Underdeveloped Countries and Manufactured Exports[1]

by Christopher Bliss

The necessity of moving from primary products to manufacturing in the UDCs

Although exports of underdeveloped countries (UDCs) are currently for the most part primary products, with manufactured exports accounting for only about 15 per cent of the total, the future growth of these exports is crucial to the success of efforts to achieve economic development in these countries. This proposition holds regardless of whether one accepts the widely held view that the outlook for primary product exports is extremely bleak. That view may turn out to be too pessimistic. The proposition that there is a secular tendency for the prices of primary products to decline relatively to those of manufactured products is not well supported by either the empirical evidence (unless that evidence is presented rather selectively) or by theoretical argument.[2] The claim that prices have a long-run tendency to move against primary products and in favour of manufactured products is often the premise to an argument that the UDCs will have to move out of specialization in primary products towards the production and export of manufactured products. But the conclusion does not depend upon this premise. Production of primary products will not be a sufficient basis for economic development even if the trends in primary product prices turn out to be extraordinarily favourable. A few countries in specially favourable circumstances may be able to raise income per head to high levels by achieving high levels of productivity in the production of primary products and obtaining their requirements of manufactured products through international trade. If, however, all UDCs were to follow this route, then no reasonable projection of demand for primary products would indicate that the supply could be absorbed.

The necessity of such a growth in manufactured exports can be seen simply if we consider the development of a single economy. In

[1]Readers interested in a deeper and more technical discussion of the questions discussed in this note will find it in H. G. Johnson, *Economic Policies towards Less Developed Countries*, Unwin University Paperback. The report of the United Nations Conference on Trade and Development is highly relevant, and a useful statistical source. Volume IV is on Trade in Manufactures. cf. also *Economic Nationalism in Old and New States*, ed. by H. G. Johnson, Unwin University Paperback.

[2]Perhaps this is just because 'primary products' is a huge collection of disparate goods subject to different influences, hence not a useful way of classifying exports. But the manner in which exports should be classified to conform to the pessimistic view is not clear.

https://doi.org/10.1111/j.1741-2005.1970.tb02030.x Published online by Cambridge University Press

all countries that have achieved high levels of income per head, the process has been associated with a decline in the proportion of the labour force engaged in agriculture. That proportion varies considerably between countries of comparable income levels (being high for example in Denmark and New Zealand, and low in the United Kingdom) due to patterns of specialization through international trade. But even the 'agricultural' economies among the advanced countries have a ratio of labour employed in agriculture and primary production far below that to be found in the world's underdeveloped economies. *If the world is to become richer in per capita terms then it must follow the route which the advanced economies have taken and move resources from primary production to manufacturing.* Naturally productivity in primary production should increase, as has happened in the advanced countries, but the higher income levels, if achieved, will imply a structure of demand inconsistent with specialization in primary production.

But manufacturing implies the need for exporting

So far the discussion has been concerned with production and not with international trade. It is, however, hardly likely that the underdeveloped economies of the world should become producers but not exporters of manufactured goods. Firstly that would imply an absurd proliferation of small-scale manufacturing enterprises as each country tried to meet its own requirements of each and every type of manufactured good. There is already far too much of this self-sufficiency in manufacturing in the UDCs, and the resulting inefficiency is a serious handicap to the growth of manufacturing production. Also, self-sufficiency in manufacturing would deny the UDCs, and the world in general, the benefits of certain special advantages which UDCs have in the production of some manufactured goods. The special advantages are of two types: those that arise from the availability of raw materials in the countries concerned, and those that arise from the availability of cheap labour in poor countries. Both these factors give cause to believe that manufacturing production in the UDCs will not be unable to compete in world markets *if opportunities are provided. That these opportunities should be provided as a matter of urgency and great importance is the main argument of the present note.* For unless manufactured exports from the UDCs can increase at rates not so far experienced they must remain for a very long time in a state of poverty and backwardness not much better than their present condition.

What, then, are the obstacles to such a process? No single answer

If the growth of manufacturing production and of manufacturing exports is of such importance to the process of economic development, and if in some cases UDCs have advantages in the production of some of these goods, why has there been such a disappointing growth of manufactured exports from the UDCs?[1] *There is no single answer to this question,* and in part the problem is the problem of economic underdevelopment itself. All the factors which explain and perpetuate poverty in the UDCs help to explain the poor performance of manufacturing exports. The consequences of social systems unfavourable to economic modernization are no less severe for the development of exporting industries than they are for any economic development. The general inefficiency of organization, lack of education, corruption and lethargy are part of the explanation of poverty in underdeveloped countries. To assume these away and look for all the solutions in international trade institutions is to assume away more than half the problem.

Attitude towards international trade nevertheless a substantial contributory factor

However, this said, there can be no doubt that a substantial part of the explanation of stagnation of manufacturing production is provided by the attitude towards international trade adopted by the nations of the world, both developed and underdeveloped.

(a) *Protectionism by the developed countries*

The advanced countries have contributed greatly to the problem of developing manufacturing exports from the UDCs by protecting their own markets against these goods by tariffs and controls. These barriers to trade have been strongest just in the case of those goods where it might be expected that UDCs would have special advantages on account of the availability of raw materials or labour intensity of production. Indeed, it has sometimes been felt in the UDCs that the barriers represent moving targets in that a successful attempt to scale the barriers by getting costs down enough to compete would lead to successful agitation by the home producers to have the barriers against foreign imports increased. This has happened notoriously in the case of cotton textiles.

Another important point is that the structure of tariffs in the advanced countries discriminates strongly against the processing by the UDCs of the raw materials that they produce. This discrimination is not readily apparent if one looks at the nominal tariff rates on the processed goods, which may often not seem to be prohibitive. However, one has to take into account in the calculations the fact that raw materials are usually admitted to the advanced countries free of charge, there being no home market to protect. The manner in which this can produce savage discrimination against the process-

[1]From data prepared for the United Nations Conference on Trade and Development (UNCTAD) 1964 it is known that exports of manufactures grew relatively more rapidly than other exports in the period 1955–61 (about 5 per cent per annum). However, this rate applies to all exports. The extent of exports of manufactures varies greatly between the UDCs. The countries with rapidly growing exports in this area are also often those that already have high levels of exports.

ing activity can be seen from an example. Suppose that a UDC can produce raw cotton and could also process this cotton to produce shirts. Let us look at the effect of a tariff on imported shirts by asking how much more efficient the industry will have to be in cost terms to compete with the processing industry of the advanced country, in spite of the tariff barrier. Suppose that half the cost of a shirt is raw cotton and half the cost is processing. If a 15 per cent tariff is levied on imported shirts, but not on imported cotton, the processing activity will have to be 30 per cent more efficient to compete with the advanced country's activity. This is because, essentially, the cotton pays a 15 per cent tariff when it comes in as a shirt, and the processing activity has to be efficient enough to make good that disadvantage as well. The influence of this effect depends upon the share of the cost of the raw material in the total cost of production of the finished good; the larger that share the stronger is the discrimination against the processing activity.

(b) *Protectionism by the UDCs*

The problems faced by the UDCs on account of discrimination against their manufacturing exports by the advanced countries are only the beginning of the story. The historical experience of the UDCs, particularly of fluctuations in primary product exports; their striving for independence, political and economic; and a desire to imitate countries that have developed behind protective barriers—all these influences have tended to produce a protectionist philosophy in the UDCs. They have implicitly come out against international trade. When faced with balance of payments problems the UDCs have usually taken the easy route of cutting back imports so as to protect and encourage home industries—the so-called 'import substitution' approach. The approach has been taken to fantastic extremes, especially in Latin America, where in some sectors phenomenal inefficiency of production is matched by massive protection through tariffs and controls. The system has a tendency to rapid reproduction since any would-be producer of an imported product will hope to persuade the authorities to provide whatever degree of protection is implied by the extent of his inefficiency: this in the interests of national autonomy and the balance of payments. The snag is that this approach is not the road to economic development that is hoped for; the example of successfully developed countries that have grown behind tariff barriers is not very apposite. Typically these countries have been much larger than many present-day UDCs, and have started from rather favourable preconditions for a high degree of autonomy in certain sectors. Also the protection provided was seldom so massive, and never so indiscriminate, as that to be found in certain present-day UDCs. Finally, the acid test, in all these now developed countries the protection formed the basis for an invasion of one or more world markets with highly competitive exports. A country in which there are no signs at all of this happening cannot strictly claim to be following the example of Britain or Japan.

A very serious drawback of the import substitution approach is that the system tends to be self-justifying. Suppose that a country argues to itself, perhaps from misconstrued evidence, that the promotion of exports is too difficult and subject to too many constraints and barriers; instead a policy of import substitution will be embarked upon. Then a situation is very likely to arise in which it is indeed true that no manufacturing industry in the country has good export prospects because any industry will be gravely handicapped by having to buy some of its inputs from high-cost inefficient and protected sectors in the home economy. If an industry can buy inputs on world markets at world-market prices and transform these inputs into output that can profitably be exported at world-market prices, then it will usually be in the interest of the UDC and its balance of payments that these exports be promoted. But in fact the required inputs will often carry high tariff rates so that home prices are far above world prices. This has the effect of implicitly 'taxing exports' whenever these would profitably make use of imported inputs at world-market prices. Import substitution thus tends to have the character of a medicine, necessary to the treatment of a dangerous disease, that has the property of giving the disease to any patient not already suffering from the complaint who happens to take the medicine.

One paradoxical feature of protective policies in the UDCs is, therefore, that they may worsen the payments position by inhibiting the growth of exports. There are other disadvantages as well. An obvious one is that a policy of import substitution must eventually 'run out of steam', for it will in the limit reduce the home economy to a state of complete autarky. Thus it stands in contrast to such policies as exchange depreciation which can be applied over and over again. There is another important matter which as such is outside the scope of the present note, but which must be mentioned here. Tariff barriers, particularly in large countries, tend to encourage capital inflows. This is easy to understand; if foreign producers find that their sales in a certain country are falling because the price of their product is being inflated by a tariff, then they will consider coming into the country to produce from an owned subsidiary whose output will not be subject to the tariff. This is not a matter about which the authorities of the UDCs can remain indifferent. Maybe they would like to see an increased inflow of private capital; indeed it may be a main aim of protective policy to get the foreign producers to confer on residents of the country where the sales take place some of the benefits of production such as employment opportunities and training and experience. In that case this is a welcome benefit of protection; however, it then follows that protection does not have such a great effect on national autonomy, and one must not forget the long-term implications for the balance of payments of repatriated profits of foreign investors. What a UDC must do, if the capital inflow effect turns out in its own case to be important, is to assess from the point of view of its own objectives and the problems that it faces whether an increased inflow of private capital would be welcome. If the answer is affirmative, then this is an added argument for protection, otherwise this must be counted a disadvantage of protective policies.[1]

One last remark is often made concerning the trade policies of the UDCs. A great deal of the discrimination against foreign imports is in effect discrimination against the exports of other UDCs. This point is important, although it is probably laboured excessively by those who maintain that the UDCs, best prospects for trade lie in trade with other UDCs, a view which in its extreme form seems dubious. It is true that the UDCs have some of the world's highest tariff barriers so that one might reasonably hope for large proportionate increases in trade should these barriers come down; to a considerable extent, however, the large size of these increases as a proportion of existing trade *between UDCs* would be merely offset by the lower importance of the UDCs for general growth in trade on account of their low incomes. Be that as it may, there is something specially agonizing about seeing the poor beating each other's backs, and there may be genuine reasons why trade expansion between certain UDCs would be particularly valuable; e.g. because of geographical proximity. The sense in which it is clearly true that the UDCs harm themselves much more than the advanced countries by their trade policies is this: the poor can less afford the luxury of sheltering inefficient producers.

To summarize the problems that the UDCs face with respect to manufacturing exports, these consist of protective tariff barriers and controls in the advanced countries, which are especially fierce and discriminatory with respect to the processing of raw materials produced in the UDCs; to these problems are added severe problems of protections and inefficiency inside the UDCs which tend to handicap even those industries which might have an advantage in exporting in the face of international competition.

So what is to be done?

What then is to be done? The question is too large to be answered just in the context of the present discussion. *The problems of the UDCs have a strong tendency to hang together; already it has been necessary to consider international movements of capital when talking of trade policy.* In

[1]Of course the UDC could combine protection with policies designed to discourage capital inflows; e.g. punitive taxation of the profits of foreign-owned companies. That such policies are not usually adopted merely reflects the fact that the official stance of most UDCs is to favour more private investment inflow, which is not to say that they find the form that it now takes ideal from their point of view.

looking for reforms of the international trade system one must not lose sight of two points. Firstly, the extent to which measures to promote exports of manufactured goods could help the UDCs varies very greatly from country to country. Hence there is no question here of a panacea for all the problems that the UDCs face. *It can be said for policies to promote manufacturing exports that they have more chance of helping significantly a wide range of UDCs than has, for example, a policy to support the prices of primary products above the level that would otherwise rule.* This is because most UDCs could produce manufactures, while the extent to which they can export primary products varies greatly, and a country ill-endowed with natural resources, such as India, can do little about it. *The second point is that trade policies have to be integrated with other policies towards the UDCs.* If there is to be reform to help promote manufacturing exports, then aid should be provided to help the UDCs transfer resources to exports and build up efficiently operating industries. Here we come face to face with a sinister conflict. In the past, advanced countries have not always been enthusiastic about giving aid and advice that would tend to aggravate the problems faced by their own protected sectors. This in part reflects the view that a successful outcome of this aid would lead to increased protection. Those responsible for giving aid might deplore this fact, but they can hardly be blamed for recognizing it.

Signs of hope, and possibilities of freer and more equitable movements of manufactured exports

In spite of the many problems the present situation is rather hopeful in some respects. The recent United Nations Conferences on Trade and Development (UNCTAD) have shown that the UDCs will unite politically behind a platform for the freeing of trade barriers against their exports and that the advanced countries are willing to give them a sympathetic hearing and (with the exception of the United States, whose views may change in the near future) to support a number of their proposals. The UDCs pressed at the UNCTAD conference for a system actually discriminating in favour of exports from UDCs. There are serious arguments in favour of such a system, but also practical problems of implementation. Also there is something rather surrealist about a group of countries presently discriminated against in international trading relations demanding the right to reverse the system. Perhaps it makes more sense at this stage to try for a system which will remove the tariff barriers against manufacturing exports from the UDCs, these agreements being negotiated on a rather one-sided basis; i.e. not requiring that the UDCs match each concession regarding their own exports with a comparable concession to the exports of advanced countries. This is not to say, however, that the advanced countries should bring no pressure to bear on the UDCs for changes in their trading policy. Indeed, from what has already been said, it should be clear that it is in the interest of the UDCs that they be encouraged to adopt less protectionist policies, and without some change it is doubtful whether in the majority of cases expansion of exports of manufacturers can be achieved.

There is much to be said then for a scheme something like this:

1. Exports of the UDCs could enter advanced countries free of tariffs and controls. The advanced countries would agree not to levy tariffs or discriminate in any way (including 'voluntary' controls) against these exports.

2. The UDCs would be allowed to levy tariffs on imports from the advanced countries. However, the agreement would specify an upper limit on the rate at which tariffs could be levied and would discourage other forms of discrimination. If the tariff levels were kept down, there would be no need to try to outlaw tariff discrimination against exports of other UDCs, an aim bound to run into political and administrative difficulties.

3. The agreement would have to include provision for adjustment to the new trading situation, particularly for those countries where particular sectors would suffer badly or where the balance of payments would run into deficit. This problem cannot be discussed in this short note; it is, however, outstandingly important, perhaps the key problem.

An advantage of the above proposals is that they are feasible from the administrative point of view, which is more than can be said for many attractive suggestions. The customs officers of the advanced countries would admit free of tariff charges goods accompanied by a certificate of origin naming a UDC. There would be no need to undertake a complete overhaul of existing trading agreements between the advanced countries, a task which might set back a scheme for decades.

Whether any of this will come about remains to be seen. There are powerful groups in both the advanced countries and the UDCs that will not readily submit to the inconveniences to which these proposals would give rise. The proposals are anyway international in nature; that is, they require agreement between a majority of the world's nations.

What Britain could do alone, apart from more general international agreements

On a more local level, it might be asked what Britain can do alone. Obviously, the arguments for everyone cutting tariffs on goods from the UDCs apply equally to one country. The difficulties, however, are increased. A single country that cuts tariffs on UDC exports suffers a deterioration in its balance of payments position with only a small increase in export earnings due to the improved position of the UDCs to import. There is also the general problem that a single small effort seems less attractive relative to the sacrifices than the same steps undertaken by all the advanced countries, with each sacrificing the same. It is much easier to persuade nations, like individuals, to take part in a collective programme of help for the UDCs than to persuade one country to go it alone. Perhaps the solution to this problem is that Britain should concentrate her tariff cuts on the Commonwealth countries. This produces anomalous discrimination between Commonwealth and non-Commonwealth nations, and is therefore far from ideal. It is not clear, however, that we can hope to attain the ideal alone.

The acid question: the political will to change trading policies in favour of the UDCs

In thinking about these problems one comes down again and again to the same issue. *There is a great deal that the advanced countries can do by way of trade policy to help the UDCs.* Even a single advanced country can do something. *However, all the really useful changes involve costs.* In particular, certain groups in the advanced countries, such as textile producers and workers, would suffer from these changes. Not unnaturally, these groups then form a concentrated lobby against tariff cuts. The good will towards the UDCs, such as it is, is widespread in the population, but those for whom this is the thing that they care passionately about are few in number; they therefore form a poor lobby. For a country like Britain, with balance of payments difficulties, *help for the UDCs is only going to be forthcoming (whether by trade or aid) if the UDCs are high on a list of political priorities.* To get them higher on that list, the public has to be educated as to the nature of the problem, the manner in which our policies contribute to it, and the methods whereby we might alleviate the problem. Here it is interesting, but depressing, to see how little political protest greeted the recent imposition of increased tariffs on textile imports. This was never presented to the public as an issue of our attitude to the UDCs and the implications for them of such policies. Sadly, this reflects the fact that *the UDCs*, although often mentioned in radical pamphlets in this country, *are not yet a lively political issue.* They are unlikely to become a lively issue while radical propaganda concentrates on imputing total responsibility for the state of the UDCs on the advanced countries; this approach has quite quickly a completely numbing effect. What is needed is an identification of those policy issues on which our attitude to the UDCs really hinges, and the bringing of these issues into the political arena. Trade policy towards the manufactured exports of the UDCs is certainly such an issue.

General Reading:

Jagdish Bhagwati, *The Economics of Underdeveloped Countries*, World University Library.

Jonathan Power, *Christian Aid Campaign Booklets.*