

School of Oriental and African Studies University of London

**DEPARTMENT OF ECONOMICS
WORKING PAPERS**

No.133

Export Promotion, the Fallacy of Composition and Declining Terms of Trade (or the Moors' Last Sigh).

Matthew McCartney

January 2004

economics@soas.ac.uk

<http://www.soas.ac.uk/departments/departmentinfo.cfm?navid=11>

Export Promotion, the Fallacy of Composition and Declining Terms of Trade (or the Moors' Last Sigh).

By

**Matthew McCartney
Department of Economics
SOAS, University of London
London
WC1H 0XG**

E-mail mm80@soas.ac.uk

Abstract:

This paper examines various schools of trade policy reform and finds little difference between them in regards their essential export optimism. This optimism is based on an unwarranted assumption in cross-country empirical studies. In practise the increasing number of large LDC's shifting towards export promotion since the 1980s is found to coincide with declining terms of trade for labour-intensive manufactures. So far this decline has been offset by growth in volume. The positive relation is actually dependent on market growth in developed countries rather than domestic policy reform. Marx (the Moor) provides a useful framework in which to analyse this process. His analysis of competition and accumulation within a national economy is transposed to that of international trade. Finally, the increasing integration of capital into 'value chains' and the formation of regional trading blocs can be related to the crisis tendencies of competition and the erosion of profit margins.

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Introduction

Export optimism is a widespread orthodoxy among trade economists. Criticisms do not tend to question the gains from free trade, which are generally accepted, but rather their size. Trade pessimists are likely to suggest these are small and less than alternative policy interventions. Others argue free trade needs to be supplemented by active policies to promote exports.

There are three loose schools to policy reform, titled here the 'minimalist', 'market conforming' and 'governing the market'. The first believes exports are best promoted through removing impediments to the free market; the second that exports are determined exogenously by factor endowments, policy can help realise this underlying potential or even exert an independent influence on trade outcome; the third that export structure can be endogenously determined by strategic government policy. Fundamentally there is little difference between the three approaches, each argues that a greater volume of exports from developing countries is both desirable and possible. All three schools do make a passing acknowledgement to the need for developed countries to liberalise markets especially in agriculture and textiles, to ensure growing market access for developing countries.

The various studies used to provide empirical backing for the three schools have been based on an unwarranted premise – that of *ceteris paribus*. Openness is demonstrated as being beneficial with the assumption that all else is constant, other economies remaining closed or open. The true counterfactual is of closed economies moving simultaneously towards openness and export promotion. This accords with the evidence of a general shift to openness since the 1980s.

A generalisation of the export experience of the East Asian countries is argued by Cline (1982) to imply politically unacceptable levels of developed market penetration by LDC exports. The optimistic outlook suggests that continued reliance on natural resource intensive exports for some LDC's, growing south-south trade and less reliance on trade among large LDC's will mitigate risks of politically unacceptable market penetration. The increasing number of large LDC's shifting towards export promotion in the 1980's¹ is found to coincide with a declining terms of trade for labour intensive manufactures. This is the 'fallacy of composition' which raises the possibility of immiserising growth. So far most studies find declining terms of trade have been offset by an increasing volumes of exports. Optimists have implicitly turned attention from the (LDC) domestic policy reform beloved of the World Bank, and posit a positive relation now dependent on domestic market growth in developed countries.

Late industrialising economies rely on learning rather than innovation, Amsden (1989, 2001). Firms and countries seek to upgrade production to earn rents in less competitive market niches. The process is a dynamic one, a race to upgrade faster than rivals, and profits being continually eroded as early leads fade away. Marx analysed the dynamics of competition that compel capitalists to invest in new methods of production. In this context we can directly link export promotion and declining terms of trade. There is a curious contradiction in the literature. Policies to increase

¹ Often through the auspices of World Bank sponsored structural adjustment programmes.

competition and atomisation, to increase the export orientation (share of output exported) of individual economies are held to coincide with general export growth (higher volume). Marx noted that greater levels of production and innovation are typically associated with greater centralisation and concentration of capital.

Marx argued the dynamic of over-accumulation and crisis is the specific mechanism through which new methods of production are introduced and generalised within the capitalist system. This generates a historical tendency to centralisation and concentration of capital, in order to reduce crises by reducing competition.

We can identify two tendencies in the world economy and better explain them within the framework of falling terms of trade, growing centralisation of capital and the stirrings of a developing world response. The increasing integration of capital into 'value chains' and the formation of regional trading blocs, can be related to the crisis tendencies of competition for rents and the erosion of profit margins.

And this is where we can explain the somewhat enigmatic alternative title. The 'Moors Last Sigh', does of course posit a new relevance for Marx (the Moor), this time transposing his analysis of competition and accumulation within a national economy to that of international trade.

"When I started researching this biography, many friends looked at me with pity and incredulity. Why, they wondered, would anyone wish to write about – still less read about – such a discredited, outmoded irrelevant figure? I carried on regardless; and the more I studied Marx, the more outstandingly topical he seemed to be....."
(Wheen, 1999, p4).

Orthodoxy: Export Promotion

'Export optimism', is claimed by many to be *the* orthodoxy,

"It is now *widely* accepted that growth prospects for developing countries are greatly enhanced through an outward orientated trade regime and fairly uniform incentives (primarily through the exchange rate) for production across exporting and import-competing goods." (Krueger, 1997, p1).

Krueger (1998) goes further, she suggests there is no longer a need to debate the question, export optimism is effectively a closed issue. We should turn attention to how so many had been deluded for so long by the false siren calls of import substitution, learn from failure:- failure in theory, in interpretation, in communication and in policy formulation.

Evidence

Perhaps the most widely cited studies extolling the merits of free trade are those of Dollar (1992) and Sachs and Warner (1995). The former constructing an 'index of

free trade' based on distortion and variability in the real exchange rate and the latter a binary index to describe a country as open or closed based on four criteria.

Rodriguez and Rodrik (2000) made a valiant effort at iconoclasm. Changes in the exchange rate and hence Dollars' distortion index were due not to 'trade policy' but to macroeconomic policy, monetary, fiscal and exchange rate policies. The index captured the effects of macro instability on growth. The openness index of Sachs and Warner (1995) was dominated by state monopoly and black market premia, which were in turn correlated with other determinants of economic growth, notably location in sub-Saharan Africa. This index was reaching the somewhat disingenuous conclusion that growth in sub-Saharan Africa had been slow.

A valiant attempt but for most little more than a footnoted curiosum. Further studies have addressed the issues of robustness and endogeneity raised by Rodriguez and Rodrik. Edwards (1998) found the positive relationship between openness and growth to be valid after testing the relationship between nine different indicators of trade policy. Frankel and Romer (1999) and Onafowora and Owoge (1998) reached the same conclusions allowing for the possibility of reverse causation (endogeneity).

There is little appetite in the literature to depart wholesale from 'export optimism', at most, a number of qualifications.

The inherent difficulty of constructing an unambiguous index of 'trade policy' will always leave a residue of doubt that motivates an ongoing literature. Effort needs to be expended to test robustness, causality and whether the positive relationship is context dependent². The emphasis of debate has shifted,

"there is a dirty little secret in international trade analysis. The measurable costs of protectionist policies...the reductions in real income that can be attributed to tariffs and import quotas...are not all that large." (Krugman, 1995, p31).

Correspondingly Rodrik (2000) argues that integration cannot substitute for a development strategy. When administrative and political capital are scarce, a clear sense of priority is needed. A case in point being that the cost of implementing WTO obligations for a typical LDC to total \$150m, and the return to such a sum being considerably higher were it to be invested in female education.

Krueger as ever is unrepentent,

"There is no doubt that the countries following outward orientated strategies grew faster." (Krueger, 1998, p1515).

Fundamentally the 'dirty secret' is a small one. The debate has shifted from comparing the relative merits of import substitution and export promotion to debating just how beneficial is export promotion. We are all optimists now, some only more so than others.

² E.g. whether the positive relationship depends on rapid growth in world trade or low trade protection in developed countries.

Trade and Policy

Within the framework of ‘export optimism’ there are three policy schools, the ‘minimalist’, ‘market conforming’ and ‘governing the market’. All share the idea that it is both desirable, possible and beneficial for LDCs to increase exports.

Policy Reform

The World Bank: A Legacy of Minimalism

Policy reform especially with regards trade policy is seen by the World Bank primarily in terms of reducing state intervention. Economic development of the rapidly growing Asian economies was associated with the rapid growth of manufactures. Removing constraints on exporting will enable other countries to utilise a comparative advantage in labour-intensive production and emulate this feat.

“The African countries undergoing structural adjustment have moved a long way toward good trade policies. They have reduced administrative rationing of foreign exchange and eliminated many non-tariff barriers. Yet they still have a long way to go...adjusters have not done enough to reduce the commercially orientated elements of protectionism – tariffs, non-tariff barriers, and industrial restrictions...” (World Bank, 1994, p61).

Market Conforming Policy Intervention

Market conforming intervention comes in variety of guises but is united by appeals to criteria such as ‘enabling’, ‘diversifying’, and ‘supporting’.

An important theoretical framework for the analysis of market conforming intervention is that of comparative advantage. In a model of endowment determined trade, the scope and composition of exports is an exogenously given variable, against which various impediments may exist. Market conforming policy is about removing such impediments to realise the underlying potential³.

Owens and Wood (1997) use a (modified) Heckscher-Ohlin model to explain the variation of trade shares in processed primary, unprocessed primary and manufacturing. The scope of sub-Saharan Africa (SSA) to follow the manufactured export led growth of East Asia is limited, because they have the wrong resource endowments. SSA has a low skill/ land ratio, giving it a comparative advantage in primary exports. Wood and Meyer (1998) argue there is ample scope for policy to enable export growth in SSA based on diversification into new crops, fruit, flowers and vegetables⁴. Only a quarter of the cultivable land in SSA is cultivated, SSA

³ Mosley (2000) notes that this debate pays insufficient attention to the need for intervention to correct for endogenous distortions in information, externalities, property rights and income distribution. The only distortions in a market economy are not policy induced!

⁴ By contrast raising relative skill (education) levels would be a long process.

currently fulfils only a small fraction of world demand so rapid output growth would have little impact on the world economy.

Such projected reliance on primary exports runs into a critique of some historical stature. Prebisch (1950) and Singer (1950) argued; there is a lower price and income elasticity of demand for primary than manufacturing goods; technical progress in developed countries leads to a secular decline in the use of primary raw materials in the manufacturing process. This argument is commodity specific. A shift from primary commodities to manufactures would lead to a secular gain in a countries terms of trade.

Empirical Results

Prebisch (1950) and Singer (1950) found the price ratio of non-fuel primary commodities and manufactures to be subject to a secular downward trend. They found support for data on coffee, bananas, cocoa, tea and tobacco. More recent studies have tended to support this conclusion⁵. Thirlwall and Bergevin (1985) found the terms of trade moved against primary products between 1954-82. Sapsford and Balasubramanyam (1999) found a downward and highly significant trend between 1900 and 1992, with a marked increase in the trend depreciation and volatility of prices after 1972/3.

Such elasticity pessimist arguments advise on both a theoretical and empirical basis for LDCs to diversify away from reliance on primary exports. This more recent debate, combined with 'export optimism' emphasises diversifying the structure of exports rather than supporting a strategy of import substitution. This is reinforced by other findings highlighting advantages of diversification.

In 1980 seventy-five percent of all LDC exports were primary commodities, now around eighty percent are manufactures. Africa by contrast is as dependent on a narrow range of primary exports as it was thirty years ago. Collier (2002) finds primary commodity dependence to be associated with poor governance, corruption and a greater risk of civil war. Continued dependence accounts for a large share of the differential performance between SSA and the rest of the world.

Including exports as an additional argument in the production function Fosu (1996) found evidence that manufacturing exports exert a positive differential impact on GDP growth (independently of the terms of trade issue). Manufactured exports provide greater economies of scale, greater backward and forward linkages with the rest of the economy⁶, and act as a more significant conduit of technological diffusion.

Sri Lanka initiated market reforms in 1977 that transformed the existing 'colonial' trade structure. Liberalisation allowed Sri Lanka to exploit a comparative advantage in unskilled labour, especially women who filled eighty percent of the jobs in the newly established export processing zones. Such reform led to a secular improvement

⁵ A more extensive review of the relevant literature can be found in Mayer (2002). The results presented there broadly support those discussed here.

⁶ E.g. Hirschman (1958).

in the terms of trade⁷. Between 1978 and 1997 manufactured exports grew at an annual rate of twenty percent, increasing their share in total merchandise exports from five to seventy percent. The ratio of exports to gross output in domestic manufacturing from three percent in the late 1970s to seventy-two percent in the mid-1990s. There was a notable increase in exports of labour intensive products such as electrical and electronic products, leather goods, ceramics, footwear, toys and plastics. The net barter terms of trade (NBTT) for total manufactures increased by slightly over seven percent p.a.

Beyond the Endowment Thesis

Though the endowment thesis argues the structure of exports is exogenously determined, policy can be crucial in helping a country realise this potential. Wood and Meyer (1998) find a wide dispersion of actual from predicted manufactured export shares, for example Zimbabwe being much higher, and Uganda and Malawi much lower than predicted by endowments.

Wood and Jordan (2000) argue that many African countries are not exporting even what would be suggested by their endowments. In 1990 a third of exports from Zimbabwe were manufactured and only one percent from Uganda. This despite similar land/skill ratios, being both tropical and landlocked and undergoing liberalisation in the 1990s. The difference is policy induced, the poor state of transport from Kampala to Mombasa, the more limited road network in Uganda, decision to expel the entrepreneurial Asian community in 1973 from Uganda....

Milner et al (2000) find conventional measures of nominal and effective protection have declined in Uganda as a result of liberalisation in the 1990s. Natural rates of protection due to high costs of transport⁸ lead to a de facto high rate of protection for the domestic market. Natural rates of protection on coffee generate an implicit export tax of twenty-five percent, on manufactured foods of one hundred percent. Despite the formal trade liberalisation there is no evidence of increased efficiency at ports, shorter delays at borders. There is thus scope for policy reform to further enable export growth.

Other authors have suggested policy can influence exports independently of comparative advantage.

Endowments do not wholly explain trade outcome. Elbadawi (1999) finds Malaysia, Indonesia and Thailand have been able to increase their share of manufactured exports to higher levels than explained by their skills and relative abundance of natural resources. Using a composite index of transactions costs, proxied by corruption, the length of paved roads and number of fax machines in the country, Elbadawi argues,

“transactions costs are major determinants of manufactured exports and that investing on reducing these costs generates the highest payoff for the capacity to export manufactures. However, our results also lend support to the view that: real exchange

⁷ See Athukorala (2000).

⁸ Milner et al (2000) use estimates of marine and air shipping costs to construct estimates of natural rates of protection.

rate-based competitiveness is a pre-requisite for a developing (especially low-income developing) country to become a successful exporter of manufactures.” (Elbadawi, 1999, p13).

Collier (2002) develops a political economy model of comparative advantage, and calculates risk corrected incomes of factors of production. He argues manufacturing is the most transactions intensive activity so will be disproportionately effected by a poor policy environment.

Sachs and Warner (1997) examine the more general causes of slow growth in SSA between 1965 and 1990. They argue there is no special ‘African’ cause of slow growth caused by its peculiar colonial history, ethnic and tribal divisions, climate and geography. Rather they reach an optimistic conclusion, poor policies and institutions explain a large share of growth. Better policies would contribute to stronger economic performance. They identify openness, human capital formation, institutional quality and central government savings as being of greater significance than the tropical climate and landlocked geography.

Vertical diversification into processing is one possible development strategy to reduce reliance on primary commodities and capture a greater proportion of value added. Owens and Wood (1997) explain trade outcome based on factor proportions, however, the performance of such strategies is mixed even among countries with the same endowments. Cramer (1999) argues the case of cashew nut exports from Mozambique demonstrates the weakness of conducting the debate at too aggregate a level. In Mozambique argues Cramer the most pressing constraints are internal, political rather than economic or technical (i.e. endowment) - the supply of raw cashew nuts, infrastructure to connect small firms, lack of new planting. There is scope with the correct policy framework for vertical integration into processes such as salting, flavouring and mixing.

Governing the Market

Going beyond the endowment approach suggests that policy can directly influence comparative advantage. The ‘governing the market’ approach argues that comparative advantage can be actively changed as a policy variable. This is thus a heterodox endowment model of trade. This approach is derived from the more general literature on the developmental state of Amsden (1989, 2001) and Wade (1990) and suggests exports can be ‘pushed’ not simply ‘enabled’. Export structure can become endogenous, directly determined by strategic government policy. A selective industrial policy where rewards and assistance are contingent on improved (export) performance is crucial. In effect using a non-liberal method to pursue the same end – higher growth of exports.

Lall (1995) notes the weakness of an African supply response in manufacturing output and exports despite sustained trade and general liberalisation. He criticises the simplistic belief that markets are efficient and government intervention distortionary and argues there are profound market failures⁹ in the process of acquiring technology

⁹ Such as externalities that may require central co-ordination, imperfect information, capital market failures preventing firms borrowing during the learning phase etc.

as a prerequisite to expanding exports. The process of becoming efficient is slow, risky and costly. Lall calls for a 'technological capacity' approach. Firms face a range of inefficiencies and government interventions may be necessary in factor and product markets. Product markets may call for infant industry protection. Governments should therefore retain powers to allocate resources, doing so in a clear and transparent manner with strict requirements of capability development leading to export growth. Industrial policy should discriminate between activities according to different technological needs, focusing on skill development, technology and financial and financial support.

The importance of a selective industrial policy, contingent on improved export performance has been noted by Mosley et al (1995) and Tsie (1996) in the context of SSA and even by the World Bank (1993) in the case of East Asia.

The Three Schools

Despite the apparent conflicting analysis of each school they share a basic similarity. The underlying 'export optimism' of the governed market approach does not differ from that of the minimalist or market conforming approaches. All three approaches are optimistic in the sense they believe higher exports from LDCs are both desirable and possible. They differ substantially from Bruton (1998) who argues in contrast for a 'reconsideration of import substitution'. The belief (or not) in the efficacy of the state to improve economic outcomes has been made without a broader consideration of the external framework in which intervention or laissez faire occurs.

Domestic Policy Reform in Developed Countries

In addition all three schools agree policy reform in developed countries is necessary to maximise the potential for export growth from LDCs. This analysis of the external framework is tacked on as a bit of an afterthought. We have already seen that once the question of the fallacy of composition is broached the external environment becomes all-important. However in the narrow world of the three export optimist schools it can merely enhance what is already positive relationship. The 1994 Uruguay Round of the GATT included agriculture for the first time, for which non-tariff barriers were to be converted to tariffs and reduced¹⁰. The Multi-Fibre Arrangement, effecting textiles and clothing is scheduled to be phased out. However, high protection is projected to remain after the round has been implemented, in agriculture twenty-four percent, textiles and clothing twelve percent and six percent on other manufactures, Anderson et al (2002). The OECD grants nominal assistance to agriculture of \$354bn a year, mostly through distortions to market prices. There is still a significant scope for expanded market access for developing countries.

There are also some risks in the possible extended use of safeguard clauses (protection to prevent serious disruption to domestic industry) and new non-tariff barriers such as eco-labelling.

¹⁰ A notable exception being Japanese rice.

A pertinent example of distortions to comparative advantage caused by policies in developed countries is provided Kaplan and Kaplinsky (1999) for the case of deciduous canned fruit. It is a resource and labour intensive activity with a high trade ratio, using a large share of local inputs. South Africa has a distinct comparative advantage offering both low costs and high quality. Protection and subsidies in industrially advanced countries have led to producers in Italy and Greece significantly displacing South Africa from EU markets.

The ‘Fallacy of Composition’

Every study so far cited has been based on an underlying premise typical to economics, they show how openness has been beneficial, or how there has been a secular decline in the terms of trade for primary producers based on a *ceteris-paribus* assumption. Openness is demonstrated to be beneficial with the assumption that all else is constant, open and closed economies remain so. The results are thus context dependent. It is not valid to draw the conclusion that all countries would experience the same level of export growth by pursuing export promotion. The counterfactual is rather closed economies moving in unison to greater openness.

This is the ‘fallacy of composition’, first discussed in the context of immiserising growth by Bhagwati (1958).

The Debate

Little attention has been paid in studies of openness to the constraints on international market demand. Most studies focused on the side of export supply and the impact of LDC policy regimes on that supply. This is odd Wood (1994) provoked a debate of profound contemporary relevance, arguing the expansion of exports from the NICs had a large impact on unemployment and inequality in developed countries.

Market Saturation

Cline (1982) calculated the levels of manufactured exports from LDC’s that would have occurred in 1976 if all LDC’s had experienced the same share of exports as Hong Kong, South Korea, Singapore and Taiwan (adjusting for normal inter-country differences associated with size and level of development). The hypothetical levels of LDC exports were then compared to industrial country consumption at the sectoral level to determine the resulting import penetration ratios. A generalisation of the East-Asian export model would have implied a rise in the LDC share of the market for manufactured imports from approximately seventeen to over sixty percent for all seven industrial countries, and from twenty-seven to over seventy-four percent for the US. Cline argues this would have generated an inevitable political reaction against free trade in developed countries.

In the 1960s and 70s Bangladesh, Indonesia, India, Pakistan and China were closed to international trade. In the 1980s they shifted to more open trade regimes. Between

1987 and 1993 developed country imports from low-income countries rose from \$28bn to \$110bn. Reflecting rapid domestic industrialisation,

“the pace and depth of this new market presence [China] in the USA and Japan is astonishing.” (Kaplinsky, 1999, p78)

Hence it is misleading to hold up the East Asian experience as a model for development. It,

“almost certainly cannot be generalised without provoking protectionist response ruling out its implementation.” (Cline, 1982, p89).

Terms of Trade for LDC Manufactured Exports

In developed countries, wages are not flexible, price declines are not passed on to labour. In LDCs by contrast, price declines are typically passed on, allowing them greater scope to compete on the basis of price and preserve profit margins. Competition between LDC exporters becomes competition among labour, UNCTAD (2000). Greater price flexibility in LDCs also exerts a downward pressure on their prices and terms of trade. The difference is not as in the early analysis of Prebisch inherent in the structure of final markets (income elasticity of demand), but rather in factor markets (price flexibility).

In the last two decades there has been increasing competition in international markets for labour intensive manufactured goods. There was a decline in market concentration of electronics and electrical goods throughout the 1980s and 90s. The concentration in clothing declined continuously from the late 1980s. Finished products from technology intensive activities such as machinery or transport equipment (aircraft, ships) remain among those with the highest and increasing concentration of export market shares. These developments are in line with LDC participation in the production and export of labour intensive manufactures. The first tier NIC's accounted for two-thirds of all clothing exports from LDC's during first half of the 1980s, their share later dropping to one fifth.

Electronics in the first tier NIC's were responsible for most of the spectacular increase in the share of LDC in world exports between the 1980s and the mid-1990s. More recently Mexico and China have been increasing their market shares. Growing price competition in these products, especially for semi-conductors has exposed traditional LDC exporters to competition from lower cost producers.

The clearest exception to the traditional stylised view of Prebisch and Singer is the fall in the price of IT goods, though these are technologically advanced manufactures, it is relatively easy to establish new small-scale production facilities and difficult for large producers to establish a monopoly position¹¹.

Manufactured Goods: Evidence

¹¹ Nolan (2001, p134-144) argues instead that there is growing market concentration in the IT sector.

Evidence suggests that openness is increasingly associated with declining terms of trade. Sarkar and Singer (1991) extend the framework of Prebisch and Singer to the exchange of manufactured exports. Between 1970 and 1987 the unit value of manufactures exported by LDCs as a group declined by one percent per annum relative to those of developed countries. This was offset by a sharp increase in volume, generating a ten-percent average increase in the income terms of trade.

By the mid-1990s China had become a major source of imports in a number of commodities. Wood (1997) suggests the speed and scale of this penetration of world markets resulted in a twenty percent decline in the terms of trade for LDC manufactured exports. Maizels, Palaskas and Crowe (1998) analysed the unit values of manufactured imports and exports between the EU and developing countries between 1979 and 1994. The technology leaders, the U.S. and Japan experienced a slightly favourable trend in their manufactures terms of trade with the EU. They found a moderately negative trend for East and South East Asian exports (minus one percent) and for other African, Caribbean and Pacific economies a strongly negative (minus five percent per annum) trend. Maizels (2000) found that the terms of trade of developing countries with respect to the U.S. had significantly worsened between 1981 and 1996. Though this was dominated by changes in trade volume, induced by the huge U.S. trade deficit. Zheng and Zhao (2002) found that China's net barter terms of trade in manufactures had declined by more than ten percent between 1993 and 2000. This decline was greater vis-à-vis developed than developing countries and less pronounced for traditional labour intensive manufactures than those of medium and high technology intensity such as computers and office equipment, telecommunications equipment and semi-conductors, those sectors in which China's participation in world trade has grown most rapidly.

This empirical evidence that global competition for labour intensive manufactures has risen recently coincides with the shift in the 1980s of several large LDCs towards export orientation. This has resulted in intensified clustering in labour intensive manufactured exports and increased market competition.

So far falling terms of trade have been more than offset by increasing volume. While studies of 'openness' have tended to tack on proposals for developed countries to further liberalise markets to maximise the benefits from openness. In practise we find the beneficial effects of export growth (volume) entirely determined by growth in high-income countries.

The Optimists

Ranis (1985) was optimistic. The different initial conditions of LDC's (size and factor endowments) and policy postures means that 'export led industrialisation' would imply producing different goods at different points in time. NIC's gaining economic maturity, moving up the production ladder and leaving room for newcomers. Terms of trade movement are thus at least partly endogenous to the export growth process, export success can generate terms of trade improvement over time.

Those developing countries with natural resource endowment e.g. Brazil and Argentina are likely to remain with a strong raw material basis to exports and a permanently lower manufactured export share than small, resource poor city states. Large LDC's such as Indonesia, India, China are unlikely to rely on foreign markets to the same extent as the first generation NIC's who were compelled to expand exports to earn foreign exchange for capital goods imports and raw materials e.g. oil.

The pessimistic also view neglects the potential of an increasing share of exports going to markets in the south. Higher income growth among middle income countries will generate a more than proportionate increase in south-south trade.

Income growth will generate expanded export growth from the north alleviating protectionist sentiments, generating a greater tolerance for worker displacement and also specific anti-protectionist countervailing political pressure – e.g. by the agricultural lobby in the U.S.

It is also important to increase market access conditions for these products, the pace at which the more advanced developing countries diversify their own production structures away from low skilled exports, and how quickly developed country producers move out of low skill products. The flying geese pattern of development can also help avert the fallacy of composition and protectionism by expanding south-south trade in manufactures and allowing newcomers some space in the markets of industrial countries.

Income inequality and unemployment in developed countries is likely to supplement pressure for protection. Complementary policies such as training and education will help labour mobility between sectors in developed countries. The contemporary export penetration of NIC's is not without precedence, between 1958 and 1975 the export penetration of goods from Japan and Italy into the US and (five member) EEC was on a comparable scale. This was not associated with labour market problems. By contrast the period also saw a large migration of labour. Rapid and sustained growth and full employment in HIC's was crucial for averting potential problems.

Far from export growth being a function of domestic policies in LDC's we are moving rapidly to the conclusion that the benefits of openness are dependent on domestic policy in developed countries. Export optimism is based on the (implicit) hope that the international economy will remain favourable.

Marx, Rents and Competition

It is a standard proposition that where barriers to entry are low, resultant competition will drive prices and profits down. Long term growth will then be dependent on upgrading to less competitive market niches to capture rents, e.g. from clothing to electronics to IT. Amsden (1989, 2001) argues that for late industrialisers learning is more important than innovation. Rents are dynamic firms fight to raise productivity and learning faster than the decline in margins as competitive pressures intensify.

”In the context of a competitive environment these rents can only be appropriated through a strategy which sustains upgrading at a higher pace than competitor economies.” (Kaplinsky, 1999, p77).

To orthodox economists supply and demand adjust smoothly. Following a decline in profit rates in an oversupplied market producers will cut back on production and exit the industry until profits have been restored to a normal level. For the export optimists the correct policy is to pursue export promotion regardless. This has an evident echo of Marx’s analysis of the secular tendency to over-production in capitalism. For Marx the capitalist is rather compelled to introduce new methods of production under the pressure of competition. To reduce costs, allow the capitalist to sell below the costs of other capitalists and capture market share. The driving force of capitalist production is the need for capitalists to constantly invest in new methods of production to exploit the possibility of earning a surplus profit and meet the threat of other capitalists doing the same thing. Rather than supply falling in response to falling profits it increases and initiates a dynamic of overproduction. There is a contradiction between the production of surplus value and the realisation of the surplus value through sale of use values. A contradiction between the social relations and the forces of production. Overproduction is the means by which less efficient producers are forced out of the market. It is not just an accident of competition but is its essential form in a capitalist economy.

There is a continual tendency towards the commoditisation of product and factor markets. The mid-1990s witnessed a massive investment boom in Asia’s electronics industry, and subsequent oversupply and price collapse. The continued growth of world trade is thus crucial. Korea suffered from a dependence on a single export, Dynamic Random Export Memories (DRAM’s). As DRAM’s became increasingly commoditised during the 1990s, the price declined and the trade balance plunged into deficits that provided the backdrop to the 1997 crisis. From a surplus on current account of \$0.4bn in 1993, Korea lurched into a \$4.5bn deficit in 1994, \$8.9bn in 1995 and \$23.7bn in 1996, Kaplinsky (1999).

“The more powerful and costly means of production that he has called into life enable him, indeed, to sell his commodities more cheaply, they compel him, however at the same time to sell more commodities, to conquer a much larger market for his commodities; consequently our capitalist will sell his half yard of linen more cheaply than his competitors....He drives them from the field, he wrests from them at least part of their sales, by underselling them...However, the privileged position of our capitalist is not of long duration; other competing capitalists introduce the same machines...on the same or on a larger scale, and this introduction will become so general that the price of linen is reduced not only below its old, but below its new costs of production.” (Marx, quoted in Clarke, 1994, p87).

There is a curious contradiction in the literature. Policies to increase competition and atomisation, to increase export orientation (share of output exported) of individual economies are held to coincide with general export growth (higher volume). Marx pointed out that greater levels of production are typically associated with greater centralisation and concentration of capital. Marx argued the dynamic of over-accumulation and crisis is the specific mechanism through which new methods of production are introduced and generalised within the capitalist system. This generates

a historical tendency to centralisation and concentration of capital, in order to reduce crises by reducing competition.

“The attempt to maintain the rate of profit in the face.....and the growing scale of production leads to an intensification of the competitive struggle, leading in turn to the further concentration and centralisation of capital and the further development of the forces of production and expansion of productive capacity, which further intensifies competitive pressure in a cumulative spiral.” (Marx, quoted in Clarke, 1994, p242).

Value Chain Analysis and Regional Trading Arrangements

We can identify two tendencies in the world economy and better explain them within the context of falling terms of trade, growing centralisation of capital and the stirrings of a developing world response. The increasing integration of capital into ‘value chains’ and the formation of regional trading arrangements. Both can be related to the crisis tendencies of competition for rents.

Value Chain Analysis

“The value chain describes the full range of activities that are required to bring a product from its conception, through its design, its sourced raw materials and intermediate inputs, its marketing, its distribution and its support to the final consumer. In other words the chain can be seen as incorporating production, exchange, distribution and consumption from the cradle to the grave of a given product or service.” (IDS, 2001, p1).

Many chains are characterised by a dominant party¹² who become responsible for upgrading activities within individual links and co-ordinating interaction between the links. There is a necessary distinction between co-ordination undertaken by buyers (buyer-driven commodity chains) and circumstances where producers take the key role (producer driven commodity chains). Buyer-driven chains are characteristic of labour intensive industries such as furniture, footwear, clothing and toys. Producer-driven chains see the producer take more responsibility for promoting the efficiency of downstream suppliers. The relationship is more likely to be based on foreign direct investment. Trade in final products manufactured locally and exported is being replaced by more complex trade in sub-components and services.

In many sectors value added (economic rents) is found increasingly in design, buying, marketing rather than production itself. As more countries have developed their capacities in industrial activities, barriers to entry in production have fallen and competitive pressures have heightened. Barriers to entry determine the distribution of rents. Rents are increasingly located in the intangible parts of the value chain.

¹² Nolan (2001, p119-122) calls this party the ‘core systems integrator’.

Copyright and brand names (seventy years and perpetuity) represent immutable forms of economic rent¹³, Kaplinsky (2000).

The value chain is an effort to simultaneously monopolise rents and benefit from falling terms of trade. The fallacy of competition results from the global spread of capabilities in manufacturing. Dolan et al (2000) examine the role of UK food retailers in a buyer driven global commodity chains. A critical role in defining what is produced, how and by whom is played by large supermarket chains in the U.K. The four largest chains account for nearly three-quarters of all food sales in the UK. They have increasingly developed their own brands in competition with more established names. The largest UK retailers control between seventy and ninety percent of fresh produce imports from Africa. The key driving process in the distribution of activities is the decision of supermarkets to concentrate on core retailing and to look for ways to reduce costs, passing back the risks of procurement, processing and quality to downstream actors in the chain.

Many former supermarket functions, quality control, logistics, storage, distribution, and transport have been pushed back. African exporters now conduct basic tasks such as washing and trimming, and also more technically complicated tasks such as bar coding and labelling. The requirements of UK supermarkets for quality and consistency, reliability of supply, cost, variety, value added and innovation have favoured concentration in a few large firms. Small and medium sized exporters and small growers have been marginalised.

The supermarket chains have focused on retaining a monopoly in areas of high value added and using the pressure of competition and falling terms of trade to institutionalise their capture of surplus.

Regional Trading Arrangements

By contrast to the vertical integration of value chains, regional arrangements are seeking to further the horizontal integration of economies in trade blocs of varying description.

The World Bank has in recent years adopted a more favourable tone with regards regional trade arrangements, endorsing them in eastern and southern Africa. Such endorsement is really of little substance, integration is treated as a means to extend liberalisation to the regional level. This narrow trade focus contrasts with the more ambitious integrationist political agendas of early SADC to reduce dependence on apartheid South Africa or even 1950s vintage EEC to reduce the risk of European war.

There are concerns that trade blocs are seen as part of broader liberalisation. The SADC trade protocol of September 2000 agrees to completely eliminate tariffs and NTB's on intra-SADC trade by 2012. Without harmonisation of external tariffs there is a danger of tariff jumping. Therefore an elaborate system of rules of origin have

¹³ It is not surprising the developed world has moved intellectual property rights to the centre of multilateral trade discussions in recent years.

been developed to overcome this potential problem. Flatters (2001) highlights concern that small high cost producers in the SADC region will be able to gain preferential access to the SADC market on the basis of their national origin. The vision of integration he argues should be directed outwards beyond the region, using inputs from the lowest cost source, or SADC markets will risk becoming irrelevant to the regions exporters.

Regional economic integration and consolidation of production would provide a crucial mechanism for LDC's to avoid exposure to falling terms of trade at the bottom of the value chain. By taking advantage of the fact that (for example) Sub-Saharan Africa collectively supplies a significant proportion of world production in a number of commodities. Weeks (1996) challenges the view that endowments in Sub-Saharan Africa are too similar to generate scope for regional trade. There is sufficient variation he argues in per capita incomes, urbanisation, land availability, rainfall conditions and consumption patterns to generate potential gains from integration.

Integration would also allow LDC's to exert bargaining influence in multilateral organisations, to donors and FDI. Without co-operation investors are better able to extract concessions on taxes, labour regulations and subsidies. Such tax competition may eventually lead to the burden of taxation being shifted to immobile factors (unskilled labour) as economies compete to host mobile (capital and skilled labour) factors. Nolan (2001) notes the emerging political response to the 1997 Asian crisis can be interpreted in these terms. As ASEAN creates its own free trade area there may also be greater space for more extensive co-operation on financial and industrial policy, crucially including cross-border mergers and acquisitions. A regionally based and integrated East Asia would provide a significant commercial challenge to the dominant corporations from the developed world. A sign of the times was the announcement in August 2000 of greater co-operation between POSCO (South Korea) and Nippon Steel (Japan)¹⁴, including cross-ownership to help prevent hostile take-overs, pooling resources in R+D, and co-operation in joint ventures overseas.

Regional integration, consolidation and trade offer developing countries the opportunity to avoid the strangulation of value chains and a,

“...Malthusian closure of globalisation in which the openness of economies drives real wages to the rate of subsistence in much of the global economy. Particularly in those economies concentrating on the realisation of comparative advantage through specialisation in labour intensive commodities. A race to the bottom remains a realistic outcome to globalisation.” (Kaplinsky, 1999, p83).

Conclusion

¹⁴ The two world leaders in steel production.

The analysis of export optimism takes place in a surprising vacuum¹⁵ despite what on the surface appear to be three radically different schools. Uniting all three is the emphasis on domestic reform being necessary to increase the volume of exports. This they argue is both possible and desirable. The fallacy of competition once introduced is not integrated with this analysis and its detractors (the fallacy optimists) quietly drop discussion of domestic policy reform in LDC's when they argue the threat is not a real one. Instead positing a dependence on continued market growth in developed countries. Once co-joined these two debates bare a striking similarity to the questions of competition and accumulation that Marx analysed in the context of the domestic economy. Once considered in this wider context we uncover a new perspective on the issues of value chain analysis and regional integration that is otherwise missed. Perhaps it is premature to term this a 'last sigh', and even not doing the topic justice to think of it in such deflationary terms but a new and contemporary relevance I think it is indeed for the Moor.

“The first sign of this bizarre reassessment appeared in October 1997, when a special issue of the *New Yorker* billed Karl Marx as ‘the next big thinker’, a man with much to teach us about political corruption, monopolisation, alienation and global markets.” (Wheen, 1999, p5).

¹⁵ The contemporary relevance of the fallacy of composition is heightened by the accession of China to the WTO and consequent reduction in constraints on a range of labour intensive exports, notably clothing and textiles.

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