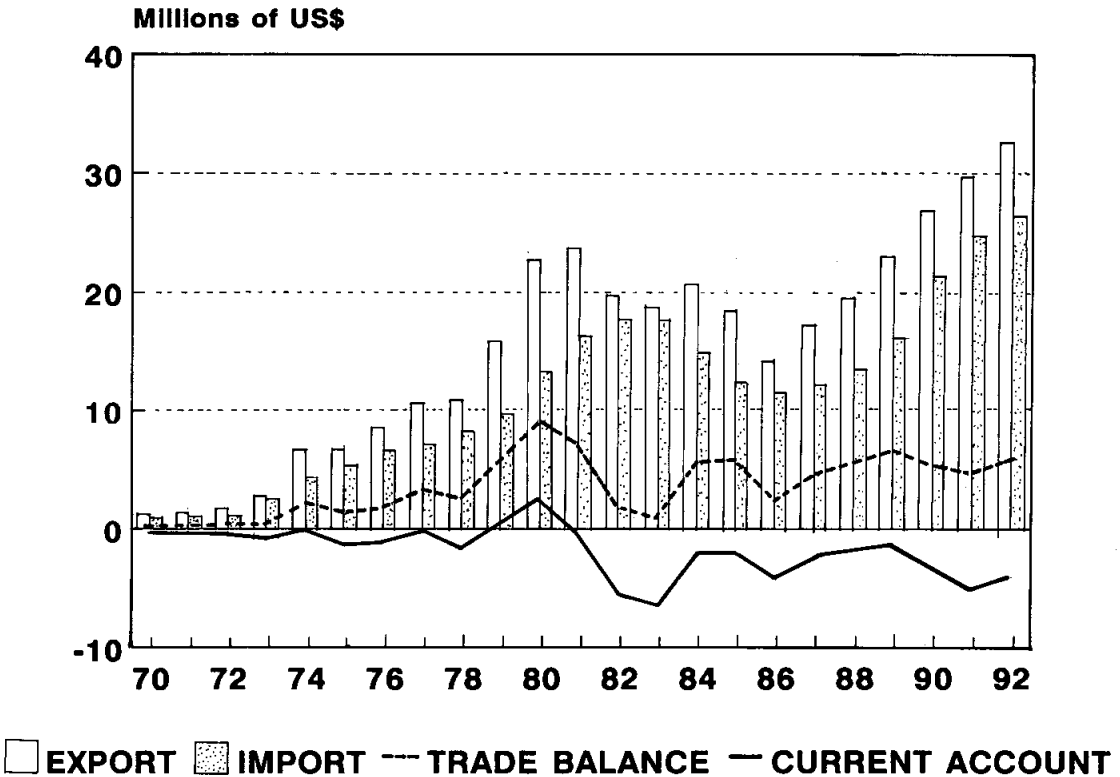
The causation between exports and economic growth has been introduced with the Granger (1969) causality test. This test helps to find out the relationship between exports (X) and economic growth (Y). This approach tries to describe whether X causes Y and to see how much the current Y can be explained by past values of Y, and then to see whether adding lagged values of X can improve the explanation. Y is said to be Granger caused by X if X helps in the production of Y, or equivalently if the coefficients on the lagged X's are statistically significant. It is important to note that the statement "X Granger Causes Y" does not imply that Y is the effect or the result of X. The null hypotheses being tested are that X is not Granger caused by Y, and Y is not Granger caused by X. If the null hypothesis is not rejected, then the conclusion is that there is no causality effect. If the null hypothesis is rejected, it implies that there exists causality condition.

The model developed by Granger is formulated as follows:

$$Y_t = a_0 + \sum_{i=1}^{M} a_i X_{t-i} + \sum_{j=1}^{N} b_j Y_{t-j} + \mu_t \qquad (1)$$

$$X_t = C_0 + \sum_{i=1}^{M} C_i Y_{t-i} + \sum_{j=1}^{N} d_j X_{t-j} + \mu_t \qquad (2)$$

Chart 2.2: **INDONESIA : TRADE BALANCE AND CURRENT ACCOUNT**
1970 - 1992



where, Y_t = Real GDP Growth, and
X_t = Real Export Growth.

The null hypotheses are: $\Sigma a_i = 0$, and $\Sigma c_i = 0$.

The direction of causality can be expressed as:

(a) unidirectional causality from x to y, if $\Sigma a_i \neq 0$, and $\Sigma c_i = 0$;

(b) unidirectional causality from y to x, if $\Sigma a_i = 0$, and $\Sigma c_i \neq 0$;

(c) feedback relationship between X and Y; $\Sigma a_i \neq 0$, and $\Sigma c_i \neq 0$; and,

(d) variables are independent, if $\Sigma a_i = 0$, and $\Sigma c_i = 0$.

2.4.1 Findings

Granger causality test for Indonesia's exports and GDP shows the following results:

Table 2.1
CAUSALITY TEST FOR INDONESIA'S EXPORTS AND GDP

Null Hypothesis	F-Statistics	Probability
D(exp) is not Granger-caused by D(GDPI)	1.288796	0.2730
D(GDPI) is not Granger-caused by D(exp)	18.69882	0.0005

According to the results, there is evidence of causal-relationship between GDP and Export with direction running from exports to economic growth. Having known this result, the Government should continuously pursue export-led growth strategy which is a suitable policy for encouraging economic development.

2.4.2 Export Demand

To investigate empirically the demand for exports, a simple long-run export demand model in log form is used:

$$\ln XD_t^* = \alpha + \beta \ln RXR_t + \delta \ln FRGDP_t + \mu \qquad (3)$$

where, XD^* = Desired or long-run demand for export,
RXR = Real effective exchange rate index, and
FRGDP = Export-weighted real domestic product of export trade partners.

The coefficient β and δ measure the long-run relative price elasticity and income elasticity, respectively, that is:

$$\ln XD_t - \ln XD_{t-1} = \tau (\ln XD_t^* - \ln XD_{t-1}) \qquad (4)$$

The parameter τ measures the spread of adjustment and $0<\tau\leq 1$.

where, $\ln XD_t - \ln XD$ = Actual change, and
$\ln XD_{t-1}^* - \ln XD_{t-1}$ = Desired change.

Substituting equation (3) into (4), the short-run demand for export function can be stated:

$$\ln XD_t = \alpha\tau + \beta\tau \ln RXR + \varepsilon\tau \ln FRGDP + (1-\tau)\ln XD_{t-1} + \tau U_t$$

Assuming, $\alpha\tau = a$, $\beta\tau = b$, $\varepsilon\tau = c$, $(1-\tau) = d$,

$$\ln XD_t = a + b \ln RXR_t + C\ FRGDP_t + d \ln XD_{t-1} + V$$

After estimating the short-run export demand function, we can simply divide each coefficient of this function by the value of adjusted coefficient, dropping the lagged dependent variable to obtain the long-run elasticity.

Note: RXR is calculated as follows:

$$RXR = \sum_{j-1}^{n} R_j^* W_t (P_i/P_j) \longrightarrow R_j^* = R_j.t/R_j.0;\ t = \text{period } ....$$

RXR = Real effective exchange rate,
$R_{j,t}$ = Rupiah exchange rate in period t,
$R_{j,0}$ = Rupiah exchange rate in base period,
W_j = Weight,
P_i = CPI, and
P_j = CPI of trade partners.

2.4.3 Methodology

(i) As formulated in the above equation, the export demand is a function of export competitiveness which is generally measured by the real effective exchange rate, income level of major export trade partners and lagged demand for export. The computation of the REER was done by using the arithmetic approach. Major trade partners consist of countries which account for around 70 percent of Indonesia exports.

(ii) The study utilized annual time-series data ranging from 1971 to 1991. Export data are in terms of FOB value and include oil/gas, non-oil/gas and services derived from balance of payments. The number of countries included as Indonesia's major trading partners consist of some countries which account for around 70 percent of total exports.

(iii) The computation of the REER was done by using the arithmetic approach. The calculation of REER is based on a basket of currencies weighted on a bilateral trade basis. It covers seven currencies of Indonesia's trading partners and 1986 was chosen as the base year.

(iv) Data on GDP of Indonesia's trading partners was obtained from IFS and data in foreign demand was obtained from Central Bureau of Statistics which is the export value to seven major destinations of Indonesia's exports. The share of export to each trading partner country used weights, and real domestic product of export trade partners is adjusted from fiscal year to calender year in line with the period of GDP.

(v) Export-weighted real domestic product of export trade partners was computed by converting all selected seven trade partners' GDP into dollar terms. Each GDP is then multiplied by the share of Indonesia's exports to the country concerned. The source of GDP data was cited from IFS while Indonesia's export to those countries was from Indonesia's BOP.

2.4.4 Estimation Results

The short-run export demand function without intercept show the following results:

$$\begin{array}{lll} \text{Ln Exp} = 0.2263\ \text{LnRXR} & +0.1277\ \text{LnFRGDP} & +0.7253\ \text{LnExp}_{t-1} \\ \quad (3.6819) & \quad (1.9752) & \quad (7.5855) \end{array}$$

$R^2 = 0.9307$
DW = 2.2299
F = 114.2076

After dividing each coefficient by the value of adjusted coefficient, we have the long-run export demand function as follows:

$$\text{Ln Exp} = 0.8238\ \text{LnRXR} + 0.4648\ \text{LnFRGDP}$$

Based on the results, the estimated income elasticity of trading partner has an expected positive sign with t-statistic significantly different from zero. While the real effective exchange rate (the price elasticity of demand) has unexpected positive sign and is significantly different from zero.

III. Export Promotion Policies

3.1 Monetary Policy Measures

Indonesian economy is a small open economy and therefore, is very sensitive to external fluctuations. In order to strengthen the external balance position and to encourage the competitiveness of Indonesian exports in the world market, it is necessary to have an appropriate macroeconomic policy framework which requires a well consistent coordinated domestic financial and exchange rate policies.

Exports are considered to be an important and strategic factor in Indonesian economic development. Owing to the world economic recession in the beginning of 1980s and the uncertainty of oil prices in the world market, the Government realized that the Indonesian economy would not be able to rely on the oil/gas export earnings in the future.

Exports financing institution is one of the important factors in facilitating and pushing up export transactions. In this case, the role of the banking sector cannot be ruled out. Indonesia has no special commercial bank which finances exports or import transactions. All limited liability (Pesero) banks - formerly state-owned commercial banks - and several national and private foreign exchange banks, as well as foreign and joint-venture banks are eligible for granting credits for those companies engaged in international transactions.

Recognizing the increasing needs of financial assistance to exporters in line with the government policy changes from inward-looking to outward-looking economy, Indonesia provided an incentive to boost non-oil/ gas exports through the banking system since 1982. Bank Indonesia provided export credit facility along with some other incentives, such as the small investment credit and the permanent working capital credit for small-scale entrepreneurs, credit for food stock in favor of the logistic body, and credit granted to the "Nucleus-Plasm Plantations", are given special treatment.

In March 1985, the Indonesian Government signed an agreement with the U.S. concerning the code on Subsidies and Countervailing Duties. Since then, the export credit facility was phased out gradually pursuant to this agreement. This export credit facility was completely abolished in 1990 and was replaced by a drawback system which was in effect since 1986. The Indonesian Government has stated that non-oil/gas exports should be a high priority concern of any government institution. Bank Indonesia, in its capacity as the monetary authority as well as bank supervisor has been supporting the government efforts in promoting non-oil/gas exports through the banking system. The measures adopted by the Central Bank is reflected in its banking, monetary and exchange rate policies.

The admission of foreign and joint-venture banks to open their offices in Jakarta and in six major provincial cities outside Jakarta as stipulated in the deregulation package of October 1988 was expected to push up the export growth. Foreign and joint-venture banks are required to allocate at least 50 percent of their credit portfolios to export activities. Furthermore, banks are now allowed to utilize off-shore borrowings to be channeled for credit, both in terms of foreign exchange and rupiah credits, with the requirement that at least 80 percent of offshore borrowings must be allocated for exports.

The mode of payment is also one of the main determining factors in encouraging export activities. Since the issuance of exports/imports and foreign exchange deregulation in January 1992, exporters have been given the freedom to choose the payment system for their exports as long as it is commonly practised in international transactions. Furthermore, through the deregulation package of May 1989, Bank Indonesia issued, among others, a measurement pertaining usance draft. Exporters are now allowed to freely set the maturity of their usance export drafts, compared to at most 180 days as required before. On the other hand, rediscount period of selling usance draft by the lending banks to the Central Bank was extended to 360 days since the shipment date (on board B/L).

3.2 Foreign Exchange System

Since 1970, just a few years after the new ruling government came to power, Indonesia adopted a free foreign exchange regime where private individuals or companies can acquire, hold, sell or buy foreign exchange without restrictions. The main purpose of implementing this free foreign exchange system was to create a conducive and better climate as well as to give an assurance to the private and foreign investors to conduct their business confidently in any economic sector.

With the government regulation announced in 1982, further deregulation in exports/imports and foreign exchange movements were enforced, whereby exporters were no longer required to sell their foreign exchange proceeds to foreign exchange banks and those banks were not required to sell such foreign exchange to the Central Bank. Private individuals and companies were free to hold, to sell and to buy foreign exchange and also free to borrow offshore loans. Capital transactions, including remittances of capital, profits, dividends are free from exchange controls. Direct investments made by foreign parties in new business undertakings or business expansions in Indonesia, however, require a prior approval by the Government. Prior approval by the Government is also required for a foreign loan with a maturity of one year or longer made to any public enterprises or public entity. All these measures were aimed at stimulating non-oil/exports in the short term in order to compensate the fall in oil/gas earnings and government revenues on account of a decline in world oil prices during that period.

A wide-ranging series of economic reform in the financial and banking sectors were introduced in October 1988. Among others, the

major change was the relaxation of certain requirement relating to the operation of foreign exchange banks. In addition, further measures were issued in February and November 1991 with the aim of strengthening the banking sector. In particular, the measures have included additional provisions regarding the net open position. The net open position is currently set at 20 percent of bank capital as a whole, and 25 percent of capital for respective foreign currencies held. Previously, foreign exchange transaction recorded as an off-balance sheet item was not subject to net open position measurement, but now it is also set at a maximum of 20-percent capital.

3.3 Exchange Rate Policy

Coordinated financial and exchange rate policies have played an important role in stimulating Indonesia's non-oil/gas exports, promoting adjustment to external shocks, and maintaining payment stability. Indonesia adopted a managed floating exchange rate system, following devaluation of the rupiah on November 15, 1978. This 1978 devaluation was not intended to forestall short-term balance of payment difficulties but rather, to improve the structure of the balance of payments over the medium- and long-term. The primary objective of the 1978 devaluation was to develop a more export-oriented economy through the expansion of non-oil/gas exports.

Since then, the rate of the rupiah was determined on the basis of trade-weighted basket of currencies. The currencies selected are based on Indonesia's major trading partner countries. This managed floating exchange rate was practically more managed rather than floating in which the magnitude of the adjustment was very little. For example, since the 1978 devaluation until the end of 1982, the rupiah was depreciated against the U.S. dollar by an average 2.7 percent per annum. As a result, the rupiah was overvalued compared to other currencies within the basket. Finally, this strong value of the rupiah weakened the competitiveness of Indonesia's products in the world market.

Such unfavorable circumstances brought about a further devaluation of the rupiah against the U.S. dollar on March 30, 1983. The magnitude of the devaluation from Rp. 703 to Rp. 970 per U.S. dollar was intended to make up for the loss in the real effective exchange rate accumulated since November 1978. This exchange rate adjustment was also intended to regain the loss of competitiveness of Indonesia's commodity prices

in the market. Another reason was to curb the foreign exchange speculation which was inducing large capital outflows.

On September 12, 1986, another devaluation occurred. The rupiah was devalued against the US dollar from Rp. 1134 to Rp. 1644. This measure was undertaken to overcome the potential problem of balance of payments. The figures on the current account deficits and projected balance of payments at that time justified the action. Current account deficit widened and was projected to reach about US$ 4.5 billions in 1986/1987. The worsening of this current account position was attributable to a rapid fall in world oil prices. The spot and contract prices for Indonesia's Minas crude oil dropped to US$ 11 per barrel in May 1986, which was far below the targeted price at US$ 25 per barrel for the state budget of fiscal year 1986/1987.

Since the 1986 devaluation measure, the Government has provided more room for gradual exchange rate adjustment to reflect market development so that the real effective exchange rate of the rupiah reflects the actual value of the rupiah relative to other currencies. The mechanism of the exchange rate determination was also changed. Before September 1989, Bank Indonesia determined the rupiah exchange rate in the morning and that rate was used in the market. It was recognized that such a rate did not fully reflect the latest development in the market. To accommodate these developments into the system, Bank Indonesia issued the rupiah exchange rate twice a day. The morning rupiah exchange rate was used as an indicative rate by the market participants. The other prevailing rate was influenced by the market forces. Bank Indonesia whenever necessary, could intervene in the market to smoothen the exchange rate movements. The management of the rupiah exchange rate was performed by taking into account both domestic and international market developments. For other major currencies, the exchange rates of the currencies to the U.S. dollar that prevail in the international market were used.

3.4 Financial Market Development

The financial sector in Indonesia had undergone an extensive structural reform since June 1, 1983 which principally constituted an abolishment of credit ceilings and the removal of interest rate controls. This was followed by the deregulation package in October 27, 1988. Subsequently, financial reform was formulated to promote public funds

mobilization, non-oil exports, efficiency in the financial and banking sector, effectiveness of monetary policy management, and stock-market development. Maintaining growth and development in the private sector and the economy at large requires a complementary financial system capable of providing indispensable financial services and resources.

To promote non-oil/gas exports, the Government has permitted new entry for the establishment of joint-venture banks between domestic banks and foreign banks. Furthermore, foreign banks and joint venture banks are now allowed to build their branch offices in six major provincial cities out side Jakarta. The Government also relaxed the requirements for foreign exchange banks. The increase in foreign exchange bank offices would provide more opportunities for exporters to have credit access which would boost exports.

The Government also requires newly opened foreign banks and joint-venture banks to expand at least 50 percent of their credit portfolios for exports. Another policy which is in line with export development is the requirement for banks to channel at least 80 percent of their total foreign borrowings to finance export activities.

The financial reform have also sparked major innovations in financial products and services. The enormous growth in stocks after years of stagnation, is a particularly important example, and non-debt financial resource can provide a more stable financial base for the rapidly expanding private sector. The reforms in the capital market have brought brighter prospects for corporations as a source of funds to finance their activities. Thus, the role of the financial market in export promotion is quite significant as reflected in the amount of export financing through the banking system.

3.5 Fiscal Policy Measures

Fiscal policy restraint has played an important role in maintaining macroeconomic stability in the face of external shocks, thereby helping to establish conditions conducive to a strong expansion of non-oil/LNG exports. During the 1980s, Indonesia faced substantial external shocks that necessitated a strong policy respond to safeguard the external balance. Moreover, the task of fiscal management in these circumstances - sharp decrease in oil prices - directly undermined the overall fiscal

policy stance, as the oil and gas sector constituted by far the largest source of fiscal revenue. The country was also facing substantial external debt services burden that impacted heavily on the government budget which was also subjected to fluctuations on account of exchange rate movements among major currencies.

In respond to the external shocks, the authorities implemented sharp cuts in budgetary expenditures under an austerity program in 1982/ 1983 - particularly in development outlays - and began efforts to mobilize additional revenues from non-oil/gas sectors. Since 1984, a series of tax reform measures has been introduced, including a new income tax system, replacement of sales tax by a value added tax and a sales tax on luxury goods, and an introduction of a new property tax and stamp duty tax. In 1988/ 1989, the authorities introduced a withholding tax on deposit interest and extended the coverage on the VAT and sales tax. A further extension of the VAT to cover services was introduced in 1989/1990. Measures were also taken to improve tax administration and compliance.

In April 1985, a series of reform was implemented in order to increase the efficiency of the Indonesian port system and also to streamline customs operations. These reforms which were promulgated in Presidential Instruction No. 4/1985 were designed to increase the competitiveness of Indonesian exports by reducing the cost and improving the flow of trade. They included a ten-fold increase in the number of ports designated to handle international trade; a reduction in port storage costs; port administration charges, tugboats and pilot fee; and, less rigorous documentation requirements for inter-island and international shipping. In line with this policy, the Government commissioned a Swiss trade inspection firm, Societe General de Surveillance SA (SGS) to act as an agent in inspecting goods and assessing duties. The release of imports is contingent upon the issuance of an SGS clean report of findings and the payment of import duty and value-added tax.

Fiscal policy influences exports directly through the tax regime. As regard to direct taxes, the level of corporate income tax affects the international competitiveness of exports and may be expected to influence production location decisions by foreign investors. On indirect taxation, of particular relevance to exporter is the tax treatment of imported goods, the system of duty drawbacks and exemptions that

are used to compensate the anti-export-bias of import policies. A further deregulation package of May 1986 was to enhance the quality and lower the cost of Indonesian exports. Indonesian firms are now free to procure abroad the inputs required for export production, if these inputs can be shown to be more competitive in quality or price than domestically available alternatives. And, for the companies which can export at least 85 percent of their production are free from import licensing requirements. To stimulate capital formation in export industries, foreign joint-ventures which can export at least 85 percent of their production are permitted to invest in any sector of the Indonesian economy. This regulation also stipulated that other facilities which can be granted to the exporters or companies that produce exportable goods can be in the form of:

(i) Import duty restitution on imported goods and material used for the manufacturing of export commodities;

(ii) Import duty exemption/relief for the importation of raw material of auxiliary goods for the purpose of manufacturing export commodities; and,

(iii) Deferment of Value-Added Tax (VAT) payment for the importation of capital goods utilized in the production of goods and services. This deferment of VAT payment shall be disbursed within five years at the most after the commencement of commercial production.

In the field of investment there is no longer differential treatment between domestic and foreign investors. Foreign investor is now allowed full control in terms of share holdings. This is true for investment worth at least US$ 50 million and can be established in 15 provinces/regions only. This is based on the recent Government Regulation issued in April 1992.

3.5.1 Tariff and Non-Tariff Barriers

Trade reform concerning tariff and non-tariff barriers was adopted in October 1986. These reforms were designed to facilitate international trade and make domestic product prices more responsive to foreign competition by shifting from a quota restrictions (abolished for 165 items) and import licensing requirements (dropped on a further 110 goods).

In addition, efforts were made to reduce and standardize the level of job tariffs, with import duties on 152 goods being lowered from a range of 10-40 percent to a range of 0-5 percent.

Additional import duty reductions were introduced with the trade deregulation in January 1987. Import duties were lowered from a range between 10-60 percent to 5-10 percent on a total of 55 types of machinery, industrial and agricultural equipment as well as various industrial materials. Non-tariff barriers were removed on more than 100 items and quota restrictions on the importation of approximately 140 categories of textile goods were abolished. In June 1987, further measures were announced easing industrial licensing requirements so as to enhance the flexibility of manufactures wishing to increase production capacity and diversify product lines.

Further, a wide-ranging deregulation package was issued in December 1987, covering measures aimed at increasing the competitiveness of exports, reduced domestic production costs, promote foreign investment and facilitate capital-raising by domestic industry. The portion of package relating to trade included the abolition of export-licensing requirements, so that normal business license is now sufficient for exporting; permission for foreign joint-ventures to export products manufactured by other companies, as well as their own products; and, exemption from import duties and sales taxes on domestic companies' imports of capital goods for export production. In addition, those privileges granted in May 1986 to companies exporting over 85 percent of their production, including exemption from import licensing requirements and import duties, were extended to firms exporting only 65 percent of their production. Measures designed to reduce domestic production costs included a reduction in the number of sole importing agents from 278 to 70; the lifting on non-tariff barriers to the import of 111 products, including machinery and parts, heavy equipment, electronic devices, chemicals, steel goods, and automotive components; and, the establishment of container terminals and attendant customs facilities at various export production locations and ports throughout the country.

3.5.2 Export Restrictions

Even though Indonesia is now strengthening the effort toward producing export commodities, it still imposes some export restrictions as follows:

(i) Export Bans: The objective is to conserve scarce resources, encourage higher value-added, increase employment and preservation.

(ii) Regulated Exports: According to this regulation, the commodities can only be exported by approved or registered exporters. The main objective of this regulation is to respond to international quota, or to stabilize the market by avoiding counterproductive competition among Indonesian exporters/ producers.

(iii) Supervised Exports: Commodities which are subject to this regulation can only be traded with approval of Minister of Trade or Officials authorized by Minister. This restriction is aimed at providing sufficient supply to meet domestic demand.

(iv) Export Tax: The amount of export tax on specific export commodities is specified with the ad-valorem tariff system and the specific tariff system. Exporters must pay export tax and, whenever applicable, an additional export tax. For some commodities, the tax is calculated on the basis of a published cheap price, not on actual f.o.b.

As of January 1989, the harmonized system has become effective and covers 9066 tariff items. Since the issuance of the policy package of May 1986, Indonesia has deleted several non-tariff regulations and substituted tariff for them, including those which have become zero present tariffs. Apart from the above, it also decreased or reduced various prevailing tariffs.

In 1990, Indonesian Government issued a new trade policy reform package concerning the removal of export restrictions. In particular, several export restrictions have been abolished such as export banks for raw and semi-finished rattan, nutmeg and vegetable from North Sumatra, cinnamon and tengkawa. However, products made from sandlewood cannot be freely exported.

Since the reduction in tariffs, the structure has changed and a majority of the tariff system items are included at a relatively low tariff rate. The structure of such tariffs is as follows:

Table 2.2

STRUCTURE OF EXPORT DUTY TARIFFS

Tariff Rates	Total Tariff Items	
	1985 (CCCN)	1989 (HS)
0 %	278	714
5 %	1130	2094
10 %	571	753
15 %	235	406
20 %	607	893
30 %	785	1634
40 %	424	571
50 %	207	581
60 %	150	1371
80 %	-	-
100 %	17	86
200 %	2	29
Specific charges	521	19
Total:	4927	9154

The Indonesian Government is still continuously reducing and simplifying the structure of the tariff system. In the policy package of May 1990, tariff policy was directed to tariff reduction/elimination, tariff simplification, changing from specific tariffs to ad-valorem tariffs and tariffication of non-tariff measures. Under this policy, the tariff items have been simplified from 3006 tariff items to 2827 tariff items. Specially for industrial products, 371 industrial tariff items subject to non-tariff barriers have been abolished (out of a total of 1013 items previously). The structure of import duty tariffs for industrial goods is as follows:

Table 2.3

STRUCTURE OF IMPORT DUTY TARIFFS FOR INDUSTRIAL GOODS

Duty Tariff	Total Tariff Items	
	Before May 1990	After May 1990
0 % - 10 %	2956	2908
15 % - 20 %	1036	1116
25 % - 30 %	1431	1706
35 % - 40 %	447	1284
45 % - 60 %	1505	88
> 60 %	103	74
Total:	7431	7176

3.6 Institutional Arrangements

3.6.1 Trade Mission and Trade Houses

In order to widen the export market, Indonesian exporters have recently increased their trade promotion frequencies both in domestic and in foreign trade promotion centers. For the Indonesian case, trade mission is conducted by different public and private organizations, as well as by the Ministry of Trade and its National Agency for Export Development (NAFED). Indonesia, unlike other countries, does not have an official Trade Promotion Organization (TPO) which usually undertakes trade fairs and exhibitions at home and abroad.

The National Agency for Export Development, established in 1974 under the jurisdiction of the Ministry of Trade, acts as a liaison between local exporters and foreign importers. NAFED disseminates information on specific products and contributes to marketing efforts by referring foreign importers to appropriate Indonesian suppliers, and by representing Indonesian manufacturers at trade fairs abroad. NAFED also advises the Government on export policy and regulations, provides

assistance and training to local manufacturers and exporters and conducts research on foreign markets.

Besides NAFED, the Government also set up an autonomous organization called Export Support Board (ESB) under the decree of Ministry of Trade in March 1986. The establishment of this organization is to facilitate exporters in developing their export capabilities through technical assistance, consultation, marketing training, publishing brochures and channeling the financial aid (in the form of loans) to encourage export promotion activities, for which the sources of fund come from both government and/or other official sources.

Another institution set up in 1985 by the Government to encourage non-oil/gas export activities is the export credit insurance company called PT. Asuransi Ekspor Indonesia (ASEI). The PT. ASEI, a state-owned corporation (BUMN) took over the management of the export credit insurance scheme from ASKRINDO which stands for Asuransi Kredit Indonesia which was set up in 1982. Originally, it was PT. ASKRINDO which was responsible for export credit guarantee and insurance along with other credits, particularly "priority credits".

PT. ASEI provides these services: (i) insurance coverage for the risk of non-payment from foreign importers of goods or services supplied by Indonesian exporters; and, (ii) warranty coverage on behalf of the banks or other financial institutions in Indonesia which is providing credit against the risk of non-settlement by Indonesia exporters. It does not insure against: (i) loss due to default by exporters under the terms of the export agreement or failure to fulfil his export insurance policy requirement; and, (ii) loss incurred as a result of devaluation, revaluation or exchange rate fluctuation of every currency or loss incurred due to default of the exporter's agent or the collecting bank.

PT. ASEI covers both commercial and political risks. The commercial risks cover the bankruptcy of the exporters, the failure of exporter to pay within six months after due date and wrongful rejection by importer of goods shipped within the terms of the export agreement. Political risk covers transfer restriction, import quota limitation, revocation of import permits and war or other hostilities.

Credit guarantee is compulsory for all export loan extended in accordance with the present export financing scheme. Lending banks are required to report the ceiling determined for individual export loans

on the basis of which a guarantee is automatically issued by PT. ASEI which does not require an analysis of the loans concerned as regard the creditworthiness of loan receiver.

Premium for export credit insurance is fixed at 0.5 percent of the invoice value of exports for a maximum period of six months. For every further period of three months, an additional premium of 0.25 percent is required. This fee is to be paid by the lending banks immediately after the issuance guarantee by PT. ASEI. Premium is borne by the lending bank and Bank Indonesia equally. The lending bank then reimburse half of the premium paid to Bank Indonesia.

PT. ASEI bears 85 percent of the loss calculated on the bases of the export credit outstanding at the time bank entitles to claim for indemnification with a maximum 85 percent of export credit ceiling. The remaining 15 percent of the loss, half of which is borne by Bank Indonesia, is calculated from the total balance of export credit with a maximum of 7.5 percent of export credit ceiling. The lending bank can reimburse the share of indemnification borne by Bank Indonesia. However, this composition is usually linked to the country risk of the importer.

The claim can, however, be rejected by PT ASEI depending on the results of the investigation. Indemnification, unlike the guarantee, is not automatic. Lending banks have complained about the lack of automaticity in connection with indemnification as it constitutes a major obstacle to export credit guarantee, mainly because of the reluctance of banks to disclose information about their customers who, in many cases, have a much wider business with their banks than just export credit. Unlike export credit guarantee, export credit insurance is optional for exporters. This is understandable in view of varying risks involved in different export receivables.

Exporters believed that an irrevocable L/C which is tantamount to cash would not require export insurance coverage on transactions. In the absence of irrevocable L/C of sales contract, however, exporters who want to benefit from the preferential interest rates of the existing export credit regulation, are required to cover their transactions with an insurance policy issued by PT. ASEI. PT. ASEI can decide discreetly on whether to insure certain export items. It reserves the right to refuse insurance because of political instability prevailing in the export market.

The insurance policy issued by PT. ASEI covers 85 percent of export value; hence, the exporters are required to shoulder 15 percent of the loss in the event of non payment and the proportion of the loss has to be borne by the exporters is even higher at 20 percent. For such a coverage, exporters pay a premium ranging from 0.5 percent to 4 percent depending on the risks involved in each transaction.

3.6.2 Export Processing Zone

Bonded zone was established in 1986 under the Government regulation in lieu of bonded warehouses formed in 1972 and further amended by government regulation in 1977. The operation of bonded zone is conducted by a state-owned entity, Limited Liability Corporation (Pesero). They are located in Jakarta and Batam island. The latter was formed pursuant to the Presidential Decree No. 33/1974.

The bonded house operating agency is responsible for the adherence of the entrepreneurs to all applicable general provision in relation to the implementations of their business activities. It also grants undertaking license and other licenses for the activities perform in the bonded zone on behalf of the Minister/head of relative agency. Rent for the land, building rights and hindrance ordinance for any company operating in that area shall be processed by the bonded zone operating agency on behalf of the relative regional administration head.

3.7 Export Finance Scheme

Export credit has been classified as a priority credit. Bank Indonesia used to provide liquidity credit for export credit together with some other credit schemes. The process of channeling export liquidity credit is as follows: (i) lending banks are required to submit their annual requirements to the Central Bank regarding export credit; and, (ii) approval of export credit is given to the lending banks. Once the documents stating that export has been made are in the possession of the lending banks, funding can be obtained from the Central Bank. Export credit is defined as working capital granted to exporters whose activities involved (i) collecting, processing and producing products initially aimed at exporting; and, (ii) suppliers of goods which needed further processing to become export commodities.

Export credit can be channeled by foreign exchange commercial banks, and other commercial banks and non-bank financial institutions

which are allowed by Bank Indonesia. One of the document required when submitting the application for export credit for the purpose of credit analyses is as follows: (i) irrevocable banker's L/C; (ii) sales contract which cannot be called off by any one of the contracted party; and, (iii) the availability of inventory for exports, one-year plan of exports and past performance of the exporters.

It is compulsory for exporters to provide self-financing of at least 15 percent of the total export values. Export commodities are divided into two categories, namely primary products and non-primary products which are stipulated by the Ministry of Trade. Export credit granted to exporters of primary goods can be refined up to 70 percent, i.e., 70 percent x 80 percent x the FOB exports' value, while that of non-primary products can be refined up to 50 percent x 85 percent x the FOB exports' value.

The interest rate charged on export liquidity credit to the lending banks is uniform at 3 percent per annum. The lending banks can only withdraw export liquidity credit once a month based on the evidence of previous export realization (PEB). At the time of withdrawal of export liquidity credit, the lending bank is required to submit promissory note, signed by the authorized bank official, to Bank Indonesia. Bank Indonesia, then, debits the checking account of the lending bank on due date of the promissory note.

In order to promote backward linkages and foster the development of trading companies, Bank Indonesia introduced domestic L/C system in 1988 to expand the pre-shipment export financing scheme to indirect exporters (who supply intermediate inputs to direct exporters or finished products to trading companies). This was aimed at encouraging backward integration to local industries, primarily small- and medium-sized firms and thereby increase export value-added. Bank Indonesia stipulates that a domestic L/C can only be opened on the basis of an original (or master) irrevocable L/C, sales contract or export order.

The principle of functioning a domestic L/C system is the creation of back-to-back credit with the indirect exporters as the beneficiary. Since banks in Indonesia do not handle loan disbursements on behalf of the final exporter, they cannot create back-to-back credit and issue domestic L/C in favor of the indirect exporter. It is thus crucial that

banks handle loan disbursements on behalf of the exporter and payments for the purchase of domestic input or products be tied to the domestic L/C system. This would also reduce banks' losses stemming from exporters' deliberate default or non-performance.

With the January 1990 deregulation package concerning credit, Bank Indonesia's liquidity credits have been streamlined. In pursuance of this new measure, Bank Indonesia's liquidity credit shall be granted to banks in support of financing certain line of business, such as farm business credits, credit for cooperative for food procurement and productive activities, credits for food and sugar procurement by logistic body, and investment credits. The interest rates on the aforementioned are based on the market level. The portion of Bank Indonesia's liquidity credits are adjusted to the needs of the respective type of credits and are subjected to review from time to time.

The abolishment of export credit facility was pursuant to the agreement with the U.S. concerning Subsidies and Countervailing Duties. Another reason was the inflationary effects caused by liquidity credit from the Central Bank. In practice, it was also evident that the facility was abused in such a way that funds meant for export promotion purposes were channeled to finance other activities in which the cost of fund would have been much higher being classified under non-priority lending.

Furthermore, the new measure was also intended to encourage banks to be more active in collecting funds. The Government is aware that the low cost of export liquidity credit as compared to funds collected from other sources would not stimulate the lending banks to mobilize funds, such as deposits, certificate of deposits and others. As funds from other sources bear higher interest rates the demand for refinancing is partly a function of requisite conditions as stipulated by the authority.

Prior to 1990, the pre-shipment export finance guarantee (PEFG) was obligatory for all exporters who received export credit facilities from the commercial banks. PT. ASEI, the guarantee agency, was required to cover all those applications submitted without reviewing the credit decisions of the handling banks. The amount of indemnification was fixed at 85 percent of the loss sustained as long as the loss constituting the basis for indemnification does not exceed the export

credit ceilings. Bank Indonesia precludes banks from demanding additional guarantees to those PT. ASEI or taking collateral other than export-related inventory and receivables. Since loan payment is made from proceeds of export sales, exporters after receiving payments of their exports should first settle export loans outstanding.

Post-shipment credit is provided for exporters who trade their products with the usuance of L/C or other deferred payment terms, as long as the payment period does not exceed the terms of the underlying loan agreement. In the absence of an L/C, banks may provide credit on evidence of a credit insurance cover note issued by PT. ASEI. The amount of export credit is equivalent to the total value of the export bill with the usuance L/C or the total amount insured by PT. ASEI for export without L/C. Bank Indonesia also provides discount facility which can be used to finance the usuance of L/C. Banks issue instrument to Bank Indonesia for the face value and the terms of the underlying L/C (from a minimum of 15 days to a maximum of 180 days) which is discounted at 6 percent. The amount of the instrument is the rupiah value of the export transaction converted on the day of the discount. This facility is apparently attractive in stimulating export activities. In order to encourage non-oil exports through the utilization of this facility, since May 1989, Bank Indonesia has freed the maturity of the L/C for exports and extended the period for discounting of export L/C from 180 days to 360 days with a minimum of 15 days. At the same time, the rediscount of export L/C to Bank Indonesia which was formerly only in U.S. dollar was expanded to many other hard currencies at a discount rate that varies according to the currency of denomination of the export bill; it is also adjusted periodically to take into account developments on international interest rates.

3.8 Export Infrastructure and Industrial Sites

Adequate infrastructure is a prerequisite to successful export development. This includes well-developed industrial sites with adequate power, water, telecommunications and transport facilities. It should be located close to urban areas in order to obtain an adequate supply of labor and related social facilities, except for primary industries based on natural resources. Indonesia's industrial sites which are located along the northern sea-coast of Java provided all of those facilities. The fast growing industrial sector in the early 1980s has increased demand of

those facilities. The infrastructure bottlenecks have also been eased considerably in recent years as a result of large investments in this sector after the 1980s deregulation.

The existing industrial sites are overcrowded along the northern seaboard and in Jakarta. In November 1989, the Government introduced a policy for industrial estates development by the private sector. Private companies, both foreign and domestic, are now allowed to develop industrial estate without the involvement of Government or its firms in the ownership of the estates. The lease term has also been extended to 30 years, as long as the land is used as an industrial estate. The main attractions of the Nusantara Zone to investors are the "one-stop" facilities for export activity, the well-developed industrial services, and the various exemptions/one stop facilities in other areas, such as "nuisance", permits, labor regulations, and land leases.

Deregulation in the maritime sector has led to major improvements in transportation and related services, including freight forwarding, shipping agency arrangements, and custom clearances. However, some bottlenecks should be resolved. The domestic shipbuilding capacity is weak and cannot address immediate problems. These problems were a result of booming conditions as reflected by the high frequencies of incoming and outgoing of vessels through the ports.

The supply of power during the last decade has also increased dramatically. Nevertheless, some of this ambitious investment program which consume a lot of foreign exchange is delayed. To overcome this power shortfall, the Government allowed private companies to build the power plant along with state owned company PLN. About 3000 MW capacity is available for industries in Java, of which about 2000 MW are connected to the PLN system.

High priority is given to telecommunication development which is an important factor industrial expansion. However, an important recent development is that the private sector has also been allowed to provide data transmission facilities, which should provide an alternative and important mode for business communications in the coming years. The prospects for an improvement in telecommunication facilities would appear reasonably bright, although it will take some time.

3.9 Role of Central Bank in Export Promotion

Prior to 1990, the role of Bank Indonesia as the Indonesian monetary authority in promoting non-oil/gas exports was direct and dominant by providing export credit liquidity. After the abolishment of this credit scheme, Bank Indonesia encourages export developments indirectly through the banking system. The areas in which Bank Indonesia can still be involved in promoting non-oil/gas exports are through the determination of exchange rate policy, swap facility and payment arrangements.

As mentioned earlier, Bank Indonesia determines the rupiah exchange rate based upon weighted average of a basket of currencies. This is conducted by taking into account both domestic and foreign market developments. This is very important in order to maintain the competitiveness of Indonesian products in the world market. Since the last devaluation of the rupiah in September 1986, Indonesia has been able to control and sustain the real effective exchange rate of the rupiah and increases the confidence of Indonesian exporters. As a result, the total value of non-oil/gas exports has increased impressively during the last few years. The total non-oil/gas exports at the end of 1988 was US$ 11.5 billion and it increased to US$ 18.2 billion at the end of 1991.

Bank Indonesia has also provided more access for banks to obtain foreign borrowing by lifting the ceiling of offshore borrowing and introduced new net open position measures. Prior to March 1989, banks licensed to deal in foreign exchange in Indonesia were subject to tight ceilings on their currencies borrowings. Consequently, Indonesian who wished to borrow in foreign exchange were constrained by these ceilings, as well as by the limited availability of domestic foreign currency deposits, and by their own capacity to borrow directly from offshore. As regard offshore borrowing, typically only large, established investors were able to tap overseas markets, usually through the domestic foreign exchange banks, through the Jakarta branch offices of foreign banks or through representative offices of banks not licensed to operate in Indonesia.

For investors with limited ability to bear exchange risk, foreign borrowing may be combined with exchange cover (swaps). Bank Indonesia offers forward cover for offshore borrowing in the form of foreign exchange/rupiah swaps to banks and non-bank financial

institutions (NBFIs). Effective October 1988, Bank Indonesia made certain changes to this facility in support of longer-term offshore borrowing. The maturity of Bank Indonesia swaps was extended to three years. The determination of the premium was modified to reflect market rates so the magnitude of the premium is the difference between the London Interbank Offered Rate (LIBOR) and the average of deposit rates at foreign exchange banks for the corresponding maturity (with the premium adjusted at the end of each year).

The replacement of ceilings on foreign borrowing by limits on banks' net open position is a welcome means for making competitively priced investment financing available to exporters. In the current environment of rapid expanding overseas sales, Indonesian exporters are well positioned to service foreign currency debt out of their export receipts, perhaps using commercially available forward cover to hedge against third-currency movements.

Improvement in export financing as a result of changes in regulations regarding banks net open positions can be complimented by further development of existing commercial swaps and forward foreign exchange markets. Key considerations in developing these markets are that the pricing mechanism remains market-determined and should adequately reflect the differential opportunity cost of money locally and abroad, and there should be free access to this market as well as a broad transaction coverage, and the assurance that foreign exchange risk will be fully borne by the private sector. In this context, exporters would be considered both as suppliers of foreign exchange and as users, whether to acquire imported input, finance their expansion plans, finance their operations within the period between export sales and receipts and/or to service debt acquired in connection to any of the above. In addition, it would be advisable that access be broadened to include importers and institutional investors and to encourage banks to cover their position in the interbank market as well as offshore. As the private market develops, it should be expected that Bank Indonesia's current role of main supplier of onward cover in the financial system of prudential regulations, including rules and regulations applicable to market makers and brokers, would need to be developed to assure the market's security and solvency.

Another means now being developed to pave the way for stimulating non-oil/gas exports is payment arrangements. Bank

Indonesia has made a breakthrough by approaching the Central bank of some potential countries to settle a framework of the agreement regarding the payment arrangement. The availability of this agreement would hopefully give confidence and assurance for contracted parties and it is expected to strengthen the non-oil/gas export growth. Bank Indonesia in this case, however, does not provide credit line and guarantee of the transaction made between Indonesian exporters and foreign buyers.

IV. Problems and Issues on Export Promotion

The short-term problems and issues regarding export promotion could be in the area of finance, marketing, and promotion, information and infrastructure. In recent years, industrial development in export oriented industries have been growing rapidly. To anticipate this fast growing industrial sector, the Indonesian Government has also given high priority in the development of infrastructure. The capacity and availability of the existing infrastructure has become an issue because it is a determining factor in boosting non-oil/gas exports. Some deregulation packages in the field of infrastructure developments have been introduced such as, deregulation in the maritime sector, export processing zone, etc. Furthermore, the Indonesian Government has also invested to build the export infrastructure. The Government through its state company (BUMN) has built new power plant to increase the electric power supply, completed and renewed port facilities, established export processing zone, etc. Because of limited government funds, the development of infrastructure has been neglected as compared to the progress achieved in the industry itself.

In the financial sector, Indonesian producers or exporters also faced some short-term problems. To support their export transactions which have increased in the past few years, financial assistance is needed. After lifting export financing from the refinancing facilities of Bank Indonesia, exporters are now competing with other debtors to obtain banks' credits. With limited available funds, banks would be more selective in channeling their credits and banks or NBFIs are now free to lend to exporters at market-determined interest rates. As a result, domestic interest rates, which have been high, became higher which discouraged Indonesian exporters. In addition, indirect exporters, who are crucial to the promotion of backward integration, do not have easy, automatic access to export financing and duty free imports.

Another crucial problem encountered by Indonesian exporters is related to the marketing strategy. Much of the marketing efforts for the Indonesian exports are performed by foreign buyers and therefore, there is a lack of marketing effort by Indonesian producers/exporters or government agencies. The links in marketing chain are complex starting from selecting the products - packaging, advertising and shipping. The marketing efforts being done abroad include receiving, storing, advertising and selling to the retailers, perhaps with arrangements for financing and after-sales service. The time, risk, money, know-how and efforts required for these tasks are daunting for Indonesian exporters to become involved with. Furthermore, Indonesian exporters lack the information about the economic situation, business, and marketing information in importing countries. As we have already known that information is a key factor for exporters to be successful.

V. Policy Recommendations

Indonesia should consistently pursue the outward-looking policy and improve business climate especially export-oriented industries. To do this, the automatic access to bank credit, duty-free imports, for export production, infrasturcutral upgrading, debureaucratization, etc., should be reconsidered to enhance particularly the promotion of non-oil commodity exports. With these efforts, the efficiency of the Indonesian economy could be increased to prepare the business community to compete in the global market.

Bank Indonesia has issued regulation pertaining to the use of domestic L/C in favor of the indirect exporters. Bank Indonesia could modify the regulation and banks could then create domestic L/Cs even if the final exporter does not have an export L/C or form export order. The handling banks can issue a certificate attesting to the past performance of the exporter, and banks can then create domestic L/Cs on the basis of the certificate.

The role of trade promotion in stimulating non-oil/gas exports is important. In order to make trade promotion more effective, it should be conducted by export promotion organization under private sector management to replace NAFED. Moreover, a private sector advisory board should be formed to approve, advise and rationalize NAFED's activities.

In the marketing field, the Government should consider the establishment of general trading companies in Indonesia to directly market Indonesian exports abroad and actively encourage alternative channels of marketing. The Government should not seek to intervene in export marketing, except under special circumstances; should not seek to actively encourage or invest in general trading companies; and, should not try to directly develop particular export line of activity (i.e., targeted export industry programs), except in certain circumstances. There is one small area in marketing in which there could be a role for support services and a role for government assistance. This is in the area of establishing and maintaining an information service to help foreign buyers to locate reliable export firms. This is potentially a cost-effective way of enhancing the efficient role of, and to court foreign buyers.

A major concern of exporters and traders in Indonesia is about the lack of overseas marketing. The increase of Indonesian exports in the past few years was due to effective marketing channels developed by overseas buyers and joint-ventures. Given these circumstances Indonesia should: (i) develop an active program to strengthen private trading groups in Indonesia in limited areas; (ii) focus on target marketing; (iii) support strong private sector groups; and, (iv) provide support through government institutions and funding.

Appendix 2.1

INDONESIA: BALANCE OF PAYMENTS (Million US$)

	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983
1. Exports f.o.b.	995	1,173	1,307	1,757	2,957	6,755	6,869	8,615	10,761	11,020	15,907	22,609	23,665	19,747	18,689
- Non-Oil/LNG	629	739	792	880	1,609	2,199	1,817	2,534	3,511	3,659	5,579	6,079	4,431	3,878	4,993
- Oil	366	434	515	877	1,348	4,556	5,052	6,081	7,177	6,900	9,347	14,461	16,955	13,459	11,413
- LNG	0	0	0	0	0	0	0	0	73	461	981	2,069	2,279	2,410	2,283
2. Imports f.o.b.	(997)	(1,116)	(1,226)	(1,445)	(2,664)	(4,632)	(5,468)	(6,828)	(7,473)	(8,382)	(9,946)	(13,456)	(16,542)	(17,854)	(17,726)
- Non-Oil/LNG	(910)	(1,024)	(1,114)	(1,282)	(2,359)	(3,427)	(4,598)	(5,219)	(5,870)	(6,780)	(7,422)	(10,055)	(12,188)	(13,421)	(13,896)
- Oil	(87)	(92)	(112)	(163)	(305)	(1,205)	(870)	(1,609)	(1,595)	(1,564)	(2,449)	(3,268)	(4,234)	(4,298)	(3,672)
- LNG	0	0	0	0	0	0	0	0	(8)	(38)	(75)	(123)	(120)	(135)	(158)
3. Services	(425)	(487)	(538)	(784)	1,098	(2,097)	(2,565)	(2,747)	(3,360)	(4,072)	(5,009)	(6,399)	(7,622)	(7,351)	(7,405)
- Non-Oil/LNG	(228)	(271)	(315)	(400)	619	(915)	(1,304)	(1,803)	(2,135)	(2,452)	(2,717)	(3,451)	(3,629)	(3,812)	(4,122)
- Oil	(197)	(216)	(223)	(384)	479	(1,182)	(1,261)	(944)	(1,200)	(1,402)	(1,882)	(2,238)	(3,126)	(2,623)	(2,462)
- LNG	0	0	0	0	0	0	0	0	(25)	(218)	(430)	(710)	(867)	(916)	(821)
4. Current Account	(427)	(430)	(457)	(472)	(805)	26	(1,164)	(951)	(72)	(1,434)	952	2,754	(499)	(5,458)	(6,442)
- Non-Oil/LNG	(509)	(556)	(637)	(802)	(1,369)	(2,143)	(4,085)	(4,479)	(4,494)	(5,573)	(4,560)	(7,437)	(11,386)	(13,355)	(13,025)
- Oil	82	126	180	330	564	2,169	2,921	3,528	4,382	3,934	5,036	8,955	9,595	6,538	5,279
- LNG	0	0	0	0	0	0	0	0	40	205	476	1,236	1,292	1,359	1,304
5. Special Drawing Rights	0	35	28	30	0	0	0	0	0	0	64	65	62	0	0
6. Official Transfer & Capital (Net)	284	361	317	378	556	596	1,778	1,632	1,397	1,491	1,725	2,204	1,963	4,117	4,776
- Inflows	314	407	389	447	624	699	1,854	1,743	1,933	2,221	2,446	2,828	2,729	5,030	5,760
- Amortization	(30)	(46)	(72)	(69)	(68)	(103)	(76)	(111)	(536)	(730)	(721)	(624)	(766)	(913)	(984)
7. Private Capital (Net)	71	75	150	427	498	382	(1,493)	237	(72)	333	(611)	(630)	148	1,639	1,826
- Foreign Direct Investment (Net)	44	97	152	258	290	471	497	370	233	272	227	180	133	225	292
- Others (Net)	27	(22)	(2)	169	208	(89)	(1,990)	(133)	(305)	61	(838)	(810)	15	1,414	1,534
8. Total (4-7)	(72)	41	38	363	249	1,004	(879)	918	1,253	390	2,130	4,393	1,674	298	160
9. Errors & Omissions	52	(6)	(95)	58	76	(314)	(104)	(182)	(55)	(233)	(566)	(2,057)	(2,069)	(2,229)	494
10. Monetary Movements	20	(35)	57	(421)	(325)	(690)	983	(736)	(1,198)	(157)	(1,564)	(2,336)	395	1,931	(654)
Offical Reserves	58	93	36	457	782	1,472	489	1,225	2,423	2,580	4,144	6,480	6,035	4,154	4,808
- Eq. of Month of Non-Oil/Gas Imp. C&F	0.7	1.0	0.3	3.8	3.5	4.5	1.1	2.5	4.4	4.1	6.0	6.9	5.3	3.3	3.7

INDONESIA: BALANCE OF PAYMENTS (Million US$)

	1984	1985	1986	1987	1988	1989	1990	1991
1. Exports f.o.b.	20,754	18,527	14,396	17,206	19,509	22,974	26,807	29,430
- Non-Oil/LNG	5,775	5,978	6,656	8,635	11,677	14,060	14,876	17,991
- Oil	11,755	8,977	5,164	6,110	5,131	6,005	7,589	7,357
- Gas	3,224	3,572	2,576	2,461	2,701	2,909	4,342	4,082
- LNG	3,224	3,572	2,576	2,423	2,612	2,676	3,970	3,733
- LPG	-	-	-	38	89	233	372	349
2. Imports f.o.b.	(15,047)	(12,705)	(11,938)	(12,532)	(13,831)	(16,310)	(21,455)	(24,626)
- Non-Oil/LNG	(12,110)	(10,152)	(9,757)	(10,305)	(11,728)	(13,904)	(18,233)	(21,283)
- Oil	(2,688)	(2,364)	(2,000)	(2,054)	(1,946)	(2,239)	(3,020)	(3,125)
- LNG	(249)	(189)	(181)	(173)	(157)	(167)	(202)	(218)
3. Services	(7,677)	(7,772)	(6,557)	(6,943)	(7,230)	(7,944)	(8,592)	(9,016)
- Non-Oil/LNG	(4,065)	(4,093)	(4,058)	(4,224)	(4,707)	(5,076)	(5,532)	(6,044)
- Oil	(2,516)	(2,343)	(1,579)	(1,705)	(1,531)	(1,671)	(1,716)	(1,660)
- LNG	(1,096)	(1,336)	(920)	(1,014)	(992)	(1,197)	(1,344)	(1,312)
4. Current Account	(1,970)	(1,950)	(4,099)	(2,269)	(1,552)	(1,280)	(3,240)	(4,212)
- Non-Oil/LNG	(10,400)	(8,267)	(7,159)	(5,894)	(4,758)	(4,920)	(8,889)	(9,336)
- Oil	6,551	4,270	1,585	2,351	1,654	2,095	2,853	2,572
- LNG	1,879	2,047	1,475	1,274	1,552	1,545	2,796	2,552
5. Official Transfer & Capital (Net)	2,865	1,739	3,074	2,104	1,965	2,776	633	1,369
- Inflows	4,058	3,228	5,070	4,890	5,512	6,519	4,536	5,588
- Amortization	(1,193)	(1,489)	(1,996)	(2,786)	(3,547)	(3,743)	(3,903)	(4,219)
6. Private Capital (Net)	757	68	1,291	1,548	407	314	4,113	4,889
- Foreign Direct Investment (Net)	222	308	258	385	576	682	1,092	1,482
- Others (Net)	535	(240)	1,033	1,163	(169)	(368)	3,021	3,407
7. Total (4-6)	1,652	(143)	266	1,383	820	1,810	1,506	2,046
8. Errors & Omissions	(709)	238	(810)	(173)	(1,141)	(1,439)	593	(839)
9. Monetary Movements	(943)	(95)	544	(1,210)	321	(371)	(2,099)	(1,207)
Offical Reserves	5,751	5,846	5,302	6,512	6,191	6,562	8,661	9,868
- Eq. of Month of Non-Oil/Gas Imp. C&F	(5.1)	(5.2)	(5.9)	(5.8)	(5.7)	(5.1)	(5.1)	(5.0)

EXPORT BY SITC COMMODITY GROUPS
(Million US$)

Commodity Group	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
Food & live animals	368	589	1066	989	1208	1291	929	905	1093	1412	1383	1774	1684	2001	2078	2293	2539
Beverages & tobacco	36	40	55862	55	58	61	54	42	48	43	49	69	72	69	115	136	154
Crude materials, inedible	1055	1582	1761	1851	3064	3569	2208	1581	1650	1763	1403	1473	1926	2661	2796	1970	2373
Mineral fuels, lubricants, etc.	5311	6004	7379	7986	10165	15743	17764	18373	16153	15970	12757	8310	8582	7723	8760	11239	11169
Animal & vegetable oils & fats	160	145	193	214	222	285	129	133	149	192	414	166	290	539	457	420	562
Chemical	24	28	60	55	64	84	64	61	119	170	210	260	251	346	499	621	853
Manufactured goods	92	74	236	332	571	615	777	817	1350	1523	1804	1984	3267	4281	5113	5644	6489
Machinery & transport equipment	32	53	60	71	116	109	154	180	133	212	98	63	57	126	202	367	668
Misc. manufactured articles	21	27	29	31	81	120	121	141	213	366	437	678	732	1154	1883	2864	4190
Commodities & transaction nes.	3	5	13	19	40	33	60	59	238	166	31	29	275	318	256	122	145
Total:	7102	8547	66659	11603	15589	21910	22260	22292	21146	21817	18586	14806	17136	19218	22159	25676	29142

IMPORT BY SITC COMMODITY GROUPS
(Million US$)

Commodity Group	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
Food & live animals	291	428	433	590	1034	1285	1356	1074	1135	676	556	610	524	642	911	852	1081
Beverages & tobacco	67	43	58	64	21	42	45	51	28	29	21	28	33	34	34	54	74
Crude materials, inedible	712	895	1065	1146	368	491	565	609	676	883	729	830	991	1205	1674	1885	2151
Mineral fuels, lubricants, etc.	610	804	1060	983	797	1754	1727	3550	4150	2705	1286	1107	1288	959	1253	1937	2323
Animal & vegetable oils & fats	3	6	8	66	31	9	29	13	12	6	36	18	97	177	151	26	41
Chemical	990	701	806	950	1019	1255	1754	1804	1893	2137	1917	1910	2328	2541	2873	3394	3432
Manufactured goods	645	784	818	913	1404	2053	2518	2732	2352	1885	1723	1668	1735	2062	2638	3553	4138
Machinery & transport equipment	1435	1984	1950	1941	2297	3634	4619	6260	5684	5037	3615	4118	4319	5096	6182	9328	11631
Misc. manufactured articles	16	28	32	35	215	285	325	376	359	379	333	389	470	451	634	797	980
Commodities & transaction nes.	1	1	1	2	41	27	334	390	65	99	47	41	33	81	10	13	17
Total:	4770	5674	6231	6690	7227	10835	13272	16859	16354	13836	10263	10719	11818	13248	16360	21839	25868

VALUE OF NON-OIL/LNG EXPORTS
(Million US$)

	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983
T O T A L	629	739	792	880	1,609	2,199	1,817	2,533	3,511	3,659	5,579	6,079	4,431	3,878	4,993
Agricultural	...	584	720	744	1,413	1,820	1,463	2,142	2,981	3,066	4,656	4,729	3,092	2,667	3,392
1. Timber	...	101	231	231	583	725	502	781	964	1,003	1,912	1,900	948	872	1,111
2. Rubber	...	260	222	196	394	487	365	534	596	715	1,023	1,113	910	606	859
3. Coffee	...	66	55	73	77	102	101	250	635	510	655	655	379	344	446
4. Tea	...	18	29	32	30	44	53	56	121	93	92	95	100	116	125
5. Palm Oil	...	37	46	42	72	166	158	143	194	208	254	215	75	83	118
6. Pepper	...	3	25	21	28	25	23	46	61	70	48	52	46	48	52
7. Tobacco	...	11	20	30	45	36	38	39	60	59	60	68	63	38	48
8. Copra Cake	...	6	11	13	18	22	26	31	38	35	42	52	37	35	32
9. Foodstuffs	...	23	42	41	44	75	63	60	61	77	145	132	107	67	106
- Tapioca	...	8	14	13	4	26	23	10	12	17	68	36	20	15	27
- Other Foodstuffs	...	15	28	28	40	49	40	50	49	60	77	96	87	52	79
10. Animal & Produce of which:	...	8	20	37	77	98	91	140	174	198	253	233	233	248	272
- Shrimp	...	0	0	31	70	84	78	123	156	173	221	180	180	197	202
11. Rattan	...	1	1	1	2	4	3	9	18	29	83	80	81	85	86
12. Hides	...	6	6	9	14	10	10	21	19	25	48	33	32	27	24
13. Others	...	44	12	18	29	26	30	32	40	44	41	101	81	98	113
Mineral	...	62	64	79	147	270	265	267	353	392	518	763	742	678	773
14. Tin	...	62	64	66	86	159	167	154	236	302	375	461	426	365	339
15. Copper	...	0	0	3	51	97	78	85	78	67	75	126	126	118	81
16. Nickel	...	0	0	10	10	14	20	28	38	22	40	134	123	134	154
17. Aluminum	...	0	0	0	0	0	0	0	0	0	0	0	0	24	134
18. Granite	...	0	0	0	0	0	0	0	1	1	1	2	6	4	11
19. Others	...	0	0	0	0	0	0	0	0	0	27	40	61	33	54
Manufactured	...	7	8	16	23	38	40	64	103	122	290	337	335	489	828
20. Textiles	...	0	0	2	5	5	3	3	3	24	59	128	87	153	236
21. Handicraft	...	0	0	2	4	10	4	8	8	10	58	18	46	21	57
22. Electrical Appliances	...	2	2	0	0	0	10	31	32	33	64	86	69	105	120
23. Cement	...	0	0	0	0	0	0	0	0	2	21	20	12	11	7
24. Fertilizer	...	0	0	0	0	0	0	0	40	32	43	31	9	21	40
25. Others	...	5	6	12	14	23	23	22	20	21	45	54	112	178	368
Unclassified	...	86	0	41	26	71	49	60	74	79	115	250	262	44	0

VALUE OF NON-OIL/LNG EXPORTS

	1984	1985	1986	1987	1988	1989	1990	1991*
T O T A L	5,775	5,978	6,656	8,635	11,677	14,053	14,876	17,992
Agricultural	2,583	2,480	2,806	3,088	3,851	3,608	3,721	4,092
1. Rubber	959	721	720	966	1,263	1,005	883	920
2. Coffee	575	580	830	537	552	490	371	370
3. Tea	226	152	101	113	133	159	173	159
4. Palm Oil	76	185	109	169	325	296	253	336
5. Pepper	65	78	140	149	142	115	83	69
6. Tobacco	45	46	73	68	66	58	65	67
7. Copra Cake	22	32	35	36	42	49	50	57
8. Foodstuffs	130	168	144	185	260	327	430	499
- Tapioca	29	45	49	91	124	82	128	110
- Other Foodstuffs	101	123	95	94	136	246	302	388
9. Animal & Produce of which:	231	245	348	449	708	781	1,006	1,174
- Shrimp	194	202	290	361	504	518	660	793
10. Rattan	88	90	96	147	74	0	0	0
11. Hides	40	37	44	51	73	70	60	45
12. Others	126	146	166	218	213	258	347	396
Mineral	779	805	738	961	1,388	1,682	1,447	1,583
13. Tin	263	246	181	139	160	211	155	144
14. Copper	136	126	158	154	224	316	400	519
15. Nickel	130	131	124	131	361	466	319	304
16. Aluminum	197	244	215	220	288	307	206	166
17. Granite	11	8	9	7	6	8	12	17
18. Gold	0	0	22	267	296	252	122	130
19. Others	42	50	29	43	53	122	233	303
Manufactured	2,413	2,693	3,112	4,586	6,438	8,763	9,708	12,317
20. Wood Products	1,173	1,210	1,419	2,265	2,854	3,405	3,286	3,612
21. Textiles	405	454	746	912	1,265	2,021	2,612	3,667
22. Handicraft	106	141	178	241	417	241	343	439
23. Electrical Appliances	141	71	8	5	14	161	236	482
24. Cement	12	21	41	53	76	123	99	44
25. Fertilizer	37	82	126	97	120	159	187	288
26. Others	539	714	594	1013	1692	2653	2945	3785

INDONESIA: DESTINATION OF EXPORTS
(Million US$; Percentage)

	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979
Japan	179.5	255.9	452.3	550.4	901.8	1707.4	3969.3	3131.8	3564.3	4360.8	4565.5	7191.9
%	23.0	30.0	39	45	51	53	53	44	42	40	39	46
United States	118.7	128.6	144.3	192.4	265.3	465.3	1580.3	1865.5	2452.0	3011.4	2962.2	3170.7
%	15	15	12	16	15	14	21	26	29	28	25	20
Major European Markets	132.7	131.5	166.3	181.7	240.3	340.1	403.0	412.1	640.0	949.1	899.4	1213.3
%	17	15	14	15	14	11	5	6	7	9	8	8
Belgium/Luxembourg	12.0	15.7	16.7	15.0	33.9	16.4	11.5	11.3	14.1	22.8	18.2	17.8
Denmark	-	-	-	-	-	6.9	10.2	8.8	22.2	53.7	40.2	42.9
F.R. Germany	52.7	46.9	54.5	62.2	66.0	118.7	161.4	134.9	204.1	235.1	226.4	337.4
France	3.7	4.8	6.9	6.9	10.6	16.9	23.5	13.3	32.2	63.1	54.1	76.6
Italy	-	-	8.8	9.2	24.5	38.6	22.4	23.5	73.4	109.4	125.8	209.9
Netherlands	52.9	52.2	63.3	71.1	78.1	100.9	139.4	180.7	228.3	372.1	354.5	399.1
U. Kingdom	11.4	11.9	14.3	11.9	23.5	32.1	21.9	31.4	44.8	61.7	53.6	68.9
Portugal	-	-	0.3	-	0.5	1.9	3.2	0.3	3.5	3.6	2.9	2.6
Spain	-	-	1.3	4.9	2.6	6.7	9.0	6.5	14.1	24.0	18.8	30.2
Ireland	-	-	-	0.3	0.3	0.4	0.3	0.9	0.9	1.2	1.1	0.2
Greece	-	-	0.2	0.2	0.3	0.6	0.2	0.5	2.4	2.4	3.8	7.7
ASEAN	148.7	184.2	197.7	187.2	142.1	377.6	644.9	404.8	758.2	1154.9	1477.9	2232.5
%	19	22	17	15	8	12	9	6	9	11	13	14
India	-	-	-	-	-	3.2	3.8	12.6	4.2	27.5	31.3	17.7
%												
Others	201.1	153.5	200.0	121.9	228.2	317.2	825.0	1275.7	1127.8	1349.0	1706.9	1764.0
%	26	18	17	10	13	10	11	18	13	12	15	11
Total:	780.7	853.7	1160.6	1233.6	1777.7	3210.8	7426.3	7102.5	8546.5	10852.7	11643.2	15590.1

INDONESIA: DESTINATION OF EXPORTS

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992*
Japan	11833.2	11949.6	11192.6	9678.2	10352.5	8593.5	6644.0	7343.3	8018.3	9321.2	10923.4	10766.8	5855.5
%	49	54	50	46	47	46	45	43	42	42	43	37	32
United States	4798.4	4852.2	3546.0	4266.7	4504.7	4040.2	2901.5	3348.7	3073.7	3496.6	3364.6	3508.5	2352.7
%	20	22	16	20	21	22	20	20	16	16	13	12	13
Major European Mkts.	1433.8	1067.7	864.6	984.1	1100.3	1156.4	1383.3	1541.1	2125.6	2338.4	3028.5	3742.2	2574.0
%	6	5	4	5	5	6	9	9	11	11	12	13	14
Belgium/Luxembourg	24.8	18.2	19.6	33.0	62.7	42.3	90.5	109.3	177.0	173.0	209.9	257.7	214.8
Denmark	40.0	14.7	9.6	4.4	6.0	2.6	5.8	12.9	2.4	35.5	54.0	74.2	56.4
F.R. Germany	389.0	239.1	252.7	252.4	246.3	254.9	334.2	361.1	455.5	492.8	749.9	907.1	504.2
France	122.2	51.7	77.2	53.1	48.6	70.6	92.9	101.8	164.4	208.9	285.7	385.9	286.5
Italy	254.4	141.5	84.0	119.5	167.3	152.0	151.8	174.9	220.5	234.1	276.1	381.5	317.5
Netherlands	414.9	347.2	266.2	289.2	331.9	392.0	452.6	493.4	646.3	681.3	723.1	837.5	586.5
U. Kingdom	141.7	131.0	126.4	199.0	167.7	191.4	196.6	212.4	340.8	383.6	516.8	653.9	436.7
Portugal	8.0	0.5	0.5	0.5	0.4	2.4	6.6	10.4	21.8	23.6	16.9	13.9	6.9
Spain	34.5	30.5	26.9	30.8	63.7	44.0	43.7	55.2	77.6	80.0	152.2	169.2	124.5
Ireland	0.7	0.3	0.4	0.8	4.3	1.5	2.3	6.7	17.1	21.8	34.6	43.1	25.2
Greece	3.6	93.0	1.1	1.4	1.4	2.7	6.3	3.0	2.2	3.8	9.3	18.2	14.8
ASEAN	3264.9	3414.8	3499.1	3476.3	2487.3	1982.6	514.9	1704.0	2079.3	2429.2	2515.1	3196.6	2056.0
%	14	15	16	16	11	11	3	10	11	11	10	11	11
India	45.7	22.6	8.2	9.7	26.5	42.8	55.8	63.8	67.3	51.0	59.8	56.1	31.8
%													
Others	2584.4	953.4	3182.8	2730.9	3416.5	2771.2	3305.5	3134.7	3854.3	4522.5	5783.9	7872.2	5232.8
%	11	4	14	13	16	15	22	18	20	20	23	27	29
Total:	23960.4	22260.3	22293.3	21145.9	21887.8	18586.7	14805.0	17135.6	19218.5	22158.9	25675.3	29142.4	18102.8

* January-July 1992.

Source: Central Bureau of Statistics, Indonesia.

Appendix 2.6

INDONESIA: EMPLOYMENT BY SECTOR, 1971-1991
(In Thousand)

	1971	1976	1978	1980	1982	1985	1986	1987	1988	1989	1990	1991
Agriculture	24.936	29.117	31.545	28.834	31.593	34.142	37.644	38.722	40.475	40.640	41.604	39.038
(%)	66.27	61.55	60.92	55.93	53.99	48.22	55.09	55.00	55.80	55.11	54.82	51.51
Mining & Quarrying	80.000	113.000	123.000	387.000	391.000	416.000	-	-	-	554.000	708.000	527.000
(%)	0.21	0.24	0.24	0.75	0.67	0.59	-	-	-	0.75	0.93	0.70
Manufacturing	2.573	3.968	3.856	4.680	6.022	5.796	5.606	5.816	6.260	7.805	8.119	8.644
(%)	6.84	8.39	7.45	9.08	10.29	8.19	8.20	8.26	8.63	10.58	10.70	11.41
Electricity, Gas & Water Supply	35.000	27.000	13.000	66.000	62.000	70.000	-	-	-	104.000	131.000	142.000
(%)	0.09	0.06	0.03	0.13	0.11	0.10	-	-	-	0.14	0.17	0.19
Construction	640.000	815.000	806.000	1.657	2.146	2.096	-	-	-	1.895	2.057	2.499
(%)	1.70	1.72	1.56	3.21	3.67	2.96	-	-	-	2.57	2.71	3.30
Trade	4.077	6.814	7.708	6.679	8.554	9.345	9.756	10.461	10.328	10.894	11.069	11.934
(%)	10.84	14.40	14.89	12.96	14.62	13.20	14.28	14.86	14.24	14.77	14.59	15.75
Transport & Communications	901.000	1.284	1.288	1.468	1.796	1.958	-	-	-	2.263	2.365	2.377
(%)	2.39	2.71	2.49	2.85	3.07	2.77	-	-	-	3.07	3.12	3.14
Banking & Other Fin. Intermediaries	87.000	94.000	43.000	302.000	113.000	250.000	-	-	-	371.000	467.000	598.000
(%)	0.23	0.20	0.08	0.59	0.19	0.35	-	-	-	0.50	0.62	0.79
Services	3.870	5.047	6.395	7.144	7.125	8.317	10.018	11.199	11.161	9.215	9.228	9.819
(%)	10.28	10.67	12.35	13.86	12.18	11.75	14.65	15.91	15.39	12.50	12.16	12.96
Others	429.000	26.000	3.000	335.000	712.000	8.414	5.313	4.201	4.314	2.000	141.000	204.000
(%)	1.14	0.05	0.01	0.65	1.22	11.88	7.77	5.97	5.95	0.00	0.19	0.27
Total:	37.628	47.305	51.780	51.552	58.514	70.804	68.337	70.399	72.538	73.743	75.889	75.782

Appendix 2.7

INDONESIA: GROSS DOMESTIC PRODUCT, 1975-1991

	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
GDP (Current Price, Billion Rupiah)	12642.7	15466.7	19010.7	22746.0	32025.4	45445.7	57126.2	62475.7	77622.8	89885.1	96996.8	102682.6	124816.9	142104.8	167184.7	196919.3	227162.8
GDP (Constant Price, Billion Rupiah)	7630.8	8156.3	8870.9	9586.5	10164.9	11169.2	12054.6	12325.4	12842.2	83037.4	85091.9	90080.5	94517.8	99981.4	107436.5	115110.0	122705.0
Exchange Rate (US$/Rp.)	415.00	415.00	415.00	441.25	624.98	626.90	631.70	661.56	914.23	1031.40	1117.00	1293.59	1649.34	1688.50	1772.50	1845.05	1951.60
GDP (Current Price, Million US$)	30464.41	37269.16	45808.92	51549.01	51242.28	72491.59	92021.47	94436.94	84905.11	87145.25	86836.88	79378.01	75676.88	84160.38	94321.41	106728.44	116398.24

1975-1983 = Based on constant price 1973.
1984-1991 = Based on constant price 1983.

Chapter 3

EXPORT PROMOTION STRATEGIES: KOREA[1]

by

Wook-Joong Kim

I. Introduction

Korea was a typical underdeveloped country with poor natural resources and industrial base when it launched its economic development plan. Furthermore, the Korean War (1950-1953) had devastated existing industrial facilities and Korea was under heavy pressure from the rapid increase in population growth. Thus, a vicious circle of poverty persisted as a result of the small domestic market and poor investment. In an effort to break free from this trap, the Government initiated a series of "Five-Year Economic Development Plans", giving first priority to economic development through industrialization. Today, the history of Korean economic development is widely regarded as being outstandingly successful in that Korea achieved one of the highest economic growth rates in the world over the last three decades and that Korea's rapid development during the period has been export-led.

In the post-war period, many developing countries including Korea adopted a policy of import substitution as an industrialization strategy. In countries where this policy was emphasized, exports were usually discouraged by an overvalued exchange rate, which profited domestic sales relative to exports. The domestic production of manufactured goods was protected by various measures including high tariffs, import licenses, quantitative restrictions and other controls. But in the case of Korea, the phase of import substitution did not last long, because the domestic market was not sufficient to maintain a newly-developing industry, and import substitution could not obtain the foreign exchange needed to finance the imports of raw materials and capital goods which Korea needed in the course of economic development.

Therefore, Korea's growth has been based on industrial development with a large proportion of its products being exported

1. The views presented here are those of the author and do not necessarily reflect the position of the Bank of Korea.

to outside markets. In short, the influence of exports on Korea's economic growth was exerted mainly through the growth of the industrial sector as a result of the rapid expansion of exports.

A strongly export-oriented economy, such as Korea's, is very sensitive to shifts in the world economic environment. In the 1960s, Korea's exports managed to grow rapidly on account of the increase of import demand in the advanced countries and the reduction or abolition of tariffs under the GATT and GSP systems. Later, Korea suffered severely from the two oil crises in the 1970s and was affected by the world economic recession and recovery in the 1980s. Given the foregoing international factors, the Government adopted a growth strategy through export promotion and introduced various policy measures which encouraged international trade and created a favorable economic environment for export promotion. Most of all, it inspired and maintained the nation-wide export drive.

A brief survey of these policies and their roles constitutes the main part of this paper.

II. Export Trade and Salient Features

2.1 Growth Trend and Changing Patterns of Exports

2.1.1 Growth Trend of Exports

Korean exports increased at an annual average rate of 22.6 percent during the period of 1972-1992. In terms of value, exports rose from US$ 1.1 billion in 1971 to US$ 76.6 billion in 1992. Notably, during the third economic development plan period (1972-1976), exports rose at a remarkably fast pace of 49 percent annually in spite of the first oil shock. The rapid increase of wages in the manufacturing sector coupled with the second oil shock worsened the competitiveness of Korean labor-intensive light industry and slowed the pace of exports down to 10.3 percent during 1982-1986, even though it remained among the fastest growth rate in the world and has brought about considerable changes in Korea's export structure.

2.1.2 Changing Patterns of Exports

2.1.2.1 Export Structure by Commodities

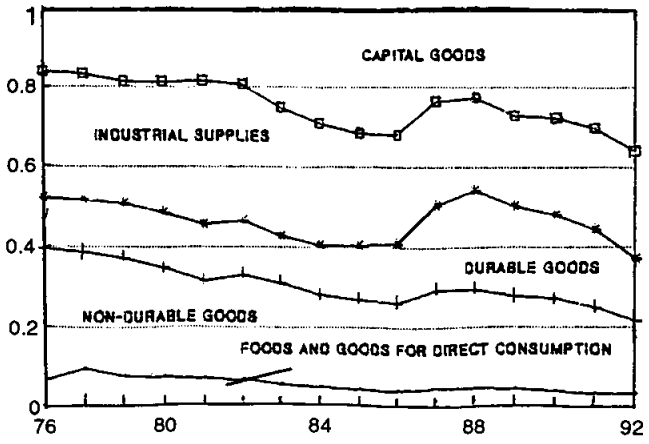
Korean exports, heavily dependent upon primary commodities at the early stage of economic development, show a typical trend of industrialization in their structure. Table 3.1 shows that the increase of Korea's exports was mainly due to the continuous growth of exports of manufactured products. Initially, light industry grew very fast, making use of cheap and abundant labor supply, and later heavy and chemical industry became the leader of export growth. By end-use, Korea's exports show that consumer goods are losing their share in total exports while capital goods are gaining on a relative term. The share of non-durable consumer goods in total exports, which was above 30 percent in the 1970s, showed a downward trend throughout the 1980s. Today, durable consumer goods showed a downward trend in Korean total exports, which had increased remarkably during 1986-1988.

In contrast, exports of capital goods and industrial materials, which had increased steadily in the early 1980s and experienced relatively low increase rates during 1986-1987, are now expanding rapidly due to demand from developing countries including those in South-East Asia.

Table 3.1
EXPORT STRUCTURE BY COMMODITIES BY INDUSTRY
(Share in Total Exports, Percent)

	Primary Commodities	Light Industry Products	Heavy and Chemical Products
1972	12.1	66.6	21.3
1982	8.1	45.0	46.9
1987	7.1	43.8	49.1
1988	6.1	41.8	52.1
1989	5.8	42.0	52.2
1990	5.3	41.1	53.6
1991	6.1	37.8	56.1

Chart 3.1
EXPORT STRUCTURE BY COMMODITIES
(By End-Use)



2.1.2.2 Export Structure by Region

Korea's exports have long been dependent upon the U.S.A. and Japan. Today, Korea is a major trading country and has trading partners throughout the world and will continue to make efforts to diversify its export markets. In the late 1970s, when Korea was suffering from the oil shocks, exports to the Middle East countries whose purchasing power had grown remarkably were very helpful to the Korean economy. In recent years, the export share of SouthEast Asian countries has been rising rapidly due mainly to the rapid growth of their economies and the region has emerged as the second largest market for Korean exports after the U.S.A.

The rapid development of Korea can be illustrated in many ways. For example, the country's imports rose faster than its exports in the early stage of industrialization because Korea lacked natural resources and the import of capital goods was essential for the construction of an industrial base. The ratio of exports to imports (customs clearance base) was below 50 percent until the early 1970s. Thereafter, exports grew remarkably and the export/import ratio rose to 93 percent in 1977

Table 3.2
EXPORT STRUCTURE BY REGION
(US$ Billion)

	U.S.A.	Japan	E.C.	S.E.A.	Others	Total
1980	4.6	3.0	2.6	2.3	5.0	17.5
1982	6.2	3.4	2.8	2.5	6.9	21.9
1984	10.5	4.6	3.2	3.1	7.9	29.2
1986	13.9	5.4	4.3	3.5	7.6	34.7
1988	21.4	12.0	8.1	7.8	11.4	60.7
1989	20.6	13.5	7.4	8.9	12.0	62.4
1990	19.4	12.6	8.8	10.4	13.8	65.0
1991	18.6	12.4	9.7	13.9	17.3	71.9
1992	18.1	11.6	9.3	17.1	20.5	76.6

and 117 percent in 1988. But Korea's trade balance remained in deficit almost every year. Moreover, Korea's trade in services has also shown a continuous deficit except for some periods, such as the construction boom in the Middle East and the 1988 Olympic Games.

As a result of such recurrent deficit in the current account, Korea has been actively inducing foreign capital. Long-term capital inflow through foreign direct investment and long-term borrowings were encouraged to acquire advanced technologies and funds required to develop the nation's industries.

These inflows, however, increased Korea's external debt to US$ 46.8 billion in 1985, imposing a heavy burden on the Korean economy. But the current account surplus during 1986-1989 brought a considerable slowdown in the external debt as measured by the volume of net external debt and the debt service ratio.

2.2 Contribution of Exports to the Economy

There being no other options, Korea has to adopt some form of export promotion policy as an economic development strategy because of its lack of sufficient domestic markets or material resources. During the last three decades, exports have been considered one of the most important indicators of economic development.

Charts 3.2 and 3.3 show the growth trend of exports and GNP of Korea and the proportion of exports to GNP. Korea's exports have grown at a much faster rate than GNP. In the early 1960s, exports remained below 6 percent of GNP, but the continuous rapid growth of exports has brought the figure up to around 37 percent in 1987.

CHART 3.2

KOREA: EXPORTS AND GNP GROWTH

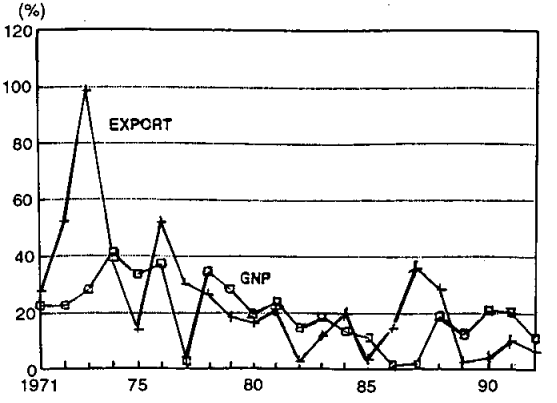
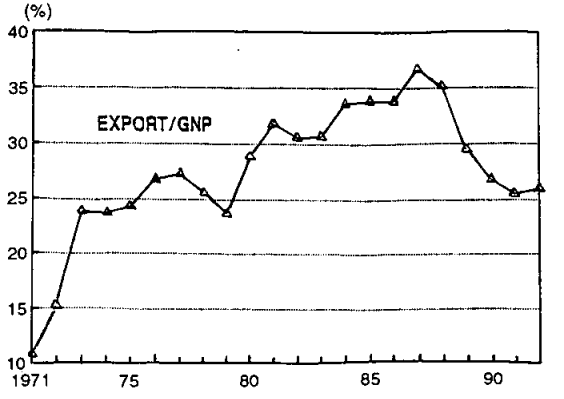


CHART 3.3

PROPORTION OF EXPORTS TO GNP



As a matter of fact the rapid growth of exports was the engine of economic development and also led to the dramatic growth and structural changes in production, employment and imports, etc.

2.2.1 Production

Exports of any one industry generally induce an increase of production in every sector throughout the economy as well as within the industry itself. I/O (Input/Output) analyses have demonstrated the effect of exports on production as shown below.

	1970	1975	1980	1985	1990	1991
Export-Induced Production / Export (times)	1.73	1.87	1.96	1.95	1.91	1.92
Export-Induced Production / Total Production (%)	9.0	21.9	23.2	26.3	23.2	22.5

Source: KFTA, Export and National Economy, various issues.

In 1970, exports caused domestic industrial production by only 1.73 times of their own volume and production induced by exports explained just 9 percent of total production. But with the growth and structural change of exports, their effects on the economy also strengthened. The share of export-induced production in total production rose above one quarter in 1985 and still remains above 20 percent, despite a decline which is in line with the expansion of domestic demand and consumption in recent years.

2.2.2 Employment

From the aspect of employment, the production of exportable goods means an additional need for labor. Thus, the share of employment induced by exports in total employment reached 18.4 percent in 1988 as against 13.9 percent in 1975 due mainly to the growth of labor-intensive light industry. The growth of heavy industry and the service sector, however, lowered the ratio to 13.6 percent in 1991. But, as a whole, the rapid growth of exports contributed to the low unemployment rate of Korea.

2.2.3 Imports

Industrialization and hence, the growth of exports leads to the import of raw materials and capital goods. It also creates demand for consumer goods through the increase of incomes. In the case of Korea, imports increased more rapidly than exports due mainly to the heavy dependence on imported capital goods and raw materials needed for its industrialization. As a result, imports induced by exports rose as much as 37.2 percent of the amount of exports in 1985 as against 35.0 percent in 1975, reflecting the growth of heavy industry highly dependent upon foreign raw materials and capital goods. But the increase of domestically availabile capital goods including components lowered the ratio to 31.9 percent in 1991.

2.2.4 Other Macroeconomic Variables

At the early stage of development, imports of capital goods and raw materials had to be financed by foreign capital because foreign exchange was not sufficient though it was almost completely under the control of the authorities. So net foreign reserve had remained insufficient until the trade balance shifted into surplus in 1986.

Thus, the foreign debt was one of the most serious problem until the mid-1980s but today, debt servicing is no longer a problem.

	1977	1980	1985	1987	1989	1991
Foreign Debt (US$ billion)	12.7	27.2	46.8	35.6	29.4	39.1
Debt Service Ratio (%)	10.1	14.4	18.6	30.1	9.8	4.6

2.3 Some Empirical Analyses

To find the empirical implication of exports in economic growth, the Granger Causality tests were conducted. In this paper, the quarterly time series data for the period 1981-I to 1991-IV with 4-quarter lags were used, both on the absolute level and the rates of change of GNP (or GDP) and export. The basic function and the null hypotheses of Granger Causality test are as follows:

2.3.1 Function

$$(1)\quad X_t = a_O + \sum_{i=1}^{m} a_I \times X_{t-i} + \sum_{j=1}^{n} b_j \times Y_{t-j} + u_t$$

$$(2)\quad Y_t = c_O + \sum_{i=1}^{r} c_i \times Y_{t-i} + \sum_{j=1}^{s} d_j \times X_{t-j} + v_t$$

2.3.2 Null Hypotheses

(1) X is not Granger-Caused by Y.

(2) Y is not Granger-Caused by X.

The results, as summarized below, show a positive feedback relationship between the (absolute level) GNP (or GDP) and export quantity. But the test results on the relationship between the rate of change show a strong one-way causality from the growth of export to the growth of GNP (or GDP).

2.3.3 Results

	X	Y	F-Statistic	Probability	Causality
Absolute Level	GNP	XQ	5.1222	0.0010	Yes
	XQ	GNP	5.6442	0.0005	Yes
	GDP	XQ	4.9646	0.0013	Yes
	XQ	GDP	5.7543	0.0004	Yes
Increase Rate	GNP	XQ	4.6072	0.0022	Yes
	XQ	GNP	2.1934	0.0778	No
	GDP	XQ	4.9315	0.0014	Yes
	XQ	GDP	2.3159	0.0650	No

The above causality test shows the export-led growth in Korea. So it is interesting to know the factors affecting export growth through the estimation of an export demand function. Generally, in a traditional export demand model, export (quantity) is a function of the foreign demand and the relative price level. In sum, relative price level shows the competitiveness of Korean exportable goods. As such, a simple equation can be specified as follows:

$$XQ_t = a + b \times FMQ_t + c \times RP_t + d \times XQ_t$$

XQ : Export quantity;
FMQ : Import quantity of trading partners; and,
RP : Relative price level (Korea's export price divided by the import price index of the advanced countries).

The equation is specified in natural logarithms with a view to measuring elasticities. The income elasticity, b, is expected to be positive while relative price elasticity, c, is to be negative. The import quantity of trading partners was calculated as the weighted average of the import quantity of the industrial countries and that of developing countries based on the regional composition of Korea's exports. A partial adjustment mechanism was assumed to get both short- and long-run elasticities. The seasonal dummy variables were used to capture the seasonal effects arising from the quarterly data.

The estimated results, as summarized below, suggest that foreign demand plays an important role in the growth of Korea's export.

$$\begin{aligned} LXQ_t = {} & -4.059 + 0.593\ LFMQ_t - 0.387\ LRP_t + 0.678\ LXQ_{t-1} \\ & (-1.47) \quad (1.97) \quad (-1.80) \quad (4.08) \\ & - 0.240\ D1 + 0.026\ D2 - 0.058\ D3 \\ & (-7.09) \quad (0.67) \quad (-1.71) \end{aligned}$$

$$R^2 / \bar{R}^2 = 0.964 / 0.958 \quad D.W. = 2.80$$

$$\begin{aligned} LXQ_t = {} & -14.638 + 1.761\ LFMQ - 0.586\ LRP - 0.179\ D1 \\ & (-13.38) \quad (16.52) \quad (-2.05) \quad (-5.25) \end{aligned}$$

$$+ 0.068\ D2 - 0.009\ D3$$
$$(-1.87) \qquad (-0.25)$$

$$R^2 / \bar{R}^2 = 0.949 / 0.941 \qquad D.W. = 2.17$$

III. Export Promotion Policies

To achieve economic growth by maintaining equilibrium both externally and internally, it is necessary for a developing country to keep a balance between export promotion and import control. With this perspective in mind, the trade policies of Korea are a mixture of both export promotion and import management. Nonetheless, more emphasis has been placed on export promotion as the engine of growth. The following is a brief survey of export promotion policies in Korea.

3.1 An Overview of Trade and Commercial Policy

After the introduction of the Five-Year Plans in the 1960s, the Government has introduced various incentives for the promotion of exports including financing, taxes, and tariffs. In order to understand Korea's export expansion since 1962, the leadership of Government in the case of "Nation Building by Export" could not be underestimated.

For example, the Government had held monthly sessions of the "Expanded Meeting for Export Promotion". These meetings were attended by high level government officials concerned with economic affairs, the presidents of major financial institutions and business associations, the top managers of leading export firms and trade associations, and experts on trade. They tried to identify the obstacles to export expansion and to provide workable prescriptions. In 1977, the "Expanded Meeting for Export Promotion" was reconstituted as the "Expanded Meeting of the Trade Promotion Committee" in accordance with the government emphasis on both exports and imports.

The Government provided not only close cooperation to all Korean exporters, but also offered merit medals for successful exporters on a regular basis. As a result, Korean exporters felt honored in contributing to national development. Moreover, this had an immense psychological impact in Korea because its society is imbued with the spirit of Confucianism.

Table 3.3

MAJOR INCENTIVES FOR EXPORT PROMOTION

	Type of Incentives	Duration
A.	Financial Incentives	
	1. Export financing	Feb.1961-
	2. Medium- & long-term financing for exports on deferred payment basis	Jul.1967-
	3. Financing for the supply of construction & other services in foreign currencies	Sep.1967-
	4. Local L/C system	Oct.1967-
	5. Financing to prepare agricultural & marine product exports	Nov.1969-
B.	Tax Incentives	
	1. Reduction of corporate income taxes on earnings from exports	Jan.1961-Dec.1972
	2. Accelerated depreciation allowance for fixed capital directly used for export production in mining, fishing & manufact'g	Jan.1968-
	3. Reserve funds deducted from taxable income to develop new foreign markets	Aug.1969-
	4. Reserve funds deducted from taxable income to defray export or foreign investment losses 1/	Mar.1973-
C.	Tariff Incentives	
	1. Tariff exemptions on capital equipment imports for export production	Mar.1964-Dec.1973
	2. Tariff exemptions on raw material imports for export production	Apr.1961-Jun.1975
	3. Tariff drawback on imported raw materials used for export production	Jul.1975-
D.	Others	
	1. Establishment of the Korea Trade Promotion Corporation (KOTRA)	
	2. Establishment of the Korea Exchange Bank	Jan.1967-
	3. Export insurance 2/	Jan.1969-
	4. Introduction of general trading companies	Apr.1975-
	5. Establishment of the Export-Import Bank	Jul.1976-

1/ Importers of materials which were later used for foreign exchange earning activities but on which tariffs had already been paid could get a refund.

2/ "The Export Insurance Law" was promulgated in December 1968 in order to protect exporters from risks. The insurance covers 70 to 90 percent of the loss.

The prestige and encouragement bestowed on exporters have undoubtedly helped channel the best of Korean businessmen into export activities. The Minister of Commerce and Industry (MCI) had set annual and monthly export targets at the beginning of each year and stepped up efforts to attain them. Furthermore, in the mid-1970s, the Government continued to introduce additional measures to help promote exports in the long run. For example, from the lesson of the Japanese experience, the Korean Government adopted the system of general trading companies in 1975. The need for specialized trading companies was felt because of the lack of efficiency of small-scale individual sales techniques in the international markets and the tendency of Korean exporters to depend upon Japanese general trading companies.

3.2 Monetary Policy Measures and Exchange Rate Policy

3.2.1 Export Financing System

The export financing system in Korea has been one of the most effective means of switching resources from domestic to export use through the provision of automatic access of credit. The scope of export financing includes all categories of finance in the process of export activities, such as loans for preshipment production activities such as domestic purchases and the importation of raw materials for export. Likewise, it comprises not only the credits based on the master L/C but also "local L/Cs", which are uniquely regarded as "domestic exports" constituting essential components of exports. To check the misuse of the fund by beneficiaries, an extensive follow-up process has been provided.

Eligible exporters benefit by automatic access to export financing and this is underpinned by the central bank rediscount facility. Moreover, the export credits are extended at substantially lower interest rates than other domestic commercial loans. Furthermore, borrowing procedures for export financing are simpler in comparison to other loans (see Appendix 3.1).

After the mid-1960s, the various kinds of financing for export promotion had been put in place, and the system certainly played an important role in facilitating export-led growth. In most developing countries, where financial markets are not fully developed, exporters have to face a lot of problems for automatic access to financial facilities

at both pre- and post-shipment stages. Therefore, Korea, which suffered from a continuous and absolute lack of available funds, needed an export promotion system in the financial sector to establish a competing environment with that of the advanced countries.

From such a viewpoint, the export promotion system including export financing was designed to provide certainty, stability, and automatic credit accessibility. In addition, there are export insurance schemes under the Export Insurance Law, promulgated in December 1968 in order to protect exporters from risks. The insurance covers 70 to 90 percent of the exporters loss. Today, this system mainly supports mid- and long-term deferred payment risk by the Korea EXIM Insurance Corporation which was established in 1992 with the initiation of the Korea EXIM Bank.

3.2.2 Exchange Rate Policy

The exchange rate arrangement of Korea has been changed on many occasions in consideration of the country's economic situation. In February 1980, a multiple-basket pegged system was introduced in place of the unitary exchange rate system. The present market average exchange rate system has been in effect since March 1990. A brief summary of Korean exchange rate regimes is presented below.

There was a unitary fluctuating exchange rate system in Korea in the 1970s. The economy, foreign trade and the domestic market were still very small and, moreover, Korea's trading commodities and trade counterparts were not fully diversified. By the late 1970s, the sharp increase in domestic price levels due mainly to soaring international prices of raw materials, especially crude petroleum, and excess of domestic demand led to a serious overvaluation of the Korean won when it was linked to the U.S. dollar. The exchange rate of the won against other major currencies oscillated severely, reflecting the movements of the currencies in the international market. Furthermore, in practice, the won/dollar exchange rate in the system was virtually fixed so that it could not reflect the market situation at the right time, and the side effects of lagged adjustments were inevitable.

Therefore, in consideration of the growth and diversification of Korea's economy and foreign trade, a multiple-basket pegged system was introduced on February 27, 1980. The exchange rate of the won

Table 3.4

MAJOR STEPS IN RELAXING FOREIGN EXCHANGE CONTROL

Enforcement of market mechanism in determining exchange rate	o Introduction of a market-average exchange rate (MAR) system (March 1990) o Widening of the range of daily exchange rate fluctuations from an upper or lower limit of 0.4% to 0.6% (September 1991) and again to 0.8% (July 1992)
Liberalization of foreign exchange payments for current transactions	o Raising of the basic ceiling on overseas travel expenses (December 1987) o Expansion of the limit on residents' remittances (November 1988) o Acceptance of the obligations of Article VIII of the IMF Agreements (November 1988)
Relaxation of foreign resident's exchange concentration system	o Exemption of amount to US$ 5,000 from concentration obligation (November 1988) o Raising of the ceilings on the overbought positions of foreign exchange banks (September 1989
Development of foreign currency call market	o Establishment of U.S. dollar call market (December 1989) o Introduction of yen market (May 1991) and DM market (September 1992)
Internationalization of the won	o Permission for export or import contracts denominated in won (November 1988) o Permission for invisible contracts denominated in won (September 1991)

was linked to multiple-baskets, i.e., a trade-weighted basket and the SDR basket, and adjusted according to market condition. This system, which was continued for a decade, also revealed its own limitations as the growth of the Korean economy and the liberalization of the overall economy proceeded. Moreover, it could not fully account for

the economic fundamentals and the demand-supply situation of the domestic foreign exchange market.

So a market average exchange rate(MAR) system was introduced as a transition towards the early adoption of a free float system. Under this system, the Bank of Korea is no longer involved in determining or posting exchange rates. The daily basic won-dollar exchange rate is determined as the weighted average of the interbank won-dollar exchange rates applied in spot transactions on the previous business day, and the basic exchange rates of the Korean won against other foreign currencies are calculated by arbitrating between the U.S. dollar rates of respective currency in the international market and Korean won rate against the U.S. dollar. One of the notable characteristics of the MAR system is that each foreign exchange bank is independent to decide its own customer rates, reflecting its view of the market situation. As a preparation of a free float, the daily fluctuation band of the exchange rate has been widened step by step up to ± 0.8 percent (August 1992) of the basic rate from ± 0.4 percent when the system was introduced, and is expected to widen to ± 1.0 percent in 1993.

These developments in exchange rate arrangements reflect a gradual liberalization and internationalization of the Korean economy and have played an important role at every stage of economic development. Since the exchange rate is an interface between the domestic economy and the external environment, it directly influences the profitability of tradable goods. As such, exchange rate policy has been an important part of Korea's export promotion measures.

The value of the won in dollar terms had decreased only fitfully but fell steadily under the multiple-basket pegged system until the mid-1980s. This aided Korea's exports which increased considerably. In contrast, the strong appreciation of the Korean won against the U.S dollar from the mid-1980s, caused by the current account surpluses and the weakness of the U.S dollar in international markets, weakened the competitiveness of Korean exports which contributed to the deterioration of the trade balance in recent years. However, Korea's exchange rate system currently represents a price mechanism reflecting the current economic situation and market information so that it is expected to be efficient and neutral.

3.3 Fiscal Policy Measures

Fiscal policy measures to promote exports can be divided into three categories; namely a favorable tariff system, tax incentives, and administrative support. The following is a brief introduction to Korea's fiscal policy measures.

3.3.1 Tariff Incentives

Tariff incentives for export promotion can be implemented on all imports of export-related goods. There had been tariff exemptions on imports of capital equipment and raw materials for export production before the mid-1970s. But in line with GATT, only the tariff drawbacks on raw materials imported for export production was introduced in 1975 in place of the previous tariff exemptions. As a result, Korea has few incentives for export promotion in terms of tariffs, but there is advantage in importing raw materials for export purposes rather than domestic consumption.

3.3.2 Tax Incentives

Tax incentives for exporting firms can be provided through direct and indirect taxes. Incentives on direct taxes in Korea has been dependent mainly upon indirect methods since the 1970s, though they are less effective than direct ones. However, the direct methods could be countervailed by the importing countries.

3.3.3 Administrative Support

Administrative support for the export business also served as an effective supplementary policy instrument in Korea. As mentioned above, the monthly export-promotion conference was itself an important administrative support mechanism. Since the meeting was attended by all important public officials and private experts concerned with international trade, it provided a forum for revising and extending administrative support in various forms. It also served as an excellent forum for the exchange of information among policymakers, businessmen and economic experts.

Those attending the monthly meeting included the president's chief economic secretary, the Minister of Economic Planning Board, the Minister of Commerce and Industry, the Director of Korea Trade Promotion Agency, and the Chairman of Korea Traders Association which

was renamed as the Korea Foreign Traders Association in 1988. The meeting conducted almost monthly picked out some businessmen as successful exporters and commended them with citations. According to Song (1990), such social recognition was a very effective motivation.

3.4 Institutions and Facilities for Export Promotion

3.4.1 Financial Institutions

Almost every banking and development institution in Korea participates in export financing. Among them, the Export-Import Bank of Korea (EXIMBANK) and Korea Development Bank (KDB) are the major institutions involved in foreign trade and industrial development.

3.4.1.1 EXIMBANK

The Export-Import Bank of Korea is a special government financial institution established in 1976 under the Export-Import Bank of Korea Act to provide medium- and long-term credits for export and import transactions, overseas investment, etc. The bank also extends credits to foreign governments and individuals to help finance their imports from Korea.

The bank has also been operating its export insurance business since 1977 on behalf of the Korean Government. It also took over the management of the Economic Development Cooperation Fund (EDCF) as entrusted to it by the Government, on June 1, 1987.

Table 3.5
CREDIT COMMITMENTS & LOAN DISBURSEMENTS BY EXIMBANK
(Million Won)

	Credit Commitments		Loan Disbursements	
	1990	1991	1990	1991
Export Credits	622,548	906,224	484,385	824,857
Industrial Plant	7,742	82,545	8,062	30,388
Ships	590,553	790,485	466,235	771,527
Machinery & Others	24,253	33,194	10,088	22,942
Relending Facility	556	365,672	556	168,469
Import Credits	161,821	205,225	120,141	197,803
Overseas Investment Credits	146,539	93,109	140,079	99,969
Total:	931,464	1,570,230	745,161	1,291,098

Source: EXIMBANK, Annual Report, 1991.

3.4.1.2 Korea Development Bank

Since its establishment in 1954 under the Korea Development Bank Act, the Korea Development Bank (KDB), as the main long-term equipment financing bank, has played an important role for the successful implementation of industrialization in Korea.

Working towards upgrading the nation's industrial structure, the Bank provides medium- and long-term loans and/or payment guarantees for the development of key sectors such as export, heavy and chemical industries, and the issuance of special bonds.

The major financial activities of the KDB are classified as follows:

- loans with longer than one-year maturity,
- investment in the form of underwriting of corporate bonds and stocks, and
- payment guarantees to help finance industrial projects.

3.4.2 General Trading Companies

A scheme for general trading companies(GTCs) following the model of Japanese GTCs was introduced in 1975 to speed up export expansion. By 1976, the Government had designated 13 GTCs, 5 of which have since lost their GTC status.

The most important feature of the GTC scheme was its in-built mechanism, i.e., the GTCs should try to expand their exports to maintain their qualifications and to compete with each other. To be designated as a GTC in Korea, the share of a business firm exports in each calendar year should be more than 2 percent of the total exports of Korea. If an existing GTC fails to meet this requirement in two consecutive years, its designation is cancelled.

GTCs have accounted for a large portion of Korea's exports; in 1980, 41 percent of Korea's total exports were handled by ten GTCs, while 42.5 percent of the total exports were handled by eight GTCs in 1991. However, there is much room for improvement because the GTCs in Korea are still lagging behind the Japanese GTCs in terms of size, information-gathering ability and overseas marketing strength, etc.

3.4.3 Other Institutions

3.4.3.1 Korea Trade Promotion Corporation

Before the introduction of the first Five-Year Economic Development Plan, no organizations were capable of implementing export marketing programs. Since then, the Korea Trade Promotion Corporation (KOTRA) was financed and established by the Government as a non-profit organization to facilitate the promotion of the export trade.

Making full use of its overseas network facilities, KOTRA has to locate potential buyers for Korean products and to match them with potential suppliers. Up-to-date information on overseas opportunties has been collected and distributed to the domestic sector continuously.

In recent years, with growing exports, KOTRA has extended the scope of its activities from just focusing on introducing potential business partners to supporting various economic cooperation with developing countries concerned with imports and overseas investment.

3.4.3.2 Korea Foreign Trade Association

Korea Foreign Trade Association (KFTA) is a private, non-profit organization established in 1946 under the name of Korean Traders Association (KTA). As a major business organization in Korea, it promotes international trade, and it has nation-wide membership of more than 30,000 companies. Under the Foreign Trade Act and the relevant laws and rules, those companies or individuals who want to engage in export-import business are required to be a member of KFTA for the registered foreign traders.

In 1972, KFTA joined the world-wide network operating under World Trade Centers, and thus, it is also known as the Korea World Trade Center (KWTC). The KFTA and its World Trade Center complex have provided a wide range of services related to the promotion of exports, international trade such as trade information services, trade inquiry services, and research activities.

IV. Problems and Issues on Export Promotion

Recently, the world economic environment has became uncertain and perhaps unfavorable for a developing country whose economy is dependent upon exports. Simultaneous recessions in the industrial countries have shrunk world trade. Protectionist sentiment in the advanced countries and emerging competitors among the developing countries have made it difficult for Korea's exports to maintain their past pace. Moreover, the Uruguay Round negotiations and spreading economic regionalism are having a tremendous impact on an export-oriented country like Korea. As a result, Korea experienced a sudden deterioration in its current account from a surplus of US$ 14.2 billion in 1988 to a deficit of US$ 8.7 billion in 1991.

The trade deficit was reduced to a deficit of US$ 4.6 billion in 1992 from a deficit of US$ 7.0 billion in the previous year due to a

Table 3.6

EXPORTS TO THE ADVANCED COUNTRIES 1/
(US$ Billion, %)

	Amount	Share in Total Exports	Rates of Increase	Contribution Rate
1980	10.3	58.7	32.9	103.6
1981	11.9	55.8	15.5	42.5
1982	12.5	57.1	5.2	102.1
1983	14.7	60.0	17.7	85.4
1984	18.3	62.5	24.6	75.2
1985	18.5	60.9	0.9	15.4
1986	23.6	68.0	27.9	116.3
1987	33.3	70.5	41.2	77.5
1988	41.5	68.5	24.6	61.1
1989	41.5	66.6	-0.1	-3.0
1990	40.8	62.8	-1.6	-24.6
1991	40.6	56.5	-0.5	-2.9
1992	38.9	50.8	-4.2	-35.7

1/ U.S., Japan and E.C.

slowdown in imports in 1992. Exports, however, have also remained relatively down in the recent years compared to the rapid increase during the mid-1980s. This suggests that Korean exports are losing their competitiveness while other competitors are making considerable headway despite the slowdown in foreign demand. Moreover, this improvement in the trade balance involves some problems as Korea is basically aiming at economic development through an expanded equilibrium. Among a number of issues in the export sector, the most urgent ones are the structural changes in exports by destination and the increasing imbalances in exports by industry.

First, the pattern of Korea's export market is undergoing a structural change. At the beginning of the 1980s, the advanced countries (U.S., Japan and E.C.) accounted for 58.7 percent of Korea's total exports and this proportion rose steadily to 70.5 percent in 1987. But it started to decrease in 1988 and has since fallen to 50.8 percent in 1992. This may be a diversification of the export market, and the serious implication is that exports to the advanced countries no longer contribute to the growth of total exports, but have dampened it since 1989.

Second, traditional export-oriented industries including apparel, footwear and electric household appliances continue to exhibit unsatisfactory or even negative trends while textile fabrics and semiconductors are currently the main thrust in total export growth. This reflects the change in the structure of comparative advantage caused by the upsurge of domestic manufacturing costs and changes in international environment.

Third, the export values, upon which the monetary, fiscal, and other promotion incentives were calculated, were expressed in gross terms rather than net terms. Furthermore, imports of raw materials for re-exports were given liberal wastage allowances, while imports of final consumption goods were tightly controlled. These policies, in effect, gave exporters tremendous incentives to import and process semi-finished intermediate goods, utilizing economies of scale, while there were few incentives to produce intermediate goods themselves. So the technologies developed were concentrated on assembling and processing of semi-finished goods. The export promotion strategies in the 1970s, thus, contributed to the growth of exports but were detrimental to the development of small- and medium-sized firms and the semi-finished goods. The profitability of Korean exporting firms is

also changing for the worse, dropping even below that of domestic sales because export unit values remain stable over time while domestic manufacturing costs are increasing continuously.

The above analyses indicate that export promotion in Korea is in need of structural realignment and qualitative upgrading.

V. Policy Recommendations

Today, any artificial bias to promote exports is irrelevant to Korea because it is internationalizing and liberalizing its overall economy as a member of the international community. Furthermore, the efficient allocation of economic resources through enhancing the role of the market is one of the most important issues in Korea and the process of deregulation and liberalization in individual sectors of the economy implies that entrepreneurs must learn to stand on their own feet.

For example, Korea adopted the Market Average Exchange Rate System as an intermediate stage towards a free float system, and so the control of the exchange rate is no longer in use as a tool to achieve a specific political goal. The trends of financial and foreign exchange deregulation are minimizing the role of administrative measures unlike in the past.

Firstly, Korea needs to enhance the economic cooperation with its neighboring countries. Korea is well on track towards an industrial country and other Asian countries are also developing rapidly. Economic cooperations between Korea and other countries in the region will help to maximize the benefit from international division of labor or specialization for all the countries concerned.

Secondly, Korea should give top priority to emerging industries to further enhance its competitiveness and seek to develop other new areas where the international comparative advantage could be higher.

But this could not be achieved by any mandatory measures or through unilateral government initiatives. In the early stages of development, the Government took the lead in establishing broad development goals for society, in providing a proper business climate for the private sector, and in mobilizing domestic and foreign resources for investment and developing the infrastructure. But, as the economy

grows, extensive government intervention becomes self-defeating and decentralized decision-making becomes the most effective means of achieving the efficient allocation of resources. In other words, individual business firms should take the initiative and the Government to take on the mission of guiding and harmonizing the overall process.

VI. Summary and Conclusion

In Korea, as in the case of many other developing countries, exports have contributed greatly in economic development overtime. In fact, the on-going export promotion strategies of the Government have played a critical role in Korea's economic development.

Given recent changes in the international and domestic circumstances, however, these policies have to be realigned and practical measures employed should be revised. The most successful adjustment scenario in Korea to changes in the international economic environments will materialize only when the economy is firmly based on free market principles and the initiative efforts of individual entrepreneurs. A deeper and more extensive analysis and a constant interchange of ideas are needed for the purpose of further enhancing economic development.

REFERENCES

1. The Bank of Korea, ***Financial System in Korea***, December 1990.

2. _____, ***Economic Statistics Yearbook***, various issues.

3. _____, ***Monthly Balance of Payments***, various issues.

4. Das, Dilip K., ***International Trade Policy: A Developing Country Perspective***, 1990.

5. Hong, Won Tack, and Krueger, Anne O., ***Trade and Development in Korea***, 1975.

6. IMF, ***International Financial Statistics***, various issues.

7. International Trade Centre UNCTAD/GATT, ***The Export Performance of The Republic of Korea***, 1984.

8. Korea Foreign Trade Association, ***The Statistics of Foreign Trade***, 1991.

9. Lee, Chang-Kyu, ***A Study on Export Financing in The Republic of Korea***, The Bank of Korea, 1985.

10. Luedde-Neurath, Richard, ***Import Control and Export-Oriented Development: A Reassessment of the South Korean Case***, 1986.

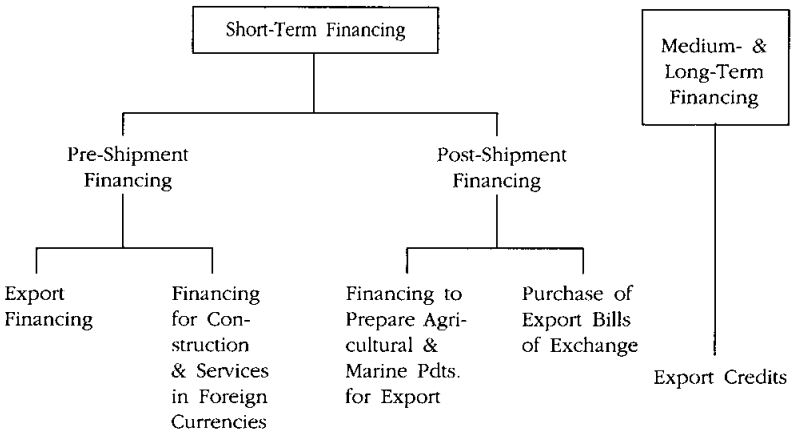
11. Song, Byung-Nak, ***The Rise of The Korean Economy***, Oxford University Press, 1990.

KOREA: EXPORT FINANCING SYSTEM

In general, when we refer to "export financing system" it may include all the financing schemes which provide traders with necessary funds at every stage of internal or external transactions related to export. The Korean financing system for exports is characterized by the provision of loans for pre-shipment production activities as well as financing for the period between shipment and collection of payments. It can be divided into two categories by the period of financing. The first is short-term financing where the period of financing is within 180 days and which is dealt with foreign exchange banks. The other is medium- and long-term financing where the period of financing is over 180 days and this is handled by EXIM Bank.

The present export financing system can be shown as follows (as of December 1992):

STRUCTURE OF EXPORT FINANCING SYSTEM



Among these, details of 'export financing' to facilitate exports by providing loans and guarantees for exporters are as follows:

(1) Eligibility of Borrowers

(a) Exporters with irrevocable export L/Cs;
(b) Exporters with D/P or D/A contracts;

(c) Producers of finished goods or raw materials for export who receive local L/Cs; and,
(d) Exporters with export performance.

(2) Type of Loans

(a) Loan for importing intermediate inputs: raw materials import fund;
(b) Loan for generating value-added: production fund;
(c) Loan for purchase of domestic intermediate inputs: raw materials purchase fund; and,
(d) Loan for overall purchase: overall purpose fund.

(3) Amount of Loans
(In case of loans based on export L/C)

(a) Loans for production:
LUP x Value-Added
* LUP is the Lending Unit Price and can be changed according to the economic situation
* Value-Added = The amount of export L/C in f.o.b. price - The amount of imports and domestic purchase of required raw materials in c.i.f. price

(b) Loans for import of raw materials:
LUP x The Amount of the Import Bill

(c) Loans for domestic purchase of raw materials:
LUP x The Amount of Bill Issued on Local L/C

(4) Credit Line Based on Past Export Performance

(a) Loans for production:
Export Performance During 3 Months Previous to Application x 1/3 x The Average Value-Added Ratio of All Export Items of the Concerned Borrower,
(Converted into the local currency by LUP)

(b) Loans for raw materials:
Export Performance During 1 Year Previous to Application x 1/3 or Export Performance During 3 Months Previous to Application x 1.5 x The Average Raw Materials Requirement Ratio of All Export Items of the Concerned Borrower,
(Converted into the local currency by LUP)

(5) Loan Period

(a) Loans based on export L/C: Up to 180 days within the expiry date of the export L/C concerned
   * In cases authorized by The Bank of Korea (BOK), it can be extended up to 270 days.

(b) Loans based on past export performance: Up to 90 days
   * In cases authorized by BOK, it can be extended up to 135 days.

(6) Time of Extension of Loans

(a) Loans for production: After confirming that the required raw materials have been secured, i.e., after opening an import L/C or a local L/C.

(b) Loans for import of raw materials: At the time of the settlement of the import bills or the delivery of the shipping documents.

(c) Loans for domestic purchases of raw materials: At the time of the settlement of the bill issued against a corresponding local L/C.

(7) Refinance by BOK

BOK provides refinance at the interest rate of 7 percent per annum to lending banks for up to 50 percent of the loan amount they extend.

Appendix 3.2

STATISTICAL TABLE

YEAR	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982
CA	-622.5	-847.5	-371.2	-308.8	-2022.7	-1886.9	-313.6	12.3	-1085.2	-4151.1	-5320.7	-4646.0	-2649.6
EX	882.2	1132.3	1676.5	3271.3	4515.1	5003.0	7814.6	10046.5	12710.6	14704.5	17214.0	20670.8	20879.2
IM	1804.2	2178.2	2250.4	3837.3	6451.9	6674.4	8405.1	10523.1	14491.4	19100.0	21598.1	24299.1	23473.6
TB	-922.0	-1045.9	-573.9	-566.0	-1936.8	-1671.4	-590.5	-476.6	-1780.8	-4395.5	-4384.1	-3628.3	-2594.4
EXC	835.2	1067.6	1624.1	3225.0	4460.4	5081.0	7715.3	10046.5	12710.6	15055.5	17504.9	21253.8	21853.4
(INCREASE RATE)		27.8%	52.1%	98.6%	38.3%	13.9%	51.8%	30.2%	26.5%	18.4%	16.3%	21.4%	2.8%
IMC	1984.0	2394.3	2522.0	4240.3	6851.8	7274.4	8773.6	10810.5	14971.9	20338.6	22291.7	26131.4	24250.8
ITB	119.3	27.8	32.9	67.1	-308.3	-442.2	-71.8	266.0	224.0	-194.6	-1385.9	-1518.4	-554.2
ITP	377.5	455.9	517.4	782.3	1146.1	1322.8	1714.5	2761.0	4226.1	5020.8	6749.2	8116.5	8030.5
ITR	496.8	483.7	550.3	849.4	837.8	880.6	1642.7	3027.0	4450.1	4826.2	5363.3	6598.1	7476.3
LKA	501.0	512.0	521.0	666.3	946.4	1178.3	1371.2	1312.7	2166.3	2662.9	1856.5	2841.9	1230.3
SKA	122.4	134.6	-16.3	84.0	-45.4	679.5	356.5	21.4	-1171.0	843.6	1944.5	-82.3	3.6
OB	-4.2	-187.8	163.6	460.3	-1093.8	-150.6	1173.6	1314.7	-401.9	-973.3	-1889.6	-2297.0	-2711.2
GDP	24813	27113	28564	32432	35117	37621	42471	46749	51289	55182	53989	57615	61821
GDP1	2768	3421	4210	5420	7669	10302	14101	18074	24327	31323	38041	47482	54443
GNP	24973	27128	28505	32274	34904	37143	42002	46135	50646	54290	52261	55354	59322
GNP1	2785	3417	4191	5376	7597	10136	13913	17807	24002	30802	36750	45528	52182
(INCREASE RATE)		22.7%	22.7%	28.3%	41.3%	33.4%	37.3%	28.0%	34.8%	28.3%	19.3%	23.9%	14.6%
GNP(US$)	8967.67	9842.14	10667.6	13497.4	18783.5	20941.7	28745.2	36790.4	49590.0	63640.0	60500.3	66821.4	71342.8
(INCREASE RATE)		9.8%	8.4%	26.5%	39.2%	11.5%	37.3%	28.0%	34.8%	28.3%	-4.9%	10.4%	6.8%
ER	310.56	347.15	392.89	398.32	404.47	484.00	484.00	484.00	484.00	484.00	607.43	681.34	731.43
BUD	-51.3	-57.6	-209.1	-87.9	-168.0	-336.5	-157.8	-149.3	-49.9	116.9	-584.2	-1050.9	-712.6
PPI	0.0	0.0	0.0	0.0	0.0	32.2	36.1	39.4	44.0	52.2	72.5	87.3	91.4
CPI	0.0	0.0	0.0	0.0	0.0	24.6	28.4	31.3	35.8	42.3	54.5	66.2	70.9
EXPORT/ GNPD	0.09	0.11	0.15	0.24	0.24	0.24	0.27	0.27	0.26	0.24	0.29	0.32	0.31

1983	1984	1985	1986	1987	1988	1989	1990	1991	1992		
-1606.0	-1372.6	-887.4	4617.0	9853.9	14160.7	5054.6	-2179.4	-8727.7	-4604.9	CURRENT ACCOUNT BALANCE	(MIL. US$)
23203.9	26334.6	26441.5	33913.2	46243.8	59648.2	61408.7	63123.6	69581.5	75103.7	EXPORT (BOP BASIS)	(MIL. US$)
24967.4	27370.5	26460.5	29707.3	38584.8	48202.8	56811.5	65127.2	76561.3	77302.1	IMPORT (BOP BASIS)	(MIL. US$)
-1763.5	-1035.9	-19.0	4205.9	7659.0	11445.5	4597.2	-2003.6	-6979.8	-2198.4	TRADE BALANCE	(MIL. US$)
24445.1	29244.9	30283.1	34714.5	47280.9	60696.4	62377.2	65015.7	71870.1	76631.5	EXPORT (CUSTOMS CLEARANCE BASIS)	(MIL. US$)
	11.9%	19.6%	3.6%	14.6%	36.2%	28.4%	2.8%	4.2%	10.5%	6.6%	
26192.2	30631.4	31135.7	31583.9	41019.8	51810.6	61464.8	69843.7	81524.9	81775.3	IMPORT (CUSTOMS CLEARANCE BASIS)	(MIL. US$)
-434.6	-877.6	-1446.1	-627.5	977.4	1267.2	210.8	-450.6	-1595.5	-2710.2	INVISBLE TRADE BALANCE	(MIL. US$)
7613.3	8193.9	8110.5	8679.2	9032.6	9984.7	12430.8	14719.2	17124.9	18473.7	INVISBLE TRADE (DEBIT)	(MIL. US$)
7178.7	7316.3	6664.4	8051.7	10010.0	11251.9	12641.6	14268.6	15529.4	15763.5	INVISBLE TRADE (CREDIT)	(MIL. US$)
1270.4	2067.4	1100.8	-1981.9	-5835.8	-2732.8	-3362.5	547.5	4185.8	7040.8	LONG-T. CAPITAL ACCOUNT BALANCE	(MIL. US$)
893.5	-757.9	-587.5	-392.1	-7.0	1336.3	60.3	3333.7	41.2	719.4	SHORT-T. CAPITAL ACCOUNT BALANCE	(MIL. US$)
-384.4	-957.5	-1254.5	1699.5	5202.1	12175.2	2453.1	-273.9	-3740.8	4754.5	OVERALL BALANCE	(MIL. US$)
69101	75606	80847	90868	101804	113492	120477	131503	142633	149463	GDP (1985 CONSTANT PRICE)	(BIL. WON)
63833	72644	80847	93426	108428	127963	143001	172724	208201	231727	GDP (CURRENT PRICE)	(BIL. WON)
66803	73004	78088	88174	99612	111980	119577	130685	141623	148251	GNP (1985 CONSTANT PRICE)	(BIL. WON)
61722	70084	78088	90599	106024	126231	141794	171488	206681	229939	GNP (CURRENT PRICE	(BIL. WON)
	18.3%	13.5%	11.4%	16.0%	17.0%	19.1%	12.3%	20.9%	20.5%	11.3%	
79523.6	86950.5	89699.0	102783.	128919.	172788.	211198.	242225.	281716.	294475.	GNP (CURRENT	(MIL. US$)
	11.5%	9.3%	3.2%	14.6%	25.4%	34.0%	22.2%	14.7%	16.3%	4.5%	PRICE)
776.15	806.02	870.56	881.45	822.41	730.55	671.38	707.97	733.65	780.84	EXCHANGE RATE	(WON/US$)
292.0	663.2	643.9	958.5	1673.6	2698.4	443.8	754.9	-1706.7	-688.5	BUDGETARY DEFICIT/ SURPLUS	(BIL. WON)
91.5	92.2	93.0	91.7	92.1	94.6	96.0	100.0	104.7	107.0	PRODUCERS' PRICE INDEX	(1990=100)
73.3	75.0	76.8	78.9	81.3	87.1	92.1	100.0	109.3	116.1	CONSUMER PRICE INDE	(1990=100)
0.31	0.34	0.34	0.34	0.37	0.35	0.30	0.27	0.26	0.26		

EXPORT BY COUNTRY
(Unit: US$ '000)

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980
ARGENTIN	227	220	39	1970	6831	4624	1051	3305	6079	27875	77421
AUSTRALI	2905	5002	9190	27101	71268	63057	99345	120135	148827	156968	230370
AUSTRIA	107	397	1262	1675	3938	10167	20503	28064	38388	46396	58616
BANGLADE	* 0	0	182	111	1930	4826	7370	14969	55705	47556	76921
BELGIUM	0	3845	13392	40278	27607	40397	104911	75404	94444	118939	139020
BRAZIL	108	1095	1074	11065	25798	4394	2319	7194	6352	4894	3676
CANADA	19553	28934	58914	124881	166763	197347	314121	298755	327173	387642	343446
CHILE	14	16	991	131	1474	387	1260	7725	22147	37552	61288
COLOMBIA	11	61	220	1062	2090	834	1174	11031	6722	9507	21604
COSTARIC	1	1	14	217	141	1134	611	3830	3721	2398	4748
DENMARK	312	892	4467	10803	11647	21895	43991	63426	50085	69014	60104
EGYPT	10	494	521	717	575	10947	14153	37523	50404	85373	105820
FINLAND	273	382	1143	816	5004	4456	6155	31835	59404	20307	26845
FRANCE	1568	2562	8186	23141	24491	40054	88723	134906	208597	249464	291227
GERMANY	27330	31363	51204	120338	241770	312282	398189	480273	662886	845340	875486
GREECE	499	755	801	1731	1630	10145	4748	8174	27570	42166	80120
HONGKONG	27574	41448	72385	117724	150883	182002	324879	342053	384687	530669	823318
INDIA	536	2502	9287	2572	4616	6631	11486	20550	77646	86892	172949
INDONESI	2704	8541	21477	32380	55206	51417	48629	68887	102990	195096	365635
ITALY	1804	5571	9524	16595	28734	42512	53160	99613	117841	153890	229446
JAPAN	234329	261935	409560	1241539	1379555	1292906	1801552	2148286	2627264	3353028	3039409
KUWAIT	1515	1845	3704	7452	34012	33976	192515	248464	240638	228221	249147
KYPROS	0	5	14	8	12	143	523	1760	2372	5779	15656
LIBERIA	111	90	230	266	31264	92718	95208	78711	57718	40600	198481
LIBYA	218	571	1666	5465	10558	17126	20124	17320	25829	31088	174115
MALAYSIA	1251	1325	3516	6016	17678	12269	18188	23654	47497	85746	183893
MEXICO	0	0	0	5376	0	0	0	13539	11126	24644	44730
MYANMAR	1383	810	626	167	909	9491	5661	30791	10118	5399	5983
NEPAL	81	231	465	1061	644	861	393	4594	10530	5117	11390
NETHERLA	13513	15960	33026	57207	106898	129281	198463	227383	307287	330695	349506
NEWZEALA	610	739	1464	4170	7941	20811	10673	11424	21721	24041	28030
NIGERIA	6221	17765	9159	8443	12250	33488	24234	27035	45497	133560	124423
NORWAY	175	351	548	1381	2030	4245	12709	25489	68814	53346	51612
PAKISTAN	314	493	4952	5716	8575	13945	26183	42250	64769	73911	76055
PANAMA	2395	4146	4186	18014	20184	9927	14569	40057	91214	127285	143039
PERU	41	541	75	999	1373	1020	619	1016	997	2486	6818
PHILIPPI	1128	4338	3519	7234	9106	9893	29091	40586	85302	110880	151530
PORTUGAL	6	343	171	233	517	864	1528	2474	2613	2973	7019
SAUDIARA	140	1253	5072	13035	24956	91197	234796	671410	717031	704173	946112
SINGAPOR	11023	10115	10078	30461	48451	58292	78482	98440	143630	196692	266282
SPAIN	892	1013	1159	5535	4428	53359	15218	45406	56593	82249	82601
SRILANKA	105	69	178	1376	2443	1707	2982	12073	13530	24280	29550
SWEDEN	7885	8703	9484	17575	29892	56045	90192	161649	157652	116302	127341
SWITZERL	426	463	994	2284	8268	17415	34889	31855	52383	75263	67403
TAIWAN	7211	12030	16541	40942	51813	64172	85517	103181	140079	161407	216324
THAILAND	5064	4558	5980	17863	17660	20535	24341	72366	82604	111477	164640
TOTAL	835185	1067607	1624088	3225025	4460370	5081016	7715343	10046457	12710642	15055453	17504864
TURKEY	56	43	177	4192	6204	11936	10106	20466	55268	54656	48348
UK	13021	14096	28686	74960	106689	161793	253968	303818	393028	541605	572532
USA	395181	531792	765624	1021182	1492081	1536288	2492542	3118650	4058345	4373929	4606624

Source: KOSIS.

1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992
63807	11121	17995	14016	11559	36056	52090	69472	72381	75264	255535	463491
293567	307387	332557	392216	368774	534588	619286	864821	1004926	955981	989988	1098065
50040	50979	62107	76532	70010	93897	162263	222855	241388	237892	227706	231016
57212	59026	71992	105965	134094	144707	163336	168277	206739	276119	290719	332621
176419	119928	116393	125638	114171	218527	251380	338760	311449	424596	496504	474732
22749	9143	36828	4531	14858	24551	26486	31530	79766	106172	174226	164765
483500	442805	629168	878507	1228650	1247699	1450764	1692327	1882251	1730788	1672881	1619901
107251	30097	41544	47245	63166	66536	114618	153488	187851	144180	269935	326051
9272	14813	29739	62781	5521	11466	20849	29155	47447	57867	53039	76600
7948	4294	5119	9848	12439	18253	33782	28579	44403	47013	147612	67792
51136	54901	118372	135122	62053	99660	145268	252622	161700	261631	304939	239314
113358	123125	142076	208514	130938	119688	124105	110515	115927	159527	157452	187573
29101	38073	33192	37461	32702	55178	96905	135274	119502	118456	176118	85657
402893	263594	311087	288038	315779	543049	879609	1069886	893967	1118870	1127853	980921
804487	757918	775316	924201	979327	1241842	2002257	2367803	2137246	2849166	3192419	2880870
63715	24595	123130	227092	231298	115432	96738	103995	98663	159614	155118	171901
1154678	903849	817696	1281180	1565544	1690774	2204121	3560944	3374586	3779949	4769044	5910857
224845	350336	556778	1048550	466671	511629	403742	465009	674641	435315	468668	441533
370395	383052	252418	254037	195494	178940	240691	402132	666812	1078635	1349105	1936312
144569	154080	156584	166844	184286	319164	551609	732838	680533	750017	837906	869727
3502785	3388107	3403580	4602187	4543434	5425745	8436756	12004068	13456797	12637879	12355839	11600735
208396	260948	566704	256685	205575	211487	188209	341781	210085	112952	392630	300235
19929	17902	19576	28348	76594	39393	79382	106645	59732	126336	138481	171589
316765	443153	257192	240492	449936	134268	168266	400913	618429	550289	2086527	1340592
586526	175427	132553	251590	348538	212056	220228	274227	150802	129162	173298	162260
163871	234106	226690	253167	449516	218768	299721	410608	542792	708379	1037236	1137630
50196	43375	51014	19595	26132	50720	133222	279712	461840	559533	774560	906768
13411	22149	11991	11839	15592	25844	14154	21169	18131	37717	28851	31232
18088	21623	18467	12517	22013	15850	22746	19863	14831	10036	12903	11826
327932	350557	413688	373297	345389	502730	769543	824935	755803	964904	1168451	1014744
36641	69751	32236	42678	37923	76467	129662	141680	153951	129696	120216	116978
105027	134981	69628	39386	38775	44154	59297	71765	62151	89715	101678	161412
288247	525322	369720	356047	484757	379688	134556	177311	114462	127629	169884	286494
96932	106052	126814	86692	98913	126607	209697	239356	245702	221483	326206	371652
206522	364935	227130	539632	745557	494002	517173	567064	461503	547162	624100	1841589
15621	12722	4607	5396	6737	15505	24134	10425	3126	10044	24625	77988
131169	175468	180763	165371	240359	186137	220177	338002	476079	500239	674808	746477
5098	11879	11365	13964	17751	31637	55021	55063	65498	74212	101626	99800
1136195	1125401	1436552	990911	968730	854853	1030982	1130309	814833	739710	980316	940975
305632	380806	538825	496771	490083	531454	927454	1355260	1532354	1804588	2701939	3221946
86026	72635	54650	72545	68260	143209	292500	395502	391913	444681	509150	575140
83993	88151	43971	45904	80378	74087	87940	96150	93268	171304	180757	209657
127020	129945	125078	174174	208844	181306	499481	423512	438114	802943	405711	284733
68995	61737	70870	81685	144159	137766	272584	454950	378079	350347	294823	242556
262634	206797	150154	258819	196118	332979	555140	954393	1308232	1248563	1608972	2264417
125693	148332	218047	235661	143199	191768	272293	537253	752002	968891	1336803	1533612
21253757	21853393	24445054	29244861	30283122	34714471	47280928	60696388	62377174	65015731	71870121	76631515
27082	6840	16546	15230	107532	57282	72335	95493	136928	349252	320692	399122
705013	1102645	1005196	955482	913365	1034095	1525426	1950899	1861334	1750432	1767502	1830842
5660593	6243180	8245405	10478797	10754099	13879959	18310794	21404087	20638992	19359998	18559257	18106013

IMPORT BY COUNTRY
(Unit: US$ '000)

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980
TOTAL	1983973	2394320	2522002	4240277	6851848	7274434	8773632	10810538	14971930	20338611	22291663
ARGENTINA	186	309	109	659	348	362	3039	7064	19682	35730	12869
AUSTRIA	231	1987	6257	8489	3746	2668	35128	30025	40455	14328	21200
AUSTRALIA	13740	38359	47346	89575	129567	203386	215875	280686	463765	599042	680019
BANGLADESH	0	0	0	175	0	30	116	213	445	4202	715
BELGIUM	12369	16646	24233	14929	23857	29656	27452	45564	88737	135836	173691
BRUNEI	4978	156	513	148	416	354	2168	314	280	838	195
BRAZIL	337	2593	835	2323	6451	2868	6270	8140	30547	61026	44397
MYANMAR	35	11	9	60	899	693	358	658	4515	3554	3414
CANADA	23165	38959	35991	82545	115703	150175	115852	149636	204033	326348	378428
SWITZERLAND	4686	3666	3683	19703	28180	31252	50822	56856	84906	154085	139643
CHILE	547	3188	765	679	4594	5714	15876	31123	40211	71839	87522
CHINA	0	0	0	0	0	0	0	0	0	0	0
GERMANY	67204	73740	66954	132030	140345	192724	238308	346949	490905	843635	636603
DENMARK	833	455	5128	3011	4919	5666	9100	8629	12124	28567	23253
ECUADOR	2	2	234	879	1275	987	495	679	1557	1976	23399
EGYPT	49	681	1815	1045	2045	1278	2212	6301	4923	6454	14814
SPAIN	106	132	78	2010	38807	4902	2892	2975	14543	23369	28521
FINLAND	241	10	20	423	289	391	1515	4574	2594	63508	11053
FRANCE	52243	71754	47797	46903	35510	137338	162752	179237	442376	356779	190810
KINGDOM	32799	46187	73872	68932	90424	123047	171306	147570	211497	499382	303591
GREECE	0	0	872	5844	8471	6455	1561	5967	12458	33730	46269
HONG KONG	19783	19732	36121	29390	30464	19790	36747	35865	50600	87866	98200
INDONESIA	19825	40964	64057	153289	165391	146824	238659	353674	407826	591987	484524
IRELAND	1	33	89	87	64	273	1091	1582	2861	2523	3697
INDIA	6075	9852	4302	11748	22104	39044	33967	23158	39339	83164	53639
ITALY	19581	19349	22881	19244	27114	29029	34270	37029	78072	134328	118878
JAPAN	809282	953618	1031201	1726901	2620521	2433604	3098982	3926575	5981486	6656698	5857809
KUWAIT	30677	65340	93511	83407	257230	553479	674245	573829	746532	1155820	1753192
LANKA	24	12	2	23	75	147	149	210	667	393	164
LIBERIA	0	0	872	4	5382	3604	15236	19285	16578	47103	49602
LIBYA	0	0	0	8	0	46	8451	0	0	20	36
MEXICO	0	0	0	1274	0	0	1630	5925	20322	22625	64231
MALAYSIA	57790	61557	48950	132389	160551	122798	186595	196483	227914	383273	471563
NETHERLAND	23255	14873	21221	9203	13705	20129	30319	36770	46954	93628	86927
NORWAY	115	218	2249	3031	3570	3823	4235	44107	35056	27151	32487
NEPAL	22	14	17	0	34	70	6	43	110	512	288
NEW-ZEALAND	3196	3027	6046	14959	16908	15681	22945	41834	80551	88087	75733
PANAMA	913	1546	2774	3481	116085	28318	127440	16102	25027	33129	4214
PERU	3506	1299	1266	198	5337	4853	4715	16436	17558	41342	53549
PHILIPPINES	41683	44190	20868	39174	27045	28453	41648	31380	48173	142416	271517
PAKISTAN	660	488	67	5019	841	333	370	288	3902	19661	18910
PORTUGAL	62	95	183	1045	1608	1018	852	848	1616	2556	1465
QUATAR	0	0	0	0	0	0	0	0	0	126	40
ARABIA	38359	57828	87704	154183	670488	605359	714559	1123075	1280673	1585365	3288405
SWEDEN	2758	1759	3571	15279	30294	13418	15719	21495	56570	70497	48763
SINGAPORE	13543	16817	17458	7438	21370	13862	19059	51261	61226	116373	161279
THAILAND	1722	2902	9133	16775	40282	44953	31977	35961	44755	70905	91135
TURKEY	3	610	1391	2758	5239	9	7809	11728	13001	7313	14848
TAIWAN	33998	40051	48906	55394	110307	164409	83131	109205	152619	209740	313335
U.S.A.	584792	658781	648266	1201884	1700818	1881144	1962907	2447438	3042951	4602581	4890248
AFRICA	4891	1517	4881	11714	8293	18581	26509	0	0	0	0

Source: KOSIS

1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992
26131421	24250840	26192221	30631441	31135656	31583899	41019812	51810632	61464772	69843678	81524856	81775257
27989	28445	60137	64301	31508	86744	55514	77864	69734	86291	108177	115706
140897	36163	39459	38884	70535	116573	126828	103406	121015	155443	157448	211308
909964	912879	970847	1095754	1116100	1079610	1279409	1797390	2243077	2589116	3009363	3085796
6874	141	108	421	6959	1317	5925	6670	1680	2524	3371	5808
276404	117564	136192	144947	214263	151371	220343	357993	410905	431756	443952	443931
446	162038	226116	160067	223752	120807	202422	178142	246123	269216	281802	313585
107577	114611	211026	240800	213500	184344	305533	439189	652242	706719	889083	796881
38021	3599	6397	13478	10296	4491	5928	4771	3320	3097	4864	5983
530663	485026	444442	637405	630248	709311	947036	1196816	1680119	1465385	1906854	1573779
91266	101665	114526	133325	194982	190605	315293	365479	437003	582109	658845	671147
94698	77566	98950	104533	148826	128558	168900	207593	334215	331172	370551	365510
0	0	0	0	0	0	0	0	0	0	3440548	3724940
671798	680333	649817	794842	978594	1215878	1799279	2073987	2623557	3283545	3698263	3742542
36683	48413	113409	161340	86553	78947	119879	138975	126815	198606	250910	223148
210104	347926	236901	377427	652758	299307	116142	255223	58275	25414	332825	393651
38515	31074	104429	97515	130508	43939	69590	150236	113201	130821	49745	99035
43152	23540	30250	74436	50892	51176	74259	149703	143799	186159	294435	268102
17561	28535	42379	56817	77969	93659	146155	146634	161685	124958	167344	203357
279805	223780	270246	346755	442255	705701	783784	1134851	879232	1223230	1421814	1380419
397860	402836	467968	564918	565765	453991	721644	914503	923432	1226052	1558869	1355249
44992	23218	136501	184725	220514	24010	11662	18701	35364	76823	15737	22611
200673	244351	221218	467970	492495	400597	395994	555794	581608	613892	773404	793968
384791	682518	387203	652839	668610	428443	825307	905297	1135185	1600253	2051845	2291969
3942	4220	4629	7770	10492	20585	54466	65215	74926	88667	101570	107002
85313	148899	300906	380462	216084	126795	202219	170108	257527	282682	484847	477505
120628	121546	167333	204837	218078	309692	536478	637550	853745	1170414	1431111	1348399
6373553	5305293	6238407	7640110	7560400	10869285	13656625	15928860	17448627	18573850	21120216	19457651
1572860	819170	692264	482931	523223	215814	159615	205785	381734	497736	38777	340583
492	855	6271	12874	36342	11604	11502	11741	16209	23468	38785	44520
50971	260664	150629	106488	227331	29524	8375	22201	89466	235471	802	75380
45826	153174	294420	261480	128508	82873	111547	48180	26371	11211	14204	8597
55886	261136	200531	212477	139356	174923	180979	220058	163363	264155	224077	172223
643178	609596	777255	1005373	1234312	901706	1086319	1331354	1503280	1585965	1868992	1758214
92214	109984	205659	302737	254585	184675	266383	510676	386012	479050	583060	628555
121867	99370	179492	292130	336252	102759	92361	99552	116169	87778	136676	157374
38	89	71	8	43	43	61	624	884	1378	1032	650
83233	95427	101831	145156	123314	120906	157245	211651	319491	451706	500695	488145
45395	26389	73879	254709	525072	226029	224972	86423	46841	98273	16209	370083
71631	82716	52702	63188	108163	111970	90972	90416	96976	93897	136427	114837
265594	173993	178237	113825	150554	121878	123689	180782	204810	269784	322660	264929
11666	18243	38330	29650	53787	103787	110478	140017	172548	171696	291127	210226
2931	2260	7366	3370	16122	16294	18232	35279	29218	29731	42230	34637
1974	2900	88014	89410	17110	64733	70434	47686	101048	194635	188386	355020
3561365	3213410	2016137	1380706	639704	634912	1065854	837503	1041830	1724865	3268564	3797383
94289	97821	145773	216982	207502	179699	174514	224440	257770	374915	499704	476036
153417	165859	401092	390206	267749	215114	431615	566195	640805	896674	1029773	1788369
174371	108675	95610	132668	152149	276710	191031	264410	416439	463851	561742	637821
18365	2289	7853	1619	79975	7750	8061	37301	35813	165594	326671	310593
355072	280411	288714	339014	333409	431930	758881	1071264	1328391	1451902	1514696	1315239
6049662	5955805	6274431	6875475	6489323	6544708	8758219	12756657	15910685	16942472	18894369	18287269
0	0	0	0	0	0	0	0	0	0	647579	549267

Chapter 4

EXPORT PROMOTION STRATEGIES: MALAYSIA

by
Lee Heng Guie and Ho Ah Weng

I. Introduction

Malaysia is a highly trade-oriented, and open economy with the total exports constituting about 73 percent of its Gross Domestic Product (GDP) as at end-1991. The export share increased markedly from around 44 percent in 1970 - an indication of a well-diversified export sector particularly in the late-1980s. Over the last three decades, the Malaysian economy has undergone significant structural transformation, evolving from being a primary commodity producer into an increasingly diversified economy with an expanding industrial base. By 1991, the nation had become not only one of the world leaders in the production and export of major commodities and minerals, but also as a net exporter of oil, as well as a growing exporter of manufactures. This remarkable achievement was attributable to a combination of economic strategies such as effective utilization and diversification of the nation's vast natural resources; adoption of market-oriented and outward-looking economic system; and, the conduct of pragmatic macroeconomic policies.

The Malaysian economy has always been strongly dependent on the external sector for growth and development, despite adverse experiences from uncertainties created by sharp fluctuations in the prices of principal exports. The Malaysian Government realized that diversification in trade is inevitable to sustain economic growth. It was only during the latter part of the 1970s, and especially during the 1980s, that a remarkable transformation took place from an economy that was purely dependent on agriculture to one that is much more diversified. As a result, the focus of policy shifted to export-led growth from the period of 1970s onwards, marking the start of a new phase of export-oriented industrialization, focusing on spearheading the private sector-led manufacturing sector.

Indeed, export expansion played a very significant factor contributing to the country's economic growth. Growth in real GDP

had accelerated from an average of 5 percent annually in the 1960s to 8 percent in the 1970s, contributed largely by the buoyant export sector, which expanded strongly at an average annual growth of 17 percent during the period. The rapid expansion in the export sector was brought about by the effective implementation of policy measures aimed at diversifying and broadening the domestic economic base so as to buffer the Malaysian economy against the vagaries of external demand. Thus, by the late 1970s, Malaysia had diversified its exports within the primary commodities. From the rubber and tin dominated exports of the early 1960s, the structure evolved to see saw logs, palm oil and manufactured products gain prominence as exports towards the end of the decade. Eventually, diversification totally reshaped the export structure, with manufactures making up substantial share of exports while other new items such as sawn timber, liquefied natural gas and cocoa also gaining greater significance.

Today, the industrial development strategy, as outlined in the Industrial Master Plan (1986-1995) and the Sixth Malaysia Plan (6MP, 1991-1995), continues to aim for further diversification of the economic base and setting the foundation for a more rapid and balanced growth. In the context of a small open economy, the scope for achieving rapid economic growth within a relatively small domestic market can be quite limited. Thus, exports could well be the only vehicle by which the economy could continue to expand and progress along the path of industrialization by creating greater employment opportunities. In this perspective, it is imperative to review strategies and approaches to export promotion in view of the dramatic changes in the Malaysian exports structure. With the emergence of new manufactured products into the export markets, there must be a greater consciousness on the importance of exports.

The main objective of this paper is to address the role of exports on Malaysia's economic growth with a particular emphasis on the effectiveness of export promotion strategies adopted, including the possibility of new thrusts and directions to underpin Malaysia's export drive. The paper is structured as follows. Section II provides a profile of Malaysia's exports including empirical analyses on the relationships between export and economic growth followed by an estimation of export demand equation. Section III presents an overview of the export promotion incentives. Section IV examines the problems and issues that would serve to impede the export drive in the face of surging tide of

protectionism. Section V prescribes some policy recommendations to enhance Malaysia's export capabilities and, Section VI summarizes some conclusions.

II. Export Trade and Salient Features

2.1 Industrialization and Trade Strategies

Before independence in 1957, the Malaysian economy was mainly geared towards the production and export of two primary commodities, namely, rubber and tin. Therefore, immediately after the independence, the diversification of the economy and industrialization were placed at the center of development plans. A number of industrial policy instruments including fiscal incentives, tariff protection and the establishment of industrial estates were introduced. The basic strategy of industrialization in the 1960s was the tariff protection granted on an ad-hoc basis. Emphasis was placed on the development of resource-based industries with import-substitution as a strategy to develop particularly domestic consumption goods industry to meet the demands of domestic market. Various incentives including tax holidays were provided under the Pioneer Industries Ordinance, 1958.

In order to provide a conducive environment for industrialization, the Government established the Malayan Stock Exchange in 1960 to mobilize private capital for industrial development. Similarly, the Malaysian Industrial Development Finance Berhad (MIDF) and the Tariff Advisory Board (TAB) were also formed in the 1960s, amongst others, to finance viable new industrial projects and to formalize the system of tariff protection. Moreover, unlike the experience of other developing countries, import substitution in Malaysia did not lead to excessively high tariff barriers. The average effective rate of protection which rose from 15 percent in 1962 to 45 percent in 1969, was relatively low compared to other countries where the rate was as high as 250 percent. In the late 1960s, import substitution had been successful in satisfying the domestic market but it failed to generate sufficient employment opportunities to absorb the increasing labor force. Although there were some incentives to produce for exports, the overall incentives system appeared to be strongly biased against manufactured exports. At the same time, the limited size of the domestic market began to show signs of saturation after a decade of rapid industrialization. Hence, in 1968, the focus of policy shifted to export-led growth, marking the start of

a new phase of export-oriented industrialization. The Ordinance of 1958 was revised and broadened by the Investment Incentive Act of 1968.

The advent of the New Economic Policy (NEP), which covered the period 1971-1990 added a new direction to industrialization in Malaysia. In line with the main objectives of poverty alleviation and equity restructuring, export expansion became a central element in Malaysia's industrial development from 1970 onwards. This is to say that export promotion was aimed at generating vast employment opportunities through export-oriented industrialization and promoting greater participation of the Bumiputeras in the industrial development process of the country. During the 1970s, the pace of industrial development gathered momentum, following the shift in emphasis towards the promotion of exports, especially in labor-intensive industries such as textiles, electronics, rubber and palm oil processing and wood-based industries. This strategy showed a drastic departure from the import substitution strategy adopted in the 1960s.

The outward-oriented strategy was aggressively pursued through the provision of a generous incentives system under the Investment Incentive Act (IIA) of 1968 both for the domestic and foreign investors. In order to encourage more direct exports, the Free Trade Zone Act was enacted in 1971 and since then, a number of free trade zone companies have been set up. Provision of credit was also made available through industrial development institutions and commercial banks. To allow firms outside the free trade zones (FTZ) to enjoy similar benefits to those in the FTZ, the Customs Act of 1967 was amended in 1975 allowing the establishment of Licensed Manufacturing Warehouses (LMW) outside the FTZ. In addition, regulations were introduced through the Petroleum Development Act and Industrial Coordination Act of 1975 to reduce foreign ownership in the domestic sector.

During the early 1980s, the industrial policy of the country took a new turn with the Government participation in the heavy industries in order to develop a capital goods sector to broaden and deepen the industrial base. Many trust agencies and non-financial public enterprises were established to spearhead the growth of heavy industries. Accordingly, the Heavy Industries Development Corporation of Malaysia (HICOM) was set up to coordinate the heavy industries projects. A number of projects were initiated including the national car project, cement plants, iron and steel mills, gas projects and pulp and paper industries. Towards the mid-1980s, it was realized that the medium-

and long-term industrial development strategies were necessary to strengthen the industrial structure, and to overcome the weaknesses of the industrialization programs. Towards this end, the Malaysia Industrial Policy Study (MIPS) and the Industrial Master Plan (IMP) were initiated to provide medium- and long-term policy strategies to spur the industrial development of the country at a sustainable pace. The IMP recommended an outward-oriented manufacturing-led growth emphasizing on the resource-based industries along with the diversification of the non-resource based industries. Meanwhile, the foreign equity requirement was also liberalized and new incentives were generously provided through the introduction of the Promotion Investment Act in 1986. Under the new guidelines, foreign investors could own up to 100 percent subject to a certain export requirements or a certain number of employment to Malaysian workers.

2.2 Contribution of Exports to the Economy

Exports have for a long time accounted for more than one-half of the total national income. Its relative importance can be assessed in terms of its contribution to Gross National Product (GNP). Although the relative importance of the export sector has declined slightly due mainly to the rapid expansion of the domestic sector, the contribution of the export sector to the growth of Malaysia's GNP has increased significantly in absolute terms. The ratio of exports to GNP rose gradually from 44.3 percent in 1970 to 54.8 percent in 1980 and surged to as high as 76.7 percent in 1991 (see Appendix 4.1).

The export sector also contributed substantially to the generation of employment opportunities. Significant changes were reflected in the patterns of sectoral employment. Evidently, the process of economic diversification has gradually reduced the relative importance of the primary sectors (agriculture and mining) as the major source of employment. Their combined shares came down from 53 percent of total employment in 1970 to 27 percent in 1991. Conversely, the manufacturing sector emerged as an important source of employment, with its share rising from 11 percent in 1970 to 16 percent and 20 percent in 1980 and 1991 respectively.

A significant diversification in the nation's exports was also reflected in the composition of its export earnings. In 1955, exports of two primary commodities, namely, rubber and tin, accounted for close to three-quarters of total export earnings; but by 1991, these two

commodities represented only 3.5 percent of the total, while exports of manufactured goods, crude petroleum, tropical hardwood (saw logs and sawn timber) and palm oil, which were insignificant up to the mid-1960s, rose substantially to account for 96.5 percent of total export receipts. Of particular significance in recent years has been the rapid growth in exports of crude petroleum since 1973 to become the largest single foreign exchange earner by 1982, contributing 27.4 percent to total export receipts at its peak. However, since 1983, exports of crude petroleum has been overtaken by manufactured goods for the lead place in terms of foreign exchange earnings. Nevertheless, crude petroleum continued to retain its position as the single largest primary commodity export earner, where its share in total gross exports stood at 10.8 percent in 1991, the lowest since 1976. The importance of manufactured goods as the leading sector of foreign exchange earner was attributable largely to the intensified efforts undertaken by both the Government and manufacturers to promote manufactured exports through the 1970s and 1980s. By 1985, the manufacturing sector surpassed the agriculture sector as the leading source of export earnings, with an export share of 32.8 percent and the share increased further to 65 percent in 1991. On the other hand, the share of agriculture goods, which had been declining since 1988, dropped further to 19 percent in 1991.

2.3 Growth Trend and Changing Patterns of Exports

Malaysia's external trade pattern was largely determined by the colonial pattern of international specialization based on natural endowment of the country. In the early period, the strength of exports was based on two main primary commodities, namely, rubber and tin, which accounted for 69 percent of export earnings in 1960. However, the export structure became increasingly diversified and broadened to see saw logs and manufactured products gain prominence as exports towards the end of the decade. The export profile continued to change towards greater diversification in the latter years, and by 1991, a totally reshaped export structure emerged, and rubber was as low as 3 percent of total exports while tin recorded a subdued 0.7 percent. Saw logs stood at 4.3 percent, palm oil 5.3 percent, crude petroleum 10.8 percent. Manufactures dominated the scene with a 64.9 percent share of exports (Table 4.1 and Chart 4.1).

During the 1970s, Malaysia's gross exports grew rapidly to increase at an average annual rate of 17 percent, compared with an increase of 3.6 percent in the 1960s. The strong export growth was evident in all

the major categories of exports. Exports of primary agricultural products, which represented 44 percent of total exports in 1980, expanded strongly from an average annual growth of 2.7 percent in the 1960s to 14.7 percent in the 1970s, attributed largely to double-digit growth recorded in the exports of palm oil, sawn timber and saw logs. The Government realized the over-reliance and specialization on the production and exports of only two commodities (rubber and tin), would render the economy vulnerable against the vagaries of world trade and commodity price fluctuations. To overcome this uncertainty, the Government embarked on a series of development programs aimed at modernizing and diversifying the agriculture sector, which includes, among other things, the use of high-yielding varieties, large-scale land development scheme, drainage and irrigation projects to improve the agricultural productivity and to promote the cultivation of new range of commercial crops. By the end of 1970, the first phase of Malaysian economic transformation, namely agricultural diversification, was already in place, keeping in view the emergence of new sources of export earnings, such as ..palm oil, saw logs and sawn timber palm oil, saw logs and sawn timber. In the 1970s, exports of palm oil, saw logs and sawn timber grew significantly by an average annual growth rate of 32.1 percent, 17 percent and 22.8 percent, respectively. Consequently, the share of palm oil, saw logs and sawn timber to total exports increased significantly to 9.2 percent, 9.3 percent and 4.8 percent in 1980, from 1.7 percent, 3.3 percent and 2.1 percent, respectively, in 1960. As a result, Malaysia's dependence on rubber and tin had been reduced significantly from 69 percent of total exports in 1960 to 25 percent in 1980.

The relative importance of tin was further reduced as the production of crude petroleum become more significant. Mineral exports grew at an average annual rate of 18.1 percent in the 1970s (5.3 percent in the 1960s) with its share to total exports increased to 33.8 percent in 1980. Higher receipts from mineral exports reflected mainly the emergence of petroleum exports in the early 1970s, which recorded an average annual growth of 37.3 percent, from RM 147 million in 1960 to RM 6.7 billion in 1980. The expansion of petroleum exports more than compensated the relative declining importance of tin as a major source of export earnings. The growth of crude petroleum was particularly robust following the signing of production sharing agreements between the national oil production company, PETRONAS, and the major oil producing companies in 1976.

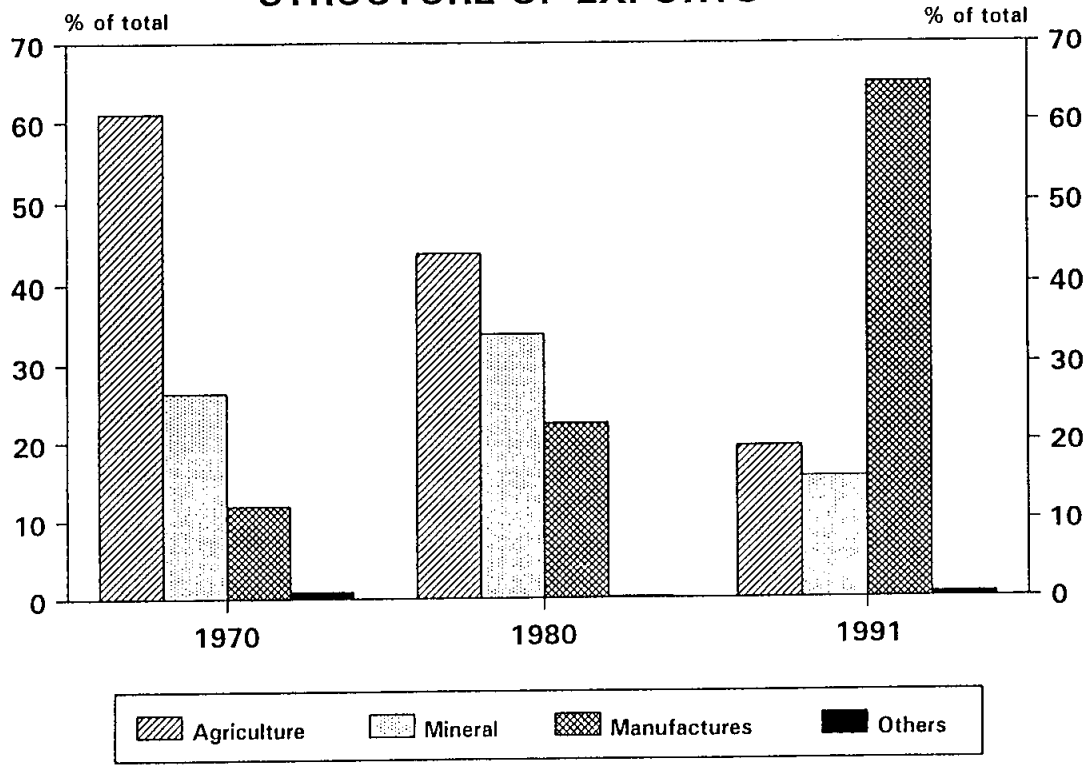
Table 4.1

MALAYSIA: EXPORTS OF PRIMARY COMMODITIES

	Average Annual Growth Rate			Percent of Total			
	1971-80	1981-86	1987-91	1970	1980	1985	1991
		(%)					
A. Agriculture	14.6	-0.6	8.6	61.0	43.7	32.7	19.0
1. Rubber	10.4	-6.0	-3.3	33.4	16.4	7.6	2.8
2. Saw logs	15.1	1.6	7.4	12.5	9.3	7.3	4.3
3. Sawn timber	20.6	-0.5	18.2	4.0	4.8	3.0	3.2
4. Palm oil	25.7	2.5	10.7	5.1	9.2	10.4	5.3
5. Others	13.8	5.0	15.7	6.0	4.0	4.4	3.4
B. Mineral	21.5	-3.0	13.0	26.3	33.8	34.0	15.5
1. Tin	9.6	-20.1	1.0	19.5	8.9	4.3	0.7
2. Crude petroleum	41.9	-3.5	13.5	3.9	23.8	22.9	10.8
3. LNG	-	-	13.3	-	-	6.0	3.6
4. Others	7.8	-32.0	59.9	2.9	1.1	0.8	0.4
Total Commodities (A+B)	17.1	-1.6	10.5	87.3	77.5	66.7	34.5
C. Manufactured Goods	26.3	15.9	31.9	11.9	22.4	32.8	64.9
1. Electronic component	46.0	16.7	17.6	1.0	8.1	11.7	13.8
2. Other electrical appliance	-	24.5	52.9	-	2.6	5.4	23.9
3. Textiles	38.1	11.6	24.8	0.6	2.9	3.4	5.0
4. Food	18.3	11.0	17.8	1.8	1.7	2.0	2.2
5. Petroleum products	1.6	25.0	9.8	3.1	0.7	2.7	1.2
6. Wood products	18.0	2.2	26.2	1.7	1.7	1.0	1.8
7. Transport equipment	21.4	15.1	44.8	0.6	0.8	1.5	3.5
8. Manufactures of metal	22.1	13.1	28.3	0.7	0.9	0.9	1.9
9. Chemicals & chemical pdt.	18.3	26.2	18.9	0.7	0.7	1.6	1.9
10. Rubber products	17.3	19.0	48.6	0.3	0.3	0.3	1.8
11. Other manufactured goods	24.2	10.2	47.0	1.4	2.0	2.3	7.9
D. Other Exports	-10.0	44.7	30.0	0.8	0.1	0.5	0.6
Total Exports (A+B+C+D)	18.5	3.8	21.8	100.0	100.0	100.0	100.0

CHART 4.1

STRUCTURE OF EXPORTS



In the early 1970s, the Government switched to an active promotion of those industries which were export-oriented, labor intensive and resource-based as the corner-stone for rapid industrial growth, emphasizing in particular the manufacture of electronics and related products, textiles and textile products, wood and wood products, and the refining of palm olein and stearin. With the provision of a wide range of incentives for exports, including tariff protection, pioneer status, the development of FTZ and the provision of credit through industrial development institutions and commercial banks, the manufacturing sector was transformed gradually from the early emphasis on import-substitution to the proliferation of a wide range of manufacturing activities for the export market.

During the period under study, exports of manufactured goods grew rapidly at an average annual rate of 14.2 percent in the 1970s, compared with 4.9 percent in the 1960s. Consequently, the export share of manufactured goods, which was negligible in 1960, rose steadily from 14 percent in 1967 to 22 percent in 1980. The expansion was fairly broadly based with exports of electrical machinery, appliances and electronics component parts, textiles, clothing and footwear, wood and wood products rising in each case by 18-46 percent during the period. Evidently, the leading source of growth emanated largely from labor-intensive industries, especially the textiles and electronics industries. These two industries were actively promoted at the initial stage to generate employment for the nation's growing work force, with the provision of facilities such as FTZ and industrial estates. By 1980, exports of electronics and textiles totaled RM 3.1 billion, accounting for 11 percent of total exports, as against RM84 million or 1.6 percent of total exports in 1970. The exports of other resource-based industries such as rubber products and food products also experienced significant growth during the period, albeit at a slower pace. Reflecting the rapid growth in the sector during the decade, the manufacturing sector's share of GDP increased from 5 percent in the 1960s to 12 percent in the 1970s.

In the 1980s, Malaysia's exports was adversely affected by the recession and slowdown in the economies of the industrial countries, which resulted in a decline in commodity prices across-the-board. The export growth fluctuated during this period, and recorded a decline in 1981 (-3.8 percent), 1985 (-1.6 percent) and 1986 (-7.1 percent). As a result, exports of manufactures grew by an average annual rate of 10.8 percent in the 1980s, compared with an increase of 17 percent in the

1970s. In terms of composition of exports, agricultural commodity exports decelerated sharply from an average annual rate of 14.7 percent in the 1970s to 4.4 percent in the 1980s. The slowdown in export receipts was due largely to a sharp decline in exports of tin (from an average growth of 9.5 percent in the 1970s to -6.7 percent in the 1980s) and rubber (8.2 percent to -1.3 percent), as well as a sharp moderation in exports of palm oil (32.1 percent to 6.6 percent), saw logs (17 percent to 4.2 percent) and sawn timber (22.8 percent to 8.1 percent). However, export earnings from the agriculture sector remained the second largest source of export earnings, even though its share in total gross exports declined sharply from 43.7 percent in 1980 to 19 percent in 1991.

With the benefit of government's strong support and encouragement, manufactured exports expanded significantly by an average annual rate of 22.4 percent in the 1980s. The growth was particularly higher during the period 1987-1991. The overall expansion in the export of the manufactures, notwithstanding the economic slowdown in major industrial countries, was mainly attributed to the continuing efforts to improve production efficiency and product quality and range to ensure an increasing share of the international market. At the same time, successful entry into new markets, aided by the introduction of an array of new products, had also contributed to higher exports. Given the poor performance of the primary commodities, the share of manufactured exports to total exports further increased to stand at 65 percent in 1991. The growth in exports during the period of study was broad-based, with the highest growth rates being recorded by industries producing electrical and electronic products (average annual rate of 52.9 percent), rubber products (48.6 percent), transport equipment (44.8 percent), textiles, clothing and footwear products (24.8 percent) and wood and wood products (26.2 percent). A large part of the gain in the exports of manufactured goods, which overtook agricultural commodities to become the largest group of exports in 1985, was attributed to the dynamic changes taking place within the manufacturing sector. Arising from the strong influx of foreign direct investment in recent years and a concerted move by industries towards product improvement and diversification, exports with higher value added content were gaining significance. For example, exports of electronic components and parts (by far the largest foreign exchange earners in the manufacturing sector since 1974) were replaced by the exports of electrical appliances and machinery (comprising electrical end-products such as audio-video and telecommunication equipment,

air-conditioners, automated office equipment and other electrical home appliances) in 1990.

However, in recent years, the more capital-intensive industries, in particular those producing chemicals and chemical products, petroleum products, non-metallic mineral products and basic metals are being expanded, and with the coming on-stream of several large petrochemical and steel projects in the next few years. Within the manufacturing sector, exports of non-resource based (NRB) industries grew more rapidly at an average annual rate of 23.3 percent in the 1980s, compared with a growth of 20.3 percent for exports of resource-based (RB) industries. Consequently, the share of NRB industries to total manufactured goods exports increased from 68 percent in 1980 to 74.1 percent in 1991, whereas the RB exports share declined from 32 percent to 25.9 percent.

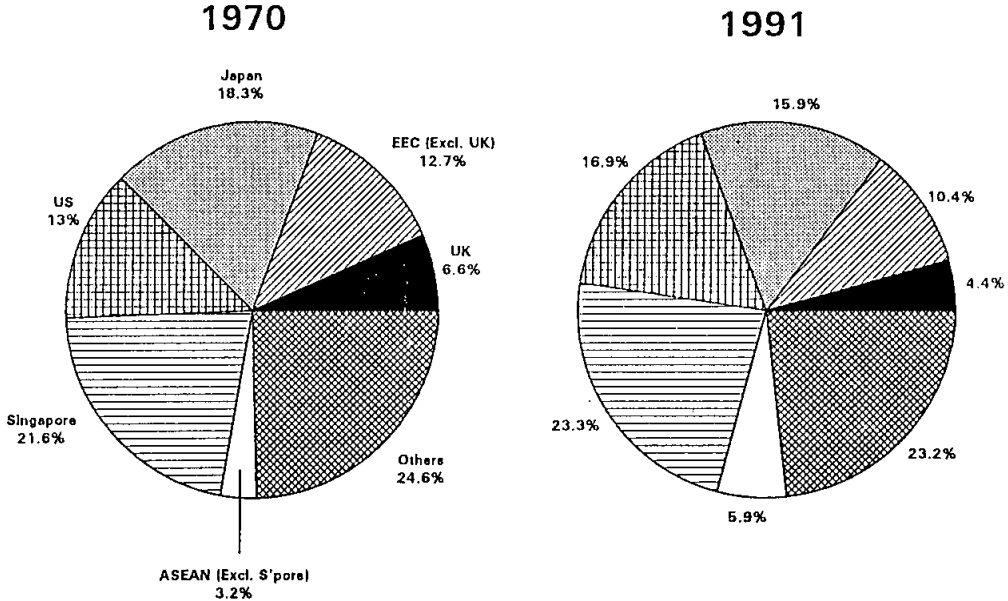
2.4 Direction of Exports

Changes in the composition of Malaysia's exports had been accompanied by significant changes in the direction of the nation's exports. The direction of trade had changed significantly in the sense that there had been market diversification for Malaysian exports as the nation's production structure became increasingly diversified and broad-based. Malaysia's traditional trade partners such as the United States (U.S.), Japan and Singapore still continued to dominate Malaysia's export trade (see Chart 4.2 and Appendix 4.2).

A significant feature of the direction of Malaysian exports in the 1970s was the growing importance of Japan and the U.S. as the major buyers, with an average annual growth rate of exports of 19.9 percent and 18.7 percent, respectively. Consequently, the share of Malaysian exports to Japan and the U.S. increased from 18.3 percent and 13 percent in 1970 to 22.8 percent and 16.4 percent, respectively, in 1980. Japan's import of Malaysian exports comprised mainly of saw logs, crude petroleum and palm oil, in addition to rubber and tin. Japan ranked second to Singapore as the major buyer of Malaysian exports during the period 1961-1975. However, Japan's import of Malaysian exports accelerated at an average annual rate of 36.9 percent between 1976-1980 to overtake Singapore as the leading importer of Malaysian goods. The U.S. improved its placing from the fourth position in 1960 to the third during the 1970s. Exports to the U.S. increased at an average

CHART 4.2

MALAYSIA : PRINCIPAL MARKETS OF EXPORTS



annual rate of 11.1 percent during the period 1961-1975, comprising mainly primary commodities such as rubber, tin, palm oil and sawn timber. Between 1976-1980, exports to the U.S. surged to an average 25.4 percent per annum, with a much wider range of products, including increasing sales of crude petroleum and manufactured goods, especially electronics components and electrical appliances.

In the 1980s, there were some changes in the pattern of marketing Malaysian exports, although Singapore, Japan and the U.S. remained the major markets. Their combined market shares which had declined from 58.2 percent in 1980 to 53.6 percent in 1988 rebounded to 56.1 percent of total exports in 1991. Among individual countries, there were relatively significant changes in their respective shares of Malaysian exports. Except for the period of 1984-1987, Singapore maintained its position as the leading buyer for Malaysia's exports for the fourth consecutive year since 1988, with the share ranging from 19-23 percent of total exports. Although Japan remained as the leading buyer for Malaysian exports throughout the period 1984-1987, its share to Malaysian exports had been on a downward trend since 1985, which continued into 1991 with a share of 15.9 percent (24.4 percent in 1985). Part of the decline was due to the trend of the Japanese-owned companies in Malaysia marketing their products through their affiliated companies based in Singapore. Since 1988, the U.S. replaced Japan as the second largest export market, to account for 16.9 percent of total Malaysian exports in 1991.

On a regional basis, Malaysia's trade with the member countries of the Association of South-East Asian Nations (ASEAN) remained significant, accounting for more than 20-30 percent of total exports throughout the period 1970-1991. Of significance, Singapore dominated the bulk of Malaysian exports, with its share maintained at around 20 percent for the past two decades. Traditionally, Singapore has functioned as one of the major trading partner of Malaysia, importing its primary products for re-exports and supplying Malaysia with goods imported from other countries. However, this role has declined over the years, indicating the trend towards greater direct marketing of Malaysian exports to importing countries and increasing utilization of Malaysia's own port facilities. Unlike trade with ASEAN countries which remained significant, Malaysian exports to EEC has been declining over the years. The share of the EEC in Malaysian exports had declined from 19.3 percent in 1970 to 14.8 percent in 1991. The decline could be attributed to the increasing protective market of European Community

(EC) as more restrictive measures were imposed on exports from non-member countries to EC. In particular, the share of the United Kingdom in Malaysian exports declined from 6.6 percent in 1970 to 4.4 percent in 1991. To some extent, increasing exports to the Netherlands and West Germany had compensated for the decline in the share of exports to the United Kingdom.

Other important markets for Malaysian exports were South Korea, Hong Kong, Taiwan and the People's Republic of China, with the share increasing from 2.6 percent, 1.2 percent, 1.3 percent and 1.3 percent in 1970 to 4.4 percent, 3.4 percent, 2.7 percent and 1.9 percent, respectively, in 1991.

2.5 Implications on Balance of Payments

Given the openness of the Malaysian economy and its dependence on the major industrial countries as export markets, the Malaysian economy is vulnerable to the cyclical fluctuations of the world economy. We can assess the extent of the impact by examining the nation's balance of payments position Charts 4.3, 4.4 and 4.5 show the trends in the balance of payments.

One of the major features of Malaysia's external position is that its balance of payments has generally been strong and favorable, characterized by a consistent surplus in the trade balance, large deficits in services and transfers, and sharp fluctuations of surpluses and deficits in the current account balance. In the 1960s and 1970s, the basic strength of Malaysia's balance of payments was in the merchandise account. Since then, there was a gradual shift in strength from current account to capital account, following significant fluctuations in the trade balance and the consequent policy changes that led to the build-up of capital account, specifically in official foreign borrowings in the late 1970s and foreign direct investments in the latter half of the 1980s.

Despite the vulnerability of its principal exports to external development and the rapidly rising import bills over the past years, the overall external payments position had been largely favorable in the 1960s and 1970s. The merchandise account was consistently in Malaysia's favor, with surpluses rising in the commodity export boom years of 1965-1966, 1969-1970, 1973, 1976-1979, 1984 and 1987-1988. During these periods, exports have almost always dominated imports to

CHART 4.3

BALANCE OF PAYMENTS

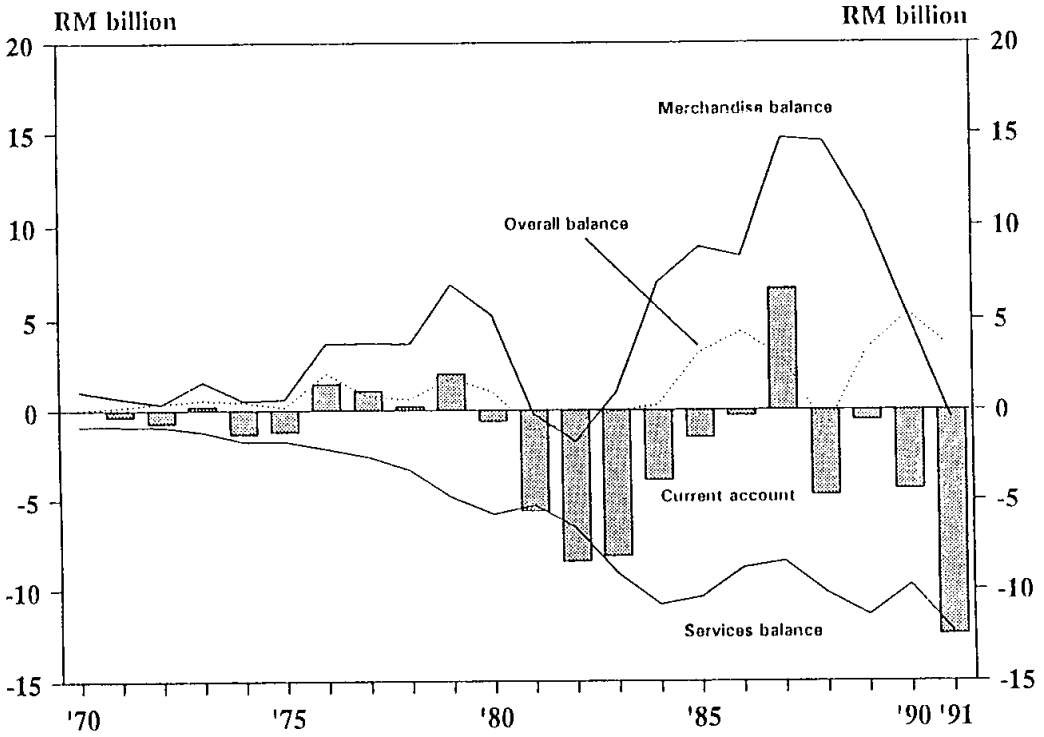


CHART 4.4

TRADE ACCOUNT

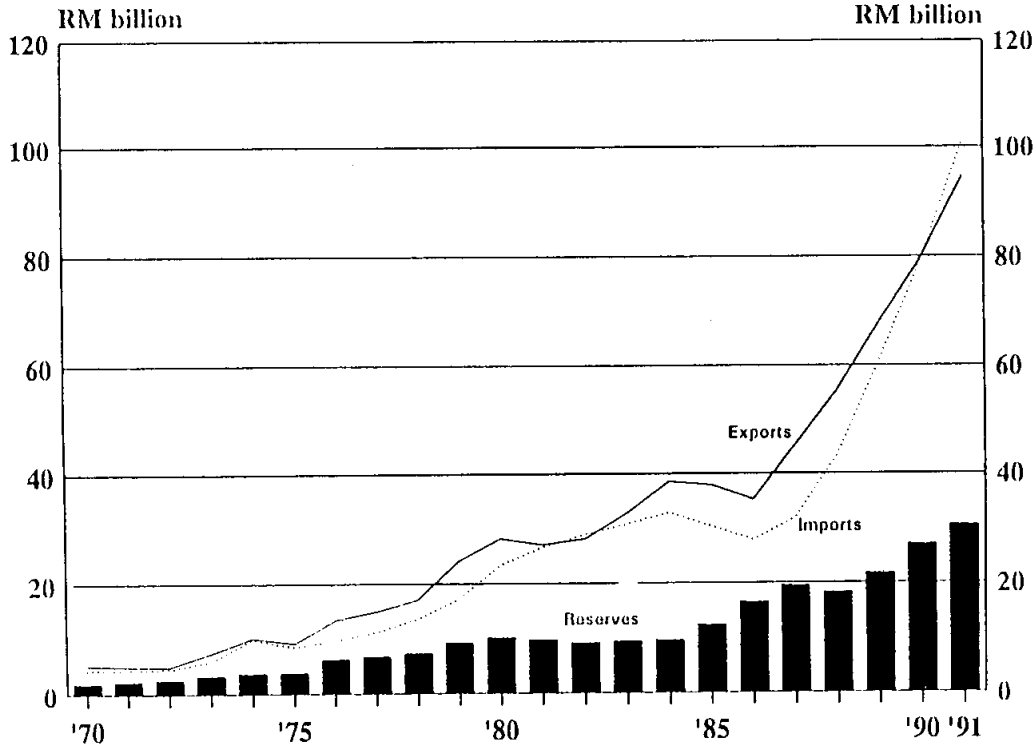
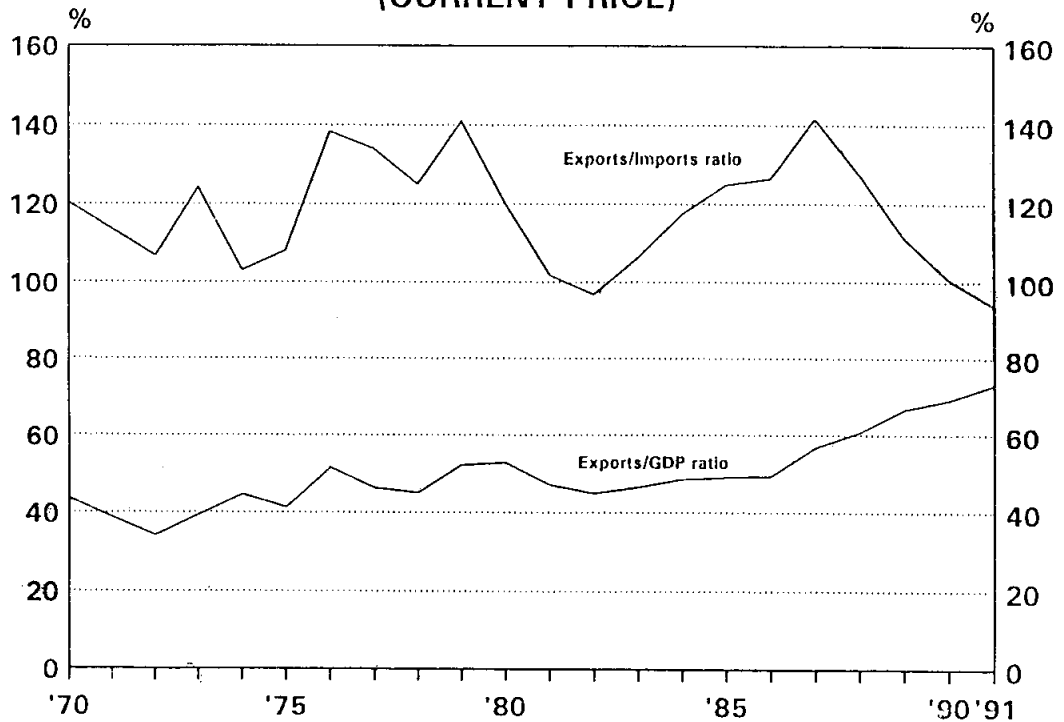


CHART 4.5

EXPORTS/IMPORTS & EXPORTS/GDP RATIO (CURRENT PRICE)



yield considerable surpluses in the merchandise balance. The favorable trade balance was reflected by the rising exports/imports ratio, which increased from 120 percent in 1970 to 141 percent in 1979, while the exports to GDP ratios (in current price) increased from 43.6 percent to 52.2 percent during the same period. The ratios tended to fluctuate depending on the commodity prices cycle as evidenced in late 1970s, which recorded a rapid rise in export earnings on account of the favorable international terms of trade. This rise can be attributed to three factors; first, the extraordinary commodity price boom, which led to a near doubling of the export price index between 1976 and 1980; second, the very rapid growth in the production of oil for export; and third, the rapid growth of export diversification in palm oil, electronics, clothing and textiles, all of which profited from the prevailing climate of high international prices. As a result, export earnings rose from RM 9.2 billion in 1975 to RM 28.2 billion in 1980.

However, in the early 1980s, the merchandise account which was adversely affected by the prolonged recession in the major industrial countries, recorded a deficit for the first time in 1981-1982. The sharp deterioration in the merchandise account reflected the impact of the world recession on export earnings, accentuated by the adverse impact of global inflation on import growth through higher import prices. Between 1980 and 1982, the terms of trade registered a decline of 20 percent, as prices of major export items declined substantially, while import prices remained strong. Correspondingly, the ratio of exports/ imports dipped sharply to 97 percent in 1982 (120 percent in 1980 and 102 percent in 1981). Coupled with the persistent deficit in the services account, due largely to the acceleration in payments for freight as well as investment income in the late 1970s and 1980s, the current account deficit was extremely high in the period 1981-1983, ranging between RM 5.6 billion to RM 8.4 billion. The consequent of falling export earnings and increased participation of the public sector in national development had also led to the worsening of the Federal Government's budgetary position. Realizing the twin-deficits were likely to be unsustainable, the Government undertook a series of comprehensive adjustment policies in mid-1982, which were spearheaded by massive cutbacks in public sector spending. The progress achieved so far was commendable as reflected in the progressively narrowing of the Government's budget deficit from a peak of RM 10.4 billion (nearly 18 percent of GNP) to RM 2.6 billion (2.1 percent of GNP) in 1991. On the external front, the deliberate policies to improve Malaysia's external

competitiveness and to reduce imports had narrowed the current account deficits progressively since 1983. By 1987, it turned around to record a surplus of RM 6.6 billion, the first surplus since 1979. However, during the period 1989-1991, the current account reverted to deficits, due mainly to markedly smaller merchandise surpluses which reflected the continued disparate growth in exports relative to imports.

Unlike the situation in many developing countries, the Malaysian payments position on the current account was supported by strong inflows of both official and private capital from abroad. As a result, the overall balance of payments position remained generally favorable despite sustained periods of current account deficits.

2.6 Export and Growth: Some Empirical Evidence

2.6.1 Some Recent Studies

An assessment of the role of exports in economic growth is obviously important. At the theoretical level, extremely diverse positions could be observed. For instance, the standard neo-classical trade argument would postulate a substantial positive impact of exports and trade on economic performance due to better allocation of resources. In addition, the "two-gap" models of development would suggest an important positive role of exports in economic development due to an attenuation of the foreign resource "gap". However, the Marxist or the neo-Marxist stances may treat trade as one mechanism for exploitation of the less developed countries (LDCs) by the industrialized West.

Several recent studies have attempted such an empirical analysis. Michaely (1977)[1] considered a sample of 41 LDCs and related the mean annual growth of per capital GNP with the mean annual increase in the share of exports in GNP for the period 1950-1973. This method was based on a simple correlation. For the entire sample, the rank correlation - coefficient between the two variables is 0.38, which indicates a positive association between the rates of growth of per capital

1. Michael Michaely, "Exports and Growth: An Empirical Investigation", *Journal of Development Economies 4* (March 1977): pp. 49-53, esp. 52.

GNP and export share. Krueger (1978)[2] in her study to assess the effect of exports on GNP for ten countries for the period 1954-1971 found that "an increase in the rate of growth of exports of 1 percent will increase the rate of growth of GNP by just over 0.1 percent". Bela Balassa[3] used both correlation and regression procedures to assess the effect of export growth on economic performance. Generally, a substantial positive effect of export growth on economic performance was observed. More recently, Tyler[4] used a sample of 55 middle-income LDCs and related growth of exports and of GDP over the period of 1960-1977. He found the conclusion that there was additional evidence demonstrating a strong cross-country association between export performance and GNP growth. Although these authors differ in their methodologies and the aspects emphasized, they agreed to the general conclusion on the growth-promoting role of exports.

2.6.2 The Model and Method of Specification

In order to investigate the role of export growth on economic growth with the emphasis to test the causation between export and economic growth, one can used the notion of Granger (1969) causality test. In this context, this paper attempts to empirically test the relationship between export growth and GDP growth using quarterly data from 1971-1991.

The Granger causality test[5] directly utilizes ordinary least square regression. That is, in order to test causality running from X to Y, one can use the following specification:

$$GDP_t = \alpha_0 + \beta_1(L)GDP_{t-1} + U_t \qquad (1)$$

2. Anne O. Krueger, *Foreign Trade Regimes and Economic Development: Liberalization Attempts and Consequences* (New York: National Bureau of Economic Research, 1978), pp. 273-74.

3. Bela Balassa, "Exports and Economic Growth: Further Evidence", *Journal of Development Economics 5* (June 1978): pp. 181-89.

4. William G. Tyler, "Growth and Export Expansion in Developing Countries", *Journal of Development Economics 9* (August 1981): pp. 121-30.

5. In the Granger sense a variable X causes another variable Y, with respect to a given information set that includes X and Y, if current Y can be better predicted by using past values of X than by not doing so.

$$GDP_t = \alpha_0 + \Gamma_1(L)GDP_{t-1} + \beta_2(L)EXP_{t-1} + U_t \quad (2)$$

where, GDP = real gross domestic product,
EXP = real gross exports,
α_1 and β_1 are parameters relating GDP_t and its lagged values, and
β_2 are relating GDP_t and past values of EXP_t.

The terms $\alpha_1(L)$ and $\beta_2(L)$ are polynomials in the lag operator L. Thus, $\alpha_1(L)$ and $\beta_2(L)$ are defined as $\sum_{i=1}^{r} \alpha_i L^i$ and $\sum_{j=1}^{s} \beta_j L^j$, respectively, where r and s are assumed for empirical purposes to be finite (see Appendix 4.4 for derivation of the variables).

Causal relationships would appear to enter this model in a very natural way. If $\beta^2(L) = 0$, then it is clear from equation (2) that EXP has no effect on future GDP; that is, EXP does not cause GDP. Thus, one could determine the causal relationship between EXP and GDP by first fitting equation (2) by ordinary least squares (OLS) and obtaining the unrestricted sum of squared residuals, SSRu. Then, by running another regression equation under the null that all the coefficients of the lagged values of EXP are zero, the restricted sum of squared residuals, SSRr, is obtained. The test of null hypothesis that X does not cause Y based on equations (1) and (2) can be carried out with the F-statistics.

$$F^* = \frac{(SSR^r - SSR^u)/h}{(SSR^u)/(n-k-1)}$$

where h is the number of restrictions, n is the number of sample size and k is the number of parameter of unrestricted equation. If the null hypothesis cannot be rejected, then the conclusion is that the data do not show causality. If the null hypothesis is rejected, then the conclusion is that the data do show causality, that is EXP does cause GDP.

2.6.3 Estimation Results

The results for the causal relationships between exports and economic growth is presented in Table 4.2.

Table 4.2
CAUSALITY TESTS WITH MALAYSIAN EXPORTS AND ECONOMIC GROWTH

	Direction	Lags	F Calculated	
(1)	EXP—>GDP	1	3.875	
				$F^{(2,80)}$ = 3.124 at 5% level of significance
(2)	GDP—>EXP	1	1.14	

As indicated, there is evidence of causal relationships running from real gross exports to economic growth. The F-statistics for the test (EXP—>GDP) is significantly different from zero at the 5-percent level. The results statistically support the export-led growth strategy for pursuing economic growth in Malaysia and is in conformity to what was found by Muzafar Shah and Dr. Mohammed bin Yusoff (1988). The findings showed strong evidence of causal relationships running from export series; total export, agricultural exports and manufacturing exports to economic growth during the period 1967-1985. Further, the results also pointed out that both agricultural export and manufacturing export play an important role in promoting economic growth as reflected by the statistically significant test at the 5-percent level.

2.6.4 Estimation of Export Demand Function

2.6.4.1 Theoretical Framework

Empirical studies of international trade flows have generally concentrated on the formulation and estimation of demand relationships for imports and exports, e.g., see the studies by Houthakker and Magee (1969), Taplin (1973), and Hickman and Lau (1973). Both the import demand of developing countries and the world demand for their exports have generally been assumed in literature to be determined by non-market forces, and therefore,

relatively insensitive to changes in prices. In this context, the paper aims to estimate the export demand function, with the simplifying assumption that there are no lags in the system so that the adjustment of export quantities and prices is instantaneous. The annual time series were used for the period 1970-1990.

2.6.4.2 Export Function

The world demand for the nation's exports is specified in log-linear form as follows:

$$\log X_t^d = a^0 + a^1 \log (PX/PXW)^t + a^2 \log YW^t$$

where,

X^d	=	value of exports demanded,
PX	=	price of exports,
PXW	=	world price level, and
YW	=	real world income (OECD real gross national product).

Since the equation is specified in logarithms, a^1 and a^2 are relative price and real income elasticities (of export demand), respectively. It is expected that a^1 will be negative and a^2 positive.[6]

2.6.4.3 Estimation Results

$$\log X^d = -13.689 + \underset{(5.0685)}{0.733\ (PX/PW)} + \underset{(25.389)}{5.496\ YW}$$

$$R^2 = 99.0; \quad DW = 1.618$$

The estimated income elasticity has the expected positive sign and is significantly different from zero at 1-percent level. In contrast, the price elasticity of demand has an unexpected positive sign and is

6. It should be noted that while the sign of the real income elasticity (a^2) is usually assumed to be positive, it need not necessarily be so. For example, if the exports of a country were simply a residual demand by the rest of the world, i.e., the difference between world production and consumption of importables, then a^2 could be negative if increases in world income were associated with faster growth in the production than in the consumption of importables. For a fuller treatment of this arguement, see Magee (1975) and Khan and Ross (1975).

significantly different from zero. This could be due to multicollinearity between the export value (dependent variable) and relative export price caused by the fact that the export value has captured the relative price effects. The coefficient sign might be different if the quantity of export demand (measured in physical output) is used instead of export value as a dependent variable.

III. Export Promotion Policies

In the Malaysian context, the export-oriented strategy is more appropriately defined as a deliberate government policy with the explicit intention to increase exports, thus going beyond laissez faire. The main thrust of the export promotion programs is towards the expansion and diversification of export products and export markets. It involves various incentives and regulations, including tax exemptions and subsidies, double taxation and investment guarantee agreements, regulations on credit and interest rates, exchange control rules, provision and pricing of physical infrastructure (the important ones being the industrial estate and FTZ). As such, Malaysia's export promotion policies involves the formulation of fiscal, monetary and trade policies. The various types of incentives can be classified into three groups; trade-related incentives, investment incentives and other special incentives. In describing the current incentive system, it attempts to review important changes in order to understand in detail the current system.

3.1 Finance and Credit Facilities

In order to encourage the private sector to make concerted efforts towards the expansion and promotion of exports, various soft loan schemes/funds, and export financing facilities have been established by the Government and to a lesser extent, the international financial institutions. Basically, these schemes were set up to provide domestic exporters with credit facilities at preferential rates of interest and also other forms of assistance, among others, working capital for the exporters as well as providing a credit to foreign buyers. Pursuant to the national objective of promoting exports, two important financing schemes were implemented, namely the Export Credit Refinancing Facility (ECR) of the Central Bank and the Malaysia Export Credit Insurance Berhad (MECIB).

3.1.1 Exports Credit Refinancing (ECR)

An important financial incentive to promote the growth of Malaysian exports is the export credit refinancing facility established by the Central Bank in 1977. The ECR scheme comprises a post-shipment refinancing facility and a pre-shipment financing facility. The former is for the use of the exporters to obtain immediate funds upon shipment of eligible goods sold on credit terms, while the latter is to provide working capital to exporters and manufacturers in producing eligible goods for exports. The ECR facilities are available not only to manufacturer-cum-exporters but also to trading companies dealing with the producers and suppliers of raw materials and intermediate goods used in the manufacturing process. The objectives of the ECR scheme are to promote exports both of manufactured and agricultural products that have significant value-added

Table 4.3

UTILIZATION OF EXPORT CREDIT REFINANCING FACILITIES BY INDUSTRIAL SECTOR (PRE & POST SHIPMENT)

	Percent of Total			
	1980	1985	1990	1991
Articles of base metal	-	-	2.9	2.8
Chemical products	4.7	2.9	1.9	2.2
Food & beverages	10.5	6.4	4.3	3.0
Footwear & headgear	2.8	2.2	0.5	0.4
Mechanical & electrical pdts.	26.5	9.2	20.4	24.8
Misc. manufactured articles	-	-	5.1	5.4
Paper products	-	-	0.9	0.8
Precious stones & jewellery	-	-	0.4	0.1
Rubber & plastic products	5.9	8.3	17.7	15.8
Stoneware & glassware	-	-	0.8	0.8
Textiles & textile products	17.8	18.4	10.1	10.3
Vegetable & animal fats & oils	19.8	33.9	24.9	24.3
Vegetable & animal products	-	-	1.2	1.2
Wood products	6.0	9.9	8.9	8.1
Others	6.0	8.8	-	-
Total	100.0	100.0	100.0	100.0

Source: Bank Negara Malaysia.

and with high local content. The annual utilization of the ECR facilities increased significantly from about RM 140 million in 1977 to RM 17.8 billion in 1991 (see Table 4.3), while the amount of exports refinanced rose to 27 percent in 1991 from a mere 3 percent in 1977. This development reflected the growing importance of the scheme to promote Malaysian exports.

3.1.2 Malaysian Export Credit Insurance Berhad (MECIB)

MECIB was incorporated in 1977 with the main objective of providing insurance coverage up to 85 percent for exporters against the

Table 4.4

EXPORTS DECLARED BY MARKETS AND BY PRODUCTS

	Percent of Total			
	1988	1989	1990	1991
By Markets				
Western Europe	31.7	27.6	23.0	29.6
Eastern Europe	12.7	11.1	14.3	10.5
Asean	10.9	14.8	11.4	11.7
Other Asian Countries	11.4	14.2	8.2	19.2
Middle East	20.1	14.6	29.8	10.9
Australia & New Zealand	4.2	6.7	5.3	6.7
North America	7.1	9.4	6.8	7.1
Others	1.9	1.6	1.2	4.3
Total	100.0	100.0	100.0	100.0
By Products				
Food	9.8	11.0	7.6	11.0
Crude material inedible	24.1	14.8	16.1	12.7
Animal & vegetable oils & fats (excluding fuel)	9.6	12.0	8.5	14.8
Chemical & related products	0.8	1.7	2.6	2.4
Manufactured goods	14.6	18.1	28.0	20.0
Machinery & transport equipment	16.6	20.3	14.6	10.5
Miscellaneous manufacture	24.5	22.1	22.6	28.6
Total	100.0	100.0	100.0	100.0

Source: Malaysian Export Credit Insurance Berhad (MECIB).

risk of non-payment by the foreign buyers, and guarantee to commercial banks and other financial institutions against default of advances made to exporters or their suppliers. As at end-1992, the total number of policies remaining in force was 305 with a total face value of RM 2,103 million declared for insurance coverage. The total value of exports declared by markets and by products are shown in Table 4.4.

In recent years, MECIB has also been active in launching new schemes in response to the changing needs of its clientele. In March 1990, MECIB launched an export credit insurance/guarantee scheme to protect commercial banks and other financial institutions against non-payment of advances granted to direct and indirect exporters due to insolvency or protracted default. In August 1989, MECIB also introduced a Bond Indemnity Support Facility to meet the needs of contractors-cum-exporters who are unable to raise adequate collateral required by the commercial banks for the issuance of bonds to support overseas projects.

These facilities would enable the exporters to carry out their prime objective of developing exports into non-traditional or high risk markets and protecting their profits without the need to worry about bad debts. Hence, Malaysian exporters can venture into the overseas market with greater confidence and security and be more competitive.

3.2 Fiscal Incentives

The two major laws that provide rules concerning fiscal incentives on investments are the Investment Incentives Act (IIA), 1968 and the Industrial Coordination Act (ICA), 1975. The IIA replaced the Pioneer Industries Ordinance, 1958 whose basic provision called for an income tax exemption for the so-called pioneer industries. In 1986, the Promotion of Investments Act (PIA) was introduced to replace the IIA, 1968 and broadened the scope of incentives to include small- and medium-scale industries, tourist and hotel projects. The ICA was introduced to rationalize industrial development and to provide some directions on the type of industries which would be promoted, subject to compliance with guidelines on equity ownership and employment structure.

Basically, the main thrust of these initiatives is the identification of products and markets that have the greatest potential for growth and the provision of a set of policy measures that would be conducive to their growth. The tax incentives provided for under the PIA, 1986, gearing towards the promotion of exports are:

(i) Abatement of Adjusted Income for Exports[7] is granted to resident manufacturing companies exporting directly or through agents. The amount of the adjusted income to be abated is equal to a rate of 25 percent of export sales as to total sales;

(ii) An Export Allowance of 3 Percent[8] based on the f.o.b. value of export sales is granted to trading companies exporting manufactured goods purchased from manufacturers in Malaysia;

(iii) Double Deduction of Expenses for Promotion of Exports Overseas: Certain expenses incurred for the purpose of seeking opportunities for exports of manufactured products are eligible for double deduction. The expenses that qualify are:

- overseas advertising,
- supply of free samples abroad,
- export market research,
- preparation of tenders for the supply of goods overseas,
- supply of technical information abroad,
- public relations work connected with exports,

7. In the 1992 Budget, several amendments to export incentives (including the abatement of in come for exports allowance) would be implemented in three phases, culminating in the abolition of both incentives with effect from the year of assessment 1995:
Phase I: The amount to be abated under the abatement of income for exports would be deducted from the statutory income instead of the adjusted income; with effect from the year of assessment 1993;
Phase II: From the year of assessment 1994, the rate of abatement of income for exports would be reduced to a rate equivalent to 25 percent of export sales to total sales. In the case of export allowance, the rate would be reduced from 5 percent of the f.o.b. value of export sales to 3 percent; and,
Phase III: Both the export incentives would be abolished with effect from the year of assessment 1995.

8. Ibid.

- exhibits and/or participation in local or international trade fairs or industrial exhibitions,
- fares in respect of travel overseas by employees of companies for business,
- accommodation and sustenance expenses incurred for overseas business, and
- maintenance cost of sales offices overseas for the promotion of exports;

(iv) Double Deduction of Export Credit Insurance Premium: To encourage exporters to penetrate into non-traditional markets, premium payments on export credit insurance are eligible for double deduction; and,

(v) Drawback of Custom Duties and Exemption from Import Duties, Excise and Sales Tax: The purpose of granting exemptions and drawbacks is to provide relief from the burden of local taxes and duties to enable the exporters to offer competitive prices.

3.3 Institutional Arrangement

Malaysia perceived the urgency for a dynamic industrial policy to improve the resilience of the economy from external shocks on the commodity front. Early initiative taken under the industrialization strategy was to establish Free Trade Zones (FTZs) in selected locations across the country in order to encourage more direct exports. Where the establishment of FTZs were not practical, the Government had allowed the setting up of licensed Manufacturing Warehouses (LMWs).

3.3.1 Free Trade Zones (FTZs)

These are areas especially designed for manufacturing establishment producing or assembling products essentially for export. Manufacturers whose entire production is essentially for export, or whose raw materials or component inputs have to be substantially imported, are encouraged to locate their factories in the FTZs. Companies in the FTZs enjoy special privileges such as minimum custom formalities and control in their import of raw materials, parts, machinery and equipment, low-cost infrastructural facilities, and a completely free trade regime in addition to the normal incentives offered under the IIA. In addition, goods exported aboard from the FTZs are not liable to customs duties. It has successfully attracted large export-oriented

industries, mainly in the electronics and textile sectors. Until today, these industries provide the lead in manufactured exports. At present, there are twelve FTZs in Malaysia.

3.3.2 Licensed Manufacturing Warehouses

In order to encourage the dispersal of industries and to enable companies to establish factories for the manufacture of products mainly for the export market, where the establishment of a FTZ is neither practical nor desirable, the Government has allowed the setting up of Licensed Manufacturing Warehouses. These establishments are accorded facilities similar to those of factories operating in the FTZs.

3.3.3 Services of Trade Commissioners

The trade commissioners, the frontliners for trade promotion of Malaysian exports, provide the necessary market information and other supportive assistance for Malaysian exporters. In essence, the trade commissioner identifies trade opportunities for Malaysian exporters; services trade enquiries; undertakes market surveys; provides introductions for Malaysian businessmen to foreign firms, assists foreign businessmen visiting Malaysia; and, identifies and reports on changes in trade regulations and policies, and makes official representation on behalf of the Malaysian Government on matters relating to the entry and sale of Malaysian goods. In some trade offices, trade display areas are provided for the Malaysian exporters to exhibit their products.

3.3.4 Malaysian Export Trade Centre (MEXPO)

The Malaysian Export Trade Centre (MEXPO), in close liaison with the trade commissioners abroad, provides Malaysian exporters with up-to-date market information to help them gain access into the world markets. It supplies foreign buyers with information on the range of goods that are available in Malaysia for export and arranges meetings between foreign buyers and Malaysian exporters. An average of ten seminars are conducted annually by MEXPO on export practices, incentives, GSP and other matters related to exporting and trade opportunities aboard. MEXPO also publishes and circulates a number of publications for the benefit of Malaysian exporters. In line with the policy to develop Malaysia's external trade, the Government has established a new trade promotion organization, namely, the Malaysian

External Trade Development Corporation (MATRADE), which is expected to be operational in the first half of 1993. It is envisaged that MATRADE will replace MEXPO, with the former acting as a corporation which consolidates and coordinates all export promotional activities in the country.

3.3.5 Missions and Fairs Programs

An average of five trade fairs and five trade missions are organized annually by the International Trade Division of the Ministry of International Trade and Industry for the benefit of Malaysian exporters seeking market opportunities overseas. The Division also organizes other export promotion programs such as in-store promotions, fact finding missions and overseas buyers' mission to Malaysia.

3.3.6 Countertrade

In its drive to further promote the country's exports, the Government has embarked on countertrade as an additional trading arrangement to complement the existing trading practices. This additional tool of trade is intended to enable Malaysia to diversify and create additional exports; to seek new markets; to trade with countries which are lacking in foreign exchange; to improve the balance of trade position with specific countries; and, to save foreign exchange. A Countertrade Unit was established by the Ministry of International Trade and Industry to facilitate this relatively new form of trade arrangements.

3.3.7 Bilateral and Multilateral Negotiations For Better Accessibility of Malaysia's Exports

The Government through the International Trade Division of the Ministry of International Trade and Industry, undertakes on a bilateral and multilateral basis, negotiations for reduction and removal of tariff and non-tariff barriers that may be encountered by Malaysian exporters. For this reason, the Division is also actively involved in such international fora as UNCTAD, GATT and MTN.

So far, Malaysia had concentrated trading with E.C., U.S., Japan and Singapore. Generally, trade between Malaysia and other developing countries have been hindered by the lack of direct banking

relationship, trade information and business contacts. In the long run, it is to Malaysia's advantage to diversify the market and steps have been taken in this direction. Towards this end, since 1989, the Central Bank on behalf of the Government has designed a mechanism to promote trade through bilateral payment arrangements with Third World countries. The first bilateral payment arrangement was signed with Iran in August 1988, which provides guarantee payments for exporters. This has instilled greater confidence among traders, as it has converted normal credit risk into sovereign risk. To-date, a total of 16 bilateral payment arrangements have been signed.

3.4 Foreign Direct Investment

Foreign investment is a very important element in the Malaysian economy. Throughout the colonial days and until 1970s, it was foreign investment that played a predominant role in the growth of the primary sector, manufacturing and wholesale trade. As early as 1975, the foreign ownership of the corporate sector exceeded 50 percent. Although the share of domestic residents, especially the share of Bumiputera individuals and trust agencies, increased over time through strong Government initiatives to achieve the NEP objectives, the share owned by foreigners remained over one-third in 1983. In the manufacturing sector, foreign direct investment (FDI) has been strongly promoted by the Government through the provision of investment incentives, tariff protections, the FTZ facilities, liberal exchange controls and Investment Guarantee Agreements. Besides these incentives, political stability, a rapidly growing domestic market, low wage levels, and proximity to other markets have contributed to the great surge of foreign capital over the years. Unlike many other developing countries, the Malaysian Government opened the manufacturing sector to foreign direct investment and tried to maximize the benefits of increased production, employment and technology transfer in the manufacturing sector.

In order to stimulate industrial and export growth, several policy reforms were undertaken in the manufacturing sector in the second half of the 1980s. The licensing requirement under the ICA of 1975 was liberalized in 1985 and 1986. Under the amended guidelines, only manufacturing firms with shareholders' funds of RM 2.5 million and above or engaging 75 or more full-time employees are required

to apply for a license. In addition to the amendments in the ICA, generous incentive packages under the PIA of 1986 were also provided. The foreign equity participation rules were relaxed under the Act for both export-oriented and domestic-oriented industries.

Since the liberalization of investment policies, foreign investment flowing into the country rose sharply from RM 959 million in 1985 to RM 17.6 billion in 1990 based on manufacturing projects approved for establishment. Unlike in the 1970s and early 1980s, when foreign direct investments were mainly in the oil-related, electronics and textile industries, the current influx of foreign capital covered a broader range of industries. At one end are several large industrial projects costing above RM 500 million each, involving the production of iron and steel products, petroleum products and petrochemicals. At the medium-cost range are a large proportion of foreign companies with projects involved in the manufacture of chemical products, electrical and electronics products, wood and wood products, textiles and apparel, and basic machinery. At the same time, there are emerging signs of industrial integration taking place, with a number of large multinational companies setting up subsidiary companies to manufacture the necessary component parts to support their end-products.

3.5 Small and Medium Scale Industries (SMIs)

The export expansion has been principally generated through foreign multinational companies which dominated the output of the FTZs. The FTZ strategy adopted in the 1970s resulted in an enclave of MNCs in the FTZs which provided very little linkages effects to the domestic economy. In line with the recommendations of the IMP, linkages between the large, small and medium industries (SMIs) were actively promoted to spur a healthy industrial development.

In this regard, the development of the SMIs was found to be essential in promoting linkages and acting as a catalyst for the growth of the economy, thereby strengthening and widening the industrial base, especially for the enhancement of export-led growth. Various facilities and incentives were introduced to spur the development of the SMIs which include the creation of funds for relocation, R&D and export purposes.

3.5.1 Incentives

Most of the Government's past incentive programs tended to favor the large industries as it was linked mainly to the size of investments and employment, and therefore did not adequately cater to the needs of the SMIs. Hence, in recognizing the important role of the SMIs in the country's industrialization drive, the Government has rectified this bias against the SMIs to ensure their full potential. This has been shown in the Promotion of Investment Act, 1986 and Income Tax (Amendment) Act, 1986 which provided the following:

- The pioneer incentives provide full tax exemption on profits for a period of five years commencing from production day irrespective of the level of investment, thus enabling many SMIs eligible to apply for the pioneer status. However, companies which apply for and are granted the incentives on or after 1 November 1991, will now pay tax on 30 percent of their statutory income.
- In the Investment Tax Allowance, the abatement of adjusted income for export is now no longer applicable only for the larger industries. Both small to large industries are eligible for this incentive provided they meet the criteria set under the incentive.

Under the export incentives, SMIs were provided with the following incentives:

- double deduction for promotion of export expenses;
- double deduction for premium credit insurance for exports; and,
- Industrial Building Allowance which consists of an initial allowance of 10 percent and an annual allowance of 2 percent.

3.5.2 Financial Assistance

The Government has established a number of financial institutions and implemented various policy measures and programs to make credit more available to SMIs. Among the major institutions providing financial assistance to the SMIs are Bank Industri, Bank Pembangunan, Credit Guarantee Corporation of Malaysia Berhad (CGC), Malaysian Industrial

Development Finance (MIDF), Majlis Amanah Rakyat (MARA) and the Standard and Industrial Research Institute of Malaysia (SIRIM).

To further develop the SMIs, an Industrial Technical AssistFund (ITAF) for SMIs was initiated in early 1990 with an initial allocation of RM 50 million. This fund was set up for the purpose of providing grants to SMIs which participate in any of the following schemes: feasibility study scheme; product development and design scheme; quality and productivity improvement scheme and market development scheme. The Fund would certainly help to enhance the development of the SMIs into a progressive, high quality and modern industry capable of supporting the large industries.

IV. Problems and Issues on Export Promotion

The export-oriented strategies formulated to develop the export sector constituted a major feature in the country's effort for industrialization. Growth of the sector was stimulated by a proliferation of incentives, as well as the liberalization and deregulation policies, which, encouraged the expansion of goods and services. A notable feature was the reliance of the private sector on the Government for new and additional incentives including export promotional measures. The overperformance of the export sector, in particular the manufacturing sector was largely attributed to the following reasons:

(i) Favorable External Environment: During the 1980s, the world economy experienced the longest post-war economic expansion, recovering strongly from the recession of the early 1980s. Output growth was 3.1 percent annually during the period 1986-1990, compared with 2.5 percent annually during the period 1980-1985. During the same period, world trade expanded from 2.5 percent per annum to 6.7 percent. The positive external developments worked favorably for Malaysia's open-economy with exports accounting for more than 76 percent of GNP in 1991.

(ii) Prudent Domestic Economic Management: Prudent macroeconomic policy management has permitted the economy to undertake a series of comprehensive structural adjustments in the 1980s in response to the global and domestic recessions in the early and mid-1980s, respectively. The

Government's consolidation efforts and policy reforms in both the fiscal and monetary areas to promote private initiative and stable growth resulted in a strong economic upturn in the late 1980s. The low domestic inflation combined with a flexible exchange rate policy has helped to enhance the competitiveness of Malaysian products.

(iii) Large Influx of Foreign Investment: Since the liberalization of investment policies, foreign investment has contributed substantially for the development and growth of the manufacturing sector, particularly during the period 1985-1990. The large influx of private investment in manufacturing resulted in corresponding increase in the value added of the manufacturing sector. Manufacturing value-added increase to 13.7 percent per annum compared to the 9.1-percent target in the IMP. Manufacturing share in GDP surpassed that of agriculture in 1987 to become the main contributor to the country's GDP. By 1991, the share has grown to 27 percent as opposed to the 22.4 percent targeted in the IMP.

(iv) Realistic Exchange Rates: The surge in exports was also partly caused by the effective depreciation of the ringgit against the major trading partners, particularly the U.S. dollar and Singapore dollar. The depreciation of the ringgit has enhanced the nation's competitiveness in the international market as far as prices are concerned. The policy of non-intervention in the management of the exchange rate regime was to allow the ringgit to find its own level in the market so that international competitiveness of the nation's exports would be maintained.

4.1 Structural Weaknesses in the Export Sector

Despite some measure of success in the nation's export diversification drive, there remained several major structural issues that have dampened the export sector. Although the nation has begun to address these issues, the structural weaknesses have yet to be completely overcome.

4.1.1 Export Concentration

Significant progress has been made in broadening the export base away from agriculture and mining to manufactured products. Within

the primary commodities sector, the export base has been well diversified, with the emergence of new sources of export earnings such as palm oil, timber and cocoa in addition to rubber and tin. This was a reflection of the success of the agricultural diversification policy. However, the manufacturing base lacks depth and remains narrow in scope and operation, with electrical machinery and appliances, textiles and rubber-based products dominating the export of manufactures. Together they account for about 32 percent of the total manufacturing output and close to 70 percent of the sector's export earnings. As such, any shift in the export demand for these products would imply serious repercussions on the entire industry as well as on the manufacturing sector.

4.1.2 Export Market Concentration

There is also concentration in terms of market destination for Malaysian exports. The major markets, namely, Japan, the U.S., Singapore and the E.C. together accounted for nearly 50 percent of total exports as at end-1991. As a result, cyclical fluctuations in the economic performance of these countries would affect the export performance of Malaysia, which is often transmitted to the entire economy adversely and pervasively.

Over the last two decades, some degree of diversification has been achieved. A study by Jaafar[9] has shown evident of diversification in terms of product by measure of concentration. In terms of primary products classified under SITC 0-4, food under SITC 0,1,4 and raw materials SITC 2 and 3, the trend has been quite distinct, indicating a lower degree of concentration or greater product diversification. Among the two categories of food and raw materials, food achieved the highest degree of diversification with a measure of 0.11, compared with 0.31 for raw materials.

4.1.3 Export Volatility

While gross exports expanded at an average annual rate of 11 percent in the 1980s (17 percent in the 1970s and 5 percent in the 1960s), it fluctuated year to year, with three periods of export declines attributable largely to external factors; either a recession or slowdown

9. Jaafar Ahmad (1989a), "Export Volatility and Stabilisation", paper presented at the North South Institute Seminar on Commodity Issues, Ottawa, Canada.

in the economies of the industrial countries which resulted in an across-the-board decline in commodity prices. Though the diversification program managed to soften the adverse impact, the slower pace of diversification could not compensate for the declining commodity prices. Therefore, fluctuations in the terms of trade can cause wide swings in the export sector, which are normally translated into sharp swings on national income as evidenced in the mid-1980s. When primary commodity prices collapsed in the mid-1980s, the resulting 15.5 percent of trade loss induced an unprecedented fall in the aggregate consumption in Malaysia by nearly $3 billion or a decline of 10 percent in nominal terms.

The volatility in the terms of trade has resulted in a high degree of instability for Malaysia. Among the reasons are the large share of commodities in the total gross exports, the high degree of export market concentration and the inelasticities of demand and supply of most primary commodities. In a study by Erb and Shiaro-Compo (1969), it was found that the instability index for West Malaysia was high at 39 compared with the average of 17.6 for 18 developed countries and 23 for 45 developing countries, for the period 1954-1966. A similar study by Leigh (1970) confirmed further the higher instability index for Malaysia (19.6 percent), as against 7.9 for developed and 12.0 for developing countries.

The diversification efforts over the last two decades have resulted in somewhat greater stability for Malaysian exports. Based on studies by Bank Negara, it was found that while individual commodities tended to exhibit sharp fluctuations, both in volumes and prices, the instability was lesser when all the commodities were considered together. The improvement, in terms of lower instability, was more pronounced when manufactured exports are included. For instance, based on quarterly data, the index of gross export instability fell from 0.9 in the 1960s to 0.5 in the 1970s, and it fell further to 0.48 in the 1980s.

4.2. International Comparison of Malaysia's Position in Terms of Export Diversification and Concentration Index

The cross-country analysis among the ASEAN nations and the NICs, namely Taiwan, Hong Kong and Korea revealed that Malaysia has achieved commendable progress in diversifying its export structure as reflected by the improvement in the index of concentration which fell

from 0.303 in 1980 to 0.204 in 1988. In terms of export diversification index, it appeared that Malaysia performed relatively well compared to Singapore, Taiwan, Korea and Thailand.

4.3 Issues and Implications

Having examined the weaknesses underlying the export sector, this section looks at some issues and choices in the country's export promotion policy for the 1990s. These included the issues of choice of products, scale and type of technology and skills, internal linkages, services, incentives and trade barriers.

4.3.1 Niche Strategies

What type of products should our industrial sector be producing or expanding into? This is a crucial question for it has a bearing on whether industrialization should be market-led or decided by government intervention in terms of picking the potential winners; on the choice of technology; the possibility or desirability of import substitution; export potential, acquisition of requisite technology and skills and the issue of the optimum balance between the participation of foreign and local firms.

At this juncture, the manufacturing base still lacks depth and remains narrow in scope and operation. The linkages between and within industries are still not well developed. Despite the massive inflow of FDI, the links between MNCs in FTZs and local firms have been poorly developed. For example, the electronics and electrical equipment industry has become one of the leading export-oriented industries in Malaysia, exporting almost all of its production (99.2 percent). The foreign-owned firms in the FTZs accounted for 87 percent of total exports. The situation is the same for the textile industry which has now become the second largest export-oriented industry. Foreign firms in the FTZ exports 92.4 percent of textile production. Although FTZ firms are contributing to the Malaysian economy in terms of expansion for production, exports and employment, they have established minimal linkages with the local firms. A recent study on linkages between multinationals and local firms revealed that the local content ratio of foreign-owned firms operating in the FTZs is only 2 percent for the electrical and electronics industry, and even lower (0.5 percent) for the textile industry.

Table 4.5

EXPORT DIVERSIFICATION AND EXPORT CONCENTRATION INDICES 1/

	Export Diversification Index			
	Number of Commodities Exported	1980	Number of Commodities Exported	1988
ASEAN				
Malaysia	214	0.663	215	0.640
Singapore	232	.581	231	0.473
Indonesia	144	0.695	192	0.716
Thailand	176	0.758	207	0.630
Brunei Darussalam	45	0.770	42	0.918
NICs				
Taiwan	210	0.652	217	0.525
Hong Kong	164	0.780	173	0.659
Korea, Republic of	207	0.649	215	0.520

	Export Concentration Index			
	Number of Commodities Exported	1980	Number of Commodities Exported	1988
ASEAN				
Malaysia	214	0.303	215	0.204
Singapore	232	0.235	231	0.143
Indonesia	144	0.530	192	0.253
Thailand	176	0.201	207	0.121
Brunei Darussalam	45	0.680	42	0.645
NICs				
Taiwan	210	0.117	217	0.093
Hong Kong	164	0.164	173	1.141
Korea, Republic of	207	0.085	215	0.098

1/ The concentration index discriminates more finely between countries which are relatively more concentrated in their export structure; the "diversification index" discriminates more finely between countries which are relatively more diversified. Both indices range between 0 and 1.0 with the latter representing the most extreme concentration.

Source: Based on UNCTAD secretariat calculations.

From Malaysia's point of view, FDI should be viewed not only as a transfer of money from the investing to the host country, but also as a transfer of "structural resources" such as know-how in production, management, technology, marketing and human resources.

Within the above scenarios it may not be possible to devise niche strategies for selected products at this time. But within the current level of development, the thrust of industrial development will be to produce export-oriented, high value-added and high technology industries with a view to widen and deepen the sector. This means a move towards capital intensive and technologically sophisticated industries producing better quality and competitive products across all industrial sub-sectors.

4.3.2 Incentive System

The evidence suggests that countries industrialize more successfully if intervention results in neutral incentives. A study has shown that the system of protection has discriminate against export-oriented industries in favor of import-substitution production. On the sectoral level, industries producing textiles and apparel products and electronic products exhibited the largest drop in the effective rate of protection. For example, the electronics and electrical machinery recorded negative ERP and net subsidy equivalent of 4 percent and 95 percent, respectively. Thus, the current incentive scheme must be periodically reviewed and revised to reinforce the market mechanism with the objective of achieving an export-oriented and resilient private sector-led economy. The underlying issues in this review is to remove any existing distortions, inconsistencies and ineffectiveness as well as the relatively high level of protection to industries. The focus will be to provide more effective, broad-based, sector and sub-sector neutral investment incentives aimed at self-reliance and the creation of competitive and efficient export-oriented industries.

4.3.3 Human Resource Development

The Malaysian products have to maintain their edge in terms of cost and quality in the highly competitive global environment, thus our work force has to be continuously conscious about productivity, efficiency and quality. As the industry grows, its sophistication grows as well. This creates a stronger demand for more skilled manpower, which implies that human resource development is an important element for

the industry to withstand competition and to enter into the world market. Therefore, the main thrust of human resource development should be geared towards the enhancement of the workforce through education and training, concurrent with the shift in the industry towards higher product quality. This will require policies formulation to encourage greater collaboration between the public and private sectors to undertake skill development in response to market signals. This will ensure that the supply of labor is relevant to industrial needs and to reduce future skill mismatches. A well-trained and skilled manpower, technically-oriented with a set of industrial values are essential to maintain a productive and competitive entity that will ensure the maintenance of Malaysia's competitive edge in the world market.

4.3.4 Technology Development

The level of quality and design competence have to be raised substantially in order to exploit the tremendous investment and export opportunities through greater product differentiation and sophistication arising from technology, quality and design variation. The expected policy on technology is to reduce dependence on multinationals, accelerate the modernization of plant, the location of high-tech industries and the growth of relevant R&D activities. At the company level, strategies include those that are aim at encouraging greater international marketing and export efforts, the upgrading of expertise of local personnel to enhance the process of technological transfer. The issue is how to increase the level and pace of our technological development in order to achieve the targeted rate of growth. There is also an urgent need to increase the importance of R&D and S&T as basic investment components of development in order to move 'up-market' in the industrialization process. We must find more innovative and speedy ways to redouble the R&D efforts if we are to make a quantum leap into an industrial sector which is more 'up-market' and capital intensive and to maintain Malaysia's competitive edge in an increasingly compeitive world trading environment.

4.3.5 Trade Barriers

While Malaysian exports do face protectionist barriers in the developed countries, the specter of protectionism is less acute than that faced by the NIEs like South Korea, Taiwan, Hong Kong and Singapore. This is mainly due to the fact that Malaysia is a small producer and exporter

of manufactured goods, unlike the NIEs. Therefore, Malaysia has yet to feel the full impact of protectionism in the developed countries. One may also argue that in the absence of protectionist barriers, the Malaysian exports would have performed better.

This would have been a possibility in the near future, as Malaysia's industrialization process reaches its advanced stage, and with the developed countries' changing perspectives and opinions on the Malaysian economy. By then, the international environment may make the export-oriented strategies less effective for Malaysia, if we are not prepared to take appropriate action. Of immediate concern to Malaysia are the tariffs imposed on textiles, footwears, wood products, and electronics goods. However, it should be stressed that tariffs have become increasingly less important over the years as instruments of protection. Tariffs have been cut mainly through the various rounds of multilateral trade negotiations under the auspicious of the GATT. It is the non-tariff barriers that pose the greatest threat to Malaysian exports. Among them are quantitative import restrictions, voluntary export restraints and orderly marketing arrangements. These are far more dangerous than tariffs, which involve administrative direction rather than open rules of protection and are based on bilateralism rather than multilateralism.

V. Policy Recommendations

This section presents some of the policy measures that would enhance the nation's export competitiveness in the context of promoting the development of the manufacturing sector in Malaysia.

5.1 Revising the Current Incentive System

In order to promote an effective export driven economic development, it is absolutely necessary to ensure that the overall incentive structure does not discriminate between production for the domestic market and exports, nor between purchase of domestic goods and foreign goods. Lowering the tariff protection for the import-substitution sector will free resources from industries which cannot successfully compete with foreign products. These resources, in turn, can be employed by the export-oriented industries which will become

more profitable as tariffs on inputs are reduced. Therefore, Malaysia should gradually move to a low uniform tariff system with some exceptions such as the duty-drawback for exports. Gradual lowering of protection in those heavily and long protected industries will certainly encourage greater competition, boosting up exports and possibly expanding growth. The relevant industries should by now be efficient enough to compete with foreign competitors. This step is consistent with GATT and AFTA in advocating free trade.

5.2 Indentification and Creation of New Market Niche

The export-led industrialization strategy must necessarily be sustained over the longer term by a constant search for market niches for our products. Continuous effort should be made to expand market shares within existing as well as new and non-traditional markets. These can be developed through the following mechanisms:

5.2.1 Expanding Intra-ASEAN Trade Opportunities

There is great potential to further expand the intra-ASEAN trade, particularly exports of manufactured products under the ASEAN Preferential Trading Arrangements (PTA). Trade under the PTA is still relatively small. However, exports under PTA has shown significant increases from RM 37 million in 1985 to RM 336 million in 1990. This was attributed largely to the competitiveness of Malaysian exports in the international market. Trade under PTA, however, has not been fully harnessed since the exports of ASEAN member countries tend to be in competition with each other. In addition, there is a tremendous opportunity to increase our exports through a comprehensive export-targeting program, following the establishment of an Asean Free Trade Area (AFTA), mainly through the adoption of the Common Effective Preferential Tariff (CEPT) Scheme, within a 15-year period beginning 1 January 1993, with the ultimate effective tariffs ranging from 0 percent to 5 percent for 15 groups of products.

5.2.2 The Generalized System of Preferences (GSP)

One of the major issues related to the GSP schemes was the inability on the part of the Malaysian exporters to fully utilize the benefits due to certain constraints, such as the limited product coverage and the

stringent rule of origin requirements. Nonetheless, exports under GSP totaled RM 8.1 billion in 1990, the highest ever achieved since Malaysia was first given the GSP benefit in 1979, reflecting substantial progress made on the part of the exporters to fully utilize the GSP benefit scheme. Currently, about 3,500 companies have registered with the Ministry of International Trade and Industry to use the GSP export scheme. In this regard, inculcating greater awareness of the benefits of the schemes would therefore be beneficial to the nation in enhancing its export capabilities. However, the exporters should be cautioned that the GSP benefits and other such facilities are not permanent features in the export markets. They should therefore develop their products and services to be able to compete in the open market, one that is without protection and preferential treatment. This will require exporters to continually enhance their competitiveness by improving efficiency and productivity of trade operations as well as the design and quality of products.

5.2.3 Intensifying South-South Trade

So far, Malaysia has concentrated on trading with the EC, the U.S., Japan and Singapore. In the long run, it is to Malaysia's advantage to seek new export markets by forging ties with non-traditional markets such as the Middle East countries, the African continent and Latin American countries. The export of manufactured goods from the South to the South gained greater importance than other exports, particularly in recent years, with its share increasing from 40.1 percent in 1970 to 45.1 percent in 1980 and 59.2 percent in 1987, reflecting the increasing orientation of activities in the developing countries towards industrialization. Already intra-South trade has picked up to increase at an average annual rate of 11.5 percent compared with 2.1 percent during the period of 1984-1986. Moreover, as a greater number of developing countries move toward industrialization and expand their manufacturing sectors, there is scope for increasing intra-South trade in manufactures, through creating new trade as well as diverting trade from the North which is presently the major supply source of manufactures for the developing countries. Towards this end, the Government should step up its efforts to strengthen and expand trade facilities for export by establishing more bilateral and multilateral payments arrangement, promoting sufficient trade information and intensifying more direct banking relationships to facilitate trade financing.

5.2.4 Revitalizing the Export Targeting System

One of the effective ways of increasing exports is through the continued usage of the Export Targeting System with further refinement. Rather than focus on the targeting for export "products", we should also focus on "targeting of foreign markets" for the products to reap maximum economies of scale in the innovative industries, that is, the level of "foreign market" in which the specific products should penetrate, and the steps needed to further encourage exports. Some progress has been made with respect to the establishment of the Market Targeting System. A number of criteria has been established, and these include market size and rate of growth, market access conditions and the availability of infrastructure and support facilities. Based on these criteria, Japan, the U.S. and the EC have been selected as target areas.

5.3 Product Standards and Quality

Standard and quality control systems will play a vital role in enhancing exports as more value-added products are produced. Within this context, R&D and innovation activities on product development and production efficiency should be intensified to ensure that products are consistent in quality and competitive in price. The adoption of advanced technologies should be encouraged for it has been proven that there exists a strong causal relationship between technological level and international competitiveness. A fundamental pre-condition for the success of such a strategic approach is that it should involve the private sector. In this regard, the Government need to create a conducive environment for fostering the growth of indigenous new technology-based firms. Special incentives to promote these firms will be introduced including grants to cover start-up costs as well as assistance in market search and in mobilizing venture capital.

5.4 Effective Human Resource Development

To sustain Malaysia's export competitiveness, it is crucial for the industries to upgrade their technology and modernize their operations to remain competitive. Therefore, there will be an increasing need for trained manpower that could take advantage of information-based manufacturing technologies as well as current managerial and organizational techniques adopted by industries worldwide. It is crucial to improve the current skill delivery system to enable it to respond

more effectively to the rapid demand. Greater involvement of the private sector in training and skills upgrading will be actively promoted in the organizational and planning of courses offered in public sector training institutions and universities. Towards this end, a Human Resource Development Fund has been launched recently in order to promote greater public-private sector cooperation, especially in skills training. Overall, the policy direction should emphasize localization of industries and development of high calibre technological manpower.

5.5 Institutional Support to Enchance Export

The promotion and development of exports should be further strengthened. In this respect, the Government should consider the establishment of trade promotion centres abroad as well as rationalize existing trade representation with a view to avoiding duplications and strengthening export promotion. An efficient information system should be established to further improve the collection and dissemination of market information in order to strengthen market analysis and international market intelligence for our exports.

Trade and industry associations should also be encouraged to carry out overseas marketing surveys as well as to gather trade information for their members to understand the external market demands and technological development. This will enhance the development of an international market-oriented approach that will influence relative cost and competitive position as well as product differentiation.

The Government, in cooperation with the private sector, should continue to organise trade fairs and missions to overseas markets, including the non-traditional markets. The Export Promotion Council will continue to assume a vital role in the formulation of export promotion programs and trade facilitation measures to assist Malaysian exporters.

VI. Summary and Conclusion

The paper attempted to provide a broad review of the export promotion policies undertaken by the Government to promote the development of the export sector of Malaysia with particular emphasis on spearheading the exports of manufactured products. It highlighted

the main structure of exports as well as associated weaknesses that often contribute to fluctuations in the performance of exports and general economic activities of the country. Notwithstanding such instability, the country has achieved an impressive record in terms of high growth that has been sustained over a prolonged period of time, which by now has spanned over three decades. The achievement over the past two and a half years has been very encouraging when economic growth averaged almost 9 percent per annum and export growth reached nearly 25 percent annually. The rapid expansion in the export sector was brought about by the effective implementation of policy measures aimed at diversifying and broadening the domestic base so as to buffer the Malaysian economy against the vagaries of external demand. The key to this remarkable success lies in the strategic promotion of an open economy, driven by a vigorous export sector in an environment of flexible prices and prudent macroeconomic management.

Malaysia's rapid industrialization has now reached a cross-road where it is imperative that in order to meet the tougher, more difficult international environment, an adequate and professional export support system is necessary to underpin the country's export drive. Malaysia should concentrate on export-oriented activities, even though there are risks associated with this approach; risks such as vulnerability to external fluctuations and to protectionism. The adverse impact of cyclical changes can be ameliorated through prudent macroeconomic management of the economy, while protectionist barriers may be overcome by such measures as market diversification, product diversification and differentiation, improved productivity and research and development (R&D) innovations.

REFERENCES

1. Abdullah Mohd. Tahir, ***Industrial Policy and Industrial Development: Issues and Policy Directions***, Paper presented at the Seminar on Managing Industrial Transition: Policies for the 1990s - organized by the Institute of Strategic and International Studies (ISIS) on 2-3 September 1991.

2. Bank Negara Malaysia, ***Annual Report***, various issues

3. Charette, Michael F., *Determinants of Export Instability in the Primary Commodity Trade of LDCs*, ***Journal of Development Economics***, 18, 1985.

4. Edwards, Chris, ***Tariff and Trade-Related Policies***, Paper presented at the Seminar on Managing Industrial Transition: Policies for the 1990s - organized by ISIS on 2-3 September 1991.

5. Ismail Muhd. Salleh, ***Non-Tariff Incentive Policies***, Paper presented at the Seminar on Managing Industrial Transition: Policies for the 1990s - organised by ISIS on 2-3 September 1991.

6. Lam, N.V., ***Export Instability, Expansion and Market Concentration***, ***Journal of Development Economics***, 7, 1980, pp. 99-115.

7. Mohamed Ariff, ***Managing Trade and Industry Reforms in Malaysia***.

8. _____, *Malaysia Exports and Trade Barriers*, ***Malaysian Journal of Economics Studies***, Vol. XXVII, June and December 1990.

9. Mohamed Ariff, and Hal Hill, ***Export-Oriented Industrialisation: The Experience***, Allen & Unwin Australia Pty. Ltd., 1985.

10. Mohamed Ariff, and Joseph L.H. Tan, *ASEAN and The Pacific*, ***ASEAN Economic Bulletin***, Vol. 8, No. 3, March 1992.

11. Mohd. Yusof Ismail, ***Export Competitiveness: Objectives and Performance of IMP***, Paper presented at the Seminar Kebangsaan - Pembangunan Ke Arah Ekonomi Perindustrian on 13-14 November 1989.

12. Osman Rani Hassan, and Mohd. Haflah Piei, ***Malaysia's Industrialization and Trade: Issues, Options and Strategies in 1990s*** - Paper presented at the Seminar Kebangsaan - Pembangunan ke arah Ekonomi Perindustrian on 13-14 November 1989.

13. Warr, Peter G., *Malaysia's Industrial Enclaves: Benefits and Costs*, ***The Developing Economies***, XXV-1, March 1987.

14. Yeats, Alexander J., *Developing Countries Exports of Manufactures - Past and Future Implications of Shifting Patterns of Comparative Advantage*, ***The Developing Economies***, XXVII-2, June 1989.

MALAYSIA: COMPOSITION OF EXPORTS
(RM Million)

Groups	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
Food & live animals	284	316	361	441	514	593	799	827	872	1082	1013	1135	1153	1273	1480	1662	1965	2458	2851	3130	3391	3652
Beverages & tobacco	22	23	28	21	24	28	28	23	16	21	29	30	22	28	28	26	37	57	83	80	95	169
Crude material,inedible	2778	2392	2249	4157	4516	3231	5668	5976	6360	9025	9105	7710	7583	8262	8121	7248	7868	10583	12418	12667	11468	11140
Mineral fuels	366	503	320	372	833	967	1905	2101	2343	4346	6898	7147	7981	9301	11435	12051	8006	8911	8731	11003	14595	14659
Animal/vegetable oils & fats	310	423	412	560	1370	1509	1378	1979	2106	3016	3131	3376	3256	3829	5868	4845	3610	4168	5763	6198	5680	6227
Chemicals	36	39	46	67	80	79	82	87	102	131	172	192	236	294	427	428	605	736	1221	1233	1298	1667
Manufactured goods	1183	1112	1218	1318	1966	1624	2133	2324	2825	3315	3691	3281	2626	3035	2555	3095	2587	3710	4488	5721	6320	7360
Machinery & transport equipment	84	84	91	142	399	573	740	1001	1816	2535	3238	3325	4335	5653	7323	7059	9010	11701	15666	21987	28419	38866
Misc. manufactured articles	43	49	72	226	396	529	609	545	496	604	738	700	754	902	1196	1391	1500	2619	3830	5621	7943	10320
Misc. transactions & commodities	58	78	58	70	97	97	100	95	138	147	156	214	163	195	214	212	133	283	210	187	438	438
Total exports	5163	5017	4854	7372	10195	9231	13442	14959	17074	24222	28172	27109	28108	32771	38647	38017	35319	45225	55260	67825	79646	94497
Manufactured exports	614	605	723	1119	1691	2020	2485	2676	3664	4860	6319	6384	7512	9748	12467	12471	15352	20344	26850	36572	46841	61347
Non-manufactured exports	4549	4412	4131	6253	8504	7211	10957	12283	13410	19362	21853	20725	20596	23023	26180	25546	19967	24881	28410	31253	32805	33150
Services exports	582	589	555	731	1371	1457	1578	1984	2490	3117	4284	5078	5447	5883	6234	6562	6810	8137	9420	11336	15897	16632
Total exports (Goods & services)	5745	5606	5409	8103	11566	10688	15020	16943	19564	27339	32456	32187	33555	38654	44881	44579	42129	53362	64680	79161	95543	111129
Merchandise imports (c.i.f.)	4288	4416	4543	5934	9891	8530	9713	11165	13646	17161	23451	26604	29023	30795	32926	30438	27921	31934	43293	60858	79119	100831
Services imports	1444	1467	1461	1928	3114	3179	3726	4570	5827	7975	10097	10390	12023	14981	17047	16953	15600	16546	19600	22728	25620	28933
Export/Import ratio	120.4	113.6	106.8	124.2	103.1	108.2	138.4	134.0	125.1	141.1	120.1	101.9	96.8	106.4	117.4	124.9	126.5	141.6	127.6	111.4	100.7	93.7
Trade balance	875	601	311	1438	304	701	3729	3794	3428	7061	4721	505	-915	1976	5721	7579	7398	13291	11967	6967	527	-6334
Current a/c balance	25	-329	-698	246	-1307	-1187	1474	1074	249	2033	-620	-5633	-8409	-8117	-3917	-1522	-316	6642	4739	-574	-4410	-12459
Overall BOP	68	203	389	576	452	171	2054	755	625	1789	1002	-1093	-614	-55	312	3209	4345	2893	-1104	3332	5365	3427
GDP at current prices	11829	12955	14220	18723	22858	22332	26085	32340	37888	46424	53308	57613	62599	70444	79550	77470	71594	79625	90861	101463	115140	129144
GDP at constant prices	11829	13016	14238	15904	17227	17365	19373	20875	37887	41428	44511	47601	50445	53583	57742	57093	57751	60863	66303	72435	79550	86551
Budgetary surplus/deficit	-475	-1050	-1371	-1049	-1381	-1901	-1705	-2476	-2249	-1535	-3704	-9015	-10421	-6933	-4775	-4407	-7506	-6153	-3290	-3410	-3436	-2641
Rate of inflation	1.9	1.6	3.2	10.5	17.4	4.5	2.6	4.7	4.9	3.6	6.7	9.7	5.7	3.7	3.6	0.4	0.6	0.8	2.5	2.8	3.1	4.4
Ave. exchange rate against US$	3.080	3.020	2.805	2.445	2.406	2.402	2.542	2.461	2.316	2.188	2.177	2.303	2.335	2.321	2.343	2.482	2.581	2.519	2.618	2.708	2.704	2.750

MALAYSIA: GROSS EXPORTS BY MAJOR COUNTRIES
(RM million)

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
ASEAN	1280	1339	1282	1828	2439	2234	2889	2830	3179	4862	6298	7261	8539	9325	10309	9805	7878	10902	13481	17284	23048	27659
Singapore	1113	1127	1130	1707	2208	1874	2455	2386	2768	4227	5385	6178	7021	7369	7900	7357	6091	8198	10689	13395	18052	22030
Thailand	45	77	39	35	94	140	174	211	230	326	409	452	1033	1343	1090	1297	924	1289	1086	1665	2787	3013
Indonesia	33	29	38	38	52	61	58	46	44	51	75	135	90	139	235	163	138	369	735	1121	921	1386
Philippines	89	106	75	48	85	159	202	187	137	258	429	428	302	379	852	912	633	813	825	881	1065	908
Brunei	...	...	...	...	...	...	...	...	...	...	...	68	93	95	232	76	92	233	146	222	223	323
EEC	999	922	1045	1625	2175	2149	2827	2968	3131	4310	4774	4129	4217	4785	4876	5504	5229	6433	7984	10434	11863	13980
United Kingdom	343	329	341	584	674	554	662	768	815	944	779	804	772	895	988	979	1243	1432	1933	2540	3136	4139
Netherlands	163	166	249	274	559	773	890	987	952	1357	1691	1608	1691	1791	1574	2229	1220	1568	1679	2423	2095	2280
West Germany	162	137	153	279	396	396	577	559	618	886	1017	794	825	1056	1181	1005	1289	1542	1896	2417	3097	3421
Other	331	290	302	488	546	426	698	654	746	1123	1287	923	929	1043	1133	1291	1477	1891	2476	3054	3535	4139
Japan	945	914	833	1336	1719	1338	2835	3049	3693	5668	6429	5728	5726	6429	8633	9272	8053	8825	9347	10904	12589	14840
United States	670	637	670	799	1430	1489	2094	2718	3183	4183	4609	3539	3224	4335	5238	4891	5939	7484	9611	12679	13487	15984
Hong Kong	64	80	87	108	123	106	168	195	265	411	529	546	537	568	551	514	806	1273	1920	2085	2523	3172
China	67	55	77	200	211	128	113	294	251	397	471	204	258	364	387	399	422	703	1089	1302	1675	1761
USSR	212	152	102	254	421	243	302	295	325	567	631	596	558	701	496	458	336	383	338	677	370	224
Australia	116	92	89	151	219	179	304	257	304	425	403	470	523	462	600	650	735	1006	1353	1547	1326	1614
India	19	29	43	75	62	65	75	391	566	510	621	694	520	789	1397	1073	929	1307	1406	903	1292	874
South Korea	134	132	80	165	179	154	242	225	303	457	570	990	1033	1539	1949	2246	1862	2396	2736	3407	3677	4169
Taiwan	65	74	53	89	96	127	181	244	364	422	498	625	729	814	889	861	879	1263	1631	1532	1728	2566
West Asian Countries	72	82	74	88	184	182	269	241	281	436	569	575	601	705	826	721	571	763	1324	1618	1997	1835
of which:																						
Saudi Arabia	...	...	...	...	...	...	...	...	...	93	133	165	165	154	311	225	137	206	324	389	409	528
Iraq	50	57	38	52	135	100	62	42	41	130	111	30	54	105	124	93	107	129	203	152	124	0
Rest of the world	520	509	419	654	937	837	1143	1252	1229	1574	1770	1752	1643	1955	2496	1623	1679	2487	3040	3452	4071	5821
TOTAL	5163	5017	4854	7372	10195	9231	13442	14959	17074	24222	28172	27109	28108	32771	38647	38017	35318	45225	55260	67824	79646	94497

MALAYSIA: GROSS IMPORTS BY MAJOR COUNTRIES
(RM Million)

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
ASEAN	687	658	724	901	1447	1289	1390	1629	1954	2511	3858	4779	5753	5785	6377	6823	6006	6632	8127	11492	14962	20054
Singapore	320	364	365	465	820	722	841	934	1162	1576	2753	3486	4164	4270	4282	4828	4198	4698	5708	8280	11800	15714
Thailand	153	131	193	266	351	336	405	518	579	617	696	908	1060	917	1115	1077	1111	1115	1323	1841	1881	2452
Indonesia	207	147	153	149	232	191	110	110	108	169	176	160	162	226	408	344	372	443	740	937	851	1390
Philippines	7	16	13	21	44	40	34	67	105	149	233	221	364	369	569	571	322	373	353	430	427	494
Brunei	...	...	...	...	...	...	...	...	...	...	...	4	3	3	3	3	3	3	3	4	3	4
EEC	998	1081	1022	1268	2098	1760	1679	1948	2471	2993	3621	3702	3534	4298	4415	4397	4087	4268	5795	8490	11555	13786
United Kingdom	578	619	570	607	928	852	719	845	1017	1096	1271	1214	1185	1088	1186	1202	1268	1359	2136	3280	4312	4669
Netherlands	50	65	56	75	105	75	70	90	114	132	129	221	206	263	337	342	241	258	329	672	599	909
West Germany	209	204	205	329	621	430	545	624	838	1016	1274	1203	1225	1570	1363	1362	1253	1355	1689	2321	3389	4397
Other	161	193	191	257	444	403	345	389	502	749	947	1064	918	1377	1529	1491	1325	1296	1639	2217	3255	3811
Japan	749	861	933	1348	2204	1707	2062	2612	3145	3832	5365	6516	7253	7769	8646	7006	5722	6918	10153	14722	18974	26289
United States	369	292	408	510	983	909	1234	1375	1897	2566	3528	3875	5079	4989	5361	4627	5253	5986	7649	10269	13233	15458
Hong Kong	94	82	91	112	160	156	210	228	250	279	321	339	384	453	648	503	576	695	968	1254	1497	2061
China	229	202	194	365	493	356	341	343	509	485	551	632	648	626	668	622	728	946	1266	1650	1511	2213
USSR	11	11	12	17	10	13	26	27	16	23	59	57	64	39	43	44	29	54	110	209	216	208
Australia	244	257	340	423	714	665	692	676	877	1041	1289	1474	1371	1305	1323	1234	1184	1326	1792	2323	2937	3233
India	64	68	54	89	133	112	149	141	171	188	221	198	183	220	250	245	220	251	319	447	572	782
South Korea	11	12	11	18	63	35	67	85	134	246	418	374	608	554	592	687	637	841	1120	1526	2034	2743
Taiwan	76	76	98	134	203	170	232	276	310	417	546	604	739	821	861	807	910	1262	1992	3048	4323	5506
West Asian Countries	139	150	160	165	504	597	746	910	972	1326	2003	2183	1498	1715	1276	1209	620	669	699	788	955	873
of which:																						
Saudi Arabia	72	64	77	91	312	194	218	476	546	532	1446	1252	946	1320	1009	648	120	270	398	272	396	536
Kuwait	0	0	0	0	0	0	0	0	0	683	228	0	0	0	188	497	298	331	127	217	84	...
Rest of the world	617	666	496	584	879	761	885	915	940	1254	1671	1871	1909	2221	2466	2234	1949	2086	3305	4640	6350	7626
TOTAL	4288	4416	4543	5934	9891	8530	9713	11165	13646	17161	23451	26604	29023	30795	32926	30438	27921	31934	43293	60858	79119	100831

EMPIRICAL TEST OF GRANGER CAUSALITY

1. Sources of Data

This study used quarterly data for the period 1971-1991, a total of 84 observations. Data on real gross domestic product (RGDP) and nominal gross exports are compiled from various issues of the Quarterly Bulletin of Bank Negara Malaysia. The export price index series were compiled from various issues of the International Financial Statistics (International Monetary Fund).

2. Derivation of the Variables

(i) The real export values (REXP) is derived by dividing the export nominal value with the export price index.

(ii) All the data were transformed into their growth rates which was calculated as follows:

$$Z_t = \frac{Z_t - Z_{t-1}}{Z_{t-1}} \times 100$$

Chapter 5

EXPORT PROMOTION STRATEGIES: NEPAL

by
Ram Bhakta Thapa

I. Introduction

Nepal is a landlocked agriculture-dominated, and of the least developed countries in the world. It has a population of 18.46 million (1991 census) with a land area of 14.1 million hectors. The population is growing by more than 2 percent per annum, and the literacy rate is 40 (1992 census) and life expectancy is 54 (1990 census). The annual per capital income is estimated to be around US$ 180. The agricultural sector plays a very important role in the country's economy. More than 90 percent of the total working population are engaged in agriculture and allied activities. There has been minimal change in the structure of production. The agricultural sector still accounts for more than 50 percent of gross domestic product (GDP). GDP is increasing at a very low rate. Nepal's industrial development is at an infant stage and the contribution of the manufacturing sector to GDP is less than 10 percent.

Foreign trade, especially export trade, has played a vital role in the economic development of Nepal. It has helped to earn foreign exchange in order to import the necessary goods for domestic consumption, and capital as well as developmental goods. It has also helped to import the new technology required for the industrial development of the country. Exports have financed not only import needs but have also met the country's debt obligations.

II. Export Trade and Salient Features

Nepal's foreign trade structure is primarily a reflection of its low level of development. Merchandise exports are numerically very small. Due to the predominant role of agriculture in Nepal's economy, agricultural products constituted a large part of exports until the 1970s. After mid-1970s, there has been a gradual shift in exports of primary goods to manufactured goods. The share of primary goods to total

exports decreased from 90 percent in 1975/1976 to less than 20 percent in 1991/1992. In the year 1991/1992, carpets and readymade garments constituted more than 70 percent of total exports of the country.

India is the main trading partner of Nepal. Until 1974/ 1975, Nepal's trade volume with India accounted for 82 percent of the total trade. More than 75 percent of the total exports was with India. However, Nepal's international trade has undergone some structural changes recently. During the year 1984/1985, India's share in the total volume of foreign trade went down to 52 percent, while exports to India declined to 58 percent of total exports. Thus, it is evident that India's share in Nepal's foreign trade is declining. It went down further to 29 percent in 1991/1992. In 1990/1991, exports to India dropped to 11 percent of total exports.

In Nepal, both GDP and exports grew at about the same rate on an average during the period under review. As a result, the ratio of exports to GDP has changed marginally from 6.8 percent in 1975/1976 to 7 percent in 1990/1991. In 1991/1992, this ratio has increased to 10.7 percent.

Since the role of export sector in the economy is relatively small, its contribution to employment is also limited. It is difficult to measure the exact volume of employment generated in the export sector. But since the production of almost all major export items is labor-intensive, this sector has a reasonably high potential of creating employment opportunities. The agricultural exports are highly labor-intensive. In the manufacturing sector, jute, handicrafts, garments and carpets are providing mass employment opportunities.

Exports in Nepal finance less than 50 percent of the country's import needs. During the 1980s, export earnings have met less than 40 percent of the import payments on an average. The poor performance of the export sector has created a serious and increasing deficit in the balance of trade. For example, in 1975/1976, the trade deficit was 4.5 percent of GDP, and it went up to 10 percent in the year 1980/1981. Trade deficit reached the level of 15 percent of GDP in the year 1990/1991. As a result, Nepal's current account deficit is widening. Such a deteriorating position in the external transactions exerted heavy pressure on its international reserve position from time to time. Therefore, Nepal had to devaluate its currency on several occasions.

Table 5.1

NEPAL: ECONOMIC INDICATORS
(In Million US$)

	1975/76	1976/77	1977/78	1978/79	1979/80	1980/81	1981/82	1982/83	1983/84	1984/85	1985/86	1986/87	1987/88	1988/89	1989/90	1990/91	1991/92
Trade Balance	-65	-67	-115	-133	-195	-237	-266	-377	-313	-280	-315	-367	-441	-472	-462	-488	-446
Export f.o.b.	98	94	86	109	97	135	116	82	110	154	156	138	186	165	183	228	327
Import c.i.f.	163	161	201	242	292	372	382	459	423	434	471	505	627	637	645	716	773
Service, Net	24	40	46	65	84	94	107	119	92	60	80	107	93	117	91	83	91
Receipts	62	75	91	121	145	174	178	183	168	152	176	215	226	242	223	237	276
Payments	38	35	45	56	61	80	71	64	76	92	96	108	133	125	132	154	185
Current A/c Balance	5	20	-24	3	-29	-25	-30	-121	-87	-104	-124	-135	-207	-248	-272	-293	-255
Capital A/c Balance	25	5	25	46	31	41	69	72	79	55	153	152	310	251	365	420	356
Overall BOP (- Surplus)	-30	-25	-1	-49	-2	-16.0	-39	49	8	49	-28	-17	-103	-3	-93	-127	-102
Export/Import Ratio	60.1	58.4	42.8	45.0	33.0	36.3	30.4	17.9	26.0	35.5	33.1	27.3	29.7	25.9	28.4	31.8	42.3
Service Export/Merchandise Export	63.3	79.8	105.8	111.0	148.5	128.9	153.5	223.2	152.7	98.7	112.2	155.8	121.5	146.7	121.9	104.0	84.4
Merchandise Exp./GDP (Current Price)	6.8	6.8	5.4	5.8	4.9	5.9	4.8	3.3	4.3	6.2	6.1	5.0	6.0	5.4	5.8	7.0	10.7
Merchandise Exp./GDP (Constant Price)	6.9	6.6	5.7	6.8	6.2	8.0	7.2	5.6	7.6	11.6	12.6	11.6	15.0	14.7	17.2	23.1	42.1
Government Revenue	122	138	167	203	226	276	285	286	278	271	293	336	426	370	395	366	340
Government Expenditure	158	187	218	254	292	344	416	507	483	471	494	533	638	705	689	464	457
Budgetary Deficit (-)/Surplus (+)	-36	-49	-51	-51	-66	-68.0	-131	-221	-205	-200	-201	-197	-212	-335	-294	-98	-117
Inflation Rate	-0.6	2.6	11.3	3.5	9.7	13.4	10.5	14.2	6.3	4.1	15.9	13.3	11.1	8.1	11.5	9.8	21.1
GDP at Current Price	1435	1388	1608	1867	1962	2295	2402	2452	2558	2491	2540	2744	3114	3037	3182	3246	3067
GDP at 1974/75 Price	1427	1431	1516	1601	1564	1694	1622	1474	1446	1325	1242	1187	1243	1121	1064	988	776
Exchange Rate	12.12	12.45	12.27	11.90	11.90	11.90	12.90	13.77	15.40	17.83	19.85	21.59	22.11	25.53	28.54	32.44	42.61

Source: Nepal Rastra Bank.

Table 5.2

NEPAL: DIRECTION OF FOREIGN TRADE
(In Million US$)

	1975/76	1976/77	1977/78	1978/79	1979/80	1980/81	1981/82	1982/83	1983/84	1984/85	1985/86	1986/87	1987/88	1988/89	1989/90	1990/91	1991/92
Export f.o.b.	98	94	86	109	97	135	116	82	110	154	156	138	186	165	183	228	327
India	74	63	41	55	44	83	77	61	75	90	63	60	71	41	23	48	37
Other Countries	24	31	45	54	53	52	39	21	35	64	93	78	115	124	160	180	290
Import f.o.b.	163	161	201	242	292	372	382	459	423	434	471	505	627	637	645	716	773
India	101	108	125	133	150	183	177	182	199	218	200	197	208	166	163	226	277
Other Countries	62	53	76	109	142	189	205	277	224	216	271	308	419	471	482	490	496
Trade Balance	-65	-67	-115	-133	-195	-237	-266	-377	-313	-280	-315	-367	-441	-472	-462	-488	-446
India	-27	-45	-84	-78	-106	-100	-100	-121	-124	-128	-137	-137	-137	-125	-140	-178	-240
Other Countries	-38	-22	-31	-55	-89	-137	-166	-256	-189	-152	-178	-230	-304	-347	-322	-310	-206
Total Volume of Trade	261	255	287	351	389	507	498	541	533	588	627	553	813	802	828	944	1100
India	175	171	166	188	194	266	254	243	274	308	263	257	279	207	186	274	314
Other Countries	86	84	121	163	195	241	244	298	259	280	364	296	534	595	642	670	786
% Share in Total Trade																	
India	67	67	58	54	50	52	51	45	51	52	42	46	34	26	22	29	29
Other Countries	33	33	42	46	50	48	49	55	49	48	58	54	66	74	78	71	71

Source: Nepal Rastra Bank.

Export promotion is necessary not only to finance the country's import needs but also to meet its debt obligations. Nepal's debt service ratio is climbing steadily. The debt service ratio was 2.0 percent in 1975/1976, and it reached 4.2 percent in 1980/1981. It further went up to 17 percent in the year 1990/ 1991. In fact, one can expect a rapid increase in debt servicing obligations in recent years because of the increased amortization of loans in the past. Therefore, exports have to increase rapidly, otherwise the debt service ratio is likely to increase which ultimately will exert heavy pressure on the balance of payments.

III. Export Promotion Policies

3.1 Review of Export Policy

A serious constraint to the promotion of exports in the past had indeed been the lack of a coherent strategy with an integrated package of policies to encourage production and exports of goods in which Nepal has a comparative advantage. The main thrust of whatever policies that had been adopted in the past had been motivated by the Government's desire to diversify its trade to as many countries as possible. The main rationales behind the adoption of the diversification policy were: (i) to decrease the dependency on India for the development of external trade; (ii) to find ways and means of earning convertible foreign exchange to meet committed obligations; and, (iii) to find new marketing outlets for Nepalese products.

The trade diversification policy in the past indeed yielded good dividends for Nepal insofar as it was possible to reduce dependency on India, but this policy had been less beneficial for the expansion of exports in general. Primary commodities that could be exported more profitably to India had also been diverted to overseas markets under the lure of various incentive provided by the Government in which individual exporters would gain but the economy would suffer a direct financial loss.

A more serious and adverse outcome of this policy had been the severe shortage of Indian rupee resources for meeting the cost of imports from India. Nepal had to sell convertible currencies to buy Indian currency just to finance imports from India.

In order to boost exports, Nepal's Government announced a new export policy in the year 1982. The basic objectives of the 1982 Export Policy were as follows:

(i) To help provide the income-generating activities and job opportunities through the medium of export trade;
(ii) To open up international markets for indigenous products instead of confining them within internal market only;
(iii) To expand the scope of export trade and raise the level of foreign exchange earnings to meet the growing import needs and to service external debts; and,
(iv) To step up contacts with international markets through the medium of export trade so that high technology, skill and management capabilities of the country could be upgraded.

As part of the working guidelines, the Government had specified various policies to facilitate the growth of exports. This includes the simplification of licensing procedures, simplification of custom procedures and provision of warehousing facilities, improvement of transit facilities, transport arrangement for export by air, duty drawback facilities in respect of excise duties and sales tax, exemption from export duty, rebate on income tax, facility for export credit, and quality control of export products. However, the implementation of these policies were slow but they represented the good intention of the Government vis-a-vis the export sector.

From the very beginning, Nepal has relied heavily on the exchange rate as the instrument of its export diversification policy. Nepal adopted the Exporter's Exchange Entitlement (EEE) scheme in 1961/1962 popularly known as the 'Bonus Scheme'. Under this system, exporters of Nepalese goods to countries other than India were given a fixed percentage of their export receipts in convertible foreign exchange as entitlements to import specific commodities. The idea was to help exporters in recovering their losses incurred from overseas exports. In other words, this was an incentive towards the diversification of the export market. This system remained in operation for 16 years.

Unfortunately, the EEE scheme created various distortions in the system which not only hindered the growth and stability of the export sector but also adversely affected other sectors of the economy. In fact, the scheme encouraged the export of non-value-added primary

products. Similarly, distortions also occurred in the import sector, whereby the traders were encouraged to import more luxurious goods rather than capital and developmental goods, which resulted in a short supply of developmental materials and essential consumer goods.

To overcome the problems created by the EEE scheme, Nepal adopted the Dual Exchange Rate (DER) System in March 1978 to achieve the objective of promoting overseas exports. The DER System was also designed to fulfil the objective of liberalizing the trade policy with a differential exchange rate system of Rs. 12 and Rs. 16 per U.S. dollar. Under this system, the exporters were paid the second rate and the importers were allowed to import freely on the second rate, except for some restricted commodities. The second rate was changed in February 1980 with a reduction in the second rate from Rs. 16 to Rs. 14 per US dollar. Except for the import of petroleum products, cement and fertilizers, all other items were imported according to the second rates.

Together with the DER System, the Government introduced a cash subsidy system. Finally, the nine-point export promotion scheme was adopted in the early 1980s. This scheme included various measures as follows: (i) cash subsidy; (ii) creation of an export promotion council under the chairmanship of the Prime Minister; (iii) retainment of 15 percent of foreign exchange earnings by the industries through the export of their products; (iv) nominal export duty, i.e., 1 percent; (v) duty drawback system; (vi) pre-export credit of up to Rs. 2.5 million for the collection and processing of goods; (vii) provision of loans at subsidized interest rate (the subsidy was to be borne by Nepal Rastra Bank); (viii) provision for investment by the Nepal Industrial Development Corporation (NIDC) of at least 10 percent of its total investment in export-oriented industries; and, (ix) to establish branches of export units by commercial banks.

3.2 Recent Policy

In the changing context of an open and liberal economic policy as pursued by many other countries, Nepal has also changed her policy from a restrictive regime to a more open and market-based economy, moving gradually towards privatization. As the private sector is expected to increase efficiency and productivity in industries and commercial operations, the Government advocated private sector-led growth. A

liberal, dynamic and transparent trade policy has been announced to diversify trade by identifying, developing and producing new exportable products through the promotion of backward linkages for making export trade competitive and sustainable. In order to boost export, the following policies have been announced recently:

(i) The production and quality of exportable products will be raised to make them competitive in the international market.
(ii) Licenses will not be required for exportable products, and also exports will be free of all charges except the service charge.
(iii) Improvements will be made in existing transit facility, transport net work and its infrastructure. Administrative procedures will also be simplified to increase efficiency.
(iv) Container service will be introduced and the existing bonded warehousing system will be further expanded and improved.
(v) The duty drawback scheme for the refund of import duty paid on the importation of raw materials and intermediate goods required for the production of exportable products will be implemented.
(vi) Export Promotion Zone (EPZ) will be established. No duty will be levied on the raw materials and auxiliary imports used by industries established in the EPZ.
(vii) In this connection, full convertibility of Nepalese currency in trade and services has been adopted recently. Under this arrangement, 100 percent of the foreign currency earnings from the exports of goods and services are converted to a market-determined exchange rates. Importers can obtain their foreign currency requirement at market-determined rates. Foreign currency for the import of petroleum products, life saving drugs and its raw materials and industrial machinery will be provided at the official exchange rate. Exporters have also been allowed to open a foreign exchange account in the banks for the purpose of spending one's foreign exchange earnings in trade promotion.
(viii) Simple and convenient procedures relating to pre- and post-shipment credits will be adopted on priority basis.
(ix) Income tax on income from exports will be fully exempted.
(x) Necessary information and training relating to technology, marketing and export procedures required for export promotion will be provided on an institutional basis

and arrangements will also be made to participate in national and international trade fairs for market promotion.

(xi) Export promotion, research and development and training schemes will be developed on an institutional basis for developing new exportable products and for raising the quality and production of traditional exportable products.

(xii) No quantitative restrictions will be imposed on returning tourists on exportable products.

(xiii) If any producer earns foreign exchange by selling one's own products to projects run under bilateral or multilateral aid or if such finished products are sold to EPZ, such sales will be granted facilities on a par with exports. For instance, custom duty, sales tax, excise duty levied on such sales will be refunded and income generated from such sales will be exempted from income tax.

IV. Problems and Issues on Export Promotion

The production base of exportable items is very weak in Nepal. The economy is moving at a slow pace, the rate of growth of real GDP in dollar terms is decreasing due mainly to the currency depreciation. The GDP in the year 1975/1976 was US$ 1427 million which decreased to US$ 776 in the year 1991/1992. The performance of agricultural sector has been particularly disappointing, whereas the expansion of non-agricultural sector is very gradual.

In recent years, private sector producers have also lacked initiative except in the case of handicrafts, carpets and readymade garments. The export of jute which was a sizable amount in the past to third world countries has become negligible in recent years. In the case of products like ginger, cardamom, medicinal herbs, the quality of improvement and training for the producers/ farmers, and the transfer of know-how are already overdue.

The production level is very low, and moreover, the quality of the goods is poor. There is no institution to take care of the quality of exportable items. Therefore, the prior inspection of goods, certification of quality to match international standards are the major concerns in export sector.

Nepal's geographic location is one of the biggest bottlenecks to export expansion as it is to the overall development of the country in general. The difficult terrain in the hills and a lack of adequate means of transportation are the major problems in the local markets, whereas these problems are even more acute beyond its border. Because of the landlocked position, Nepal has to rely only on road transportation.

Nepal is lacking on knowledge of market, including demand patterns, price changes, users' preference, trend of substitutes and future prospects, and their timely monitoring. With regard to marketing in India because of the treaty provisions, the manufacturing products of Nepal have to comply with a number of procedures and formalities. There is also the problem of value-added factor.

Transit through India is a big problem for the promotion of exports. The transit treaty between Nepal and India stated that exports of goods to third world countries passing through India will follow the procedures specified in the memorandum of treaty.

V. Policy Recommendations

Nepal is a small country with an equally small domestic market, therefore, reducing the possibilities of operating large-scale industries. Nepal has to depend on trade even to meet her domestic demand and at the same time, it has to reap the economies of international division of labor by enhancing her export capabilities. Since Nepal's industrial development is in the early stage, it is difficult to promote export-oriented industries. Because of the lack of capital, Nepal should also concentrate on labor-intensive industries. Currently, total exports comprise largely of woolen carpets and if quality can be maintained, it should flourish in the future assuming there is lesser competition for handmade carpets in the European markets.

Since the objective of export promotion is to maximize the economic gains and to stabilize export earnings, there is much room for improvement on the policy level for the promotion of exports.

(i) As we know by the experiences of successful countries, the overall macroeconomic balance is a necessary condition for the promotion of exports. Therefore, there should be further

liberalization on the recently introduced market-based policy of the government so that the potential exporters could be encouraged by such conducive environment to help expand the exportable products.

(ii) Although Nepal is at an early stage of industrialization, and operating on small-scale basis, it should also identify the comparative advantage of her exportable items. Towards this end, there should be detailed studies on the possibility of upgrading newly emerging industries like carpets, garments, handicrafts, etc.

(iii) In the export sector, production itself is not a sufficient condition, more importantly, it is the quality of the exportable products which ensure competition in the external markets. Therefore, there should be some arrangement to ensure the quality and standard of the exportable products, at least in the case of so-called prominent exportable items to maintain their position in the international markets.

(iv) In Nepal, import substitution and export promotion policy should go side by side so that the level of necessary consumer goods to be imported to meet public demand can be substituted by local products.

(vii) The exporters are still facing the problems of market identification and buyers' choice through lack of marketing information. There is a need to introduce Nepalese products in international markets through trade fairs and missions.

VI. Summary and Conclusion

Apart from the poor performance of exports in general, the balance of trade and payments with India have particularly deteriorated in recent years. The stagnant level of exports, on the one hand, and the continued need for increased imports, on the other, have caused a huge current account deficit.

In the early days, primary products had constituted a greater part of exports from Nepal. However, after the 1970s, there has been a gradual shift to manufactured goods because of the decline in production of agricultural goods. The high rate of population growth also contributed to the fall in exportable agricultural products.

Exports grew at a rate slightly higher than the rate of growth of GDP in nominal terms. The ratio of exports to GDP has been decreasing until 1989/1990. However, the ratio has increased to 10.7 percent of GDP in the year 1991/1992. The contribution of export sector to employment is limited because the role of this sector to the economy is relatively small. Export import ratio has also decreased from 60.1 percent in 1975/1976 to 42.3 percent in 1991/ 1992. As a result, there has been a huge trade deficit, which in turn has added to the higher current account deficit. Nepal's balance of payments position has been favorable for most years because of the huge inflow of foreign borrowings. Nepal's debt service ratio is increasing and has reached 17 percent in the year 1990/1991. Since the 1980s, the diversification policy has helped to divert its exports to countries other than India.

As Nepal changed her economic policy from a restricted regime to a liberalized one, its export policy has also been liberalized recently; a more dynamic, transparent and liberal trade policy has been announced in order to boost the export trade.

Chapter 6

EXPORT PROMOTION STRATEGIES: THE PHILIPPINES

by
Carmen V. Hemedes

I. Introduction

The role of trade in a country's development cannot be overemphasized. The economic history of European countries is replete with country-growth experiences in which trade, particularly exports, served as the main engine driving the industrial development.

For the Philippines, a generally protectionist trade policy impeded industrial development, and limited the pattern of manufacturing growth to one consisting mainly of import-substituting industries starting in the 1950s. At that time, protection took the form of strict foreign exchange controls, as foreign exchange was rationed according to a criterion of essentiality. Hence, only producer goods could be imported since foreign exchange was not obtainable for non-essential consumer goods. This system thus encouraged the emergence of import-substituting industries which favored the finishing stages of manufacturing and penalized backward linkages and exports.

Although the liberalization of import controls under the decontrol program was completed in the 1960s, the control system was not discarded. Instead, protection shifted to one based on tariff as rates were further raised to assure local producers of a market for their products. This move, however, also discouraged the promotion of exports. With foreign exchange earnings to support industrial needs dependent on a few primary exports, the country remained vulnerable to balance of payments (BOP) problems. A return to import controls was thus resorted to by the end of the 1960s.

Such inward-looking development orientation was intensified during the martial law years with the reimposition of controls on consumer goods which required central bank approval prior to their importation. Despite awareness of the existing bias in the system on the part of government planners, export promotion measures nevertheless were pursued alongside an import-substituting strategy in the 1970s.

As the absorptive capacity of the limited domestic market was reached, however, the need to improve efficiency in order to compete internationally became apparent.

Realizing the setback suffered by Philippine exports in the past, this paper reviews efforts to promote exports. It also proposes steps, particularly those which can be undertaken by monetary authorities, so that these measures may become operative. The study is divided into five parts; the first part discusses the salient features of export trade, i.e., the structure, composition and direction of exports. It then tries to establish the determinants of export demand, using Central Bank's Department of Economic Research-International's (DER-I) aggregate trade model. The Government's export promotion policy is also reviewed, together with measures and institutional arrangements for exports. Based on the foregoing, problems and issues on export promotion are presented and recommendations are forwarded. A summary of the major points made in the study, including conclusions derived, is provided in the final section.

II. Export Trade and Salient Features

2.1 Export Growth

Philippine merchandise exports have grown considerably since the 1970s from a level of $1.06 billion to $8.8 billion in 1991. From 1970-1980, export growth accelerated, reaching an annual average growth of 20.7 per cent for the period, comparable to the growth of world and Asian trade at 21.4 and 26.2 percent respectively. While export performance generally declined during the first five years of the 1980s, partly reflecting world conditions, but largely was due to the country's foreign exchange crisis, growth picked up steadily starting in 1986, and exceeded world growth rates during the three succeeding years. However, political events such as the coup d'etat in 1989 and natural calamities as earthquakes, typhoons and volcanic eruption which struck the country in succeeding years, pulled down the country's export growth to 4.7 and 8 percent respectively in 1990 and 1991.

Meanwhile, services exports registered a significant contribution to export growth during the latter part of the 1980s. Services exports grew from $258 million in 1970 to $1.08 billion in 1977 and posted

double-digit growth rates averaging 27.5 percent from 1977-1981. This is mainly attributable to the share of remittances by contract workers to total earnings which rose from an annual average of 14 percent in the latter years of 1977-1981 to 18 percent from 1982-1991. The growth of services exports slowed down during the years of foreign exchange crisis (1983-1984), but picked up starting 1985 to reach $5.6 billion in 1991 (Table 6.1).

2.2 Structure of Merchandise Exports

The composition of exports underwent some transformation during the last two decades. Using the central bank classification based on the Board of Investments (BOI) concept of traditional and non-traditional products, Philippine traditional exports consisted largely of resource-based agricultural exports which accounted for 92 percent of total exports in 1970 (Table 6.2). In the 1980s and the 1990s, the share of resource-based exports showed a declining trend to reach 15.7 percent by 1991.

Meanwhile, the share of non-traditional items (manufactured items, mainly electronics and garments and manufactures like nickel, iron ore, bananas, mangoes, fish) has risen significantly from 8 percent in 1970 to 83 percent in 1991.

The change in structure of Philippine exports may also be seen in Table 6.3 using the one-digit Philippine Standard Commodity Classification (PSCC) scheme. In 1970, almost 90 percent of Philippine exports were classified under Food and Food Preparation (0), Crude Materials Inedible (2), and Animal and Vegetable Oils and Fats (4). By 1991, the share of these commodities, has gone down to 23 percent. Meanwhile, exports of miscellaneous manufactured items (8), machinery and transport (7) and commodities/transactions not classified elsewhere (9) wherein the bulk of consigned exports of garments and electronics are lodged, rose from a 1.4-percent share in the 1970s to 62.3 percent in 1991.

It should be noted, however, that while the composition of exports has changed considerably, the import-dependent nature of exports has remained. While the resource-based exports of the 1960s and 1970s required imported inputs in terms of fertilizers and insecticides, agricultural and transport equipment, the major manufactured items of

Table 6.1

PHILIPPINES: SELECTED INDICATORS, 1970-1991

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
Total Exports	1062	1136	1106	1886	2725	2294	2574	3151	3425	4601	5788	5722	5021	5005	5391	4629	4842	5720	7074	7821	8186	8840
Growth Rate		6.97	-2.64	70.52	44.49	-15.82	12.21	22.42	8.70	34.34	25.80	-1.14	-12.25	-0.32	7.71	-14.13	4.60	18.13	23.67	10.56	4.67	7.99
Manufactured Exports	72	73	76	211	324	365	545	709	1042	1468	1996	2369	2373	2357	2775	2539	2672	3430	4338	5192	5706	6403
Share to Total (%)	6.78	6.43	6.87	11.19	11.89	15.91	21.17	22.50	30.42	31.91	34.49	41.40	47.26	47.09	51.47	54.85	55.18	59.97	61.32	66.39	69.70	72.43
Non-Manufactured Exports	990	1063	1030	1675	2401	1929	2029	2442	2383	3133	3792	3353	2648	2648	2616	2090	2170	2290	2736	2629	2480	2437
Share to Total (%)	93.22	100.09	96.99	157.72	226.08	181.64	191.05	229.94	224.39	295.01	357.06	315.73	249.34	249.34	246.33	196.80	204.33	215.63	257.63	247.55	233.52	229.47
Total Exports (Goods & Serv.)	1320	1401	1453	2525	3559	3201	3445	4236	4909	6256	8010	8618	8004	8132	8017	7917	8633	9174	10666	12407	13028	14464
Services Exports	258	265	347	639	834	907	871	1085	1484	1655	2222	2896	2983	3127	2626	3288	3791	3454	3592	4586	4842	5624
Share to Total (%)	19.55	18.92	23.88	25.31	23.43	28.33	25.28	25.61	30.23	26.45	27.74	33.60	37.27	38.45	32.76	41.53	43.91	37.65	33.68	36.96	37.17	38.88
Merchandise Imports (CIF)	1210	1326	1370	1790	3468	3776	3953	4270	5143	6613	8295	8479	8263	7979	6428	5435	5394	7188	8731	11171	13042	12857
Merchandise Imports (FOB)	1090	1186	1230	1596	3143	3459	3634	3915	4732	6142	7727	7946	7667	7487	6070	5111	5044	6737	8159	10419	12206	12051
Services Imports	400	352	402	639	868	952	1130	13333	1591	1966	2621	3205	4023	3867	3449	3288	3076	3454	3672	4274	4231	4273
Export/Import Ratio	97.43	95.78	89.92	118.17	86.70	66.32	70.83	80.49	72.38	74.91	74.91	72.01	65.49	66.85	88.81	90.57	96.00	84.90	86.70	75.06	67.07	73.35
Trade Balance	-1090	-1186	-1230	-1596	-3143	-3459	-3634	-3915	-4732	-6142	-7727	-7946	-7667	-7487	-6070	-5111	-5044	-6737	-8159	-10419	-12206	-12051
Current A/C Balance	-51	-3	9	536	-176	-892	-1050	-752	-1102	-1497	-1904	-2061	-3200	-2750	-1116	-103	954	-444	-390	-1456	-2695	-1033
Overall BOP	23	6	84	674	108	-519	-158	137	-91	-578	-353	-547	-1671	-2118	243	2301	1242	264	650	451	-185	1405
GDP at Current Prices 1/	39505	47652	53514	68125	93545	107953	127214	145455	167251	202897	243749	281596	317177	369077	524481	571883	608887	685068	802519	925161	1070900	1242871
GDP at Constant Prices 2/	343163	361792	381499	415525	418640	449064	496306	527377	560449	580726	605631	639356	642619	647409	623704	559456	612425	622937	658782	698382	715152	707858
Budgetary Surplus/Deficit 1/	59	-183	-1101	-843	445	-1403	-2349	-2852	-2167	-342	-3387	-12146	-14405	-7431	-10065	-11141	-30593	-16693	-23206	-19568	-37194	-26331
Rate of Inflation (1978=100)	14.8	21.8	8.2	16.5	34.2	6.9	9.2	9.9	7.3	17.5	18.2	13.1	10.2	10.0	50.3	23.1	0.8	3.8	8.8	10.6	12.7	17.7
Consumer Price Index (1978=100)	35.3	43.0	46.5	54.2	72.7	77.6	84.8	93.2	100.0	117.5	138.9	157.1	173.2	190.5	286.4	352.6	355.3	368.7	401.0	443.5	499.7	588.2
Exchg. Rate W/US$ (Period Ave.)	6.02	6.43	6.67	6.76	6.79	7.25	7.44	7.40	7.37	7.38	7.51	7.90	8.54	11.11	16.70	18.61	20.39	20.57	21.09	21.74	24.31	27.48
MEMO ITEMS:																						
World Exports (Billion US$)	290.5	327.0	390.1	542.3	811.4	835.0	941.7	1066.2	1234.3	1584.8	1910.9	1881.2	1731.4	1697.5	1810.8	1822.0	2005.4	2360.7	2697.3	2908.6	3330.9	3441.7
Growth Rate		12.56	19.30	39.02	49.62	2.91	12.78	13.22	15.77	28.40	20.58	-1.55	-7.96	-1.96	6.67	0.62	10.07	17.72	14.26	7.83	14.52	3.33
Exports of Asian Countries	17.1	19.4	24.8	38.4	54.6	54.4	68.8	81.7	98.0	128.8	164.0	176.5	175.6	183.9	211.1	209.3	227.5	296.0	364.0	405.5	450.5	514.53
Growth Rate		13.39	27.85	55.27	42.14	-0.50	26.49	18.82	19.93	31.47	27.33	7.63	-0.51	4.69	14.81	-0.86	8.73	30.08	22.98	11.41	11.09	14.21

1/ In million pesos.

2/ In million pesos; Data for 1970-1978 are based on 1972 prices.

Sources: National Statistics Office, the Philippines.
International Financial Statistics, IMF.

Table 6.2

EXPORTS BY MAJOR COMMODITY GROUP, 1970-1991
(Percent to Total Exports)

Commodity Group	1970	1975	1980	1985	1990	1991	1992
TRADITIONAL EXPORTS	91.53	77.03	53.01	28.13	17.55	15.70	15.64
Coconut Products	19.68	20.31	14.01	9.92	6.06	4.97	6.44
Sugar & Products	18.46	26.81	11.35	4.00	1.62	1.54	1.12
Forest Products	26.18	9.81	7.34	4.30	1.15	0.83	0.58
Mineral Products	20.43	14.47	15.86	5.25	4.41	3.50	3.53
Fruits & Vegetables	2.45	1.92	1.92	2.94	1.98	2.22	1.87
Abaca Fibers	1.41	0.61	0.47	0.37	0.20	0.19	0.21
Tobacco Unmanufactured	1.32	1.48	0.50	0.52	0.24	0.49	0.35
Petroleum Products	1.60	1.61	1.55	0.84	1.89	1.98	1.53
NON-TRADITIONAL EXPORTS	8.00	21.97	45.78	70.75	81.05	83.18	82.98
Non-Traditional Manufactures	6.78	16.00	34.64	59.73	73.23	75.03	76.60
Elect. & Elect. Equipment/ Parts & Telecom	0.00	2.05	11.59	22.81	23.99	25.94	28.02
Garments	0.00	4.36	8.67	13.46	21.70	21.05	21.78
Textile Yarns/Fabrics	0.56	0.96	1.28	0.84	1.14	1.13	1.23
Footwear	0.09	0.13	1.16	0.84	0.95	1.38	1.23
Travel Goods & Handbags	0.09	0.44	0.16	0.22	0.53	0.51	0.54
Wood Manufactures	1.04	1.26	0.60	0.93	1.43	1.32	1.15
Furniture & Fixtures	0.09	0.22	1.33	1.81	2.31	2.00	1.84
Chemicals	0.47	0.92	1.54	3.24	3.19	3.44	2.73
Copper Metal	0.00	0.00	0.00	3.63	3.43	2.51	2.21
Non-Metallic Mineral Manufactures	0.28	1.44	1.04	0.52	0.70	0.84	0.81
Machinery & Transport Equipment	0.09	0.44	0.81	0.65	1.83	2.05	2.93
Processed Food & Beverages	0.75	0.61	1.59	2.29	2.53	2.64	2.24
Misc. Manufact'd Articles, n.e.s.	0.47	2.01	2.57	2.94	4.01	4.36	4.53
Others	2.82	1.18	2.30	5.55	5.51	5.87	5.34
Non-Traditional Unmanufactured	1.22	5.97	11.14	11.02	7.82	8.14	6.38
Nickel	0.00	1.44	2.38	1.38	0.00	0.01	0.00
Iron Ore Agglomerates	0.00	0.00	2.04	2.05	0.99	0.88	0.64
Bananas	0.47	3.18	1.97	2.44	1.82	1.96	1.61
Mangoes	0.09	0.09	0.12	0.15	0.18	0.27	0.30
Coffee, Raw, not roasted	0.00	0.09	0.78	1.51	0.10	0.06	0.01
Fish, Fresh or preserved	0.19	0.70	1.85	2.14	3.59	3.99	2.95
of which: Shrimps & Prawns	0.09	0.31	0.36	1.34	2.68	3.09	2.15
Rice	0.00	0.00	1.26	0.00	0.00	0.02	0.09
Others	0.47	0.48	0.74	1.34	1.14	0.95	0.78
SPECIAL TRANSACTIONS	0.00	0.92	0.57	0.26	0.23	0.19	0.41
RE-EXPORTS	0.47	0.09	0.64	0.86	1.16	0.93	0.98
TOTAL EXPORTS:	100.00	100.00	100.00	100.00	100.00	100.00	100.00

Source: National Statistics Office, the Philippines.

Table 6.3

PHILIPPINES: COMPOSITION OF EXPORTS

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
Food & Live Animals	25.71	27.64	28.66	23.06	35.63	36.09	29.18	30.05	19.65	18.54	24.12	23.42	22.51	19.08	18.29	17.82	18.09	15.56	14.94	14.06	13.13	13.93
Beverages & Tobacco	1.41	1.41	1.72	1.48	1.17	1.57	1.17	0.98	0.93	0.76	0.55	0.94	1.04	0.76	0.63	0.67	0.60	0.49	0.45	0.43	0.71	0.97
Crude Materials, excl. fuels	53.86	50.26	46.93	46.18	32.77	28.42	27.00	27.61	26.04	26.86	24.27	18.79	17.29	14.91	10.46	10.37	10.72	9.35	10.02	9.32	6.66	5.45
Mineral Fuels, etc.	1.60	2.11	1.72	0.85	0.62	1.61	0.89	0.60	0.29	0.24	0.66	0.73	0.66	2.32	1.61	0.91	1.36	1.70	2.16	1.51	2.21	2.39
Animal, Vegetable Oil & Fats	9.04	9.15	7.69	8.06	14.09	10.16	11.73	13.17	18.19	16.26	9.83	9.40	8.03	10.45	11.24	8.04	7.13	6.94	6.01	5.01	4.58	3.53
Chemicals	0.47	0.53	0.54	0.58	0.59	0.92	1.05	1.62	1.72	2.43	2.04	1.84	1.91	1.74	1.95	3.24	5.06	4.32	3.65	3.57	3.20	3.44
Basic Manufactures	6.50	7.13	10.22	13.63	8.44	10.37	9.32	8.09	8.93	9.11	9.21	8.32	6.69	7.43	6.94	10.13	8.98	8.29	9.75	9.50	9.33	7.98
Machines, Transport & Equipment	0.09	0.18	0.45	0.21	0.29	0.52	0.74	1.71	2.19	1.91	2.28	2.81	3.41	5.17	8.03	6.89	8.94	10.47	9.81	12.20	12.46	13.90
Misc. Manufactured	0.85	0.88	1.54	2.23	2.42	4.40	6.57	6.85	9.40	10.13	10.57	12.30	12.19	12.25	9.87	11.62	12.12	13.25	13.49	15.30	16.38	16.29
Unclassified Goods	0.47	0.70	0.54	3.71	3.96	5.93	12.35	9.30	12.64	13.76	16.47	21.44	26.29	25.89	30.98	30.31	26.99	29.63	29.71	29.09	31.33	32.13
Total Exports:	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00
(in Million $)	1062	1136	1106	1886	2725	2294	2574	3151	3425	4601	5788	5722	5021	5005	5391	4629	4842	5720	7074	7821	8186	8840

Source: National Statistics Office, the Philippines.

Table 6.4

EXPORTS OF ELECTRONICS & GARMENTS (REGULAR & CONSIGNED), 1980-1991

(FOB Value in Million US$)

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989*	1990*	1991*	Average Growth Rate/Share (%) 1980-1985	Average Growth Rate/Share (%) 1986-1991	Average Growth Rate/Share (%) 1980-1991
A. EXPORT LEVELS															
ELECTRONICS	671	838	1000	1053	1329	1056	919	1119	1476	1638	1806	2115			
Regular	81	114	120	219	381	279	348	475	623	712	682	851			
Consigned	590	724	880	834	948	777	571	644	853	926	1124	1264			
Material Value	406	493	603	596	707	588	432	485	701	740	907	1015			
Labor	184	231	277	238	241	189	139	159	152	186	217	249			
GARMENTS	502	618	541	545	603	623	751	1098	1317	1575	1776	1861			
Regular	280	349	306	318	248	264	290	372	440	571	681	678			
Consigned	222	269	235	227	355	359	461	726	877	1004	1095	1183			
Material Value	140	160	144	136	222	222	274	409	486	543	601	689			
Labor	82	109	91	91	133	137	187	317	391	461	494	494			
B. GROWTH RATES (%)															
ELECTRONICS	62.86	24.89	19.33	5.30	26.21	-20.54	-12.97	21.76	31.90	10.98	10.26	17.11	19.67	13.17	16.42
Regular	102.50	40.74	5.26	82.50	73.97	-26.77	24.73	36.49	31.16	14.29	-4.21	24.78	46.37	21.21	33.79
Consigned	58.60	22.71	21.55	-5.23	13.67	-18.04	-26.51	12.78	32.45	8.56	21.38	12.46	15.54	10.19	12.87
Material Value	70.59	21.43	22.31	-1.16	18.62	-16.83	-26.53	12.27	44.54	5.56	22.57	11.91	19.16	11.72	15.44
Labor	37.31	25.54	19.91	-14.08	1.26	-21.58	-26.46	14.39	-4.40	22.37	16.67	14.75	8.06	6.22	7.14
GARMENTS	23.95	23.11	-12.46	0.74	10.64	3.32	20.55	46.21	19.95	19.59	12.76	4.79	8.22	20.64	14.43
Regular	29.03	24.64	-12.32	3.92	-22.01	6.45	9.85	28.28	18.28	29.77	19.26	-0.44	4.95	17.50	11.23
Consigned	18.09	21.17	-12.64	-3.40	56.39	1.13	28.41	57.48	20.80	14.48	9.06	8.04	13.46	23.05	18.25
Material Value	15.70	14.29	-10.00	-5.56	63.24	0.00	23.42	49.27	18.83	11.73	10.68	14.64	12.94	21.43	17.19
Labor	22.39	32.93	-16.51	0.00	46.15	3.01	36.50	69.52	23.34	17.90	7.16	0.00	14.66	25.74	20.20
C. RATIO TO TOTAL															
ELECTRONICS	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00
Regular	12.07	13.60	12.00	20.80	28.67	26.42	37.87	42.45	42.21	43.47	37.76	40.24	18.93	40.67	29.80
Consigned	87.93	86.40	88.00	79.20	71.33	73.58	62.13	57.55	57.79	56.53	62.24	59.76	81.07	59.33	70.20
Material Value	68.81	68.09	68.52	71.46	74.58	75.68	75.66	75.31	82.18	79.91	80.69	80.30	71.19	67.72	69.32
Labor	31.19	31.91	31.48	28.54	25.42	24.32	24.34	24.69	17.82	20.09	19.31	19.70	28.81	17.99	22.98
GARMENTS	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00
Regular	55.78	56.47	56.56	58.35	41.13	42.38	38.62	33.88	33.41	36.25	38.34	36.43	51.78	36.16	43.97
Consigned	44.22	43.53	43.44	41.65	58.87	57.62	61.38	66.12	66.59	63.75	61.66	63.57	48.22	63.84	56.03
Material Value	63.06	59.48	61.28	59.91	62.54	61.84	59.44	56.34	55.42	54.08	54.89	58.24	61.35	48.34	54.35
Labor	36.94	40.52	38.72	40.09	37.46	38.16	40.56	43.66	44.58	45.92	45.11	41.76	38.65	37.37	37.96

* Total electronics less wiring harness.

Source: National Statistics Office (NSO), the Philippines.

recent years, as electronics and garments, also manifest heavy reliance on components/accessories which are either imported directly by producer-exporters under the regular category, or provided by importers under consignment arrangements. Under the latter arrangement, the value of imported items are deducted from the value of export sales upon collection of payment. The difference between total sales and material value is attributed to labor or local value-added.

Based on records of the National Statistics Office (NSO), the share of consigned electronics exports to total exports declined from 87.9 percent in 1980 to 59.8 percent in 1991 (Table 6.4) as the 12 -year average annual growth of regular electronics exports at 33.8 percent was almost triple the growth of consigned electronics exports at 12.9 percent. Over the twelve-year period, consigned electronics exports accounted for an average annual share of 70.2 percent of total exports vis-a-vis the 29.8 percent share of regular exports. Meanwhile, the growth of material value at 15.4 percent was more than double the growth of labor value at 7.1 percent, and accounted for an annual average share of 69.3 percent to export value during the twelve-year period.

In the case of garments, the annual average share accounted for by consigned exports rose from 44.2 percent during the 1980-1985 period to 63.6 percent during the 1986-1991 period, as its average annual growth at 18.2 percent during the twelve-year period outpaced that of regular exports at 11.2 percent. Similarly, the average annual share of material value to total consigned garment exports for the period is higher at 54.4 percent than labor value at 37.9 percent.

2.3 Direction of Trade

The U.S. and Japan continue to be the country's leading export market, though their combined share had declined from 81.1 percent in 1970 to 55.51 percent in 1991. Principal exports to the U.S. included electronics, garments, coconut oil, and sugar. Exports to Japan diversified from logs and lumber to include non-traditional products consisting of copper concentrates, shrimps and prawns, brass bars, bananas, iron agglomerates, gold from copper ore, and concentrates, petroleum naptha and garments.

Meanwhile, the share of Philippine exports to EEC, ASEAN, and the NICs (Hong Kong, South Korea and Taiwan) have risen (Table 6.5).

Table 6.5
DIRECTION OF EXPORTS, 1970-1991
(Percent Share to Total)

Country	1970	1975	1980	1985	1990	1991
T O T A L (All Countries)	1062	2294	5788	4629	8186	8840
UNITED STATES	41.46	28.95	27.44	35.72	37.80	35.56
JAPAN	39.63	37.70	26.49	18.89	19.74	19.95
EUROPEAN ECONOMIC COMMUNITY	7.98	16.20	16.95	13.59	17.70	18.57
France	0.27	1.02	1.64	1.88	1.76	1.86
F.R. of Germany (West) *	1.87	2.89	4.41	3.78	4.77	5.68
Netherlands	4.10	7.68	6.32	3.14	4.36	3.83
United Kingdom	1.01	3.59	2.53	3.61	4.28	4.20
Italy	0.32	0.43	1.15	0.62	0.75	0.89
Others 1/	0.40	0.59	0.89	0.57	1.78	2.10
MIDDLE EAST COUNTRIES	0.26	2.20	1.99	1.54	1.57	1.69
Iraq	0.00	0.00	0.85	0.04	0.00	0.00
Iran	0.02	1.72	0.08	0.12	0.03	0.00
Kuwait	0.02	0.05	0.08	0.13	0.07	0.03
Saudi Arabia	0.00	0.15	0.46	0.85	0.78	0.67
Bahrain	0.00	0.01	0.01	0.03	0.03	0.05
Others 2/	0.22	0.27	0.51	0.38	0.67	0.94
ESCAP COUNTRIES 3/	6.09	6.74	16.04	19.92	15.59	15.92
ASEAN	1.21	2.64	6.51	11.47	7.14	6.97
Indonesia	0.16	0.86	1.85	0.39	0.74	0.47
Malaysia	0.05	0.21	1.63	3.75	1.55	1.39
Singapore	0.69	1.38	1.95	5.40	2.93	2.60
Thailand	0.30	0.19	1.09	1.90	1.91	2.50
Brunei 4/	0.00	0.00	0.00	0.01	0.01	0.01
Other ESCAP Countries	4.88	4.10	9.52	8.45	8.45	8.95
Australia	0.42	1.38	1.69	1.74	1.18	1.18
Hong Kong	1.07	1.20	3.31	4.05	4.04	4.43
R. of Korea (South)	2.95	0.63	3.50	1.55	2.80	2.58
New Zealand	0.03	0.06	0.07	0.35	0.11	0.11
India	0.08	0.21	0.28	0.34	0.03	0.19
Brunei 4/	0.00	0.08	0.06	0.00	0.00	0.00
Others 5/	0.33	0.54	0.61	0.43	0.29	0.46
SOCIALIST COUNTRIES	0.00	1.57	4.42	2.66	1.01	1.72
P.R. of China	0.00	1.10	0.78	1.72	0.75	1.45
U.S.S.R.	0.00	0.45	3.27	0.71	0.19	0.18
Romania	0.00	0.00	0.07	0.00	0.02	0.06
Others 6/	0.00	0.02	0.30	0.23	0.06	0.04
OTHER COUNTRIES	4.59	6.64	6.67	7.67	6.58	6.58
R. of China (Taiwan)	1.84	1.25	1.74	1.86	2.56	2.37
Canada	0.33	0.81	1.11	1.60	1.50	1.65
Brazil	0.03	0.03	0.40	0.03	0.02	0.06
Sweden	0.37	0.34	0.31	0.30	0.22	0.24
Switzerland	0.03	0.21	0.18	0.66	0.19	0.19
Others	1.99	4.00	2.94	3.24	2.10	2.08

1/ Comprising Belgium, Denmark, Ireland, Luxembourg, Spain, Portugal and Greece.
2/ Comprising Abu Dhabi, Aden, Egypt, Israel, Jordan, Lebanon, Oman, Qatar, Syrian Arab R., Yemen & Demo. Yemen.
3/ Excluding regular and associate members which are included in other groups: P.R. of China, France, Iran.
4/ Brunei became a member of the Association of Southeast Asian Nations (ASEAN) in 1984.
5/ Comprising Afghanistan, Bangladesh, Bhutan, Burma, Demo. Kampuchea, Laos, Mongolia, Nauru, Nepal, Pakistan.
6/ Comprising Albania, Bulgaria, Czechoslovakia, German D.R. (East), D.R. of Korea (North), Poland, Yugoslavia.
* With the formal reunification of East and West Germany on 3 October 1990, data on the former starting in 1991, and which previously was lodged under Other Socialist Countries, was classified under the latter.

Source: National Statistics Office, the Philippines.

It is also worth noting that Philippine exports to these countries rose dramatically during the period 1975-1992, surpassing the growth of the country's total exports to the world.

2.4. Empirical Evidence on the Determinants of Exports

In order to determine the factors which have a significant effect on export demand, this study updated the export demand equation derived from DER-I's aggregate trade model. This equation relates export to three factors, namely: (i) the foreign demand for the Philippines' exports; (ii) the export price; and, (iii) the level of imports, given the import dependence of Philippine exports, particularly manufactured exports.

The study utilized 1970-1991 data in the initial runs, and eliminated the abnormal years (those of the foreign exchange crisis, i.e., 1983-1986) in later runs. It also eliminated variables which proved to be insignificant in the initial runs.

Data on foreign demand was obtained from IMF statistics on the growth rate index of non-oil import volume of developed countries (PCNOM); the export price index was used for exports (PIX); the import volume index was used for imports (VIM); and, the volume index of exports was the variable used for real exports (VIX). Domestic demand in constant terms was also selected as a determinant of export demand (see Appendix 6.1).

The equation which yielded the most significant result was that allowing for breaks in the series during the 1984-1986 crisis, the impact of which was most severely felt in 1984. The initial runs also showed that foreign demand for exports was not a significant factor in export expansion, considering that Philippine exports account for only a negligible portion of world exports.

The second set of runs, which eliminated the foreign demand variable (PCNOM), resulted in improved t-statistic for the other set of variables.

Hence, it may be concluded that domestic demand, the price of exports and the volume of imports are major determinants of Philippine exports. A positive relationship exists between GDP and imports on the

one hand, and exports on the other; while an inverse relationship exists between the export price and exports. Meanwhile, the industrialized countries' demand for exports does not significantly affect real exports.

The equation describing this relationship is summarized as follows (Appendix 6.2):

VIX = -67.09377 + .0002262 GDP - 0.2519471 PIX + 0.4234515 VIM
r^2 = 0.956121; DW = 1.663222; FSTAT = 101.68690

where: VIX = Volume index of exports
GDP = Constant GDP (1985=100) in million pesos
PIX = Price index of exports
VIM = Volume index of imports

III. Export Promotion Policies

3.1 Review of Trade, Industrial and Monetary Policy

It has been observed that trade, tariff and monetary policies implemented in the past have converged to create a bias against exports, thus explaining the slow-paced movement of exports. In the 1950s, the Philippine authorities imposed strict foreign exchange controls as when it encountered balance of payments difficulties with the reduction of U.S. economic assistance. In its defense of the pre-war parity of the peso vis-a-vis the dollar, the Government resorted to the rationing of foreign exchange according to essentiality, wherein only producer goods could be imported. Import control, thus, became a permanent feature of the Government's import policy for that decade, thus encouraging investments in import-substituting industries which rewarded the final stages of manufacturing and penalized backward linkages, as well as exports.

With the decontrol program completed in 1962, the existing bias was reinforced by the tariff system of 1957 which replaced controls as the tool of protection, thus preserving the structure of protection during the control system of the 1950s.

Aware of the setback facing exports, government planners, towards the end of the 1960s, promoted exports without reforming the protection structure. As part of its export promotion drive in the 1970s,

two major pieces of legislation were enacted, namely, the Investment Incentives Act and the Export Incentives Act of 1970, encouraging investments in identified priority areas for export and export industries. Complemented by the February 1970 major devaluation of the peso, these efforts resulted in the emergence of new non-traditional exports in the mid-1970s. Growth, however, was concentrated along two non-traditional exports, namely, semi-conductors and garments.

Import controls on consumer goods again became widespread in the 1970s with the protection of local industry cited as a major consideration behind such moves, thus largely preserving the tariff structure which escalated according to the stage of processing. In the 1970s, the inadequacy of export promotion measures alongside a protective industrial structure was recognized. Unlike previous trade liberalization efforts which aimed to redress balance of payments problems and provide partial support to exports, the trade reform package of the 1980s aimed at correcting the adverse effects of the previous trade regime by reducing overall protection to industry. Thus, a comprehensive trade reform program was launched in 1981, with two major components; (i) the Tariff Reform Program (TRP); and, (ii) the Import Liberalization Program (ILP).

Under the TRP, nominal tariff rates declined modestly from 31 percent in 1982 to around 28 percent in 1985. Further tariff reform implemented under E.O. No. 470 of January 1992 will reduce by 1995, the tariff range is 3-30 percent (except for a number of items with 50 percent and 0 duty).

Under the ILP which was started in August 1981, the Philippine Government formally committed to remove licensing restrictions on 1229 items on a staggered basis. During the foreign exchange crisis of 1983, the program was temporarily shelved, but was resumed in two phases starting in 1986. As at end-December 1992, only 135 items were restricted, including 69 items which shall not be liberalized for reasons of health, safety and national security.

3.2 Recent Developments in Monetary Policy

3.2.1 Foreign Exchange Policy

Complementary moves in the area of exchange rate policy and provision of export financing were also undertaken by the Government

in the 1990s. In order to arrive at a more market-oriented determination of the exchange rates, the Central Bank (CB) pursued a series of bold moves in 1992, starting with the removal of restrictions on off floor foreign exchange trading among commercial banks and the launching of the Philippine Dealing System on 28 April 1992. Under this system, authorized dealers of participating banks were allowed to access prices and initiate the purchase and sale of foreign exchange anytime between 8:30 a.m.- 5:30 p.m. By allowing instant access to market prices dealers were able to take immediate action in case of price changes. This increased market liquidity at the same time that a more market-determined exchange rate was established.

In addition to the deregulatory moves which lifted restrictions on non-trade transactions on 3 January 1992, the Central Bank moved on to liberalize restrictions on foreign trade transactions with the issuance of CB Circular No. 1348 of 28 July 1992 and CB Circular No. 1353 of 24 August 1992. These measures included, among others: (i) the removal of the mandatory surrender requirement for export proceeds, in effect, allowing 100-percent retention by exporters; and, (ii) streamlining and liberalization of the export and import process, thus resulting in lower transaction costs for exporters.

3.2.2 Foreign Currency Loans

To improve and expand financing available to exporters, the Central Bank introduced under Circular No. 1262 of 9 November 1990, the Foreign Currency Deposit Unit (FCDU) loans which allowed exporters to avail of a U.S. dollar-based working capital credit financing facility for their peso requirements at terms aligned with those prevailing in the international market. Initially, the maximum loan amount allowed was 50 percent of the confirmed letter of credit (L/C), purchase order (P/O), or sales contract (SC). The allowable loan amount was raised to 70 percent in December 1991 under CB Circular No. 1317 of 11 December 1991, and to 100 percent under CB Circular No. 1353 of 24 August 1992. These privileges were also extended to indirect exporters, i.e., manufacturers/producers in the domestic market. In addition, exporters were allowed, with prior central bank approval, to borrow funds from FDCUs to fund the full amount of their project's foreign cost component, and up to 50 percent of the peso cost (Circular No. 1249 of 22 August 1990). It also gave exporters the option to choose whether to avail of the loans in local currency to pay for local costs or in foreign

exchange to pay for import costs of machinery, spare parts, or raw materials to be used in the production of, or as inputs to export commodities.

3.2.3 Rediscounting Policy

Meanwhile, Central Bank also pursued its major role of providing credit assistance to the export sector, mainly through the rediscounting facility for export papers of exporters to fund their domestic as well as foreign costs.

Availment of the central bank rediscounting facility is possible through Authorized Agent Banks (AABs) which act as retailers of the facility. Currently, there are 30 commercial banks, four of which are subsidiaries of foreign banks, and two of which are government-owned. These banks provide pre- and post-shipment loans which they can rediscount with the Central Bank.

In March 1990, central bank regional officers were allowed to rediscount export credits up to a maximum of P 5 million/ application for commercial banks. P 3 million for rural banks, and P 450,000 for thrift banks. Per CB Memo Circular No. 420 of 12 April 1991, the rediscounting facility was extended to include indirect exporters (i.e., manufacturers who have supply arrangements with direct exporters) of less than P 5 million for cottage and small-scale industries, and less than P 20 million for medium and small-scale industries. These loans are made subject to certain conditions, such as the requirement that at least 70 percent of the raw materials used by the borrower should be indigenous or locally produced.

To ensure greater access by exporters, the 1991 export rediscount budget of the Central Bank was raised to P 8 billion from P 5 billion in 1990. Although there is no ceiling on the lending rate that the banks can charge on their rediscount papers, the Central Bank has monitored the bank's spread, using moral suasion in order that commercial banks would limit their spread to 3 percent.

3.3 Other Financial Assistance to Exporters: Export Insurance and Guarantees

The Philippine Export and Foreign Loan Guarantee Corporation (PHILGUARANTEE) operates a pre-shipment export finance guarantee

(PEFG) scheme, with the objective of providing a collateral substitute to protect commercial banks' pre-shipment export loans against exporters' default risks, thus enhancing the ability of exporters to secure finance. The PEFG is distinct from an export insurance or guarantee scheme, which protects exporters or commercial banks against non-payment risks by foreign buyers.

The PEFG can apply to either a transaction-based pre-shipment loan related to a single export sale or revolving pre-shipment loans related to numerous export sales over a one-year period. Interest rates are determined by the bank, usually at market rates; the filing fee is 0.2 percent of the guarantee accommodation with a minimum fee of P 1000, while the guarantee fee is 1.5 percent per annum. For transaction loans, the amount can range between P 150,000 and P 4.5 million, while for revolving loans, the range is P 150,000 to P 7 million provided the loan does not exceed 150 percent of the previous year's exports. PHILGUARANTEE guarantees prepayment of 85 percent of the principal and interest of a transaction loan and 70 percent of a revolving loan.

However, PHILGUARANTEE has not been able to develop significant guarantee instrument, as only 15 exporters and less than 2 percent of the central bank export loans were covered by the guarantee scheme in 1988. The problems are reported to have emerged from the lack of credit standing of PHILGUARANTEE, stemming from earlier problems with overseas construction project guarantees, and flaws in the basic technical and operational approach, which applied stringent eligibility requirements.

3.4 Fiscal Policy

3.4.1 Fiscal Incentives

Fiscal incentives available to exporters are in the form of tax credit available to BOI-registered exporters to compensate for taxes and duties paid on imported raw materials used in the export product. Non-BOI registered exporters may also claim this incentive from Bureau of Internal Revenue (BIR) and the Bureau of Customs (BOC).

3.4.2 Duty and Tax Concessions

To enable exporters to obtain inputs at internationally competitive prices, imported inputs are allowed to enter free of duty under the

bonded manufacturing warehouse, customs bonded warehouse and a duty exemption scheme. A duty drawback/refund scheme is also allowed.

3.5 Institutional Measures for Export-Oriented Industries

3.5.1 Bonded Manufacturing Warehouses

The bonded manufacturing warehouse (BMW) scheme exempts exporters-manufacturers from payment of duties and taxes on their imports. The Bureau of Customs administers the rules and regulations for such establishments. In the case of garments and textiles, the administering agency is the Garment and Textile Export Board (GTEB). Apart from the requirements common to BMWs in most developing countries that the firm be primarily engaged in manufacturing for export and that it should have a separate warehouse duly approved by customs, the Philippines imposes the following additional requirements: (i) "formula of manufacture", determining input-output coefficients, or its equivalent, must be submitted and approved by the Industrial Technology Development Institute, or by the GTEB in the case of garments; (ii) the company must export at least 70 percent of its production; and, (iii) if the products belong to the regulated list, it needs to be certified for every shipment that there are no competitive substitutes available locally.

The duty exemption scheme (DES), under Section 105(d) of the Tariff and Customs Code of the Philippines (TCCP), allows duty-free importation of raw materials that are to be processed into finished products for export. These importations must be covered by a re-export bond equivalent to 150 percent of the value of ascertained duties and taxes, and reexported within six months of the shipment date. Initially, there were certain ineligibility requirements in terms of asset size and consignment importations, but these have been repealed since October 1990.

The duty drawback/tax credit scheme (DDS), under Section 106 of the Tariff and Customs Code of the Philippines, allows direct and some indirect exporters to obtain drawbacks on duties and taxes paid on intermediate goods. Although the Department of Finance is the main implementing arm, the Board of Investment is mandated under the Omnibus Investment Code of 1987 to grant duty drawback in the form of tax credit certificates (TCCs) to BOI-registered exporters. The TCCs

are either issued at an established standard rate which is a fixed percentage of export value, or are based on the actual taxes and duties paid on imports. TCCs may be issued after the evaluation of an application, or in advance against a surety bond of 25 percent of the tax credit claimed.

3.5.2 Export Processing Zone Authority

The Export Processing Zone Authority (EPZA), a government corporation created in October 1992, operates and manages zones with the goal of making them major contributors to the country's industrialization and export expansion programmes and promoting the zones as suitable sites for foreign investments. EPZA manages four fully operational zones in Bataan, Mactan, Baguio and Cavite, as well as three industrial areas in Batangas, Leyte and Zambales, which have been designated as special zones. The zones have been operating as a separate, self-contained enclaves for a variety of industries that use imported raw and intermediate materials for processing, assembly and manufacture of goods for export.

The preferred industries in the Bataan, Mactan and Cavite zones are similar. These include food, beverages, tobacco; textiles, garments and leather; wood and wood products, including furniture and fixtures; fabricated metal products, machinery and equipment; chemical and chemical products, rubber and plastic products; and, non-metallic mineral products.

On the other hand, the cool and dry environment in Baguio is more likely to suit high technology and labor-intensive industries, including electronics and electrical products and accessories; light metal products; light machinery and accessories; footwear and leather products; pharmaceuticals, chemicals, and medical supplies; and, toys, gifts, housewares and handicrafts.

3.5.3 Incentives

Incentives offered to some enterprises include tax and duty exemptions, tax credits and other special privileges and priorities, as follows:

(i) New registered firms are fully exempted from income taxes for a period of six years for pioneer firms and four years for

non-pioneer firms. This can be extended to another year if the project utilizes indigenous raw materials or if the project meets the prescribed ratio of capital equipment to number of workers, or the net foreign exchange savings or earnings amount to at least US$ 500,000 during the first three years of operation. Expanding firms are entitled to an exemption from income taxes proportional to their expansion for a period of three years.

(ii) Zone enterprises are exempt from the payment of duties and taxes for goods intended for use in the manufacturing process, unless such goods are exempted from export taxes, imposts or fees. EPZA has its own customs facilities. Zone enterprises also benefit from simplified export and import procedures and are exempt from the requirement of pre-shipment inspection.

(iii) Zone enterprises are exempted from all local taxes, contractor's tax, wharfage fees, branch profit remittance tax and are subject to zero rating of the value-added tax on purchases from local suppliers. They do, however, have to pay real estate taxes between 2-3 percent of the assessed value.

(iv) Zone enterprises are given priority in the allocation of foreign exchange, and are given the same priority as enterprises registered with the Board of Investment in obtaining financial assistance from government financial institutions.

(v) There is no limitation on the ownership of equity by foreigners, or foreigners may be employed in supervisory, technical or advisory positions for five years from registration. Enterprises registered with the EPZA are allowed to remit earnings and repatriate capital.

IV. Problems and Issues on Export Promotion

Philippine exports have generally been exceeded by imports, thus causing large deficits in the balance of trade and the balance of payments. This has been the chronic problem of the Philippines since the 1950s.

The problem may be traced to the underperformance of exports, attributable to policies which have created an inherent bias against exports, resulting in the failure to promote a wider and more diversified

export base. Thus, an effective export promotion program would have to provide arrangements necessary to achieve neutral status for export activities, namely:

(i) a realistic exchange rate;
(ii) a free trade regime that enables exports to have access to inputs at competitive terms;
(iii) automatic access to export financing at reasonable rates;
(iv) competitive prices for primary inputs; and,
(v) compensatory export incentives to establish neutral status.

Given the low domestic savings rate in the Philippines, foreign direct investment becomes a necessary component for export development, as it is needed to fill up the country's investment-savings gap. In the past, however, a series of events in the country has served to create an impression of instability. Also, frequent changes in the operating conditions resulting from too much politicking in the administrative process adds to the uncertainty, thus inducing investors to seek less risky investment areas.

Meanwhile, recent liberalization measures including those in the exchange market which were expected to lead to a more market-determined exchange rate, have initially resulted in the appreciation of the peso to the detriment of exports. On the supply side, the increase in foreign exchange can be traced to the generally liquid foreign position of the banking system, due to limits imposed on individual banks' foreign exchange position and the external sector's improved performance, spurred principally by the rise in overseas workers' remittances and influx of portfolio investments in fixed income securities, given the interest rate differential between dollars and pesos. Meanwhile, the slack on the demand side resulted from the weak domestic activity and the preference for pesos due to high interest rates on peso-denominated assets.

In the area of financing, the introduction of FCDU loans to exporters has enhanced the existing system of export finance available to both exporters and indirect exporters. Financing available to exporters from regular banking channels, however, continue to be limited and subject to high interest rates.

It has also been observed that although the foreign exchange rules on trade and trade transactions have been liberalized, these have not

been accompanied by appropriate infrastructure support facilities, as for instance, port, communications, transport facilities, power and water supply. The lack of these factors prevent the efficient functioning of export firms and is also one of the reasons for the slow pace of foreign investments.

Lastly, the country's limited export base consisting of resource-based and manufactured exports is further aggravated by the fact that the two dominant categories of manufactured exports are import-intensive, as evidenced by the high import content of consigned products, where imported material value averaged at 69.3 percent for electronics and 54.3 percent for garments.

V. Policy Recommendations

Effective export promotion in the Philippines would have addressed the more basic issues of attracting foreign investments since it has been identified as a basic component in the country's export strategy. First and foremost, therefore, the Government should concentrate on establishing peace and order to project a stable image for the country. Government should also strive to adhere to a consistent set of policies.

Private sector participation should be harnessed to support government efforts. A coordinating body that would bring in all the key decision-makers to provide direction, guidance, and coherence to the development and promotion of exports and investments should be created. There is currently a bill in Congress proposing the creation of such an export coordinating agency.

Areas which this agency should study include:

(i) the development of a wider export base which are less import-intensive, including services exports of "knowledge workers", such as engineers and computer technicians;
(ii) identification of areas which need improvement of basic infrastructure facilities where build-operate-and-transfer (BOT) schemes may be undertaken, specifically transport, communication, and power projects; and,
(iii) recommendation on further steps to be taken in order to promote a more open system and thus improve the efficiency

of domestic industries, enabling them to compete in the international market.

Competition in the banking sector should be enhanced by allowing the entry of more banks so that borrowers, including exporters and manufacturers get better service at the lowest possible cost. A bill deregulating the banking industry is currently pending in Congress.

Finally, the Government should dismantle the 180-day forward cover scheme under the OPSF so that the real demand for foreign exchange may be reflected. This, however, may not be readily implementable as it needs to be pursued in coordination with the deregulation of the industry.

VI. Summary and Conclusion

(1) The performance of Philippine exports has lagged behind those of its ASEAN counterparts. This may be traced to the inherent bias against exports resulting from the inward-looking and protectionist development strategy pursued by the country since the 1940s.

(2) While the problem has been recognized in the 1970s, meaningful effort to correct the adverse effects of previous trade and industrial policy was launched only in 1981 under the comprehensive trade reform program. Two major components of the program consisted of the Tariff Reform Program (TRP) and the Import Liberalization Program (ILP).

(3) The TRP reduced average nominal tariff rates from 31 percent in 1982 to 28 percent in 1985; while further tariff reform implemented under E.O. No. 470 of 20 July 1991 will reduce the tariff range to 3-30 percent. The ILP was implemented on a staggered basis starting in 1981. After it was temporarily shelved during the foreign exchange crisis of 1983, it was resumed in two phases starting in 1986. To-date there are restrictions on 135 items, inclusive of the 69 items which are regulated for reasons of health, safety and national security.

(4) In the 1990s, further liberalization moves were undertaken along the area of exchange rate policy, trade process and availment of

foreign currency loans in order to promote the competitiveness of the country's export industry.

(5) To-date, arrangements to achieve neutral status for exports have not yet been completed. Moreover, given the low domestic savings rate in the Philippines, foreign direct investment becomes a necessary component for export development. However, the unstable image of the Philippines, together with the current lack of infrastructure support facilities pose as serious deterrents to foreign investments.

(6) Meanwhile, the study also observed that, aside from the narrow export base, Philippine exports are highly import-intensive. This was supported by the trade model developed by DER-I which identified imports as among the factors directly affecting exports.

(7) In view of the above, it is recommended that:
   (i) Government should concentrate on creating an image of stability for the Philippines by securing peace and order in the country. Relatedly, it should pursue a consistent set of policies;
   (ii) private sector participation especially in the banking, energy and oil sector, be harnessed to support government efforts and that an overall coordinating body be organized to provide direction, guidance and coherence to export development and promotion;
   (iii) competition in the banking sector should be enhanced by allowing the entry of more banks, including foreign banks to help increase accessibility to private sector, thus benefiting clients, including exporters, who will get better services at the lowest possible cost due to higher competition and hence, lowering intermediation cost;
   (iv) the 180-day forward cover arrangement for oil under the OPSF which tends to depress demand for foreign exchange should be gradually dismantled together with the gradual deregulation to further extent than the recently introduced system of service contracts to mobilize private sector in the oil industry.

REFERENCES

1. Alburo, Florian and Geoffrey Shephered, ***Trade Liberalization Experience in the Philippines***, Philippine Institute of Development Studies, 1989.

2. _____, and Ronald Bobel, et. al., ***Philippine Trade and Investment Regimes: A Comparison with Neighbors***, prepared for the U.S. Agency for International Development, December 1991.

3. Corbo, Vittorio, et. al., ***Export-Oriented Development Strategy***, Westview Special Studies in Social, Political and Economic Development, 1985

4. Estanislao, ***Philippine Economic Structure from the 20's to the 70's***, Manila: Southeast Asian Science Foundation, 1974.

5. Lamberte, Mario, et.al., *A Study of the Export Financing System in the Philppines*, Philippine Institute of Development Studies, ***Working Paper No. 89-112***, June 1989.

6. Manasan, Rosario, *A Review of Investment Incentives in ASEAN Countries*, Philippine Institute of Development Studies, ***Working Paper Series No. 88-27***, 1988.

7. Naya, Zita Lopez, ***Wage and Productivity Competitiveness of Filipino Manpower in the Asean Region***, The Philippine Economy in Transition Center for Research and Communication, December 1992.

8. ***Report of the Philippine Government to the GATT Trade Policy Review***, February 1992.

9. Power, John, and Gerardo Sicat, ***The Philippines: Industrialization and Trade Policies***, London: Oxford University Press, for OECD Paris, 1971.

10. Sicat, Gerardo P., ***Economic Progress in South Korea and Taiwan: Lessons for the Philippines***, University of the Philippines, 1969.

11. Valdepeñas, Vicente B., ***The Protection and Development of Philippine Manufacturing***, Ateneo de Manila University Press: 1970.

12. World Bank, ***The Philippines: Country Economic Memorandum - Issues in Adjustment and Competitiveness***, Report No. 8933PH, 31 October 1990.

13. _____, ***The Philippines: Country Economic Memorandum - Towards Sustaining the Economic Recovery***, 30 January 1989.

DATA USED IN REGRESSION ANALYSIS

obs	GDP	PIX	VIX	VIM	X	M	Y	GDPA	PCNOM	GDPB
1970	343163.0	54.6700	45.1600	91.9000	61526.0	80336.0	-18810.0	361973.0	0.0000	341625.0
1971	361792.0	51.9600	49.4500	98.3000	63826.0	79877.0	-16051.0	377843.0	7.9000	356581.0
1972	381499.0	49.2100	51.3000	99.2300	71372.0	82354.0	-10982.0	392481.0	11.6000	370981.0
1973	415525.0	71.7900	55.2700	92.8000	73058.0	86696.0	-13638.0	429163.0	15.7000	398251.0
1974	430313.0	119.2300	49.3700	109.5000	73581.0	99864.0	-26283.0	456596.0	2.4000	433634.0
1975	454264.0	94.8700	52.2500	114.8600	76181.0	105930.0	-29749.0	484013.0	-11.4000	472754.0
1976	494262.0	83.0600	66.9500	121.6100	85954.0	107656.0	-21702.0	515964.0	18.9000	509905.0
1977	521952.0	84.2900	80.7600	118.3300	100062.0	114654.0	-14592.0	536544.0	6.7000	528441.0
1978	548947.0	94.5300	78.2700	139.8000	106121.0	129249.0	-23128.0	572075.0	12.7000	558547.0
1979	579910.0	116.1800	85.5600	152.6000	110678.0	150063.0	-39385.0	619295.0	9.2000	594267.0
1980	609768.0	121.0700	103.2700	154.5300	154748.0	179477.0	-24729.0	634497.0	3.6000	608651.0
1981	630642.0	87.2900	137.8200	152.5100	164698.0	178057.0	-13359.0	644001.0	6.0000	622292.0
1982	653467.0	85.1500	124.4100	162.3900	151489.0	182414.0	-30925.0	684392.0	2.7000	653969.0
1983	665717.0	82.8900	128.2000	155.7900	158252.0	176841.0	-18589.0	684306.0	11.1000	664731.0
1984	616962.0	83.1400	138.2300	119.2800	164327.0	145934.0	18393.0	598569.0	19.5000	597302.0
1985	517883.0	100.0000	100.0000	100.0000	137030.0	125205.0	11825.0	506058.0	5.3000	552049.0
1986	591423.0	88.8300	116.6100	119.7100	160453.0	138021.0	22432.0	568991.0	9.3000	573409.0
1987	619707.0	97.6600	124.1600	158.0400	170889.0	177532.0	-6643.0	626350.0	8.7000	609766.0
1988	658463.0	107.7300	138.2000	191.2700	195997.0	212357.0	-16360.0	674823.0	12.7000	655009.0
1989	697816.0	105.6800	155.0000	229.2900	215347.0	244590.0	-29243.0	727057.0	7.7000	711261.0
1990	712869.0	102.6800	166.1600	246.3700	219703.0	271521.0	-51818.0	764687.0	6.1000	745544.0
1991	712492.0	164.6900	171.7600	250.5800	235625.0	264012.0	-28387.0	740879.0	3.1000	741554.0

Where:

GDP	=	Constant GDP in P million
GDPA	=	Constant GDP - (X=M)
GDPB	=	Constant GDP - (X-M) - statistical discrepancy or C+I+G
PCNOM	=	Growth rate index for partner countries' non-oil imports
PIX	=	Price index of exports
VIX	=	Volume index of exports
VIM	=	Volume index of imports
X	=	Exports in constant P 1985=100
M	=	Imports in constant P 1985=100
Y	=	Exports - Imports

ESTIMATION RESULTS

SMPL 1971 - 1983 1987 - 1991
18 Observations
LS // Dependent Variable is VIX

VARIABLE	COEFFICIENT	STD.ERROR	T-STAT.	2-TAIL SIG.
C	-67.0973770	14.3006970	-4.6918956	0.000
GDP	0.0002262	4.633D-05	4.8817777	0.000
PIX	-0.2519471	0.1211169	-2.0801981	0.056
VIM	0.4234515	0.1178341	3.5936242	0.003

R-squared	0.956121	Mean of dependent var	101.0089
Adjusted R-squared	0.946719	S.D. of dependent var	42.92457
S.E. of regression	9.908175	Sum of squared resid	1374.407
Durbin-Watson stat	1.663222	F-statistic	101.6869
Log likelihood	-64.55955		

SMPL 1971 - 1983 1986 - 1991
19 Observations
LS // Dependent Variable is VIX

VARIABLE	COEFFICIENT	STD.ERROR	T-STAT.	2-TAIL SIG.
C	-73.0180400	15.1593680	-4.8166943	0.000
GDP	0.0002619	4.607D-05	5.6834619	0.000
PIX	-0.2414680	0.1313549	-1.8382866	0.086
VIM	0.3300220	0.1164834	2.8332116	0.013

R-squared	0.944995	Mean of dependent var	101.8300
Adjusted R-squared	0.933994	S.D. of dependent var	41.86844
S.E. of regress ion	10.75666	Sum of squared resid	1735.587
Durbin-Watson stat	1.269751	F-statistic	85.90120
Log likelihood	-69.84912		

Chapter 7

EXPORT PROMOTION STRATEGIES: SINGAPORE

by
Alison Lim

I. Introduction

International trade has been fundamental to the growth of the Singapore economy. Export trade in particular, has played a crucial role in expanding the manufacturing sector and accelerating GDP growth. In Singapore, total merchandise exports comprise domestic exports and re-exports. Re-exports are goods exported from Singapore without transformation while in Singapore.[1] Under the category of domestic exports, oil and non-oil domestic exports have been separated for the purposes of analysis. This is because oil exports are large in terms of both volume and value, constituting about one-third of total domestic exports, but its value-added is relatively low. The volume and value of non-oil domestic exports are more proportional to their contribution to GDP.

This paper thus examines the role of exports in terms of total merchandise exports and both total and non-oil domestic exports. It also reviews the export promotion strategies adopted by the Government.

II. Export Trade and Salient Features

2.1 Contribution of Exports to the Economy

The share of total merchandise exports in GDP expanded from 76.3 percent in 1970 to 155.3 percent in 1980. This share has remained fairly constant in the 1980s (Table 7.1).

The share of domestic exports in nominal GDP increased from 26.7 percent in 1970 to 91.2 percent in 1991. The share of re-exports, however, stagnated at about 50 percent. The decline in importance of

1. Repacking, splitting into lots, sorting or grading and marking are not considered as undergoing the process of transformation.

primary commodities has been somewhat offset by the rapid expansion of re-exports of consumer products, industrial equipment, components and parts. Non-oil domestic exports' share in GDP has increased significantly from 13 percent in 1970 to 71 percent in 1991. Service exports are also becoming more important, with its share in GDP expanding from 29.4 percent in 1970 to 60.5 percent in 1991. This reflects increased tourist arrivals and Singapore's development into a regional transport hub.

Single-variable regressions were run to estimate the relationship of non-oil domestic exports (NODX) to GDP growth, import growth and growth of employment in the manufacturing sector. The empirical results are summarized in Appendix 7.1. The time period 1980-1991 was chosen as being more indicative of existing trends.

As expected, NODX and nominal GDP have a fairly strong correlation, with a 1-percent change in the former resulting in a 0.43-percent change in the latter. The contribution of NODX to import growth is also strong. The effect of a 1-percent change in NODX is a 0.48-percent change in imports. This could be explained by the high import content of domestic exports (over 70 percent).

NODX affects employment mainly in the manufacturing sector, given that 86 percent of total non-oil domestic exports in 1991 were manufactured products. The link, however, is weak as manufacturing employment is determined by various other factors. Regression results show that a 1-percent change in NODX is correlated with only a 0.17-percent change in manufacturing employment.

An internal study on business cycles has also shown that export growth leads and moves procyclically with respect to GDP. Granger Causality Tests (Table 7.2) concluded that export growth "causes" income growth, i.e., lagged values of NODX are able to help predict GDP. Quarterly data from 1980-1993 was used for each of the variables and was pre-filtered to remove trend factors prior to running the equations. Changes in the growth rate of GDP were depicted as a function of changes in the growth rate of NODX (please refer to equations in Appendix 7.2). However, causation from income to exports is unconfirmable. The coefficients of the equation are ambiguous.

Table 7.1

SHARE OF EXPORTS IN GDP

Period	As Percentage of Nominal GDP				
	Merchandise Export 1/	Services Exports 1/	Domestic Exports 2/	Non-Oil Domestic Exports 2/	Re-Exports 2/
1970	76.3	29.4	26.7	13.1	50.4
1971	74.2	26.8	31.2	15.8	43.8
1972	70.0	41.3	33.6	20.3	37.2
1973	82.1	41.1	39.1	26.7	43.8
1974	107.2	48.6	60.0	31.7	45.5
1975	90.1	55.9	49.8	25.8	38.8
1976	104.9	53.4	56.8	32.0	47.1
1977	117.8	53.0	65.3	36.0	52.6
1978	122.3	53.5	67.6	38.3	54.7
1979	142.0	55.6	80.0	44.9	62.1
1980	155.3	60.1	92.6	46.3	62.4
1981	141.6	69.9	89.3	43.2	50.6
1982	127.3	71.7	79.1	36.7	46.9
1983	117.5	61.0	71.2	38.0	46.1
1984	120.7	48.9	75.1	43.2	45.7
1985	121.7	46.3	76.3	43.0	45.2
1986	120.2	47.5	77.2	51.9	43.8
1987	135.7	51.1	85.9	64.1	49.7
1988	152.9	53.0	94.7	76.4	59.0
1989	148.3	55.7	93.1	73.9	56.1
1990	144.3	61.7	94.2	71.6	51.0
1991	142.1	60.5	91.2	70.7	51.9

1/ BOP data.
2/ Customs data adjusted to BOP definition.

Table 7.2
GRANGER CAUSALITY TESTS

Equation	$\bar{R}^2$	F-Statistic	Critical F-Level	Accept/Reject Hypothesis
Hypothesis: NODX Does Not Cause Real GDP				
Dependent Variables: RGDP Focus Variables: RGDP (1-3 Lags) NODX (0-4 Lags)	0.696	60.5	5.18	Reject
Hypothesis: Real GDP Does Not Cause NODX				
Dependent Variables: NODX Focus Variables: NODX (1-3 Lags) RGDP (0-4 Lags)	-	-	-	Accept because coefficients of equation ambiguous

2.2 Growth Trend and Changing Patterns of Exports

During 1970-1980, Singapore's total merchandise exports grew at an average annual rate of 23 percent from US$ 1.5 billion to US$ 19.4 billion. The share of domestic exports in total trade increased from 14.9 percent in 1970 to 27.8 percent in 1980. The share of re-exports, on the other hand, fell from 23.8 percent in 1970 to 16.9 percent in 1980, reflecting the gradual erosion of Singapore's traditional dependence on entrepot trade.

From 1981 to 1991, total merchandise exports grew at an average annual rate of 8.9 percent from US$ 21.0 billion to US$ 59.0 billion. The share of both domestic exports and re-exports in total trade increased marginally. The share of non-oil domestic exports has increased from 6.2 percent in 1970 to 22.6 percent in 1991 (Tables 7.3 and 7.4).

The merchandise exports/nominal GDP ratio has increased steadily from 76.3 in 1970 to 142.1 in 1991, as has the export/ import ratio

Table 7.3

SINGAPORE: TOTAL TRADE

	1970		1975		1980		1981		1985		1990		1991	
	US$ Bil.	% Share	US$ Bil.	% Share	US$ Bil.	% Share	US$ Bil.	% Share	US$ Bil.	% Share	US$ Bil.	% Share	US$ Bil.	% Share
Total Trade	4.0	100.0	13.5	100.0	43.3	100.0	48.5	100.0	49.1	100.0	113.1	100.0	125.1	100.0
Imports	2.4	61.3	8.1	60.2	24.0	55.3	27.6	56.8	26.3	53.5	60.6	53.6	66.1	52.8
Exports	1.5	38.7	5.4	39.8	19.4	44.7	21.0	43.2	22.8	46.5	52.5	46.4	59.0	47.2
Domestic Exports	0.6	14.9	3.2	23.5	12.1	27.8	13.9	28.7	14.8	30.2	34.6	30.6	38.2	30.6
Non-Oil Domestic Exports	0.2	6.2	1.5	10.8	5.4	12.5	6.0	12.4	7.6	15.5	25.2	22.3	28.3	22.6
Re-Exports	0.9	23.8	2.2	16.3	7.3	16.9	7.0	14.5	8.0	16.3	17.9	15.8	20.8	16.6

Table 7.4

ANNUAL GROWTH RATE OF EXPORTS

Period	Annual Growth Rates (Percent)				
	Merchandise Export	Services Exports	Domestic Exports	Non-Oil Domestic Exports	Re-Exports
1970	-0.9	15.0	7.1	38.5	-4.6
1971	14.6	7.6	37.7	41.9	2.5
1972	13.1	84.5	29.0	54.0	1.7
1973	46.7	24.8	45.5	64.7	47.4
1974	60.6	45.2	88.5	46.1	27.7
1975	-10.4	22.5	-11.4	-13.3	-9.1
1976	26.8	4.3	24.1	35.1	32.3
1977	23.0	8.6	26.0	23.4	22.2
1978	15.4	12.1	15.0	18.1	15.7
1979	33.7	19.7	36.3	34.9	30.5
1980	33.7	32.1	41.5	26.2	22.8
1981	6.6	36.0	14.1	9.0	-5.2
1982	0.1	14.3	-2.5	-5.3	3.2
1983	3.8	-4.4	1.2	16.5	10.7
1984	12.0	-12.5	14.9	23.9	7.9
1985	-2.0	-7.9	-1.1	-3.3	-3.7
1986	-1.9	1.9	0.4	20.0	-3.9
1987	24.5	18.6	22.7	36.0	25.2
1988	32.2	21.5	29.3	39.9	39.2
1989	10.3	19.5	11.8	10.0	8.0
1990	8.9	24.2	13.3	8.5	1.8
1991	6.8	6.4	5.1	7.0	10.5

which has increased from 78.0 in 1970 to 106.1 in 1991. These reflect further the growing importance of export trade to the economy (Table 7.5).

Table 7.5

EXPORT/IMPORT, EXPORT/GDP RATIO
(Percent)

Period	Export/ Import	Merchandise Exports/ NGDP	Non-Oil Domestic Exports/ NGDP	Merchandise Trade Balance as % of GDP
1970	78.0	76.3	13.1	-45.1
1971	76.1	74.2	15.8	-44.1
1972	86.7	70.0	20.3	-37.3
1973	90.9	82.1	26.7	-31.4
1974	89.1	107.2	31.7	-42.8
1975	93.8	90.1	25.8	-42.3
1976	94.8	104.9	32.0	-37.5
1977	97.8	117.8	36.0	-30.2
1978	97.1	122.3	38.3	-31.9
1979	96.4	142.0	44.9	-32.3
1980	94.5	155.3	46.3	-35.8
1981	95.7	141.6	43.2	-44.1
1982	96.5	127.3	36.7	-44.3
1983	98.7	117.5	38.0	-33.5
1984	99.5	120.7	43.2	-21.7
1985	100.7	121.7	43.0	-16.0
1986	101.7	120.2	51.9	-11.6
1987	100.2	135.7	64.1	-12.1
1988	102.4	152.9	76.4	-9.4
1989	105.0	148.3	73.9	-8.4
1990	103.7	144.3	71.6	-14.6
1991	106.1	142.1	70.7	-10.3

2.3 Markets

The United States (U.S.) has been a major market for Singapore's domestic exports. Its share increased from 11.1 percent in 1970 to 15.1 percent in 1980. In the 1980s, the U.S. market continued to grow strongly and in 1991, its share rose to about 25 percent. Its share of non-oil domestic exports was even higher at 33.1 percent in 1991.

The NIEs have also grown in importance as a market for Singapore's domestic exports, with its share almost doubling from 7.2 percent in 1970 to 12.9 percent in 1980 (Table 7.6). This share remained fairly

Table 7.6

SINGAPORE: DOMESTIC EXPORTS BY SELECTED COUNTRIES
(% Share of Total)

Country	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
EEC	17.4	14.8	16.0	18.9	13.7	14.5	15.5	15.1	13.4	14.4	12.8	11.0	9.7	9.6	10.1	10.6	11.2	12.2	13.0	13.4	14.4	13.9
ASEAN of which:	27.1	28.8	26.6	22.4	20.9	23.9	20.5	20.0	20.8	21.7	22.2	22.7	24.8	25.5	23.1	21.9	20.9	21.1	21.4	21.7	22.0	23.3
Malaysia	21.9	22.9	20.8	18.1	16.6	17.2	15.3	14.3	13.9	14.3	15.0	15.6	17.7	17.6	16.2	15.5	14.8	14.2	13.6	13.7	13.1	15.0
Thailand	3.3	3.0	3.5	2.3	2.4	3.5	3.0	2.8	3.9	4.3	4.4	4.2	3.8	4.3	4.8	4.2	3.6	4.2	5.5	5.5	6.6	6.3
NIEs	5.6	7.1	7.9	7.4	8.6	9.2	9.9	10.4	10.4	9.8	10.9	11.5	11.2	10.4	9.4	9.3	10.2	10.7	11.0	11.3	12.3	13.1
Japan	7.6	7.1	6.4	8.0	11.4	8.7	10.3	9.5	9.7	9.6	8.1	10.1	10.9	9.2	9.4	9.4	8.6	9.0	8.6	8.5	8.7	8.7
U.S.A.	11.1	11.8	15.4	17.0	14.8	13.9	14.7	15.5	16.0	13.8	12.7	13.2	12.6	18.1	20.0	21.2	23.3	24.3	23.8	23.3	21.3	19.7

constant during 1981-1991. The ASEAN countries, on the other hand, have represented a stable 15-19 percent of demand for Singapore's domestic exports since 1970. Strong regional growth is expected to support export demand in the 1990s.

2.4 Composition of Exports

In 1970, 58.5 percent of Singapore's domestic exports comprised mineral fuels (Table 7.7). By 1980, the proportion of mineral fuels in total domestic exports started to decline, falling to 26.1 percent in 1991. The relative importance of transport equipment and machinery, however, has increased, with its share rising significantly from 10.8 percent in 1970 to 52.2 percent in 1991.

Table 7.7

COMPOSITION OF EXPORTS

	1970		1976		1980		1991	
	US$ Mil.	% Share	US$ Mil.	% Share	US$ Mil.	% Share	US$ Mil.	% Share
Total Domestic Exports	592.1	100.0	3789.2	100.0	12051.7	100.0	38221.3	100.0
Mineral Fuels	256.0	43.2	1470.1	38.8	5423.2	45.0	8213.6	21.5
(incl. Oil Bunkers)	346.4	58.5	1893.5	50.0	6622.5	55.0	9957.1	26.1
Chemicals	14.0	2.4	108.6	2.9	267.6	2.2	2435.9	6.4
Machinery & Equipment of which:	63.9	10.8	1014.1	26.8	3066.8	25.4	19956.8	52.2
Office Machines	NA	NA	55.2	1.5	86.2	0.7	249.8	0.7
Radio & TV Receivers & Parts	NA	NA	215.1	5.7	977.9	8.1	4140.7	10.8
Electronic Components & Parts	NA	NA	384.7	10.2	1120.4	9.3	3871.7	10.1
Data Processing Machines	NA	NA	7.8	0.2	36.9	0.3	8545.1	22.4
Others	167.9	28.3	773.1	20.4	2094.8	17.4	5871.6	15.4

Domestic exports of computers, computer peripherals and telecommunication equipment expanded rapidly during the last two decades.

III. Export Promotion Policies

3.1 Trade and Commerce Policy Environment

Trade policy in Singapore is aimed primarily at maintaining a free, open and stable multilateral trading system. Free trade is believed to lead to long-term economic growth in the country. There is thus no conscious attempt to coordinate trade policies with specific macroeconomic policy objectives.

Other trade policy aims include developing Singapore into an international trading center; identifying new markets while defending existing ones; increasing services exports; and, safeguarding and diversifying import sources.

The trading system is thus kept, as far as possible, free of tariffs and other border measures. Customs and trade documentation procedures are also kept simple to minimize inconvenience to traders.[2]

3.2 Exchange Rate Policy

In Singapore, the exchange rate policy is primarily aimed at maintaining low inflation to ensure sustainable economic growth. Exchange rate manipulation to boost export competitiveness is regarded as counterproductive. Depreciation results in both cheaper exports and dearer imports. As the import content of Singapore's domestic exports exceeds 70 percent, a higher import price would be translated into a higher export price, thus defeating the objective of making exports more price competitive via depreciation of the exchange rate.

3.3 Fiscal Policy

Tax exemption is allowed for companies promoting their products in overseas markets under the double tax deduction schemes.

2. Trade is facilitated by TradeNet, a one-stop electronic data interchange system, introduced in 1989. TradeNet enables companies to submit trade declarations and permit applications at their convenience and to obtain quick administrative clearance.

Under the International Trading Company Scheme, approved export-oriented companies are entitled to a 20-percent concessionary tax rate.

3.4 Export Finance

3.4.1 MAS Rediscounting Scheme

This was introduced in 1975 for export and pre-export bills of exchange. Presently, it is aimed at helping small- and medium-sized enterprises that penetrate external markets.

For pre-export financing, an exporter can, upon receipt of a purchase order or a sales contract, arrange with his bank to have a pre-export bill drawn up in Singapore dollars and discount with the bank to receive funds for financing the production of the goods. His bank can, in turn, obtain refinancing from the MAS by rediscounting the bills.

For export financing, the exporter is able to receive immediate payment as soon as he has shipped goods under the scheme by discounting a usance bills of exchange with his bank, which in turn would rediscount with the MAS.

A maximum commission of 1.5 percent is paid to the negotiating bank. With the current rediscount rate at 3 percent, exporters can obtain financing at a rate not more than 5.5 percent. MAS can readjust the rediscount rate as and when the market conditions change.

3.4.2 The Export Credit Insurance Scheme (ECICS)

ECICS was established at the end of 1975. The major shareholder is the Singapore Government.

ECICS provides insurance to exporters against commercial (financial) and/or non-commercial (non-financial and uncontrollable) risks of non-payment of buyers. Such insurance is aimed at making banks more willing to provide finance to exporters and on better terms.

3.5 Institutional Arrangements

The Trade Development Board (TDB) was set up to promote Singapore's exports of goods and services; to develop new markets; to develop Singapore as an international trading hub; to safeguard and further external trade interests; and, to administer the trading system.

Various export promotion schemes are administered by the TDB. These are aimed not only at boosting the cost competitiveness of export companies but also at enhancing the quality of their products and upgrading the skills of their employees.

To help defray the initial costs of companies' export development activities, the Market Development Assistance Scheme offers grants to overseas market-sourcing trips and participation in overseas trade fairs and missions.

To enhance the quality of locally manufactured exports, the Design Center was set up by the TDB to heighten design awareness in Singapore and to develop creative talent. The center implements design promotion and development policies of the Singapore Design Council. The Design Ventures Program was launched in 1987 to encourage local manufacturers to invest in product design and packaging. Grants of up to 75 percent of eligible costs of design projects are offered, subject to a ceiling of $100,000.

Other schemes administered by the TDB include the Certification Assistance Scheme which helps local companies to obtain required international certification and the Approved International Fair (AIF) Scheme.

The AIF scheme supports local trade show organizers. Its endorsement helps to attract participation of exhibitors and trade visitors to local trade shows, thus promoting international and regional trade. Features of the scheme include overseas market development for the organizer, double tax deduction for local exhibitors and full promotional support from TDB and publicity in TDB's GlobaLink System.

To train and develop Singapore's export marketing and international trading expertise, the TDB set up the Export Institute of Singapore which offers a Diploma in Export Marketing.

3.6 Export Information System

TDB-GlobaLink offers a customized on-line information service. It provides a comprehensive and extensive range of information on international business and trade, Singapore and international tenders, banking and finance, transport schedules, property and legislation.

3.7 Schemes of Trade Preferences

Singapore firmly supports the multilateral trading system and will participate in schemes of trade preferences if they are not intended to be protectionist trade blocs and if they conform to the GATT.

The ASEAN Preferential Trading Arrangements (APTA), established in 1967, is in line with Singapore's objectives for liberalization and stabilization of regional trade. Singapore participates in the APTA, the Generalized System of Preferences and the Global System of Trade Preferences.

IV. Problems and Issues on Export Promotion

4.1 Persistent Trade Deficit

Singapore's trade balance is characterized by a persistent trade deficit. This reflects its small and open economy. A large proportion of its consumption goods, raw materials and capital goods need to be imported. However, on a trend basis, the trade deficit as a percentage of GDP has been declining (Table 7.5). To ensure that such a trend continues, Singapore should concentrate on raising the value-added of domestic exports.

4.2 Labor Shortage

Singapore's export potential is limited by the shortage of labor. There is thus a need to specialize in the production of skill- and capital-intensive exports, shifting away from highly labor-intensive industries. To enlarge the pool of indigenous skilled labor and professionals, more resources should be devoted to the training and education of the workforce.

4.3 Dependence on Performance of External Economies

Singapore's export performance is largely affected by the production patterns and markets of MNCs (U.S., EC and Japan), which account for two-thirds of domestic exports. In 1991, U.S., Japan and Germany alone accounted for more than one-third of Singapore's domestic exports. Singapore's trade is thus highly vulnerable to economic downturns and protectionism in the major developed countries, its main export markets.

4.4 Trade Actions

Protectionist measures have been taken against Singapore by Australia, the U.S. and the EC. The main ones include quantitative restrictions, anti-dumping and countervailing duty actions. Singapore is also concerned with the indiscriminate use of other trade measures. Examples include the arbitrary interpretation of product-specific rules of origin or technical standards and the use of environmental protection as a pretext for trade barriers.

V. Policy Recommendations

Trade policies should continue to be directed at promoting Singapore as an international trading and transportation hub. There should be a sustained upgrading of Singapore's trading infrastructure in order to attain world-class standards.

In view of emerging trade blocs amongst Singapore's major markets, there should be more measures aimed at encouraging Singapore companies to product-diversification as well as to expand to the emerging markets such as China, India, Eastern Europe and Latin America. Local companies should also be encouraged to regionalize and then to globalize their operations.

EQUATION 1: CONTRIBUTION OF NODX TO GDP GROWTH

TDX_NOIL
Ordinary Least Squares
QUARTERLY data for 51 periods from 1980Q1 to 1992Q3
Date: 24 DEC 1992

log(ngdp85)

= 0.42767 * log(tdx_noil) + 5.55078 - 0.00454 * SEASON_2
(27.5406) (41.2738) (0.19059)

+ 0.00487 * SEASON_3 + 0.01115 * SEASON_4
(0.20370) (0.45806)

Sum Sq.	0.1690	Std. Err.	0.0606	LHS Mean	9.2719
R Sq.	0.9437	R Bar Sq.	0.9388	F 4, 46	192.583
D.W. (1)	0.1790	D.W. (4)	0.6159		

EQUATION 2: CONTRIBUTION OF NODX TO IMPORT GROWTH

|TM equation tm log(tm) = log(tdx_noil);
Ordinary Least Squares
ANNUAL data for 12 periods from 1980 to 1991
Date: 24 DEC 1992

log(tm)

= 0.48185 * log(tdx_noil) + 6.34389
(8.53713) (11.2172)

Sum Sq.	0.1071	Std. Err.	0.1035	LHS Mean	11.1653
R Sq.	0.8793	R Bar Sq.	0.8673	F 1, 10	72.8826
D.W. (1)	0.5948	D.W. (2)	1.5229		

EQUATION 3: CONTRIBUTION OF NODX TO GROWTH OF EMPLOYMENT IN MANUFACTURING SECTOR

|LE_M equation le_m log(le_m) = log(tdx_noil);
Ordinary Least Squares
ANNUAL data for 12 periods from 1980 to 1991
Date: 24 DEC 1992

log(le_m)

= 0.16562 * log(tdx_noil) + 4.17133
(3.44285) (8.65403)

Sum Sq.	0.0778	Std. Err.	0.0882	LHS Mean	5.8285
R Sq.	0.5424	R Bar Sq.	0.4966	F 1, 10	11.8532
D.W. (1)	0.4531	D.W. (2)	1.2536		

EQUATIONS USED IN GRANGER CAUSALITY TESTS

GDP
Restricted Ordinary Least Squares
QUARTERLY data for 53 periods from 1980Q1 to 1993Q1
Date: 31 MAY 1993

dlogya(ngdp85)

= 0.36654 * dlogya(ngdp85) [-3] + 0.24436 * dlogya(ngdp85) [-2]
(8.13441) (8.13441)
+ 0.12218 * dlogya(ngdp85) [-3] + 0.02684 * dlogya(tdx85_noil)
(8.13441) (2.81008)
+ 0.02147 * dlogya(tdx85_noil) [-1]
(2.81008)
+ 0.01610 * dlogya(tdx85_noil) [-2]
(2.81008)
+ 0.01074 * dlogya(tdx85_noil) [-3]
(2.81008)
+ 0.00537 * dlogya(tdx85_noil) [-4] + 0.00652
(2.81008) (1.03112)

Polynomial Lags:

dlogya(ngdp85)
from 1 to 3 degree 1 far

dlogya(tdx85-noil)
from 0 to 4 degree 1 far

Sum Sq	0.0203	Std Err	0.0202	LHS Mean	0.0690
R Sq	0.7076	R Bar Sq	0.6959	F 2, 50	60.5019
D.W.(1)	0.6248	D.W.(4)	2.2194		

TDX
Restricted Ordinary Least Squares
QUARTERLY data for 54 periods from 1979Q4 to 1993Q1
Date: 31 MAY 1993

dlogya(tdx85_noil)

= 0.41741 * dlogya(tdx85_noil) [-1]
(6.75722)
+ 0.27827 * dlogya(tdx85_noil) [-2]
(6.75722)
+ 0.13914 * dlogya(tdx85_noil) [-3] - 0.17604 * dlogya(ngdp85)
(6.75722) (1.15929)
- 0.14084 * dlogya(ngdp85) [-1] + 0.10563 * dlogya(ngdp85) [-2]
(1.15929) (1.15929)
- 0.07042 * dlogya(ngdp85) [-3] + 0.03521 * dlogya(ngdp85) [-4]
(1.15929) (1.15929)
+ 0.05814
(1.95432)

Polynomial Lags:

dlogya(tdx85-noil)
from 1 to 3 degree 1 far

dlogya(ngdp85)
from 0 to 4 degree 1 far

Sum Sq	0.4310	Std Err	0.0919	LHS Mean	0.1421
R Sq	0.5138	R Bar Sq	0.4948	F 2, 50	26.9525
D.W.(1)	1.0092	D.W.(4)	2.6204		

SINGAPORE: EXPORTS BY LEVEL TERMS

Period	Merchandise Exports	Services Exports	Domestic Exports	Non-Oil Domestic Exports	Re-Exports
1970	1431.2	550.7	501.7	245.7	944.9
1971	1676.8	605.8	706.2	356.6	990.5
1972	2042.9	1204.2	981.5	591.7	1085.2
1973	3445.1	1727.2	1642.1	1220.7	1839.3
1974	5547.2	2514.7	3103.6	1641.6	2355.9
1975	5110.1	3166.3	2825.5	1462.1	2200.3
1976	6217.8	3169.3	3365.8	1895.7	2794.0
1977	7745.3	3485.7	4295.0	2369.4	3459.3
1978	9586.4	4191.5	5300.3	3002.6	4291.6
1979	13400.4	5248.4	7554.2	4236.4	5858.5
1980	18199.8	7038.6	10852.3	5429.1	7307.7
1981	19661.8	9704.7	12545.0	5999.0	7023.6
1982	19434.6	10951.7	12076.0	5605.8	7156.5
1983	20424.4	10597.4	12379.9	6611.1	8019.0
1984	22662.5	9184.3	14090.8	8113.9	8573.8
1985	21534.1	8197.2	13507.6	7606.8	8001.2
1986	21336.2	8439.0	13708.2	9222.9	7772.0
1987	27463.9	10347.7	17388.2	12971.2	10064.2
1988	37993.0	13162.0	23528.5	18989.1	14656.9
1989	43239.6	16225.0	27147.9	21549.9	16338.7
1990	50683.4	21677.4	33085.7	25167.8	17904.1
1991	56819.1	24208.7	36478.9	28265.0	20751.0

Appendix 7.4

SINGAPORE: RE-EXPORTS BY SELECTED COUNTRIES
(US$ Million)

Country	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
EEC	197.7	184.7	208.2	382.6	358.1	282.2	446.5	558.6	607.5	899.9	936.0	753.2	593.0	705.0	813.7	881.3	924.5	1173.4	1615.4	1830.3	2105.1	2174.7
ASEAN	229.4	369.1	402.2	558.2	735.8	808.7	898.9	1079.9	1345.1	1868.8	2351.0	2437.5	2583.4	2827.0	2886.8	2410.4	2406.8	3229.9	4679.5	5236.4	5588.0	6667.1
of which:																						
Malaysia	265.6	314.5	347.1	482.7	641.5	639.2	716.5	861.9	1010.0	1408.3	980.5	1889.0	1981.5	2136.7	2246.0	1824.2	1827.2	2446.6	3346.7	3792.3	3963.1	4872.2
Thailand	15.3	22.5	28.8	30.8	35.9	74.6	91.1	100.1	192.5	233.7	234.3	223.0	258.6	338.2	343.2	303.8	271.2	377.1	774.2	783.8	953.0	1107.0
NIEs	43.4	50.4	56.7	108.8	159.1	150.5	226.5	278.1	365.7	488.0	551.6	564.7	701.4	705.1	706.7	785.9	822.9	1086.2	1660.9	1770.7	2096.5	2813.4
Japan	46.9	31.2	32.5	98.5	87.7	82.5	115.1	114.3	150.0	186.6	215.3	245.8	276.1	350.4	394.7	391.8	414.2	617.4	969.9	968.3	1153.5	1621.8
USA	104.4	103.0	104.6	169.1	272.7	252.3	311.7	403.6	514.9	570.1	643.5	687.1	652.8	1114.2	1111.7	1118.0	891.7	1155.9	1594.9	1925.9	1971.1	2111.5

SINGAPORE: RE-EXPORTS BY SELECTED COUNTRIES
(Percent Share of Total)

Country	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
EEC	20.9	18.6	19.2	20.8	15.2	12.8	16.0	16.1	14.2	15.4	12.8	10.7	8.3	8.8	9.5	11.0	11.9	11.7	11.0	11.2	11.8	10.5
ASEAN	31.7	37.3	37.1	30.3	31.2	36.8	32.2	31.2	31.3	31.9	32.2	34.7	36.1	35.3	33.7	30.1	31.0	32.1	31.9	32.0	31.2	32.1
of which:																						
Malaysia	28.1	31.8	32.0	26.2	27.2	29.1	35.6	24.9	23.5	24.0	25.3	26.9	27.7	26.6	26.2	22.8	23.5	24.3	22.8	23.2	22.1	23.5
Thailand	1.6	2.3	2.7	1.7	1.5	3.4	3.3	2.9	4.3	4.0	3.2	3.2	3.6	4.2	4.0	3.8	3.5	3.7	5.3	4.8	5.3	5.3
NIEs	4.6	5.1	5.2	5.9	6.8	6.8	8.1	8.0	8.5	8.3	7.5	8.0	9.8	8.8	8.2	9.8	10.6	10.8	11.3	10.8	11.7	13.6
Japan	5.0	3.1	3.0	5.4	3.7	3.8	4.1	3.3	3.5	3.2	2.9	3.5	3.9	4.4	4.6	4.9	5.3	6.1	6.6	5.9	6.4	7.8
USA	11.1	10.4	9.6	9.2	11.6	11.5	11.2	11.7	12.0	9.7	8.8	9.8	9.1	13.9	13.0	14.0	11.5	11.5	10.9	11.8	11.0	10.2

SINGAPORE: ANNUAL GROWTH OF RE-EXPORTS BY SELECTED COUNTRIES
(Percent)

Country	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
EEC	-8.6	4.7	59.9	-6.7	-23.3	64.9	23.5	1.4	41.7	2.4	-20.6	-20.3	17.4	16.5	11.7	3.8	22.8	31.5	9.8	6.9	-1.5
ASEAN	20.6	1.1	20.7	31.4	7.0	15.8	18.6	16.1	32.9	23.9	2.3	7.4	8.1	3.1	-13.9	-1.2	29.8	38.4	8.4	-0.8	13.7
of which:																					
Malaysia	15.8	2.4	21.0	32.5	-3.0	16.8	18.8	9.2	33.3	29.4	0.7	6.3	6.5	6.1	-16.2	-0.9	29.5	30.7	9.8	-2.9	17.2
Thailand	44.0	18.9	-7.0	16.3	101.8	27.4	8.5	69.9	22.4	-1.3	-6.1	17.4	29.2	2.4	-8.7	-11.6	34.5	96.2	-1.9	13.0	10.7
NIEs	13.6	4.5	66.8	45.8	-7.9	56.8	21.2	22.6	27.6	11.3	1.0	25.8	-0.7	1.2	14.7	3.6	27.7	46.1	3.3	10.0	27.9
Japan	-34.9	-3.3	163.6	-11.2	-8.5	45.3	-1.9	22.3	18.9	13.6	12.6	13.8	25.3	13.7	2.4	4.6	44.2	50.1	-3.2	10.7	34.0
USA	-3.5	-5.7	40.7	60.8	-10.0	28.8	27.8	18.9	5.9	11.1	5.4	-3.8	68.6	0.7	3.7	-21.1	25.4	31.8	17.0	-4.9	2.1

SINGAPORE: DOMESTIC EXPORTS BY SELECTED COUNTRIES
(US$ Million)

Country	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
EEC	69.6	78.3	141.5	306.1	438.2	495.6	574.3	681.8	724.2	1153.9	1547.7	1546.8	1413.9	1381.8	1622.1	1544.4	1594.4	2329.2	3494.4	4156.8	5452.6	6007.5
ASEAN	116.7	141.8	180.0	258.1	478.9	477.1	450.5	566.7	757.5	1221.1	1948.1	2312.2	2569.9	2733.2	2668.8	2587.6	2303.0	2799.6	3723.4	4463.8	5971.3	7091.4
of which:																						
Malaysia	70.4	91.4	107.7	177.2	321.8	283.6	287.6	316.3	394.3	627.7	1052.8	1380.1	1690.8	1705.8	1656.4	1715.1	1500.0	1617.8	1980.7	2317.1	2904.9	3947.2
Thailand	35.4	30.2	47.5	51.4	104.9	113.3	105.6	130.3	210.6	373.5	610.7	659.5	539.5	605.5	809.2	647.3	549.8	835.4	1368.1	1680.3	2528.5	2598.0
NIEs	42.6	74.9	115.9	162.5	339.9	345.0	427.5	574.5	680.8	909.7	1559.3	1853.8	1632.7	1558.5	1552.9	1337.7	1465.6	1947.9	2677.4	3260.6	4367.3	4929.0
Japan	70.0	94.3	107.2	193.4	573.2	386.8	560.3	672.0	828.8	1178.1	1343.8	1878.4	1987.4	1657.8	1858.7	1754.6	1516.7	1970.2	2422.9	2850.5	3426.6	3493.2
USA	66.0	106.8	233.3	451.0	589.4	496.4	657.0	875.7	1105.4	1391.6	1818.6	2081.2	1960.8	2847.7	3713.1	3708.7	4360.5	5812.0	7760.0	8478.2	9198.6	9525.2

Appendix 7.8

SINGAPORE: ANNUAL GROWTH OF DOMESTIC EXPORTS BY SELECTED COUNTRIES
(Percent)

Country	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
EEC	37.4	10.0	67.8	88.2	42.8	10.0	20.7	17.2	1.5	48.6	32.1	-1.4	-7.4	-3.5	18.5	-1.8	2.2	41.3	43.4	15.3	21.9	5.0
ASEAN	-7.0	18.8	17.8	24.7	85.0	-3.0	-1.6	24.2	24.6	54.1	57.1	17.1	12.6	5.0	-1.5	0.0	-11.9	17.6	27.1	16.2	24.3	13.2
of which:																						
Malaysia	0.1	27.0	9.4	43.2	81.0	-14.2	5.7	8.6	16.2	52.2	65.2	29.3	24.1	-0.4	-2.0	6.8	-13.4	4.3	17.0	13.4	16.5	29.5
Thailand	-22.2	-16.4	45.8	-5.8	103.3	5.1	-2.9	21.9	50.7	69.6	61.0	6.6	-17.1	10.8	34.9	-17.5	-15.9	47.0	56.5	19.0	39.9	-2.1
NIEs	38.8	71.9	43.6	21.9	108.6	-1.2	29.1	32.7	10.5	27.8	68.8	17.3	-10.8	-5.7	0.6	-11.2	8.4	30.3	29.5	18.0	24.5	7.6
Japan	18.2	31.8	5.5	57.0	195.5	-34.3	50.9	18.4	15.0	35.9	12.3	37.9	7.2	-17.6	13.2	-2.6	-14.4	25.6	17.5	14.0	11.7	-2.8
USA	96.3	58.2	102.8	68.2	30.3	-18.0	37.9	31.6	17.7	20.4	28.7	12.9	-4.6	43.4	31.6	3.0	16.4	28.9	27.6	5.9	0.8	-1.3

SINGAPORE: NON-OIL DOMESTIC EXPORTS BY SELECTED COUNTRIES
(US$ Million)

Country	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
EEC	353.8	421.2	514.4	586.0	858.5	1102.6	1131.2	1038.8	1101.1	1311.4	1142.5	1347.4	2084.1	3296.9	3922.2	5168.2	5648.7
ASEAN	177.1	180.7	214.4	302.2	494.4	651.1	678.3	676.4	794.5	964.7	895.4	982.7	1400.7	2162.8	2580.2	3157.7	4091.8
of which:																	
Malaysia	114.1	131.1	147.3	191.6	301.1	380.5	410.4	426.7	534.6	674.1	609.6	637.1	898.3	1288.2	1512.1	1806.9	2599.9
Thailand	11.3	12.6	18.7	31.1	90.9	126.3	122.2	93.4	124.5	150.4	152.4	190.6	289.9	615.1	751.2	960.2	1113.1
NIEs	74.0	96.5	118.8	208.1	276.1	351.1	431.3	450.8	474.9	529.5	493.9	667.7	1112.2	1809.2	2036.1	2463.4	2953.5
Japan	88.0	121.2	136.8	175.1	230.4	258.3	285.0	310.0	300.4	394.2	411.1	491.9	700.7	1102.7	1483.0	1648.7	2045.0
USA	392.0	563.1	710.1	959.5	1235.6	1616.3	1883.1	1790.8	2630.0	3346.4	3174.5	4081.4	5543.2	7556.9	8256.6	8990.2	9350.7

Appendix 7.10

SINGAPORE: ANNUAL GROWTH OF NON-OIL DOMESTIC EXPORTS BY SELECTED COUNTRIES
(Percent)

Country	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
EEC	24.1	20.6	6.2	40.1	26.5	1.2	-7.0	4.7	20.2	-10.1	16.7	49.6	51.2	15.3	22.5	4.2
ASEAN	6.3	17.1	31.4	56.5	29.7	2.8	1.0	16.0	22.5	-4.3	8.6	37.9	47.5	15.6	13.7	23.5
of which:																
Malaysia	19.7	11.0	21.3	50.2	24.4	6.4	5.3	23.7	27.2	-6.7	3.4	36.4	37.0	13.8	11.1	37.1
Thailand	16.1	46.2	55.2	170.5	36.9	-4.6	-22.5	31.6	21.9	4.5	23.8	47.1	102.7	18.4	18.8	10.5
NIEs	35.8	21.6	63.3	26.8	25.2	21.2	5.9	4.0	12.5	-3.8	33.8	61.1	55.4	9.1	12.4	14.3
Japan	43.6	11.4	19.3	25.8	10.4	8.9	10.2	-4.3	32.4	7.6	18.4	37.8	50.4	30.3	3.3	18.2
USA	49.7	24.5	26.0	23.1	28.8	15.0	-3.7	45.0	28.4	-2.2	27.2	31.4	30.3	5.9	1.2	-0.9

SINGAPORE: NON-OIL DOMESTIC EXPORTS BY SELECTED COUNTRIES
(Percent Share)

Country	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
EEC	24.2	22.2	21.7	19.5	20.3	20.3	18.9	18.5	16.7	16.2	15.0	14.6	16.1	17.4	18.2	20.5	20.0
ASEAN	12.1	9.5	9.0	10.1	11.7	12.0	11.3	12.1	12.0	11.9	11.8	10.7	10.8	11.4	12.0	12.5	14.5
of which:																	
Malaysia	7.8	6.9	6.2	6.4	7.1	7.0	6.8	7.6	8.1	8.3	8.0	6.9	6.9	6.8	7.0	7.2	9.2
Thailand	0.8	0.7	0.8	1.0	2.1	2.3	2.0	1.7	1.9	1.9	2.0	2.1	2.2	3.2	3.5	3.8	3.9
NIEs	5.1	5.1	5.0	6.9	6.5	6.5	7.2	8.0	7.2	6.5	6.5	7.2	8.6	9.5	9.4	9.8	10.4
Japan	6.0	6.4	5.8	5.8	5.4	4.8	4.8	5.5	4.5	4.9	5.4	5.3	5.4	5.8	6.9	6.6	7.2
USA	26.8	29.7	30.0	32.0	29.2	29.8	31.4	31.9	39.8	41.2	41.7	44.3	42.7	39.8	38.3	35.7	33.1

DOMESTIC EXPORTS TO OTHER COUNTRIES BY COMMODITY SECTION (US$ Million)

Period	Food & Live Animals	Beverages & Tobacco	Crude Materials	Mineral Fuel	Animal & Veg. Oils & Fats	Chemicals	Manufactured Goods	Mach.& Transp. Equip.	Manufactured Articles	Others	Dom. Exports	Non-Oil Dom. Exports	Bunkers
1969	29.0	4.0	11.4	365.9	9.5	14.2	45.7	26.5	35.4	2.6	544.1	178.2	73.5
1970	34.1	3.8	9.7	346.4	15.8	14.0	54.9	63.9	46.7	2.9	592.1	245.7	90.4
1971	37.9	3.1	8.0	427.6	24.1	20.1	69.6	118.1	71.6	4.0	784.2	356.6	77.9
1972	43.8	3.7	10.6	512.1	11.9	24.4	94.8	263.2	133.0	6.3	1103.9	591.7	122.4
1973	69.0	5.3	17.4	684.9	16.7	75.3	179.1	525.7	233.9	8.5	1805.6	1120.7	163.5
1974	103.7	7.4	18.8	1811.0	27.4	239.4	189.8	790.2	255.1	9.8	3452.6	1641.6	349.1
1975	117.3	10.9	18.9	1717.8	23.7	87.8	205.0	711.2	281.8	5.4	3179.9	1462.1	354.4
1976	82.9	12.0	25.2	1893.4	25.3	108.6	254.0	1014.1	366.2	7.4	3789.2	1895.7	423.4
1977	121.6	17.9	30.3	2407.1	53.1	133.4	315.6	1262.2	424.4	11.0	4776.5	2369.4	481.5
1978	151.2	32.7	37.5	2813.7	75.1	171.0	450.5	1531.0	544.9	8.7	5816.2	3002.6	515.9
1979	207.0	40.5	59.4	4133.3	105.7	210.6	550.8	2330.6	720.7	11.2	8369.7	4236.4	815.5
1980	280.5	47.9	71.1	6622.5	183.9	267.6	617.7	3066.8	881.0	12.6	12051.6	5429.1	1199.3
1981	254.0	55.0	66.3	7941.5	222.6	288.6	627.9	3468.0	1000.9	15.7	13940.5	5999.0	1395.5
1982	210.0	62.7	58.6	8019.2	225.5	322.8	567.5	3252.8	891.2	14.9	13625.0	5605.8	1548.9
1983	221.9	54.3	85.0	7207.6	190.2	411.5	512.5	4125.1	992.4	18.2	13818.7	6611.1	1438.8
1984	226.9	48.0	80.8	7380.7	314.1	625.3	554.9	5127.1	1066.6	70.2	15494.6	8113.9	1403.8
1985	217.3	47.0	86.2	7199.9	286.3	726.3	552.4	4607.2	1009.4	74.8	14806.7	7606.8	1299.1
1986	276.7	55.8	113.3	5502.1	306.1	820.0	524.6	5784.8	1230.8	110.7	14725.1	9222.9	1016.9
1987	347.2	84.2	163.3	5581.0	287.4	1120.9	630.6	8460.3	1751.4	125.9	18552.2	12971.2	1164.0
1988	449.5	123.7	232.9	5635.6	303.5	1540.5	883.3	12991.4	2321.0	143.4	24624.7	18989.1	1096.1
1989	530.5	164.0	264.7	6780.6	394.1	1724.7	947.9	14974.5	2416.5	132.9	28330.5	21549.9	1182.6
1990	528.6	213.0	253.9	9454.5	323.9	1996.4	1173.4	17848.9	2684.9	144.8	34622.3	25167.8	1536.7
1991	651.1	230.2	259.8	9957.3	321.8	2436.0	1300.6	19957.3	2950.0	158.2	38222.4	28265.0	1743.4

DOMESTIC EXPORTS TO OTHER COUNTRIES BY COMMODITY SECTION (Annual Growth Rates %)

Period	Food & Live Animals	Beverages & Tobacco	Crude Materials	Mineral Fuel	Animal & Veg. Oils & Fats	Chemicals	Manufactured Goods	Mach.& Transp. Equip.	Manufactured Articles	Others	Dom. Exports	Non-Oil Dom. Exports	Bunkers
1970	17.9	-3.3	-14.8	-4.9	66.6	-0.7	20.8	142.2	32.4	15.2	9.4	38.5	23.6
1971	8.9	-19.5	-19.1	20.7	49.4	40.6	24.0	80.8	50.0	33.0	29.5	41.9	-15.7
1972	7.1	10.5	23.1	11.2	-54.2	12.6	26.4	107.0	72.3	45.5	30.7	54.0	45.7
1973	37.0	22.9	42.3	16.3	21.9	168.1	64.3	73.7	46.5	18.2	42.3	64.7	16.2
1974	50.0	39.5	8.3	163.7	64.1	217.2	5.7	49.9	13.6	14.9	90.7	46.1	112.9
1975	10.0	43.3	-2.2	-7.7	-16.0	-64.3	5.1	-12.4	7.5	-46.0	-10.4	-13.3	-1.2
1976	-26.3	15.1	38.7	14.9	11.6	28.9	29.1	48.6	35.4	42.4	24.2	35.1	24.5
1977	44.7	46.9	18.6	25.5	106.6	21.3	22.7	22.9	14.4	45.7	24.5	23.4	12.3
1978	16.0	70.4	15.5	9.0	31.9	19.4	33.1	13.1	19.7	-26.3	13.5	18.1	-0.1
1979	30.9	18.3	51.5	40.5	34.6	17.8	16.9	45.6	26.5	23.4	37.6	34.9	51.1
1980	33.4	16.6	17.8	57.8	71.3	25.1	10.4	29.6	20.4	11.2	41.8	26.2	44.8
1981	-10.6	13.3	-8.0	18.3	19.4	6.4	0.3	11.6	12.1	22.8	14.1	9.0	14.8
1982	-16.3	15.3	-10.5	2.3	2.6	13.3	-8.5	-5.0	-9.8	-4.4	-1.0	-5.3	12.4
1983	4.4	-14.5	43.3	-11.2	-16.7	25.9	-10.8	25.2	10.0	21.3	0.2	16.5	-8.3
1984	3.2	-10.7	-4.0	3.3	66.7	53.4	9.3	25.4	8.5	288.5	13.2	23.9	-1.5
1985	-1.2	0.9	10.1	0.6	-6.0	19.8	2.7	-7.3	-2.4	9.9	-1.4	-3.3	-4.6
1986	26.0	17.7	30.0	-24.4	5.8	11.7	-6.0	24.3	20.7	46.6	-1.6	20.0	-22.5
1987	21.4	45.8	39.4	-1.9	-9.2	32.2	16.3	41.5	37.6	10.0	21.9	36.0	10.7
1988	23.7	40.4	36.3	-3.5	0.9	31.3	33.8	46.7	26.6	8.8	26.8	39.9	-10.0
1989	14.4	28.5	10.2	16.6	25.8	8.5	4.0	11.7	0.9	-10.1	11.5	10.0	4.6
1990	-7.4	20.7	-10.9	29.6	-23.6	7.6	15.0	10.8	3.3	1.2	13.6	8.5	20.8
1991	17.4	3.0	-2.5	0.4	-5.3	16.3	5.6	6.6	4.7	4.1	5.2	7.0	8.1

RE-EXPORTS TO OTHER COUNTRIES BY COMMODITY SECTION (US$ Million)

Period	Food & Live Animals	Beverages & Tobacco	Crude Materials	Mineral Fuel	Animal & Veg. Oils & Fats	Chemicals	Manufactured Goods	Mach.& Transp. Equip.	Manufactured Articles	Others	Total Exports	Non-Oil Exports
1969	141.6	19.7	526.0	9.9	17.9	30.9	89.8	87.0	33.5	39.1	995.5	985.6
1970	143.6	19.3	452.6	9.8	29.5	27.7	81.8	104.5	33.4	42.6	944.9	935.0
1971	141.1	19.7	385.3	28.9	44.7	40.9	107.0	126.6	41.8	54.5	990.5	961.6
1972	153.5	19.8	392.5	26.1	41.8	53.5	117.2	171.3	44.0	65.6	1085.2	1059.1
1973	183.6	10.0	863.5	38.4	53.5	85.8	197.5	279.5	60.9	66.6	1839.3	1800.9
1974	230.3	8.5	1009.6	53.5	119.5	136.9	249.3	407.5	76.3	64.5	2355.9	2302.4
1975	268.9	6.4	695.6	92.0	79.9	112.8	253.2	509.5	89.4	92.7	2200.3	2108.3
1976	300.7	7.8	1053.2	61.4	75.6	138.1	283.8	663.8	116.8	92.8	2794.0	2732.5
1977	448.0	8.8	1265.1	72.6	141.5	160.1	341.2	769.9	134.0	118.0	3459.3	3386.7
1978	503.1	11.2	1494.2	46.0	150.8	211.5	543.1	1009.9	186.0	135.8	4291.6	4245.6
1979	563.0	20.1	1969.9	91.8	288.9	306.4	756.0	1448.0	255.0	159.4	5858.5	5766.7
1980	657.4	25.5	2123.9	165.1	327.8	394.9	989.6	2112.3	320.3	190.8	7307.7	7142.6
1981	751.7	27.5	1668.6	163.8	165.5	448.1	1109.1	2107.6	380.9	201.0	7023.6	6859.9
1982	905.9	38.7	1241.0	359.9	139.1	482.1	1226.3	2142.6	432.0	189.0	7156.5	6796.6
1983	736.2	45.1	1518.3	367.5	107.0	514.1	1230.1	2819.5	466.6	214.4	8019.0	7651.4
1984	1130.6	50.3	1518.0	204.2	408.1	529.7	1144.3	2779.2	531.2	278.2	8573.8	8369.6
1985	779.6	62.4	1140.9	278.1	411.5	508.8	1082.9	2923.2	526.1	287.7	8001.2	7723.0
1986	929.1	96.6	1015.9	174.9	98.1	484.3	1143.7	2895.4	625.6	308.2	7772.0	7597.1
1987	942.9	99.6	1262.7	211.1	90.5	665.3	1517.0	4015.5	886.9	372.7	10064.2	9853.1
1988	1182.9	151.0	1778.0	502.8	136.5	1042.9	2361.0	5860.8	1212.4	428.6	14656.9	14154.1
1989	1026.7	290.5	1643.5	112.3	126.9	1216.8	2684.2	7146.7	1590.8	500.3	16338.7	16226.4
1990	979.9	552.7	1354.2	87.5	95.8	1297.3	2496.2	8485.8	2004.5	550.2	17904.1	17816.5
1991	1104.4	835.3	1199.8	97.9	96.2	1430.9	2936.9	9967.5	2392.2	690.0	20751.0	20653.1

RE-EXPORTS TO OTHER COUNTRIES BY COMMODITY SECTION (Annual Growth Rates %)

Period	Food & Live Animals	Beverages & Tobacco	Crude Materials	Mineral Fuel	Animal & Veg. Oils & Fats	Chemicals	Manufactured Goods	Mach.& Transp. Equip.	Manufactured Articles	Others	Total Exports	Non-Oil Exports
1970	1.9	-1.6	-13.5	0.0	65.9	-9.9	-8.4	20.6	0.3	9.5	-4.6	-4.7
1971	-3.9	-0.5	-16.7	187.8	47.9	44.5	28.0	18.5	22.4	25.2	2.5	0.6
1972	1.0	-6.7	-5.4	-16.3	-13.2	21.5	1.6	25.5	-2.3	11.6	1.7	2.2
1973	4.1	-55.9	91.3	28.1	11.5	39.5	46.6	42.0	20.2	-11.7	47.4	47.9
1974	25.1	-15.9	16.6	39.0	122.6	59.1	25.9	45.4	25.0	-3.4	27.7	27.5
1975	13.6	-26.7	-33.0	67.3	-35.0	-19.8	-1.2	21.6	14.1	39.9	-9.1	-10.9
1976	16.5	27.4	57.8	-30.4	-1.4	27.5	16.8	35.8	36.1	4.2	32.3	35.0
1977	47.1	11.9	18.6	16.6	84.9	14.4	18.7	14.5	13.2	25.6	22.2	22.4
1978	4.7	18.6	10.1	-40.9	-0.7	23.2	48.4	22.3	29.4	7.2	15.7	16.9
1979	8.0	70.9	26.1	90.9	83.3	38.5	33.1	37.1	31.1	12.3	30.5	29.9
1980	15.0	25.1	6.2	77.0	11.7	26.9	28.9	43.6	23.7	17.9	22.8	22.0
1981	12.8	6.4	-22.5	-2.1	-50.2	11.9	10.6	-1.6	17.3	3.9	-5.2	-5.2
1982	22.1	42.7	-24.7	122.5	-14.9	9.0	12.0	3.0	14.9	-4.7	3.2	0.4
1983	-19.7	15.0	20.8	0.9	-24.0	5.3	-0.9	30.0	6.7	12.0	10.7	11.2
1984	55.0	12.5	0.9	-43.9	284.8	4.0	-6.1	-0.5	14.9	31.0	7.9	10.4
1985	-28.9	27.9	-22.5	40.5	4.0	-0.9	-2.4	8.5	2.2	6.6	-3.7	-4.8
1986	18.0	53.4	-11.9	-37.8	-76.4	-5.8	4.5	-2.0	17.7	6.0	-3.9	-2.6
1987	-1.8	-0.3	20.2	16.7	-10.8	32.9	28.3	34.1	37.1	17.0	25.2	25.4
1988	19.9	44.8	34.6	127.6	44.1	49.8	48.7	39.5	30.6	9.9	39.2	37.3
1989	-15.9	86.5	-10.4	-78.4	-9.8	13.1	10.2	18.2	27.2	13.1	8.0	11.1
1990	-11.3	76.8	-23.4	-27.6	-29.8	-0.9	-13.6	10.4	17.1	2.2	1.8	2.0
1991	7.4	44.1	-15.6	6.6	-4.3	5.1	12.1	12.0	13.7	19.5	10.5	10.5

RE-EXPORTS TO OTHER COUNTRIES BY COMMODITY SECTION
(Percent Share)

Period	Food & Live Animals	Beverages & Tobacco	Crude Materials	Mineral Fuel	Animal & Veg. Oils & Fats	Chemicals	Manufactured Goods	Mach. & Transp. Equip.	Manufactured Articles	Others	Total Exports
1970	15.2	2.0	47.9	1.0	3.1	2.9	8.7	11.1	3.5	4.5	100.0
1971	14.2	2.0	38.9	2.9	4.5	4.1	10.8	12.8	4.2	5.5	100.0
1972	14.1	1.8	36.2	2.4	3.8	4.9	10.8	15.8	4.1	6.0	100.0
1973	10.0	0.5	46.9	2.1	2.9	4.7	10.7	15.2	3.3	3.6	100.0
1974	9.8	0.4	42.9	2.3	5.1	5.8	10.6	17.3	3.2	2.7	100.0
1975	12.2	0.3	31.6	4.2	3.6	5.1	11.5	23.2	4.1	4.2	100.0
1976	10.8	0.3	37.7	2.2	2.7	4.9	10.2	23.8	4.2	3.3	100.0
1977	13.0	0.3	36.6	2.1	4.1	4.6	9.9	22.3	3.9	3.4	100.0
1978	11.7	0.3	34.8	1.1	3.5	4.9	12.7	23.5	4.3	3.2	100.0
1979	9.6	0.3	33.6	1.6	4.9	5.2	12.9	24.7	4.4	2.7	100.0
1980	9.0	0.3	29.1	2.3	4.5	5.4	13.5	28.9	4.4	2.6	100.0
1981	10.7	0.4	23.8	2.3	2.4	6.4	15.8	30.0	5.4	2.9	100.0
1982	12.7	0.5	17.3	5.0	1.9	6.7	17.1	29.9	6.0	2.6	100.0
1983	9.2	0.6	18.9	4.6	1.3	6.4	15.3	35.2	5.8	2.7	100.0
1984	13.2	0.6	17.7	2.4	4.8	6.2	13.3	32.4	6.2	3.2	100.0
1985	9.7	0.8	14.3	3.5	5.1	6.4	13.5	36.5	6.6	3.6	100.0
1986	12.0	1.2	13.1	2.3	1.3	6.2	14.7	37.3	8.1	4.0	100.0
1987	9.4	1.0	12.5	2.1	0.9	6.6	15.1	39.9	8.8	3.7	100.0
1988	8.1	1.0	12.1	3.4	0.9	7.1	16.1	40.0	8.3	2.9	100.0
1989	6.3	1.8	10.1	0.7	0.8	7.4	16.4	43.7	9.7	3.1	100.0
1990	5.5	3.1	7.6	0.5	0.5	7.2	13.9	47.4	11.2	3.1	100.0
1991	5.3	4.0	5.8	0.5	0.5	6.9	14.2	48.0	11.5	3.3	100.0

Chapter 8

EXPORT PROMOTION STRATEGIES: SRI LANKA

by
S.P.D. Nanayakkara

I. Introduction

Export trade plays a significant role in determining the overall economic performance of the country in terms of its contribution to domestic production, foreign exchange earnings, government revenue and employment generation. In the case of Sri Lanka, 86 percent of total agricultural production is exported while 65 percent of total foreign exchange earnings are generated from exports. The employment figure in organized agricultural sector was 389,549 while 96,736 were employed in the major export-oriented industrial firms (1992). In view of the government budget, 10 percent of revenue from the duties on foreign trade comes from export duties.

Since the colonial era, the development in export trade in Sri Lanka was based on traditional agricultural crops of tea, coffee, rubber and coconut. Even after a period of three decades of political independence in 1948, agricultural products dominated Sri Lanka's export sector. However, the significance of the agricultural products in total exports gradually declined particularly in the last two decades. In 1970, 94 percent of total export earnings came from agricultural exports and of that, 55 percent came from a single commodity of tea. In promoting industrialization, the dominant position of agricultural exports dropped to 62 percent of total export earnings in 1980 and decreased further to 24 percent in 1992 while the contribution of industrial exports increased from 32 percent to 69 percent between the same period.

As a small import-export economy, the growth performance of export sector is a key to the overall growth of the economy. Therefore, "export promotion" has been treated as an essential element in the formulation of the overall economic development strategy. In this respect, mitigating growing trade deficits is an important target and accelerating the growth of exports is considered as the most effective way of reducing the trade deficits. Consequently, several fiscal, monetary and other institutional incentives are provided to stimulate export growth

particularly for non-traditional industrial exports. As a result, the share of textile and garment exports to total exports has increased from 2 percent in 1977 to 48 percent in 1992. Though, there has been a positive development in diversifying the export structure from primary agricultural products, the high import content reduced the net foreign exchange earnings of these exports by approximately 30 percent than that of their gross earnings. Thus, in formulating appropriate strategy for export development, special priority is given to promote exports with high domestic value-added.

In the context of employment, organized agricultural export sector (tea, rubber, coconut) provides employment of 389,000 while the industrial enterprises in the Greater Colombo Economic Commission (GCEC) absorbed the work force of 104,220 by end 1992. With lack of opportunities for further expansions in the organized agricultural export sector, the major employment prospects are to be provided in the industrial exports particularly from the garment industries. With a well-educated and a dynamic work force in Sri Lanka, the expansion of industries based on higher technological production processing would be more beneficial to the economy in expanding the industrial base in the long-run.

During the period 1960 to 1970, the annual average growth rates of exports of Sri Lanka was only 4.6 percent when compared with some other Asian countries like Malaysia (6.1 percent), Thailand (5.2 percent), Taiwan (23.7 percent) and South Korea (34.7 percent). During the period 1970 to 1980, the average growth of exports was 13 percent while that for the period 1980 to 1991 was 10.5 percent.

The following sections analyze the structure and growth trends of exports, policy environment of export incentives in Sri Lanka and finally, the problems and recommendations to achieve sustainable long-run growth with successful diversification of export structure in favor of enhanced utilization of domestic resources.

II. Export Trade and Salient Features

2.1 Contribution of Exports to the Economy

Exports contribute 29 percent of GDP and generate 67 percent of total foreign exchange earnings (1992). According to past growth trends,

Table 8.1

SRI LANKA: COMPOSITION OF EXPORTS (Million US$)

GROUPS	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
Food & Live Animals	215.8	218.9	211.8	235.7	263.3	323.1	304.3	474.8	502.9	482.3	476.7	453.3	422.9	466.2	741.0	548.7	426.1	468.7	564.9	491.8	625.3	565.7
Beverages & Tobacco	0.4	1.2	1.1	1.0	1.0	0.7	1.4	1.8	2.2	3.4	1.6	4.2	2.0	2.0	3.6	2.1	2.6	2.7	4.1	4.1	6.3	13.5
Crude Materials, excl. fuels	9.3	19.0	24.7	26.9	42.5	27.0	25.4	28.2	204.1	241.8	208.0	191.6	162.9	161.2	171.6	140.7	144.7	169.3	186.9	173.3	73.5	100.8
Mineral Fuels, etc.		3.4	3.1	17.3	12.2	8.4	16.6	76.8	49.6	94.7	161.0	133.9	131.1	102.1	126.3	112.4	68.5	4.6	11.2	14.5	13.2	8.3
Animal, Veg. Oil & Fats	20.8	26.7	23.1	7.1	23.4	29.0	23.9	5.8	21.1	33.3	3.2	10.7	17.7	20.1	12.4	35.1	25.1	8.7	6.3	21.9	7.7	2.2
Chemicals	0.4	0.3	0.3	1.2	3.4	1.8	3.5	3.9	14.0	33.1	32.1	18.2	21.9	20.9	11.8	34.3	23.8	31.7	35.8	29.8	44.8	49.6
Basic Manufactures	84.8	53.9	46.8	118.0	134.0	125.8	150.7	156.7	7.8	12.3	44.8	36.9	57.5	63.1	52.3	61.3	104.8	242.1	187.0	222.3	790.1	834.9
Machines, TranspORT & Equip.	1.1	1.6	0.4	0.5	2.3	2.1	1.9	2.4	1.5	2.5	4.2	26.6	21.3	14.2	20.6	33.5	39.6	22.7	21.8	21.9	55.3	64.5
Misc. Manufactured	8.7	1.6	12.2	1.0	42.8	42.9	44.3	51.3	39.0	73.6	113.2	158.8	175.7	215.4	313.0	304.8	357.2	403.1	462.5	560.4	221.5	292.2
Unclassified Goods	0.0	0.2	0.0		0.8	0.6	0.4	3.8	3.7	3.8	6.9	15.3	4.0	5.1	2.2	16.9	24.4	0.1	0.1		74.9	55.8
Total Exports	341.3	326.8	323.5	408.7	525.7	561.4	572.4	745.5	845.9	980.8	1051.7	1049.5	1015.0	1070.3	1454.8	1289.8	1216.8	1353.7	1480.6	1540.0	1912.6	1987.5
Manufactured Exports	5.9	8.3	10.2	36.2	90.4	96.8	121.4	137.2	158.5	271.5	382.2	420.3	430.3	414.9	532.0	546.9	593.7	728.5	778.0	850.9	1109.3	1283.4
Non-Manufactured Exports	335.4	318.5	313.3	372.5	435.3	464.6	451.0	608.3	687.4	709.3	669.5	629.2	584.7	655.4	922.8	724.9	623.1	625.2	702.6	689.1	803.3	704.1
Services Exports	39.8	52.7	49.6	60.6	66.8	80.6	76.4	104.0	124.4	192.1	278.5	312.7	334.5	341.4	336.8	328.6	378.4	398.1	411.8	404.9	533.2	637.4
Total Exports (gds. & serv.)	338.4	324.1	305.7	38.4	178.5	190.1	71.1	73.7	145.7	420.6	934.6	807.1	995.4	917.1	534.0	863.2	892.5	836.5	916.5	822.8	800.0	1103.0
Merchandise Imports (cif)	391.4	372.3	346.8	412.9	701.1	761.2	644.0	708.9	999.3	1449.4	2051.2	1876.9	1994.1	1921.4	1928.1	2044.3	1973.2	2075.1	2240.2	2225.6	2686.4	3035.0
Services Imports	57.1	55.1	52.0	52.3	55.3	67.9	63.1	69.8	116.8	144.7	-226.6	308.5	349.6	401.4	405.0	462.9	507.4	555.1	565.3	560.6	630.7	744.9
Export/Import Ratio	0.9	0.9	0.9	0.9	0.7	0.7	0.9	1.1	0.8	0.7	0.5	0.6	0.5	0.6	0.8	0.6	0.6	0.7	0.7	0.7	0.7	0.7
Trade Balance	-53.0	-48.2	-41.1	-46.7	-139.9	-202.8	-84.4	39.4	-153.3	-468.0	-986.6	-811.4	-980.3	-857.2	-465.8	-729.0	-763.5	-679.4	-763.0	-667.2	-702.5	-995.5
Current A/c Balance	-58.7	-36.3	-31.6	-25.1	-133.4	-110.2	-5.9	142.7	-66.1	-228.4	-660.0	-441.5	-569.1	-472.7	-55.0	-420.0	-425.1	-342.8	-389.1	-307.1	-259.3	-510.7
Overall BOP	5.7	43.3	22.1	45.0	-54.4	-57.1	63.1	373.4	119.2	50.9	-179.4	-21.1	-48.5	14.5	276.6	-39.0	-63.3	-41.6	-105.0	-52.8	179.6	241.0
GDP at Current Prices	2213.3	2295.1	2371.1	2798.7	3503.5	3666.5	3332.4	3908.9	2503.0	3196.9	3764.7	4122.3	4549.3	4839.9	5505.1	5460.4	5843.3	6036.0	6398.5	328.9	7251.0	8195.5
GDP at Constant Prices	9582.4	9582.4	9490.8	9533.0	9508.0	7728.1	7967.7	7878.5	4849.7	5168.1	5149.8	4680.7	4549.3	4223.5	4103.9	4033.8	4078.3	3936.9	3742.9	3377.0	3226.0	3272.6
Budgetary Surplus/Deficit	193.0	222.7	220.3	222.6	240.4	385.2	425.1	346.4	459.0	564.5	984.3	772.4	965.4	918.2	623.5	945.2	1001.9	928.6	1359.5	1046.5	1099.8	1520.1
Rate of Inflation	16.1	3.9	4.2	17.6	25.2	7.3	5.8	18.7	7.9	15.7	18.1	20.5	13.5	14.6	17.0	1.0	5.8	7.0	11.5	9.6	20.0	11.4
Consumer Price Index	138.2	141.9	150.8	165.4	185.8	198.3	200.7	203.2	227.8	252.3	318.2	375.4	416.1	474.2	553.1	561.2	606.0	652.8	744.1	830.2	1008.6	1131.5
Exchange Rate with US$	6.0	6.0	6.2	6.4	6.7	7.0	8.4	8.9	15.6	15.6	16.5	19.2	20.8	23.5	25.4	27.2	28.0	29.4	31.8	36.0	40.1	41.4

the earnings from merchandise exports to GDP increased from 15 percent in 1970 to 19 percent in 1977 and further to 29 percent in 1992.

The ratio of exports to total foreign exchange earnings was 86 percent in 1977. During 1977 to 1992 approximately 62 percent to 70 percent of total foreign exchange earnings were generated from exports. The gradual decline in relative value share of exports to total foreign exchange earnings was a reflection of the increase in earnings from services and private transfers.

The export/import ratio varied between 0.75 to 0.98 during the period 1970 to 1977 (Table 8.1). With the liberalization of imports, this ratio gradually declined and varied between 0.51 to 0.74 between 1977 to 1992. This was partly due to the large flow of imports after the removal of restrictions on imports relative to the sluggish growth in exports particularly for agricultural commodities.

The role of exports in enhancing the employment opportunities is accorded a high priority in the political economic scenario of the country. With limited opportunities in traditional agricultural sector to absorb the growing labor force, industrial export sector is a key area in generating new employment opportunities. For instance, annual average increase of employment in enterprises in GCEC has been growing at 15 percent during the past six years and 22 percent in 1992.

2.2 Growth Trends and Changing Patterns of Exports

Sri Lanka's experience for the past two decades has shown that the structure of exports has been changed from primary agricultural exports to primary industrial exports. In 1970, 94 percent of total exports comprised of agricultural exports of which tea (55 percent), rubber (22 percent) and coconut (14 percent) earned total foreign exchange amounting to US$ 322 million. Both the industrial and mineral exports contributed 3 percent respectively to total exports in 1970. When the country's economic policies were based on inward-looking trade strategies during the period 1971-1977 traditional exports were not given a high priority. Moreover, with the nationalization of plantations in 1972 and resulting managerial inefficiencies led to a depressed traditional agricultural exports. In the meantime, both the agricultural and industrial exports of non-traditional type were granted incentives and subsidies. Against this background, the share of

traditional exports dropped from 91 percent in 1970 to 75 percent in 1977 while the shares of minor agricultural products and industrial products increased from 3 percent to 5 percent and 1 percent to 14 percent, respectively.

The structural transformation towards an industrial export economy was more evident during the 1980s. The share of industrial exports continuously increased from 32 percent of total exports in 1980 to 69 percent of total exports in 1992 while that of agricultural exports dropped from 62 percent to 24 percent during the same period. The contribution of mineral and minor agricultural products remained around 3 percent and 4 percent respectively in 1991.

Although the relative share of agricultural exports declined considerably in the recent past, their economic significance remain high due to higher content of domestic value-added. The share of tea exports indicated a decline from 53 percent in 1977 to 33 percent in 1985 and further to 14 percent in 1992. Tea exports adversely affected by domestic factors such as bad weather, inability of maintaining quality standards, managerial inefficiencies and lack of technological improvements in line with the changing market demand and also by the external factors of high global supply, competition from other beverages, recession in industrialized countries and political uncertainties in major consumers like former USSR and other Middle-Eastern countries. Global consumer preferences on tea gradually moved in favor of CTC-type tea which Sri Lanka produces in low quantities (approximately 3 percent of total tea production). With the objective of upgrading the production of exports, steps have been taken recently to hand over the management of tea plantations to the private sector with a view to developing tea production with higher managerial skills and required technological improvements in tea factories.

The share of export of rubber to total exports declined from 14 percent in 1977 to 7 percent in 1985 and further to 3 percent in 1992. Apart from sluggish international market prices and competition from synthetic rubber, the decline in Sri Lanka's rubber exports was largely attributable to higher domestic consumption in rubber based industries.

A similar trend has also been observed in the case of coconut which declined from 8 percent in 1977 to 6 percent in 1984 to further 3 percent in 1992. With increased population, utilization of coconut lands for other constructions and higher domestic consumption largely

account for the decline in the quantity of coconut exports. Against this background, even with the recent upsurge in the prices of coconut products in international markets, the volume of exports of coconut has in fact declined.

Minor agricultural products contributes approximately 4 percent of total exports. Major commodities of this category are vegetables, fruits, coffee, cocoa, spices and unmanufactured tobacco. Limited production, high fluctuations in supply, and the difficulty of maintaining quality standards required by well-organized developed markets, and lack of technological and managerial skills in production were among the main inhibiting factors of the growth of minor agricultural exports.

The exports of industrial products reflect the highest percentage share of earnings among all major categories of exports. The relative share of these exports increased from 32 percent in 1980 to 43 percent in 1985 and further to 69 percent in 1992. This export category is dominated by textile and garments which increased its share from 32 percent in 1980 to 52 percent in 1985 and further to 66 percent of total industrial exports in 1992. Except for energy and labor, almost all input for the textile and garment industry are being imported. In spite of the lower domestic value-added, the percentage of exports to total production of the industry is above 96 percent and the capacity utilization also remains as high as 98 percent. Moreover, in terms of annual average growth rate of export earnings, the textile and garment industry is in a commendable position indicating a 19-percent average annual growth for the last five years compared with only 2-percent growth recorded for tea. Moreover, during the last two years, the textiles and garments recorded an impressive 39 percent increase in their export earnings.

Another development observed in the industrial exports was the decline in relative share of exports of petroleum products and the increase in respective share of other industrial exports. The expansion in other industrial exports is a welcome development since the value-added of those industries are much higher than the petroleum products and textiles and garments. Other industrial sector comprised of food beverages and tobacco, wood and wood products, paper and paper products, rubber and plastic products, jewellery, diamonds and precious and semi-precious stones, non-metallic mineral products, machinery and transport equipment and other manufactured products. The share of

other industrial exports to total exports rose from 4 percent in 1980 to 7 percent in 1985 and to 17 percent in 1991. Moreover, the share of other industrial products to total industrial exports rose from 13 percent in 1980 to 16 percent in 1985 and to 27 percent in 1992. A category-wise breakdown of other industrial exports showed that food, beverages and tobacco represents the highest value-added category while its capacity utilization also reached 90 percent in 1992. However, this sector contributes only around 3 percent of total industrial exports. Non-metallic mineral products category contributes 12 percent of total industrial exports while chemicals, petroleum, rubber and plastic products contributes 11 percent. Fabricated metal products, machinery and transport equipment contributes 5 percent of total industrial exports. The growth rates of industrial exports categories showed wide fluctuations on an annual basis. However, all the categories indicated annual average export growth rate of above 15 percent during the last five year period. Particularly, much higher annual growth rates were recorded by manufactured products (81 percent), fabricated metal products (60 percent), basic metal products, wood and wood products (39 percent), paper and paper products (38 percent) and textiles and garments (29 percent).

In summary, the growth trends and changing patterns of exports in Sri Lanka showed a major structural change towards industrial exports from agricultural exports. The industrial products which contribute a high percentage share of exports and have shown high growth performance is also highly dependent on imported input. Industries which are largely based on domestic resources reflect slower growth performance and contribute lower value share to total industrial exports. The exports of traditional agricultural crops are not very conducive in stimulating overall growth in the export sector.

2.3 Structure of Exports on Country-Wise Basis

The direction of export trade during the past ten years showed a shift away from developing countries towards industrialized western countries (Table 8.2). For instance, export to industrial countries was 46 percent of Sri Lanka's total exports in 1983 and the share continuously increased to 74 percent in 1992 while that of developing countries declined from 43 percent to 21 percent. This is largely a reflection of change in the structure of Sri Lanka's exports with increasing bias towards textiles and garments which are mainly exported

Table 8.2
SRI LANKA: MERCHANDISE EXPORTS (Million US$)

TO	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
United States	24.1	27.6	22.6	28.1	36.4	31.2	39.8	57.0	59.3	101.9	116.4	146.0	143.4	186.6	280.9	283.2	317.9	355.2	367.3	400.0	492.5	559.0
Canada	8.7	7.4	10.2	7.5	19.7	13.6	13.9	14.3	18.6	14.5	15.6	13.9	21.7	18.8	29.2	24.6	23.0	24.4	22.6	25.6	29.0	32.0
Australia	12.1	15.2	11.7	11.6	16.0	15.7	15.4	22.5	16.3	14.7	114.5	11.0	12.6	8.0	13.9	15.9	14.0	16.1	20.8	18.5	24.2	24.4
Japan	11.2	11.0	9.4	19.6	19.6	25.6	25.6	36.3	49.4	66.9	33.5	50.6	50.3	48.5	62.4	65.4	67.1	67.2	84.9	89.0	102.4	101.6
New Zealand	5.7	6.1	4.8	5.6	6.0	4.9	5.0	7.7	8.2	8.1	8.4	5.3	4.3	4.1	6.9	5.2	6.5	4.7	3.6	3.6	5.1	3.4
Germany	17.0	16.1	15.1	20.2	32.6	20.7	22.3	31.6	36.1	58.0	55.6	62.3	56.0	65.6	70.9	69.9	83.3	101.1	104.3	95.4	126.7	148.8
Italy	6.6	5.4	6.3	8.5	14.0	9.7	15.6	12.4	19.7	27.4	22.0	16.9	21.5	18.5	17.7	14.7	14.3	14.0	15.6	21.1	36.6	37.2
Switzerland	0.3	0.2	0.3	2.7	4.3	4.3	2.9	6.2	10.1	5.1	7.9	4.6	7.0	7.9	4.3	3.4	11.6	13.7	8.8	9.6	13.9	12.1
United Kingdom	76.3	55.8	43.9	46.9	53.2	44.7	55.3	60.0	66.7	79.7	77.5	67.7	68.0	53.5	86.1	82.6	69.8	75.2	80.9	88.4	115.1	126.2
Saudi Arabia	7.2	9.1	9.9	8.8	9.3	13.4	14.5	19.7	40.2	28.8	36.7	33.0	27.1	34.3	51.3	47.6	33.3	11.5	36.4	33.3	42.3	38.4
Iran	5.0	4.3	5.9	5.8	11.2	16.6	11.9	13.8	36.4	21.0	33.2	25.4	12.3	13.2	35.0	16.2	16.1	28.6	31.4	33.7	64.7	78.0
Kuwait	3.9	4.2	4.9	5.0	6.6	8.4	12.4	11.0	19.0	21.0	17.5	17.7	5.8	8.8	13.5	9.7	7.7	6.7	6.5	9.8	5.5	3.5
Indonesia	0.0			0.2	0.6	0.8	0.3	1.0	0.5	0.3	0.2	0.3	1.2	1.2	1.1	1.5	1.0	0.2	0.6	0.4	2.7	1.8
Korea, Republic of	0.1	0.8							1.2	1.1	0.2	0.5	0.8	5.6	5.0	0.5	2.1	5.1	2.8	2.2	5.1	11.2
Malaysia	0.3	0.3	0.3	0.6	0.3	0.3	0.4	0.3	0.3	0.4	4.7	24.2	12.7	9.0	3.6	11.7	4.7	1.2	2.2	1.4	2.5	26.6
Myanmar	0.4		0.1				0.2		0.1				6.9		0.7				0.1			
Nepal													0.1	0.2		0.1		0.2	0.6	2.6	0.1	0.1
Philipines						0.1	2.2		0.3	0.3	3.3	0.1	0.4	0.1	0.3	0.4	0.2	0.6	0.8	0.1	1.2	2.6
Singapore	2.1	2.1	2.9	5.5	6.8	7.2	17.0	11.1	17.9	10.3	11.9	24.7	38.7	37.5	21.0	43.8	31.5	32.4	44.5	36.3	49.5	67.5
Sri Lanka																						
China, Taiwan										4.5	20.6	1.1	2.5	1.4	1.2	1.2	1.3	3.9	3.4	2.9	8.5	7.9
Thailand	0.1	0.1	0.1	0.2	0.2	0.2	0.3	1.7	2.2	0.2	0.1	0.4	0.7	2.4	2.0	1.3	2.8	10.4	21.7	22.7	21.7	14.4
Hong Kong	1.2	1.1	2.0	13.4	7.1	8.3	14.4	17.2	12.7	10.3	10.5	8.5	9.4	9.9	17.3	10.6	11.5	19.6	16.6	18.1	17.1	14.9
India	3.5	1.7	1.8	1.6	0.7	0.4	0.2	1.2	7.1	12.8	34.6	29.5	21.9	27.9	12.9	6.8	12.2	6.4	19.3	9.9	20.6	12.6
Pakistan	7.1	18.5	25.0	33.4	40.2	49.2	43.2	60.2	44.1	44.1	34.4	55.8	38.4	29.3	34.3	27.6	34.1	31.6	52.8	44.9	32.5	32.0
Bangaladesh	0.9	0.8	1.2	1.7	2.5	1.7	2.4	1.6	3.5	4.1	4.0	2.7	3.5	4.7	16.4	14.6	6.9	10.1	11.4	22.9	10.3	4.7
Argentina	0.2	0.1	0.1	0.2	0.2	0.1	0.1	0.5	0.7	1.8	1.4	1.5	0.3	0.4	0.3	0.9	0.9	0.9	1.5	1.5	1.3	2.8
Brazil		0.1			2.6	0.1		0.1	0.1		0.1	0.1	0.1	0.1	0.8	0.4	0.3	0.3	0.2	0.2	0.4	0.5
South Africa	13.5	12.2	11.8	13.3	16.6	17.2	16.8	22.7	12.9	16.7	18.9	18.4	15.1	15.8	21.8	12.7	10.7	13.9	12.8	13.2	12.3	9.8
Kenya	0.2	0.2	0.2	0.6	0.2	0.2	0.3	0.7	0.6	0.6	1.4	1.3	0.8	1.0	2.0	0.7	1.0	0.9	1.1	6.5	1.0	1.3

Table 8.3

SRI LANKA: MERCHANDISE IMPORTS (Million US$)

TO	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
United States	22.2	17.0	25.4		21.8	48.0	45.0	60.6	76.9	77.7	90.3	129.3	111.5	114.7	164.2	128.9	118.4	114.0	152.7	137.0	207.7	174.5
Canada	11.4	6.7	5.7		4.8	8.9	12.6	7.9	16.9	18.7	24.3	20.0	19.9	33.6	26.8	34.1	21.1	17.4	40.7	14.8	18.9	1506.0
Australia	18.8	21.4	13.6		40.7	61.3	32.3	32.7	47.2	69.2	39.5	55.5	41.8	22.9	26.3	57.9	27.4	20.3	26.1	36.5	43.4	36.6
Japan	32.8	28.5	32.5		53.0	63.8	44.6	44.8	101.8	192.9	260.1	258.2	269.1	317.1	307.6	282.3	318.8	304.2	305.1	259.4	325.3	358.4
New Zealand	3.4	2.6	4.7		0.8	1.8	1.8	2.6	8.6	6.8	7.4	8.3	3.9	14.2	8.8	17.6	20.3	17.1	22.5	22.6	29.4	32.3
Germany	23.4	23.3	17.3		29.9	35.9	21.7	25.1	53.2	78.4	71.1	90.5	76.3	75.1	87.9	98.5	85.8	90.0	102.6	71.1	83.9	101.9
Italy	4.5	4.1	4.1		8.9	5.4	6.1	15.6	17.6	16.9	14.1	12.5	12.2	12.3	14.1	15.0	16.4	21.8	21.1	29.6	18.9	19.3
Switzerland	1.9	2.9	2.1		2.2	2.2	1.6	2.5	6.4	18.9	17.0	8.9	12.6	16.4	15.2	8.6	25.7	20.7	14.6	14.5	18.2	26.1
United Kingdom	55.4	41.4	35.8		25.6	31.9	32.7	36.8	89.4	129.3	193.9	111.1	116.5	121.4	86.8	96.4	102.8	140.4	126.5	125.1	145.9	166.3
Saudi Arabia	6.1	6.2	3.2		51.9	90.8	70.8	84.2	88.7	100.8	213.3	272.6	219.4	79.0	306.7	173.0	11.6	11.2	14.0	45.6	83.4	9.4
Iran	3.2	4.2	1.2		25.9	31.1	59.3	65.9	54.9	47.5	109.7	122.1	206.0	187.4	53.8	39.3	38.2	104.1	101.7	96.5	222.3	144.7
Kuwait	-					1.1	1.3	0.6	1.5	1.7	20.2	0.4	0.3	2.1	0.9	0.7	3.6	3.9	5.8	5.5	2.7	
Indonesia	0.5		0.2			0.1	0.1		0.8	3.4	8.9	1.6	0.2	0.5	2.1	6.6	15.3	21.2	27.1	27.5	39.4	41.1
Korea, Republic of						2.5	4.3	6.1		22.1	35.3	80.8	35.6	35.8	39.1	45.9	70.0	78.8	89.3	94.6	127.8	219.0
Malaysia	1.5	2.0	1.4		2.2	2.2	1.9	3.2	4.8	9.0	12.0	22.6	76.7	58.7	43.7	28.3	41.9	58.7	61.9	60.8	114.3	139.8
Myanmar	15.0	16.6	19.7		30.6	17.2	27.4	18.8	31.9	12.6	23.5	24.2	17.9	30.8	6.3	4.6	2.7	5.1	3.0	4.0	6.8	0.1
Nepal										0.1	0.4					4.4	14.0	3.0	0.3	0.1		5.3
Philipines						1.4	0.2		1.2	0.7	6.1	19.8	9.8	7.1	8.6	6.2	1.2	3.0	2.3	2.6	3.5	3.1
Singapore	5.2	3.4	4.1		8.6	14.8	9.4	14.1	25.9	87.2	91.9	98.9	106.2	148.7	100.9	73.7	71.7	100.1	92.9	94.4	102.5	134.9
Sri Lanka																						
China, Taiwan	48.5	27.0	15.4		53.9	94.4	6.6	32.0	28.9	66.7	50.8	35.6	43.7	46.7	50.5	57.3	95.3	106.0	105.3	116.1	155.8	207.4
Thailand	4.9	6.4	13.8		7.8	50.7	20.4	32.3	3.1	10.7	10.0	14.8	15.0	18.7	14.1	21.4	39.8	40.1	41.9	97.3	85.1	39.0
Hong Kong	2.4	0.5	1.6		1.2	1.1	2.9	4.9	13.6	33.2	41.7	52.5	41.3	54.1	59.1	57.5	85.5	129.8	116.6	109.9	120.3	212.5
India	37.8	34.9	17.7		32.9	21.4	21.6	40.2	86.3	149.9	96.4	75.8	73.0	115.1	111.3	74.6	79.3	83.5	90.9	64.1	118.0	220.1
Pakistan	9.7	11.2	13.4		41.9				11.0	31.6	50.0	17.0	19.6	13.6	17.1	33.9	46.1	46.6	69.6	49.6	50.8	73.7
Bangaladesh						0.1		0.4	0.4	1.6	3.1	2.3	0.1	0.6	0.2	0.2	0.3	0.2	16.8	3.7	8.9	3.9
Argentina						1.3		0.9	8.6		11.1	0.1	0.1	0.1	4.9	0.2	0.3	0.2	0.2	0.6	0.8	6.4
Brazil						0.5	0.4	6.0				0.2	1.4	0.9	9.5	10.3	12.1	12.8	19.3	16.6	2.6	7.1
																						87.6
South Africa	0.7	0.5	3.2		7.4	4.3	0.6	6.0	6.4	22.7	31.6	34.5	25.1	23.4	20.4	24.9	43.5	61.1	67.8	79.8	83.4	1.7
Kenya						0.2	0.2	0.4	0.8	1.8	29.5	19.1	2.2	5.3	3.7	2.5	3.2	3.1	0.4	2.2	2.9	

to industrialized countries. On the basis of individual countries, the major export markets in 1992 are the USA (33 percent), the UK (7 percent), Federal Republic of Germany (8 percent), Japan (5 percent), Belgium-Luxembourg (5 percent) and Iran (2 percent). According to past growth trends, the share of exports to the USA has increased continuously from 18 percent of total exports in 1983 to 33 percent in 1992 while the share of exports to Iran increased from 1 percent to 2 percent during the same period. The relative share of other major individual exporting countries remained more or less the same. In the meantime, export trade with Middle Eastern countries declined from 23 percent in 1983 to 10 percent in 1992 due mainly to declined exports to Iraq and Saudi Arabia. During the same period, exports to the USSR also showed the same downward trend lowering its share from 4 percent to an insignificant (0.6 percent) level due mainly to the absence of tea buying from the USSR.

2.4 Causality Between Exports and Economic Growth

With the view to examining the nature of causality between export growth and the overall economic growth, a causality test is carried out in the case of Sri Lanka. In this regard, the two-variable model developed by Granger (1969) is used as specified in the following form:

$$Y_t = a_o + \sum_{i=1}^{m} a_i \, X_{t-i} + \sum_{j=1}^{n} b_j \, Y_{t-j} + U_t \qquad (1)$$

$$X_t = c_o + \sum_{i=1}^{r} c_i \, Y_{t-i} + \sum_{j=1}^{s} d_j \, X_{t-j} + V_t \qquad (2)$$

Y_t = Real GDP Growth
X_t = Real Export Growth

Time series data covering a 15-year period since 1977 are used in estimating the model. Growth of GDP is calculated on the basis of percentage changes of constant GDP figures reported by the Central Bank of Sri Lanka. Real export growth is estimated by taking the percentage change of the value of exports deflated by the export price index.

Equations (1) and (2) were estimated based on the OLS regression method. Independent variables in both the equations were lagged for two years.

2.4.1 Estimated Results

(i) $Y_t = a_0 + a_1 X_{t-1} + a_2 X_{t-2} + b_1 Y_{t-1} + b_2 Y_{t-2} + U_t$

$Y_t = 4.59 + 0.71X_{t-1} + 0.84 X_{t-2} + 0.32Y_{t-1} + 0.20 Y_{t-2}$

$R^2 = 0.86$

DW Statistic = 2.07

$$\text{Calculated F-Value} = \frac{(SSR_r - SSR_u)/V}{SSR_u/(n-k-1)}$$

$$= \frac{(18.46 - 8.67)/2}{8.67/(15-4-1)}$$

$$= \frac{4.895}{0.867}$$

$$= 5.65$$

$H_0 : a_i = 0$

$H_1 : a_i \neq 0$

$F_T = F^2_{10(0.05)} = 4.10$

F_c = Calculated F-Value

F_t = Table value of F

Since $F_c > F_t$ = 5.03 > 4.10, H_0 is rejected at 5-percent level.

(ii) $X_t = C_0 + C_1 Y_{t-1} + C_2 Y_{t-2} + d_1 X_{t-1} + d_2 X_{t-2} + V_t$

$X_t = 23.29 + 0.68 Y_{t-1} + 0.74 Y_{t-2} + 0.34 X_{t-1} + 0.42 X_{t-2}$

$R^2 = 0.72$

DW Statistic = 1.91

$$\text{Calculated F-Value} = \frac{(SSR_r - SSR_u)/V}{SSR_u/(n-k-1)}$$

$$= \frac{(1270.4 - 633.2)/2}{633.2/(15-4-1)}$$

$$= \frac{318.6}{63.32}$$

$$= 5.03$$

$F_t = F^2_{10(0.05)} = 4.10$

Since $F_c > F_T$ => $5.03 > 4.10$, H_0 is rejected at 5-percent level.

Since $a_i \neq 0$ and $c_i \neq 0$, a feedback relationship between economic growth and export growth is proved by the causality test.

2.5 Export Demand Function

An export demand function is estimated with a view to analyzing the impact of major factors influencing exports in the case of Sri Lanka. Real effective exchange rate and export-weighted real GDP of major export trade partners are taken as independent variables.

Time series data covering 15-year period since liberalization were used to estimate the demand function. The estimations of real effective exchange rates are defined in terms of US$ per rupee after adjustments are made for taxes and subsidies. The figures on nominal GDP of USA, U.K., Germany, Japan, Italy and France in terms of US$ deflated by respective GDP deflators and weighted by value shares of exports with respect to each individual countries were used to represent the export-weighted real GDP of major trading partners.

A long-run export demand function in log form is specified as follows:

$$l_n X^d = a + b\, l_n RXR_t + c\, l_n FGDP_t + U_t$$

X^d	=	Demand for exports
RXR	=	Real effective exchange rate
FGDP	=	Export-weighted real domestic product of export trade partners

2.5.1 Estimated Results

Variable	Estimated Coefficient	Standard Error	T-Statistics
a	19.20	870.19	10.5481927
RXR	0.601357	0.495	2.4052578
FGDP	0.740621	0.6292789	3.78260
R Squared	= 0.897064		
F-Statistics(2,15)	= 52.2888		
DW Statistic	= 1.89		

As shown in the value of R^2, approximately 90 percent of the export demand is explained by the specified model. Income elasticity of export demand is highly significant as expected whereas the price elasticity shows an unexpected positive sign. Based on t-statistics, both the coefficients are significant at 95-percent level.

These results partially confirmed the validity of theoretical fundamentals on demand for exports. However, in formulating export development strategies, special emphasis should be placed on the policies to maintain price competitiveness of export by controlling domestic inflation and thereby securing the external value of the domestic currency. On the other hand, income of the major trading partners are beyond the direct control of domestic policies. However, the significance of income elasticity indicated the practical importance of penetrating the export markets in growing economies like NICS in export promotion.

III. Export Promotion Policies

3.1 Review of Trade and Commerce Policy Environment

Even before the introduction of liberalized trade policies in 1977, export promotion policy was already implemented to stimulate economic growth. During the period when the country followed restrictive trade policies, assistance was provided to promote non-traditional exports through special schemes of premium exchange rate

called Foreign Exchange Entitlement Certificate (FEEC) and the Convertible Rupee Account (CRA) scheme. However, the effectiveness of these policies was largely undermined by the overall inward looking restrictive policies which distorted relative prices between traded and non-traded goods. Under the restrictive policy regime, discrimination of the export sector by higher export taxes was observed. In addition, high import tax structure which in turn increase the cost of raw materials for exports also adversely affected export promotion. On the other hand, due to additional incentives provided to non-traditional exports, the traditional export sector which had higher comparative advantage was discriminated. For instance, the official exchange rate of FEEC system which offered a 65-percent premium on foreign exchange earnings was extended to all sectors other than traditional exports. Moreover, under the CRA system, non-traditional exports were permitted to utilize a certain percentage of their foreign exchange earnings for purposes of imports, foreign travel, etc., while traditional exports had no such options. Furthermore, cost of exports increased due to high tariffs and quantitative restrictions on intermediate and investment goods imports. The relative prices of import substitutes were higher than that of exports due to higher protection levels. Therefore, production of import substitutes were much more profitable than producing goods for export. In addition, restrictions on direct foreign investment also adversely affected exports since it prevented the availability of required initial capital to expand the export base and also prevented the acquisition of efficient technological know-how to increase the efficiency of export industries. Moreover, overvalued exchange rate threatened the international competitiveness of exports. Under the commercial policy followed during the restrictive trade regime, government's direct control over trade and commerce were observed through direct controls, exchange control regulations, licensing system and public sector trade monopolies.

Since 1977, Sri Lanka's trade and commerce policy focused on outward looking strategy which was based on promoting trade within an environment of a liberalized system.. Consequently, the policy measures of lowering export duties, easing of exchange control regulations, removing quantitative restrictions on imports, devaluation of the rupee and implementation of flexible exchange rate were carried out. In the meantime, several fiscal, monetary and institutional incentives were provided to encourage and to diversify the export sector.

The nominal devaluation of rupee by 46 percent against the US dollar immediately removed the bias against exports and other tradeable items that had been placed at a disadvantaged position under the dual exchange rate system. In other words, devaluation removed a 65-percent nominal implicit tax on traditional exports in the dual exchange rate system.

A new tariff structure was introduced to reduce the adverse effects of pervasive quantitative restrictions on imports. Tax reforms led to an establishment of a six-band duty system that ranged from 5 percent for essential consumer goods (rice, flour, pharmaceutical) to a 500-percent prohibitive tax on luxury items. Higher export duties on traditional exports were gradually lowered and changes were made in ad valorem sales tax which was reduced time and again according to international market conditions. In addition to the relaxation of taxes, steps have also been taken to expand the export base of the economy through the establishment of Free Trade Zones to provide special incentives to enhance foreign direct investment, particularly for industrial exports.

In line with the liberalized trade and commercial policy environment, new institutions were established to extend various services to promote export and direct foreign investment. Among them are, the Greater Colombo Economic Commission (GCEC), Foreign Investment Advisory Committee, Export Development Board (EDB), Export Credit Insurance Corporation (ECIC), National Development Bank (NDB) and the Development Finance Corporation of Ceylon (DFCC).

With the view to facilitating liberalized trade and payments system, financial sector reforms have also taken place gradually at the latter stage of liberalization particularly during the latter half of 1980s. The major changes among them are liberalization of capital markets for foreign investors, opening up of foreign commercial banks, and establishment of Regional Rural Development Banks (RRDBs) and foreign currency banking facilities for exports, etc.

In summary, a review of trade and commerce policies showed that the overall economic policies since 1977 aimed at liberalizing the economy have made considerable impact on all sectors of the economy. These policy changes largely influenced the export sector in particular the export structure of the economy.

3.2 Role of the Central Bank of Sri Lanka (CBSL)

3.2.1 Monetary Policy Measures

Apart from maintaining monetary stability of the country, CBSL is also responsible for overall development of the country. In the context of development objectives of CBSL, the export sector is treated as one of the priority sectors of the economy. In formulating overall macroeconomic policy, monetary policy is aimed at maintaining stable monetary conditions with controlled domestic credit and inflation, on one hand, while maintaining adequate level of financial incentives to priority sectors like exports, on the other. On overall monetary policy, restrictive policy stance has been continued with increasing reserves and ceilings on commercial banks' credit on non-priority sectors. However, the export sector has not been affected by these measures since no restrictions were imposed on commercial banks credit to the sector, and it has also benefited by absorbing subsidized credit from the central bank refinance credit window.

In terms of the Monetary Law Act (MLA), refinance is one of the policy instrument available for the central bank to achieve its development objectives. The central bank commenced the grant of refinance facilities for the first time in 1960. Thereafter refinance facilities have been modified and expanded time and again to consider the development needs of the economy.

3.2.2 Short-Term Refinance Schemes

(i) Category 1: Pre-Shipment Export Credit Refinance Scheme

With the objective of providing subsidized credit for traditional exports, this scheme was established in 1982 when commodity prices were at an all-time low. Initially, the central bank provided refinance under Category 1 at 4-percent interest rate and permitted the commercial banks to keep 2-percent margin. Currently, Category 1 - export credit refinance is provided at 18 percent rate of interest by the central bank and a maximum of 1.5-percent margin is permitted for commercial banks. Compared with around 24-percent interest rate for commercial lending, the exporters are still benefiting from refinance facilities. The central bank covered

60 percent of each loan and the current ceiling for Category 1 is Rs. 500 million.

(ii) Category 2: Supplementary Export Credit Refinance Scheme

This facility is granted only for non-traditional exporters. At present, the central bank provides Category 2 refinance at 15-percent rate of interest allowing commercial banks to keep 1.5-percent maximum margin. The central bank provides a 60-percent of the coverage of each loan under Category 2 and the ceiling is Rs. 600 million for this scheme.

These two schemes are facilitated for working capital requirement of both traditional and non-traditional exports.

3.2.3 Refinance Under the Medium- and Long-Term Credit Fund (MLCF)

Under the MLCF, refinance credit is provided for fixed capital requirements of production and manufacturing industries which are export-oriented and value-added agro-based industries of primary traditional exports. Under the MLCF projects up to Rs. 5 million capital are eligible for loans at a concessional rate of 11 percent and for projects above Rs. 5 million, credit is provided at 12-percent rate by the central bank allowing commercial banks to earn a 3-percent margin respectively for both schemes. The central bank also provides 70-percent coverage of these loans.

Apart from these major schemes, a special refinance facility for tea factory owners is provided at 17-percent interest by the central bank allowing commercial banks to earn a 3-percent margin.

Sectoral allocation of export credit refinance showed that the share of refinance credit was largely allocated to the sectors of tea (46.5 percent) garments (30 percent), rubber (13.5 percent) and coconut (6 percent). Moreover, 80-percent of the refinance credit under category 1 was granted to ten major tea-exporting firms. Tea exports which accounted for 24 percent of total export earnings constituted the largest share of refinance credit under category 1 and 30-percent was channelled to garments export with high import content.

Central bank refinancing has expanded sharply in the recent past with adverse implications on monetary aggregates, prices and the set targets of the economic stabilization program. For example, the outstanding amount of total short-term central bank refinance credit increased from Rs. 2,740 million at the end of 1989 to Rs. 4,785 million at the end of 1990 due mainly to the granting of refinance credit for finance companies. Total refinance credit including MLCF loans expanded from Rs. 4,312 million to Rs. 7,330 million between the same two periods. At the end of 1990, the short-term export credit refinance recorded Rs. 2,638 million.

The rapid expansion of central bank refinancing defeated the objectives of restrictive monetary policies which aimed at controlling domestic credit expansion and the acceleration of inflation. Moreover, it was also evident that the refinance credit facility was abused in some cases. In addition, refinance facilities with preferential interest rates distorted the interest rate structure and undermined the competitiveness of financial sector reforms, therefore, generating an unfavorable impact on the efficiency of resource allocation.

Therefore, to eliminate the said distortions, certain measures have been taken to increase the refinance interest rates and to lower the coverage provided by the central bank while imposing maximum ceilings on each category of export credit refinance schemes. With the implementation of rationalized measures in respect of the central bank refinance facilities, total central bank short-term refinance outstanding amount dropped to Rs. 923 million at end-1992 from Rs. 1,394 at end-1991. Moreover, total refinance including MLCF loans also declined to Rs. 5,763 million at end-1992 from Rs. 7,330 at end-1990. Meanwhile, short-term refinance credit for exports also dropped to Rs. 230 million at end-1992 from Rs. 773 million at end-1991. Refinance facilities for exports are currently provided only for high value added or pioneering industries with the objective of diversifying export structure and promoting the value added exports.

Under the rationalization of central bank refinance scheme, the extent of coverage of each refinance loan is limited to 70 percent of the loan granted by the commercial banks, therefore, compelling the banks to seek the balance from their own resources in respect of each loan. With the objective of promoting only the pioneering industries and preventing well-established firms from enjoying subsidized credit

on a continuous basis, items that are under Category 2 are reviewed and updated annually, by removing well-established products and incorporating new products into the scheme. Moreover, any new industry will be eligible to receive refinance only for the first three years of its operation. Thereafter, these firms can have access to refinance facility only if they introduce new products or new processing systems to existing production techniques. In line with the central bank's objective to reduce the overall short-term refinance level to Rs. 1.5 billion by the end of 1992 as specified under the ESAF proposal, a maximum ceiling of Rs. 600 million for Category 2 is also imposed in December 1991. In addition, a ceiling of Rs. 10 million is also to be imposed on each individual exporter under Category 2.

3.2.4 Exchange Rate Policy

In line with the liberalized trade and payments system, exchange rate was unified on 16 November 1977 at an initial level of Rs.16 = US$1 and subsequently a flexible exchange rate was adopted. In terms of official rate, the unification of exchange system was accompanied by a depreciation of the rupee by 46 percent. The cumulative changes since November 1977 indicated that the Sri Lanka rupee had depreciated by 62 percent against the US dollar, 64 percent against the pound sterling, 75 percent against the deutschemark, 60 percent against the French franc and 81 percent against the Japanese yen by the end of 1991. Based on the annual average change of trade-weighted Nominal Effective Exchange Rate (NEER) with respect to major trading partners, the rupee reflected continuous depreciation against all major currencies while the respective changes in Real Effective Exchange Rate (REER) adjusted for inflation differentials between Sri Lanka and her major trading partners continued to appreciate since 1988. An analysis of the impact of change in exchange rate policy showed that the nominal devaluation reduced the bias against exports and other tradeable goods that had been placed at a disadvantaged position under the dual exchange rate system. Accordingly, the devaluation removed the 65-percent nominal implicit tax on traditional exports that was imposed by the dual exchange rate system.

However, the objective of maintaining the exchange rate at a favorable level to support the international competitiveness of exports was overshadowed by high domestic inflation which led to an appreciation of the real exchange rate which hindered the desired objective of maintaining a favorable external competitiveness.

3.3 Fiscal Incentives

Since the implementation of liberalized economic policy measures in 1977, several fiscal incentives have been offered to stimulate the export sector. With the removal of quantitative restrictions and the lowering of high tariffs on imports, the bias against exports in relation to import substitution industries has been largely removed. Moreover, a gradual reduction of high export duties on traditional exports also generated a positive impact on exports. In addition, direct fiscal incentives are offered to stimulate the export drive.

Tax and tariff incentives for the export sector are available through two major schemes.

General Incentive Scheme

These incentives are provided under certain domestic legislations, namely:

(i) Inland Revenue Act No. 28 of 1979
(ii) Turnover Tax Act
(iii) Excise (Special Provisions) Act
(iv) Customs Ordinance
(v) Revenue Protection Act
(vi) Exchange Control Act

Special Incentive Scheme

These incentives are provided under the Greater Colombo Economic Commission (GCEC) Law No. 4 of 1978 as amended from time to time and other regulations made under that law. Now, the GCEC is renamed as the Board of Investment (BOI) of Sri Lanka. It is important to note that the GCEC special incentive schemes are provided only for the non-traditional exports.

For the purpose of granting tax and tariff incentives to the export sector, enterprises are categorized into different schemes by the GCEC Act. Incentives offered by the GCEC differ according to the specific categories of industries, as follows:

(i) Incentives and Concessions Available to Area Enterprises and Licensed Enterprises: These enterprises are established under the GCEC Regulation No. 1 of 1978. The export component of the output of these enterprises should be 90 percent for industrial products and 75 percent for agricultural products. Minimum investment is US$ 250,000 and all fixed assets should be provided from abroad and all working capital be financed from abroad.

Incentive or Concession	**Period**
Exemption from corporate income tax (tax holiday)	Up to a maximum period of 15 years reckoned from first year of profit as defined in GCEC Regulations No. 1 of 1978
Concessionary rate of income tax at rates varying from 2-5% on annual turnover profits	Up to a maximum period of 15 yearsreckoned from the expiry of the tax holiday
Exemption from tax on dividends paid to non-resident shareholders	During lifetime of enterprise
Exemption from dividend tax on dividends paid to resident share-holders out of exempt profits	During tax holiday and for 1 year thereafter
Income tax on royalties to non-residents	Total exemption during tax day: thereafter at a rate not exceeding 15%
Exemption from income tax on emoluments paid to foreign employees	During the tax holiday period
Duty-free imports of plant, machinery, equipment, raw materials and other project-related goods	During lifetime of enterprise
Duty free export of finished products	During lifetime of enterprise
Exemption from Import and Export Control Act	During lifetime of enterprise

Incentive or Concession	Period
Exemption from Exchange Control Act and authorization to open a Foreign Currency Banking Unit (FCBU) Account	During lifetime of enterprise
Exemption from payment of tax on transfer of shares to non-citizens	During lifetime of enterprise
Exemption from income tax on capital gains arising from the transfer of shares	During lifetime of enterprise
Relief for investment amount invested in the purchase of ordinary shares other than existing shares for deduction from purchaser's assessable income subject to established limits	During lifetime of enterprise

(ii) Incentives for Enterprises under the GCEC Regulation No. 1 of 1991: Export-oriented projects which do not meet the Criteria for Area and Licensed Enterprises.

Incentive or Concession	Period
Exemption from corporate income tax (tax holiday)	5 years reckoned from the first profit-making year
Exemption from dividend tax on dividends paid out of exempt profits	During tax holiday and for 1 year thereafter
Tax credit equivalent to 50% of normal tax rate provided net foreign exchange earning from export sales each year is not less than 25% of the fob value of exports	For each of the 5 years immediately succeeding the tax holiday
Qualifying payment (investment) relief for persons who buy shares in a company declared as an approved undertaking	Period specified with approval; the Government has announced its intention to abolish this measure as at 1 April 1992

Incentive or Concession	**Period**
Duty and tax-free import of approved inputs under manufacture in bond scheme and customs duty rebate at predetermined rates to reimburse the cost of customs duties and taxes incurred in the import of raw materials or ancillary materials used in the manufacture of export products	During lifetime of undertaking
Duty and tax-free import of machinery, equipment and accessories certified by the Export Development Board that they have been imported for the exclusive use of an industry which exports 100% of its output	During lifetime of undertaking
Access to foreign currency credit under central bank regulations	During lifetime of undertaking
Exemption from payment of tax on transfer of shares to non-citizens if the shares held in the company after such transfer by non-citizens do not exceed 40% of the total paid-up share capital of such company	During lifetime of undertaking
Exemption from exchange control permission for the allotment or transfer of shares to a non-resident or a non-citizen within the approved limit of foreign direct investment applicable to the company	During lifetime of undertaking
Exemption from exchange control permission for the remittance of dividends to non-resident shareholders, sale proceeds of shares held by non-residents and any royalty/technical service fee/fee for use of patent or manufacturing process, provided such remittance is certified as correct by the company's auditors	During lifetime of undertaking

Incentive or Concession	Period
Resident Foreign Currency Accounts as described in paragraph 7.3.	As from 1 January 1992

(iii) Incentives for Enterprises Set Up in the Provinces and Less Developed Areas: 200 AGA divisions have been identified for this purpose. These enterprises should have a minimum capital investment of Rs. 10 million. The export component of the output should be 90 percent for industrial products and 75 percent for agricultural products.

(a) New Projects Set Up in Designated AGA's Divisions

Concession	Period
Exemption from income tax	15 years for most difficult areas. 10 years for difficult areas, 5 years for others, reckoned from the year in which the enterprise commences to make profit
Partial tax-credit after the expiry of the above tax exemption period	Up to 5 years stipulated under Section 85A of the Inland Revenue Act No. 28 of 1979
Exemption from customs levies and turnover tax, on the import of plant, machinery, equipment, raw materials and other project related goods including one passenger car	During lifetime of the project
Right to maintain a foreign currency account	During lifetime of the project
Funding and credit facilities are obtainable from the DFCC, NDB and local banks	During lifetime of the project

(b) Existing Projects: Incentives for expanding units of existing export-oriented projects in designated AGA's divisions should provide employment for 500 initially.

CONCESSIONS TO EXPANSION UNITS OF EXISTING EXPORT-ORIENTED PROJECTS (BOTH GCEC AND OTHERS) IN DESIGNATED AGA'S DIVISIONS

Incentive	Period
Exemption from income tax reckoned from the commencement of exports by the expansion unit	5 years reckoned from commencement of exports by the expansion unit
Partial tax credit after the above period expires	For 5 years immediately after the expiring of the tax holiday
A tax holiday for the parent company of an expansion project with a minimum employee cadre of 500 in the designated Pradesheeya Division	5 years reckoned from commencement of exports by the expansion unit
Exemption from duty and turnover tax on plant machinery, equipment, raw materials and other project-related imports, including 1 passenger car	During the lifetime of project
Funding and credit facilities are obtainable from the DFCC, NDB and local banks	During lifetime of the project
Right to maintain a foreign currency account	During lifetime of the project

(iv) Incentives for Infrastructure Development and Tourism-Related Enterprises: Infrastructure development enterprises should have a minimum investment of US$ 2.5 million or Rs. 100 million. Taiwan related enterprises should have a minimum investment of Rs. 10 million and a minimum room capacity of 50.

(a) Infrastructure Projects

Incentive or Concession	**Period**
Exemption from corporate income tax (tax holiday)	Up to a maximum period of 7 years reckoned from first year of profit as defined in GCEC Regulation No. 1 of 1978
Concessionary rate of income tax at a rate of 2% on annual turnover profits	Up to a maximum period of 15 years reckoned from the expiry of the tax holiday
Exemption from dividend tax on dividends paid to non-resident shareholders	During lifetime of enterprise
Exemption from dividend tax on dividends paid to resident shareholders out of exempted profits	During tax holiday and for 1 year thereafter
Exemption from income tax on emolument paid to foreign employees	During lifetime of the enterprise
Duty-free imports of plant machinery, equipment, raw materials and other project-related goods	During lifetime of the enterprise
Exemption from Import and Export Control Act	During lifetime of the enterprise
Exemption from payment of tax on transfer of shares to non-citizens	During lifetime of the enterprise
Exemption from income tax on capital gains arising from the transfer of shares	During lifetime of the enterprise
Investment relief within permitted limits available for purchases of new ordinary shares	During lifetime of the enterprise

(b) Tourism Development

TOURISM INFRASTRUCTURE DEVELOPMENT PROJECTS

New Hotels

Category:		
5-Star 150 rooms or more 4-Star 100 rooms or more	2-3 Star over 50 rooms	Up to 50 rooms
Minimum Investment:		
Rs. 150 million	Rs. 50 million	Rs. 10 million
Concessions:		
(a) 10-year tax holiday (Exempt from income, corporate and dividend tax)	(a) 5-year tax holiday	(a) 5-year tax holiday
(b) Income tax of 2% on turnover up to 15 years thereafter thereafter	(b) Income tax of 2% on turnover up to 10 years	(b) Duty free import of plant fixtures, fittings, furnishing & equipment
(c) Duty free import of plant fixtures, fittings, furnishing & equipment	(c) Duty free import import of plant fixtures, fittings, furnishing & equipment	
(d) No limit on foreign equity holdings & free transferability of shares	- do -	- do -
(e) No tax on transfers of capital and proceeds of liquidation	- do -	
(f) Tax free income of expatriates during company tax holiday		

RECREATION CULTURAL ENTERTAINMENT COMPLEXES

Development of Recreation Cultural Entertainment Complexes

Category	Category
Capital cost over Rs. 80 mn. (inclusive of tourist shopping complexes)	Capital cost between Rs. 10 mn. & Rs. 80 mn.
Concessions	
(a) 10-year tax holiday	(a) 5-year tax holiday
(b) Income tax of 2% on total turnover up to 15 years thereafter	(b) Income tax of 2% on total turnover up to 10 years thereafter
(c) Duty free import of plant, fixtures, fittings, furnishing equipment	(c) Duty free import of plant, fixtures, fittings, furnishing & equipment
(d) No limit on foreign equity holding & free transferability of shares	(d) Joint-venture companies
(e) No tax on transfer of capital and proceeds of liquidation	(e) No tax on transfers of capital & proceeds liquidation
(f) Tax-free income of expatriates during company tax holiday	

Incentives for flagship companies with an initial investment of over US$ 50 million will be the same as given in the first Table.

Pioneering industries will be exempted from income tax and other taxes for five years commencing from the first year in which they start making profits.

Only the first two categories can be considered as GCEC enterprises. The other categories will be provided with some of the incentives given to GCEC enterprises or to a lesser extent.

3.4 Banks and Financial Institutions

The institutional framework that facilitates export sector consists of the following institutions:

(i) Commercial banks;
(ii) Development banks; and,
(iii) Non-bank financial institutions.

3.4.1 Commercial Banks

The country's commercial banking sector comprises of six domestic banks including two major state banks and seventeen foreign banks. As a major incentive scheme for exporters, the central bank refinance to exporters include pre-shipment packing credit and other medium- and long-term credit channeled through the commercial banks. A large share of production loans to exporters have been provided by the two state banks while private sector banks are mainly providing short term commercial credit to exporters. The outstanding loans provided by all commercial banks to the industrial export sector was Rs. 18,110 million as at end 1992.

3.4.2 Development Banks

The National Development Bank (NDB), Development Finance Corporation of Ceylon (DFCC), Regional Rural Development Banks (RRDBs), regional bank branches of the central bank are the major institutions that provided facilities for exports.

(i) The National Development Bank

With the objective of facilitating long-term credit requirements the NDB was established in 1979. The NDB provides direct project finance, refinance and equity funding to public and private enterprises export-oriented as well as refinancing of small- and medium- industrial (SMI) projects. The NDB gives special emphasis to export-oriented projects. Accordingly, between the period 1979-1991, allocation of direct lending to major export-oriented

projects are as follows (refinance facilities for SMI projects are in brackets):

Sector	No. of Loans	Value (in Rs.Mn.)
Textiles & Garments	172 (821)	1,137.18 (439.1)
Wood & Paper Pdts.	38 (924)	171.90 (345.5)
Rubber & Leather Pdts.	119 (265)	918.15 (145.1)
Metals, Chemicals & Other Manuf'g Pdts.	256 (934)	2408.8 (373.9)
Food Beverages & Tobacco	112 (2105)	1,548.96 (825.0)

(ii) Development Finance Corporation of Ceylon (DFCC)

The DFCC was established under Act No. 35 of 1955 to provide long-term finance to private sector enterprises and lending activities of the DFCC expanded further with the establishment of the Medium- and Long-term Credit Fund (MLCF) of the central bank in 1964. During 1980s, with the acceleration of policy changes to promote private sector industrialization of the economy, the DFCC activities expanded rapidly. Consequently, in addition to granting long-term loans several other activities including merchant banking, co-financing, hire-purchase activities, equipment leasing, consultancy services, professional project appraisal and underwriting of equity are also carried out by the DFCC. Currently, 30 percent of the small industry financing in the country is funded by the DFCC including 50 garment factories under the 200 garment factories program of the government. Loans granted to major export related enterprises by the DFCC as at end-March 1992 are as follows:

Sector	No. of Projects	Rs. Million
Textile & Wearing Apparel	129	408
Leather, Leather Products & Footwear	11	14
Wood & Manuf'g of Wood Products	32	37
Paper & Paper Products	43	134
Chemicals	28	181
Manufacturing of rubber Plastic Products	49	176
Non-Metallic Mineral Pdts.	26	298
Basic Metal Products, Fabricated Metal Products, Machinery & Transport Equip.	82	195
Food Beverages & Tobacco	128	525

3.4.3 Other Institutions

(i) The Export Development Board (EDB)

The EDB was established in 1979 by the EDB Act No.40 as a coordinating and catalytic body to function as a focal point within the Government where exporters can deal with their problems.

Major functions of the EDB are as follows:

(a) To advise and forward recommendations to the Export Development Council of Ministers an overall national

export development policy and programs in the context of export-oriented investment;

(b) Formulation, implementation and monitoring of National Export Development Plan;

(c) To administer the Export Development Fund and implement all programs of assistance for export production and marketing in close cooperation with the various agencies of the Government and of trade and industry;

(d) To recommend the adoption of trade agreements or negotiation of inter-country commercial policy, financial and other related arrangements that will facilitate the development of Sri Lanka's exports;

(e) To carry out export potential surveys, research and development on export products and to promote and sponsor trading houses, joint export groups, etc.

(f) To carry out feasibility studies on export-oriented projects and to undertake special projects for export development on pilot basis;

(g) Providing trade information, marketing research and organization of buyer-sellers meetings in Colombo and in foreign locations; and,

(h) Providing assistance in quality control standards, packaging, export credit and insurance and import and export procedures and documentation.

The EDB has identified a list of products around forty items as having higher potential for export development including jewellery, coir fibre, tea bags and packets, rubber and rubber products and handloom products. Moreover, the EDB provides concessional financing for selected projects and also contributes for equity participation in export-oriented ventures. Moreover, the marketing and the project management divisions of the EDB provide required information and advisory services in the stages of identification of products and survey of markets. In addition, assistance will also be provided for feasibility studies, arranging bridging loans, and for pioneering projects. The services division of the EDB involves in resolution of problems faced by exporters. With a view to providing financial assistance to small-scale export-oriented manufacturers, a loan scheme was established by the EDB at a concessional rate of 7 percent. Under this Scheme, a maximum

of Rs.100,000 is provided for each enterprise and 15 projects have benefited from the Scheme in 1992. Moreover, the EDB assists exporters by offering fiscal incentive schemes such as the duty rebate scheme, the manufacturer in bond scheme and the duty free clearance of machinery scheme.

The duty rebate scheme is the prompt refund of import duties paid on imported raw materials, components, etc., that were utilized in export production. The duty refunds payable to exporters of specified products are gazetted as a percentage of the f.o.b. price of each product and are recoverable from the exporter's commercial bank upon presentation of export documents and realization of export proceeds. Meanwhile, commercial banks continue to issue bank guarantees to the Customs Department for the payment of imported material in used in export products. Therefore, duties payable at the time of importation of production materials will not affect the working capital resources of the exporter. Moreover, the EDB Annual Award Scheme and Export Expansion Grant (EEG) are also provided by the EEG to encourage exporters. Under the EEG scheme an unified across-the-board grant free of tax is made available to help exporters of non-traditional exports to facilitate at least a part of the costs involved in export market research and marketing, product adaptation and training in the initial stages of any export-oriented projects. These grants are made to exporters on the basis of increment of export earnings in each specified products (expressed in terms of SDRs) achieved by them in each calendar year over the average export earnings in the previous three years. The amount of grant is a percentage of the increment of export earnings and varies according to the net foreign exchange earnings capacity of the product.

(ii) Sri Lanka Export Credit Insurance Corporation (SLECIC)

The SLECIC was established by the Government of Sri Lanka with the authorized capital of Rs. 5 million of which Rs. 2.5 million was initially paid-up by the Central Bank of Sri Lanka and the Insurance Corporation of Ceylon in equal proportion. In September 1980, the authorized capital had been increased to Rs. 20 million.

The main functions of the SLECIC are as follows:

(a) to issue policies to exporters of goods and services against non-receipt or delayed receipt of payments resulting from commercial and non-commercial risks;
(b) to issue guarantees to banks and other financial institutions to facilitate the granting of pre-shipment and post-shipment finance;
(c) to issue guarantees to persons or institutions abroad in connection with goods exported by any person or institution from Sri Lanka or for the due performance of any services to be rendered to such persons or institutions within or outside Sri Lanka;
(d) to provide financial assistance to exporters for the promotion and development of export of goods and services from Sri Lanka;
(e) to provide guarantees to exporters against losses that may be sustained in undertaking market surveys, publicity and any other promotional measures in foreign countries;
(f) to provide refinancing facilities to banks and other financial institutions in respect of credit facilities granted by such banks and institutions for promotion of exports;
(g) to undertake market studies abroad for promotion of exports from Sri Lanka and to conduct seminars and courses on various aspects of export promotion and to collect and disseminate information relating to marketing possibilities and procedures;
(h) to act as an agent of the Government, or with the approval of the Government on its own account, to provide insurance and guarantees, undertake such responsibilities and discharge such functions as are considered by the Government as necessary in the national interest;
(i) to help exporters to diversify and expand exports, find new markets and sell their goods abroad on competitive terms of payment; and,
(j) to discharge such other functions as the corporation may consider as necessary for the achievement of any of its objects.

The three major guarantee facilities provided by the SLECIC are as follows:

(a) Pre-shipment Credit Guarantee Scheme

In terms of the SLECIC Act, the Corporation took over the guarantees operated since January 1977 under the earlier Packing Credit Guarantee Scheme and redesignated as Pre-shipment Credit Guarantee Scheme by widening it to include the export of all commodities of Sri Lanka whereas the earlier scheme was confined to non-traditional exports.

Under this scheme, pre-shipment credit granted by commercial banks to exporters for the purchase, manufacture and packing of goods for export against a confirmed export order or in connection with the execution of an export order was made eligible for export cover. The amount of loss guaranteed under the above scheme is 66 percent, thereby protecting commercial banks against non-payment by exporters. Several new and small exporters who are unable to obtain export credit from banks due to security considerations particularly benefited from this scheme.

(b) Post-shipment Credit Guarantee Scheme

The earlier Packing Credit Guarantee Scheme operated by the central bank was limited in its scope and also in its appeal to commercial banks; the cover it provided to banks ceased with the shipment of the relevant goods by the Exporter. This meant that when exports were made on terms other than Letters of Credit, banks had still to contend with the risk of loss if the exporter defaulted consequent to non-payment by the foreign buyer to whom he extended credit. There was no protection for banks during the period between shipment and receipt of export proceeds. Thus, the exporter who sold goods on non-LC terms did not benefit from the earlier Packing Credit Guarantee Scheme.

(c) Export Payment Insurance Scheme

Under this scheme, SLECIC insures the policy holders against losses resulting from the failure of foreign buyers to pay for goods sold on credit terms. The cover extended under the policy is 80

percent for commercial risks and 85 percent for non-commercial risks.

(d) The Export Performance Guarantee Scheme

This scheme has been designed to help exporters to secure on easier terms. Bank guarantors are called upon to furnish to either Government Authorities in Sri Lanka or to parties awarding contracts of construction works or services in the course of export business. Accordingly, this is a counter-guarantee for indemnity that SLECIC issues to banks against guarantees/bonds that are issued by them on behalf of the exporter, who undertakes to perform a particular export function. Therefore, it protects commercial banks from losses that may be sustained by them in respect of such guarantees and thereby enable the banks to issue such guarantees on more liberal basis.

In addition to those functions, the SLECIC also provides economic intelligence services for their clients, organizes seminars and provides training facilities.

(iii) The Greater Colombo Economic Commission (GCEC)/Board of Investment (BOI)

Following the liberalization of the economy and introduction of market-oriented policies in 1977, the GCEC was established under the GCEC Act No. 28 of 1979 as an autonomous statutory body which was responsible for promoting foreign investment, maximizing exports, promoting transfer of technology and generating employment opportunities. The activities of the GCEC has a special significance in export promotion since it mainly engages in encouraging foreign direct investment to the country and expanding and diversifying of export sector. The incentives and concessions depend on the type of project (details are given in the section on "Fiscal Incentives".

In order to promote exports, the GCEC has established three Export Processing Zones (EPZ) with well-developed industrial estates and improved infrastructural facilities; one at Katunayaka with 190 hectares in extent and more than 60,000 employees, the second at Biyagama with 180 hectares in extent and around 20,000

employees, and the third at Koggala of 80 hectares with around 2500 employees. Since setting up of export-oriented projects are not confined to the Export Processing Zones, a number of licensed factories are operating outside these zones.

The number of units of GCEC firms in commercial operation as at end-1991 was 179 and total approved investment was Rs. 46,203 million. The industrial enterprises operating under GCEC are currently contributing 26 percent of the country's total exports and providing total direct employment around one million.

Foreign investment approvals in most sectors are automatic except in some sectors such as mining and processing of non-renewable natural resources.

(iv) Other Institutional Arrangements in Promoting Exports

The year 1992 has been declared as Sri Lanka's year of exports and several promotional activities are to be implemented during the Export Decade of 1992-2002. Sri Lanka's first export fair 'Expo-1992' was held in November 1992. This attracted 3,600 overseas buyers and investors. It provided an excellent opportunity of international exposure of Sri Lankan products displayed in 340 stalls of both traditional and non-traditional exports.

IV. Problems and Issues on Export Promotion

The considerable policy changes carried out in the course of economic liberalization for the past 15 years resulted in Sri Lanka succeeding in generating a higher GDP growth rate through enhanced economic activity. However, the economy was adversely affected by the unfavorable balance of trade due mainly to relatively high growth rate of imports against exports. With a few exceptions, the trade balance has been in deficit for the last 20 years and is continuously deteriorating at an accelerated rate. In 1991, trade deficit deteriorated by 50 percent in rupee terms (44 percent in US-dollar terms) reflecting only 6-percent increase in export earnings against 18 percent increase in expenditure on imports. The sluggish growth in the prices of exports

as against a higher relative growth in import prices gave rise to adverse terms of trade.

On the export front, the experiences of past 20 years showed a wide range of fluctuations in annual export earnings. During the years 1971, 1972, 1982, 1985 and 1986; exports recorded negative growth rates due largely to the adverse international developments of oil crisis and slump in commodity prices. During the years of commodity boom, the annual average growth rates of exports recorded impressive growth of above 25 percent (1973, 1974, 1977, 1984 and 1990).

The problems and issues inhibiting the success of export promotion policies originated from both internal as well as external forces.

An internal obstacle on the domestic front being the erosion of international competitiveness of Sri Lankan exports due to unfavorable macroeconomic imbalances. Lack of stability and consistency in monetary, fiscal and exchange rate policies are crucial issues of concern in this regard. Despite the nominal depreciation of Sri Lankan rupee against the major trading partners, the rupee appreciated in real terms due mainly to higher domestic inflation. A high level of domestic credit expansion with inflationary deficit financing made it extremely difficult to manage the internal macroeconomic policies. For instance, during the past two decades budget deficit remained above 10 percent of GDP and it has increased to 23 percent of GDP in 1980, before it gradually declined to 9 percent in 1984. Moreover, domestic bank borrowings to finance the budget deficit also hasten to push up domestic inflation. Exporters and producers are affected by high cost, particularly by high interest rates which in turn erodes the international competitiveness of our exports.

Sri Lanka has been successful in diversifying her export structure by increasing the share of industrial exports to 60 percent of total exports. However, a large share of industrial exports depend heavily on imported input, therefore lowering the net foreign exchange earnings by 30 percent as against gross earnings. This problem resulted partly from the structural nature of the resources which has limited industrial raw materials for production input. Moreover, these products are less stable in the long run depending on the extent of special concessions and other international developments. For example, a large number of

enterprises operating in the Free Trade Zones are engaged in textiles and garments production based on foreign capital enticed by attractive fiscal and monetary incentives. At the end of the period of the tax holidays and other incentives, these firms will transfer their capital out of the country. Moreover, the level of production technology of the garments, toy manufacturing, rubber products, etc., are not highly advanced, thereby limiting the acquisition of a high level of technological know-how which would be beneficial in enhancing the industrial base of the country in the long run.

Compared with the industrial exports, agricultural products contain higher domestic value-added, and therefore high net foreign exchange earnings. However, expanding these exports are limited by several structural, institutional and technological constraints.

Some of the major issues which inhibit the effectiveness of export promotion policies on the external front are discriminatory tariff barriers and other indirect procedural restrictions imposed by major importers. As discussed earlier, lower domestic value-added has been one of the problems in promoting Sri Lanka's exports. Attempts are being made to improve domestic value-added by increasing the processing of natural resource-based products exported in primary forms. However, this effort is largely undermined by the structure of tariffs and other forms of trade barriers in major importing countries. For instance, zero or low rate of tariffs are applied by the industrial countries for their input of primary (unprocessed) commodities with duties increasing in proportion to the degree of processing a product undergoes. Such discriminatory tariffs have been taken as an indication of bias against imports of processed goods. Sri Lankan exports of rubber products, manufactured leather, processed fruits and beverages are among the Sri Lankan exports that are affected by these tariffs.

External developments in the EEC countries are critical in promoting the exports of Sri Lanka since nearly 25 percent of her exports are currently being exported to these countries. Although there are no specific tariffs or quota barriers to most of Sri Lanka's minor agricultural exports to the EEC, some products including gerkins, spices and foliage plants face heavy competition from similar products from the African and Caribbean countries which receive preferential market access to the EEC countries under the Lome Convention. In addition, the enhancing of

EEC standards also affect adversely the Sri Lanka's exports. The International Organization for Standardization (ISO) and the European Committee for Standardization (CES) signed an agreement in 1990. Consequently, international standardization will be basically dominated by the EEC standards which requires additional safety measures, such as the concern on public health and environment. Under these circumstances, it is necessary to make technological improvements to satisfy these conditions.

V. Policy Recommendations

(1) Maintaining Sound Macroeconomic Policies

Based on Sri Lanka's experience, stable macroeconomic policies that are conducive to export growth is the key in determining the success of export development strategies. If a country is able to manage relatively lower inflation rates and hence, the interest rates and lower level of budget deficits, it will guarantee the international competitiveness of her exports. In this regard, Sri Lanka has made some progress in the recent past in lowering the fiscal deficits and domestic credit expansion. Even though the overall deficit to GDP remained at 17.4 percent in 1992, domestic borrowings to finance deficits were contained at 3.6 percent of GDP. Moreover, the growth rate of broad money supply went down to 15.8 percent in 1992 compared with 23 percent in 1991.

(2) Institutional and Structural Changes

In view of the need to remedy the problem of changing the export structure towards more value-added industries, it is necessary to implement institutional and structural changes. The following recommendations are important in this respect:

(i) Traditional Agricultural Exports

(a) Tea: New type of products should be experimented in line with the changing international demand, i.e., expansion of CTC tea, green tea and tea-bag production.
(b) Rubber: Technical assistance to increase the process of rubber-based industries.

(ii) Non-Traditional Exports

(a) Setting up of village level production units with technical assistance to maintain the standards required by western markets.
(b) Expanding the extent of acreage or enhance multicropping methods of growing in order to guarantee adequate supplies on a continuous basis.
(c) Carrying out market research on the products to be exported to EEC countries which are not subject to high tariff barriers.

(3) Requirements for Changes

In line with the new developments in the international markets especially the emergence of European common markets, changes are required to cope with this situation since Sri Lankan exports are sizable in this region. However, more protectionist developments will also appear with non-tariff barriers in terms of anti-dumping laws, standardization and preferential treatments within the EEC. It is necessary to improve the quality standard and to identify new products that are to be promoted without affecting higher tariffs. For example, agricultural products which contain higher value-added should be promoted as duty-free items to the EEC.

Chapter 9

EXPORT PROMOTION STRATEGIES: THE REPUBLIC OF CHINA (ROC), TAIPEI

by
Susan M. F. Hwang

I. Introduction

Over the last four decades, the Republic of China (ROC), Taiwan has apparently moved from an underdeveloped economy to a newly industrialized economy. There are several factors that have contributed to this remarkable growth. One of the most important factors is the adoption by the Government of key policies and strategies which emphasized the need for improving ROC's foreign trade.

Export-oriented policy has played a vital role in ROC's economic development over the past forty years. In the 1950s, there were few exportable products in the island. The Government adopted import-substitution strategy to control foreign exchange expenditure and develop domestic industry. During the period, the share of exports in GNP did not rise much, but it increased significantly thereafter. The major export items were sugar and rice, comprising well over half the total exports until 1959. However, when the island's small domestic market became saturated, the Government shifted its policy to export expansion to further develop its industry and trade. This is an important stage of ROC's economy; the export-oriented policy successfully set forward a rapid economic growth path and a remarkable structural transformation. Beginning in 1971, the ROC has started to experience a trade surplus. As the economy entered the decade of the 1980s, the rising trend of protectionism and the stiff competition in global markets caused the Government to swing its policy to place equal emphasis on both exports and imports. At present, a balanced development of foreign trade is still the basic guideline of the nation's trade policy. Furthermore, the Government also aims to develop closer trade relation and cooperation with the international community.

This paper is organized as follows. Section II describes the most noticeable features of ROC's exports, including the relationship between exports and the nation's economy and the trend analysis. Section III

describes the major export promotion policies adopted by the ROC Government, including a historical review of its trade policy environment, and the role played by the Central Bank of China in the nation's export promotion strategies. Section IV points out some problems which have arisen on export expansion in recent years, and Section V offers some recommendations for policy making. Finally, Section VI summarizes and concludes this paper.

II. Export Trade and Salient Features

2.1 Contribution of Exports to the ROC's Economy

Foreign trade performance, especially in exports, is widely considered as a decisive factor in the successful development process of the Republic of China. In 1952, ROC's global trade value amounted to only US$ 304 million; by 1991, however, it reached a total amount of US$ 139 billion, ranking the ROC as the fourteenth largest trading country in the world. In just four decades, the ROC's trade value increased by more than four hundred times.

Taking a view of the contribution of foreign trade to GNP, the ratios of exports and imports to GNP are large and have grown rapidly, increasing to 42 percent and 35 percent, respectively, in 1991, from 9 percent and 15 percent in 1952 (see Chart 9.1). The ROC's economy has heavily depended on external trade. The share of employment in the manufacturing sector was only 12 percent in 1952. Following the export-oriented policy adopted in the 1960s, the agricultural sector has been gradually replaced by the industrial sector. The ratio of employment in the manufacturing sector to total employment increased to over 20 percent in 1970. By 1991, the share exceeded 30 percent. Meanwhile, the ROC's foreign exchange reserves (excluding gold) had soared to US$ 82 billion at the end of 1991, the highest level in the world, from only US$ 1 billion at the end of 1972. In just around twenty years, the foreign exchange reserves increased by more than eighty times.

2.2 Growth Trend and Changing Patterns of Exports

Foreign trade has played an important role in the development of the ROC's economy. The value of exports amounted to only US$ 116

million in 1952. As a result of a series of appropriate export promotion policies adopted by the Government, exports expanded significantly. During the period of 1961-1970, the average annual growth rate of exports was 25 percent, but in the period of 1971-1980, the rate went up to 31 percent (35 percent, if 1975 was excluded). During the 1980s, the growth of exports slowed down, while it still maintained an average rate of around 10 percent. By 1991, the value of exports amounted to US$ 76 billion, over six hundred times of that in 1952, and with an annual growth rate of 13 percent.

As can be seen in Table 9.1, the growth rates of imports revealed a similar pattern. The value of imports amounted to US$ 187 million in 1952, slightly higher than that of exports. But during the period of 1961-1970, its average annual growth rate was 18 percent, significantly lower than that of exports over the same period. The rate soared to 31 percent during the period of 1971-1980, the same as export growth rate over the same period, and it continued to grow at an average rate of 12 percent in the 1980s. In 1991, imports amounted to US$ 63 billion and its annual growth rate was 15 percent.

Chart 9.1
THE RATIO OF TRADE TO GNP

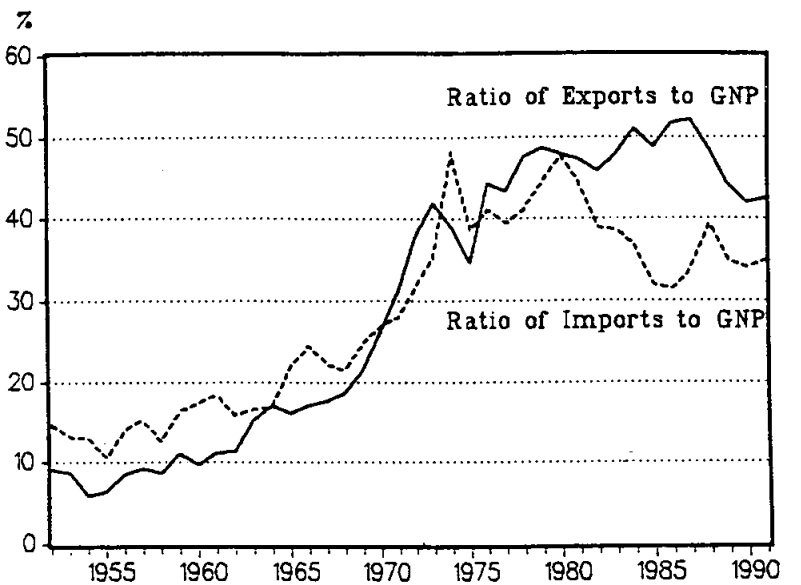


Table 9.1

AVERAGE GROWTH RATE OF FOREIGN TRADE

	Growth Rate of Exports	Growth Rate of Imports
1952-1960	6.8%	6.4%
1961-1970	25.3%	18.4%
1971-1980	30.8%	31.4%
(1975 excluded)	34.9%	36.5%
1981-1990	9.3%	12.1%
1991	13.3%	14.9%

Source: Department of Statistics, Ministry of Finance, *Monthly Statistics of Exports and Imports*, The Republic of China.

With the transformation of the economic structure, the composition of exports has shown a remarkable change. In the early days, agricultural products and processed agricultural products were the major items of ROC's exports. Their share accounted for 92 percent in 1952 and dropped to only 5 percent in 1991. In contrast, the share of industrial products in total exports rose from 8 percent in 1952 to 95 percent in 1991 (see Chart 9.2). Meanwhile, the composition of industrial products has revealed a great change in recent years. The share of exports of non-heavy chemical enterprises dwindled from 61 percent of total exports in 1981 to 49 percent in 1991, while that for heavy chemical enterprises increased from 32 percent in 1981 to 46 percent in 1991. The industrial structure has gradually shifted toward the heavy and chemical industries, a shift that was encouraged by Government's industrial upgrading policy (see Table 9.2).

The rapid growth of exports in the ROC was led by the manufacturing industry. Manufactured exports accounted for 93 percent of total exports in 1991. In the early period, food processing was the most important industry among the leading exports. By the 1960s, its place in exports was overtaken by textiles. Then, electrical machinery

expanded rapidly and replaced the position of textile industry in exports. In recent years, exports of electronic products, machineries, information and communication products, and transport equipment have expanded significantly, while exports of toys, garments and footwear shrank, reflecting the change in the industrial structure. By 1991, based on Standard Classification of Commodities of the Republic of China (C.C.C.) (in the ROC, SITC has been abolished since 1989), mechanical appliances and electrical machinery were the most important export products. The shares of vehicles and plastics to total exports have increased steadily. However, the shares of toys and footwear have declined yearly. Apparently, the capital- and technology-intensive products have gradually replaced the labor-intensive products.

Chart 9.2
EXPORT STRUCTURE

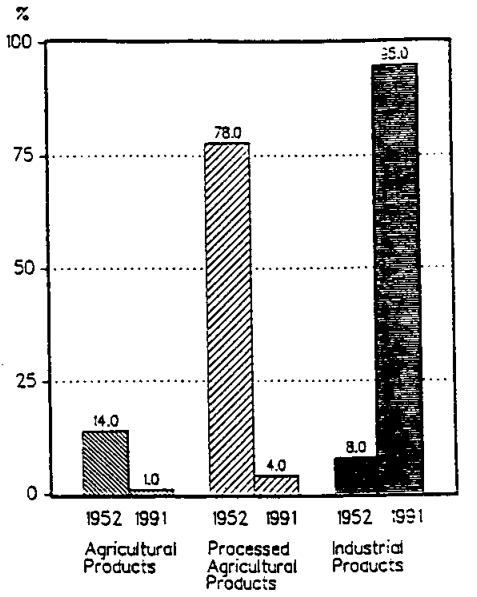


Table 9.2

EXPORT STRUCTURE
(Unit: Percent)

	Agri-cultural Products	Processed Agri-cultural Products	Sub-Total	Industrial Products	
				Heavy Chemical Enterprises	Non-Heavy Chemical Enterprises
1981	2.6	4.6	92.8	32.3	60.5
1982	2.0	5.1	92.9	33.2	59.7
1983	1.9	4.8	93.3	33.0	60.3
1984	1.7	4.3	94.0	34.0	60.0
1985	1.6	4.5	93.9	33.9	60.0
1986	1.6	4.9	93.5	34.1	59.4
1987	1.3	4.7	94.0	36.5	57.5
1988	1.4	4.1	94.5	41.3	53.2
1989	0.7	3.9	95.4	44.0	51.4
1990	0.6	3.8	95.5	45.9	49.6
1991	0.7	4.0	95.3	46.0	49.3

Source: Department of Statistics, Ministry of Finance, *Monthly Statistics of Exports and Imports*, The Republic of China.

The destination of the ROC's exports has concentrated primarily in the United States (US). The US share in ROC's total exports was about 20 percent in the 1960s. It continued to grow in the 1970s and 1980s, and reached a peak of 49 percent in 1984. Thereafter, it fell gradually to 29 percent in 1991. Another important export market is Japan. The share of total exports to Japan was about 25 percent in the 1960s. Thereafter, it dropped and touched the bottom of only 10 percent in 1983, and then recovered to 12 percent in 1991. In recent years, owing to a rapid increase in indirect exports to mainland China via Hong Kong, active direct investment abroad in South-East Asia, and significant achievements in respect of efforts to diversify ROC's export markets to European countries, exports to these areas have risen noticeably. Since 1990, the share of exports to Hong Kong has been

greater than that to Japan, and Hong Kong has surpassed Japan as the second largest market for ROC's exports. In 1991, the ratio of exports to Hong Kong to total exports was 16 percent, 4 percent more than that of Japan. The share of European countries also rose rapidly, from 8 percent in 1961 to 18 percent in 1991 (see Table 9.3).

Table 9.3
STRUCTURE OF EXPORTS BY DESTINATION
(Unit: Percent)

Year	USA	Japan	H.Kong	Europe	Others
1961	21.9	28.5	11.6	8.0	30.0
1971	41.7	11.9	7.8	9.9	28.7
1981	36.1	11.0	8.4	12.8	31.7
1982	39.4	10.7	7.0	11.7	31.2
1983	45.1	9.9	6.5	11.0	27.5
1984	48.8	10.5	6.9	10.1	23.7
1985	48.1	11.3	8.3	9.8	22.5
1986	47.7	11.4	7.3	12.0	21.6
1987	44.1	13.0	7.7	14.7	20.5
1988	38.7	14.5	9.2	16.3	21.3
1989	36.3	13.7	10.6	16.5	22.9
1990	32.4	12.4	12.7	18.2	24.3
1991	29.3	12.1	16.3	18.4	23.9

Source: Department of Statistics, Ministry of Finance, *Monthly Statistics of Exports and Imports*, The Republic of China.

As to the developments in balance of payments, because exports rose faster than imports (on the balance of payments basis) in 1961-1970, the trade balance improved. The surplus on trade increased further in 1973, as the ROC responded to the surge in world demand. However, the growth of exports fell dramatically in 1974, due to the first oil crisis and the worldwide economic recession at that time. The growth of imports, however, was still reflecting the upward trend of the early 1970s, and continued to rise. The combined result was a very

large deficit on trade balance in 1974. In 1975, the exports fell. The imports, however, dropped even more than the exports, so the trade deficit was reduced. In late 1975, exports recovered, and they rose strongly in 1976. Imports rose less rapidly, and in 1976, a trade surplus was once again achieved. Thereafter, the trade balance continued to exhibit surpluses, except in 1980, due to the second oil crisis. The surplus on trade increased rapidly in the 1980s, and reached a peak of US$ 20 billion in 1987. Then, it fell to US$ 16 billion in 1991, due mainly to the policy of an equal emphasis on both exports and imports, especially the endeavor for liberalizing imports.

The balance of current account exhibited deficits until 1970. The current account surplus increased further in 1972. However, owing to the first oil crisis and the poor state of the world economy, the current account showed deficits once again in 1974-1975. Thereafter, it continued to experience surpluses except in 1980. The current account surplus increased sharply in the 1980s. By 1991, the current account surplus was US$ 12 billion.

Non-monetary capital transaction has swung from a net inflow to a net outflow in 1984. After the Government relaxed the foreign exchange controls in mid-July 1987, non-monetary capital outflow increased. Thereafter, the net capital outflow rose significantly and reached a peak of US$ 11 billion in 1990, resulting from increases in direct investment abroad as well as purchases of foreign securities and real estate. By 1991, the non-monetary capital outflow plummeted to US$ 5 billion. The decrease in outflow was due mainly to a sharp drop in direct investment abroad and the appreciation of the new Taiwan dollar, which caused capital outflow largely to be offset by the capital inflow.

The balance of payments, as measured by the change in the net foreign assets of the banking system, has exhibited surpluses since 1981. The surplus continued to increase in the following years. In 1987, it reached a peak of US$ 20 billion, due mainly to the huge current account surplus in that year. Thereafter, it fell and touched the bottom of US$ 55 million in 1990, resulting from the enlarged private capital outflow. In 1991, the balance of payments surplus recovered to US$ 7 billion, as a result of the sharp drop in net capital outflow (see Table 9.4).

Table 9.4

MAJOR ITEMS IN BALANCE OF PAYMENTS
(Unit: Million US$)

Year	Current Account	Trade Balance	Net Services & Income	Non-Monetary* Capital Transaction	Change in the Net Foreign Assets of the Banking System
1970	1	105	-118	233	-134
1971	172	292	-132	68	-254
1972	512	647	-152	21	-607
1973	566	734	-168	227	-610
1974	-1113	-830	-295	461	597
1975	-589	-255	-341	621	149
1976	292	688	-416	884	-981
1977	911	1143	-237	351	-1132
1978	1639	2189	-522	437	-1951
1979	181	1320	-917	62	-21
1980	-913	77	-895	957	52
1981	519	1825	-1214	995	-1299
1982	2248	3646	-1263	739	-2589
1983	4412	6268	-1813	646	-4862
1984	6979	9233	-2087	-828	-5859
1985	9198	11173	-1726	-493	-9352
1986	16277	16917	-343	13	-16621
1987	17999	20285	-1590	1627	-20313
1988	10177	13834	-1733	-7514	-5180
1989	11384	16202	-2693	-8249	-3119
1990	10769	14928	-3424	-10725	-55
1991	12015	15754	-3488	-4731	-7329

* Includes private long-term and short-term capital.

Source: Economic Research Department, the Central Bank of China, *Financial Statistics Monthly*, Taiwan District, The Republic of China.

2.3 Empirical Analyses

In order to examine the nature of causality between exports and economic growth for the ROC, Granger causality test is used. The variables are growth rates of real exports and real GDP, with quarterly data from the first quarter of 1976 to the fourth quarter of 1991. The export unit price indices are used to deflate exports.

As shown in Table 9.5, the results of the test, from one lag to four lags, suggest that the growth rates of real GDP do not add significantly to the explanation of the growth rates of real exports, while the growth rates of real exports do play a significant role in explaining the growth rates of real GDP. The causality test reveals the conclusion that there exhibits a positive causality from export growth to economic growth in the Republic of China.

Table 9.5

RESULTS OF CAUSALITY TEST BETWEEN EXPORTS AND ECONOMIC GROWTH

Null Hypotheses:

(1) Growth rates of real export are not Granger Caused by growth rates of real GDP

(2) Growth rates of real GDP are not Granger Caused by growth rates of real export

	1 Lag		2 Lags		3 Lags		4 Lags	
	F-stat.	Prob.	F-stat.	Prob.	F-stat.	Prob.	F-stat.	Prob.
(1)	2.4629	0.1222	1.7166	0.1895	0.4683	0.6933	0.3387	0.8505
(2)	16.9845	0.0001	4.2956	0.0187	3.1898	0.0315	2.9009	0.0316

Results: Accept null hypothesis (1)
Reject null hypothesis (2).

Moreover, for the purpose of assessing the ROC's export performance, the export demand function is also examined empirically.

In a traditional export demand analysis, export is a function of gross domestic product of the major trading partners and the competitiveness of exporters which is affected by real effective exchange rates (the reciprocal of export competitiveness). Based on the ROC's quarterly export data, it can be found that the data exhibit the seasonal patterns (regular oscillatory movements). Therefore, the export demand function should include seasonal dummy variables. Furthermore, the foreign exchange rate system in the ROC has changed from a fixed system to a managed floating system since 1979. Therefore, another dummy variable is used to capture the policy change effect.

According to these considerations mentioned above, the long-run, or equilibrium, export demand function can be set in the form of natural logarithm as function (1):

$$\ln EX_t^* = a_0 + a_1 \ln WGDPt + a_2 \ln REERt + a_3 Q1_t + a_4 Q2_t + a_5 Q3_t + a_6 D_t + u_t \quad (1)$$

where, EX* = The desired, or long-run, demand for exports
WGDP = Real gross domestic product of the world
REER = Real effective exchange rate index
Q1 = 1 for the first quarter
= o otherwise
Q2 = 1 for the second quarter
= 0 otherwise
Q3 = 1 for the third quarter
= 0 otherwise
D = 1 under the managed floating exchange rate system
= 0 otherwise
$a_1>0$ and $a_2<0$

The coefficient a_1 represents the long-run income elasticity, a_2 represents the relative price elasticity.

In order to measure short-run elasticities, a partial adjustment model can be used, as follows:

$$\frac{EX_t}{EX_{t-1}} = \frac{EX_t^{*\,b}}{EX_{t-1}}, \quad 0<b<1 \quad (2)$$

or, $$\ln EX_t - \ln EX_{t-1} = b\,(\ln EX_t^* - \ln EX_{t-1}) \quad (3)$$

where, b is the coefficient of adjustment and $\ln EX_t - \ln EX_{t-1}$ = actual change and $\ln EX_t^* - \ln EX_{t-1}$ = desired change.

Now substitution of (1) into (3) gives the short-run demand function for exports:

$$\ln EXt = ba_0 + ba_1 \ln WGDP_t + ba_2 \ln REER_t + (1-b)\ln EX_{t-1} + ba_3 Q1_t + ba_4 Q2_t + ba_5 Q3_t + ba_6 D_t + bu_t \quad (4)$$

Once the short-run function (i.e., function (4)) is estimated and the adjustment coefficient, b, is obtained from the coefficient of $\ln EX_{t-1}$, the long-run function (i.e., function (1)) can be easily derived by simply dividing ba_0, ba_1, ba_2, ba_3, ba_4, ba_5, and ba_6 by 'b' and omitting the lagged lnEX term.

Using the quarterly data from the first quarter of 1976 to the fourth quarter of 1991, the regression results can be obtained as:

$$\begin{aligned} \ln EXt = {} & 1.0720 + \underset{(1.7091)}{} + \underset{(2.4589)}{0.3274}\ \ln WGDP_t - \underset{(-2.9286)}{0.4196}\ \ln REER_t \\ & + \underset{(12.2413)}{0.8214}\ \ln EX_{t-1} - \underset{(-3.4314)}{0.0664}\ Q1_t + \underset{(7.0150)}{0.1454}\ Q2_t \\ & + \underset{(2.9670)}{0.0552}\ Q3_t + \underset{(2.2481)}{0.0760}\ D_t \end{aligned} \qquad (5)$$

$R = 0.9904$ D.W. = 2.40 Durbin-h = -1.85

The estimated short-run demand function shows that the short-run income elasticity and relative price elasticity are statistically significant at the 5-percent level of significance. The coefficient of adjustment is b = 1 - 0.8214 = 0.1786, implying that about 18 percent of the discrepancy between the desired and actual exports is eliminated per quarter. To go back to the long-run demand function (1), all that needs to be done is to divide the short-run demand function by b and drop the $\ln EX_{t-1}$ term. The result is:

$$\begin{aligned} \ln EX_t^* = {} & 6.0023 + 1.8331\ \ln WGDP_t - 2.3494\ \ln REER_t - 0.3718\ Q1_t \\ & + 0.8141\ Q2_t + 0.3091\ Q3_t + 0.4255\ D_t \end{aligned}$$

It can be seen that both the long-run income and relative price elasticities are substantially greater than the corresponding short-run elasticities. Furthermore, the estimated Durbin-h is -1.85, leading to the acceptance of the hypothesis that there is no first-order serial correlation.

The empirical results obtained above suggest the conclusion that, for the ROC's export performance, the export competitiveness effect is stronger than income effect from major trading partners.

II. Export Promotion Policies

3.1 Review of Trade and Commerce Policy Environment

Rapid export expansion of the Republic of China has contributed greatly to the sustained and rapid economic growth of the country during the last forty years and has been more influential than any other factors in the economy. To promote its exports, the ROC Government has adopted a series of concrete measures to meet the needs according to the economic situation.

In the early 1950s, Taiwan was only an agricultural economy encountering many difficulties such as rampant inflation, budgetary deficits, trade deficits, a shortage of foreign exchange, and a lack of infrastructure and industrial development. To deal with all of these problems, the ROC Government essentially relied upon the import-substitution strategy. The major measures that are related to this strategy included import restrictions through high tariffs to protect infant industries such as textiles, flour and sugar, and a multiple exchange rate system to keep down the costs of essential imports. Throughout the period, the ROC's international trade was limited. The economic build-up focused on developing light industry, which in turn provided an industrial base that the Government could launch an export promotion strategy.

By the late 1950s, Taiwan's small domestic market had become saturated with the products of the import-substitution industries, while the Government continued to experience the difficulties of foreign exchange shortage. The current account of the balance of payments remained in heavy deficit. In the early 1960s, the Government thus shifted its policy emphasis away from import-substitution toward export expansion, which was a decisive move for the successful, rapid industrial growth of the 1960s and 1970s.

The promotion of exports and structural change began with the simplification of the multiple exchange rate system and the avoidance of overvaluation of the new Taiwan dollar. Then, the enactment of Nineteen-Point Economic and Financial Reform laid the foundations for ROC's "take-off" in the next two decades. Statute for the Encouragement of Investment was enacted to facilitate the acquisition of plant sites and to provide production incentives through tax

exemptions and deductions, which in turn provided a greater incentive to domestic saving, encouraged industrial investment, and promoted exports. Meanwhile, a special export loan program was made available on favorable terms to those industries engaged in export business. The export promotion measures also included the setting up of bonded factories and export processing zones, within which no duties were imposed on imports. In the mid-1960s, foreign companies began to be attracted to Taiwan by the improved environment and invested mostly in electronics, mainly for export.

In the 1970s, because exports and the economy expanded quickly, the Government adopted further measures to upgrade the level of industry and international competitiveness. These included the establishment of China External Trade Development Council (CETRA), a professional trade promotion institution in the ROC, to help small businesses enter and compete in world markets.

The rapid growth of light industrial exports created high demands for intermediate inputs and capital goods, most of which were imported from abroad. In the mid-1970s, the Government entered the second phase of the import-substitution strategy to promote the manufacture of intermediate inputs and capital goods to replace imports, to improve the country's infrastructure, and to shift to high value-added products. The export-oriented industrial structure then shifted rapidly toward the heavy and chemical industries. The trade deficit dropped significantly. Since 1971, the ROC has achieved a trade surplus position except in 1974 and 1975, due to the first oil crisis and the worldwide economic recession during that period.

As the economy entered the decade of the 1980s, the rising trend of protectionism, the competition in international markets, and the continuous appreciation of the new Taiwan dollar caused the Government to shift its trade policy away from export expansion toward an equal emphasis on both exports and imports. On the export side, the Government endeavored not only to upgrade its industrial structure to increase the competitiveness of the ROC's products in global markets but also to diversify its export markets to reduce the heavy dependence on the US market by exploiting the European and South-East Asian markets. As to the imports, the Government liberalized imports by opening the market, lowering tariff rates, loosening import controls, and relaxing the foreign exchange control.

In recent years, the ROC has been under the pressure for an economic transition. Traditional labor-intensive industries such as garments, textile, shoe-making and toys, have gradually lost their comparative advantages in world markets. For further growth and upgrading of ROC's industrial structure, the Government has made efforts to develop capital- and technology-intensive and high value-added industries, which in turn increases its competitiveness. Furthermore, the Government has focused on developing a closer trade relationship and cooperation with the international community.

3.2 The Role of the Central Bank of China

The Central Bank of China was first established in Canton province, China in 1924. In 1949, the Bank was evacuated with other government organizations to Taiwan. It resumed its operations on 1 July 1961.

As the banker's bank and the banker to the Government, the Central Bank of China has played a crucial role in export promotion of the Republic of China. It introduced the following measures in accordance with the government policies to help business enterprises solve their financing problems and to promote export sales.

3.2.1 Monetary Policy Measures

After resuming its operation in Taiwan, the Central Bank of China has offered export credit refinancing to local banks in order to promote export sales and accelerate the economic development.

In 1974, the Bank stepped up its rediscount financing of export loans, due to the sluggish export sales and deepening worldwide economic recession. To promote economic recovery, it raised the loanable ratio of export loans and reduced the Bank's discount rate and interest rate on such loans in the next year. In 1977, the Bank further stepped up its export refinancing and rediscounts of commercial bills to improve the investment environment.

In order to assist export industries to solve their financing problems, a special export loan program was initiated in 1957. Under such program, short-term loans were extended to finance the materials and work in progress of export enterprises. During the times of

economic recession, the Central Bank of China appropriated funds and reduced interest rates, including the export loans interest rate, to help export industries reduce their costs and improve their competitiveness of export products.

In 1973, the Bank appropriated funds for financing the imports of machinery and industrial raw materials by major export industries. In 1978, the bank earmarked funds for technology-intensive and major export industries to assist them in renewing equipment, increasing productivity and improving the quality of their products. In 1981, the Bank further appropriated funds to refinance infrastructure projects such as electricity and telecommunication development, etc., and, for export promotion, made loans to the small- and medium-sized enterprises.

3.2.2 Exchange Rate Policy

When the policy changed from import-substitution to export promotion in the 1960s, the foreign exchange policy also transferred from a multiple foreign exchange rate system into a unified exchange rate system. In 1963, the Bank promulgated a unified exchange rate and restored the normal buying and selling rates for foreign exchange. The unitary exchange rate could be applied to all kinds of exports and imports. The market exchange rate then was gradually stabilized and fixed at the rate of NT$ 40 per US dollar by the Bank. Because of the avoidance of overvaluation of the new Taiwan dollar by adopting the unitary exchange rate, exports were encouraged. In 1973, the Bank changed the basic exchange rate to US$1 = NT$38, which was mainly based on the consideration of the country's foreign trade, price structure, and economic growth. In 1978, the Bank promulgated a revised foreign exchange regulation to establish a managed floating rate system under which the new Taiwan dollar was de-pegged from the U.S. dollar. Since then, the value of the new Taiwan dollar has fluctuated. The fluctuation, however, had been very mild until 1981.

It is clear that the measures adopted by the Central Bank of China focused on providing funds to help export enterprises cope with financing problems and stabilizing foreign exchange rates to increase the competitiveness of export products. Following the changes of government policies, the Bank's measures were successful in financing export enterprises and promoting their export sales.

3.3 Nineteen-Point Economic and Financial Reform

Before 1958, the ROC Government adopted the import-substitution policy to reduce capital outflows and stimulate domestic industry. But, as the limited domestic market became saturated and foreign exchange earnings were urgently needed, the Government drew up plans to speed up the development of the economy in 1959.

In 1960, to meet the needs of a speedy economic progress and in anticipation of the termination of the US aid program after 1965, the Government enacted the Nineteen-Point Economic and Financial Reform Program which comprised fundamental reforms in the economic, financial and monetary systems. The basic objectives of the Nineteen-Point Economic and Financial Reform were as follows:

(i) to make a thorough review of various control measures taken in the past to liberalize those measures;
(ii) to provide private business with preferential treatment in the areas of taxes, foreign exchange settlements and financing;
(iii) to reform the tax system and its administration to enhance capital formation;
(iv) to reform the foreign exchange rate and to liberalize trade control; and,
(v) to broaden the measures that encourage exports, to improve procedures governing settlements of foreign exchange earned by exporters and to increase contacts with foreign business organizations.

The Nineteen-Point Program laid the foundations for ROC's "take-off" in the 1960s and 1970s and has represented the basic policy structure to-date which underlines the ROC's economic environment.

3.4 The Export-Import Bank of the ROC

To help ROC's exporters to minimize loss from export credit risks, the ROC Government established a specialized financial institution, the Export-Import Bank of the Republic of China, in 1979. The Bank assists local businesses by financing their export of capital goods and services and import of raw materials in addition to insuring their exports against political and commercial risks abroad. The Bank provides export

insurance to protect exporters against overseas political and commercial risks and assists those who apply for financing to facilitate export trade.

The Export-Import Bank of the Republic of China provides seven types of export insurance, which are Comprehensive D/P, D/A Export Insurance, Comprehensive Export Finance Insurance, Medium- and Long-term Export Insurance, Overseas Investment Insurance, Medium and Long-term Export Exchange Risk Insurance, General Comprehensive Export Credit Insurance, and Overseas Construction Insurance. These insurance policies have proven helpful in promoting the ROC's export sales and its economic development.

Besides the export insurance, the Bank also offers a wide range of financial support programs which include loans and guarantees to supplement the functions of local commercial banks for the promotion of the ROC's export sales.

The loans offered by the Bank include credits mainly for medium- and long-term exports, fixed-rate refinancing, overseas construction and investment, medium- and long-term imports, shipbuilding and technical services. Its guarantee provides protection against risks on debt obligations acquired by foreign suppliers and local exporters.

3.5 Fiscal Policy Measures

3.5.1 Regulations for Rebate of Taxes on Export Products

Before the export expansion strategy enacted during the period of 1958-1961, the "Regulations for Rebate of Taxes on Export Products" had been passed by the Executive Yuan in July 1955. It provided rebates of commodity tax, import duty, and defense surtax to encourage the processing of imported materials for export.

3.5.2 Investment Incentives

In 1960, besides the Nineteen-Point Economic and Financial Reform, another important legislation, the Statute for the Encouragement of Investment, was enacted to facilitate the acquisition of plant sites and provide production incentives through tax exemptions and deductions.

Major tax incentives provided by the Statute for Encouragement of Investment were as follows:

(i) Five-year income holiday: Productive enterprises conforming to the criteria prescribed by the Government could enjoy a five-year exemption from the business income tax.
(ii) Limit on income tax payable: The maximum rate of income tax, including any surtax, payable by a productive enterprise was limited to no more than 18 percent of its annual taxable income.
(iii) Tax exemption for undistributed profit: The amount of retained earnings used for the purchase of productive equipment was deductible from taxable income. The amount of exemption could be as much as 25 percent of the taxable income.
(iv) Tax deduction of exports: Two percent of the export sales of a productive enterprise was deductible from taxable income.
(v) Installment payments of import duties on industrial equipment: Productive enterprises that imported industrial equipment for their own use would pay import duties by installment schedule.
(vi) Exemption of export sales of productive enterprises from business tax.

It is clear that the Statute was aimed at promoting investment in productive enterprises and stimulating export sales. After it was put into effect, the whole economic performance improved. The volume of exports increased significantly and investment in many industries also increased rapidly. For the past several years, the ROC's economic environment has changed remarkably, and the Statute was often revised to meet the needs of economic development overtime. The Statute for the Encouragement of Investment expired at the end of 1990, and was replaced by the Statute for Industrial Upgrading.

3.6 Institutional Arrangements

3.6.1 Export Processing Zone

To attract investment to export-oriented industries, the ROC Government promulgated the "Statute for the Establishment and Management of Export Processing Zone" in 1965. Right after the

enactment of the Statute, the first export processing zone was set up in Kaohsiung, where export enterprises were granted exemption from import duties and other incentives. After its establishment, foreign and overseas Chinese investors poured into Taiwan, some investing directly in the zone, others setting up bonded factories at suitable locations outside the zone. In 1969 another two export processing zones were established in Nantze and Taichung. The export processing zones have been very successful in attracting investment from local and foreign enterprises and have created many jobs and also improved export performance in general.

Since the establishment of the first export processing zone in 1966, total exports from the three zones have accumulated US$ 36.5 billion (from September 1966 to the end of 1991). In 1991 alone, they exported US$ 4 billion of goods and provided jobs for 66,000 people.

In recent years, export enterprises in these three zones are facing the challenge of a steep increase in the cost of labor. So, the companies are shifting toward capital-intensive and technology-intensive types of production. Meanwhile, the ROC Government is planning to transfer the Kaohsiung Export Processing Zone to a high-technology industrial park.

3.6.2 Bureau of Commodity Inspection and Quarantine

To assure good quality of goods produced in the ROC, the Government conducts inspections on a wide variety of export products. These inspections have been handled by the Bureau of Commodity Inspection and Quarantine under the Ministry of Economic Affairs.

3.6.3 China External Trade Development Council (CETRA)

The ROC Government established China External Trade Development Council as a centralized trade promotion agency in 1970. CETRA provides local companies with business information, new market opening, and contacts establishment. In the meantime, CETRA also serves as the link between the Government and the local business community.

CETRA's major function is to combine the strength of the Government and the private sector to break through the barriers and

competition in international trade. The major services and assistance provided by CETRA are as follows:

(i) Marketing:
- provide face-to-face inquiry services and answer telephone inquiries,
- arrange meetings between overseas importers and local exporters,
- host trade shows at home to help visiting importers locate supply sources and meet the ROC's exporters,
- help local manufacturers take part in trade exhibitions abroad,
- assist overseas importers to hold purchasing shows in the ROC,
- conduct market surveys to find out more sources of raw materials and suppliers of industrial equipment,
- establish the ROC's trade centers abroad, which provide exhibition spaces, offices, warehouses and information to help local business open up foreign markets;

(ii) Information Services:
- furnish trade data and information to both overseas importers and local exporters,
- set up a trade information library to display the most up-to-date trade and economic information,
- publish materials for the reference of ROC's exporters;

(iii) Exhibitions:
- Provide CETRA-owned exhibition hall for long-term lease,
- design short-term trade shows to provide businessmen a chance to meet their customers;

(iv) Product Design Promotion:
- assist local manufacturers to improve product design and packaging,
- collect product design information and stage seminars and shows to promote better design and merchandising; and,

(v) Training of Talent:
- provide training courses to senior trading talents,
- hold short-term seminars on special topics to meet the needs of business personnel,

- provide a two-year course aiming to train trading experts for the future.

3.6.4 Hsinchu Science-Based Industrial Park

The Government established the Hsinchu Science-based Industrial Park in 1979 to adjust ROC's export structure by developing technology and capital-intensive industries so as to reduce the reliance on labor-intensive products. The park is designed to carry out industrial research and development work. It has attracted many foreign investors to establish factories manufacturing products that require advanced technology and high precision.

3.6.5 Vocational Training Centers

To develop technology-intensive industries producing for export, the ROC Government established ten vocational training centers to upgrade the labor quality and to boost productivity. In addition, it has been expanding, diversifying and modernizing the nation's vocational schools to prepare young people for productive services and to train them periodically in technology-related industries. In 1981, a vocational training bureau was established under the Ministry of the Interior to coordinate the supply of and demand for technical personnel to meet the needs of high-technology development.

3.7 Other Incentives

Many other export promotion incentives were provided by the Government and its agencies. For instance, the ROC Government promulgated the "Statute for Industrial Upgrading" to encourage enterprises to adopt technology-intensive, high value-added, low-energy consumption, and low-pollution-creating forms of export production. The amendment of laws and regulations to improve the investment climate also had a tonic effect on both export and industrial production. Meanwhile, the Government urged local businessmen to form their own big trading companies to cope with strong competition from large manufactures and large-scale traders in international markets.

IV. Problems and Issues on Export Promotion

Export expansion has been an important factor contributing to economic growth in the Republic of China. However, the persistent

trade surplus accumulated huge foreign exchange reserves, and exerted an upward pressure on the exchange value of the new Taiwan dollar, and also intensified trade friction with the US. Several critical challenges to the economy have arisen in recent years. In the 1990s, the Republic of China is facing new export promotion problems which can be classified as follows:

(i) Unbalanced trade;
(ii) Protectionism in overseas market;
(iii) Predominance of small- and medium-sized enterprises (SMEs);
(iv) Dependence on foreign technologies, imported machinery and raw materials;
(v) Lack of own brand names; and,
(vi) Increase in production cost caused by labor shortage, wage raise and increasing price for plant sites.

V. Policy Recommendations

To cope with the problems described above, the policies of the ROC Government focus on the following areas:

5.1 Continuous Expansion of Foreign Trade

In the Six-year National Development Plan, which was launched in 1991, the Government has set targets for the development of the nation's trade. According to the Plan, the annual export growth rate is expected to reach around 6.9 percent, and the annual import growth rate , around 10 percent. It is clear that trade policy in the Plan is aimed at balancing the development of foreign trade.

To achieve the targets set in the Plan, further market diversification and promotion strategies are encouraged to help enterprises expand their shares of world markets and to improve the nation's overall trade structure.

On the whole, the Government can further promote exports by opening up more export markets, helping prominent export industries, opening new trade territories, increasing overseas business relationship, and improving ROC's international status. For individual enterprises, the Government can assist them, through some related institutions, to achieve

cost reduction and secure high technology, to strengthen the business information collection and analysis, to set up more overseas sales network, to improve designing capabilities and product image, and to train more trade talents.

5.2 Upgrading the Industrial Structure

In the early stages of economic development when labor cost was comparatively low, the Government concentrated on developing light industries such as textiles and footwear. However, with increased labor cost in recent years, these industries have gradually lost their comparative advantages in international markets. To enhance the competitiveness of ROC's products in overseas market, a structural change must be pursued. To this end, a prompt movement from labor-intensive, light industries to technology and capital-intensive, heavy industries is the most important step to upgrade the industrial structure.

5.3 Promoting Big Trading Companies

In the past, ROC's small trading companies played an important role in helping the growth of the nation's export trade. However, the relatively smaller size of the trading companies were at a disadvantage when compared with their foreign rivals. These small companies lacked their own brand names and strong support from manufactures as well as financing resources and, therefore, do not have strong international marketing capabilities. Therefore, promotion of big trading companies is urgently needed, not only for trade development but also for the advancement of the industrial structure and the reduction of production cost.

5.4 Joining Important International Economic Organizations

With a spectacular performance in economic development, the ROC has an unavoidable obligation to contribute to the world and become more integrated into the world economy through bilateral and multilateral relations with other countries, especially in the area of international economic cooperation. In recent years, the Government has endeavored to join international organizations such as the GATT, IMF and World Bank, to improve the nation's international status. To further develop a closer relationship and cooperation with other countries, the ROC Government must persist in its efforts to actively

join more international economic organizations and share the "Taiwan Experience" with other countries.

VI. Summary and Conclusion

The export-oriented policy of the Republic of China, Taiwan has played a vital role in its economic development over the last forty years.

With limited natural resources, the trade strategy in the early years concentrated on restricting imports in order to protect infant industries and to reduce the cost of essential imports. In 1958, the Government moved to an export-oriented development strategy and the economic environment became conducive to exporting. The Nineteen-Point Economic and Financial Reform Program laid the foundations for the nation's future economic growth and stability in the 1960s and 1970s. The unitary exchange rate system also significantly encouraged exports. In addition, export loan program provided favorable interest rates for export financing to local export enterprises. The Statute for the Encouragement of Investment also promoted investment in productive enterprises and stimulated export sales. To help local exporters minimize loss from export credit risks, the Government established an Export-Import Bank, a specialized financial institution, to handle export insurance. The establishment of Export Processing Zones have been successful in attracting investment, creating jobs and improving exports. The Bureau of Commodity Inspection and Quarantine conducts export inspection to maintain the quality of goods. The establishment of China External Trade Development Council (CETRA), a professional trade promotion institution in the Republic of China, which provided further assistance to small businesses to engage and compete in international trade. Many other export promotion incentives were provided by the Government such as the establishment of vocational training centers and the enactment of the Statute for Upgrading Industries.

In recent years, the Government has changed its strategy to emphasize equally on both exports and imports, in view of protectionism and stiff competition in world markets. With foresight, the direction of trade policy is to liberalize, internationalize and systemize the market to achieve the potential of regional activities, to strengthen the nation's economic institutions and to revise laws and regulations to meet policy objectives.

The ROC's economy has long been noted for its successful choice of trade policies in the past years. When the policies and measures could no longer resolve new problems or difficulties, the Government is always ready to propose new strategies and introduce new policies. Despite the thoughtful measures and policies adopted by the Government, the economic miracle of the ROC was also achieved by its industrious people. At present, although the ROC is not considered a fully developed country, it is happy to share "Taiwan experience" to help the less developed countries in solving their economic development difficulties. Meanwhile, the Republic of China is glad to take up appropriate joint responsibility with the international community in contributing to the growth of the world economy.

REFERENCES

1. Board of Foreign Trade, Ministry of Economic Affairs, 1992, ***Trade Promotion in Chinese Taipei: CETRA's Achievements in the Past Twenty Years***, unpublished report.

2. The Central Bank of China, ***Annual Report***, various issues.

3. The Export-Import Bank of the Republic of China, ***Annual Report***, various issues.

4. Gujarati, Damodar N., 1988, ***Basic Econometrics***, second edition, McGraw-Hill, Inc.

5. Kuo, Shirley W.Y., G. Ranis and John C.H. Fei, 1981, ***The Taiwan Success Story***, Westview Press, Inc.

6. Li, K.T. (1990), *The Export Processing Zone — A Tool for Promotion Exports*, ***Industry of Free China***, July, pp. 1-7.

7. _____ (1990), *The Economic Transformation of the Republic of China: A Model of Success*, ***Industry of Free China***, November, pp. 1-11.

8. Mohsen B.O., M. Hamid and S. Ghiath (1991), *Exports, Growth and Causality in LDCs, A Re-examination*, ***Journal of Development Economics***, vol. 36, pp. 405-415.

9. Pai, Patrick P.Y. (1991), *Tax Policy and Economic Development in the Republic of China*, ***Industry of Free China***, December, pp. 47-56.

10. Siew, Vincent C. (1988), *Trade Policy of the Republic of China*, in ***Reference Papers on Economic Development and Prospects of the Republic of China***, edited by the Board of Foreign Trade, Ministry of Economic Affairs.

ROC, TAIPEI: COMPOSITION OF EXPORTS (Million US$)

Groups	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981
Live Animals; Animal Product												679
Vegetable Products												377
Animal or Vegetable Fats and Oils, etc.												2
Prepared Foodstuffs; Beverages, etc.												683
Mineral Products												528
Products of the Chemical												295
Plastics, Rubber and Articles Thereof												986
Raw Hides and Skins Leather Furskins, etc.												897
Wood and Articles of Wood, etc.												931
Pulp of Wood; Paper and Paperboard, etc.												167
Textiles and Textiles Articles												4777
Footwear, etc.												1932
Articles of Stone, Plaster, Cement Asbestos, etc.												391
Natural or Cultured Peals Precious, etc.												70
Base Metals												1533
Machinery and Mechanical Appliances, etc.												4982
Transport Equipment												841
Optical, Photographic, etc.												529
Arms and Ammunition, etc.												0
Miscellaneous Manufactured Articles												2009
Works of Art, Collectors Pieces, etc.												4
Total Exports	1481	2060	2988	4483	5639	5309	8166	9361	12687	16103	19811	22611

ROC, TAIPEI: COMPOSITION OF EXPORTS (Million US$)

1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992
569	751	839	969	1488	2037	1861	1793	1653	1958	
439	422	425	363	445	521	555	575	524	604	
2	2	10	3	3	4	9	8	19	16	
647	547	548	533	620	635	828	613	733	871	
538	616	670	664	519	521	499	494	455	499	
321	340	416	425	603	775	981	1058	1281	1572	
937	1120	1427	1589	2136	2970	3865	4336	4430	5171	
868	967	1079	1015	1223	1515	1433	1494	1316	1263	
784	906	925	848	956	1238	1312	1162	962	922	
162	145	130	157	253	314	443	505	609	750	
4605	4758	5850	6003	7303	9061	9313	10356	10285	11999	
1873	2283	2725	2759	3607	3421	4503	4484	4116	4424	
372	474	619	565	711	1092	1158	1143	1104	1162	
72	91	135	149	194	258	272	274	255	304	
1638	1958	2307	2354	2797	3628	4502	5192	5215	5806	
4584	5640	7466	7441	10141	15344	19172	21859	23131	26300	
1067	997	1186	1241	1702	2303	2456	3020	3449	3930	
530	560	641	614	829	1186	1454	1681	1721	2035	
0	0	0	0	0	0	0	0	0	0	
2189	2542	3055	3028	4325	5949	6043	6151	5828	6454	
4	3	3	5	6	6	9	11	39	18	
22204	25123	30456	30726	39862	53679	60667	66304	67214	76178	81480

ROC, TAIPEI: SELECTED INDICATORS (Million US$)

Groups	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979
Manufactured Exports										
Non-Manufactured Exports										
Services Exports			303	510	674	736	913	1055	1311	1760
Total Exports (Goods and Services)			3282	4986	6266	6040	8719	10549	13913	17589
Merchandise Imports (cif)	1524	1844	2514	3792	6966	5952	7599	8511	11027	14774
Services Imports			458	675	964	990	1196	1158	1771	2690
Export/Import Ratio	97.18%	111.71%	118.85%	118.22%	80.95%	89.20%	107.46%	109.99%	115.05%	109.00%
Trade Balance	105	292	647	734	-830	-255	688	1143	2189	1320
Current A/C Balance	1	172	512	566	-1113	-589	292	911	1639	181
Overall BOP	-134	-254	-607	-610	597	149	-981	-1132	-1951	-21
GDP at Current Prices (Billion NT$)	227	264	316	410	550	590	708	829	992	1196
GDP at Constant Prices (Billion NT$)	729	823	933	1052	1065	1117	1272	1402	1592	1722
Budgetary Surp./Def. (Million NT$)	2062	2516	2700	9781	25898	7598	16109	1335	6744	32709
Rate of Inflation		2.79	2.97	8.19	47.47	5.22	2.50	7.04	5.76	9.76
Consumer Price Index (1991=100)		27.27	28.08	30.38	44.80	47.14	48.32	51.72	54.70	60.04
Exchange Rate with US$	40.00	40.00	40.00	38.26	38.00	38.00	38.00	38.00	37.04	36.02

ROC, TAIPEI: SELECTED INDICATORS (Million US$)

1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992
	21995	21662	24484	29803	30098	39107	52788	59553	64225	62670	70537	
	616	542	639	653	628	755	891	1114	2079	4544	5641	
2025	2403	2289	2444	2678	2762	3805	4332	5871	7336	7214	8602	
21600	24811	24065	27472	32863	33231	43357	57629	66190	73210	74037	84137	
19733	21200	18888	20287	21959	20102	24181	34983	49673	52265	54716	62861	72000
2863	3356	3624	4329	5395	5508	6002	7985	10690	13455	14545	16474	
100.40%	106.66%	117.56%	123.84%	138.69%	152.85%	164.85%	153.44%	122.13%	126.86%	122.84%	121.18%	113.17%
77	1825	3646	6268	9233	11173	16917	20285	13834	16202	14928	15754	
-913	519	2248	4412	6979	9198	16277	17999	10177	11384	10769	12015	
52	-1299	-2589	-4862	-5859	-9352	-16621	-20313	-5180	-3119	-55	-7329	
1491	1774	1900	2100	2343	2474	2855	3223	3497	3879	4222	4712	
1848	1962	2032	2203	2437	2557	2855	3207	3443	3703	3884	4168	
23526	4486	-2974	2996	15105	12310	3543	45708	100700	126853	43059	6849	
19.00	16.33	2.96	1.37	-0.03	-0.16	0.70	0.52	1.29	4.40	4.13	3.62	4.46
71.45	83.12	85.58	86.75	86.72	86.58	87.19	87.64	88.77	92.68	96.51	100.00	104.46
36.00	36.84	39.11	40.06	39.60	39.85	37.82	31.77	28.59	26.40	26.89	26.81	25.33

ROC, TAIPEI: MERCHANDISE EXPORT: BY COUNTRY (Million US$)

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981
Total Exports	1481	2060	2988	4483	5639	5309	8166	9361	12687	16103	19811	22611
United States	564	859	1251	1677	2037	1823	3039	3636	5010	5652	6760	8158
Canada	51	115	140	171	205	182	313	276	327	415	460	568
Australia	20	35	52	108	191	126	224	243	334	419	539	677
Japan	216	245	377	824	844	694	1095	1120	1570	2249	2173	2454
New Zeland	1	2	2	6	11	7	10	12	18	29	36	50
Germany	71	88	135	215	306	316	422	418	572	743	1076	906
Italy	12	14	28	54	67	49	63	78	99	195	288	215
Switzerland	2	1	2	4	8	14	38	32	46	60	70	59
United Kingdom	14	30	56	112	150	138	163	272	323	406	472	566
Saudi Arabia	4	8	22	25	60	117	124	226	322	476	545	607
Iran	7	8	5	3	7	9	17	36	37	24	40	84
Kuwait	5	5	14	24	32	43	110	91	100	134	197	167
Indonesia	33	44	78	118	127	178	219	234	305	399	478	424
Korea, Republic	28	37	42	53	159	120	74	91	142	171	267	280
Malaysia	12	15	15	31	58	44	54	73	87	130	170	184
Myanmar	0	0	0	0	0	0	0	0	0	0	1	0
Nepal	0	0	0	0	0	0	0	0	0	0	0	0
Philippines	16	21	18	29	46	82	78	95	162	201	195	280
Singapore	36	46	73	130	135	141	214	233	296	422	545	589
Sri Lanka	0	0	0	0	0	0	2	2	0	4	25	32
Thailand	25	31	46	64	69	68	80	100	168	186	176	195
Hong Kong	136	160	229	296	338	363	610	638	858	1140	1551	1897
India	0	1	2	1	2	2	2	5	15	41	70	111
Pakistan	1	2	1	1	1	3	2	2	4	5	13	53
Bangladesh	0	0	0	0	0	0	1	4	6	9	7	5
Argentina	0	1	1	0	2	2	1	4	6	48	93	63
Brazil	5	2	2	5	9	6	4	3	7	11	15	12
South Africa	4	7	6	13	24	25	34	31	45	77	161	279
Kenya	1	1	2	2	3	4	5	10	12	14	19	12

ROC, TAIPEI: MERCHANDISE EXPORT: BY COUNTRY (Million US$)

1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992
22204	25123	30456	30726	39862	53679	60667	66304	67214	76178	81480
8758	11334	14868	14773	19014	23685	23467	24036	21746	22321	23572
510	728	916	945	1272	1561	1584	1759	1559	1624	1643
644	634	832	747	870	1103	1359	1538	1279	1354	1428
2369	2477	3186	3461	4560	6986	8772	9065	8338	9189	8894
54	55	73	76	120	173	212	224	195	194	201
788	854	871	807	1278	1993	2345	2578	3198	3869	3602
205	181	227	246	382	655	835	869	985	1027	1071
54	59	72	69	118	227	274	306	370	364	335
528	617	691	650	966	1548	1907	2102	1979	2072	2205
719	760	728	590	627	706	630	557	459	616	563
8	64	14	12	14	14	6	11	35	84	114
300	214	147	117	142	151	167	139	89	32	96
422	429	346	281	392	446	633	934	1246	1207	1216
199	223	230	254	352	638	917	1133	1213	1287	1151
222	224	232	195	206	272	451	695	1104	1465	1601
2	0	0	1	0	1	0	0	0	3	2
0	1	1	0	0	1	3	5	8	7	7
235	246	191	239	329	460	601	778	811	848	1023
562	711	878	885	931	1350	1683	1976	2204	2404	2508
11	54	58	56	94	98	110	124	164	190	194
214	264	245	236	279	425	754	1110	1424	1445	1810
1565	1644	2087	2540	2921	4123	5587	7042	8556	12431	15416
107	98	59	90	107	123	176	214	229	158	174
54	60	57	50	77	93	112	122	123	130	143
20	19	29	36	52	76	55	112	100	125	164
10	10	11	10	20	20	13	12	20	93	182
15	9	11	26	41	31	40	60	104	128	117
219	231	269	149	223	432	627	--	--	382	581
8	12	15	19	22	25	26	29	22	22	18

ROC, TAIPEI: MERCHANDISE IMPORT BY COUNTRY (Million US$)

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992
United States	364	408	543	953	1880	1652	1798	1984	2376	3381	4673	4766	4563	4648	5042	4746	5433	7648	13007	12003	12612	14114	15772
Canada	17	14	28	28	62	48	56	73	106	132	249	268	316	361	400	369	486	652	954	996	839	1040	1178
Australia	48	62	76	101	165	160	183	216	322	454	512	593	644	682	778	801	883	1000	1336	1631	1660	2018	2056
Japan	653	827	1046	1428	2215	1812	2451	2843	3678	4561	5353	5929	4780	5587	6442	5549	8255	11841	14825	16031	15998	16858	21790
New Zeland	3	2	8	14	14	23	31	36	39	49	59	67	71	90	90	75	91	134	166	210	191	266	289
Germany	62	80	92	203	475	371	352	277	412	636	722	648	788	696	772	849	1146	1665	2205	2660	2716	3013	3920
Italy	12	14	15	28	67	44	54	65	111	148	183	195	188	180	222	234	273	442	650	789	817	795	1002
Switzerland	15	12	13	42	77	40	50	39	77	115	151	191	105	135	149	140	205	463	1034	830	1200	991	1070
United Kingdom	26	30	37	73	158	127	165	178	244	296	289	302	270	308	294	282	357	792	1113	927	1154	1124	1337
Saudi Arabia	3	5	77	42	335	228	409	489	649	865	1419	1797	1969	1925	1971	1361	910	1075	1237	1375	1539	1679	1465
Iran	3	2	2	7	41	20	37	71	91	30	173	0	0	32	0	7	24	36	33	3	167	291	296
Kuwait	42	45	96	59	389	412	680	670	792	1155	2241	2244	1282	1132	728	671	443	730	489	434	369	36	224
Indonesia	12	21	46	101	182	168	201	314	320	452	540	467	260	345	423	414	357	567	613	706	921	1234	1406
Korea, Republic	15	10	13	42	68	59	87	102	146	177	209	301	233	165	244	187	329	533	900	1239	1344	1747	2301
Malaysia	29	32	44	62	82	58	105	148	227	329	425	453	470	494	551	481	501	729	943	887	1003	1409	1829
Myanmar	0	0	0	0	1	2	2	3	9	20	12	23	18	20	21	16	20	17	13	18	8	19	24
Nepal	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	3	0	0	0
Philippines	21	31	37	55	46	33	32	37	51	73	117	121	68	91	134	104	153	194	242	238	236	235	305
Singapore	5	8	19	27	53	36	38	91	83	124	222	199	152	167	268	278	340	522	740	889	1406	1446	1697
Sri Lanka	0	1	0	1	0	0	0	0	1	13	17	3	1	3	7	6	8	4	8	5	9	11	8
Thailand	41	27	42	57	177	70	92	98	61	74	90	117	107	74	140	147	163	200	342	390	448	586	825
Hong Kong	27	39	60	100	117	75	101	200	153	205	250	309	307	299	370	320	379	754	1922	2205	1446	1947	1781
India	6	8	3	6	12	12	26	26	22	30	51	42	18	50	28	24	48	101	92	135	215	241	218
Pakistan	0	0	8	7	2	0	1	0	2	2	8	8	5	16	23	65	136	138	104	161	141	216	220
Bangladesh	0	0	2	1	1	0	0	2	0	0	0	0	5	5	0	1	2	2	5	3	5	4	9
Argentina	8	15	6	8	18	7	33	67	63	52	42	18	21	63	37	30	32	30	77	136	57	106	98
Brazil	27	14	22	70	14	8	6	14	28	37	43	73	194	162	151	144	207	287	540	637	558	799	751
South Africa	3	6	35	33	32	93	98	88	145	215	273	370	224	225	189	207	326	790	999	--	--	564	1136
Kenya	0	0	0	0	0	0	0	0	1	1	0	0	0	0	0	0	1	0	3	2	2	2	3

ROC, TAIPEI: MERCHANDISE IMPORT/EXPORT (Million US$)

TAIWAN, CHINA	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992
Exchge. Rate/US$	40.00	40.00	40.00	38.26	38.00	38.00	38.00	38.00	37.04	36.02	36.00	36.84	39.11	40.06	39.60	39.85	37.82	31.77	28.59	26.40	26.89		
Exports-mil.US$	1481	2060	2988	4483	5639	5309	8166	9361	12687	16103	19811	22611	22204	25123	30456	30726	39862	53679	60667	66304	67214		
Exports-mil.Cur.	59240	82400	119520	171520	214282	201742	310308	355718	469926	580030	713196	832989	868398	1006427	1206058	1224431	1507581	1705382	1734470	1750426	1807384		
Exports-bil.LCur.	59.2	82.4	119.5	171.5	214.3	201.7	310.3	355.7	469.9	580.0	713.2	833.0	868.4	1006.4	1206.1	1224.4	1507.6	1705.4	1734.5	1750.4	1807.4		
United States	0.246	0.196	0.182	0.213	0.30	0.311	0.220	0.210	0.187	0.210	0.236	0.211	0.206	0.185	0.166	0.154	0.136	0.142	0.214	0.181	0.188	0.185	0.194
Canada	0.011	0.007	0.009	0.006	0.01	0.009	0.007	0.008	0.008	0.008	0.013	0.012	0.014	0.014	0.013	0.012	0.012	0.012	0.016	0.015	0.012	0.014	0.014
Australia	0.032	0.030	0.025	0.023	0.03	0.030	0.022	0.023	0.025	0.028	0.026	0.026	0.029	0.027	0.026	0.026	0.022	0.019	0.022	0.025	0.025	0.026	0.025
Japan	0.441	0.401	0.350	0.319	0.39	0.341	0.300	0.282	0.290	0.283	0.270	0.262	0.215	0.222	0.212	0.181	0.207	0.221	0.244	0.242	0.238	0.248	0.267
Germany	0.042	0.039	0.031	0.045	0.08	0.070	0.043	0.030	0.032	0.039	0.036	0.029	0.035	0.028	0.025	0.028	0.029	0.031	0.038	0.040	0.040	0.040	0.048
United Kingdom	0.018	0.015	0.012	0.016	0.03	0.024	0.020	0.019	0.019	0.018	0.015	0.013	0.012	0.012	0.010	0.009	0.009	0.015	0.018	0.014	0.017	0.015	0.016
Indonesia	0.008	0.010	0.015	0.023	0.03	0.032	0.025	0.034	0.025	0.028	0.027	0.021	0.012	0.014	0.014	0.013	0.009	0.011	0.010	0.011	0.014	0.016	0.017
Singapore	0.003	0.004	0.006	0.006	0.01	0.007	0.005	0.010	0.007	0.008	0.011	0.009	0.007	0.007	0.009	0.009	0.009	0.010	0.012	0.013	0.021	0.019	0.021
Thailand	0.028	0.013	0.014	0.013	0.03	0.013	0.011	0.010	0.005	0.005	0.005	0.005	0.005	0.003	0.005	0.005	0.004	0.004	0.006	0.006	0.007	0.008	0.010
Hong Kong	0.018	0.019	0.020	0.022	0.02	0.014	0.012	0.021	0.012	0.013	0.013	0.014	0.014	0.012	0.012	0.010	0.010	0.014	0.032	0.033	0.022	0.026	0.022
Korea, Republic	0.010	0.005	0.004	0.009	0.01	0.011	0.011	0.011	0.012	0.011	0.011	0.013	0.010	0.007	0.008	0.008	0.008	0.010	0.015	0.019	0.020	0.023	0.028
Malaysia	0.020	0.016	0.015	0.014	0.01	0.011	0.013	0.016	0.018	0.020	0.021	0.020	0.021	0.020	0.018	0.016	0.013	0.014	0.016	0.013	0.015	0.018	0.022
Italy	0.008	0.007	0.005	0.006	0.01	0.008	0.007	0.007	0.009	0.009	0.009	0.009	0.008	0.007	0.007	0.008	0.007	0.008	0.011	0.012	0.012	0.010	0.012
Saudi Arabia	0.002	0.002	0.026	0.009	0.06	0.043	0.050	0.052	0.051	0.054	0.072	0.079	0.089	0.077	0.065	0.044	0.023	0.020	0.020	0.021	0.023	0.022	0.018
Philippines	0.014	0.015	0.012	0.012	0.01	0.008	0.004	0.004	0.004	0.005	0.006	0.005	0.003	0.004	0.004	0.003	0.004	0.004	0.004	0.004	0.004	0.003	0.004
Exports Share %	0.901	0.781	0.728	0.736	1.04	0.931	0.750	0.736	0.705	0.739	0.770	0.728	0.681	0.638	0.593	0.524	0.501	0.533	0.676	0.648	0.657	0.673	0.720
TAIWAN EXPORTS (Million US$)																							
United States	364	408	543	953	1680	1652	1798	1964	2376	3381	4673	4766	4563	4646	5042	4748	5433	7648	13007	12003	12612	14114	15772
Canada	17	14	28	28	62	48	56	73	106	132	249	268	316	361	400	369	486	652	954	996	839	1040	1178
Australia	48	62	76	101	165	160	183	216	322	454	512	593	644	682	778	801	883	1000	1338	1631	1660	2018	2056
Japan	653	827	1046	1428	2215	1812	2451	2643	3678	4561	5353	5929	4780	5587	6442	5549	8255	11841	14825	16031	15998	18858	21790
Germany	62	80	92	203	475	371	352	277	412	636	722	646	788	698	772	849	1146	1665	2205	2660	2716	3013	3920
United Kingdom	26	30	37	73	158	127	165	178	244	296	289	302	270	308	294	262	357	792	1113	927	1154	1124	1337
Indonesia	12	21	46	101	182	168	201	314	320	452	540	467	260	345	423	414	357	567	613	706	921	1234	1406
Singapore	5	8	19	27	53	36	38	91	83	124	222	199	152	167	268	276	340	522	740	889	1406	1446	1697
Thailand	41	27	42	57	177	70	92	98	61	74	90	117	107	74	140	147	163	200	342	390	448	586	825
Hong Kong	27	39	60	100	117	75	101	200	153	205	260	309	307	299	370	320	379	754	1922	2205	1446	1947	1781
Korea, Republic	15	10	13	42	68	59	87	102	146	177	209	301	233	165	244	187	329	533	900	1239	1344	1747	2301
Malaysia	29	32	44	82	82	58	105	148	227	329	425	453	470	494	551	481	501	729	943	887	1003	1409	1829
Italy	12	14	15	26	67	44	54	65	111	148	183	195	188	180	222	234	273	442	650	789	817	795	1002
Saudi Arabia	3	5	77	42	335	228	409	489	649	865	1419	1797	1969	1925	1971	1361	910	1075	1237	1375	1539	1679	1485
Philippines	21	31	37	55	46	33	32	37	51	73	117	121	68	91	134	104	153	194	242	238	236	235	305
Total Exports:	1481	2060	2988	4483	5639	5309	8166	9361	12687	16103	19811	22611	22204	25123	30456	30726	39862	53679	60667	66304	67214	76178	81480

Chapter 10

EXPORT PROMOTION STRATEGIES: THAILAND

by
Nuannute Thana-anekcharoen

I. Introduction

Prior to the 1980s, agriculture was a dominant sector in the Thai economy both in terms of GDP and export shares. Main exports were rice, maize, rubber, tapioca products and mung beans. During the past two decades, the Thai economy changed significantly, with exports shifting from agricultural to manufactured products, such as textile products, precious stones, canned food, footwear and integrated circuits. The share of manufactured goods in the total export earnings has also increased from 6.1 percent in 1970 to 32.3 percent in 1980 and 74.7 percent in 1990.

The process of developing manufactured exports began in the third national development plan (1972-1976). In the 1970s, emphasis was placed on the promotion of manufactured exports, with the Thai Government initiating various facilities to support export industries, such as the Board of Investment's special privileges for export activities, import duty and tax refunds, bonded factories, export processing zones and export credit.

Many of the export promotion policy measures needed revision after implementation, while others were deemed inappropriate for later circumstances. However, from studying export promotion measures in the past, we have learned about actual problems which occurred and ways in which future policy measures should be formulated to promote exports.

II. Export Trade and Salient Features

2.1 Contribution of Exports to the Economy

Thailand has undergone a rapid transformation, from a predominantly agricultural-based society to an industrial economy

oriented towards manufacturing, services, and external trade. The share of manufacturing in the GDP has risen from 16 percent in 1970 to 25 percent in 1990, with most of the increase occurring during the past five years. Exports of goods and services have been the primary stimulus of growth, accounting for 50 percent of the growth in GDP from 1988 to 1989, and 31 percent of the growth from 1989 to 1990.

The primary engine of growth has been the manufacturing sector which expanded rapidly during the period of 1986-1990. As a result of vigorous promotion, exports from this sector have grown significantly in terms of their share of both GDP and merchandise trade. Manufactured products rose from 49.4 percent of exports in 1985 to 74.7 percent in 1990. During this period, the annual increase in total exports never fell below 20 percent. Manufacturing growth has helped rectify a basic imbalance on both the fiscal and external accounts and also enabled the Government in recent years to repay loans and to lower the debt-service ratio on long-term debt.

2.1.1 Contribution of Exports to Gross Domestic Product

The contribution of exports to GDP growth can be measured by the domestic value-added in the incremental exports. The estimates for Thailand in Table 10.1 are based on the share of merchandise exports to GDP in real terms and the share of manufactured exports to total exports. The contribution of incremental manufactured and total exports to GDP growth in each year can be estimated.

The percentage of overall GDP growth estimated to have been generated directly by export growth is called the "export reliance ratio". During the period 1986-1988, both this ratio (41 percent) and the level of GDP growth directly generated by export expansion (3.8 percent of GDP) reached exceptionally high levels by historical standards. A rise in the domestic value-added of this degree indicates that economic growth has been based on exports since 1986.

The broad industrial breakdown of GDP growth confirms that growth in manufacturing exports was the major driving force behind the GDP growth since 1986. Other factors also contributed significantly to growth particularly the initial external stimulus.

Table 10.1

CONTRIBUTION OF EXPORTS TO GDP GROWTH
(Period Averages; As % of GDP)

	1971-75	1976-80	1981-85	1986-88	1989-91
GDP Growth Rate	5.6	7.9	5.6	9.2	10.1
Contribution of:					
Total Exports	0.94	1.70	1.23	3.80	4.1
Manufactured Exports	0.38	0.56	1.03	3.08	3.66
Export Reliance Ratio a/	17	21	22	41	41

a/ The percentage of the GDP growth that is attributable to the value-added in incremental total exports

Sources: National Economic and Social Development Board and World Bank, 1989.

Table 10.2

SUPPLY STRUCTURE OF GDP GROWTH
(Period Average, As % of GDP)

	1971-1975	1976-1980	1981-1985	1986-1988	1989-1991
Agriculture	1.0	0.9	1.0	0.6	0.4
Crops	0.7	0.6	0.7	0.1	0.3
Other	0.3	0.3	0.3	0.5	0.1
Mining	0.0	0.3	0.1	0.2	0.5
Manufacturing	1.8	2.0	1.0	3.0	3.0
Construction	-0.1	0.5	0.2	0.4	1.0
Utilities & Transport a/	0.5	0.9	0.7	1.0	1.3
Wholesale & Retail Trade	0.9	1.3	0.8	1.8	1.9
Finance & Real Estate b/	0.5	0.5	0.4	0.8	1.3
Public Administration c/	0.3	0.5	0.4	0.2	-
Services	0.7	1.0	1.1	1.2	0.7
GDP	5.6	7.9	5.6	9.2	10.1

a/ Includes electricity, water supply, transportation and communication.
b/ Includes home ownership.
c/ Includes defense.

Sources: National Economic and Social Development Board and World Bank, 1989.

The major impetus for growth during the period 1986-1988 clearly came from the manufacturing sector. The contributions of the construction, utilities and transportation, trade, banking and services sectors all rose over the same period. This pattern indicates that the initial growth stimulus in the manufacturing sector had a broad ripple effect into most other sectors.

2.1.2 Contribution of Exports to Employment

The transformation in the Thai economy over the past 20 years from an agriculture-based economy to a modern labor-intensive industries has affected the sectoral distribution of employment.

Table 10.3

EMPLOYMENT DISTRIBUTED BY SECTOR
(Percent Share)

	1971	1980	1985	1986-1989	1990
Agriculture	78.8	70.6	66.0	61.6	58.9
Non-Agriculture	21.2	29.4	34.0	38.4	41.1
- Mining, electricity & water supply	0.7	0.7	0.6	0.7	0.7
- Manufacturing	3.9	7.9	8.9	9.9	10.9
- Construction	1.1	1.9	2.1	2.8	3.2
- Transportation & Communication	1.3	2.0	2.1	2.4	2.5
- Commerce, banking & insurance	7.1	8.5	9.9	11.3	12.0
- Service & public administration	7.1	8.4	10.4	11.3	1.8
Total Employment	100.0	100.0	100.0	100.0	100.0

Source: National Statistical Office: Labor Force Survey.

Employment in the manufacturing sector has increased rapidly due to the expansion in manufactured exports, most of which are labor-intensive. The ratio of employment in manufacturing to total employ-

ment increased from 3.9 percent in 1971 to 7.9 percent in 1980 and 9.9 percent during the period 1986-1989. The share of employment in the construction, banking and services sectors also increased significantly. However, the trend of employment in the agricultural sector had declined, partly due to the growing numbers of landless laborers caused by the emergence of land constraints, and also because of the modernization of agriculture with required capital input, which poorer farmers cannot afford. Therefore, the rapid growth in the manufacturing sector was able to absorb the excess labor force from the agricultural sector.

2.1.3 Contribution of Exports to Imports

While export growth was satisfactory during the export boom period (1986-1990), the imports also reflected the fact that the import content of manufactured exports remained at a high level, and thus the trade balance was adversely affected.

Table 10.4

PROPORTION OF TRADE IN GDP

	1970	1975	1980	1985	1987	1989	1991
Exports	10.9	15.1	20.2	19.1	23.9	29.1	29.4
Imports	19.6	22.4	28.7	24.8	26.7	37.3	41.7
Total Trade	30.5	37.5	48.9	43.9	50.6	66.4	71.1
Balance of Trade	-9.0	-7.3	-8.4	-5.7	-2.7	-8.2	-12.3
			Annual Growth Rate				
Exports	2.7	-9.6	22.8	-3.7	31.2	26.0	23.5
Imports	12.0	1.9	23.1	-9.4	42.0	27.6	15.7

Source: Bank of Thailand, *Monthly Bulletin*, various issues.

Table 10.4 shows that the proportion of imports in GDP was always larger than those of exports. The trade balance therefore grew wider.

2.2 Growth Trend and Changing Patterns of Exports

2.2.1 Structural Change in Type of Exports

Until 1970, exports of primary commodities, i.e., agricultural, forestry, fishery and mining products, made up 85 percent of total exports, with rice alone comprising 30 percent. Manufactured products, however, accounted for only approximately 6 percent of total exports. By 1980, manufactured products accounted for 32 percent of total exports, and primary commodities only 63 percent. This change reflected the shift in export structure in favor of manufactured goods, and the dramatic diversification of Thai exports.

In the early 1980s, the pattern of exports remained virtually unchanged from the late 1970s. Primary commodities continued to constitute the major share of total exports, with an average share of 58 percent during 1980 to 1984. Nevertheless, an increasing trend is observed for exports of manufactured goods since 1974, reflecting the Government's increasing emphasis on export-oriented production, which begun under the third five-year national economic and social development plan, and continued under the fourth and fifth plans (ending 1986), as opposed to the emphasis on import-substitution that prevailed in the 1960s. On the other hand, depressed prices of primary commodities in the world markets had significantly lowered export earnings of Thai primary commodities. Consequently, the composition of Thai merchandise exports had changed drastically in 1986, when manufactured goods recorded a 55 percent share in total exports. Manufactured goods that recorded large increases were textile products, integrated circuits, jewellery, canned fish, footwear, etc. Export earning from textile products was only about 12 percent of total export earnings in 1985 (Table 10.5).

During the 1970s, fifteen products, of which thirteen were primary commodities, accounted for nearly 80 percent of merchandise exports. By 1985 the share of the seven main primary exports (rice, tapioca products, rubber, maize, shrimps, tin and sugar) had fallen to less than 40 percent, and this commodity diversification has continuously increased throughout the 1980s. Within manufactured exports, the share of textile products, integrated circuits and jewellery has increased considerably in the last ten years. The sectors that have exhibited higher growth rates since 1985 are textile products, computers and parts, footwear, canned foods, furniture and parts, toys and jewellery (Table 10.6).

Table 10.5

STRUCTURE OF EXPORTS
(Percent Share)

	1970	1975	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
Manufactures	6.1	30.6	32.3	35.8	39.6	41.9	43.4	49.4	55.3	62.7	65.4	68.6	74.7	76.2
Primary Commodities a/	85.4	65.1	62.7	59.9	56.8	55.7	54.1	48.9	43.3	36.0	33.6	30.2	23.8	22.3
Others	8.5	4.3	5.0	4.3	3.6	2.4	2.5	1.7	1.4	1.3	1.0	1.2	1.5	1.5
Total Exports:	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

a/ Includes agricultural, fishery, forestry and mining products.

Source: Bank of Thailand, *Monthly Bulletin*, various issues.

Table 10.6

STRUCTURAL CHANGES IN EXPORTS
(Percentage)

1970		1975		1980		1985		1990	
Rice	17.0	Rice	13.0	Rice	14.6	*Textile products	12.2	*Textile products	14.3
Rubber	15.1	Maize	12.7	Tapioca products	11.2	Rice	11.6	*Computer & parts	6.6
Maize	13.3	*Sugar	12.7	Rubber	9.3	Tapioca products	7.7	Rice	4.7
Tin	11.0	Tapioca products	10.2	Tin	8.5	Rubber	7.0	Rubber	4.0
Tapioca products	8.3	Rubber	7.7	*Textile products	7.2	*Integrated circuits	4.3	Tapioca products	3.9
Jute products	4.9	Tin	5.0	Maize	5.5	Maize	4.0	*Precious stones	3.7
Mung beans	1.7	*Textile products	4.4	*Integrated circuits	4.6	*Precious products	3.3	*Integrated circuits	3.7
Shrimps	1.5	Shrimps	2.0	*Precious stones	2.4	*Sugar	3.2	Shrimps	3.5
Fluorite	1.5	*Precious stones	1.7	*Sugar	2.2	Tin	2.9	*Footwear	3.4
Tobacco leaves	1.3	Jute products	1.4	Shrimps	1.5	*Canned fish	2.7	*Sugar	3.0
Kapok fibre	0.9	Tobacco leaves	1.3	*Jute products	1.1	Shrimps	1.8	*Canned fish	2.7
*Precious stones	0.9	Sorghum	1.1	Mung beans	1.1	*Canned pineapple	1.7	*Precious stones	2.2
Sorghum	0.7	*Molasses	1.1	*Canned pineapple	1.0	*Footwear	1.2	*Furniture & parts	2.0
*Sugar	0.6	Cuttle fish	1.1	*Wood products	1.0	Mung beans	1.2	*Plastic products	1.5
Tungsten	0.6	Wood products	1.1	Tobacco leaves	1.0	*Jewellery	1.1	Frozen fowl	1.3
Top 15 Products	79.3	Top 15 Products	76.5	Top 15 Products	72.4	Top 15 Products	66.0	Top 15 Products	60.5
Others	20.7	Others	23.5	Others	27.6	Others	34.0	Others	39.4
Total:	100.0	Total:	100.0	Total	100.0	Total:	100.0	Total:	100.0

* Manufactured goods.

Source: Customs Department.

2.2.2 Direction of Export Market

Since the structural change in the composition of exports for the past two decades, Thailand's major export markets have also changed considerably. In 1970, Japan was the largest market for Thai exports, but in 1980, the European Community (E.C.) replaced Japan due to the increase in tapioca exports which contributed 40 percent of the total export value to the E.C. Since 1985, however, the major market for Thai exports has been the United States (U.S.), as a result of both strong growth in the U.S. relative to other trading partners and the effective pegging of the baht to the dollar (until November 1984), which induced a greater loss of competitiveness of Thai exporters relative to non-U.S. than to U.S. markets. The U.S. share in total exports surged from 12.6 percent in 1980 to 19.7 percent and 22.7 percent in 1985 and 1990 respectively (Table 10.7).

Table 10.7

DIRECTION OF EXPORT MARKET
(Percent Share)

1970		1980		1985		1990	
Japan	25.3	E.C.	26.0	U.S.A.	19.7	U.S.A.	22.7
E.C.	19.0	ASEAN	16.4	E.C.	19.1	E.C.	21.5
ASEAN	13.7	Japan	15.1	ASEAN	14.5	Japan	17.2
U.S.A.	13.1	U.S.A.	12.6	Japan	13.4	ASEAN	11.4
NICs 1/	12.5	Middle East	7.2	NICs 1/	7.5	NICs 1/	7.8
Middle East	3.5	NICs 1/	7.2	Middle East	7.2	Middle East	5.2
Others	12.9	Others	15.5	Others	18.6	Others	14.2
Total:	100.0	Total:	100.0	Total:	100.0	Total:	100.0

1/ Including Taiwan, Korea and Hongkong.

Source: Customs Department.

2.2.3 Trends in Imports

There have been relatively few changes in the import composition in the past 15 years. As industrialization proceeded, the shares of imports of consumer goods and intermediate goods have been more diverse in the 1980s than in the past years. For a country at Thailand's level of development, a short-term income elasticity of import is lower than the long-term income elasticity. After a decline for three years, imports at constant prices rebounded in 1983, probably due to the appreciation of the baht, as well as the income effect of the terms of trade improvement. The large increases in imports in 1987 to 1988 were due mainly to the income effect and the current growth in capital formation. The structure of imports by economic classification has changed marginally in favor of consumer goods since 1984. Currently, the share of oil to total imports is almost the same level as before the oil price shocks of the 1970s due mainly to low oil prices since 1986 coupled with a 5 percent reduction in import volume (Table 10.8).

2.2.4 Foreign Direct Investment (FDI)

Foreign direct investment in the form of foreign equity investment and direct loans to their subsidiaries has accounted for between 1.8 percent and 4 percent of gross domestic investment, and between 3 percent and 6 percent of private sector gross investment during 1981-1987. FDI has constituted a significant proportion of the total investment that has received promotional privileges from the Board of Investment (BOI). Data on BOI-approved projects in recent years showed that in the period 1987 to 1991, the number of promoted projects amounted to almost three times the number promoted in the two and half decades prior to 1987 (Table 10.9).

The tripling of FDI inflows in 1988 and continued rapid growth in 1989 and 1990 represents a significant inflow of new foreign investment. The FDI boom in the late 1980s was dominated by investors from Japan and the Newly Industrialized Countries (NICs) which accounted for more than 76 percent of FDI inflows from 1988 to 1990. This influx resulted mainly from the appreciating yen and NIC currencies, escalating labor costs in these countries, and Thailand's ability to maintain its competitive advantage as an export base.

Table 10.8

STRUCTURE OF IMPORTS
(Percent Share)

	1970	1975	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
1. Oil Imports	8.6	21.3	30.1	29.7	30.9	24.1	23.4	22.1	13.0	12.7	7.6	9.0	9.2	8.9
2. Non-Oil Imports	91.4	78.7	69.9	70.3	69.1	75.9	76.6	77.9	87.0	87.3	92.4	91.0	90.8	91.1
2.1 Consumer goods	19.3	12.7	9.9	8.3	9.1	9.4	9.2	13.6	9.8	9.7	7.6	8.4	8.9	8.9
2.2 Intermediate goods	24.9	24.1	23.2	26.5	27.0	28.1	28.4	25.7	33.9	34.4	35.3	35.4	32.9	33.0
2.3 Capital goods	34.7	33.3	24.9	27.0	24.5	29.5	30.0	31.0	31.4	33.0	37.8	36.5	39.4	40.6
2.4 Others	12.5	8.6	11.9	8.5	8.5	8.9	9.0	7.6	11.9	10.2	11.7	10.7	9.6	8.6
3. Total:	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Bank of Thailand, *Monthly Bulletin*, various issues.

Table 10.9

NET INWARD FOREIGN DIRECT INVESTMENT (FDI)
GROSS DOMESTIC INVESTMENT
(Million Baht)

Year	FDI Inflows	Gross Domestic Investment	FDI as % of Gross Domestic Investment	Gross Private Investment	FDI as % of Gross Private Investment
1970	890	37731	2.4	24566	3.6
1975	1745	81134	2.2	53676	3.3
1980	3878	174045	2.2	107104	3.6
1981	6414	199723	3.2	120059	5.3
1982	4331	189577	2.3	125793	3.4
1983	8225	236090	3.5	144808	5.7
1984	9644	242506	4.0	156546	6.2
1985	4442	243949	1.8	148363	3.0
1986	6908	238643	2.9	155087	4.5
1987	9044	299790	3.0	218868	4.1
1988	27964	434546	6.4	329614	8.5
1989	45698	559707	8.2	457891	10.0
1990	64695	753952	8.6	619600 1/	10.4
1991	51389	912500	5.6	721200 1/	7.1

1/ Estimated by the Bank of Thailand.

Sources: Bank of Thailand.
National Economic and Social Development Board.

The traditionally dominant role of the U.S. has declined significantly in the past five years, and European investment has stagnated. However, FDI data from 1991 indicated that American and European investment is picking up again (Table 10.10).

Table 10.10

NET FLOWS OF FOREIGN DIRECT INVESTMENT BY COUNTRIES

	1970	1975	1980	1985	1986	1987	1988	1989	1990	1991
Net FDI Inflows (Bil. Baht)										
U.S.	0.4	0.8	0.7	2.4	1.3	1.8	3.2	5.2	6.2	5.9
Japan	0.3	0.4	0.9	1.5	3.0	3.3	14.6	18.8	27.9	15.6
EC	0.1	0.3	0.5	0.4	0.5	0.9	2.2	3.8	4.2	4.0
NICs 1/	0.1	0.1	1.4	0.3	1.5	2.0	7.8	13.8	20.8	21.1
Others	-	0.1	0.4	-0.2	0.6	1.0	0.2	4.1	5.6	4.8
Total:	0.9	1.7	3.9	4.4	6.9	9.0	28.0	45.7	64.7	51.4
Shares in Total (%)										
U.S.	44.5	47.1	17.9	54.5	18.8	20.0	11.4	11.4	9.6	11.5
Japan	33.3	23.5	23.1	34.1	43.5	36.7	52.1	41.1	43.1	30.3
EC	11.1	17.6	12.8	9.1	7.3	10.0	7.9	8.3	6.5	7.8
NICs	11.1	5.9	35.9	6.8	21.7	22.2	27.9	30.2	32.1	41.1
Others	-	5.9	10.3	-4.5	8.7	11.1	0.7	9.0	8.7	9.3
Total:	100.0	0.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

1/ Include Singapore.

Source: Bank of Thailand.

III. Export Promotion Policies

3.1 Review of Trade and Commerce Policy Environment

Since 1961, the Thai Government has started the Five-Year National Development Plans, prepared by the National Economic and Social Development Board (NESDB). In the first two Plans (1961-1971), the Government emphasized the promotion of private investment in import- substituting industries, and the use of domestic raw materials. The Government also encouraged joint-ventures between Thai and foreign investors and supported small-scale and cottage industries in order to promote employment. In addition, the Government tried to restrict the establishment of new public enterprises which would compete with the private sector. The main task of the Government is to invest heavily in the development of infrastructure, such as transports, telecommunications, dams and electricity, etc.

Many of the consumer goods industries grew rapidly in the 1970s, thus saturating the domestic market which can no longer provide an engine for continued rapid growth. The efficiency costs of the aggressive protectionist and anti-export policies were increasing. However, during the 1960s and 1970s, imports increased at an average annual rate of around 16 percent. As a percentage of total imports, consumer goods declined from 31 percent in 1962, to 19 percent in 1970, of which raw materials and intermediate products, and capital goods, increased from 19 percent and 28 percent to 25 percent and 35 percent respectively. Thailand's import dependency, therefore, appears to have merely shifted from consumer goods to raw materials and capital goods.

Since the late 1960s, the Thai economy was able to meet the balance of payments deficits. These deficits were due to high level of imports of machinery and raw materials, the stagnation of primary exports, the decline in U.S. military spending in Thailand, and the decline in foreign investment. Therefore, the Government turned to manufactured export promotion policies in the third plan (1972-1976), with the confidence that export demand would be a major impetus for the expansion in production and national income. Moreover, export earnings would enhance the ability to import capital goods or other goods essential for the country's development, whilst reducing the reliance on external capital.

During the fourth plan period (1977-1981), the Government indicated its desire to encourage linkages between industry and agriculture, to promote small-scale and labor-intensive industries, and to spread industries into the rural areas. The impact of the second oil shocks on developing countries between 1979 to 1982 has been extremely severe. Developing countries were hit from three sides - deteriorating terms of trade, declining growth of export volumes due to OECD recession, and rapidly growing debt-service obligations due to rising interest rates. Thailand suffered as badly as most developing countries in 1981 and 1982, effectively losing 10 percent of its total national product.

The fifth plan (1982-1986) set out the objectives for industrial structural adjustment reforms in the 1980s. The major components of the industrial policy included: (i) a comprehensive examination and rationalization of the tariff structure; (ii) an overhauling of the existing structure of industrial incentives; and, (iii) the improvement and further development of measures to promote the growth of manufactured exports.

In addition, the Government stated its intention to promote regional development, to support the growth of small- and medium-scale industrial enterprises, to encourage the development of labor-intensive activities, and to establish procedures to evaluate large-scale investment projects.

With the exception of initial progress, the policy soon lost its momentum during the plan period. A major attempt at tariff reform in October 1982 was only partly successful and the exchange rate became progressively overvalued. The reforms in investment incentives did not progress very far, and efforts towards restructuring of key sub-sectors faded. Little progress was made towards improved policy coordination While export promotion policies were strengthened to offset the anti-export bias embedded in the protection regime, they remained partial in scope and had limited impact.

In late 1984, the Government took several steps in response to the deteriorating macroeconomic and trade environment. These included the devaluation of the baht, the adoption of a more flexible exchange rate policy and the elimination of the general import duty surcharge. However, with continued revenue shortfalls, a new and wide-ranging

set of tariff adjustments was adopted in April 1985, partly offsetting the beneficial impact on incentives of the earlier tariff adjustments. The net impact of tariff adjustments for the 1980-1985 period, nevertheless, remained positive, particularly for the manufacturing sector. Also, on the positive side, steps taken towards reducing the role of quantitative restrictions, and price and industrial controls, were not reversed. Overall, however, progress on trade and industrial policy has fallen short of the objectives set under the fifth plan. External circumstances and tight fiscal constraints were undeniably major impediments to policy adjustments. But the difficulties encountered also point to the need for a closer scrutiny of the design and implementation of the various policies.

The sixth plan (1987-1991) aimed to improve the structure of production and basic services of the country by diversification, thus reducing risks, lowering production costs and improving the quality of goods and services and enabling stronger competition with foreign countries. During the period 1986-1989, the Thai economy achieved rapid economic growth, which was widely attributed to the success of manufactured exports and a tremendous influx of FDI in export-oriented projects.

The sustainability of the boom was greatly enhanced by a sharp improvement in the fiscal position, and thus, the current account deficit remained well below the levels of the previous decade. By late 1989, it had become clear that the strength of the Thai economy had brought with it a number of problems - infrastructural bottlenecks, shortages of skilled labor and inflation. However, the overheating of the economy in 1990 put mild pressure on domestic inflation which was aggravated by the surge in oil prices in the second half of the year. Input costs rose and productivity growth was curtailed.

For accelerated industrial development in the 1990s, market liberalization has become an important program. In May 1990, the money market and exchange rate were liberalized so as to promote Thailand's role as a regional financial center, and attract foreign investment. On the trade side, tariffs on capital goods used in manufacturing were reduced from 20 percent to 5 percent in October 1990, and the tariff exemptions or reductions on these goods that could previously be granted by the BOI were abolished. This should not only simplify both the tariff and the investment incentive system, but should also particularly benefit small exporting firms that profit less from the BOI incentives.

The second package of tariff reforms is expected to include reductions in tariffs on raw materials, intermediate products and certain capital goods, and some finished products, with the aim at benefiting exporters and exporters' suppliers who have been unable to gain from the BOI exemptions or to participate in the various duty drawback schedules.

In the seventh plan (1992-1996), Thailand expects to sustain satisfactory growth, and to maintain high levels of industrial output. Thai export products and their markets are becoming more highly diversified and better established as private investment increases, and new firms enter into production. This is encouraged by improved prospects for regional trade in Asia, and Indo-China, as well as in Eastern Europe. Furthermore, new opportunities for the expansion of Thailand's industrial production base, particularly in petro-chemicals, engineering, and other basic industries, are emerging. The country is making a serious effort to enhance production efficiency by introducing appropriate production technology, and by training new generations of workers in modern work methods.

3.2 Role of Central Banks

The most important role of a central bank is to maintain the stability of the currency in order to build up a strong base for the financial system, and consequently stable economic growth. The central bank's role in developing countries however is wider than those in the developed countries.

Many factors prompted the central bank in developing countries to be the key organization in the process of economic development; these factors are, e.g., the inefficiency of public organizations, the shortage of professional in certain areas, and the lack of initial fund for operation.

As capital funds are often at the core of the development of various economic sectors, central banks have to assure the adequacy of funds as well as preempt the shortage of funds in priority sectors. To alleviate fund shortages, the Bank of Thailand's (BOT) direct assistance to priority sectors, such as lending through institutions or rediscounting of promissory notes arising from promoted undertakings, is important. The format of direct assistance includes not only lending

facilities, but also subsidized interest rates so as to reduce the interest burden on undertakings which deserve promotion. Nonetheless, the aforementioned fund allocation must be carefully administered to ensure benefits to the economic system as a whole, and the financial support should not be excessive as to exert unfavorable impact upon the country's financial stability. The role of the BOT in promoting export is as follows:

3.2.1 Export Credit

The BOT's export credit was introduced in 1958, in the form of a rediscount facility, which allowed commercial banks to use documents other than government securities as collateral for loans from the BOT for financing rice exports. In 1960, the BOT reviewed its regulations relating to export rediscounting, and since that time exporters of any kind of goods have been able to use the facility.

Promissory notes rediscounted by the BOT must be issued by creditworthy exporters as approved by both a commercial bank and the BOT and must be supported by documents such as an irrevocable letter of credit, contract or order, warehouse receipt, or bill of exchange.

The maturity period of the export refinancing was extended from 90 days to 180 days in 1983. Export credit was covered either for pre-shipment or post-shipment credit.

The amount of rediscounted finance to be granted depends on the supporting documents provided by the exporter, which are as follows:

(i) not more than 70 percent of the face value of the contract or order;
(ii) not more than 80 percent of the face value of the letter of credit;
(iii) not more than 40 percent of the face value of the estimated amount of goods in the warehouse receipt; and,
(iv) not more than 90 percent of the face value of the bill of exchange.

In 1978, the BOT started a scheme to help small exporters (i.e., those with less than B 5 million in operating capital) by providing them a special rediscount facility with a credit allowance of up to 100 per-

cent of the face value of the essence export bill, but not more than B 500,000.

The rediscount rate charged by the BOT is a concessionary rate of 5 percent per annum and the commercial banks are allowed to charge exporters not more than 7 percent per annum. This gives the commercial banks a 2-percent margin for handling the rediscount transaction.

In October 1984, the rediscount rates were changed to 7 percent for promissory notes, for which commercial banks charged exporters 9 percent, for large exporters and those exporting general products. On the other hand, small exporters and those exporting manufactured goods which were promoted by the BOI were charged a concessional rate of 8 percent annually, with the commercial banks paying a 5-percent annual rediscount rate to the BOT. Due to the decline in general interest rates in March 1986, the rates for the former were changed to 5 percent and 7 percent, and for the latter to 4 percent and 7 percent.

Another change in policy regarding the refinancing of export bills was the introduction, in April 1985, of the initial phase of the Domestic Letter of Credit (LDC) scheme for manufacturing firms that complemented the BOI promotion of international trading firms. The rediscount rate charged by the BOT on these notes was the same as for other rediscounted export bills.

In 1988, the criteria of export refinancing were changed, with the BOT rediscounting only 50 percent of the face value for any type of export bill.

As the amount of exports increased, the volume of the rediscount facilities has also been rising steadily during the past decade. Export bills which were rediscounted by the BOT have increased from US$ 43 million in 1970 to US$ 2092 million in 1980 and US$ 4366 million in 1988. The amount then declined to US$ 3504 million in 1991, accounting for 12.2 percent of total export value (Table 10.11).

3.2.2 Exchange Rate Policy to Promote Exports

During the 1970s, the value of the Thai baht relative to the U.S. dollar was very stable. This was evident from the fact that during the

Table 10.11

BOT REDISCOUNTS OF PROMISSORY NOTES FOR EXPORT ACTIVITIES BY COMMODITY, 1970-1992
(In Million US$)

Year	Agriculture Products	Manufacturing Products	Others	Total
1970	n.a.	n.a.	n.a.	43.4
1975	n.a.	n.a.	n.a.	511.9
1980	673.9	1277.8	140.7	2092.4
1981	659.3	1635.7	167.0	2462.0
1982	955.7	1543.3	194.3	2696.3
1983	1098.5	1793.8	208.8	3101.1
1984	1249.6	1916.7	293.3	3459.6
1985	978.9	1619.2	422.8	3020.9
1986	986.0	1782.2	504.0	3272.3
1987	1269.3	1469.2	21.0	2759.5
1988	2001.5	2331.5	33.5	4366.4
1989	1256.1	1300.1	74.6	2630.8
1990	1301.6	1509.8	111.6	2923.0
1991	1565.0	1896.4	43.0	3504.4
Jan-Oct 1992	1387.7	1219.2	279.9	2886.8

Source: Bank of Thailand.

period from 1973 (the beginning of first oil crisis) to 1978, most countries had to adjust their exchange rates several times either to remedy the balance of payments deficits, or to keep in line with the volatility in the international foreign exchange markets. In the case of Thailand, only two adjustments in the baht value were made in 1973 (in March, the baht was devalued by 10 percent in terms of gold; and, in July, it was revalued by 4 percent against the U.S. dollar). Since then, the exchange rate between the baht and the U.S. dollar remained constant at B 20 per U.S. dollar. In 1978, the authorities became aware of the

need to conduct a more flexible exchange rate policy, so that it could be used as a supplementary measure to maintain the economic stability of the country. Thus, legislative changes were made in order to allow the external value of the baht to be determined by a basket of currencies of major trading partners. According to the daily fixing system, the exchange rate between the baht and U.S. dollar moved from B 20.00-20.37 per dollar in 1978 to B 20.67-21.0 per dollar in the first half of 1981.

Realizing that Thailand's export prospects would be damaged if the baht was permitted to appreciate continuously with the dollar, the baht was then devalued by 8.7 percent with respect to the dollar and remained fixed at B 23 = US$1 in July 1981. During the period of July 1981 to November 1984, since the dollar appreciated against other major currencies, the baht also appreciated on a trade-weighted basis. Therefore, the baht was devalued by 14.8 percent against the dollar in November 1984, and since then the baht has been pegged to a basket of currencies. Due to the devaluation, the real exchange rate and price competitiveness were improved substantially with the U.S.

From the description of Thailand's experience in exchange rate management, it can be seen that the authorities have on several occasions used the exchange rate as a tool to mitigate the effects on trade of foreign exchange volatility.

3.3 Fiscal Policy

Recently, the Government has placed a high priority on improving the incentive environment for exporters in order to promote the development of manufactured exports. In particular, efforts have been made in late 1970s to promote the development of manufactured exports. These included the provision of special BOI incentives to exporting firms, and the establishment of a variety of import duty drawback and exemption schemes to improve the competitiveness of Thai exporters.

3.3.1 BOI Incentives

The BOI is the principal government agency responsible for administering incentive to encourage industrial development.

According to the 1972 Investment Promotion Act, the BOI can grant one or more of the following special privileges to promote export-oriented activities:

(i) Exemption from both import duties and business taxes on imported raw materials and components;
(ii) Exemption from both import duties and business taxes on re-exported items;
(iii) Exemption from business taxes for producers or sellers of domestic raw materials which are supplied to export-oriented activities;
(iv) Exemption from both export duties and business taxes on products or commodities exported; and,
(v) Permission to deduct from the profits on which corporate income tax is assessed an amount equal to 2 percent of any increase in income derived from export activities over the previous years, excluding costs of insurance and transportation.

In 1977, the law was revised, the above privileges remained the same, except that the taxable corporate income deduction was raised to 5 percent. In addition, promoted projects were granted exemptions from corporate income tax for another year if the foreign exchange earnings generated amounted to at least US$ 500,000 annually during the first three years of operation.

The BOI has set up a range of export conditions on certain activities which are eligible for promotion. In addition to the provision of extra privileges to export-oriented firms, the BOI also developed a streamlined procedure to enable certain large exporters under BOI promotion to avail themselves more easily of the exemptions of import duties and business taxes on imported input.

The BOI's attempts to encourage export-oriented activities in recent years are reflected in the number of export-oriented projects approved by the BOI, which has increased substantially from 17 in 1975 and 46 in 1980 to 133 and 143 in 1984 and 1985 respectively. Its share in the total number of approved projects also grew from 20 percent in 1975 to more than 50 percent in each year since 1983. The total amount of investment and employment by these export-oriented activities, which were concentrated in the agricultural products and other

products sectors, also significantly increased over time (Table 10.12).

Considering the value of export sales and export propensities of promoted firms, which responded to the BOI surveys from 1971 to 1984 grouped by nationality, it can be seen that average export sales and average export propensities increased over time for most groups. The surveys also revealed that the export performance of foreign firms was better than that of local firms throughout the 1970s. However, in 1984, the export performance of local firms surpassed that of foreign firms. This was probably due to the development of a group of modern, Thai-owned companies in the 1980s that were able to compete effectively in export markets in a variety of sectors (Table 10.13).

In order to improve the marketing expertise in the Thai private sector, and to reduce dependence on foreign trading firms for the handling of Thai exports, the BOI began to promote international trading companies (ITCs) in October 1978. These promoted ITCs are required to achieve the following export targets: (i) B 300 million in the first year; (ii) B 400 million in the second year; and, (iii) B 500 million in the third and subsequent years. Moreover, the ITCs must satisfy certain diversification requirements which are embodied in limitations of the permitted contribution of exports of various commodities to the overall target.

It may be concluded that ITCs have not been truly successful in promoting new manufactured exports from Thailand. The major problems facing ITCs are the lack of ability to satisfactorily identify and exploit foreign markets, and failure to gain the confidence of small manufacturing firms. Moreover, sub-contracting has often proved to be a risky venture for the ITCs. Several have been known to pay a heavy price for failing to deliver quality products on time due to the failure of their sub-contractors in terms of timeliness and/or quality levels.

3.3.2 Import Duty and Tax Refund

While promoted firms are entitled to tax exemptions on intermediate input that are used in the production of exports, non-promoted firms or promoted firms whose period of privilege has expired, can also claim similar tax refunds from the Customs Department and/or tax rebates from the Fiscal Policy Office concerning their export activities.

Table 10.12
NUMBER OF BOI-APPROVED INVESTMENT PROJECTS WITH EXPORT REQUIREMENT
BY TYPE OF ACTIVITY, 1975-1985

Category	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1975-1985 Total	1975-1985 Investment
Agriculture & Agricultural Products	14	4	13	20	13	14	24	11	18	26	22	179	7860
Mineral, Metals, & Ceramics	1	6	2	7	6	8	7	6	10	4	9	66	55394 1/
Chemical Products	0	0	0	1	2	2	1	2	2	11	6	27	4327
Mechanical & Electrical Equipment	1	1	4	3	11	3	3	6	6	19	21	78	19437
Other Products	1	4	14	16	15	19	20	17	37	71	84	298	14080
Services	0	0	1	9	9	0	1	4	2	2	1	29	591
Total Number of Projects	17	15	34	56	56	46	56	46	75	133	143	677	
Investment (Million Baht)	210	322	803	1685	1900	1946	3835	1997	7372	14464	33930	68465	
Number of Employees	2657	2880	6430	11255	11953	10044	15019	10217	17485	46388	36801	171129	
Total Project Approvals	83	61	102	202	233	160	170	110	140	266	210	1737	
Export Projects as % of Total Projects	20.5%	24.6%	33.3%	27.7%	24.0%	28.8%	32.9%	41.8%	53.6%	50.0%	68.1%	39.0%	

1/ Includes components of the Eastern Seaboard Petro-Chemical Project amounting to B 24,239 million.

Source: Office of the Board of Investment.

Table 10.13

EXPORT SALES AND EXPORT PROPENSITIES OF PROMOTED FIRMS BY NATIONALITY, 1971-1984 1/
(Million Baht)

Nationality	1971			1975			1979			1984		
	Total Exports	Average Exports	Export Propensity	Total Exports	Average Exports	Export Propensity	Total Exports	Average Exports	Export Propensity	Total Exports	Average Exports	Export Propensity
Thai	116.7	6.9	6.4%	1019.7	19.6	14.2%	4070	43.3	20.9%	7292.8	88.9	39.0%
Japanese	50.4	3.6	2.9%	995.1	33.2	18.4%	3110.7	75.9	17.6%	1940.1	77.6	21.0%
American	41.2	4.6	7.1%	162.8	14.8	18.1%	5517.4	344.8	41.7%	1450	207.1	35.0%
European	1847.4	142.1	29.0%	2543.2	149.6	23.7%	2634.7	109.8	37.6%	3479	193.3	51.0%
LDC	47.4	6.8	3.7%	212.7	21.3	27.1%	940	39.2	51.8%	904.5	69.6	39.0%
Total:	2103.1			4933.5			16272.8			15066.4		

1/ These figures only include exports of firms that responded to the Board of Investment questionnaires in the respective years.
The average export values refer to total exports divided by the number of exporting firms.
The export propensities refer to the ratio of export sales to total sales.

Source: Board of Investment Surveys (Sibunruang 1986).

3.3.2.1 Customs Department

During the 1960s, firms were entitled to a refund of 87.5 percent of the amount of duties and business taxes paid on imported raw materials used in the production of exports. The rate of exemption was increased to 98.75 percent in September 1971. Producers had to pay 10 percent of the total amount of duties and taxes at the time of importation of raw materials and could pay the remaining 90 percent in the form of cash, government bonds or a bank guarantee. When products which used imported raw materials were actually exported, the producers were returned the 90 percent in whatever form it had been paid and received a refund of 7/8 of the 10 percent of the taxes previously paid.

Since December 1972, the exemption rate became 100 percent if the products were actually exported within a year after the raw materials are imported. Producers can either pay the full amount of duties and taxes or use a bank guarantee at the time of importation and the refund is subsequently made in the form of a cheque issued by the BOT or the return of the bank guarantee.

3.3.2.2 Fiscal Policy Office

The Fiscal Policy Office started to provide tax rebates to exporters in January 1972. The taxes on inputs into exported goods, for which producers were entitled to receive rebates, included excise taxes, municipal taxes, business taxes, customs duties, and other taxes and charges added in the costs of materials, equipment, spare parts, machinery, fuel, and power. Income taxes and natural-resource royalties were not refundable.

Before 1982 the rebate rates were specific rates, estimated on a case-by-case basis, using the cost structure of producers who had applied for the rebate. Once the rate for a product was declared, it would be applied to other producers of a similar product.

In order to improve the tax rebate system, the Ministry of Finance announced a change in rebate rates in February 1982. The new rebate rates were calculated by the Fiscal Policy Office for certain categories of products based on the technical coefficients of the Input-Output Table of Thailand (1975). However, the old

rates continued to be used until August 1985 to enable exporters to adjust to the new system. In addition, the new system allowed the rebate to be adjusted according to changes in production costs, and the coverage of the system was also extended to all exported products.

The new rebate rates, however, proved to be too aggregated, and were subject to countervailing duties imposed by importing countries. Consequently, in February 1986, the Fiscal Policy Office announced more disaggregated rates based on four-digit CCCN codes. In May 1979, the actual administration of the tax rebate scheme was transferred to the Customs Department, but the regulations have remained the same and the Fiscal Policy Office still retains the authority to estimate and announce the refund rates.

3.3.2.3 Bonded Factories and Export Processing Zones

The bonded factory system allows large firms engaged exclusively in manufacturing for export to completely bypass customs procedures when they import input to be used for producing manufactured exports. Customs officers are stationed at the bonded factories to monitor the imported input and the manufactured exports. The number of firms being granted bonded factory status has increased rapidly in recent years, from 12 in 1982 to about 70 in 1985. However, the number of firms which are allowed to use this facility is some what limited due to staff constraints in the Custom Department. A new procedure has recently been introduced to enable the limited number of customs officials to meet the increasing demands for bonded factory status. Under the new system, a custom official covers many factories in a prescribed area, and exporters are required to submit detailed input coefficients for inspection by the custom official.

Export Processing Zones (EPZ) allow a firm to obtain an exemption from import duties and business taxes on machinery, equipment, tools, supplies and components essential for the manufacture of goods, and on raw materials required for the construction, assembly and installation of factories or buildings. At present, there are some seven EPZs in operation, with several more to become operational in the next few years.

3.3.2.4 Non-Tariff Measures

Exporters are subject to a number of control measures and regulations as follows:

(i) Export taxes on certain products such as rice, metal scraps, and wood products. In addition, export duties may be levied on certain items to prevent the imposition of countervailing duties or anti-dumping duties of some importing countries.

(ii) Minimum export prices on two products, namely canned pineapple and canned clams, exported to Italy.

(iii) Export controls administered by the Ministry of Commerce through the export licensing system which aims at preventing or relieving critical shortages of certain food items and raw materials, regulating exports, conserving wild life, environment and energy, maintaining standardized exports and minimum price controls, and honoring bilateral agreements. There are also controls by other Ministries for health and safety reasons.

(iv) Export quotas, which are currently imposed on tapioca products exported to the E.C., textiles and garments exported to some countries (e.g., the U.S.), and sugar. These export quotas are imposed in accordance with bilateral or multilateral agreements.

(v) Export performance requirements by the BOI, and on certain products, to promote exports and to protect the existing non-promoted firms supplying the domestic market. In addition, wholly foreign-owned projects must export their total production. However, the BOI has recently relaxed the regulation to allow 80 percent export activities to be wholly foreign-owned.

(vi) The local content requirement imposed by three agencies, namely the BOI, the Ministry of Industry, and the Ministry of Agriculture and Co-operatives, with the objective to promote domestic industries. Despite protecting domestic industries, the local content requirement may create impediments to industrial efficiency improvement and export potentials.

3.4 Banks and Financial Institutions for Export Finance

3.4.1 Commercial Banks

Commercial banks are considered to be the most essential source of export credit in Thailand. Credit extended is in the form of export bills (some of which are refinanced by the BOT), loans, and overdrafts. The main criteria used for extending such credit is the credit-rating of each exporter. Therefore, most of the customers who qualified for such credit, usually have established credit line with a bank.

As for the total credit outstanding of all commercial banks at the end of each year, the proportion of export bills is more than that of loans and overdrafts. Approximately 70 percent of all export credits extended by commercial banks are from the five largest banks. However, the behavior of small and large banks are different such that for the five largest banks, about 60 percent of total export credits extended is in the form of export bills while only about 50 percent of total export credit extended by smaller banks is in the form of export bills (Table 10.14).

Commercial banks play an important role as agents of the BOT in providing a rediscounting facility. Each application is carefully reviewed by the commercial banks, which also have full right to reject any application that does not prove satisfactory. Once the rediscount of any promissory note is carried out, commercial banks must see to it that the exportation of goods is made, and also to find out reasons for failure to export if such a case occurs.

As for export credit in the form of export bills, two categories of bills are used: first, direct export bills from commercial banks; and second, indirect export bills which are refinanced by the BOT. The interest rates charged by commercial banks are between the prime rate and the ceiling rate per annum for the first category, and not more than 7 percent per annum for the second category. The proportion in each category depends on the economic and financial conditions of the country. Generally, the proportion is about the same for both categories, except in a tight money situation where commercial banks tend to hold more export bills refinanced by the BOT.

Table 10.14

FORM OF EXPORT CREDIT EXTENDED BY COMMERCIAL BANKS, 1975-1991

	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
	Outstanding as of 31 December (Million Baht)																
1. Large Banks	7522	9035	9562	13044	19379	17879	18641	21471	24245	29061	29776	33755	39639	47146	53932	57717	60852
Export Bills	4096	5283	5805	7634	11879	12115	12644	14899	19447	22377	23645	27548	30824	38372	41967	44969	45811
Loans & Overdrafts	3426	3752	3757	5410	7500	5764	5997	6572	4798	6684	6131	6207	8815	8774	11965	12748	15041
2. Small Banks	2846	3742	4031	5239	6381	6299	7436	7521	7849	10672	15244	16389	21170	24921	29310	33650	34405
Export Bills	1217	1787	1929	2541	2661	2865	3907	3037	4002	6603	9699	10683	13842	16253	18644	21060	19260
Loans & Overdrafts	1629	1955	2102	2698	3720	3434	3529	4484	3847	4069	5545	5706	7328	8668	10666	12590	15145
3. Total	10368	12777	13593	18283	25760	24178	26077	28992	32094	39733	45020	50144	60809	72067	83242	91367	95257
Export Bills	5313	7070	7734	10175	14540	14980	16551	17936	23449	28980	33344	38231	44666	54625	60611	66029	65071
Loans & Overdrafts	5055	5707	5859	8108	11220	9198	9526	11056	8645	10753	11676	11913	16143	17442	22631	25338	30186
	Outstanding as of 31 December (Percent Share)																
1. Large Banks	72.6	70.7	70.3	71.3	75.2	73.9	71.5	74.1	75.5	73.1	66.1	67.3	65.2	65.4	64.8	63.2	63.9
Export Bills	39.5	41.3	42.7	41.8	46.1	50.1	48.5	51.4	60.6	56.3	52.5	54.9	50.7	53.2	50.4	49.2	48.1
Loans & Overdrafts	33.0	29.4	27.6	29.6	29.1	23.8	23.0	22.7	14.9	16.8	13.6	12.4	14.5	12.2	14.4	14.0	15.8
2. Small Banks	27.4	29.3	29.7	28.7	24.8	26.1	28.5	25.9	24.5	26.9	33.9	32.7	34.8	34.6	35.2	36.8	36.1
Export Bills	11.7	14.0	14.2	13.9	10.3	11.8	15.0	10.5	12.5	16.6	21.5	21.3	22.8	22.6	22.4	23.0	20.2
Loans & Overdrafts	15.7	15.3	15.5	14.8	14.4	14.2	13.5	15.5	12.0	10.2	12.3	11.4	12.1	12.0	12.8	13.8	15.9
3. Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Export Bills	51.2	55.3	56.9	55.7	56.4	62.0	63.5	61.9	73.1	72.9	74.1	76.2	73.5	75.8	72.8	72.3	68.3
Loans & Overdrafts	48.8	44.7	43.1	44.3	43.6	38.0	36.5	38.1	26.9	27.1	25.9	23.8	26.5	24.2	27.2	27.7	31.7

Note: Large banks means the five largest banks.

Source: Bank of Thailand.

3.4.2 The Industrial Finance Corporation of Thailand (IFCT)

The Industrial Finance Corporation of Thailand extends longer-term credits which are mostly project loans to producers of industrial products. Some of these credits are refinanced by the BOT. The interest rate charged for all industries is periodically adjusted in line with the market rate. In August 1981, the rate varied between 15 to 16 percent per annum, depending on the location and type of industry. For example, the rate charged for agro-industry is 15 percent per year. The period of maturity is between 3 and 15 years.

Industries which export in excess of 50 percent of their total production, and where value-added exceeds 80 percent of the total costs, are eligible for low cost funds from the BOT. The BOT provides 40-80 percent of each loan extended by the IFCT under the above conditions. The interest rate charged by the BOT is 7 percent, while the IFCT lends at 10 percent per annum.

3.5 Supporting Services

3.5.1 Department of Export Promotion

The Department of Export Promotion is the principal government agency responsible for assessing exporters, by providing information on potential markets, identifying buyers, providing relevant training, and helping them to deal with any problems encountered in the business of exporting. It also promotes Thai exports by arranging trade fairs and trade missions. The Department of Export Promotion has overseas trade centers in New York, Los Angeles, Rotterdam, Frankfurt, Vienna, Sydney, Vancouver, Dubai and Osaka since 1986, and recently the Department of Export Promotion has increased to 17 overseas trade centers.

3.5.2 Commercial Counselors

The Ministry of Commerce has 45 Commercial Counselor Offices abroad. Their main responsibilities include promoting Thai trade interests overseas by negotiating with government officials to solve commercial problems, facilitating inter-governmental contracts, and preparing trade treaty negotiations. In the export field, they assist exporters by providing market information, answering trade queries,

identifying export opportunities and helping to arrange trade missions and trade fairs.

3.5.3 Export Development Fund

The Export Development Fund was created from import charges collected in February 1982, with an endowment of B 300 million. This fund yields annual interest of some B 30-40 million which is allocated to export promotion activities such as trade missions, fairs and negotiations. Now the endowment has increased to B 2500 million, which would greatly facilitate the export promotion projects particularly the export promotion plan set up by the Export Development Committee annually.

3.5.4 Export Development Committee

The Export Development Committee was set up in June 1977 to design and implement an export development strategy. The major achievement of the Export Development Committee is that it has simplified export procedures, reducing the required number of stages from 25 to 9 since 1983, and standardized the export forms used by various government agencies to those recommended by the United Nations. Recently, the Export Development Committee has incorporated with private sector to set export target and export promotion plan annually.

In addition to government agencies, there are a number of private organizations, such as the Board of Trade, the Federation of Thai Industries, foreign chambers of commerce, and various industrial associations which assist their members by providing information on export opportunities, organizing trade missions abroad and arranging for their members to meet foreign buyers.

IV. Problems and Issues on Export Promotion

Even though the Thai economy has achieved rapid growth in manufactured exports over the past five years, imports have also grown by an increasing rate over this period, and the trade deficit has remained large. This trend was due to the influx of FDI in export-oriented industries and the expansion of the domestic economy,

resulting in a need of capital goods. Also, the new types of exports demanded the import of raw materials such as computer components, electrical appliances and jewellery, etc. This implied that the trade deficit would go up in the same direction as export growth. To reduce the size of the trade deficit, the Government needs to encourage exporters to raise the value-added and reduce the import contents in their exports.

Moreover, the fast growth in exports which led to economic growth caused a number of problems in the Thai economy. Firstly, infrastructural constraints emerged requiring the public sector to extend telecommunications, transportation facilities - particularly ports, airports, and mass transit in Bangkok, water supply and electricity supply in regional areas. Secondly, shortages of skilled labor also emerged especially technicians, engineers, and management personnel. Thirdly, the overheating of the economy put upward pressure on prices, increased trade deficits, increased the investment - saving gap, and worsened the income distribution. Fourthly, the rapid growth of the manufacturing sector has not yet been accompanied by the development of environmental infrastructure to curb the damage done to the environment through industry-related pollution and waste disposal.

In addition, there are some weaknesses in the export promotion policies in Thailand that should be considered:

(i) The red tape of government agencies caused increased costs for exporters, such as the tax refund system, and the BOI's approval, etc. These delays came from the shortage of government personnel during the boom period. The complexity of the system also caused delay.

(ii) Government incentives unintentionally favored big scale industries and large exporters. Small firms have difficulties or no access to preferential treatment.

(iii) The tax incentive distorted the allocation of resources because the components of export promotion relied more on raw materials or intermediate products from aboard.

(iv) Although the exporters' major source of fund come from the BOT in the form of packing credit, with lower than market interest rate, the BOT's main responsibilities to contain inflation and maintain the value of the baht at times come in conflict with the provision of assistance to exporters. The

BOT, therefore, is unable to fully support exporters resulting in their lack of sufficient fund to expand exports to new markets.

(v) The rapid economic growth, which was led by the export sector, did not solve the problem of income distribution in Thailand.

(vi) The protectionist measures in various developed countries, particularly the major export markets of Thailand, such as the U.S., Japan, the E.C. and Asian NICs, impeded the expansion of export potential. Moreover, the formation of trading blocs in each region, such as Single European Market and the North American Free Trade Agreement (NAFTA), limited the market access of Thai exports. Thus, the Thai Government strongly supports the success of multilateral negotiations in order to promote freer trade around the world. Despite the success of the General Agreement on Tariffs and Trade (GATT) negotiations, the emergence of trading blocs in various regions is a challenge. Thailand and other SEACEN countries should therefore intensify their cooperation.

V. Policy Recommendations

Acknowledging the recent problems faced by Thai exporters, the Thai Government plans to implement a number of measures to enhance Thailand's production efficiency and international competitiveness. The major measures to be undertaken include:

(i) Infrastructure facility improvement with an increase in expenditure on infrastructure - particularly on telecommunication and transportation;

(ii) Manpower development, with both short-term and long-term measures, to address shortages, especially in science and technology;

(iii) The Customs Department's measures to facilitate exports, such as a bonded packaging warehouses, bonded manufacturing warehouse zones, customs offices in large industrial estates and computerization of tax collection and goods release procedures to increase service efficiency;

(iv) Additional inland container depots will be set up to alleviate the congestion at the Bangkok Port, and to support the development of a door-to-door delivery system;

(v) Establishment of an Export Credit Guarantee Fund which will be provided against post-shipment risks;

(vi) Establishment of an Export-Import Bank which will provide manufacturers and exporters with financial services;

(vii) Thailand is now concerned with the need to "upgrade" or "deepen" the industrial structure, thus, the industrial strategy should place greater emphasis on building backward linkages by encouraging the manufacture of machinery, parts and equipment rather than concentrating on the assembly of these components. There must also be a shift from single manufacturing to more sophisticated production;

(viii) In order to spread the benefits of industrial growth to a wider segment of the population, the Government must encourage rural industrialization by removing the constraints on basic infrastructure, information flow for marketing and technology, etc.;

(ix) Since FDI has been a major source of technology, markets and management skills, the Government should encourage greater overseas investment in Thailand, and assist Thai exporters entering overseas markets; and,

(x) The most important role of the BOT is to stabilize the economy in order to build the confidence of investors, both foreign and domestic.

VI. Summary and Conclusion

Export promotion strategies in Thailand have been implemented for more than two decades. The assessment of these strategies is difficult to make. However, the results of various export promotion policies showed clearly in the structural change in exports, and increasing diversification, both in terms of products and markets.

The success of export-led growth during 1986-1991 resulted partly from prior export promotion policies, and the depreciation of the baht, which improved the competitiveness of Thai exports. The BOI's incentives benefited from a surge in FDI particularly from Japan and Asian NICs in response to the relocation of export base and the continuation of low wages relative to Thailand's main competitors. However, the benefits will not remain since infrastructural bottlenecks and domestic constraints are causing the Thai economy to lose ground

with respect to the East Asian NICs, particularly with regard to manpower. In a number of areas, however, the Government hopes that FDI will make significant contributions towards overcoming the above deficiencies, and continue to help fuel economic growth and the expansion of exports.

Due to the increasingly intense competition in the world market, and protectionist measures, including the impact of trading blocs such as Single European Market and NAFTA, etc., these export promotion strategies need to be adjusted in order to solve the problems. Enlarged cooperation in economic and trade relations between SEACEN member countries would help each country to develop its potential output and export in line with the appropriate policy direction respectively, and also increase the individual comparative advantage.

REFERENCES

1. Bank of Thailand, ***Quarterly Bulletin***, various issues.

2. International Monetary Fund (1991), ***Thailand: Adjusting to Success - Current Policy Issues***, by D. Robinson, Y. Byeon, and R. Teja with W. Tseng.

3. Sibunruang, A. (1986), ***Industrial Development Policies in Thailand***, A report prepared for the World Bank.

4. _____, and P. Brimble (1992), ***Export-Oriented Industrial Collaboration: A Case Study of Thailand***.

5. World Bank (1986), ***Thailand: Growth with Stability - A Challenge for the Sixth Plan Period***.

6. _____ (1989), ***Thailand: Country Economic Memorandum, Building on the Recent Success - A Policy Framework***.

7. _____ (1991), ***Thailand: Country Economic Memorandum***.