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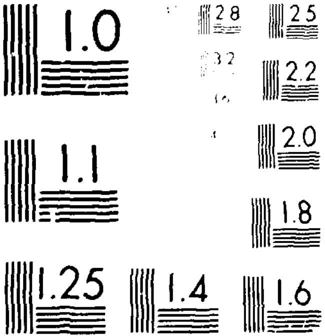
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ISSUE III

FORMS AND CONDITIONS
OF
INTERNATIONAL CO-OPERATION
INCLUDING
LONG-TERM ARRANGEMENTS BETWEEN
DEVELOPED AND DEVELOPING COUNTRIES
AND AMONG DEVELOPING COUNTRIES
FOR
CAPITAL GOODS PRODUCTION *

Prepared by the Secretariat of UNIDO

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1. <u>Introduction</u>:-

This paper aims at presenting to the Consultation, for its consideration, certain important issues on international co-operation and long-term arrangements for the capital goods industry

For example -

- the role of long-term arrangements in international co-operation and the conditions required for adopting and implementing the concept of a New International Division of Labour in capital goods based on "mutuality of economic interest between the developing and developed countries";
- types of capital goods that are potentially suitable for such long-term arrangements;
- special emphasis to be placed on the involvement of the least developed countries in such long-term arrangements for international co-operation.

2. <u>Importance of the capital goods industry</u>

The capital goods industry occupies a pivotal position in the movement towards world industrialization and in the establishment of a new international economic order.

For the developing countries, it is the main catalyst in the economic and industrial development process and in their efforts to achieve technological advancement.

The dynamism of capital goods development - with some developing countries already well advanced in the field and others moving into it - may help the developing countries to increase their share in capital goods production, in terms of value added, from 6% in 1976 A.D. to about 16% to 18% in 2000 A.D.

3. Government participation

In the case of developed countries, the capital goods industry is the key sector for industrial restructuring, with the governments of these countries becoming increasingly involved in the industry and influencing its development through direct and indirect intervention.

There is already a very long history of government participation in industrial activities in these countries, but two new trends have emerged in recent years.[1/] OECD governments have in various ways assumed a growing involvement in advanced technological activities. Furthermore, to prevent certain traditional industries from declining too rapidly, some governments have intervened in these industries. They have also not hesitated to take action to assist industries which have been "taken ill" but are too important to be allowed to "die".

4. Interdependence of the developing and developed countries

There is an increasing appreciation of the concept of "mutuality" of economic interest between the developing and developed countries".

Interdependence takes many forms - political, cultural, economic, etc. Economic interdependence has a special significance in the process of international co-operation.

The developing countries are striving, through a process of development, to move out of an era of dependence into one of equitable interdependence with the developed countries.

From the point of view of the developed countries, capital goods development in the developing countries can be an "engine of growth" having beneficial effects on their own industries.[2/] It will continue to provide the developed countries with a market for their capital goods exports. This is borne out by the fact that newly industrializing countries (NIC) capital goods imports rose from $7.1 billion in 1970 to $18.6 billion in 1977.[3/] The emergence of the developing

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1/ OECD Interfutures "Facing the future", 1979

2/ Report - Brandt Commission - Dec. 1979

3/ OECD Report "The Impact of the Newly Industrializing Countries on Production and Trade in Manufactures", Paris, 1979 countries as manufacturers of capital goods is not likely to pose any serious threat to the developed countries' economies. According to the forecast in the World Bank Report of 1979, developing countries' exports to the developed countries by 1990 may cover only about 5% of the developed countries' needs.

The developing countries are already heavily in debt to the developed countries. In the coming years, faced with problems of financial constraints, efforts to industrialize will tend further to increase these debts.

5. <u>Absence of long-term arrangements for promoting interdependency</u>

Mutuality of economic interest envisages a partnership between the developing and developed countries for a long enough period to ensure benefits from such a relationship accruing to both sides. In actual practice, however, arrangements in several cases are for short periods, and are on an <u>ad hoc</u> basis or take the form of a "one-time-buy arrangement". Such arrangements tend to ignore the long-term perspective that should guide both the developed and developing countries in their capital goods programmes.

There may be some exceptions:-

Some intergovernmental agreements ensure that the long-term perspective is kept in view, particularly when there is the possibility of linking supply of equipment with the import of strategic raw materials.

Then there are enterprises and industries in the market economy countries which are promoting capital goods development in the developing countries through their subsidiaries. While doing so they are keeping a long-term objective in sight.

The developing countries hope that their capital goods development programmes, promoted through the international division of labour, should not only help in generating self reliance, but also ensure movement from a lower technological level to a higher one. Such an objective may not always be in consonance with the goals of the foreign companies which have invested in the developing countries. The policies of these companies (e.g. transnational corporations) may not encourage such movement to higher levels. This problem arises because of the absence of a policy promoting interdependence through long-term arrangements.

6. Advantages of long-term arrangements

Agreements based on long-term arrangements help to promote "mutual economic interest" of all the partners concerned.

For the developed countries:

- in the present situation of uncertainty, and given the stresses and strains related to the economy, such long-term arrangements would help to introduce some stability into the system;

- they would help the developed countries interested in restructuring their capital goods industry to implement their schemes in a more purposeful and durable manner;

- such an arrangement would be more beneficial than a single transaction involving equipment or technology and would enable them to have permanent and ever greater access to the markets in developing countries.

For the developing countries:

- it would help the industries become established in line with the countries' long-term industrial and economic development plans; and it would enable better absorption and assimilation of imported technology into the indigenous system;

- if co-operation between the two sides involves direct foreign investment or setting up subsidiaries, the long-term arrangement would help the developing country to ensure that the operation of these companies and the policies they follow are in line with national economic and social objectives;

- import of equipment and external finance for capital goods projects may often involve repayment through a trade or "production compensation" arrangement. This may extend over several years, thus necessarily implying partnership on a long-term basis;

- in the implementation of the projects, problems relating to contractual terms like performance guarantees, developmental damage, arbitration clauses, etc. might arise. A long-term arrangement could ensure satisfactory implementation of the contract and thereby foster a healthy relationship between the two sides.

7. Increasing imports and national debt

Developing countries are faced with a complex situation:-

Their national objectives call for rapid industrialization. This would necessitate massive imports of capital goods from the developed countries.

But imports need foreign exchange support - not an easy commodity for most developing countries to find.

Substantial internal resources are needed for infrastructure development, without which industry cannot be established and thrive, and these resources too are limited.

National debt may be very heavy. With additional borrowing for the capital goods programme, the situation could become worse, and doubts may arise about the country's creditworthiness and ability to repay the debt.

How then do the developing countries proceed in order to overcome these apparent incompatibilities and gather resources for their programmes? By increasing aid or through concessional credit? Through trade agreements - perhaps linked to the concept of "production compensation"?

All these issues point towards establishing a dialogue with the developed countries to elaborate a programme of mutual interest and interdependence.

8. Restructuring of the capital goods industry[4/]

This restructuring process leading to the development of the capital goods industry in the developing countries is likely to continue in the next decade, although perhaps at a slower rate.

4/ OECD Interfutures report, op. cit. 1

Transfer may take place either through product manufacture or through standardized production processes, but this is no doubt only an intermediate stage. The developing countries, though gaining from such transfers, are not likely to offer much competition to the developed countries, which have two distinct advantages: technological innovation making more extensive use of automation; and the manufacture of products very closely linked to market characteristics.

Activities requiring high technological capacity will for obvious reasons be increasingly concentrated in the developed countries. Straightforward products or activities involving high manpower costs can be transferred, as in the past, to most of the developing countries. Intermediate level countries which already have a domestic market and some technological capacity could take up a more or less independent development of production and even design for mass consumption products.

9. Role of small and medium-scale industries[5/]

In the restructuring process, the role of small and medium-scale industries will be of particular importance. These industries

- are not a second rate substitute for large-scale production units, and do not have a less developed technological potential; and
- are a complementary - and perhaps less troublesome - means of access for developing countries to capital goods technology.

10. Need for international co-operation based on long-term arrangements

The dynamism of the development process therefore leads us to conclude that a co-operation based on long-term arrangements will bring lasting benefits to both parties and will help to promote rapid and balanced growth of the capital goods industry by:

- enabling the developed countries to find common ground between their concept of "industrial restructuring" and the hopes and aspirations of the developing countries;

5/ UNCTAD Report "Role of Small and Medium Sized Enterprises in International Transfer of Technology", Geneva, 1980

- ensuring that due emphasis is placed on the growth of small and medium-scale industries and financial institutions which can play a vital role in the establishment, development and expansion of the capital goods industry;
- enabling the developed countries to give special attention to the development programmes of the least developed countries, e.g."Lagos Plan of Action" for the African States, with a view to integrating co-operation in capital goods development with these programmes;
- taking a long-term view and thus helping to reduce the "uncertainties" faced by some of the industries in the developed countries;[6/] and
- helping the developing countries to achieve their objective of reducing the imbalance between them and the developed countries.

11. Forms and conditions of long-term arrangements

The forms and conditions for such arrangements can be widely divergent and will depend upon several factors.

Based on their levels of development and their national strategy, groups of countries like the newly industrializing countries, countries with an embryonic industrial base or the least developed countries may require different forms of long-term arrangement. A broad categorization of these forms could be -

(a) with a developed country (market economy);

(b) with a developed country (planned economy);

(c) with a developed country plus a more developed developing country;

(d) amongst the developing countries;

(e) with a financially affluent developing country;

(f) regional, sub-regional or inter-regional.

6/ Report of the French "Federation of Mechanical and Metal Processing Industries" (FIMTC) "Prospects 1980 - 1990"

These forms may be intergovernmental, inter-company or between an enterprise and a government. They may involve direct financial investment, the establishment of subsidiaries, turn-key projects or sale of equipment and technology linked with trade and financing, or cover training programmes and supply of experts etc.

The terms of such arrangements may also vary depending upon the choice of projects, the country's technological level, infrastructure availability, financial resources/national debt, market demand, trade relationship etc.

12. Conclusions

Two of the important questions to be considered by the Consultation are therefore as follows:

(i) what should be the content and scope of bilateral, multilateral, regional, and sub-regional long-term arrangements between the developed and the developing countries and amongst the developing countries?

(ii) in what ways can the international community assist the least developed countries in their efforts to enter into the capital goods sector?