

THE DILEMMA OF DEVELOPING COUNTRIES WISHING TO INDUSTRIALISE, AT A LUNCHEON JOINTLY HOSTED BY THE ASIA SOCIETY, THE FAR EAST AMERICAN BUSINESS COUNCIL AND THE ASEAN-AMERICAN TRADE COUNCIL
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I am greatly honoured by this opportunity to address this distinguished gathering of American businessmen and personalities in this great City of New York. While I am sure that you all know where I am from, Malaysia is not the best-known country in America. Everyone knows Thailand because of the 'King and I'; Singapore because Bob Hope and Bing Crosby took the 'Road to Singapore', Indonesia because you had trouble with Sukarno and the Philippines because you once ruled it. But Malaysia is a new country and has not done those things so loved by the sensationalist western press. Head hunting went out of fashion in the early part of this century and the biggest tree is no longer reserved for the prime minister as his house.

2. Not being known in America is actually a good thing it means that we are peaceful and stable. So I am not unduly worried about Malaysia not being famous although a lot of other Malaysians feel hurt when they are asked whether Malaysia is in China or Africa. So long as the business community knows Malaysia, that is all that really matters.

3. I am not here to publicise Malaysia but to talk about developing countries and the dilemma they are in because they want to industrialise. Malaysia is, of course, such a developing country, and so the subject is relevant to Malaysia. Also whatever I say here is largely based on the Malaysian experience.

4. In the good old days when the world was divided into a number of Empires belonging to European countries and America there existed a division of economic function, albeit forced. The colonies belonging to the European and American powers were given the task of producing raw materials which were then shipped to the metropolitan countries, processed into manufactured goods and sold back to the closed markets that the colonies provided. Of course the raw materials were extracted by entrepreneurs from the colonial powers themselves and sold in the markets in their great cities so as to ensure maximum profits to the colonialists. The colonised people were given sufficient to survive and no more. Having had a good experience in Boston, the colonial powers were

quite adept at ensuring that the kind of tea-party that the Bostonians invented did not find addicts among the colonies.

5. Be that as it may the division of economic functions enabled the economy of the world to function satisfactorily i.e. to the various imperial powers. But then came World War II and the subsequent release of most of the colonies from imperialism. New countries sprouted which did not subscribe to the divisions in economic functions. Some rushed to nationalise imperial enterprises, only to burn their fingers. Lacking expertise and refused access to the markets, the nationalised industries of the newly independent countries soon stopped functioning.

6. But some, and Malaysia is included among these, moved with greater caution. Allowing the former colonial masters to own and operate the industries, they tried to extract more revenue for themselves. If pressure was applied it was mild. Indeed there was even encouragement for new investments. It was realised that if a part of the profit from the old enterprises was ploughed back into the country, there was much to be gained.

7. Among the areas which received encouragement was manufacturing for domestic consumption or import substitution manufacturing. Soon the locals became involved in this kind of manufacturing. As more and more items began to be manufactured locally, pure import substitution became less and less economic. In the first place the domestic market is not big enough for the kind of economies of scale needed. In the second place foreign manufactured products were often dumped on the small local market, knocking out the substitute products.

8. Cheap local raw materials and cheap labour could not overcome the high cost of imported inputs and dumping practices of foreign manufacturers. Protection was sought from the Government. This is a costly burden, for not only will the Government lose revenue from duty on imports but have to subsidise local manufacturing.

9. At this stage Malaysia decided to switch its strategy and go for greater employment opportunities instead. Foreign companies were invited to start labour intensive industries in special free trade zones. To encourage investors tax holidays and other incentives were given. The nett gain for the country's economy was minimal. Certainly the Government got no revenue from the profits of these manufacturing enterprises. This is especially so when the raw materials, machinery etc. were brought in tax-free and the processed products also exported tax-free.

10. The import substitute industries and the labour intensive industries, between them changed the landscape in the newly independent countries. It seems as though they are industrialised countries. In a sense they are. But the benefit to them is minimal. Certainly it is not the same as the benefit obtained by the industrialised nations.

11. There emerged at about this time a new phenomenon. South Korea, Taiwan, Hong Kong and Brazil took rather bold steps into industrialisation. They disregarded the domestic market but concentrated on exports. Starting with garments, which they frequently manufacture under buyers labels, they were able to penetrate the huge markets in the industrialised countries. Encouraged by their success they moved into textiles, toys and other relatively simple consumer items. Soon they were moving into heavy machinery, ships and even manufacturing plants.

12. Growth was rapid. Suddenly they and their products were everywhere. They were successfully competing with similar goods from the old industrialised countries not only in the world market but in the domestic market of the industrialised countries themselves.

13. What was happening did not go unnoticed in the developed countries. Having seen Japan's economic miracle, fear was expressed that the developing countries would become little Japans, flooding the world markets with competitive products and displacing the traditional suppliers of manufactured goods. As the first move towards discrimination, the successful industrialising countries were named Newly Industrialising Countries or NICs and classified as dangerous threats. The Japanese had long since ceased to be funny bespectacled pedallars of inferior goods. Now the NICs have come and they cannot be laughed into oblivion.

14. Europe had already formed into a common market perhaps the most uneconomic of economic schemes. In this economic community, butter sells at 5 times the world price, beef at twice the average price and grains at 1.5 to 2 times the world price. Off and on mountains of butter and beef piled up while millions starved in other parts of the globe.

15. America was at first quite sanguine. But it soon realised the threat. America's answer was voluntary quotas principally against the Japanese but without doubt if the NICs have the temerity to threaten the American manufacturers, they too will be asked to volunteer cutbacks in their exports to America. When recession came the clamour went up for outright protectionism.

16. For the other developing countries the successful industrialisation of the NICs was an inspiration. It would seem that competition with goods of the established industrialised countries was possible. Provided they go in a big way into manufacturing, their cheaper labour and raw materials might give them sufficient comparative advantage. But then, to their dismay they see the doors to the most lucrative markets being closed before they even have a chance to knock and ask to be allowed in. This is their dilemma. Obviously they can industrialise but if they do so they will be ostracised.

17. Malaysia is facing this dilemma. We are convinced we can industrialise. We have the raw materials, the energy and the man-power. The domestic market cannot support an extensive manufacturing programme. To manufacture we must have access to the world market. But we see the access being denied even before we embark on the modest industrialisation programme we have drawn up.

18. Many developing countries need aid but a substantial number, and Malaysia is one of them, do not care for aid. They want trade, fair trade. Producing primary commodities is fine. A substantial amount of foreign exchange can be earned that way. But a rapidly growing population cannot possibly find employment in just the production of raw materials. Manufacturing employs more people and can grow more rapidly. The amount of tin that can be mined is limited. The number of trees that can be chopped down is also limited and so is the acreage that can be planted with rubber or oil palm or cocoa. Manufactured goods on the other hand can create their own market. Ten years ago there was no market for video-tape players, today the market is worth billions of dollars.

19. Besides, the raw material market is a manipulated market. Between the managed commodity markets in the developed countries which are sometimes not averse to selling stolen products and the threats posed by stockpiles, it is all a raw material producer can do to survive. There is no choice for the developing countries but to exploit their low labour cost and available raw materials and go into manufacturing.

20. If possible they would like to be like Korea or Taiwan or Brazil. But if not, they would like to have a piece of the action. In the case of Malaysia, we have decided to add value to our raw materials before exports. This is not easily done. Only palm oil offers this kind of opportunity. But immediately we run up against a road-block.

21. The EEC imposes a 4% tax on refined palm oil and none on crude. So if we try to add value through refining we may be uncompetitive. In fact on

the average the import duty imposed by the industrialised countries on unprocessed raw materials is 3%. This rises sharply to over 20% at the next stage of processing. What this means to the developing countries is clear from a World Bank estimate that a 15% across the board tariff increase on raw materials could lead to a 3 to 3.5% decrease in the national income of the developing countries. Of course the developed countries too have to pay a price as they are forced to consume their own high-cost produce.

22. Preventing the developing countries from industrialising is not doing anyone any good. Everyone is forced to pay high prices when there is an abundance of everything. It is ridiculous to force people to pay a high price merely because you want to maintain a production facility that is no longer economic. Perhaps there are strategic considerations in the production of butter in Europe or rubber shoes in Sweden. But the developing countries are not convinced. To them it looks like selfish vested interests having their way.

23. The developing countries must industrialise each in his own way and in his own area as determined by comparative advantage. They will not all achieve what Korea, or Taiwan or Hong Kong or Singapore or Brazil have achieved. But industrialise they will, limited though the exercise may be.

24. For Malaysia coping with this dilemma is something that we have accepted. We have gone in rapid succession through the different phases from manufacturing import substitutes to labour intensive industries and on to processing of our raw materials. Now we want to go into heavy industries and the production of small engines and motor cars. Some people think we are being quixotic. That is left to be seen.

25. For the other developing countries the choice will be more difficult. There are too many countries already ahead of them other than the established manufacturing countries of Europe and America. While the first few NICs had a more accessible market when they started, the newcomers will be faced with protectionism, quotas and all-round hostility when they venture forth. Yet what choice have they? A growing population, better communication and knowledge of the developments going on elsewhere in the world, better education and rising expectations demand that the developing countries move away from being mere producers of raw materials. On the other hand if they industrialise they are going to be faced with horrendous problems. This is their dilemma.

26. I hope I have succeeded a little in explaining the dilemma of the Newly Industrialising Countries. Their cry for a place in the sun should not

go unheeded. The developed world will not lose by understanding the problem. The developed world will not lose if the developing countries industrialise. No matter how much they try, these countries will be at least 20 years behind the developed world in industry. In these days when technology advances so rapidly, 20 years is a long time. The NICs are never ever going to displace you. They may in a few unsophisticated areas and this will be to the good. But on the whole they are going to remain relatively backward.

27. The dilemma facing them is real. It is an economic dilemma. We should not allow that dilemma to be solved politically, especially by people with rather dubious credentials. The fate of Kampuchea, Afghanistan and the Central American republics should not be allowed to fall on countries which are sincerely struggling to remain a part of the free market system.

Thank You.