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SUBJECT · PPC Research Program (Economic) ERP Summary No. 25
Study of Regional Economic Cooperation in South and Southeast Asia
University of Wisconsin Contract AID/csd 355

REFERENCE: (A) AIDTO CIRCULAR XA 1348, ERP Summary No. 20, 10/25/67
(B) AIDTO CIRCULAR XA 2229, Abstracts of Research Papers (RPs), 1/31/68

A. Introduction: Presentation of Research Results

Results of the Wisconsin research program on Economic Interdependence in Southeast Asia are available in several forms: research papers, conference papers, background materials and a final report. The main documents are Research Papers (RPs), so designated because they are suitable in scope and content to warrant submission to and publication in professional journals. These documents are listed in Appendix A and form the core of this Summary of Research. Copies of all RPs are available from AID/Washington. Abstracts of RPs are included in a Supplemental Airgram, AIDTO CIRCULAR XA 2229 dated January 31, 1968.

Conference Papers (CPs) are similar in form and substance to research papers, but have been listed separately because they were specifically prepared for the Wisconsin-AID Conference on Economic Interdependence in Southeast Asia held in Bangkok in January 1967, and will be published in a separate volume by the University of Wisconsin Press, 1968. Brief abstracts of the conference papers are included in Appendix B.

Certain other background materials have been prepared in connection with the contract objectives. In this category are papers considered by their authors or the Director of Research as either (a) not having reached the stage of research papers as defined above; (b) consisting of general surveys or background materials on a particular subject; or (c) representing

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short reports on a specific contract topic. Where appropriate these materials have been referred to in the following paragraphs, but they have not been abstracted.

A Final Project Report (IV-22*), now in progress, will systematically summarize and integrate individual Research Papers, Conference Papers and Background Materials.

B. Interrelations of the Separate Studies

Since most of the papers address themselves to a relatively narrow range of problems within the broad framework of this research project, this brief summary has been prepared to point out some of the most important inter-connections among the various papers. Viewpoints of individual authors sometimes differ and the University of Wisconsin itself does not always concur with the views of the individual authors. The five-fold division used during the project and outlined in AIDTO Circular XA 1348 is followed here.

1. Selected Aspects of the Theory and Experience of Economic Growth in Southeast Asia. -- Several studies have been undertaken to attempt to improve our general understanding of the development process in Asia and thus to provide background information for determining the applicability of various forms of economic cooperation and integration in Southeast Asia. At the most general level, Myint (RP:III-37) warns that the basic diversity among underdeveloped countries and particularly those in Asia precludes applying automatically any single theory of development. One implication of this position is that the more conventional forms of cooperation based on a general or uniform set of rules applying equally to all countries as in the European Economic Community (EEC) may be difficult to achieve in Asia. Myint pursues this theme (RP:III-38) by comparing the approaches to planning and economic policy-making for Asia's inward and outward looking countries.

In a monograph-length background paper (III-96), Higgins traces this diversity in colonial backgrounds, postwar developments, and current plans and policies for Indonesia, the Philippines, Ceylon, Malaysia, Burma, Taiwan, and Thailand. Following summary chapters on the main features of economic development in Southeast Asia, and the role of trade in the region, Higgins concludes with a proposal for a major multilateral program of "reconstruction" in Southeast Asia.

Other papers have focussed on selected long-term variables in the development process. Morgan (RP:III-35) has synthesized the theoretical and empirical evidence on the role of investment in economic growth, with particular emphasis on the distinction between physical and human capital. Whereas Morgan's paper

*The document numbers used in this airgram refer to the ERP Document Numbers e.g., RP:III-37 refers to ERP Document No. III-37 and CP:IV-21-4 refers to ERP Document No. CP:IV-21-4.

is a contribution to the traditional analysis of development from the supply side, other papers prepared under this contract have focussed on the demand side. Kelley (RP:III-82) applied to Philippine data hypotheses about the role of demographic change (age-structure, urban-rural migration, etc.) in determining the level and composition of economic activity as reflected in consumer expenditure patterns. Hawkins (RP:III-93) has indicated the possible relevance of these concepts for Indonesia by identifying significant "hollow" age cohorts followed by a population boom in that country's population. Kelley and Williamson (RP:III-83) were able to use Indonesian sample survey data to test some of their hypotheses about consumer behavior.

Another group of papers deal with selected topics in the shorter-run relationship between economic policies and economic performance. The role of inflation in economic growth is an important question in itself, and rates and causes of inflation may be a crucial determinant of success or failure in some schemes for economic cooperation or integration. In a statistical study of this issue, Sen (RP:III-87) has concluded that patterns and causes of inflation among Asian countries illustrate considerable diversity, just as do the other structural parameters and policy variables discussed above. A detailed study of Indian inflation by Ramana is the subject of a Conference Paper (CP:IV-21-11). The implications of inflation of a different kind--job inflation in Indonesia--have been discussed by Hawkins (RP:III-26).

2. Patterns of Trade and Their Determinants. -- Trade is basic to understanding economic growth performance and potential in individual Asian nations as well as for evaluating the prospects for several major types of economic cooperation and integration.

(a) Patterns and Prospects -- Changes from 1956-57 to 1962-63 in 9 commodity groups of Asian exports were statistically partitioned into "compositional" and "competitive" effects or changes, and the results were reported by Naya(RP:III-39). The results indicated that the relatively poor export performance of Asia as a whole may be attributed to a significant extent to competitive rather than compositional or structural change, and that individual differences among commodities and countries deserve further study. More recent data have been further disaggregated by country and commodity, with particular emphasis on intraregional trade in Southeast Asia, and these results will appear as RP:III-95.

Naya observes in a background paper that various export projections for Asian countries generally do not take into account these unfavorable competitive shifts. Thus, existing projections unfavorable as they are, may still be overly optimistic.

Many of the Conference Papers (IV-21) described and analyzed the trade performance of individual countries. Suparb's study of Thailand (CP:IV-21-4) documents the emergence of new export products and markets; Chou (CP:IV-21-6) traces a similar phenomenon for Hong Kong; Castro (CP:IV-21-7) discusses Philippine export performance before and after devaluation; Lim CP:IV-21-8) looks at the composition and direction of West Malaysian trade; Lakdawala (CP:IV-21-9) evaluates the prospects of Indian trade with Asia and speculates on the types of policy measures that may be necessary to bring about increased regional trade; and Panglaykim and Thomas (CP:IV-21-12) examine Indonesia's export prospects in terms of present conditions of production and government policies.

(b) Determinants of trade patterns. -- Principles of comparative advantage play an important role in trade and growth. In a background paper Mrs. Fag El Nour has tested, with disaggregated Philippine and Malysian data, the hypothesis that there are many more types of industrial production in which LDCs may show some genuine comparative advantage than has been previously imagined. These industries are ones in which value-added per employee and wages are lower than average in all industries, and in which the share of wages and salaries in value-added in production is larger than average. Ellsworth's background paper examines the experience of several Asian and non-Asian countries in attempting to modify their apparent comparative advantage through various government policies. Naya in RP:III-86, examines the role of natural resources in determining the pattern of exports and imports for the U.S. and Japan.

Transport costs are a factor given great emphasis by the countries of the region as animportant determinant of their trading performance. Abrahamsson (RP:III-92) presents a model that integrates features of market structure, institutional arrangements and technological factors to determine shipping rates for conference lineㅁs, independent liners, and tramp carriage.

(c) Policy Variables. -- The importance of competitive effects in explaining the falling share of exports of Asian countries suggests that policy variables deserve careful study. One important policy variable is national tariff structure and any differences that might exist between nominal and effective rates of tariff protection for particular industries. Leith (RP:III-84) catalogued the difficulties of translating the theoretical concepts of effective protection developed by Harry Johnson and others into meaningful and reliable empirical terms, with illustrations from Taiwanese data. In a background paper, Leith shows the results of modifying several of the crucial theoretical assumptions usually employed in work on effective rates.

The importance of these theoretical and empirical pitfalls was demonstrated by Ellsworth (RP:III-6.b.) in his comment on the interpretation of the rates of effective protection in Pakistani industry. Two of the Conference Papers provided additional empirical estimates of effective rates of protection. For Taiwan Sun (CP:IV-21-5) used conventional input-output techniques to estimate effective rates for an economy that has had remarkable success in exporting new manufactured products. Nurul Islam (CP:IV-21-3) reported on a study based on a new source of Pakistani data, which allowed him to avoid some of the difficulties described by Leith and Ellsworth.

A comprehensive analysis of interactions of various types of policy measures was made in a monograph-length background study by Sen. A case study of the impact of exchange controls on trade patterns was documented for Ceylon by Karunatilake in a Conference Paper (CP:IV-21-10).

3. Specific Measures for Increased Regional Cooperation. -- Specific measures for further regional cooperation and integration fall into three broad categories: relatively "easy" measures involving informal or formal cooperation that does not make significant demands on national sovereignty; integrative measures emphasizing freer trade through greater reliance on the price mechanism; and cooperation or integrative measures relying on harmonization of national plans. Wu's Conference Paper (CP:IV-21-1) surveys the possibilities and experience in Southeast Asia for each of the three types. In a background note, Spoelstra and McClellan have reviewed the activities of ECAFE and other regional organizations as forces in Asian regional cooperation. Spoelstra has prepared a background note on the implications of the newly formed Asian Development Bank (ADB) for regional cooperation.

Cooperative measures based on freer trade are the familar "traditional" forms of market integration--payments unions, free trade areas, customs unions, common markets and full economic unions. However, the applicability to LDCs of much of the theoretical discussion of these measures has been questioned both by economists and policy-makers in LDCs. A survey of this literature by McClellan, Spoelstra and Sen reveals a disapproprortionate emphasis on static welfare analysis rather than questions of economic growth, as well as very little discussion of the important question of the distribution among participating countries of the gains from cooperation. Leith's background survey of empirical estimates of trade creation in the European Economic Community (EEC) suggests that even the static effects appear to be quite small.

Kelley and Knowles (draft RP:III-94) integrate customs union theory with a simple model of economic growth to indicate some of the ways in which regional integration may conflict with the goals of industrialization and national economic development, particularly for capital-short countries. Schmitt (RP:III-50) provides an analysis of the experience of the EEC that employs a similar implicit model.

In addition to these theoretical and comparative studies that help clarify some of the issues about economic integration, several specific studies have been made for Asia. McClellan's background paper discusses the possibilities and problems of a payments union among six Southeast Asian countries. A background study by Naya and Richards notes that several countries in Asia have recently moved toward greater reliance on the price mechanism for controlling trade and investment flows, and thus may be possible candidates for increased co-operation through a free trade area or customs union. In a background paper, Huang identifies another group of countries that might be able to integrate because of complementary comparative advantage patterns and similarities in economic performance and political orientation. Leith estimates that revenue losses from a customs union among Malaysia, the Philippines and Thailand would, in the short run, be relatively small.

Finally, many economists would argue that the case for regional economic cooperation is strong and that any difficulties in achieving this objective owe more to political problems than to economic ones. Spoelstra's backgronnd study of various interdisciplinary hypotheses about the possibilities of regional integration in Southeast Asia in light of the experiences of other regions will be summarized in the Final Report.

Bell observes that policies to promote small-scale industry employed in most Asian countries contradicts their simultaneous emphasis on the economies of large-scale production expected from economic integration. In RP:III-81 Bell examines the logic of promoting small-scale industries and in RP:III-6.a. he studies the impact of these policies on entrepreneurship through a factor analysis of socio-economic variables.

4. National Planning. -- One approach to regional cooperation would require some degree of coordination or harmonization of national development plans. The rationale for plan harmonization was set forth by Kitamura and Bhagat in a Conference Paper (CP:IV-21-2). Lakdawala (CP:IV-21-9) indicates ways in which policies of this type could be used to expand India's trade with ECAFE nations.

Actual possibilities for plan harmonization depend, however, on the record of and prospects for meaningful planning among Asian countries. Sen notes (RP:III-51) that even in some of the most thorough-going centrally-planned economies, requirements of efficiency have led to decentralization and greater use of the price mechanism. In two papers (RP:III-34 and III-36) Morgan notes that all large-scale enterprises; including planning agencies, are prone to built-in sources of bias and error. Aside from these difficulties in plan execution, there may be, as Sen shows in RP:III-52, conflicts of goals that may make national plan harmonization quite difficult. The paper by Myint (RP:III-38) mentioned above notes that Asian countries approach planning in very different ways. Outward-looking countries such as Malaysia, Thailand and the Philippines that use indicative planning and rely on private enterprise and the market system, might have difficulty coordinating their policies with the inward-looking economic policies of Burma, Cambodia, Ceylon, India and Pakistan.

5. Policy Implications. -- Authors of research papers have in each case been asked to indicate the policy implications of their studies, and in all of the foregoing sections references have been made to policy implications. The Final Report (IV-22)(now in progress) will attempt systematically to synthesize these and to add a number of additional points growing out of the entire research project. A few of the policy implications, which generally fall into two categories, warnings and policy proposals, follow.

As pointed out in Section 1, Myint (RP:III-37 and RP:III-38) warns that the diversity among countries in the area has important policy implications. Other warnings are sounded by Morgan. He has brought together a strong case (RP:III-35) against neglecting human as opposed to conventional capital formation in selecting development policies in Southeast Asia and other LDCs. He also points out the possible dangers of large errors in planned economies in his RPs (III-34 and III-36). With Naya he also shows the large sources of error in the international trade data of various Asian countries and warns that great care must be used by policy-makers in interpreting these data. Naya also points out the difficulties in evaluating trade projections for the region.

Sen (RP:III-52) urges policy-makers to be aware that in Asian countries nation building frequently has priority over economic development and efficiency. Measures for economic integration and cooperation will, therefore, tend to be more readily accepted if they can be shown to result in greater national strength. He (RP:III-87) has also pointed to the dangers of inflation in Asian countries while Hawkins in RP:III-26 shows how a possible run-away inflation has resulted in Indonesia in a serious manpower problem--job inflation. Population booms also put pressures of varying degrees of severity on all Southeast Asian countries.

Some of the specific proposals apply primarily to the countries in Southeast Asia, others to the donor countries, including the United States, and some to both. The Final Report (IV-22) will suggest that forms of economic cooperation involving little or no interference with sovereignty will be more readily accepted. It is not easy to have cooperation even among Ministers of Higher Education in Southeast Asia. It would seem much more difficult, therefore, to arrive at some common patterns of trade, customs regulations or finance. Even if these problems were overcome, single programs might not be successful. For example, a customs union would need to secure for the capital-short countries either loans from the Asian Development Bank or assistance from the donor countries (RP:III-94). Similar help would be needed for persistent debtor countries in a payments union. With the possible exception of India and Pakistan, most planning in Southeast Asia has only been of an indicative nature. It seems premature, therefore, to anticipate any early success with a formal type of "plan harmonization".

Trade expansion is still possible within the region and with the developed world, although the experience among the Southeast Asian countries has differed widely, as Naya shows in RP:III-95. Southeast Asian countries may also find that they have a comparative advantage in certain manufacturing industries with low wage rates and high labor intensities. Rising exports of manufactured goods from Southeast Asian countries are widening the scope for regional specialization and cooperation, but a regional cooperation program that does not provide for greater exchange of primary commodities will be less successful than is possible. Abrahamsson (RP:III-92) suggests that on the grounds of effectiveness, domestic employment and income effects, and net foreign exchange earnings, countries of Southeast Asia working to obtain lower water transportation costs should try to lower the 60% or more of freight costs associated with non-water movements--i.e., port charges.

In a separate background paper on "Human Resource Policy and the Evaluation of Technical Assistance" Higgins offers a number of valuable policy insights into the use and evaluation of technical assistance. Morgan believes that the countries in Southeast Asia would be assisted by a carefully balanced system of trade preferences by the developed countries for the less developed countries (RP:III-85). While additional forms of U.S. and multilateral assistance have been suggested, regional cooperation and development depends to a large extent on the plans and programs of the Southeast Asian countries.

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APPENDIX A

STUDY OF REGIONAL COOPERATION IN SOUTH AND SOUTHEAST ASIA

List of Research Papers and Research
of
University of Wisconsin
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A. RESEARCH PAPERS AND RESEARCH REPORTS	ERP DOCUMENT NUMBER
1. Bernhard Abrahamsson, Developing Nations and Ocean Transportation: An Analysis of Price and Cost of Ocean Transportation. The Balance of Payments and the Case for National Merchant Marines with Special Reference to Southeast Asia, September 1967.	III-92
2. Peter Bell, Small Industry, Socio-Economic Aspects of Its Promotion in Asia, September 1966.	III-6-a
3. Peter Bell, A Quantitative Study of Entrepreneurship and the Socio-Economic Determinants of Development in Asia, February 1967.	III-81
4. P. T. Ellsworth, Import Substitution in Pakistan, A Comment, June 1966	III-6-b
5. E. D. Hawkins, Job Inflation in Indonesia, October 1965.	III-26
6. Allen C. Kelley, Regional Integration, Demographic Change, and Patterns of Industrial Growth, June 1967.	III-82
7. Allen C. Kelley and Jeffrey G. Williamson, The Prospects for Regional Economic Cooperation and the Rate of Household Savings in the LDCs, March 1967.	III-83
8. J. Clark Leith, The Specification of Nominal Tariff Rates in Effective Protection Estimates, October 1966.	III-84
9. Theodore Morgan, Economic Planning - Points of Success and Failure, February 1965.	III-34
10. Theodore Morgan, Investment Versus Economic Growth, August 1966.	III-35
11. Theodore Morgan, Theory of Error in Centrally-Directed Systems, August 1964.	III-36
12. Theodore Morgan, Trade Preferences as a United States Policy, With Special Reference to Southeast Asia, August 1967.	III-85

13. H. Myint, Economic Theory and the Underdeveloped Countries, March 1965 III-37

14. H. Myint, The Inward and the Onward Looking of Southeast Asia and the Economic Future of the Region, February 1966 III-38

15. Seiji Naya, The Commodity Pattern and Performance of Asia's Exports to the Developing Areas, May 1966. III-39

16. Seiji Naya, Natural Resources, Factor Mix, and the Factor Reversal in International Trade, May 1967. III-86

17. H. O. Schmitt, The Integration of Capital Markets in Europe: A Step Toward Political Unification, January 1966. III-50

18. K. C. Sen, Convergence in Planned Economics, June 1965. III-51

19. K. C. Sen, Nation-Building and Regional Integration, May 1966. III-52

20. K. C. Sen, Economic Growth and the Price Level--An Analysis of Some Asian Data, 1950-1963, March 1966. III-87

21. E. D. Hawkins, Indonesia's Population Problem, July 1966 III-93

22. Benjamin Higgins, Trade Versus Aid in the Reconstruction and Development of Southeast Asia, August 1967. III-96

23. Allen C. Kelley and James C. Knowles, Trade Theory, Regional Integration, and National Economic Development: The Case of Southeast Asia, August 1967. III-94

24. Seiji Naya and Theodore Morgan, The Accuracy of International Trade Data: The Case of Southeast Asian Countries, August 1967. III-95

B. REPORTS IN PROCESS DECEMBER 1, 1967 — ERP DOCUMENT NUMBER

Theodore Morgan and N. Spoelstra, eds., Economic Interdependence in Southeast Asia: Proceedings of the Bangkok Conference, January 1967 to be published by the University of Wisconsin Press. IV-21

C.P.#1 (CP:IV-21-1) Problems and Prospects of Economic Cooperation in Southeast Asia by Wu Ta-yeh (Advisor, Economic Development Board, Singapore.) IV-21-1

C.P.#2 (CP:IV-21-2) Regional Harmonization of National Development Plans and Trade Cooperation: Approaches to Economic Integration in the Development ECAFE Region by Dr. Hiroshi Kitamura and Dr. Ajit Bhagat. (Planning and Research, ECAFE Secretariat, Bangkok) IV-21-2

B. Reports in Process December 1, 1967 (cont)

C.P.#3 (CP:IV-21-3) Tariff Protection, Comparative Costs and Industrialization in Pakistan by Professor Nurul Islam (Director Pakistan Institute of Development Economics, Karachi) IV-21-3

C.P.#4 (CP:IV-21-4) Trade Policies and Economic Development in Taiwan by Dr. I-Shuan Sun (Secretary-General, Central Bank of China,Taipei) IV-21-4

C.P.#5 (CP:IV-21-5) Some Salient Aspects of Thailand's Trade, 1955-1964 by Mrs. Suparb Yossundara and Mr. Yune Huntrakoon (Research Department, Bank of Thailand, Bangkok) IV-21-5

C.P.#6 (CP:IV-21-6) Hong Kong's Changing Pattern of Trade and Economic Interdependence in Southeast Asia by K. R. Chou (Private Consultant; formerly Chinese University of Hong Kong) IV-21-6

C.P.#7 (CP:IV-21-7) Philippine Export Development, 1950-1965 by Professor Amada A. Castro (Dean, School of Economics, University of the Philippines) IV-21-7

C.P.#8 (CP:IV-21-8) West Malaysian External Trade, 1947-1965 by Professor Lim Chong-yah (Head, Department of Economics, University of Malaya, Kuala Lumpur) IV-21-8

C.P.#9 (CP:IV-21-9) Prospects of India's Foreign Trade with ECAFE Countries by Professor D. T. Lakdawala and Dr. R. M. Patil (Director and Research Associate, respectively, Department of Economics, University of Bombay) IV-21-9

C.P.#10 (CP:IV-21-10) The Impact of Import and Exchange Controls and Bilateral Trade Agreements on Trade and Production in Ceylon by H.N.S. Karunatilake (Research Department, Central Bank of Ceylon) IV-21-10

C.P.#11 (CP:IV-21-11) Deficit Financing and Import Substitution: India, 1951-1965 by Dr. D. V. Ramana (Development Economist, Asian Institute for Economic Development and Planning) IV-21-11

C.P.#12 (CP:IV-21-12) Indonesian Exports; Performance and Prospects by Dr. J. Panglaykim and Mr. Kenneth D. Thomas (Senior Research Fellow, Australian National University and Research Fellow, La Trobe University, respectively. IV-21-12

C. FINAL REPORT: In Process December 1, 1967 IV-22

APPENDIX B

Abstracts of Conference Papers
of
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C.P.#1 (CP:IV-21-1): "Problems and Prospects of Economic Cooperation in Southeast Asia" by Wu Ta-yeh (Advisor, Economic Development Board, Singapore)

Wu's general survey of the development problems of Asian countries leads him to the case for some form of regional cooperation. Existing trade patterns and production structure, however, provide little hope for cooperation through a free trade area or customs union. Similarly, nationalistic pressures may make extensive agreed specialization difficult to achieve. Experience with bilateral cooperation, however, suggests that some steps are possible through sectoral coordination and joint industrial ventures. Particularly promising joint ventures are the Asian Development Bank (ADB), various plans of the Association for Southeast Asia (ASA) for subregional joint shipping and airlines, tourist promotion and research. Large numbers of countries might participate in cooperative ventures for management training, research in technology, export standards and promotion, tourism and agricultural development.

C.P.#2 (CP:IV-21-2): "Regional Harmonization of National Development Plans and Trade Cooperation: Approaches to Economic Integration in the Developing ECAFE Region" by Dr. Hiroshi Kitamura and Dr. Ajit Bhagat (Planning and Research, ECAFE Secretariat, Bangkok)

The authors review the major points of the theory of economic integration in relation to trade and growth theory and to the experience of cooperative ventures in other regions, and conclude that trade liberalization without a program of plan harmonization will be unsuited to the needs and desires of developing ECAFE countries. The possibilities of this approach for Asia are then examined in the light of the experience of the Regional Cooperation for Development (RCD), the Mekong Committee and the ASA.

C.P.#3 (CP:IV-21-3): "Tariff Protection, Comparative Costs and Industrialization in Pakistan" by Professor Nurul Islam (Director, Pakistan Institute of Development Economics, Karachi).

Professor Nurul Islam extends earlier work by Soligo and Stern and others in estimating rates of effective tariff protection in Pakistan manufacturing. Islam uses new data from the Pakistan Tariff Commission to provide direct estimates of c.i.f.-f.o.b. price differences for specific industries as well as for changes in levels of effective protection over time. Islam also examines some of the criteria employed by the Commission in setting tariff rates and speculates on the proper role of tariff protection in Pakistan. The relationship between effective protection, the exchange rate and various export-promotion schemes is discussed.

C.P.#4 (CP:IV-21-4): "Trade Policies and Economic Development in Taiwan" by Dr. I-Shuan Sun (Secretary-General, Central Bank of China, Taipei)

After a brief survey of Taiwan's economy and postwar growth performance, Dr. Sun turns to an analysis of changes in the commodity and geographical pattern of exports and imports. Coefficients of trade concentration show shifts in the composition of trade toward industrial exports and imports of industrial raw materials and in the direction of trade toward high dependence on Japanese and U. S. markets. Exchange control seems to have been the most important policy determinant of this pattern, with calculated rates of effective protection appearing to be less important. A discussion of trade and growth prospects indicates that the need to export will be great in years to come. The ending of U. S. aid may lead to greater Taiwanese imports of raw materials from Southeast Asia.

C.P.#5 (CP:IV-21-5): "Some Salient Aspects of Thailand's Trade, 1955-1964" by Mrs. Suparb Yossundara and Mr. Yune Huntrakoon (Research Department, Bank of Thailand, Bangkok)

Thailand's trade grew at an impressive rate in the ten years prior to 1964. Import growth has involved a substantial shift in composition, reflecting a normal pattern of industrialization through import-substitution. Accompanying the compositional shift has been a shift in the source of imports to developed countries and particularly Japan. Exports, while still concentrated in primary products, have shifted remarkably from Thailand's traditional products to new exports, directed particularly to Japan. The authors attribute this performance and current pattern of Thai trade to the unification of the exchange rate in 1955 and to special commercial arrangements with Japan.

C.P.#6 (CP:IV-21-6): "Hong Kong's Changing Pattern of Trade and Economic Interdependence in Southeast Asia" by K. R. Chou (Private Consultant; formerly Chinese University of Hong Kong)

Hong Kong is the most highly-industrialized country in Asia except for Japan. Chou traces this achievement to a number of unique features: the influx of capital and skilled labor from mainland China; the expansion of markets in developed countries for Hong Kong's products; the shift from an entrepot to a manufacturing center; and a high awareness of the necessity coupled with favorable policies for trade.

C.P.#7 (CP:IV-21-7): "Philippine Export Development, 1950-1965" by Professor Amado A. Castro (Dean, School of Economics, University of the Philippines)

Professor Castro deals with three propositions: (1) over-valuation was not detrimental to Philippine exports; (2) the pattern of Philippine exports differs significantly from other Asian countries; and (3) this pattern may facilitate

Philippine participation in regional cooperation. Evidence offered in support of the first point includes rates of export growth, relative price changes, direct estimates of the relative over-valuation of the peso and profit levels in export industries. With respect to the second point, Castro argues that compared with Hong Kong and Taiwan new and promising Philippine exports tend to be those that appeared in response to home rather than export demand. And third, because most of these exports also correspond to Philippine comparative advantage, there will be possibilities for greater trade with the region.

C.P.#8 (CP:IV-21-8): "West Malaysian External Trade, 1947-1965" by Professor Lim Chong-yah (Head, Department of Economics, University of Malaya, Kuala Lumpur)

West Malaysia has a very high ratio of export proceeds to gross domestic product, even for an Asian country. Thus, the record of and prospects for West Malaysian growth depend mainly on exports. The most significant feature of the export sector has been the fall in rubber prices, which has meant also a fall in the Malaysia's commodity terms of trade and a reduction in the balance of trade surplus. The more active role taken recently by the government has meant greater insulation of national income from exports and greater emphasis on import-substitution. However, West Malaysia faces serious problems as foreign exchange reserves dwindle and as inflationary pressures mount from increased development and defense expenditures and an increasing burden of debt-service.

C.P.#9 (CP:IV-21-9): "Prospects of India's Foreign Trade with ECAFE Countries" by Professor D. T. Lakdawala and Dr. R. H. Patil (Director and Research Associate, respectively, Department of Economics, University of Bombay).

After first examining the present composition and direction of India's exports to developed and developing ECAFE countries, the authors use the global export target of the Fourth Plan to indicate which export commodities could be expanded during the Plan period. Major attention is given to the types of policies that would be required for India to provide the exportable surplus and that would be necessary to allow the various ECAFE countries to increase their purchases from India. The paper concludes with some speculation about long-run trade and production patterns in the region.

C.P.#10 (CP:IV-21-10): "The Impact of Import and Exchange Controls and Bilateral Trade Agreements on Trade and Production in Ceylon" by H. N. S. Karunatilake (Research Department, Central Bank of Ceylon)

Karunatilake traces the appearance and progressive tightening of trade and exchange controls after the Second World War and Korean War through various methods used and the impact on the pattern of trade and production. A number of bilateral trade agreements were negotiated in this period and details of the operation of these with China, Burma, India and Egypt are given. Ceylon's prospects for entering some type of regional cooperation are explored.

C.P.#11 (CP:IV-21-11): "Deficit Financing and Import Substitution: India, 1951-1965" by Dr. D. V. Ramana (Development Economist, Asian Institute for Economic Development and Planning)

Dr. Ramana makes an ingenious attempt to use aggregate Indian data to estimate the impact of deficit financing on that country's growth. After a brief review of the arguments offered for and against deficit financing, Ramana estimates regression equations for alternative measures of income growth, money supply and price changes. This evidence is then related to features of import dependence of major sectors to arrive at some indicators of the extent of cost-push inflation in the economy.

C.P.#12 (CP:IV-21-12): "Indonesian Exports: Performance and Prospects" by Dr. J. Panglaykim and Mr. Kenneth D. Thomas (Senior Research Fellow, Autralian National University and Research Fellow, La Trobe University, respectively)

The authors provide a detailed discussion of trends and fluctuations in major Indonesian exports from 1950 to 1964-65. Products covered are rubber, palm oil, coffee, tea, tobacco, copra, petroleum, and minor exports. Particular emphasis is given to the role of investment policy on the government estates, the relationship between plantation and small-holder production and government policies toward foreign investment in the export sector. Indonesia's place in intra-regional trade of rubber and rice is discussed separately.

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1. The attached abstracts of the Research Papers (RP) developed under this Wisconsin Research Contract were prepared by Wisconsin for use with and as a Supplement to Ref (A), ERP Summary No. 25.

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ERP No. III-92

Abstracts of Research Papers
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B. J. Abrahamsson, Developing Nations and Ocean Transportation: An Analysis of Price and Cost of Ocean Transportation, the Balance of Payments and the Case for National Merchant Marines with Special Reference to Southeast Asia

One of the problems of developing nations is their dependence on third countries for shipping services. The two major grievances stemming from this dependence are: (1) liner freight rates are unduly high and are discrimatory against the exports of development countries; and (2) the balance of payments is strained by large freight payments.

Available data indicate that liner freight rates have followed an upward trend in the post war period whereas tramp rates have generally fallen. Liner conferences cite rising costs of operating as the cause of the increased freight rates.

The steady increase of conference liner freight rates is considered by the countries in Southeast Asia as a serious threat to the expansion of trade in the area. Since the region is heavily dependent on foreign tonnage and the trade is dominated by conference shipping, it may seem natural for a particular country to view conference rates as discriminatory against its trade if the rates on similar commodities are lower when applied to a neighboring country's trade. Although a simple comparison of rates is not valid, the feeling of discriminatory treatment has led to attempts to affect the rate structure by developing national shipping.

Conferences maintain that the increased rates reflect the steadily increasing costs of operations and that these costs must be the subject of corrective actions if lower rates are to be obtained. Developing national shipping will not influence operation costs and, in the present situation of "over-supply" of tonnage, it may actually increase these costs in particular trades by contributing to port congestion.

Although we do not dispute the claim that operation costs have increased, we argue that such increases explain only part of the total increase in conference rates. Part of the rise in the rates is due to compensatory increases which result from the different market structures in the liner and tramp trades.

The second and third sections of this paper present a shipping model that integrates features of market structure, institutional arrangements, and technological factors to determine shipping rates for conference liners, independent liners, and tramp carriage.

The shipping model indicates that policies aimed at securing lower conference freight rates should try to affect compensatory increases or the cost structure of conference liner shipping or, preferably, both. Compensatory increases can be affected by changing the competitive environment. While legislation can do this, effective administration will require international cooperation to an extent not likely to come about the foreseeable future.

A more direct economic measure would be to encourage domestic operation of tramps and non-conference liners. Alternative means of transportation would become available through such operations. In case of retaliatory actions from conferences, e.g., rate wars, it might be necessary for governments to provide financial support. New tonnage would promote competition and innovation leading to lower rates and, if pursued with that aim, to the breaking-up of the conference system.

However, the massive development of national shipping that would be needed to achieve these results is not necessarily the best course of action. First, large investments, usually in foreign exchange, would be required; against these large outlays would be set relatively small returns in terms of gains to the balance of payments. Second, freight rates would be reduced only to the extent that compensatory increases have occurred. Rate increases caused by rising costs would remain unaffected. Third, it is also questionable if the breaking-up of the conference system is indeed desirable. Whatever the defects of this system, its beneficial effects in providing reliable, stable liner services seem to be well established.

An argument can be made for the development of ports before shipping on the grounds that port development will at a later stage increase the potential contribution of shipping to the balance of payments. However, port developments are part of a general program of economic development. Recent progress in container, pallet and other shipping techniques, together with the technical capacity for building increasingly larger cargo ships, makes the modern port dependent on adequate internal transportation networks. The full benefits of containers can only be realized if internal movement is facilitated. Large ships require large ports in which it would be necessary to consolidate many small cargo lots originating from numerous inland points. Port developments must, therefore, be only one phase of a larger scheme of transportation development which entails far larger capital expenditures than shipping alone.

However, employment and income effects from port improvements would be greater than they would be from investment in national shipping alone. Social overhead would be created and freight rates would decline because of decreased turn-around-time. The impact of forward looking port facilities on shipping techniques and ship design would also tend to reduce freight rates. Port costs as a proportion of total operation costs of shipping would decrease.

The long gestation period of port developments, nevertheless, may make it desirable to develop some national tonnage concommitantly. This would provide competition and leverage to pass on savings from port developments to shippers. Although the long-run goal should be to utilize containers, pallets should be extensively used in the early stages since they require small capital investments and few new facilities, and have a large impact on cargo handling costs. In this context it is also important to improve procedures so as to minimize documentary and administrative aspects of cargo movements.

Peter F. Bell, Small Industry: Socio-Economic Aspects of its Promotion in Asia ERP No. III 62

Policies for economic development in Asia continue to stress the importance of promoting small business enterprises for a variety of reasons--economic, political and social. The economic rationale of this promotion is based on an assumption of their economic advantage in terms of capital-saving and labor-intensity. Available statistical evidence, however, suggests that these policies cannot be supported on economic grounds. There is, moreover, a conflict between the various objectives of promotion which may invalidate some or all of them.

There is a need for more extensive studies of the operating conditions of small units and an examination of the non-economic benefits which are alleged to accrue from their promotion. It is also necessary that the role which small units are to play in the overall development strategy be decided upon and that their promotion, rather than be isolated into a separate category, be integrated into the overall development plan. Efforts to arrive at an overall optimum size of firm which includes all aspects bearing on firm size are unlikely to be successful--the statement of the factors bearing on this optimum provide, however, a useful theoretical frame.

It may be that development policy should stress "disability-removing" rather than direct protection of small industry. Both in terms of individual country plans and the need for an overall regional view, small industry promotion must be based on sounder theoretical premises than hitherto.

Peter F. Bell, A Quantitative Study of Entrepreneurship and Socio-Economic Determinants of Development in Asia ERP No. III 81

Development theory and development policy presume relationships among economic and social variables that have, in many cases, not been subjected to any quantitative tests. Such tests would help to clarify some of the areas of dispute between theorists -- for example the response of the private sector to economic disequilibria.

The theory of entrepreneurship is composed of a multitude of widely differing generalizations, nearly all of which lack empirical support. This pilot study uses the technique of factor analysis to attempt to shed some light on the systematic relationships which have been assumed to exist between the supply of entrepreneurs and certain social and economic characteristics.

Two groups of countries were chosen for study. The first group, selected on the basis of reliability and availability of data, were countries in Southeast and South Asia: Pakistan, India, Burma, Thailand, Japan, and the Philippines. The second group comprised countries for which sample studies of entrepreneurship have already been completed (two countries which fall into this category are duplicated from group I); these are Pakistan, the Philippines, Turkey, Lebanon, Greece, and Puerto Rico. The decade of the 1950's was the period chosen for study although some figures used refer to slightly later dates.

The analysis suggested the following tentative results: (i) a large entrepreneurial class appears to be associated with some of the generally accepted characteristics of developing countries, namely, a decreasing agricultural sector, increasing urbanization, literacy and contact with the outside world, and a slowing down in the rate of population growth; (ii) the growth of such a group might be related to a development pattern which favors capital formation, an expanding government sector, stability of exports and of internal prices coupled with improvements in wages; (iii) a vigorous group of entrepreneurs may also be affected by an expanding export sector, and export-oriented economy ("outward-looking"), with a degree of dependence in foreign trade. In spite of the great heterogeneity between the two groups of countries, and between the countries in each group, the results displayed a remarkable degree of consistency and "significance" when judged by the standard tests. Although the results are heuristic and tentative, the semi-quantitative insights provided suggest useful hypotheses and delineate the areas to which more detailed studies might be directed. More thorough-going studies of the inter-relations between social and economic variables would increase our understanding of the mechanisms by which growth may be promoted -- both nationally and regionally -- and would assist in the selection of policies which would more rapidly achieve this goal

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ERP No.
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P. T. Ellsworth, Import Substitution in Pakistan--A Comment

The methodology and the results of a paper published in the Pakistan Development Review (Summer 1965) by Soligo & Stern are stated briefly. The authors, using a simplified input-output model, examined 48 industries in Pakistan and found that in 23 of them, value added (at world prices for inputs and outputs) was negative -- that is, the value of inter-industry inputs alone exceeded the total value of output when world prices were used. Attribution of this striking result to the respective industries being either (a) premature, or operating at too early a stage of their increasing return phase, or (b) over-expanded, or operating beyond the minimum cost point, is criticized as resting on inaccurate diagrammatic argument. It is contended instead that the results can be interpreted as reflecting wasteful use of inputs, factor prices distortions, or methodological difficulties due to improper assumptions about price relations, or to improper weighting. Further, it is suggested that the "investment" industries shown by Soligo and Stern to have a comparative advantage are not investment industries in the usual sense of producing heavy industrial goods, but rather the producers of light manufactured goods almost exclusively.

E.D. Hawkins, Job Inflation in Indonesia ~~ERP No.~~ III-26

Inflation has forced Indonesians to adopt many methods to increase family incomes: (1) working longer hours to secure overtime pay; (2) having additional members of the family work; (3) securing an extra job (moonlighting) or, in Indonesia, several individual jobs; (4) asking for wage increases or, if they are frozen, promotions to get more money; (5) engaging in self-employment such as buying and selling; and (6) performing certain services for fees outside the legal channels. The most important of these is to hold multiple jobs. If only a few people take on multiple jobs, they will bring in more income to their families, and such a small increase in income relative to aggregate income of all Indonesians would have so little effect on prices, no matter what their additional output, that they would gain relatively by this move. As more and more engage in multiple jobs, the individual gains in income may be more and more offset by new price rises, especially if the net increase in output demanded is low relative to added earnings.

Price inflation has encouraged job inflation as a means of avoiding lowered real income, but the widespread extension of job inflation is probably leading to further price inflation, which may encourage more job inflation. Other methods are needed to halt the spiral of inflation. The 1963 stabilization efforts were abortive, largely because the government failed to consider the political implications of the measures and as a result did not receive the support of any of the major power groups. Any new attempt should have a more solid political base.

E. D. Hawkins, Indonesia's Population Problem ERP No. III-94

The 1961 Census and other sources present a demographic picture of Indonesia that shows a baby boom during the 1950's following a "hollow" generation in the 1940's. This increase has led to urgent problems in schooling, labor force and urbanization. Twice as many young people are entering the labor market now as compared to about five years ago. They are also reaching the marriagable age, with a new baby boom in sight. All of the population projections point to large increases in Indonesia, including overcrowded Java even with a substantial number of transmigrants to the less crowded islands.

An analysis of the possibilities for decreasing fertility and increasing the tempo of economic activity indicates that, unlike the development pattern in Western countries, even greater urbanization and education and faster agricultural and industrial development will not be sufficient to limit the expansion of population in Indonesia. Positive measures to reduce births such as "Guided Parenthood" are proposed.

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A. C. Kelley, Regional Integration, Demographic Change, ERP No. III 82
and Patterns of Industrial Growth

Any realistic analysis of the probable success of regional cooperation must be couched in terms of its impact on both the economic growth and the rate of industrialization of each individual member of the union. The prospects of successful economic cooperation increase in so far as the results of integration further the joint national goals of economic growth and industrialization.

An important problem is to identify the factors explaining differential rates of industrialization as economic development takes place. The present study focuses on demographic change and its relationship to the structure of economic growth and development. The nature and significance of the impact of family size, total population growth and rural-urban migration on industrial patterns is developed in detail. A model is presented which provides a technique for isolating the influence of selected elements of demographic change on the level and composition of demand. The Philippine experience in the 1960's is used as a case study to illustrate the properties of the theoretical framework.

A principle finding of the study is that many forms of demographic change, in particular total population growth and an expansion of average family size, may operate to diminish the rate of industrialization. It is shown that systematic trends tend not only to counter Engel's Law (i.e., the shift in demand away from agricultural products as per capita income advances), but also that demographic factors constitute, in the Philippine case, the major demand-originating influence changing broad industrial patterns. In fact, the net influence of income and demographic demand elasticities creates a pressure toward a relative expansion of agricultural production.

The implications of the theoretical model and empirical findings are 1) examined with respect to Chenery's finding on the relative unimportance of demand factors in explaining industrial patterns, 2) compared with the implications of the Leibenstein 'population trap' framework, and 3) used as a basis for formulating selected population and development policies.

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A.C. Kelley & J.G. Williamson, The Prospects for Regional Economic Cooperation and the Rate of Household Savings in LDC's — ERP No. III 83

One of the principal obstacles to international economic integration, whether it takes the form of trade expansion, factor market integration, or a combination of the two, is the danger that some members of the union will enjoy, as a result of the integration process, more rapid growth than others.

The theme is a simple one. Differential growth rates arising out of the integration process are based in part on the behavior of factor prices in the face of trade expansion, as well as on the possibility of adverse capital flows resulting from a liberalization of factor movements. Even partial factor price equalization will result in a lower rate of return to capital in those countries which are the relatively capital-poor members of a union. It is reasonable to expect that a lower rate of return in these countries will exert a downward force on the rate of return in the capital stock. If, in addition, trade expansion is coupled with the development of integrated factor markets, and if this latter aspect of integration gives rise to adverse capital flows, the supply of capital in capital-poor members will be seriously curtailed.

Capital may flow to those countries which already enjoy a concentration of capital and technology in order to take advantage of what Hans Schmitt has called, "economies of agglomeration" (see, "The Integration of Capital Markets in Europe: A Step Towards Political Unification," ERP Document No. III-50). Or alternatively, as Kelley and Knowles argue, in a study "Regional Integration and National Economic Development: The Case of Southeast Asia," (ERP No. III-94), differences between real rates of return as derived from production functions, and those actually received by owners of capital when appropriately discounted for such factors as risk of confiscation, taxes, and exchange rate fluctuations, may also result in adverse capital movements.

The supply of savings and the demand for investable resources thus become crucial factors in the degree of success experienced by any integration scheme. An inquiry into the determinants of the supply of savings constitutes the subject of the present study, which attempts to identify the determinants of household savings behavior in the Daerah Istimewa Jogjakarta Region of Indonesia. The data consist of a 1959 household survey of 490 families. While several non-linear models are explored, the analysis and findings relate to linear per capita functions. The variables considered include income, occupation (farmer, trader and craftsman, owner of business, government employee, other wage earner), degree of asset ownership, education, location (urban, rural), and age.

Two models of savings behavior are explored. The first examines the influence of source of income and occupation. We conclude that the development hypotheses which stress source of income (e.g., Lewis model) might better be formulated by stressing the ownership of earning assets. This approach was found very useful in interpreting differential savings behavior by income source. Access to an efficient capital market may emerge as a significant element in determining average household savings levels, given household income.

The second model is a straight forward representation of the life-cycle hypothesis. The empirical results, constrained by the relatively small sample size, are somewhat neutral regarding the applicability of life-cycle formulations in Indoneaia.

J.C. Leith, The Specification of Nominal Tariff Rates in Effective Protection Estimates ERP No. III-84

A number of economists have called attention to the significance of a tariff structure that distinguishes between intermediate inputs and final goods. Estimates of effective rates of protection can be useful guides to policy makers concerned with the impact of national protective structure on domestic resource allocation. However, this paper shows that estimates of protection are sensitive to any misstatement of nominal tariff rates. Furthermore, obtaining more accurate specification of nominal tariff rates may be very difficult. Problems include converting rates from specific to ad valorem basis and from an f.o.b. to c.i.f. valuation. Because the detail of tariff rates is much greater than the available information on the industries involved, there is also a problem of weighting individual tariff rates. Finally, the nominal tariff rate may not in fact reflect accurately the divergence between world and domestic prices.

Although the analysis of effective rates may provide considerable insight into the process of economic growth, users should realize that the analysis rests on certain restrictive assumptions and that the estimates are sensitive to errors in the specification of actual nominal tariff rates. The sources of potential error in nominal tariff data are numerous and important, and, data necessary for adequate adjustment are not ordinarily available.

Theodore Morgan, "Economic Planning -- Points of Success and Failure ERP No. III-34

Failures of economic planning originate both in (a) government instability, with its context of maneuvering for political power and shifts of persons and policies, and in (b) the nationalist and one-party policies that governing groups use to keep themselves in power. They originate also in (c) centralized large organizations that attempt to control economic life in detail, with their tendencies to substitute ideology for reality; to alienate the people of the villages and farms for whom the planning is done; and to delay and to be rigid.

Successes of planning, actual and potential, originate in (a) influencing the economic enrivonment in which private individuals make their decisions, and in trying to supplement those decisions; (b) in evoking expression of felt wants for improvement from the people in the villages and fields, and hence stimulating their ideas and energy, which the government can then assist. Finally, planning is in our time a popular word,like democracy: Hypocrisy being the homage vice pays to virtue, dictatorships proclaim they are democracies, and governments that have no intention of serious planning go through the motions. Even so, planning (c) keeps alive the hope of economic advance, which makes more likely its eventual reality.

Theodore Morgan, Investment versus Economic Growth ERP No. III-35

Often investment in a national income accounting sense is identified with those resource uses that add future potential income. The identification is fallacious. Human resource development and non-material capital formation, often served by resource uses normally labelled "consumption" are significant contributors to growth. The empirical marginal-capital-output-ratio, often used to measure the effect of capital input, is in fact a conglomerate whose main significance is that of being an inverse measure of the rate of growth. Economic growth is a complex phenomenon which may be correlated with a rise or decline in the quantity of capital, and is frequently associated with the need for increased consumption.

The policy implication is that in Southeast Asia as in other areas the international flow of investment goods should be much less a preoccupation of AID and domestic developers than it has been. The evaluation of resource uses directed toward improving human productivity and organization is a candidate for regional cooperative activity.

Theodore Morgan, The Theory of Error in Centrally-Directed Economic Systems — ERP No. III-36

The article analyzes the nature and sources of consistent administrative error in centrally-directed economic systems. The division is not between government and private economic units, but between large and small ones.

There is reason to be (A) a tendency toward fewer-but-bigger errors than in decentralized systems. Bookkeeping and other checkable mistakes -- that is, little mistakes -- can be avoided; but there will be drift toward kinds of errors not readily checked for three reasons.

(B) There are tendencies toward delay, excessive optimism, and multiplication of controls. Delay and excessive optimism derive from the normal psychology of the chief and his estimate of his own policies, coupled with political pressures on him, the tact of subordinates, and the nature of bureaucratic work. Well-documented military catastrophies of World War II suggest a dependable pattern of bureaucratic error originating in wish-fulfillment bias and a tendency to pay attention to information that supports current expectations. Then, when something goes wrong, the normal administrative reaction is to impose laws and regulations and/or extend them.

(C) Adequate incentives to the top leaders contrast with modest incentives or the treadmill for the many. Central authorities, in their quest for general approbation, tend to rely on what their communities regard as the highest motives; but work gets done best when reliance is on the strongest motives.

(D) The divergence between highest motives and strongest motives, and between public policies and private interests, leads to hypocrisy and on to avoidance, evasion, and corruption. Hypocrisy is plainly a social loss but the latter resorts can at times be socially useful, offering the only way that woodenheaded or unlucky policies can be made consistent with economic survival or progress.

Some implications for policy are drawn.

Theodore Morgan, Trade Preferences as a United States Policy, With Special Reference to Southeast Asia — ERP No. III-85

LDCs should be generally well fitted to compete internationally in those commodities that are relatively labor intensive in low level kinds of skills. These can normally be identified statistically as commodities in which the wages component of value-added is relatively large. Among LDCs of the world in general, these include among manufacturers: textiles and apparel, wood products, furniture, leather, and "miscellaneous manufactures". From our study of six Asian countries, we would add to the list metallic products, and machinery and transport equipment. Sample calculations for the United States suggest that these are subject to very high effective rates of duty. (For example, plywood is subject to 16% nominal duty; but 99% effective duty; metal manfactures 19% versus 75%; clothing 27% versus 136%).

LDCs are being handicapped in their effort to modernize by DC protectionism--which is much higher than it appears to be, which is erratic, and which handicaps especially exports of LDC manufactures, and so exports of those LDCs that have been most energetic in expanding their manufactures. These manufactures markets are of special interest to LDCs since basic world demand for manufactures is relatively expansive, and since manufactures growth is, for right reasons and wrong, much emphasized in LDC development policy. Among the right reasons, the feedback and dynamic effects of manufactures growth offer especially hopeful vistas.

The extension of trade preferences for manufactures by DCs, especially the United States, to LDCs, specifically to the LDCs of Southeast Asia, would be an offset to the present invidious tariff duties levied against them. A general high tariff duty could be offset by the LDCs through currency depreciation; but a differential impost against manufactures can be offset only through a special reduction of that impost, assuming that the LDCs do not set up dual, or even multiple exchange rates.

The extension of such trade preferences to LDCs would satisfy their official and emphatic wish, which is more firmly rooted in fact and anlysis than their usual arguments have conveyed. The United States could well seriously explore the practicalities of preferences, as a major step toward lower trade barriers generally, rather than remain conspicuous in opposition. The extension of such preferences could be made conditional on a substantial lowering by LDCs of tariffs and related trade barriers to other LDCs, perhaps within regional groupings such as Southeast Asia. Such a policy carries with it a double gain: The present U. S. differentially high barriers against LDC manufactures exports are lowered, at the same time that trade flows among LDCs for all types of commodities are encouraged.

This recommended policy is consistent with the long run U. S policy maintained since 1934 toward lowering world trade restrictions. It is in the obvious interest of world efficiency of production statically and still more dynamically.

Hla Myint, Economic Theory and the Underdeveloped Countries ERP No. III-37

There is no reason to suppose that economic policies considered appropriate for the advanced countries will prove to be equally appropriate to the underdeveloped countries. But this "realistic" objection to generalizations should apply not only to the laissez-faire but also to the planning policies in the underdeveloped countries. Further, given the wide differences which exist among the underdeveloped countries themselves with respect, say, to the degree of population pressure, the overall size of the economy, the general level of administrative efficiency and the coherence of the institutional framework, etc., it is highly unlikely that any single standard model of development planning will be appropriate for all of them.

Seiji Naya, The Commodity Pattern and Performance of Southeast Asia's Exports to the Developed Areas ERP No. III-39

As an analysis of the export performance of Southeast Asia, this report aims to find those commodities responsible for the region's slow expansion of exports to the developed areas. The exports of 15 Asian countries to 20 developed nations are compared with the latter's imports from the world for two periods, the averages of 1956 and 1957 (Period I) and 1962 and 1963 (Period II). The comparison is made in terms of nine commodity groups, five of primary and four of manufactured goods, which are re-arranged from the three-digit Standard International Trade Classification.

Although the export trade of Southeast Asia to the developed countries (DCs) increased 13.89% (from $4 billion in Period I to $4.5 billion in Period II), the total imports of the DCs from the world rose 39.77%, a difference of -25.88%. Of this total difference, -17.99% is explained by the import pattern of the DCs which moved against the region's export commodity composition (compositional effect). The remaining -7.89% is due to the region's inability to maintain its share in the exports of individual commodity groups (competitive effect). In other words, the export lag has been considerably affected by the region's poor performance even in exporting primary products, as compared to the rest of the world.

In contrast to the stagnant exports of primary products, manufactured exports have grown rapidly, even faster than the import growth of similar products in the DCs. Within the manufactured exports, however, only Light Industrial Goods can be singled out for its export contribution. This is the only manufactured group which has a relatively large share in total exports and constitutes a relatively large proportion of the DC's imports (5.8% in Period I and 7.7% in Period II). The increase in exports of this group alone accounts for more than 90% of the region's over-all increase, the export share of other manufactured groups being too small to affect appreciably the region's total exports.

The four major DC areas, the U. S., the U. K., the E.E.C., and Japan absorbed approximately 90% of the region's exports to the 20 DCs while the remaining 10% is accounted for by exports to Australia, Canada, and Other Europe. The exports to the four major areas grew far less than the import growth rate of these areas, especially with respect to the E.E.C. and Japan. Although an unfavorable compositional effect is shown for all four areas, a weakened competitive effect is found to explain a large part of the region's export lag with the U. K., the E.E.C., and Japan.

Although this paper considers Southeast Asia as a group, much variation is found in the export performance of individual Asian countries. Hong Kong, Formosa, Thailand, and the Philippines increased their exports very rapidly, compared to the relative export stagnation of Indonesia, Vietnam-Cambodia-Laos, Pakistan, India, and Ceylon. It is not clearly evident that those countries with a high export concentration in primary products always performed poorly. Thailand and the Philippines, for example, have done well even with a high degree of specialization in primary exports. Examination of specific commodity items reveals that these countries were able to offset the decline of some primary exports with increases in other primary goods, such as maize (Thailand) and copra (Philippines).

It is likely that the region's exports will continue to be concentrated in primary goods in the near future, implying that the export lag is also likely to persist. As indicated above, however, the performance of some Asian countries suggests that the gap can be narrowed. Manufactured exports should be encouraged in order to reduce the export lag by lessening the unfavorable compositional effect.

Seiji Naya, Natural Resources, Factor Mix, and the Factor Reversal in International Trade — ERP No. III-86

The paradoxical finding of Professor Leontief that American exports are, on the average, labor-intensive and imports capital-intensive is known as the Leontief Paradox. Some critics of this controversial finding have pointed to the methodological problem or the seriousness of omitting factors other than capital and labor, e.g., natural resource factor. Others have argued that the resulting Paradox is due to the invalidity of the factor proportions theory of comparative advantage which Leontief tested.

That the Paradox is due to the natural resource factor is implied by Leontief himself in one of his computations. Only in this computation, which exludes natural resource sectors, was the Paradox reversed. More recently, Vanek has empirically shown that the U. S. foreign trade pattern reflects a relative scarcity of natural resources. In his attempt to explain away the Paradox, Vanek reasons that capital and natural resources are a pair of complementary factors and, hence, although capital may be an abundant factor, more of it is needed to replace U S. imports than is needed for exports.

In order to compare the factor structure of U. S. foreign trade with that of Japan, the natural resource products as well as capital and labor structure of Japan's foreign trade have been computed. The result reflects the generally accepted scarcity of natural resources of Japan's economy--the resource content of its imports is more than three times that of its exports. The computation of capital-labor requirements, however, reveals that its exports are capital-intensive and its imports labor-intensive.

If natural resources and capital are complementary, exclusion of the natural resource sectors should increase the capital-intensity of Japan's exports relative to its imports. But the result of the computation excluding the resource sectors shows that the capital intensity of exports is no longer larger than its import, implying that the complementary argument does not adequately explain the case for Japan as it appears to for the U. S.

Separate studies of India and Canada, both employing Leontief's technique, add to the evidence of the influence of natural resources on the capital-labor structure of trade. Bharadwaj's study shows that Indian exports to the U. S. tend to be capital-intensive relative to its imports from the U. S. A similar result is shown in Wahl's study of Canada. Both writers point out that the relatively large share of primary products in the commodity composition of their country's trade might have influenced the paradoxical finding.

What then is the implication of the above analysis for the C-L structure of the foreign trade of a given country? For a country such as Canada, the C-L requirements of its composite exports tend to be capital-intensive since exports are raw material-oriented and its import requirements labor-intensive because of large imports of manufactured goods. On the other hand, for a country like Japan, exports are also likely to be capital-intensive not simply because the country is capital-rich but because it is land-scarce and imports large amounts of agricultural products which are extremely labor-intensive (in contrast to the capital intensity in the U. S. and Canada). This reasoning can similarly be applied to explain both the Leontief Paradox and the Indian bilateral trade with the U. S.

We have so far proceeded within the framework of the factor proportions theory; let us go back now to the question of validity. Are the assumptions of this theory, and consequently its applicability, valid? One of the assumptions that has been criticized is that of "strong factor intensity", i.e., a given product remains relatively capital (or labor) intensive at any relative factor price ratio. If this assumption does not hold true (i.e., a machine product could be more capital-intensive than a textile product in the U. S. and vice-versa in, say, the Philippines), the relative price ratios of products and the pattern of comparative advantage may not be in accordance with the relative factor endowments of the two countries. The possibility of such a phenomenon (called factor reversal) has been theoretically and empirically demonstrated by Minhas.

One of Minhas' tests to show the occurrence of factor reversal is based on the comparison of the rankings of comparable U. S. and Japan industries by capital-labor ratios. The significantly dissimilar rankings of the two countries are given as evidence of factor-reversal. However, this writer finds that the dissimilarity is largely due to the large difference in the capital-intensity of agriculture and agriculture-related sectors. Since efficient production of agricultural products is dictated by a "land" factor and not solely by capital and labor, a ranking comparison excluding these sectors was made. This comparison raises the degree of similarity between the U. S. and Japan rankings significantly enough to question the generality of the factor-reversal argument as applied to the ranking test.

The outright refutation of the theory on the basis of the two-factor paradoxes of the U. S and other countries does not appear justified, since the inclusion of natural resources tends to explain these paradoxes. However, more research is needed on such topics as the nature of the production function and complementarity and/or substitutability of different factors as well as the role of the factors not treated in this paper. Such research would further clarify the real status of the Heckscher-Ohlin theory.

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Hans O. Schmitt, The Integration of Capital Markets in Europe: A Step Towards Political Unification — ERP No. III-50

The expectation that a customs union in Europe will ultimately lead to political unification is based on the so-called "spill-over" effect. This effect operates whenever any step towards integration creates new needs and fresh demands to proceed further in the same direction. Thus a customs union may create pressures to integrate not only commodity, but capital markets as well. An integration of capital markets in turn may necessitate currency unification for its effective functioning, and a unified currency area finally may imply a pooling of sovereignties sufficiently complete to destroy the separate identities of the participating nation states.

This paper argues that a sequence of that sort is in fact one of the mechanisms at work in the European integration process. Trade integration is not likely to prove acceptable except within a context of full-scale economic integration. For freer trade will strengthen tendencies towards factor price equalization. As the distribution of income shifts against capital in the poorer regions, the propensity to save will decline there, and the growth rate fall if financial stability is maintained. Thus "core areas" -- where capital and technology are already plentiful -- would gain at the expense of the periphery. Entrepreneurs and workers at the periphery cannot rationally accept this consequence unless they are themselves free to move to the center to participate in its gains. One of the requirements would be an integrated capital market.

A close intermingling of claims and liabilities in a single capital market requires a single currency to eliminate exchange risks. The political significance of money derives from the fact that it cannot exist without a set of individual producers accepting a collective identity. For if each producer issues his own currency, in terms of which he prices his product, the distinction between a currency depreciation and an individual price fall disappears. Money itself would then have given way to barter. But once several producers have joined in a single currency arrangement, they may, by a depreciation of the exchange rate, respond collectively to a fall in the external demand for any one of their products.

The option of such a collective response to economic adversity would be destroyed by a common currency. Producers would henceforth have to meet in the Common Market as individuals only, assuming a national identity only toward third countries. If in fact this fusion of national identities is not intended, the customs union must also be called in question. For by itself, it clearly creates tensions that cannot be resolved except by moving forward in the direction of political union -- or else by giving up the enterprise altogether. For no inevitability can be ascribed to the "spill-over" process. Precisely at the point where the creation of a common currency comes to threaten the foundations of sovereignty, the impulse to withdraw may be strongest.

A prefatory section to this paper explores the implications of the European experience for prospects for economic cooperation in Southeast Asia. Any discussion must first make clear to whom such cooperation is likely to yield political 36 advantages. Arguments based on economic welfare -- even if they can be consistently formulated -- are not likely to carry decisive weight in actual decision making.

The major interest groups, that just now might have a political stake in regional solidarity, are business communities in the various countries under consideration. Hard pressed as they are in Burma and Indonesia as well as in Vietnam, they would do well to cooperate for the mutual strengthening throughout the region.

The closest form of cooperation would be in a currency union. A common currency in Southeast Asia, if one is to develop, must be based on business communities indigenous to the region. Is it realistic to expect them to draw together on the European pattern?

Economic integration is a "nuclear process" in the sense that larger communities tend to crystallize around "core areas" where capital and technology are plentiful. In Europe, this process currently centers on the Ruhr. What core area could fulfill a similar function in Southeast Asia? Singapore as a commercial, financial, and also progressively industrial center, seemed for a while to be a candidate. In fact, it could have been argued that the Malaysian Federation was the first visible evidence that a "nuclear process" focussed on Singapore had begun. The Indonesian "confrontation" campaign can still be seen as a defensive reaction to that possibility.

But was the Malaysian Federation ever viable, independent of the British presence? The fact that the "entrepreneurial" elite on which it was based is ethnically mainly Chinese, makes this a questionable proposition for an otherwise predominantly Malay region.

Abandoning any hope for an agglomerative process in Southeast Asia, then, is it perhaps still possible to advocate a widening of Southeast Asian markets through lowered barriers to regional commodity trade? Through restrictions on capital account would continue, such an arrangement could still aim to realize economies of scale that would otherwise create barriers to investment even on a national basis.

But unfortunately, as argued above, trade "integration" is not likely to prove acceptable except within a context of full scale economic integration.

Neither a "free trade area" or a common market, therefore, let alone a common currency, seem likely prospects in Southeast Asia. There remains a last possibility, something on the pattern of the O.E.E.C. in Europe, similarly based on large-scale foreign aid from abroad. The organizational form such aid should take must be carefully adapted to the positive goal of strengthening business communities in the region. Most worth investigating perhaps is the creation of a regional development bank on the pattern of the International Finance Corporation rather than of the World Bank itself. The I.F.C. grants loans and participates in the capital specifically of private enterprises, without so much as a government guarantee.

We have defined four possible ways of organizing cooperation in Southeast Asia: a common currency, a common market characterized by a free flow of resources, a free trade arrangement with continuing barriers on capital account, and a regional development bank. The problems encountered in Europe in the effort of moving from the last of these to the first suggest that at this stage only the last offers sufficient hope of success to be seriously considered in Southeast Asia. But that is only a hypothesis to be investigated at this stage, not a conclusion based on a completed investigation.

K. C. Sen, Convergence in Planned Economies ERP No. III-51

It is the thesis of this paper that, regardless of the ideological commitments of the planners or the degree of plan comprehensiveness, certain basic tendencies to converge emerge in all forms of economic planning. Five such areas have been isolated and illustrations presented from the experience with widely different types of planning in a number of countries-- Yugoslavia, China, the U. S. S. R., Czechoslovakia, Mexico, France, Scandanavia, and the ECAFE countries. There is increasing recognition of the roles played in the process of economic growth by: (1) the price mechanism, interest rates, cost-profit relationships, tnd productivity, with a view toward improving allocative efficiency, minimizing waste, and rationalizing the cost structure; (2) material incentives, in order to foster work effort; (3) economic pluralism, to mobilize public participation and support; (4) functional banking, with a view toward catering to and increasing the financial viability of firms; and (5) flexibility in planning, in order to provide against administrative bottlenecks.

Hence: (1) If not the market rate of interest, then at least some kind of rate-of-return-equalization criterion must be applied by the planners, in order to avoid misallocation of resources. (2) "Enterprises" must be operated not merely on the basis of "output maximization". (3) "Average-cost-plus" policy does not necessarily lead to maximization of returns from investment, as the cost structure itself may not be optimal. (4) "Financial responsibility" requires that "enterprises" be subjected to various forms of charges, like depreciation and amortization charges. (5) To arouse active enthusiasm among workers towards increased efficiency, aid must be sought from "differential wage" payments, non-economic incentives being insufficient. (6) It is necessary to have many centers of decision-making and implementation of policy (though within the over-all framework of plan strategy), and some sort of "economic pluralism" is essential in bringing the plan to the people. (7) Both the strategy and the implementation of planning must be flexible in order to lend resilience to the plan. (8) "Functional banking" is a potent factor of accelerated growth rates, (9) Once the economy gets going and the dimensions of various economic issues get unwieldy, central or monolithic management leads to definite errors; the state must consider a phased and graduated withdrawal through delegation of authority; "target planning" or "indicative planning" with guidelines of policy, rather than crippling the market through multifarious controls, is desirable. (10) Though the empirical evidence is not conclusive, the tendency towards decentralization is associated with fewer bottlenecks, greater efficiency, and higher growth rates.

K. C. Sen, Nation-building and Regional Integration ERP No. III-52

The central objective of all economic policy-making in emerging nations of Southeast Asia seems to be nation-building or "national coherence" through economic nationalism or autarkical policies. Accordingly, their planning documents include a multiplicity of collateral objectives, each designed to promote the central objectives, but often conflicting among themselves. This gives rise to what may be called a "goal index" - a composite of economic goals which is the closest possible approximation of the central objective, with a marginal trade-off among the goals. In addition, the permissible means of policy are chosen within the range of the "goal index".

If these nations participate in a regional integration program, there is implied a compromise on the central objective itself. The burden of adjustment is likely to fall most heavily on two collateral objectives, economic self-sufficiency and diversified industrialization. Also, both the certainty and the range of permissible policy means are further reduced, especially when the particular advantage of this or that group within countries needs to be explicitly emphasized.

The success of any regional integration program among emerging nations depends, therefore, upon the effectiveness with which the economic benefits resulting from participation can offset the losses arising from the necessary compromises. The task will be easier the less sudden or drastic the compromise called for and the more cogent and compelling the case for economic integration. Expert pre-investment and feasibility studies and resource-potential surveys will be required, as well as expert advice on the prospects for joint industrial enterprises and marketing systems. The benefits accruing from economies of scale, external economies, vertical division of labor within the region, and the establishment of institutions such as a regional development bank or a payments union must be emphasized. In fact, economic nationalism itself can be used to promote regional integration, after these studies have been made, since many bottlenecks--for example, those arising from the small size of a market and the lack of resource-complementarity-- may now be overcome. Moreover, the economic viability of the region vis-a-vis the rest of the world may be increased.

In this study an attempt has been made to study systematically the nature of the contraints on economic nationalism which arise (1) from the competition among collateral objectives in (a) a closed economy, with foreign trade; (2) from determining permissible policy means in individual countries; and (3) from participation in a regional integration scheme, both as regards collateral objectives and permissible policy means.

K. C. Sen, Economic Growth and the Price Level--An Analysis of Some Asian Data, 1950-1963 ERP No. III-87

This paper deals with the question of the relationship between economic growth and the price level in Asian countries. The format of the paper is as follows: (1) A survey of the important studies in the field of the relationship between economic growth and the price level; (2) discussion and evaluation of three interpretations of the causes of inflation, namely, the "monetary fundamentalists", the "structural fundamentalists" and the "behaviorists"; (3) analysis of data between 1952 and 1962 in relation to the behavior of prices in some Asian countries; and (4) policy implications.

In whatever way inflation may be defined--as a sustained rise in the general level of prices, or as a state of generalized excess demand where too much money chases too few goods, or in some other way--the phenomenon does not lead itself to a simple explanation. The juxtaposition of the relevant variables--monetary, structural, and behavioral--differs from time to time and from country to country. It is essential to keep in mind the heterogeneity of situations and the interdependence of the factors involved.

It is even hard to say whether inflation is an inescapable cost of economic growth at all. The empirical evidence--in Europe, the U. S., Latin America, and elsewhere--does not indicate any necessary or casual relationship between the rate of economic growth and the price level.

The analysis of part 3 attempts to explain the behavior or prices in some Asian countries through the rates of change in the aggregate real gross national product, money supply, wage rates, terms of trade, and past price behavior. Since the number of years for which the necessary data on each individual country are available is not sufficient to give us the necessary degrees of freedom, we have employed a temporal cross-section approach. The countries covered are Ceylon, India, Indonesia, Japan, Pakistan, and the Philippines for the period 1952-62. There are variations between countries in the number of years covered, but all these countries have observations in all the variables.

The analysis gives some insight into the phenomenon of price-change. There is considerable variety of experience among countries, but the magnitudes of the coefficients are sensitive to the specification of the model. No single-variable approach to an explanation of the behavior of prices is sufficient. Thus, whereas money supply is a very significant variable for some countries in explaining the course of prices, in others it is less so. Whereas improvements in the terms of trade do exert a downward pressure on prices in certain countries, in others they do not. Whereas a rise in money wages tends to be price-stimulating in general, the impact is greater in certain countries than in others. It is possible to say broadly what the course of prices will be in certain countries by extrapolating from the past behavior of prices, while in others this approach is too hazardous.

To have economic growth without inflation we need a composite policy. In the LDCs particularly, where precise estimation of the relative magnitudes of the relevant variables is not possible, the need for certain rules of thumb becomes imperative. For that matter, even in the DCs, governments do follow the so-called "guidelines" of policy. In the LDCs, where a substantial chunk of the economy is non-monetized and several structural bottlenecks (for example, in transport) reduce factor and product mobility, there is greater reason to formulate such rules of thumb.

Another serious problem arises from the lack of integration and coordination among various policies--monetary, fiscal, and commercial. For instance, whereas stringent controls on the banking sector might be exercised, on the one hand, it is not infrequent to find huge budget deficits side by side. Similarly, the drive for self-sufficiency of the economy might lead the country into trade and tariff policies that are essentially inflationary.

Part of the problem may be of the LDC's own making. Defective tariff-rate structures, over-valued exchange rates, excessive zeal for attaining economic self-sufficiency, impatience and the tendency to shift the responsibility to the outsiders (e.g., the

DCs) are greatly responsible for the inflationary impact of LDC growth policies. This is not to deny that there are certain real bottlenecks in these economies, e.g., lack of savings and skills and a very thin base of infra-structure.

One of the ways in which cost structures and investment patterns could be rationalized is through intra-regional economic cooperation. With resulting economies of scale, richer resource availability, greater factor and product mobility, and less autarky in trade and tariff policies, it may be possible to minimize the cost of economic growth in terms of inflation.