INDUSTRIALIZATION PROSPECTS FOR SWAZILAND AND THE EXPERIENCE OF NEWLY INDUSTRIALIZED COUNTRIES

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INTRODUCTION

Swaziland is a small country with a relatively limited resource base. It is highly dependent on the export earnings of a few resource-based industries, particularly sugar and timber. With a high rate of population growth and little prospect for expansion of traditional activities, the country must look to new industries to create the jobs necessary to keep real incomes improving. The internal market is very small so exports must be the focus of new initiatives.

Swaziland has a policy environment that is hospitable for export industries. Macroeconomic stability has been achieved through conservative fiscal policy. The exchange rate is tied to the rand and the balance of payments and the international debt position are much better than in almost any other African country. Tax policies and a moderate level of government intervention are conducive to foreign investment.

These facts suggest that Swaziland might be able to enjoy significant economic growth based on expansion of new industries, especially those that produce labor-intensive consumer goods and are able to make effective use of lower-cost Swazi labor. There are already signs of this kind of growth in the manufacturing sector.

Export-lead growth focusing on production of consumer non-durable was the key to the impressively rapid rise of the Newly Industrialized Countries (NICs) in Asia. This paper takes a close look at the experience of the NICs in an effort to draw conclusions about the prospects for Swaziland's growth. The countries covered include Mauritius, Korea, Taiwan and Hong Kong. The paper summarizes the factors that were necessary for growth in these four countries. It then considers whether the necessary preconditions exist in Swaziland. Finally, it suggests what needs to be done to assist where Swaziland's circumstances vary from those of the NICs.

THE EXPERIENCE OF OTHER COUNTRIES

KOREA

Korea did not move directly from the peasant agricultural system that existed at the turn of the century, to the high-growth, export-oriented economy of today, all in one step. The transition took place over a period of more than 60 years. Although the rapid growth of output and income did not begin until 1961, the events of the previous 50 years are critical to understanding the process. The history of Korea's economic development can be divided into four periods.

1. The Japanese colonial period	1910 to 1945
2. The Korean War and partition	1945 to 1953
3. Post-war reconstruction	1953 to 1960
4. Rapid growth	1961 to 1975

The Japanese Colonial Period (1910 to 1945)

The Japanese colonial period began with the formal annexation of Korea in 1910. Initially, the Japanese focused on building social and economic institutions and promoting agricultural development. They conducted exhaustive land surveys. They introduced a comprehensive land reform program which included legal guarantees on land ownership. Large tracts of land that had been of unclear title were transferred to the Japanese colonial government. A full separation was affected between the property of the former royal family and that of the government. However, the colonial administration was careful to ensure the cooperation of the noble class by providing legal guarantees for the traditional tenant system - the mainstay of agricultural production.

At first the Japanese used Korea as a source of raw materials and grains, and as a market for industrial output. Accordingly, they imposed restrictive licensing rules that discouraged growth of modern manufacturing enterprises in Korea. They did, however, make significant investments in infrastructure including roads, highways, railways, telecommunications. They also established the Chosen Postal and Shipping Company that controlled all Korean international and coastal shipping.

As World War I drew to a close the Japanese export boom softened. Sharp increases in manufacturing excess capacity lead to the abolition of the Decree on Business Entities freeing the Japanese to export capital goods to Korea. Investment in Korea rose substantially especially in plants processing Korean primary materials. Major programs to increase Korean rice production were implemented to cover the rice shortage in Japan. Land improvement and extension programs were implemented. In addition, the government promoted production of raw cotton and silk to feed the Japanese textile manufacturers. During this period there was a progressive integration of the Korean and Japanese economic systems. The Korean won was tied to the yen shortly after annexation. The abolition of the Decree on Business Entities in 1920 removed some of the barriers to industrial investment. In addition, Korea was included within the Japanese tariff zone allowing free passage of goods between the two countries and giving them similar incentives vis-a-vis trade with third countries.

The world economic crisis which began in 1929 precipitated a radical restructuring of the Japanese economy. Exports and domestic production dropped sharply and a wave of mergers took place. In 1931 the government of Japan enacted a Law for the Regulation of Major Industries which controlled the marketing and production of major industries in Japan. But Korea was not subject to this law and many firms set up plants and subsidiaries there to avoid the more restrictive environment at home. During the period from 1930 to 1937 Korean manufacturing output increased sharply because of Japanese investment especially in textiles, processed food, cement and fertilizer. However, these new industries were unconnected with Korean national enterprises which were small, individually and collectively, and were engaged in small-scale production of textiles, vegetable oils and processed foods mostly for domestic consumption.

The situation in Korea up to this point is similar to, and perhaps even a bit further advanced than that of Swaziland today. The similarities in terms of the relationship with Japan (South Africa), the common currency and trade area, and the tendency to benefit from disinvestment in the large more advanced neighbor and the dominance of the neighbor in external trade, will be pursued further below. But it is important to recognize that, at this time, Korea was still 30 years away from its period of rapid economic growth.

The effects of war were felt even before the Japanese colonial period drew to a close. In 1937 Japan invaded Manchuria and the Sino-Japanese war began. Heavy and chemical industries were expended rapidly in Korea to support the Japanese war effort. Gold and mineral ore production were also increased. From then until the end of World War II production was tightly controlled by the colonial government. Goods were rationed and the emphasis was on large-scale production of industrial goods related to the military in plants owned and operated by Japanese. The few emerging small and medium industries owned by Korean nationals were forced out of business because of shortages of intermediate goods and war-time production controls.

During the colonial period there was significant industrialization of the Korean economy. But consumption standards did not improve. In fact, per capita consumption of polished rice, the major food grain, fell by 30 percent largely because of forced exports of rice to Japan. The initial Japanese agricultural investments involved consolidation of small farms with increasing tenancy rates and emigration to urban areas. Agricultural output grew at less than 2 percent a year while mining and manufacturing output increased by an average rate of over 10 percent per year. The rapid increases in industrial production absorbed some of those released from agriculture, but despite steady (1.6 percent annual) increases in per capita value added, real wages fell by almost 30 percent according the Seoul indices of prices and wages. In short there were advances in industrial output, but the complete domination of the economy by the Japanese and the progressive impoverishment of the Koreans did not lay a solid foundation for self-sustaining growth.

The Korean War and Partition (1945 to 1953)

There was severe disruption of the economy after the Second World War. Most of the Japanese entrepreneurs, technicians and managers left, and the partition of the country left the South isolated from the mineral resources, chemicals, ceramics and electrical power of the North. Many industrial plants suspended production as experts left, intermediate inputs disappeared and Japanese export markets were cutoff. Refugees from the North and Koreans repatriated from Japan helped swell the population of the South by 2.3 million in 1946-48. Food shortages emerged as agricultural production fell and the US Government had to step in with food aid. Uncontrolled money growth caused hyperinflation gave rise to abortive price control measures.

Despite these problems industrial production did begin to build. But the outbreak of the Korean war in 1950 again caused severe dislocation and destruction of productive capacity. By the end of the war in 1953, the country had lost about half of the manufacturing plants it had in 1949. Overall production was at roughly the same level as in 1940. The structure of manufacturing had regressed as indicated by a rise in the proportion simple manufacturing industries in total output. Investment shrank to a level too low to cover even depreciation. The $40 million of exports consisted predominantly of primary goods including tungsten, coal, fish, dried laver, and similar items. Meanwhile imports were running at $347 million and included food, manufactured goods and chemicals. This deficit and the reconstruction effort could only be covered by massive inflows of foreign aid.

Post-war Reconstruction (1953 to 1960)

In general the policies adopted during this period were designed to promote import substitution. Tariff rates were maintained at high levels and there were a variety of quantitative restrictions on imports. There were export promotion programs but export levels remained low. Inflation was a recurring problem stemming from the excessive expansion of the money supply during the war and immediately after. Exchange rates were not adjusted sufficiently to compensate for the domestic inflation, with the result that exports were further discouraged. The tendency for imports to rise because of an overvalued currency was resisted by high tariffs and the use of quotas.

In 1957 a stabilization program was introduced to cut inflation primarily by reducing the government deficit. These efforts were moderately successful until the student riots of 1960 which reignited inflation.

Another important feature of macroeconomic environment during this period concerns savings and investment. Investment was only 10 percent of GNP in this period which is low by most standards. Moreover, virtually all of this reflected foreign savings in the form of foreign aid inflows. Interest rates were controlled at low levels in hopes that the low financing costs would stimulate investment. The view was that domestic incomes were too low to allow for significant domestic savings even if interest rates on deposits were increased.

Rapid Growth (1961 to 1975)

A military government took over in 1961 and was replaced by President Park Chung Hee and the Democratic Republican Party after elections in 1964. The arrival of the new government marked a sharp break in economic policy. Post-war reconstruction was complete. Import-substitution opportunities were nearly exhausted as Korea now produced most of the non-durable consumer goods and intermediate goods used in there production. In addition, the US announced its intention to scale down and eventually terminate its aid program.

The government formulated a five-year plan that gave the first priority to the development of export industries. Virtually all the reforms that followed were directed at this objective. These reforms included the following important changes made over the period from 1961 to 1967.

1. The won was devalued by almost 50 percent.
2. A unified, floating exchange rate system was established.
3. Interest rates on bank deposits were doubled to increase domestic savings and encourage efficient use of bank credit.
4. Tax revenues were increased to cut the public sector deficit and increase price stability.
5. Trade liberalization and reform packages were introduced
6. A wide range of export incentives were implemented including:
    a) subsidized credit
    b) exemption of sales taxes on inputs used for export production
    c) a 50 percent reduction on income taxes related to export sales.
    d) tariff exemptions and wastage allowances on raw materials and equipment used in export production.
    e) government support for export marketing.

The results of these policy initiatives were dramatic. The growth rate of real per capital GNP accelerated from 1.7 percent over the period from the early 1950s to the early 1960s, to 7.1 percent over the period from the early 1960s to the mid-1970s. Exports made a major contribution to this sharp increase in growth rates rising at 30 percent a year for the 14 years after 1961. They amounted to only 1.5 percent of GNP in the 1950s, but this figure rose to 29 percent of GNP by the end of the period.

Imports also increased substantially over the period as one would expect given the liberalization of the trade regime and the incentives given the export producers in respect of their imported inputs. This rise in imports is best regarded as part of the industrialization process and reflects inflows of material inputs and equipment rather than final consumption goods.

This view is substantiated by the changes in investment and savings. While the government continued to encourage foreign investment and loans, there was sharp increase in the portion of investment financed from domestic sources. Total investment increased from 10 percent of GNP over the period from 1953 to 1960, to 23 percent over the period from 1961 to 1975. The share of domestic savings in this increasing total rose from roughly a quarter to over two thirds. The role of increased interest rates was undoubtedly important in encouraging this massive mobilization of domestic savings. The corporate sector was the major source of this saving through the reinvestment of profits.

Despite the increased per capita GNP, real wages stayed virtually constant from 1957 to 1966. Then tightening labor market conditions stimulated a sustained rise in wage rates. Real wages in manufacturing doubled between 1966 and 1975.

The changes in the structure of Korean industry can be seen in the shifts in relative output by sector. Table 1 below shows the share of GDP in each industrial sector over three time periods: 1953-55, 1960-62 and 1973-5. The share of agriculture dropped by half from the earliest to the latest period and that of manufacturing rose from 6 percent to 27 percent.

The development pattern in Korea is typical for the NICs supports the view that smaller emerging countries may be able to exploit the same opportunities. Most importantly the export lead development pattern seems capable of generating large increases in employment and ultimately in real wages.

The Role of USAID in Korea

The USAID Mission played a central role in the reconstruction effort. During the period 70 percent of Korea's imports were covered by foreign grants. Extensive use was made of counterpart funds. In fact, all major economic policy decisions even those not involving aid funds were made jointly by the Korean government and the USAID mission. Over the period from 1946 to 1976 the US supplied $12.6 billion making Korea the third largest recipient of foreign aid on a per capita basis after Israel and Vietnam. The American programs in support of Korean development were large-scale, complex and changed considerably over time starting with the US Military Government in 1945 and ending with a wind-down of the USAID program in the 1970s. Only a brief overview can be provided here.

In the immediate post-war period the major objectives were 1) prevention of starvation and disease; 2) boosting agricultural output; and 3) provision of large amounts of commodities to prevent shortages and price rises.

TABLE 1: GROSS DOMESTIC PRODUCT BY SECTOR (percentage shares)

	SWAZILAND	KOREA			MAURITIUS		TAIWAN	
	1982-86	1953-55	1960-62	1973-75	1973	1984	1951-53	1971-73
AGRICULTURE	23.4	\	\	\	\	\	\	\
FORESTRY	1.3	50.3	45.2	24.6	29.9	13.7	33.2	13.1
FISHING	/	/	/	/	/	/	/	/
MINING	2.7	1.0	1.5	1.2	0.1	0.2	1.8	1.1
MANUFACTURING	22.8	5.9	9.4	27.2	16.8	16.8	15.5	37.9
CONSTRUCTION	3.7	1.9	2.7	5.5	6.9	6.0	3.8	4.1
UTILITIES	/	0.3	0.6	2.0	2.6	2.4	1.0	2.2
TRANSPORT AND COMM	5.7	1.6	2.8	6.4	9.8	11.4	4.1	6.0
TRADE	10.6	10.0	13.0	16.9	12.3	13.8	17.8	11.1
BANKING	6.3	1.4	1.8	1.9	12.3	5.0	8.5	8.9
DWELLINGS	3.8	4.4	3.9	2.2	4.7	12.8	na	na
COMUNITY AND BUS SERVICES	na	na	na	na	4.6	12.1	5.2	5.5
GOVERNMENT	17.8	13.8	8.6	4.3	0.0	0.0	9.1	10.1
OTHER	1.8	9.3	10.3	7.9	0.0	5.9	na	na
TOTAL	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

SOURCES: Economic and Structural Change in Taiwan
Studies in the Modernization of Korea
Swaziland Annual Statistical Review
World Bank Economic Memorandum on Mauritius

An overhaul of the education system was begun under the Americans as were major investments in coal, thermal electrical power and fertilizer production. But the Korean war derailed these initiatives. In the post-war period sharp differences emerged between the Korean government and the US advisors managing the aid program. The Koreans wanted use external resources to build heavy industry and infrastructure while the Americans wanted to promote light, smaller-scale industry that would soon make Korea self-sufficient in commodities that were mainly being supplied through commodity aid. Further differences arose over the conduct of macroeconomic stabilization policy with the Americans favoring fiscal and monetary restraint, devaluation, reduction of import restrictions and general liberalization.

To summarize, the US program of economic aid had two basic components - massive commodity aid, and technical assistance. Economic stabilization and self-sufficiency were the central longer-run objectives. Project aid was largely directed at the establishment of new industries and associated infrastructure especially in transportation, manufacturing and electric power. Agriculture, education, health and other social services received relatively little direct funding. The government was nonetheless able to make some increases in social spending using the budgetary support provided by sales of commodity aid. Table 2 below shows the composition of government expenditures. Although the data are not directly comparable between countries because of accounting differences, the table shows up the relatively weak priority attached to social spending in Korea and the dominance of defence spending.

TAIWAN

The pre-war experience of Taiwan parallels that of Korea. Subsequent development was different in several important respects but it is important not to overlook the fact that, as in Korea, major steps on the path to development were taken several decades prior to the war. In fact, the war might be viewed as a temporary deviation in a continuous development process beginning at the turn of the century.

In the early 1900s trade under Japanese colonial rule consisted largely of the exchange of Taiwanese sugar and rice for Japanese textiles and fertilizer. By 1930, close to 20 percent of GDP was generated in industry. Food processing - largely sugar processing operations owned by Japanese - accounted for most of it. Some fruit and vegetable processing existed and there were the beginnings of non-durable consumer goods industry producing textiles and a few other items. This, rather than the high growth period starting after World War II is probably the best parallel to the current situation in Swaziland.

In the 1930s the Japanese began a program of investment in non-agricultural infrastructure in power and transportation as well as basic industries such as cement, chemicals, pulp and paper, fertilizer, petroleum refining and metallurgy. Unlike the pattern in other colonies, the road, rail and electrification investments were not directed solely at the extraction of a few primary raw materials, but to broad-based agricultural mobilization, especially in the fertile west coast. These investments and the extensive surveys conducted by the Japanese set the stage for later land reforms and the establishment of farmers' associations.

TABLE 2: COMPOSITION OF GOVERNMENT EXPENDITURES (percent of total)

	SWAZILAND 1984/85	MAURITIUS 1976/77	HONG KONG 1952/53	TAIWAN 1952	KOREA 1953
ADMINISTRATION AND DEFENSE	36.4	21.1	28.1	59.3	56.0
EDUCATION	23.6	14.1	\	7.8	\
HEALTH	7.9	8.0	\	\	\
SOCIAL SECURITY AND WELFARE	0.3	12.5	22.4	5.6	5.5
HOUSING	0.1	2.3	/	/	/
OTHER COMM. AND SOC SERV.	0.7	1.0	/	/	/
ECONOMIC SERVICES	31.0	40.9	28.7	11.7	37.8
Administration	2.1	0.7	na	na	na
Agricult. Fish Forest	8.0	6.5	na	na	na
Mining Manuf. Construct.	3.1	0.1	na	na	na
Utilities	0.5	1.8	na	na	na
Roads	2.8	1.3	na	na	na
Other Transport	0.4	4.9	na	na	na
Other	0.2	2.3	na	na	na
OTHER	13.9	23.3	20.8	14.1	0.9
TOTAL	100.0	100.0	100.0	100.0	100.0

Japanese policy sharply limited the participation of Taiwanese entrepreneurs in the larger industries such as food processing and intermediate goods production.

The war brought large-scale destruction of Taiwanese industrial capacity. After a period of political turmoil the National government took control in 1949. Inflation was running and 3400 percent and export production dropped disastrously. GDP was less than $100 per capita.

The government enacted a range of important policies at this time. Monetary restraints were imposed as were exchange and import controls. The introduction of tariffs, quotas, licensing arrangements and industrial subsidies, marked the beginning of the period of import-substitution. As in other countries the non-durable consumer goods were the focus of these new investments. The rupture of the colonial trade with Japan reinforced the process as Japan was no longer able to supply these goods in exchange for Taiwanese raw materials and food.

Another critical factor in the rapid switch from production of primary goods for export to consumer goods for the domestic market, was the arrival of over a million people from the Chinese mainland who filled the critical managerial and technical skill gaps left by the departing Japanese. In 1937, 64 percent of Taiwan's textiles and garments, and 57 percent of its wood and furniture products were imported. By 1954 these figures dropped to 5.6 and 7.3 percent.

Taiwan's experience in this early industrialization period is some what different than that of other countries. The degree of protection given the import substituting industries was relatively mild. Interest rates were kept relatively high, and the exchange rate was held at a high enough level to ensure some degree of competition from imports. Finally, the government generally resisted direct interventions in the markets for heavier goods such as steel, cement, fertilizer where the Japanese legacy was somewhat stronger than in other developing counties.

The infrastructure established by the Japanese helped facilitate the transition to domestic production. The high density of road and rail as well as the electrical power generation and distribution begun by the Japanese and extended by the USAID program helped to decentralize production, to keep production costs low and avoid the special problems associated with urban agglomeration.

In sharp contrast to the Korean case, Taiwan maintained and strengthened the rural infrastructure base left by the Japanese. Agricultural production increased steadily from the earliest stages of the postwar period. Rural incomes were stronger than they would otherwise have been and this helped sustain demand for the output of the new consumer goods industry. Rising urban incomes in turn assured a market for increased agricultural output. This sectorial-balanced growth is an important and unique feature of the Taiwan case.

The success of these policies was such that by the early 1950s the domestic markets for goods such as textiles, paper, rubber goods, and soap had begun to saturate. The government then had to choose between a second phase of import-substitution into more capital intensive consumer durable and producer goods, and a move towards export of the lighter goods already being produced for local consumption. They chose the latter.

The package of policies adopted in the late 1950s and early 1960s is very similar to the list of export promoting reforms undertaken in the Korean case. In broad terms they involved the partial dismantling of protection in the trade regime, elimination of the multiple exchange rate system, liberalization of the exchange allocation scheme, and a major package of tax incentives for domestic and foreign investors. These policies sparked an increase in the annual industrial sector growth rate from 10 percent in the 1950s to 20 percent in the 1960s and a gradual displacement of agriculture as the most important sector. Over this period gross savings rates also jumped form 12 percent to 26 percent of GDP exports of goods and services jumped from 13 to 43 percent of GDP between 1962 and 1972.

Part of Taiwan's success stems from the availability of cheap efficient labor. While the pool of surplus rural labor did not begin to tighten until well into the development process it is important to note the positive role of the agriculture sector in helping to keep the labor costs competitive. Of primary importance is the fact that food production was in surplus and was exported. The competitive price of food helped to keep consumer prices down which helped keep wage costs down. The decentralized nature of industry stemming from the infrastructure patterns established by the Japanese facilitated the transition from farm to factory. Transport was easy and cheap. In fact, in the 1960 less that 50 percent of farm families were fully engaged in farming.

The savings and investment picture is dominated by the USAID program. From the early 1950s until 1964 USAID provided 90 percent of foreign capital accounting for roughly 40 percent of gross fixed capital formation. Beyond 1964 USAID contributions declined rapidly. But investment accelerated from roughly 15 percent of GDP to 25 percent by 1970. The financing needed for this investment came partly from increased inflows of capital from private sources, but more importantly there were sharp increases in the rates of domestic savings. These rose from roughly a quarter to almost a half of gross fixed capital formation over the decade of the 1960s.

The Role of USAID in Taiwan

American aid was critical in assisting Taiwan along the path to sustained economic development. At the outset the aid was mainly in the form of basic foodstuffs and consumer products that helped to break the deeply rooted inflationary process. After 1955-56, the composition of American aid shifted sharply to defense. During the whole post-war period defense accounted for 59 percent of total aid, although this includes a significant portion of commodity support in the form of food, cotton, wheat, tools and lubricants.

The US also supported a substantial technical assistance program which included sending US specialists to Taiwan to assist in land reform agricultural extension services, civil aviation administration, public health, education and infrastructure projects.

The impact of American aid was summarized by the Taiwanese government in the 1965-66 China Yearbook as have the following four main thrusts.

1. Financing of 93 percent of the foreign exchange deficit between 1951 and 1964.

2. Stabilizing prices by providing large quantities of commodity aid for sale in local currency

3. Provision of $421 million in foreign exchange and NT$27 billion in local currency through counterpart fund arrangements to support investment in infrastructure including electric power, transportation, communications, mining, and military projects.

4. Technical assistance projects that provided training to some 2,700 Chinese technical and managerial personal.

HONG KONG

The industrialization experience of Hong Kong is differs somewhat from that of Taiwan and Korea. It is essentially a city state with limited land and almost no agricultural potential. It is also strategically located and initially developed as an entrepot trading center.

From its beginnings as a colony of Great Britain in the mid-1800s Hong Kong developed trade which linked China and the rest of the world. The expansion of entrepot trade led to the development of banking insurance, warehousing and port facilities that were critical for laying the foundation of the colony's future economic development. The trade also helped local businesses establish important international marketing connections that would serve them well in the later industrial period.

Until the Second World War trade dominated the economy, with industrial and manufacturing enterprises a distant second. The war severely disrupted the Hong Kong economy. Upon liberation the population was a third of its former size and both trade and industry were virtually at a standstill.

Two important factors influenced the course of subsequent development. First, the Chinese Civil War created large waves of refugees that swelled Hong Kong's population from 600,000 to 2,400,000 between 1946 and 1954. Among these refugees were a number of Shanghai industrialists who brought with them entrepreneurial skills and large quantities of capital equipment. Shanghai businesses traditionally ordered their capital equipment through Hong Kong and much of this equipment was brand new and had been sitting in storage warehouses since the outset of the war awaiting shipment to the mainland.

The second important factor conditioning development was the embargo imposed on China by the UN. This cut Hong Kong's traditional entrepot trade which had linked the markets of Mainland China with those of the West and the rest of Asia.

With these developments it became clear that Hong Kong had to shift the focus of its economic activity from trade to production. This shift involved the creation of new manufacturing industries producing light, inexpensive, labor-intensive consumer goods such as plastic products, metal ware, toys and electronic products. The speed and magnitude of the shift was dramatic. In 1953 entrepot trade accounted for 73 percent of exports. By the mid-1970s it fell to 20 percent. The role of small and medium-sized enterprises in this was important with over a third of employment provided by firms with less than 50 employees, primarily as suppliers to other export-oriented manufacturers.

How was this change possible? The marketing connections, the existence of an entrepreneurial class and the trading history have already been mentioned. The role of government was also important. A very conservative fiscal policy was adopted from the beginning. The debts incurred for post war reconstruction were quickly paid off through sinking funds and block repayments from the government surpluses generated in the early 1950s. The government offered virtually no subsidies or special concessions to industries or consumers. High reliance was placed on charges that reflected the full cost of public services. Much of the provision of public services and utilities were entrusted to private hands which, where monopolies were involved, were regulated.

For these reasons the government was able to avoid large deficits and still devote significant resources to key social sector programs and infrastructure development. The government made large expenditures on the public school system and on subsidies to the private school system. Per capita expenditure on education increased 13-fold from 1949 to 1976. Despite these increases, econometric studies suggest that the contribution of education to growth and development was relatively minor

[Ho, 1979]. This is partly explained by the structure of the Hong Kong population in which the relative of proportion of those of (expensive) secondary school age rose rapidly in the post-war period. It also reflects the relatively low priority given by students to the acquisition of technical and vocational skills which where in chronic short supply throughout the rapid growth period.

Health expenditures were also a high priority, growing by seven fold in real per capita terms between 1949 and 1975. The standards in terms of hospital beds per capita were better than in neighboring countries such as West Malaysia and Singapore but were still well below those of developed countries. Improved health can increase productivity both by reducing absenteeism. Health standards did increase as measure by crude death rates, mortality and morbidity. Available research suggests that, as desirable as these improvements may be from as social perspective, they probably contributed only a little more to growth than did the education expenditures.

The government devoted up to a quarter of its social expenditure to housing largely to deal with the squatter problem that emerged with the influx of refugees from the Civil War in China. [Ho, 1979] estimates that housing construction contributed about 1.8 percentage points to the growth over the whole period from 1961 and 1971. However housing may have had additional indirect effects through its impact on living conditions and hence productivity. Overall, social spending probably increased GDP by about 4 percent between 1961 and 1971 with housing contributing the most followed by health and education.

After social spending the second most important category of government expenditure was community expenditure which includes capital spending on roads, water supply, and land development. These had a significantly larger impact on growth than social spending and accounted for 11.1 percent of the total growth over the 1961 to 1971 period. It must be recognized, however, that Hong Kong has special development constraints in terms of the availability of land and fresh water. Much of the industrial development could not have taken place without public expenditures on land reclamation and provision of water. While these special circumstances are not may have exact parallels in other countries, the Hong Kong experience nonetheless suggests that infrastructure development can contribute significantly to economic growth.

What government did to enhance growth was as important as what it did not do. Labor markets were allowed to develop without regulation. Union activity was minimal and restricted to very narrow segments of the labor force. Real wages grew steadily throughout the period of industrialization, but because of the positive work ethic of the Chinese workers and the freedom from regulation, productivity grew even faster, and labor's share of total income shrank.

Taxes are a necessary evil. In Hong Kong the high demands for serviced land for rapid industrial development, the unparalleled increases in population, and the need to pay off debts for post-war reconstruction placed serious demands on fiscal system. The restraint exercised in offering industrial and consumer (other than housing) subsidies helped to keep overall demands on the treasury low. But the structure of the system used to collect needed revenues was also important. Charges related to industrial development including land sales and rates for water and other services were high and geared to recovering costs. The "user charge" principle was effective in promoting efficient development as well as reducing budgetary demands. Direct taxes were structured to ensure that disincentive effects on both corporations and individuals were minimized. In keeping with the entrepot tradition, Hong Kong maintained its status as a free port. This gave export-oriented firms duty-free access to both capital goods and raw materials without the cash drain, administrative clumsiness and uncertainty of the rebate or temporary admission schemes other developing countries have instituted to keep their export industries internationally competitive.

MAURITIUS

The Mauritian development experience is different from that of the other countries discussed so far. The island changed hands from the French to the British at the end of the Napoleonic wars. The British wanted it because of its good harbor, its strategic position along the trade routes to the Far East, and its stands of tropical hardwoods that could be used for repairing ships. The French had established sugar plantations in the years before the war. They were allowed to continue cultivation and the British were quite generous in allowing the French to continue their traditional cultural and economic activities. The administration of government and justice, and control of the port, however, were in the hands of the British.

The British also allowed the use of large numbers of indentured laborers from Southern India to work the French plantations. With time, the Indian population grew. The inevitable disputes between the commercial interests of the French and the laboring class of Indians arose. These were equitably dealt with by the British whose only real interest in the area was keeping the peace and keeping the port open. The separation of commercial from political power during the colonial period was an important and positive feature of Mauritian development not enjoyed by other African countries. Independence came bloodlessly and relatively late by African standards (1968). The British institutions of government and justice which had served so well during the colonial period were adopted with little modification. Today there is a democratically elected government, a diversity of relatively free newspapers and a British-style court system. French and French Creole are spoken in business and in the street, but parliament is conducted in English. Virtually nothing of the Indian languages remains.

At independence the economy was almost entirely agricultural. Sugar and sugar milling accounted for over half of GDP. The agricultural potential was almost fully exploited by the early 1970s with most of the arable land already planted with sugar, tea and a few crops for local consumption. The recurrent cyclones, roughly one every five years, limit the potential for tree crops. There are virtually no mineral resources.

From 1964 to 1972 the economy experienced low growth. GDP increased at an average rate of 1.75 per year. Investment ran at a consistent but rather low rate of 16 percent of GDP. The government deficit was very modest and the accumulation of foreign debt was kept so small that by 1972 debt service amounted to only 0.7 percent of export earnings. Population growth during this period was 3.3 percent and outstripped the 2.1 percent average annual increase in employment, with the result that the unemployment rate reach 14.9 percent in 1972.

1973 brought an unprecedented bumper crop of sugar and 1974 was again a good year. This combined with high world prices to produce a strong stimulative effect on the Mauritian economy. Two cyclones in 1975 reduced sugar production by 33 percent and world prices began to decline. But Mauritius was insulated to some degree from the adverse price movements because of long term contracts. When the price declines did make themselves felt in 1976, production had recovered. Taking the period from 1973 to 1977 as a whole sugar was undoubtedly the most important growth factor.

At the same time however, there was a sharp increase in non-sugar manufacturing. Since 1964 the government had pursued import-substitution policies through its Development Certificate scheme. This provided tariff and quota protection to local industry and gave production monopolies to certain firms. Although the domestic market is limited the scheme may have helped overcome biases against locally produced goods. With the surge in demand associated with the sugar boom these industries expanded. More important, though, was the expansion of the export-oriented industries. An Export Processing Zone was introduced in 1970, giving tax concessions and duty free access to imported inputs to export producers. The boom in sugar prices gave plantation owners an opportunity to plough back profits into new investments in the export sector. Sugar companies and traders formed joint ventures with foreigners diversifying into knitwear, clothing and other goods. Largely because of these recycled profits, investment rose sharply from 16 percent of GDP in the 1960s to over 32 percent by the mid-1970s.

Another important component of the rise in economic activity during the 1970s was the growth of the construction industry. Housing demand grew with the sugar boom and government financial support. The need to rebuild after the cyclones gave a further boost to construction.

Although savings levels initially rose in step with the sugar boom they dropped markedly after 1975 falling from 30 percent of GDP in 1973-75 down to 21 percent in 1979. The drop in savings was partly due to reductions in sugar profits, but it also important reflects important trends in the public sector. During the boom government revenues and expenditures both increased rapidly. The government held income distributional objectives as central to its development plan. Subsidies were brought in to keep basic consumer goods inexpensive. Wages and salaries in the government sector rose 5.5 fold between 1972 and 1978 while spending on goods and services rose only 2.6 fold. The government also shifted the composition of its investment sharply from productive sectors to social infrastructure including housing, education, health and water. Expenditure on these plus social security and other social services increase almost six-fold from 1972 to 1978.

Expenditures rose but with the end of the sugar boom revenues stagnated and by 1978/79 the government deficit widened to 12.7 percent of GDP. This financing gap was partly filled by increasing domestic credit and partly by increased foreign borrowing. The balance of payments deteriorated as sugar prices weakened and exports failed to keep pace with imports. Mounting debt and a hardening of credit terms brought the crisis to a head in 1979 and an economic stabilization program was established with the support of an IMF Stand-by arrangement. In 1981 the first of several structural adjustment loans was made by the World Bank. Mauritius had difficulty making these adjustments. Sugar prices were not favorable and the early 1980s saw

The parallels to Swaziland are striking. A limited domestic market and a heavy dependence on exported sugar with little opportunity for expanded sugar production are the most obvious. The conservative fiscal and balance of payments policies adhered to until 1972 closely resemble the Swazi policies of today. The sugar boom of the early 1970s generated an investable surplus which has its current counterpart in the high banking system liquidity in Swaziland. Whether the Swazi surplus is married with foreign capital and technology to produce Mauritian-style increases in manufacturing capacity and exports remains to be seen.

The strong emphasis on education is another similarity. But in Mauritius the tradition was much longer. In other areas of social expenditure Mauritius was much more liberal. The extensive use of consumer subsidies and the minimum wage scales negotiated under government auspices, especially in the sugar sector, reflect a strong income redistribution policy of the government. Health, education, and housing programs received priority from and early stage. Between 1962 and 1972 live births per thousand women of child-bearing age fell from 181.4 to 104.5. The infant mortality rate fell from 65.5 per thousand to 33.8. Life expectancy at birth rose steadily since World War II and stood at 60.7 for men and 65.3 for women by 1972. These statistics suggest that by the time Mauritius entered the 1970s period of high growth, it had made greater progress on social front than Swaziland has so far managed. These factors were important in ensuring that economic growth was not diluted by surging population growth and in attuning the population to the work standards required of modern manufacturing.

The Mauritian experience was not with out difficulties. At independence, the Indian segment of the population came to dominate most positions in government and the Franco-Mauritians lost political influence. The high export taxes imposed on the sugar during the sugar boom were not removed when sugar prices fell. The Frano-Mauritians were forced to reduce fertilization and replanting on their estates. These policies may have had a political component going beyond the desire to achieve income redistribution objectives and there was an exodus of Franco-Mauritians at the time which represented a loss of human as well as financial capital. The importance of reinvested sugar profits in fueling investment in new export industries has already been mentioned. It might well have been greater if the industry had not been so heavily taxed.

The retrenchment of the sugar industry coincided with the rise of new manufacturing industries. The mostly male plantation workforce shrank, while most of the new textile and garment factory jobs went to women. The resulting social tensions, as well as those arising between the Moslem and Hindu communities and between rural Indians and wealthier urban Chinese, were undoubtedly moderated by the progressive educational and social policies pursued in the decade before high growth.

These policies were costly however. At the beginning of the 1980s it was not clear whether Mauritius would be able to overcome the difficulties of large government deficits, inflation, foreign debt and an entrenched pattern of spending on consumer subsidies and social transfers. The government was determined, however, to build modern new industries and realized that this would not be possible if the level of intervention were not reduced and the public sector finances put in order. The measures taken included reductions in social expenditures and subsidies, and freeing of prices, interest rates and credit controls. The import licensing and quota systems were relaxed. Progress was frustrated by low world sugar prices and high interest rates. But eventually the economy turned the corner and in the latter 1980s Mauritius has resumed its course on export - lead growth with a range niche industries including cut flowers, watch faces, eyeglass frames and other small, labor-intensive consumer products joining the established textile and knitwear industries.

Finally, it bears emphasis that as a general development proposition, the old landowning classes must somehow be drawn into the creation of new industries. They are the ones with capital and often the ones with the greatest local managerial and technical skills. If the old class is corrupt and dissipated (Philippines) or the surplus is confiscated through manipulation of commodity prices and taxes (Egypt, Guyana), the leap to modernization will be difficult. Sometimes the agricultural surplus can be channeled from the old class through an efficient banking system to a new class of entrepreneurs. But such aggressive and far-sighted bankers are often lacking. Lastly, the potential involvement of the old class will be greater if, like the Franco-Mauritians, they are resident landowners facing difficulties in emigration, whose personal destinies are tied to those of the country and are not absentee landlords or foreign corporations that can easily fold operations and withdraw.

SUMMARY OF THE EXPERIENCE OF OTHER COUNTRIES

The various stages of development in the NICs are summarized in point form below:

The traditional economy

* subsistence agriculture
* feudal political structure

The colonial period
* plantation agriculture/entrepot trade
* basic agro-processing industries
* foreign control and management of manufacturing
* export of primary commodities
* import of manufactured goods
* development of basic infrastructure
* establishment of modern property rights
* subsistence wages
* forced surplus contributions
* limited but positive changes in education, health

The period of political/military instability
* destruction of manufacturing capacity
* exodus of technical/entrepreneurial class
* drop in exports

The reconstruction period
* large foreign aid flows especially food and commodities
* rebuilding of infrastructure
* modest investment
* high inflation
* large government deficits
* low interest rates
* low domestic savings
* large scale immigration including key entrepreneurial and technical groups from China

The import substitution period
* establishment of strong national government with solid technocracy and clear development objectives
* increased protection for domestic industry
* local production of consumer goods
* replacement of colonial sources of supply by local production.
* creation of labor-intensive manufacturing for local market
* neglect of agriculture
* surplus of rural labor
* slow growth of real wages
* low domestic savings
* continued flows of foreign aid and technical assistance
* negligible inflows of foreign private capital
* monetary and budgetary restraint
* limited use of subsidies
* saturation of domestic consumer goods markets
* increases in social spending
* steady improvements in health, education, housing
*

The export growth period
* liberalized trade
* liberalization of foreign exchange controls
* export incentives
* increased interest rates

* end of foreign aid
* increased domestic savings
* increased flows of foreign private capital
* sharp increases in exports of labor-intensive consumer goods
* renewed interest in agricultural sector
* tightening of labor markets
* rising real wages

The experience of the Asian NICs outlined above suggests some general conclusions about export-led development. First, it is clear that the manufacturing sector is capable of generating impressive growth in output, employment and foreign exchange earnings over a sustained period once conditions conducive to growth are attained. All of the countries in our sample experienced high growth rates in which labor-intensive manufacturing played a major role. In all cases the primary outlet for increased production was exports.

Second, all the countries benefitted from strong and coherent leadership from their governments prior to, and during, the high growth period. The forms of government vary across the countries spanning the range from military dictatorship, through personalized autocratic rule, to modern parliamentary democracy. But in each case the leaders had a clear and consistent view of where the country was going and that view was both modern and economically liberal.

Third, the NICs had extensive periods of contact with more advanced industrial and commercial economies. During this time there were important investments in infrastructure. In addition, large-scale immigration of entrepreneurs to Hong Kong from Shanghai, the movement of Japanese industrialists and technicians to Korea and Taiwan, the presence of Chinese and French and Indian entrepreneurs and traders in Mauritius all played an important part in creating a resident class capable of exploiting the opportunity to industrialize given the right circumstances.

Fourth, through land reform or other means all five countries had established modern land tenure and property rights systems well before rapid growth began.

Fifth, these countries had relatively high population densities.

Sixth, with the exception of Hong Kong all of the NICs studied here went through a period of import-substitution during which industries supplying the domestic market benefited from a number of special policies. These included high levels of protection from imports by virtue of tariffs and quotas. In addition, licensing regulations, and exchange rationing also served to protect domestic industry. These policies are judged to have spawned a certain level of inefficiency in production. The industries involved tended, with some exceptions, to be labor intensive which meant increases in employment. But the potential for advancement through these channels were exhausted within roughly a decade as firms encountered limits imposed by domestic market size and an inability to compete internationally.

Seventh, prior to industrialization some NICS, especially Korea and Taiwan, experienced periods of rapid inflation, large government deficits and excessive monetary growth. Before the economies "took off" these problems were addressed with a range of inappropriate polices including price controls and restrictions on bank deposit rates that implied a negative real return to savings.

Eighth, with the end of the "easy growth" afforded by import substitution, there came a period of major changes in macroeconomic policy. These included:

1. Sharp increase in bank deposit rates

2. Adjustments to the balance between government revenue and expenditure

3. Stricter control of the money supply

4. Liberalization of the trade regime

5. Changes in the structure of taxation designed to promote foreign and domestic investment

Ninth, the period of rapid growth was characterized by a sustained high level of investment in which foreign savings played an important role. USAID funding in Korea and Taiwan was large but its importance was confined to the import-substitution period. Foreign private capital did not materialize until the export period. But the single most important source of finance in most of the NICs during the period of rapid growth was domestic savings.

Tenth, during the initial stages of the rapid growth period there was only a weak tendency for real wages to rise. This pattern persisted until excess labor, mostly from the rural sector, was absorbed. Then the pace of wage gains quickened, but not sufficiently to thwart further investment. Investment remains relatively labor-intensive throughout.

Eleventh, the growth in exports was accompanied by a parallel growth in imports of raw materials, intermediate goods, and capital equipment. While value added in the manufacturing sector exhibited some tendency to deepen over time it all the countries continue to be highly open economies in which relatively unobstructed access to imported inputs is critically important.

SWAZILAND

The Colonial Inheritance

In 1902 when the British Colonial Administration took office in Swaziland its first task was to sort out the conflicting land claims arising out of the concessions granted by the Swazis in the late 1800s. Despite an obvious misunderstanding on the part of the Swazis about the permanence of the concessions, the country was carved up with 34 disjointed areas covering about 37 of the total land area allotted to the Swazis. The rest was held by Europeans.

Prior to 1940 the British had little interest in development of the region. Swaziland was regarded as remote, resource-poor and it was widely assumed that it would eventually be incorporated into the Union of South Africa. Until 1939 there were no railroads and the roads were largely impassable in the rainy season because of lack of bridges. By 1938 there had been very little development and 40 percent of the European landowners were absentee landlords.

Nonetheless important features of economic and social system had emerged by this time. Some 15,000 Swazi were squatters living and working on privately owned land. Another 14,000 worked on a temporary basis in South Africa, largely in the gold mines. The asbestos mine at Havelock was opened in 1939 and there were three small tin mining operations. But on the whole the pre-war efforts at economic development had been minimal and exports reached only 450,000 Rand by 1940

After the war the climate changed. It became clear that the British Administration would continue for some time as the South Africans had dropped there pursuit of incorporation. A number of important resource sector investments were made. The Colonial Development Corporation started plantations of eucalyptus and softwoods. With subsequent private investment, the total forest area grew to 240,000 acres by 1968. Irrigated sugar plantations and a sugar mill were established in the lowveld. The asbestos mine at Havelock led the development and from an early stage contributed as much as seventy percent of the territory's income tax revenues. An iron mine was established in 1964 to supply ore to Japan.

These developments reflect a sharp dualism in the economy. Exports were overwhelmingly of primary raw materials. Participation by Swazis in at the management and technical levels was virtually nil. Important infrastructure investments were made in roads, railways, power and communications, but between 1955 and 1966, 78 percent of public investment went into economic overhead, largely in support of the modern sector. Only 12.5 percent went into social overhead and a mere 9.1 percent into Swazi agriculture, although about half of the economically active Africans were engaged in subsistence farming.

The Swazi agricultural sector lagged far behind the modern sector. Less than 7 percent of the irrigated land was in Swazi territory in 1968. Traditional subsistence methods dominated with a high reliance on cattle raising. The cattle furthermore play a central role in Swazi culture as a measure of wealth and as part of the lobolo, or bride-price, system. The gross income from sales of cattle and cattle products among cattle owning families in 1964 was only 20 rand or about the equivalent of 3 - 4 weeks work in the wage sector.

After 1964 there was a shift in the pattern of public expenditures that reflected concerns about the imbalances in development. Relatively larger amounts were devoted to education, training and agricultural credit in the Swazi sector. Independence came in 1968, but the brief period of investment in human capital in the previous three years was inadequate for the needs of self-government. In the main the course of economic development over the next two decades remained broadly consistent with the patterns that emerged under colonial rule.

The Manufacturing Sector and Exports

Table 3 shows export patterns in Taiwan, Korea and Swaziland. In the early 1950s exports of the two NICs were highly concentrated in food and crude materials. Swaziland's exports are primarily sugar, pulp, fruit and vegetables. This is similar to the structure of Korean and Taiwanese exports in which there was a high proportion of sugar, rice, grains and canned fruits and vegetables. In fact the relatively higher proportion of manufactured goods in Swazi exports, which reflects the new textile and footwear industries, suggests that Swaziland may be slightly ahead of the stage that these two NICs had achieved in the early 1950s.

The data on the sectoral distribution of GDP shown in Table 1 supports this conclusion. The share of manufacturing is higher than in the NICs in the early 1950s. Some of this is attributable to the new relatively labor-intensive textile and footwear industries, but a large portion is accounted for by the relatively capital-intensive processing of primary commodities, particularly sugar and pulp. These are industries where there is relatively little prospect for growth. Moreover, the share of manufacturing has been stagnant over most of the 1980s and would have declined without the establishment of the Coca-cola plant.

Further manufacturing sector growth will have to come from the production of lighter non-durable consumer goods if Swaziland hopes to follow the same path as the NICs. This will mean expansion of the existing textile and garment industries. It will also mean branching out into a range of other products. Opportunities in these areas are identified in the section on the role for USAID.

Labor Markets

The distribution of economically active Swazis between wage and non-wage employment, and the high proportion absorbed in traditional rural activities, is perhaps the best indication of the differences that exist between the structure of the Swazi economy and that of the pre-takeoff NICs. The traditional sector accounts for three quarters of domestic employment (excluding migrant labor in South Africa). This proportion is rising, largely because formal sector growth is failing to keep pace with population growth of 3.6 percent annually - one of the highest rates in the world.

Underemployment in the traditional sector is difficult to measure accurately, but it is undoubtedly high. Moreover, the additional number of people seeking paid employment each year is estimated to be about 8500. With formal sector growth of projected at 1.7 percent in the fourth plan, there will be a shortfall of roughly 4000 jobs per year. Many of these people will end up in the traditional sector by default.

Migrant labor to South Africa is an important part of the employment picture. There were 22,000 migrants in 1986 (and perhaps 20-25 percent more working illegally). This is about 23 percent of the total number of wage earning Swazis. The number of migrants has changed sharply from year to year depending on the needs of the South African mines and on the perceptions about the diligence of Swazi workers relative to that of workers from other countries in the region. The longer term trend is towards increasing migration. This runs counter to the trend for other countries who have supplied a shrinking number of workers especially in the mines. The other states are seeking eventually terminate the migrant labor system through the Southern African Labor Commission. By contrast Swaziland (which is also a member) has made explicit provision for migrant labor in its current development plan.

Wages for labor in South Africa are higher sufficiently than in Swaziland that there has always been an excess supply of willing migrants. Increasingly there are pressures from neighboring Mozambique. Competition is sharpening for jobs in South Africa and also in Swaziland itself as Mocambicans fleeing military disturbances at home are willing to work for very low wages.

South Africa has shortages of skilled workers technicians and managers. The system of work permits is much less limiting for people with these skills and the wage rates are much higher in South Africa. Data on the numbers of such migrants are weak but it is clear that there is a strong incentive for people with skills to migrate.

Interviews conducted for this study suggest that the central problem facing industry here is lack of local management skills. One major firm with investments in several separate enterprises said that there were opportunities for some of its companies to expand production to supply additional markets and to add new items to the product lines. However, for lack of management capacity these opportunities are not being exploited. Another businessman stated that he could hire 100 Swazis for every 2 managers that he could get here. Difficulties in getting residence permits for foreign managers are therefore a sensitive issues.

TABLE 3: COMMODITY COMPOSITION OF EXPORTS

	SWAZILAND	KOREA			TAIWAN	
	1986	1953-55	1960-62	1973-75	1952-54	1973-75
FOOD AND BEVERAGES	49.5	5.9	32.1	10.1	91	16
CRUDE MATERIALS	21.5	86.7	44.0	4.3		
MINERAL FUELS	6.6	2.7	4.8	1.9	4	2
CHEMICALS	0.2	0.6	1.5	1.7		
MANUFACTURES	11.6	3.7	13.2	67.9	5	29
MACHINERY, TRANS EQUIP	0.6	0.3	1.9	13.9		23
OTHER	10.0		2.6	0.3		
TOTAL	100.0	99.9	100.1	100.1	100	

Labor markets in Swaziland are slack because of the large supply of rural labor for most jobs other than very low wage cane-cutting or casual farm labor where Mozambicans can be hired. Real wages in the industrial sector are somewhat higher than what was earned in the pre-takeoff NICs. Productivity standards are lower than what prevailed in the NICs. Excessive wage increases without increases in productivity will stall the industrialization process.

Government Finances and Macroeconomic Policy

In many respects the Swazi public sector finances and macroeconomic policies compare quite favorably with those of the NICs at the critical time when they began their periods of rapid economic growth. In the late 1940s and early 1950s Korea and Taiwan had serious problems with inflation and a public sector deficits. Hong Kong and to a lesser extent Taiwan had sharp increases in population that put major pressures on the government sector.

Mauritius, Korea and Taiwan all adopted inward-looking industrial policies that did little to encourage exports, and they maintained overvalued currencies and rigid foreign exchange allocation systems. These policies plus the tariff and quotas imposed on trade did not favor foreign investment, and foreign private capital inflows were minimal.

By contrast, Swazi macroeconomic and public sector policies are widely regarded as liberal. Direct intervention in the private sector is minimal. The government deficit presents no threat to stability. Foreign debt is manageable. Personal and corporate tax rates compare favorably with those in other countries and there are liberal rules regarding the repatriation of dividends and profits.

These are all important and positive features of the Swazi system, but they need to be put in perspective. Much of the economic turmoil experienced by the emerging NICs was as a result of the war. Their ability to stabilize their economies and rebuild damaged productive capacity in a very brief period is remarkable. The import-substitution policies they subsequently adopted seem out of step with modern notions about export led development. But they were probably the best policies for the circumstances and reflect development opportunities that are not available to Swaziland. Korea and Taiwan had large domestic populations which suddenly lost the prewar sources of manufactured consumer goods from Japan. Replacement of these goods, especially the lighter labor-intensive ones, by domestic production was logical for them and enabled them to move by stages into export production.

Hong Kong had too small a domestic market to make the import substitution phase a practical intermediate step. But it had strong commercial links to Western markets and a tradition of banking and finance. These factors made it easier for them to make the transition to production of goods in which they were already trading. Both Hong Kong and Singapore sidestepped the import substitution phase and left foreign trade relatively free. Only Mauritius tried an import-substitution in a small market. Barriers to trade were erected to stimulate development in a few selected industries including batteries, rubber tires, television and motorcycle assembly, and several others. But these efforts were not judged to be very successful and it was feared they would begin to create a high cost economy. Gradually the barriers have been reduced.

Swaziland has neither a large domestic market nor established trading and banking business to link it with external markets for manufactured goods. What it does have is a large and relatively developed neighbor.

The Special Relationship With South Africa

Membership in the Southern African Customs Union (SACU) and the Common Monetary Area (CMA) are two important features of the relationship between South African and Swaziland. SACU provides for the free passage of goods between South Africa, Lesotho, Botswana and Swaziland. It also establishes a common tariff for these countries with respect to the rest of the world. SACU also provides for the distribution of revenues from customs, excise and sales duties collected within the SACU countries according a formula that roughly approximates the revenues that each country would collect if they applied the common sales, customs and excise duty rates independently. The shares due the BLS states according to this process are then grossed up by 42 percent to reflect costs of loss of fiscal autonomy by the smaller BLS countries. Provisions have also been introduced to allow BLS states to impose additional temporary duties to protect infant industries.

Swaziland gets over half of its revenue from customs duties and excise taxes. While there are undoubtedly some costs to being in SACU it seems likely that the 42 percent gross-up more than compensates for them. Moreover, withdrawal from SACU would mean establishing a full customs administration system which would strain already thin human resources. Swaziland already compensates exporters for duties paid on imported inputs. The system does not function perfectly but this type of problem would exist even if Swaziland withdrew from SACU.

Over 90 percent of Swaziland's imports come from South Africa and about 25 percent of the exports go there. Trade with South Africa is unbalanced. While Swaziland maintains a moderate deficit in trade as a whole - E 199 million in 1986 - it has a large deficit with South Africa. In 1986 this deficit was E 575 million which was partially offset by a surplus of E 376 million with other countries. An important factor in the deficit with South Africa is that, despite the customs union, Swaziland's most important export barred from the South African market because of the powerful sugar producers' association there.

Sanctions may provide an opportunity for Swaziland to encourage South African investors to establish production here. Swazi products are not currently subject to sanctions and if domestic value added exceeds 25 percent the goods get duty-free access to the European market under the Lome convention. Further benefits to local production stem from Swaziland's membership in the Preferential Trade Area (PTA).

These are powerful incentives to locate in Swaziland. They counter the effects of South Africa's wide-ranging system of industrial subsidies designed to attract industry to the homelands. A number of firms have already moved here. It is worth examining these cases closely. Companies that come to Swaziland because of sanctions may not be coming here because of economic fundamentals reflecting Swaziland's comparative advantage. Capital-intensive operations such as the new Coca-Cola concentrate factory are not moving here to take advantage of the lower wages. The jobs that are generated as well as the additional tax revenues are welcome, but it must be remembered that all firms create demands for infrastructure development that require government resources. Labor-intensive operations that move here because of sanctions may generate more wage income per unit of infrastructure required. On the other hand, if their own capital investments are relatively small, they may be the first to pull if political improvements lead to a softening of sanctions. In addition, there is potential for sanctions-busting firms to spoil Swaziland's reputation by false labelling or similar practices that might cause some countries to extend sanctions to Swaziland as well.

Export development will be key for industries hoping to produce on any significant scale. It is natural for South African investors to consider sales in the Republic as a first step towards building international markets and a number of them have followed this pattern. However, South Africa is a relatively highly protected market to which Swaziland has duty-free access. Being competitive there will not necessarily mean being competitive in other countries. Very capital-intensive industries that gain little advantage from Swaziland's cheap labor may find international competition stiff. Firms that buy outmoded or poorly reconditioned, second hand equipment may also find it difficult to move beyond the protected SACU market.

South Africa is an economy with some serious economic problems. Inflation and interest rates are much higher than most industrialized countries. The government finances are not well-ordered, and the pressure on the rand reflects more fundamental problems than just the short-term liquidity difficulties of rolling over foreign debt. For these reasons it will be wise for Swaziland to diversify its trade with countries outside the SACU area. The greater the focus of new manufacturing experts on markets in North America and Europe the less reliance will have to placed on South Africa where a fairly sharp economic contraction is possible.

Currently disinvestment dominates the investment picture in the South Africa. But this may not always be the case. There is a natural tendency for such a large country to use a small neighbor a source of raw materials and to consolidate production in its own core industrial area. Swaziland needs to be conscious of this fact over the longer run. If a close association of South African interests has control over most of the timberlands, it might not be in their interest to maintain pulp production here. Coca Cola might have decided to leave South Africa even without the effect of sanctions. But would it have left if the sugar producers had not been so effective in keeping the cost of South African sugar high. What would happen if the sugar producers managed to close off imports of high sugar content imports as the American sugar producers did with Canadian confectionery imports?

These particular cases may pose no serious problems, and it would send damaging signals to the international investment community if Swaziland were to start discussing investment review procedures or tightening rules relating to foreign ownership and control. But given the already high proportion of foreign ownership, the relatively small local participation in management and control, the natural tendency for small countries suffer a drain of skilled people and raw materials to larger, more developed neighbors, and the uncertain and perhaps temporary effects of sanctions, it is important that Swaziland have the capacity to monitor and analyze developments in the industrial sector. In this regard it is worth noting that the government does not currently publish accessible statistics on value added by manufacturing subsector and this is the sector on which the greatest hopes for growth are pinned.

The CMA is an institution which has probably good for Swaziland over the longer term. The linkage of the lilangani to the rand has meant an effective surrender of control over monetary policy. Foreign exchange reserves must be held in South Africa. Interest rates here cannot deviate from those in South Africa by more than a point or two without straining the system. Inflation in South Africa is directly exported to Swaziland via the fixed exchange and the high volumes of imports from the RSA. But the system has provided stability in transactions with the rest of the world, and the constraints on the Swazi monetary authority have ensured that inflation has been very moderate by African standards and the buildup of foreign debt has been modest.

There have been some costs to membership in the CMA. There is a loss of seigneurage on currency, the reserve interest rate could be higher, and there are limitations on the way credit can be used to influence sectoral and regional development. These costs have probably been small relative to the benefits. The question for the future is whether South African monetary policy results in stable prices and interest rates in the RSA. If economic conditions there deteriorate too much delinking the liLangani may become necessary. But this is a decision that will be taken with the advice of the IMF and there is probably little input that USAID usefully provide.

Institutional and Social Considerations

The strength of the traditional system is the single most important difference between Swaziland and the pre-takeoff NICs. In the colonial period of the NICs the traditional power structure was completely supplanted by a colonial one. Land ownership and property rights systems were fully implemented. The laws governing economic transactions were set on modern lines. Where elements of the older systems were left intact, as was the feudal landowning class in Korea, they were subordinated to the modern system in terms of taxation, land titles, labor laws, etc. When independence came the new leaders inherited unified systems of government with well defined areas of authority and a bureaucracy experienced in running government according to modern principles. These factors also made it easier for foreign donors to implement programs of reconstruction and development.

Because these steps were not taken in Swaziland an economic and social dualism has emerged that does not fit the NIC pattern. In particular, the system of common land use and the fact that allocations of Swazi Nation Lands for individual or family use are made by local chiefs on a temporary or indefinite basis has slowed the development of these lands. Families have a reduced incentive to establish permanent housing if they do not hold inalienable title to the land. The shift into the monetary economy by the growing of cash crops is slowed for the same reason. There have been some changes in this area, notably the rise in the commercial cultivation of cotton by small farmers. But it is likely that production of cotton and as well surpluses of maize, vegetables and other crops for local market sales would increase more quickly if the land tenure system were changed. Development of irrigation and other common property resources will proceed more quickly if the benefits of such investments can be exploited by individuals with a clear stake in the land improvements. Swaziland may be able to industrialize without modernization of the agricultural sector, but the advantages of the balanced development of agriculture and industry are clear from the Taiwan experience.

The Prospects For Growth

In Swaziland there is clear potential for increased employment through export of labor-intensive consumer goods. This process has already begun with investments in footwear, textiles, garments, furniture and other products. The current set of industries is somewhat more capital-intensive than was the case in the NICs, but this will probably change as value added deepens and production moves downstream into more labor-intensive activities.

Particularly encouraging is the high level of investment. The National Accounting data indicate that investment is running at about 30 percent of GDP. This is very high and compares quite favorably with the NICs. While accounting practices, which vary from country to country, may partly explain Swaziland's relatively high investment ratio, there was clearly a rise in the rate of investment over the 1970s and this has been sustained through the 1980's. It must be remembered, however, that much of the investment is financed out of the retained earnings of private corporations many of which are foreign owned.

The experience of the NICs suggests that appropriate macroeconomic policies, particularly the trade regulations, the exchange regime, fiscal policy, and money credit and banking policies are essential. In addition, a unified political structure with clear development objectives, supported by a bureaucracy of depth and integrity are needed.

In summary, the plusses and minuses of the current Swazi situation vis a vis the NICs stack up as follows. On the negative side there are these points.

* Lack of a large internal market and the impracticality of using import substitution policies to nurture new industries.

* Lack of a trading tradition and market linkages to exploit in establishing new industries.

* No wave of immigrants with entrepreneurial skills and capital for development.

* A very small base of resident entrepreneurs and managers.

* A drain of human resources to other countries able to offer higher economic rewards.

* An awkward blend of modern and traditional elements in the political structure.

* Weaknesses in government administration resulting in delays and unevenness in the decision making process that frustrate the conduct of business.

* High levels of foreign ownership

On the positive side of the ledger there are a number of important factors.

* Stability of the political structure.

* Relatively cheap and cooperative labor.

* A favorable climate for foreign investment in terms of taxes, credit and foreign exchange transactions.

* A well-ordered macroeconomic picture especially in terms of the fiscal and balance of payments situations.

* Some qualified benefits from participation in the CMA

* Some clear trade advantages because of the Lome convention and membership in the PTA and SACU.

* High rates of investment.

The experience of the NICs also indicates that a healthy balance between agricultural and industrial growth will benefit the developing country. In Swaziland the opportunities for expansion of sugar and citrus are limited by the availability of irrigated land. Several schemes are under consideration and a large feasibility study is being supported by the French. The main issue is whether the investment will generate an adequate return. With the exception of one state-owned sugar operation, all irrigated agriculture takes place on ITF land. Some rainfed maize and cotton is also produced on ITF land. The output of the ITFs has been relatively steady and is not likely to increase significantly.

Growth prospects in the agricultural sector are subject to a number of limitations. Sugar is the most important agricultural product. Virtually all of it is on irrigated land. But the costs of further irrigation are probably too high to make expansion economic. There have been a few employment gains in sugar production because of the reversion to manual cutting brought about by currency movements and increased costs of machinery. But these job gains are a one time thing and the wages earned by cane cutters are seasonal and very low. The dependence of the sugar industry on quota access to the artificially high prices in the protected markets exposes it to some risk and limits the potential for profitable expansion. Gradual conversion of sugar lands to other crops with sounder economic prospects would be prudent. Citrus is an obvious candidate.

An irrigation scheme is currently being considered to support citrus production north of Bhalekane. Another large scheme involving several separate dams is under discussion to irrigate as much as 55,000 hectares in the middleveld and the lowveld. The difficulty again, however, is ensuring an economic rate of return.

The timber industry is unlikely to expand in the foreseeable future and there are even tentative plans to automate production in one mill which would mean a net loss of jobs.

If economic factors limit increases in irrigation, it would seem that the scope for greater large-scale plantation style agriculture is relatively restricted. By contrast there may be potential for increases in small scale production. There have been steady increases in the planted areas, yields and production of maize. Much of this increase is attributable to smallholder production. Commercial Individual Tenure Farms currently account for less than half the maize production.

Cotton is often mentioned as an important potential area for growth especially for smallholder. Rainfed smallholder cotton production is important, however, its share has slid from roughly 60 percent down to 50 percent of total production since 1980 despite good rains last year. Total production is highly variable but trend growth is very low.

To summarize the prospects for growth it is perhaps easiest to compare the current situation in Swaziland with that which occurred in the NICs at the time they were entering their periods of high growth. Table 4 tries to capture graphically this comparison. Each of the five countries is rated on a scale of one to five according to a range of indices of development potential.

What the table indicates is that while Swaziland compares favorably in terms of social/economic stability, cheap labor, trade preferences, savings rates and general macroeconomic policy, it is well behind the others in terms of economic dualism, property rights, health, management skills, resident entrepreneurial skills, government administration and foreign ownership. If Swaziland is to succeed in attaining export lead growth, these are the areas it will have to address most urgently.

TABLE 4: COMPARISON OF SWAZILAND AND NICS AT POINT OF TAKEOFF

	SWAZILAND	MAURITIUS	KOREA	TAIWAN	HONG KONG
DUALISM	*	***	***	***	****
SOCIAL/POLITICAL STABILITY	*****	***	**	**	*****
MODERN UNIFIED GOVERNMENT	**	****	****	****	*****
PROPERTY RIGHTS	*	*****	*****	*****	*****
EDUCATION	***	****	****	****	*****
HEALTH	*	***	****	****	***
STRONG AGRICULTURAL SECTOR	****	****	****	*****	*
RESOURCES	***	*	***	****	*
MANAGEMENT SKILLS	*	**	***	****	*****
CHEAP LABOR	*****	*****	*****	*****	*****
RESIDENT ENTREPRENEURIAL CLA	*	***	***	****	*****
GOVERNMENT ADMINISTRATION	*	**	***	****	*****
FOREIGN OWNERSHIP	**	***	***	***	****
INTERNAL MARKET SIZE	*	*	*****	*****	**
TRADING TRADITION	*	**	**	**	*****
TRADE PREFERANCES	****	****	**	**	***
MOBILIZATION OF SAVINGS	****	***	**	**	*****
MACROECONOMIC POLICY	*****	***	**	***	*****
EXTERNAL AID	?	***	*****	*****	**

* POOR
** FAIR
*** AVERAGE
**** GOOD
***** EXCELLENT

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THE ROLE FOR USAID IN PROMOTING DEVELOPMENT IN SWAZILAND

The paper entitled Industrialization Prospects for Swaziland and the Experience of the Newly Industrialized Countries outlined a number of parallels that exists between the NICs and the Swaziland. These suggest that there may be some prospect for Swaziland to enjoy the same sort of export lead manufacturing growth that the NICs succeeded in achieving in the 1950s 60s and 70s. However the paper also concludes that there are some important gaps that will have to be filled first. There is a potential role for USAID to play in filling these gaps. While it would seem unlikely even under the most favorable circumstances that Swaziland will reach the same sustained rates of real growth that the NICs did, USAID can still be instrumental in raising growth above what it would otherwise be. The purpose of this short paper is to examine what specific options USAID has in this area.

Business Management Skills Development

The existing training programs supported by USAID focus on a range of professional skills such as accountancy, engineering, education and health. The Manpower Education and Training Report of the ILO confirms that these are indeed areas of need in which the levels of localization are low. However, of the 45 skilled occupations in the private and parastatal sector reported in the National Manpower Survey, management is the one that employs the most non-citizens. The level of localization of these private sector management positions is also low - less than 40 percent. Firms interviewed during the preparation of this report all indicated that shortages of good managers were a major constraint on the expansion of industry. The repeated complaints about residence permits are symptomatic of this problem. Given these concerns it would seem appropriate that management training be given priority in the USAID program.

Government Administration

There is general concern about the ability of the bureaucracy to make timely and informed decisions affecting business. The largest firms may be able to get the required attention by going to the highest levels, but the rest suffer because of weaknesses in administration. USAID can assist in overcoming these problems in a number of ways. Training with a focus on public administration could be pursued within the context of new or existing programs.

Placing experts in key ministries is a standard method for improving the civil service. The best results are obtained when the expert has explicit responsibility for counterpart training and where a portion of his time is insulated from line-duty demands. The expert should have the scope to help improve the system, not just cope within the context of the existing system.

An arrangement in which there is one expert in the ministry and a parallel expert in the USAID mission or in the US might be useful. It could provide the minister with needed day-to-day services and at the same time provide a window on ministry affairs that would sustain work on improvements to administrative structures and procedures.

The government has showed some inclination to set up special bodies to deal with problem areas. The Tax Advisory Council and the soon-to-be-announced Customs Advisory Council are examples of bodies established because the existing bureaucracy found it difficult for a number of reasons to function effectively. These represent opportunities for key groups to influence the formation of new administrative structures. The input of USAID supported experts could prove valuable.

Product Diversification and Export Promotion

Swaziland has already had some successes in establishing manufacturing sector enterprises. Textiles, garments and footwear have a good foothold here. These were key areas of development in most of the NICs and are likely to be important to Swaziland. But there is a long list of other products that were important to the NICs. These include such things as: toys, dolls, wigs, eyeglass frames and sunglasses, party masks, dog collars, low quality kitchen utensils, luggage, hand bags, sports equipment, gloves, handkerchiefs, sheets, pillow cases, towels, key chains, dime store jewelry, umbrellas, brushes, nailfiles, watchbands, buttons, pen and pencil sets, clocks. This list is representative rather than comprehensive but it demonstrates some important facts about NIC exports.

1. The goods are all labor-intensive

2. They are small "niche market" items unlikely to provoke tariff or quota restrictions from developed countries. (Even tiny Mauritius faces quotas for some of its garment products).

3. They are based on relatively simple production technologies.

4. They are all consumer products and as such require specialized knowledge of design, packaging and quality consistency relevant to foreign buyers.

5. They are marketed through distributors who deal in a wide range of goods, or go directly to buyers for large retail outlets such as department and drug stores that often have multi-store chains.

Establishing new businesses in these areas requires product and market research in which USAID might play an important role. The first step would be to commission a study to determine new product possibilities. The focus should be on finding those that have relatively simple labor-intensive production processes. The second step should be to identify the potential markets for these products. Lists of distributors should be drawn up and price and volume information should be collected. Data on other suppliers should be compiled as well.

Some products from developing countries are made using local designs. The small furniture and wooden shelves produced by Swazi Pine are a good example. Research into product design appropriate to Swazi skills and resources could be supported and the tooling and plant requirements identified.

But in many cases the products are made from designs and specifications set by the buyers. This is typical of most clothing consignment orders and applies top a wide variety of other products as well. Knowledge of these specifications and standards is essential to determining the nature of capital equipment needed and to assessing the profitability of making a given product. Information of this sort could be compiled in a series of industry studies. Promising projects for development could be exposed to both domestic and foreign interests.

It is important to remember that the pleasant living conditions and favorable macroeconomic policy environment will not attract business if no one is aware of the opportunities here. Mauritius, for instance, has been very aggressive in marketing itself and this has paid off for them.

Some Opportunities in the Agricultural Sector

Research into alternative crops might be considered especially for the sugar lands. Nut crops such as cashews, macadamia nuts, pecans and almonds are possibilities as well as a variety of spices such as allspice, nutmeg, cinnamon, cardamom, pepper and coffee. These are high-value low-volume products with limited transportation and storage costs. The harvesting and basic processing required is also fairly labor-intensive. A number of them are tree crops that would take 5 or more years to yield. However, if they prove suitable for cultivation on sugar lands it is possible that the trees could be intercropped with the sugar until they mature thereby minimizing the costs of plantation development. Some of these non-traditional crops may also be suitable for rainfed cultivation.

Casual observation suggests that rainfed agriculture opportunities on SNL are less than fully exploited despite the fact that the intensity of agricultural effort is increasing there. The number of tractors on SNL rose from 884 in 1976 to 2116 in 1983. Over the same period the number of tractors on the ITFs declined from 1989 to 1671. The relatively greater opportunities for agricultural sector growth outside large scale "plantation-style" sugar and citrus cultivation are already reflected in USAID's program. The major projects include The Cropping Systems Research and Extension Training Project, Commercial Agriculture Production and Marketing, and the Swaziland Economic and Entrepreneurial Development Support project.

Support for the agricultural sector may be successful in increasing cotton production on SNL. There may be potential for production and export of some of the non-traditional crops mentioned above. Although they are not related to exports, there is undoubtedly greater potential for maize and dairying on the SNL. But the vast majority of SNL remains as common grazing land that is increasingly subject to population pressures and environmental degradation. Traditional political structures may slow the effective and environmentally benign development of these lands.

Housing and Urban Planning

Strictly speaking this is not an area that comes under the heading of export development. But there are a couple of important links. The first is that if export oriented manufacturing does grow rapidly in the coming years there will be a sharp increase in the level of activity at Matsapa. Currently there are indications of a housing problems there and these will become more critical with time. Development of a large unregulated squatter's slum around the industrial district can be avoided, but only if appropriate steps are taken soon.

The whole of the Manzini-Mbabane corridor is likely to increase rapidly in population especially if the manufacturing sector grows. Currently much of this land is SNL but parts of it are title deed land as well. There needs to be a coherent plan for the development of the region or there is potential for serious difficulties which may ultimately affect the attractiveness of the area to foreign investors.

This is an area in which USAID might play a role. With cooperation of the relevant ministries, the objective would be to develop a longer term development plan for the region.

Program Aid

Program aid is a key part of the American aid in many countries. It is usually included for one of several reasons. First, there may be shortages of specific commodities that the US is in a position to supply. Second, the country may experience budgetary or balance of payments pressures that can only be addressed with relatively liquid and fast-disbursing program aid. Finally, program aid can be used to help leaders make difficult decisions regarding economic policy.

These conditions do not exist in Swaziland. There are no acute chronic commodity shortages, the fiscal and balance of payments situations are quite healthy, and economic policies are generally solid. The only areas where policy changes might have a favorable economic impact concern land tenure and political structures. But these are very sensitive areas that are probably best not addressed through program aid.

The one area where program aid might be considered is in promoting sector adjustment policies in agriculture. There have been difficulties with agricultural marketing arrangements especially with pineapples. Program aid might be effective in promoting better privatization, pricing and marketing policies.