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*for a sustainable future*

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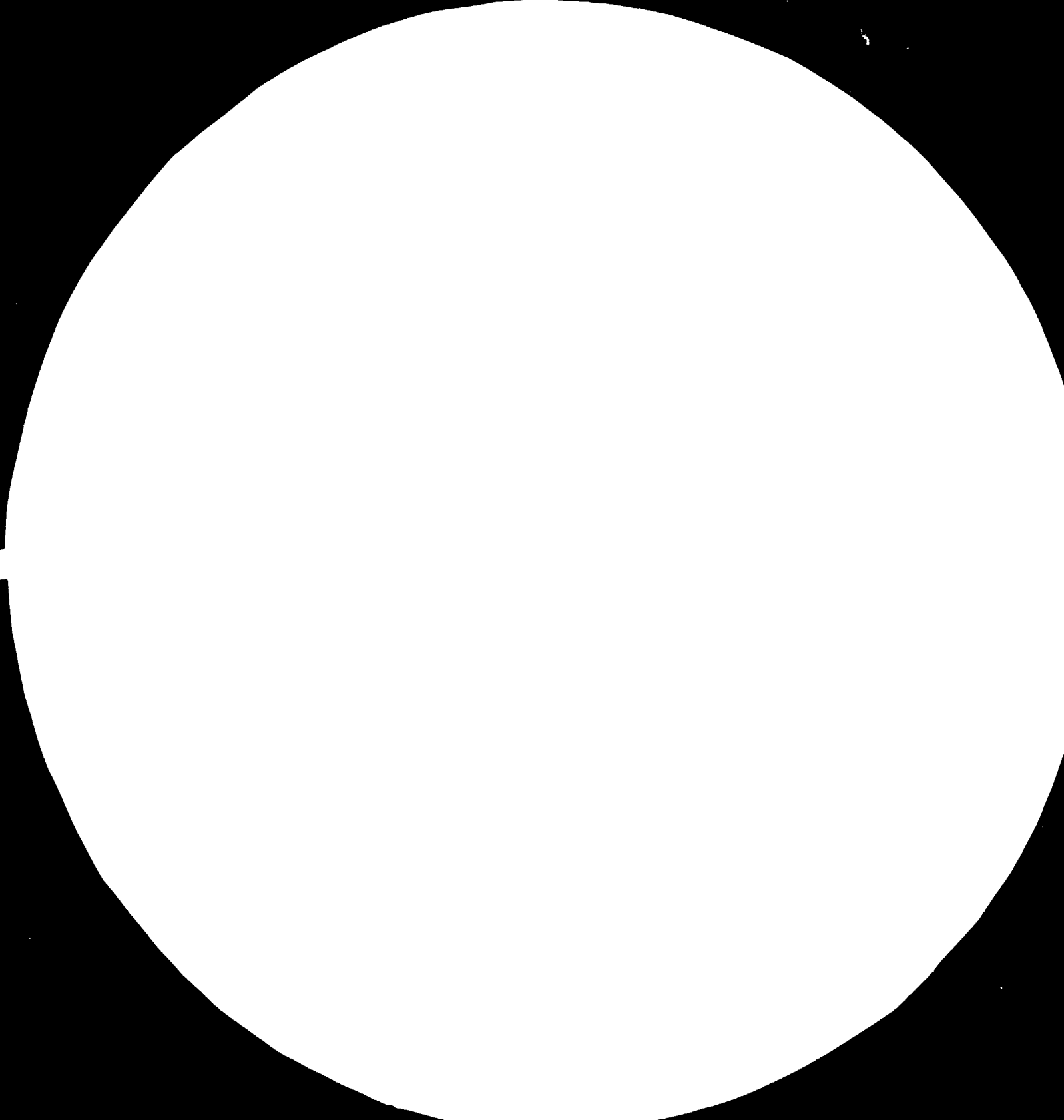
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MICROCOPY RESOLUTION TEST CHART

NATIONAL BUREAU OF STANDARDS-1963-A

UNIDO

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Stockholm School of Economics  
Oct 26, 1963

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[ Industrial restructuring in Thailand ]

Economic growth is change. It implies changes in the industrial structure. These changes are wanted as growth is sought after but they need not be painless.

However, "industrial restructuring" to have any operative significance means something else than just accepting and accomodating the changes of growth. Restructuring as an explicit aim is called for, if an economy has travelled the wrong way with a misallocation of resources as a result and special measures are called for to bring about adjustment.

There can be two reasons for such a situation to have arisen. There can have been changes in supply and demand conditions on international markets calling for output adjustments in the domestic economy. Or, internal policy interventions may have given a distorted and inefficient output mix. These two causes of adjustment needs often coexist in that domestic policies creating distortions often have their initial explanation in a wish among policy makers to shield a country from adjustment requirements arising from changes on the international level. In this way a back-log of adjustment needs is accumulated. For instance, inept policy responses to the energy price increases have in many countries given rise to such a back-log.

Indeed, baring major international disruptions, the flexibility of an economy permitted to absorb change is enough for a specific restructuring program not to appear necessary. It is when domestic policy measures reduce adaptability and when they in themselves create domestic distortions that eventually a need for industrial restructuring is perceived.

Thai economic performance deteriorated during the seventies. Unfavorable external conditions reduced the growth rate. A further reduction was caused by efforts to avoid adjustment to external change and by some inappropriate policies to promote industry. Industrial protection increased, contradictory investment incentives were applied, large-scale capital investment projects received Government subsidies, and unintentionally policies worked to the disadvantage of regional balance.

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These problems have been addressed in the Fifth five year plan. The plan calls for a more outward oriented strategy with reductions in

protection and a rationalization of promotional policies.

Restructuring can hardly take place through reallocation of resources in the literal sense of the word. If not physically impossible a reallocation is from political view-points extremely difficult to bring about. Instead, the restructuring must take place as part of the changes which economic growth under all circumstances entails. With growth it is easier to accommodate the pains which restructuring causes. It is from this point of view fortunate that restructuring policies adopted in the Plan would also contribute to a higher growth rate through more efficient use of future resources.

In spite of this and in spite of the considerable efforts made when the plan was being worked out and when it was presented for adoption to secure necessary political support, its implementation has proceeded more slowly than intended. Given the thinking and the political pressures which in the first place have resulted in a need for restructuring, it should not come as a surprise that there are obstacles to the new policies. Indeed, the vested interests created by faulty domestic policies have increased the political pressures for protection and subsidy.

Nonetheless, it is imperative that the plan strategy is permitted to be executed. Otherwise, even those who now profit from the rents of protection and subsidy and from the powers of regulatory interventions will in the long run stand to lose through a deterioration in the over-all performance of the economy. Yet, they may not easily be persuaded to give up their present favors. In spite of this, what was clearly seen when systematic work was made on strategy must not be lost in the tactics of day to day politics.

The plan strategy has not been proven wrong. The particular kind of obstacles plan implementation has run into, i e various vested interests, indicate through their existence that the measures set out in the plan are called for.

The major task ahead is to stay with the convictions which have inspired the plan and to use available empirical material to educate in order to increase popular and political support for the plan strategy and to overcome vested interests. This, as I read it, rather than the writing of ever finer and more detailed industry studies is what Thai industrial restructuring is all about in its present phase. Studies which help to make the basic case are surely much in need. Studies which go into the specifics of this and that industry may not be so helpful. If plan momentum is lost, they will be irrelevant. If plan implementation continues, well then the very idea is that more of structuring decisions will be left to the markets and to the private sector. I am not arguing that back-up studies for ministries and agencies are not required for their policy decisions. The case I am making is that, in order not to do unproductive or counter-productive intellectual work, great care has to be taken in deciding what studies are required and which are not.

Again: the thinking behind the plan has not been disproved. If

anything it has during the last few years been given additional support from additional experience.

All successful developing countries have relied on an outward looking, trade oriented market strategy. They have managed to secure the benefits set out in international trade theory. It has also become increasingly clear that they have benefitted from the improved feed-back and the increased discipline of responding to it which contact with international markets have given. This mechanism is not well incorporated in trade theory, although surely not contradictory to it.

There are countries which have tried to rely on this kind of strategy and not done so well. There is, indeed, no guarantee of success in adopting this development. For one thing it is, as we can see also from the mismanagement in many of the developed countries, easy to go wrong in other aspects of economic policy most notably in macro-economic stabilization policy. An outward looking strategy is no guarantee of success. But, if it is not a sufficient condition for sustained and rapid growth, it seems to be a necessary condition. No country trying to do it alone has succeeded. Poor performance in many of these countries also seems to have enticed the authorities to use the centralized planning powers for purposes they were not originally intended for.

The trade oriented strategy has proved to be advantageous even during the turbulence of the last years of oil-price shocks, recession, and protectionism. The market system has permitted a greater, much needed flexibility. Furthermore, far-reaching import substitution has left such countries in a position of extreme dependence on the remaining imports for operating the production apparatus. A rapid terms of trade deterioration, for instance in the form of dramatic oil price increases, has left the economy without the means of obtaining essential imports. The need for flexibility has then become impossibly high at the same time as the capacity to adjust has been made uncomfortably low.

Empirical studies also show that there has not yet at least been cause for an export pessimism. The examples of the newly industrializing countries can be repeated, as well as these countries are on the way of repeating the example of Japan for long thought to be unique. A group of developing countries, and Thailand being one of them, have during recent years been experiencing a faster growth of manufactured exports than have the newly industrializing countries! This growth has taken place from a low base which means that impressive percentages need not stand for so much in absolute terms. Yet, the performance should not be written off for that reason as the first steps on the world markets of manufactured goods may be the most difficult ones.

The trade engine of growth is not just, as is sometimes argued, propelled by a growing aggregate demand in the developed countries creating a demand for the exports of the developing countries. Studies again show that price elasticities are such that even during periods of low or no growth it has been possible to expand exports through

substitution.

These points should be made to overcome "export pessimism". Recession and protectionism in the developed countries are problems but they can be overcome. Experience from a number of developing countries show this. Changes of a very different kind in the developed countries - for instance fast technological progress or increases in export subsidies - are also often given presently as reasons for writing down a trade oriented development strategy. Again such phenomena may cause difficulties. Yet, what they call for is flexibility. Trade opportunities do not disappear, but they change. It is interesting to note that in many developed countries a popular argument is that competition from the so-called "low-cost" countries cannot be met. And it is difficult - in certain industries. Flexibility and adjustment is needed.

For Thailand as for other developing countries - and developed countries - it is difficult to operate on world markets. But trade also gives advantages whereas operating in isolation from international markets only gives problems. Those who enumerate present difficulties rarely provide an alternative strategy. And those who listed "present difficulties" twenty years ago were also numerous. Yet, some countries have done it and have done it well and continue to do it. (The value of HongKong exports for the first nine months of this year has just been reported to be up by 30 per cent.)

To bring about the industrial restructuring that is required industrial and export promotion policies can be enlisted. They must be worked out so that they are in harmony. It is unnecessarily cumbersome to have export promotion policies the main objective of which it is to try to compensate for some anti-trade biases in industrial policies. Such anti-trade biases should be removed. Trade promotion can then be added to try to assist firms in their efforts to overcome certain difficulties in entering world markets.

To bring industrial policies and export promotion in correspondence it may be considered to combine them in one agency. There are certain attractions in such an institutional rearrangement. However, to avoid having agencies of an unwieldy size and to avoid institutional surgery that may give scars, the necessary coordination should be obtained through appropriate guide-lines.

One institutional change that could well be made, however, is to upgrade the political standing of the export promotion agency. This should facilitate a reorientation of the philosophy of the industrial policy agencies to a more trade oriented approach. Furthermore, it could set the priorities of the plan strategy more in popular focus and give business an impetus and exporting activities a higher social standing. One may even contemplate copying the Korean regular and frequent export promotion meetings between industry and Government presided over by the Head of State. To succeed on world markets is a question of competitiveness but competitiveness is not a question only of price and quality but also of enthusiasm and perseverance. The sociology of this should not be overlooked.

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Promotional policies have their risks. They easily become counter-productive. What goes under the name of "industrial policy" is not necessarily good for industry. Industrial policy is presently much in vogue in some of the developed countries. Its attractiveness, however, often seems to be that, somehow, it should in this way be possible to avoid hard decisions. The same risks exist in developing countries. It must be understood - but often it is not - that industrial policy is no substitute for good macro-economic policy resulting in economic balance and good basic growth conditions. Nor can export promotion ever succeed if the economy is not competitive and exchange rates have become unrealistic.

The promotional policies must be general in their nature. Otherwise they come in conflict with the basic development strategy of market and outward orientation. Complex discretionary policies have a bias against small scale business. Small business does not have the capacity to stay informed about rules and regulations and subsidy opportunities. Nor does it have the time to solicit favours in the corridors of power; and the bureaucrats do not have the time to see them all. Big companies are in this way favored at the expense of small firms but the history of economic growth shows that progress is borne by small and medium-sized firms growing. For very similar reasons complex policies work against firms outside the capital city. Business men there are put at a disadvantage as they have greater costs of being in contact with the centers of power. Complex policies also tend to yield capital intensive projects rather than labor intensive.

Industrial policy must be transparent. Otherwise business uncertainty increases in a detrimental way. It is one thing to try to cope with market uncertainties. It is another to try to handle the uncertainties of discretionary industrial policies which imply frequent changes in the rules of the game. Adjustment to changing market conditions is difficult but it appears more acceptable as it is a condition of efficiency in the allocation of resources. Adjustment to what often may appear as capricious governmental decisions is more taxing. As windfall profits - and losses - from government decisions can exceed what can be obtained on the market, management resources will be diverted from the running of company affairs to the running of government relations. This system also carries with it risks of corruption.

Industrial policy must create a good industrial infrastructure: labor training, engineering schools, research and testing facilities, quality control standards, patent office, a system for transfer of technologies, clear rules for foreign investment, a tax system which does not destroy incentives and which does not set up the wrong sort of competition from smuggling or from a "grey" production system outside of government control; and so on.

These are the tasks: to create a fertile soil; not to try to pick winners by extensive tariff and subsidy schemes. Government is organized to shape a political process. It is not organized to take



business decisions. These decisions must be taken where the particular expertise can exist and where the economic responsibilities rest for the decisions in question. In virtually every country state owned business enterprises have a bad record. It has for political reasons proved difficult to take the hard decisions necessary. Similarly, studies show that Governments have been poor pickers of winners in the industrial race.

Indeed, certain studies show that, on the whole, Governments have picked losers rather than winners. Or, perhaps better, potential winners have often become losers when interventionistic policies have distorted the decision making process.

To the extent Government wants to single out industries for special support, be it through tariffs or subsidies, it must be clearly understood that it is in this way only possible to support a limited number of industries. It is not possible to support all through protection because support to one will raise costs for the others which use the services of the protected industry. If tariffs are high on steel imports, this will raise the cost level of the engineering industry. High tariffs on machinery will hurt consumer goods industries using the machines. Extreme protection of an automotive industry makes the tourist industry less competitive and all other industries using transport services. And so on. It is possible to close off trade altogether but this will not help everyone. It will be harmful to the potential export industries and also to those industries which lose markets from the decline in incomes associated with such an isolationist trade policy. These observations are elementary but nonetheless often overlooked.

Similarly, subsidies to one industry hurt other industries as the subsidies must be paid for by taxes, taxes which will end up as burdens on economic activity.

Governments to give direction and stimulus to a solid development effort must have strength. They must be powerful. But a powerful Government is a Government that knows not to try to decide everything but use efficient mechanisms to decentralize decision making. In this way Government can concentrate on the crucial functions. A Government exercising powers to do everything is not powerful: it is bogged down with an agenda problem and fierce inter-departmental and inter-agency strifes and contradictory policies and saddled with a weak economy.

To stimulate efficiency and development the Fifth Five Year Plan adopts a outward trade-oriented strategy. This implies a lowering of trade obstacles and a stream-lining of tariff structures. This deregulation is attempted because it serves Thailand and not because it would fit into some sort of international code of behavior. However, there is also such a code laid down in the GATT. The members there assume certain obligations in order to secure for themselves certain rights. The obligations are to apply most favored nation treatment to other members, to abstain from the use of certain particularly harmful trade obstacles, and to participate in international efforts to bring about a general lowering of trade


obstacles. These obligations should not be looked upon as a burden in the sense of something a country would undertake to do only to get other countries to do the same. It is not a burden as it pays a country under all circumstances to have a liberal trade regime. In line with this analysis the Fifth plan sets out a new trade policy irrespective of what other countries are doing. Yet, it is an added advantage, if other countries have the same ambitions. The GATT serves the purpose then of making it additionally attractive for any one country to have liberal trade policies. The GATT brings together countries in a framework of mutual undertakings.

Thailand has recently joined GATT. The majority of developing countries have long been members. However, these countries have really not been parts of the GATT system. They have tried to use the GATT machinery parallelly with UNCTAD to secure a special treatment hopefully resulting in special advantages. However, by opting out of any obligations they have made it too easy for the developed countries to opt out of their obligations. The developed countries have made certain concessions to the developing countries, e g preferences, but having done that they have not hesitated to absent themselves from important and central undertakings in GATT.

If GATT membership shall prove to be valuable to Thailand, the country must try to join not just in name. To join in practice does not mean a wholesale scrapping of import obstacles. It means the imposition of certain rules in trade policy but the assumption of these makes it possible to ask for a better treatment by the advanced countries. A price could be extracted for tariff reductions which Thailand wants to undertake anyhow. It would become more difficult for other countries to impose high-handed trade obstacles on Thailand. The relatively weak countries have more to lose than the strong countries, if power rather than law is allowed to rule on the international trade stage. Considering the intensity of present protectionist sentiments these considerations should not be overlooked.

Indeed, these sentiments may be so wide-spread that isolated Thai activities in the GATT along these lines may not give much results. Under all circumstances it would be useful for Thailand to seek cooperation with other countries to get more muscles in international trade policy. By spending their energies on many irrelevancies in the North-South dialogue the South has not managed to secure more important market access assurances. If, for instance, the ASEAN countries would participate in GATT activities so that they would get more than a moral case to refer developed countries to and then combined forces to penalize those countries that discriminated against them, they could achieve considerable results. There is surely a loss of income in those developed countries which apply quotas on textile imports but that cost is not so easy to make visible in the domestic political processes where battles over trade policies are being fought. If, on the other hand, a concerted behavior by an important group of countries made it very clear that particular restrictive measures would bring with them retaliatory measures, for instance in Government procurement policies, this group of countries would get important allies among exporters in the developed countries.

In such a way ASEAN could get an important new role in the complexities and dangers of current international trade policies. This role is in line with keeping ASEAN on an outward looking integration course. If ASEAN instead tries to meet international protectionism by inward looking integration behind high trade obstacles, the centrifugal forces of costly trade diversion would soon break the group apart.

By a reorientation of its GATT policies and through cooperation Thailand and ASEAN could gain an important initiative and leadership much needed on the international stage presently. Increasing strength of South East Asia could make such an effort possible. Its chances of success are enhanced by the likelihood that it should prove possible to make the many other successful Asia Pacific countries join in this great  effort.

