To the Graduate Council:

I am submitting herewith a dissertation written by Baban Hasnat entitled "Patterns of Trade and Payment: South and Southeast Asian Countries, 1970-1985." I have examined the final copy of this dissertation for form and content and recommend that it be accepted in partial fulfillment of the requirements for the degree of Doctor of Philosophy, with a major in Economics.

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South and Southeast Asian Countries,

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A Dissertation

Presented for the

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Degree

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Baban Hasnat

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To My Family

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ABSTRACT

This study analyzes the patterns of trade and payment of eight South and Southeast Asian countries--Bangladesh, Burma, India, Malaysia, Pakistan, the Philippines, Sri Lanka, and Thailand--during 1970-1980. The study examines (i) the structure of merchandise trade and transfer and services accounts, (ii) the nature, magnitude, and causes of external payments problems, and (iii) the policy reaction of the countries in response to these problems.

The study finds significant structural changes in the commodity composition and the direction of trade for our countries over the study period. Manufacturing exports, particularly the "other manufactured goods" category--which includes the cotton and textile products--increased significantly for all countries. On the import side, capital and intermediate goods imports increased substantially. While the developed countries are still the major trade partners, newly industrializing and oil-exporting countries of the Middle East have become important trade partners for our countries. The structure of the services account is unfavorable for our countries, although one component of it--the travel account--indicates an encouraging trend. South Asian countries also experienced a large inflow of remittance earnings from the oil-exporting countries of the Middle East.

Except for Malaysia, balance of payments deficits are a regular feature for our countries and the magnitude of the problem is

large in most cases. There is some association between the trade orientation and the external deficits of our countries: strongly inwardly oriented countries have more deficits than strongly outwardly oriented countries.

The main causes of the external payment problems are evaluated. Three external factors (terms of trade, economic growth in industrial countries, and real interest rates in the international market) and two internal factors (real effective exchange rates and fiscal position) are analyzed. The study finds that both external and internal factors are responsible for the payments imbalance.

Regression analyses are also used to examine the determinants of balance of payments problems. Reduced form models are estimated with current account deficits as the dependent variable and the external and internal variables as discussed above as the independent variables. Poor results are obtained from both time series study of the individual countries and pooled cross-section and time-series study of the groups of countries.

The policy responses of the countries are also analyzed. It is found that the current account deficits are mainly financed through external borrowing, in particular, through official development assistance. Exchange rates, trade policies, or slowing down of domestic economic growth played minor roles.

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CHAPTER I

THE PROBLEM

In the process of economic development, effective management of the balance of payments (BOP) is crucially important. Economic development is often obstructed and is even perverted if the BOP problem is not overcome: "an adverse balance of payments is at the same time a dangerous symptom and itself a menace to economic stability. It is a symptom because it is an effect of economic weakness; a menace because it engenders tendencies which if left unchecked may culminate in a state of economic breakdown."[1] On the other hand, development efforts and the higher level of economic activity that accompanies them facilitate the BOP adjustment process. Many economic polices at the present time (foreign exchange policies, the use of tariffs, quotas, and other non-tariff barriers, the management of international reserves) are largely founded upon BOP considerations.

The purpose of this study is to examine the underlying patterns in the BOP experiences of a selection of developing countries in recent years. An effort is made to disentangle quantitative relationships among the BOP problems, economic policies

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[1]Ralph G. Hawtrey, The Balance of Payments and the Standard of Living (London: Royal Institute of International Affair, 1950), p. 9.

and adjustment experiences of eight developing countries of South and Southeast Asia: Bangladesh, Burma, India, Malaysia, Pakistan, the Philippines, Sri Lanka, and Thailand. Among these countries Bangladesh, Burma, India, Pakistan, and Sri Lanka belong to the South Asian region and Malaysia, the Philippines, and Thailand belong to the Southeast Asian region, the classification scheme followed by the United Nations Conference on Trade and Development (UNCTAD).[2] Together these countries have a population of over a billion. Within the group, per capita gross national product (GNP) varies from as low as $150 in Bangladesh to as high as $2000 in Malaysia (Table I-1).[3]

The South and Southeast Asian countries not included in the analysis are: Afghanistan, Bhutan, Brunei, Indonesia, Kampuchea, Laos, Maldives, Nepal, Singapore, and Vietnam. The reason they are excluded are not that they are not important but because they have some distinct characteristics: Afghanistan, Laos, Kampuchea, and Vietnam are socialist countries; Singapore is a city state; Bhutan, Brunei, Maldives, and Nepal are small countries; and Indonesia is a major oil exporting country.

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[2]It differs from the common scholarly classification that includes Burma in Southeast Asia.

[3]World Bank, World Development Report 1987 (New York: Oxford University Press, 1987). Throughout the study $ means United States dollar unless otherwise stated.

Table I-1 Basic Economic Indicators

	Population (Millions, mid-1985)	Area (thousands of square kilometers)	GNP Per Capita	
			1985 U.S. dollars	Average Annual Growth Rate (percent) 1965-85
Bangladesh	100.6	144	150	0.4
Burma	36.9	677	190	2.4
India	765.1	3288	270	1.7
Malaysia	15.6	330	2000	4.4
Pakistan	96.2	804	380	2.6
Philippines	54.7	300	580	2.3
Sri Lanka	15.8	66	380	2.9
Thailand	51.7	514	800	4.0

Source: World Bank, World Development Report 1987 (New York: Oxford University Press, 1987).

Note: Throughout the study $ means United States dollar unless otherwise stated.

In recent years, BOP difficulties have become a major economic problem for a large number of countries. The period has been marked by an unprecedented increase in trade deficits and the burgeoning debts of developing countries. The persistent BOP difficulties have raised two important questions. First, what factors account for the nature, size, and direction of external payments imbalances? And, second, what types of adjustment mechanisms have been adopted in response to imbalances?

In answering the first question, economists sometimes divide factors into 'external' and 'internal' categories, although this distinction is not perhaps useful in practice--partly because many events occur simultaneously and partly because close interrelationships exist among different factors. Nevertheless, for expositional and analytical purposes, it is useful to categorize some factors as 'external' in the sense that these factors are beyond the influence and control of less developed countries, and other factors as 'internal' in the sense that these factors are within the influence and control of individual less developed countries.

Throughout the 1970s a series of external events contributed to the BOP difficulties of less developed countries. Energy prices quadrupled in 1973-74, and then rose again by 80 percent in real terms in 1979-80. The industrial countries went into recessions in 1974-75 and 1979-80, and again in 1981-82, followed each time by a relatively slow recovery. These effects were aggravated by a steady

decline in the prices of most primary commodities produced by less developed countries and a steady rise in the prices of imports of less developed countries, thus causing terms of trade to deteriorate. At the same time, increasing protectionist measures in industrial countries also contributed to the fall of exports from the less developed countries. The proportion of imports subject to non-tariff barriers doubled in the U.S. between 1980 and 1983 and increased by 38 percent in the European Common Market.[4] In addition, sharp increases in real interest rates in the international capital market increased the debt service burdens of many less developed countries; and, in particular, the countries already in substantial current account deficits.[5]

In most industrial countries output continued to rise after 1982, but the recovery was slow compared to previous periods. The World Development Report 1986 calls it "the hesitant recovery."[6] For

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[4]To give an idea of extent of protection, 20 percent of imports from developing countries were subject to non-tariff barriers alone in industrial-country markets in 1983. See World Bank, World Development Report 1985 , p. 40.

[5]Sweder van Wijnbergen estimated the 'first-round' effect on the current account for developing countries of changes in interest rates, terms of trade, and GNP growth in industrial countries. According to his simulation results, a 1 percent increase in interest rate in 1984 results in an extra cost of $2.3 billion in total debt; a 1 percentage improvement in terms of trade yields $2.2 billion; and 1 percentage point improvement in industrial country GNP growth yields $3.5 billion without dollar appreciation and $1.3 billion with dollar appreciation. See Sweder van Wijnbergen, "Global Interdependence via Trade and Capital Markets: An Empirical Analysis," background paper for the World Development Report 1985.

[6]World Bank, World Development Report 1986.

developing countries output growth followed a similar pattern, but slowed in 1985 as a result of (i) slower growth in industrial countries, particularly in the U.S., starting from the middle of 1984; (ii) a slowdown in the growth in world trade relative to industrial country growth; and (iii) a further deterioration in the terms of trade of developing countries, combined with restricted capital flows.[7]

Domestic factors also contributed to the BOP problem. Throughout the period 1973-81, the fiscal position of non-oil developing countries was consistently in deficit. Inflation was a common feature, averaging almost 30 percent a year during 1973-81. More importantly, real effective exchange rates continued to rise, causing demand for imports to rise and foreign demand for exports to fall, and thus contributing adversely to the BOP of non-oil developing countries.

In answering the second question--about the kinds of adjustment mechanisms that have been adopted--economists recognize that there are a number of possible ways to adjust in response to the BOP problem. One way to adjust is to restrain demand for imports by slowing economic growth. This is often essential for a country with low foreign exchange reserves. Another way to adjust is to maintain the growth rate and to borrow abroad and/or to use foreign exchange

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[7]Ibid., p. 16.

reserves to pay for the deficits. This policy depends on the amount of foreign reserves available and the extent to which external resources can be attracted. Lastly, as a long term policy, a country can restructure the economy towards export expansion and import-substitution. In practice, each developing country combines these measures but emphasizes one or another approach, the choice depending on the extent of payments difficulties and the structure of the economy.

The broad outlines of the above aspects have been discussed in the literature of international trade and development, but there is considerable controversy over the relative role of external and internal factors responsible for developments in the BOP problems and on the relative merits of policy measures adopted in response. The continuing controversy stems from the fact that current literature on the BOP places significantly higher emphasis on stochastic model building than on explaining facts and figures. Even when studies explain facts and figures, most studies rely on causal observation rather than on systematic examination of <u>trends</u> and <u>patterns</u>. Although a vast body of comparable data for different countries exists, the data have not been examined from the point of view of examining underlying patterns. The literature on this aspect of BOP shock-policy-adjustment is conspicuously absent and what exists is largely confined to the reports of governments and other international organizations. The IMF's and the World Bank's annual reports provide excellent summaries of the BOP performance of its

member countries, but these reports give aggregate pictures that mask divergent trends in different groups of developing countries. A large group of countries does not permit analysis of divergent trends that vary systematically with country size (therefore, magnitude of shock), level of development (therefore, ability to reallocate resources), and quality of policy actions taken (therefore, ability to minimize cost of adjustment). On the other hand, a single country study provides a detailed picture of the country's experience but no generalization can be derived about developing countries in general.[8] Such considerations call for an intensive study of the patterns of BOPs in a sample of countries large enough to allow generalized analysis, yet small enough to allow detailed investigation. This project makes an effort to examine descriptively, analytically, and empirically the nature, magnitude, and consequences of BOP performances and adjustment processes of a small group of countries, to compare country experiences, and to derive systematic patterns "with due regard to geographical, historical, and noneconomic factors, leaving theoretical generalizations or policy implications to emerge (if at all) at the end."[9]

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[8]For individual country studies see UNCTAD/UNDP, The Balance of Payments Adjustment Process in Developing Countries: Studies of the Experience of Selected Developing Countries in the 1970s, INT/75/015 (New York: United Nations, 1979). For a brief review of the World Bank Computable General Equilibrium Model, see Warren C. Sanderson and Jeffrey G. Williamson "How Should Developing Countries Adjust to External Shocks in the 1980s?" World Bank Staff Working Papers, no. 708 (Washington, D.C.: World Bank, 1985).

[9]M. J. H. Yaffey, Balance of Payments Problems of a Developing Country: Tanzania (München: Weltforum Verlag, 1970), p. 12.

In this study I examine descriptively, analytically, and empirically (i) the structure of merchandise trade and services and transfer payments; (ii) the nature, magnitude, and consequences of BOP problems; (iii) the external and internal factors that have contributed to the BOP problems; and (iv) the policy responses of the governments.

Analytical concepts that are used to interpret empirical patterns and relationships will be drawn from the field of economic development, international monetary relations, and contemporary economic history. The method in this study consists of conventional tools of economic analysis. Simple statistical techniques such as rank order correlations and regression analysis are used whenever need arises and data permit.

The main period of analysis is 1970-85. The year 1970 has been chosen as the beginning of analysis because comparable data for all countries become available from that date and the period contains periods of heavy fluctuations in commodity and energy prices, and protracted recession in the industrial countries. The study ends with 1985, when the available data on all countries ceases. The sixteen year period should provide a fairly satisfactory interval for systematic observations.

A study of the development of the BOP positions of developing countries must by its nature deal overwhelmingly with quantitative

data. This study will not be an exception. All data have been taken from standard statistical sources such as the International Monetary Fund, the World Bank, and the United Nations.

The outline of the study is as follows: the reminder of this chapter discusses some relevant literature. Chapter II concentrates on structures of merchandise exports and imports. Chapter III is intended to show the importance of services and transfer payments. Chapter IV undertakes a detailed study of the magnitude, causes, and consequences of BOP problems. Chapter V provides an analysis of the policy responses of our countries. Chapter VI summarizes the study.

SOME EXPLANATIONS OF BALANCE OF PAYMENTS PROBLEMS

External payments difficulties may adversely affect the performance of the economy for at least three reasons.[10] First, external payments difficulties usually become manifest in the shortage of foreign exchange. Since imports of typical developing countries include, among other things, capital and intermediate goods, payments difficulties of a persistent nature limit access to these inputs and thus impede capital formation and the growth of

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[10]For a detailed discussion on this point see Tony Killick and Jennifer Sharpley, "Extent, Causes, and Consequences of Disequilibrium in Developing Countries," in Tony Killick (ed.), The Quest for Economic Stabilization: The IMF and the Third World (New Hampshire: Heinemann Educational Books, 1984), p. 27.

output. Second, payments difficulties associated with slow or declining export growth may adversely affect saving, investment, and gross domestic product (GDP). Third, there is the point that Thirlwall makes:

> The importance of a healthy balance of payments for growth can be stated succinctly. If a country gets into balance of payments difficulties as it expands demand, before the short term capacity growth is reached, then demand must be curtailed; supply is never fully utilized; investment is discouraged; technological progress is slowed down, and a country's goods compared to foreign goods become less desirable so worsening the balance of payments still further ... [11]

The BOP stages hypothesis states that a country's BOP passes through a number of stages that correspond to stages in its economic development. John E. Cairnes was probably the first to show how colonies initially borrowed abroad to finance import surpluses; then, over a period of time, developed export surpluses and paid back interest charges and debt; and eventually started lending abroad.[12] The idea that the structure of the BOP of a country evolves in a certain and regular pattern has certain intuitive appeal. In the words of Charles P. Kindleberger,

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[11]A. P. Thirlwall, "The Balance of Payments Constraint as an Explanation of International Growth Rate Differences," Banca Nazionale del Lavoro Quarterly Review (March 1979), p. 46.

[12]John E. Cairnes, Some Leading Principles of Political Economy (New York: Harper & Brothers, 1874), pp. 355-63.

> in the early stages of growth when investment opportunities exceed savings, a country may make up the gap with international borrowing. At a later stage as its income and savings rise beyond its investment requirements, it pays back debt and accumulates foreign investments of its own. Still later, its propensity to save may shift again downward, as consumption rises through demonstration effect but the productive drive flags. At this stage the country may choose to consume some of its accumulated foreign capital. These are the basic factors with widely varying detail, underlying an old classification of balance of payments of various countries, which has existed long before the postwar interest in economic development.[13]

Based on the sign of the net balance on goods and services, the net balance on investment income, and the net flow of capital transfers, George L. Bach and Hans Genberg and Alexander K. Swoboda list four stages; Geoffery Crowther lists six stages; Stephen Enke and Virgil Salera list seven; and Nadav Halevi lists twelve stages.[14] While many intermediate stages are possible, four basic stages can be found in all writings: young debtor, mature debtor, young creditor, and mature creditor. Genberg and Swoboda find theoretical foundations for the BOP stages hypothesis in the life cycle hypothesis, Hecksher-

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[13]Charles P. Kindleberger, International Economics, 4th edition (Homewood III: Irwin, 1968), p. 483.

[14]George L. Bach, Economics, 3rd edition (New Jersey: Prentice-Hall, 1960), pp. 699-700; Hans Genberg and Alexander K Swoboda, "The Stages in the Balance of Payments Hypothesis Revisited," background paper for the World Development Report 1985; Geoffery Crowther, Balances and Imbalances of Payments (Boston: Plimpton Press, 1957); Stephen Enke and Virgil Salera, International Economics (New York: Prentice-Hall, 1947), pp. 638-41; Nadav Halevi, "An Empirical Test of the 'Balance of Payments Stages' Hypothesis," Journal of International Economics, vol. 1, no.1 (February 1971), pp. 103-117.

Ohlin models, and recent developments in current account theory. They also try to find empirical validity in cross sectional and time series data. But, like Halevi, they could not find any correlation between per capita income--used as the proxy for the stage of development--and the structure of BOP in cross country data. Long term data for countries like the U.S.A. and U.K. lend some support to a BOP stages hypothesis, but the pattern could not be verified for many developing countries due to lack of historical data. The stages of the BOP of developing countries also show some contrasting patterns since 1950. There are also some countries that move back and forth without permanent progress due to various external and internal shocks. Michael Bazdarich presents a model where no such stages exist. He states that "a developing country will always be a net debtor and net borrower, with its net debt position monotonically approaching some long-term steady-state level"[15] except in some special conditions such as a richness of natural resources. Further, a country's net position cannot be judged in such simple terms as the stages hypothesis suggests. Exports or imports of capital today have different meanings: grants-in-aid, political loans, and capital flight play important roles that are quite inconsistent with a neoclassical stages hypothesis.

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[15]Michael J. Bazdarich, "Optimal Growth and Stages in the Balance of Payments," Journal of International Economics, vol. 8, no. 3 (August 1978), p 426.

Various approaches to BOP adjustments constitute the second source for patterns in BOPs. Since we are not primarily interested in models, here we only review relevant parts of these models. Different theories tend to focus on different components of the BOP. The Keynesian approach focuses on current account, the monetary approach makes little distinction between current and capital accounts, and the structural approach highlights the structures of production and trade.

According to the traditional Keynesian approach, if exports are exogenously determined, economic growth causes a country's trade balances to deteriorate, because, as income rises, imports rise at a higher rate relative to exports. On the other hand, according to the monetary approach, economic growth leads to a surplus in the BOP because, as real income rises with money supply growing at less than the growth rate of income, the price level will fall and the demand for real cash balances will rise. Excess demand for real cash balances leads to an inflow of reserves, and thus a BOP surplus:

> These results are to be contrasted with various Keynesian theories about the relation between economic growth and the balance of payments. According to one such theory derived from the multiplier analysts, economic growth must worsen the balance of payments through increasing imports relative to exports; this theory neglects the influence of demand for money on export supply and import demand and on

the international flow of securities.[16]

It may be mentioned that Germany, Japan, and the Scandinavian countries show a pattern of higher economic growth rates and BOP surpluses in the 1960s and 1970s. According to the structural approach, a typical less developed country would face payment difficulties because it tends to suffer from commodity concentration and secular decline in terms of trade vis-à-vis developed countries.[17]

In various recent works A. P. Thirlwall and R. J. Dixon and A. P. Thirlwall and have presented a BOP constraint growth theory.[18] Thirlwall says "[it is] a fundamental law that, except where the balance of payments equilibrium growth rate exceeds the maximum feasible growth rate, the rate of growth of a country will

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[16]Harry G. Johnson, "The Monetary Approach to the Balance-of-Payments Theory," in Jacob A. Frenkel and Harry G. Johnson (eds.), The Monetary Approach to the Balance of Payments (London: George Allen and Unwin, 1976), p. 158.

[17]Raul Prebisch, The Economic Development of Latin America and its Principal Problems (New York: UN, 1950); Arthur W. Lewis, "Economic Development with Unlimited Supplies of Labour," The Manchester School, 22 (May 1954), pp. 139-91; Gunner Myrdal, Economic Theory and Underdeveloped Regions (London: Duckworth, 1957); Hans W. Singer, "The Distribution of Gains Between Borrowing and Investing Countries," American Economic Review, 40 (May 1950), pp. 473-85.

[18]A. P. Thirlwall and R. J. Dixon, "A Model of Export-led Growth with a Balance of Payments Constraint" in J. K. Bowers (ed.), Inflation Development and Integration (Leeds: Leeds University Press, 1979); A. P. Thirlwall, Balance of Payments Theory and the United Kingdom Experience (London: Macmillan Press, 1980); A. P. Thirlwall, "The Balance of Payments Constraint as an Explanation of International Growth Rate Differences," Banca Nazionale del Lavoro Quarterly Review, 32 (March 1979), pp. 44-53.

approximate to the ratio of its rate of growth of exports and its income elasticity of demand for imports."[19] If the BOP growth rate is higher (lower) than the actual growth rate, a country will experience BOP surpluses (deficits). Thirlwall substantiates his thesis with empirical evidence, using income elasticities calculated by Hendrick S. Houthakker and Stephen P. Magee; John Cornwell; and Mordechai E. Kreinin.[20] Recently Peter G. McGregor and J. K. Swales have questioned the validity of a general law as suggested by Thirlwall, and also point out that it is not supported by the empirical evidence that Thirlwall investigates.[21]

The persistent BOP crises of non-oil developing countries have stimulated a number of empirical works designed to find the main cause of crisis and to estimate the effect of such shocks. In the aftermath of the oil price increases in 1973-74 and 1979-80, many non-oil developing countries experienced deterioration in their current accounts. The conventional wisdom pointed out that countries heavily dependent on oil imports would experience BOP pressures. In

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[19]Thirlwall, Balance of Payments, p. 255.

[20]Hendrick S. Houthakker and Stephen P. Magee, "Income and Price Elasticities in World Trade," Review of Economics and Statistics, vol. LI, no. 2 (May 1969), pp. 111-125; John Cornwall, Modern Capitalism: Its Growth and Transformation (London: Martin Robertson, 1977); Mordechai E. Kreinin, "Price Elasticities in International Trade," Review of Economics and Statistics, vol. XLIX, no. 4 (November 1967), pp. 510-516.

[21]Peter G. McGregor and J. K. Swales, "Professor Thirlwall and Balance of Payments Constraint Growth," Applied Economics, 17 (February 1985), pp. 17-32.

an ambitious and stimulating paper, Jeffery D. Sachs argued that there is no theoretical ground and empirical support for such a belief.[22] He showed that no correlation between current account and oil dependence exists. "The correlation between high deficits and large oil imports holds only for the years of major price rises (1974 and 1979)."[23] He claimed that the pattern of current account movements observed outside OPEC in the 1970s was dominated by shifts in investment. He disposed of two alternative hypotheses that changes in saving and cyclical movements in output can explain current account shifts. However, for some countries, saving was more important than investment. For example, improvements in Pakistan's current account balance in recent years can be attributed to increased remittances of emigrant workers.

S. N. Naqvi traced the BOP problems to a failure to channel equilibrium resources to the export sector from the rest of the economy and consequent allocative inefficiency.[24] According to him, unbridled growthmanship, wrong strategies of economic development, and sub-optimal policy mixes caused long term BOP problems. Many developing countries emphasized maximizing industrial growth via import substitution. Easy availability of foreign aid led to

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[22]Jeffery D. Sachs, "The Current Account and Macroeconomic Adjustment in the 1970s," Brookings Papers on Economic Activity, 1 (1981), pp. 201-68.

[23]Ibid., p. 210.

[24]S. N. Naqvi, "The Balance of Payments Problems in Developing Countries," Pakistan Development Review, 12 (Autumn 1973), pp. 259-72.

disregarding BOP constraints. But, as foreign debt accumulated, reverse flows grew larger and deficits became a problem. In this situation foreign aid became necessary, not only for economic growth, but also to pay for debt services. In the meantime, the industrial sector became dependent on imports, and export expansion lagged behind import restriction.

In a number of studies by the World Bank and the Organization for Economic Co-operation and Development (OECD), Bela Balassa provided estimates of external shocks (defined as worsening terms of trade and slowing down of export demand) and policy responses (net external financing, export promotion, import substitution, and temporary lowering of economic growth) to these shocks.[25] Several interesting patterns emerged from these studies. External shocks to relatively industrialized developing countries were larger than to relatively less industrialized countries; but relatively industrialized countries were more successful in overcoming external

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[25]Bela Balassa, "The Policy Experience of Twelve of Less Developed Countries, 1973-78," World Bank Staff Working Papers, no. 449 (Washington, D.C.: World Bank, 1981); Also by same author, "Structural Adjustment Policies in Developing Countries," World Bank Staff Working Papers, no. 464 (Washington, D.C.: World Bank, 1981); "The Adjustment Experience of Developing Countries after 1973," in John Williamson (ed.), IMF Conditionality (Washington, D.C.: Institute for International Economics, 1983), pp. 145-174; "Export Incentives and Export Performance in Developing Countries: A Comparative Analysis," Weltwirtschaftliches Archiv, 1 (1978), pp. 24-61; "Exports and Economic Growth: Further Evidence," Journal of Development Economics (June 1978), pp. 181-89; "The Newly Industrializing Developing Countries After the Oil Crisis," Weltwirtschaftliches Archiv, 1 (1981), pp. 142-94; "Policy Response to External Shocks in Selected Latin American Countries," Quarterly Review of Economics and Business (Summer 1981), pp. 131-64.

shocks than were less industrialized countries. The countries with outward-looking development strategies experienced greater shocks (7.5 percent of GNP) than inward-looking countries (3.8 percent of GNP).[26] But outward-looking countries coped with the shock far better than inward-looking countries. Three-fourths of the adverse balance of payments effects were offset through domestic adjustment in newly industrialized countries. However, "in agricultural based economies including the least developed and South Asia, additional net external financing was one-and-a-half to two times as large as the balance of payments effect of external shocks, indicating that domestic policies aggravated the adverse effects of these shocks."[27] In general, export promotion appeared to be positively and import-substitution negatively related to economic growth.

The methods used in the above studies are ingenious and deserve appreciation. However, there are several drawbacks. For example, the approach ignored the cross effects of external shocks and consequent policy responses. A fall of exports from competing exporters may show up as a successful export promotion policy, and a lower demand in foreign countries causing lower domestic demand may show up as a successful growth reduction policy. Further, Balassa

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[26]Outward-looking or export-oriented development strategy refers to the strategy of production of goods for external markets and inward-looking or import-substitution strategy refers to the strategy of production for the home market for the previously imported goods.

[27]Balassa, "The Adjustment Experience," in IMF Conditionality, pp. 152-153.

did not consider the impact of external shocks on services and transfer payments. It is possible for a country's trade account to be in deficit while its services and transfer account is in surplus, so that the net balance in current account is positive. For instance, in 1979 India's trade deficit was $884 million but services and transfer surplus was $1654 million; as a result, the current account balance was in surplus at $688 million. Neglect of interest rate effects was particularly serious since everything that caused a trade balance to go into deficit also caused interest payments to go up and debt service to rise, and hence aggravated the BOP problem. In a later study Bela Balassa and F. Desmond McCarthy included interest rate effects.[28] The principal cause of balance of payments difficulties appeared to be terms of trade during 1979-81 period.

Using a very simple Keynesian model, Pradeep K. Mitra estimated the external shock on thirteen semi-industrialized oil importing countries after the oil price rise in 1973-74.[29] He found that, on the average, about 80 percent of the external shock was

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[28]Bela Balassa and F. Desmond McCarthy, "Adjustment Polices in Developing Countries, 1979-82," World Bank Staff Working Papers, no. 675 (Washington, D.C.: World Bank, April, 1984); Balassa and McCarthy, "Adjustment Polices in Developing Countries, 1979-83: An Update," World Bank Staff Working Paper, no. 675 (Washington, D.C.: World Bank, November, 1984).

[29]Pradeep K. Mitra, "Accounting for Adjustment in Selected Semi-industrial Countries," World Bank document (May 1983) quoted in Sanderson and William, "External Shocks in the 1980s" in World Bank Staff Working Papers, no. 708 (Washington, D.C.: World Bank, 1985); Pradeep K. Mitra, "World Bank Research in Adjustment to External Shock," Research New (Fall/Winter 1983).

price related, mainly to import prices. On the adjustment side, about 60 percent of the adjustment was trade related, although increased external financing was also important.

Toney Killick and Jennifer Sharpley concluded that less developed countries as a group, showed greater deficits than developed countries.[30] After 1973, external factors contributed more to payment difficulties than internal factors. Non-oil less developed countries, particularly low income LDCs, were vulnerable to export fluctuations, worsening terms of trade, and fluctuating international reserves. According to Killick and Sharpley, internal factors contributed more to payments difficulties than did external factors. International reserves relative to imports were lower in the LDCs than in developed countries, although greater instability in LDC export earnings would have called for proportionately higher reserves.

Sidney Dell and Roger Lawrence maintain that external factors, and specifically deterioration of terms of trade, were the main cause of payments difficulties in the developing countries during 1973-78.[31] They also find a pattern of asymmetry in adjustment as the responsibility to adjust is shifted from surplus

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[30]Killick and Sharpley, "Disequilibrium in Developing Countries," in Killick (ed.), The Quest for Economic Stabilization.

[31]Sidney Dell and Roger Lawrence, The Balance of Payments Adjustments Process in Developing Countries (New York: Pergmon Press, 1980).

countries to the weakest countries in various ways. For example, while the deficit may be the result of factors partly or wholly outside the control of a deficit country, IMF assistance may lead to a serious austerity program (which may be technically feasible but politically unfeasible) in a deficit country. A surplus country, on the other hand, remains outside the regulation of IMF. According to Dell and Lawrence,

> it is a serious inconsistency in the present situation, and a major source of international disequilibrium, that surplus countries are permitted an indefinite period of time in which to adjust their surpluses downward while counterpart deficits must be adjusted within the standard periods provided under IMF standby arrangements.[32]

William Cline and Sidney Weintraub maintain that during the 1950s and 1960s domestic factors were mainly responsible for payments difficulties, and even in the 1970s not all payments difficulties could be attributed to external shocks.[33] Thomas M. Reichmann similarly concluded that, in 15 out of 21 countries he studied, over-expansionary demand policies were the major causes of payments problems.[34] Using a pooled cross-section and time series analysis for a sample of 32 non-oil developing countries during 1973-80,

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[32]Ibid., pp. 99-100.

[33] William Cline and Sidney Weintraub (eds.), Economic Stabilization in Developing Countries (Washington, D.C.: Brooking Institute, 1981).

[34]Thomas M. Reichmann, "The Fund's Conditional Assistance and the Problems of Adjustment, 1973-75," Finance and Development, vol. 15 (December 1978), pp. 38-41.

Mohsin S. Khan and Malcolm D. Knight came to the conclusion that external as well as internal factors were responsible for deterioration in current accounts.[35]

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[35]Mohsin S. Khan and Malcolm D. Knight, "Determinants of Current Account Balances of Non-oil Developing Countries in the 1970s," International Monetary Fund Staff Paper (December 1983), pp. 819-42.

CHAPTER II

THE STRUCTURE OF MERCHANDISE TRADE

Balances of payments depend significantly on the trade balance. Proper assessment of the developments in exports and imports is, therefore, crucial to any investigation into the BOP experience of developing countries. This chapter provides an analysis of major developments and relevant experiences in the merchandise trade structures of the sample countries.

RELATIVE IMPORTANCE OF FOREIGN TRADE

The ratios of exports to GDP and imports to GDP, sometimes called export and import coefficients, are two crude but widely used indices of the size of a country's external sector. Table II-1 shows exports and imports as percentages of GDP for individual countries. The countries are ranked in descending order of 1985 values. A substantial variation from country to country is immediately apparent from the table. Exports accounted for as much as 59 percent of GDP for Malaysia in 1980, while it was as little as 3 percent for Bangladesh in 1975. Judged by either the export or import ratios or by the composite ratios of exports plus imports to GDP, Malaysia ranked overwhelmingly first, followed by Sri Lanka, and Thailand, and

Table II-1 Exports and Imports as Percentages of GDP, 1970-85

	1970	1975	1980	1985
Exports as Percentages of GDP				
Malaysia	46.1	45.5	59.2	54.9
Sri Lanka	25.5	27.5	32.2	26.0
Thailand	16.7	19.1	24.5	26.0
Philippines	19.1	18.6	20.4	20.8
Pakistan	7.6	11.6	12.4	10.4
Bangladesh[a]	3.0	2.9	5.9	6.7
Burma	5.6	5.1	8.2	4.6
India	4.4	6.5	7.1	4.5
Imports as Percentages of GDP				
Malaysia	44.4	47.2	54.8	49.8
Sri Lanka	28.6	35.0	54.8	38.0
Thailand	21.6	23.7	29.9	26.6
Pakistan	10.1	20.5	22.9	22.3
Philippines	19.4	25.3	18.8	17.8
Bangladesh[a]	12.5	11.2	18.4	15.4
Burma	8.2	6.2	12.0	8.6
India	4.5	7.6	10.7	7.1
Exports and Imports as Percentages of GDP				
Malaysia	90.5	92.6	114.0	105.1
Sri Lanka	54.1	62.5	87.0	64.0
Thailand	38.2	42.8	54.4	52.6
Philippines	27.0	36.9	31.3	38.6
Pakistan	29.4	39.1	43.3	32.8
Bangladesh[a]	16.9	17.7	25.4	22.1
Burma	13.8	11.2	20.2	13.1
India	7.5	10.6	16.6	11.6

Source: Calculated from the International Monetary Fund (IMF), International Financial Statistics Yearbook (Washington, D.C.: IMF, various issues).

[a]1970 data calculated from the World Bank, World Tables, vol. I, 3rd edition (Baltimore: John Hopkins University Press, 1984).

the Philippines at a fifth or higher. The contribution of exports to GDP increased for all countries from 1970-75 to 1980, but fell again for the South Asian countries after 1980.[1] The four South Asian Countries--India, Burma, Bangladesh, and Pakistan--experienced higher fluctuations in export coefficients than did the Southeast Asian countries. A similar pattern can be seen in import coefficients. This is probably because import coefficients usually track export coefficients, rising when exports are rising and falling when exports are doing poorly.[2] The general trend was, thus, upward until 1980, whereupon it declined. The fluctuations were heavy for South Asian countries but modest for Southeast Asian countries.

The data in Table II-1, read together with the data on per capita GNP shown in Table I-1 (page 3), show that countries with higher levels of per capita GNP also have higher export and import ratios. Spearman rank order correlations between export and import ratios and per capita GNP in 1985 was strong: 0.82 for export ratios and 0.77 for imports ratios.

The variations in export and import coefficients are due to a number of factors--namely, the structure of the economy, the

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[1]See also Adrain Wood, "Growth and Structural Change in Large Low-income Countries," World Bank Staff Working Papers, no. 763 (Washington, D.C.: World Bank, 1986); Moshe Syrquin, "Patterns of Development Since 1960: A Comparison for China," unpublished document (1985) quoted in Wood.

[2]Lloyd G. Reynolds, Economic Growth in the Third World, 1850-1980 (New Haven: Yale University Press, 1985), p. 412.

geographic size of the country, and the absolute size of the GDP. Internal trade tends to be higher in large countries and consequently, international trade tends to be relatively less important. Further, the absolute size of the GDP can cause export and import ratios to vary. For example, although absolute values of exports and imports were large in India compared to Thailand, the relatively large Indian GDP meant that export and import ratios were smaller in India than in Thailand. However, neither a country's geographic size nor the absolute size of its GDP causes substantial variations in export and import ratios. Rather differences in economic structure may explain the variability of export and import coefficients across the countries. An economic structure with a high export and import orientation (for example, Saudi Arabia or Singapore) tends to have higher export and import coefficients. A number of countries in our study--Malaysia, Sri Lanka, and Thailand in particular--have traditionally been high export- and import-oriented countries. High export and import coefficients of these countries were, therefore, not surprising. On the other hand, India and Pakistan, as a result of a strong bias toward import substitution, have traditionally been relatively closed economies. Consequently, these countries have low import and export coefficients.

Low export and import ratios of a country should not be interpreted to mean that its foreign sector plays only a minor role in the domestic economy. The composition of exports and imports may

give the foreign sector a strategically important place in the economy that is out of proportion to its size,[3] as where a large percentage of imports consists of goods essential for development.

SIZE AND GROWTH OF FOREIGN TRADE

The foreign trade of the region was marked by rapid growth. Table II-2 shows the structure of the trade balances of individual countries during 1970-85. All countries experienced trade deficits throughout the period except Malaysia. Exports increased by three to five times in most countries and by ten times in Malaysia and Thailand. Imports show a similar upward trend, in fact increasing proportionately more than exports. As a result, the trade deficits increased for all countries except Malaysia.

The countries with higher levels of per capita GNP also had higher levels of per capita exports and imports, the Spearman rank order correlation coefficients between per capita GNP and per capita exports and imports being 0.89 and 0.73 respectively.

While the secular trends of exports and imports were upward in the region, the growth rates were not evenly spread. Table II-3

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[3]Gunner Myrdal, Asian Drama: An Inquiry into the Poverty of Nations, vol. I (New York: Pantheon, 1967), p. 590.

Table II-2 Structure of Trade Balances, 1970-85
(All figures in US $; Exports, Imports, and Trade Balances in millions)

Country	Year	Exports	Imports	Trade Balances	Per Capita Exports	Per Capita Imports
Bangladesh	1970[a]	340	551	-212	5	8
	1975	323	1,170	-848	4	15
	1980	793	2,353	-1,560	9	27
	1985	1,000	2,286	-1,287	10	23
Burma	1970	117	159	-42	4	6
	1975	162	249	-87	5	8
	1980	483	788	-360	14	10
	1985	311	513	-202	11	17
India	1970	1,879	2,010	-131	4	4
	1975	4,666	4,952	-286	7	10
	1980	8,330	13,947	-5,644	11	21
	1985	9,465	15,081	-5,616	13	20
Malaysia	1970	1,640	1,291	349	162	135
	1975	3,784	3,527	256	323	296
	1980	12,868	10,462	2,406	933	774
	1985	15,133	11,556	3,577	965	737
Pakistan	1970[b]	672	1,210	-538	12	19
	1975	1,050	2,207	-1,157	15	30
	1980	2,569	5,445	-2,876	32	65
	1985	2,648	5,878	-3,230	28	61
Philippines	1970	1,064	1,090	-26	31	35
	1975	2,263	3,459	-1,196	53	90
	1980	5,788	7,727	-1,939	120	172
	1985	4,629	5,111	-482	86	93
Sri Lanka	1970	339	353	-14	27	31
	1975	558	686	-127	41	55
	1980	1,061	1,845	-784	71	138
	1985	1,303	1,960	-657	82	124
Thailand	1970	686	1,148	-462	20	36
	1975	2,177	2,850	-673	52	78
	1980	6,449	8,352	-1,902	137	203
	1985	7,059	8,391	-1,332	138	164

Sources: Columns 3-5 from IMF, International Financial Statistics Yearbook (Washington, D.C.: IMF, various issues); Columns 6 and 7 from the United Nations (UN), International Trade Statistics Yearbook, all volumes (New York: UN, various issues); [a]1970 data from the World Bank, World Development Report 1986

Notes: [b]Per Capita Exports and Imports data include Bangladesh.

Table II-3 Annual Average Growth Rates of Exports (f.o.b.), 1950-85

	1950-85	1950-60	1960-70	1970-80	1970-75	1975-85
Malaysia	9.6	0.6	4.3	24.2	24.0	14.7
Pakistan	7.8	-4.2	10.3	13.3	10.9	11.8
Thailand	11.1	1.5	5.9	24.7	31.8	11.8
Bangladesh	3.0	-0.4	5.3	6.3	-6.4	9.9
Sri Lanka	3.7	0.9	-1.4	13.6	12.3	8.7
Philippines	9.3	4.5	7.5	17.5	20.2	8.2
Burma	1.0	1.0	-8.8	14.3	11.5	7.3
India	6.8	0.0	3.7	17.2	18.7	5.8
Major Country Groups						
World	11.6	6.5	9.2	20.3	25.9	8.4
Developed Market Economy Countries	11.6	7.1	10.0	18.8	23.3	8.2
Developing Countries	11.6	3.0	7.2	26.1	36.5	8.4
All South & Southeast Asian Countries	11.5	0.2	6.7	25.8	29.6	14.7

Source: United Nations Conference on Trade and Development (UNCTAD), Handbook of International Trade and Development Statistics (New York: UN, various issues).

shows the annual growth rates of exports for a longer period (1950-85), where countries are ranked in descending order of 1975-85 averages. Several points emerge from this table. During 1950-85 Southeast Asian countries achieved an average export growth rate of 10 percent, while it was only 4 percent for South Asian countries. Export growth rates also varied substantially, from 11 percent (Thailand) to 1 percent (Burma). During 1950-85, all countries in this study showed lower growth rates than did the groups of other countries listed in the table.

Export growth rates were higher in the 1970s than in the 1950s and 1960s. The highest growth rate achieved by any country in the 1950s was only 5 percent, by the Philippines. Some countries even recorded negative growth rates. Growth was a little higher in the 1960s, although Burma and Sri Lanka showed negative growth rates. Spectacular improvement can be observed in the 1970s, when growth rates were higher than the previous two decades for all countries. A substantial increase can be observed in the early part of 1970s. However, the growth rate fluctuated heavily in the 1980s. All countries experienced negative growth rates at least once in first three years of the 1980s.[4]

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[4]UNCTAD, Handbook of International Trade and Development Statistics (New York: UN, various issues).

Table II-4 shows the import growth rates for the same period, where countries are ranked in descending order of 1975-85 averages. Again, growth rates were higher for the Southeast Asian countries than for the South Asian countries, and again import growth rate for Malaysia was the highest and for Burma was the lowest. Over the longer period 1950-85, import growth rates were comparatively high in Thailand, Malaysia, Pakistan, and the Philippines; modest in Bangladesh, Sri Lanka, and India; and low in Burma. During the 1950s Burma recorded the highest growth rate (7 percent), followed by Thailand and India, while Pakistan showed the lowest growth rate (1 percent). However, during the 1960s Burma's growth rate became negative and Thailand's almost doubled. Like export growth in the region and for all groups of countries, import growth rates were higher in the 1970s than during the previous two decades for all countries. Except for Malaysia no country in this group had an import growth rate higher than the South and Southeast Asian average (covering all countries, not just the eight countries of the study). Inclusion of high import countries such as Korea, Taiwan, and Hong Kong probably inflated the area average.

Tables II-5 and II-6 show, probably in somewhat crude form, the growth in the indices of value, unit value, and volume of exports and imports during 1970-85. It is clear from Table II-5 that the major contributor to the growth of value of exports in the 1970s was increase in unit values, while volume growth played a minor role. This is consistent with a recent IMF report that less than one-third

Table II-4 Annual Average Growth Rates of Imports (c.i.f.), 1950-85

	1950-85	1950-60	1960-70	1970-80	1970-75	1975-85
Malaysia	10.1	3.3	3.5	22.0	26.4	16.2
Sri Lanka	5.5	3.7	0.8	17.7	17.5	13.3
ThaiLand	12.6	6.6	12.7	22.5	24.4	12.7
Pakistan	9.8	1.0	6.6	20.4	16.4	12.2
India	7.3	5.2	0.0	20.5	26.2	10.9
Bangladesh	7.3	3.8	8.0	16.4	10.4	9.4
Philippines	9.8	3.7	8.5	21.2	26.7	6.0
Burma	1.6	6.9	-4.6	8.8	6.3	1.5
Major Country Groups						
World	11.6	6.5	9.1	20.3	25.5	8.6
Developed Market Economy Countries	11.7	6.5	10.2	19.5	24.2	8.4
Developing Countries	11.0	4.2	6.4	24.1	30.4	9.5
All South & Southeast Asian Countries	11.3	0.2	6.7	25.8	29.6	13.7

Source: UNCTAD, Handbook of International Trade and Development Statistics (New York: UN, various issues).

Table II-5 Value, Unit Value, and Quantum Indices of Exports (Compound Annual Percentage Changes), 1970-85

	1970-75			1975-80		
	Value	Unit Value	Quantum	Value	Unit Value	Quantum
Bangladesh	-10.12	6.33	-15.59	19.52	13.35	5.10
Burma	9.98	14.48	-3.99	22.00	11.13	10.03
India	16.72	16.15	0.29	13.97	11.13	7.39
Malaysia	18.21	19.57	-1.41	27.23	17.85	8.02
Pakistan	7.39	15.18	6.96	20.11	5.92	13.54
Philippines	14.87	18.89	-3.04	20.11	1.03	18.95
Sri Lanka	10.35	15.29	-4.13	13.12	12.70	0.41
Thailand	27.46	19.57	6.96	22.00	8.67	12.30

	1980-85			1970-85		
	Value	Unit Value	Quantum	Value	Unit Value	Quantum
Bangladesh	-4.73	2.97	8.01	3.74	5.06	-1.33
Burma	-7.70	6.10	-1.65	7.39	6.35	0.94
India	-1.87	-2.74	0.98	9.29	6.25	2.84
Malaysia	3.54	-5.59	9.70	15.91	10.40	4.95
Pakistan	0.98	-3.89	5.06	9.20	5.45	3.35
Philippines	-4.61	-5.34	0.59	9.59	5.11	4.27
Sri Lanka	3.71	3.20	7.11	1.22	7.95	1.03
Thailand	1.74	-6.89	9.17	16.52	6.56	9.45

Source: Calculated from the UNCTAD, Handbook of International Trade and Development Statistics (New York: UN, various issues).

Table II-6 Value, Unit Value, and Quantum Indices of Imports (Compound Annual Percentage Changes), 1970-85

	1970-75			1975-80		
	Value	Unit Value	Quantum	Value	Unit Value	Quantum
Bangladesh	2.98	16.52	-11.50	17.85	11.51	5.64
Burma	8.14	15.65	-6.64	7.09	10.76	-3.09
India	24.57	18.64	5.00	17.32	16.30	0.61
Malaysia	20.48	15.77	4.24	24.82	13.97	9.34
Pakistan	12.70	17.37	-3.70	20.11	15.34	4.05
Philippines	23.52	19.34	4.35	16.80	16.80	0.20
Sri Lanka	14.26	18.47	-3.96	35.37	15.34	5.64
Thailand	20.79	18.64	1.95	22.67	16.30	5.64

	1980-85			1970-85		
	Value	Unit Value	Quantum	Value	Unit Value	Quantum
Bangladesh	1.92	-4.13	6.34	7.34	7.60	-0.20
Burma	-4.36	-2.08	-2.30	3.46	7.84	-4.03
India	0.20	-2.30	2.47	13.56	10.47	2.68
Malaysia	2.66	-2.30	5.06	15.58	8.83	6.19
Pakistan	1.92	-2.09	4.23	11.33	9.85	1.46
Philippines	-8.83	-1.87	-6.89	9.57	11.00	-0.89
Sri Lanka	-1.44	-3.20	1.74	11.57	9.77	1.06
Thailand	0.20	-1.65	1.92	14.08	10.71	3.16

Source: Calculated from the UNCTAD, Handbook of International Trade and Development Statistics (New York: UN, various issues).

of the increase in value of exports in the world is due to growth in volume.[5] The experiences in the 1950s and 1960s were just the opposite; almost 90 percent of the growth of world trade represented growth in volume. During 1970-75 unit values (both exports and imports) increased rapidly and volume growth was actually negative for four out of five South Asian countries during 1970-75. However, for all our sample countries unit values (Table II-6) fell during 1980-85.

Trade deficit was, thus, a common characteristic of our countries (except Malaysia). Both export and import growth rates were higher for the Southeast Asian countries. The major contributor to growth in trade was changes in unit values, growth in volume playing only a minor role.

SHARE OF WORLD MARKET

A country's export performance can be expressed as the value of each country's exports as a percentage of world imports. Table II-7 lists the market share of individual countries in 1970-85, where countries are ranked in descending order of 1985 market share. Several interesting patterns can be observed. The market shares of Malaysia and Thailand increased while it declined for rest of the

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[5]IMF, International Financial Statistics, supplement series, no. 4 (Washington, D.C.: IMF, 1982), p. viii.

Table II-7 The Value of Each Country's Exports as Percentages of World Imports, 1970-85

	1970	1975	1980	1985
Malaysia	.57	.46	.67	.82
India	.68	.53	.41	.52
Thailand	.24	.32	.34	.38
Philippines	.35	.28	.30	.24
Pakistan	.24	.13	.14	.14
Sri Lanka	.11	.07	.05	.07
Bangladesh	.07	.04	.04	.05
Burma	.04	.02	.02	.03
Major Country Groups				
Industrial Countries	73.73	69.40	64.44	66.60
Non-oil Developing Countries	15.88	15.05	16.36	18.60
Oil-Exporting Countries	5.87	13.21	15.37	8.32

Source: IMF, International Financial Statistics (Washington, D.C.: IMF, various issues).

countries. The increase in market shares of these two countries was probably due to improvement in terms of trade. For Thailand, the gain was small; but for Malaysia, it was substantial. In 1970, Indian and Malaysian market shares were 0.68 and 0.57 respectively. By 1985, India's market share declined to 0.52 while Malaysia's share increased to 0.82. The market shares of Bangladesh, Burma, India, and Sri Lanka continued to decline until 1980, whereupon a slight upward movement can be observed. The industrial and non-oil developing countries as a group also experienced a similar trend. The oil-exporting countries, on the other hand, experienced just the opposite trend as their market shares increased during 1970-80 and fell during 1980-85.

The eight countries together accounted for only 2.25 percent of world exports in 1985, 0.05 percent less than 1970 figure. The Southeast Asian countries' share were substantially higher than that of the South Asian countries.

However, the importance of these countries in the world trade cannot be judged from their low market share. As a matter of fact, a significant percentage of world exports of specific commodities came from the region. For example, based on 1982 figures, 80 percent of world exports of jute came from Bangladesh alone, 50 percent of tea from India and Sri Lanka, 45 percent of vegetable oil from Malaysia, 20 percent of silver and platinum ore from the Philippines, and 28 percent of tin from Malaysia.

Another point to remember is that a given changes in the export market shares will have different implications for different countries. For example, a small decline in export market share may not matter much to India but may be important for Malaysia because export and import ratios are quite high for Malaysia.

CONCENTRATION OF EXPORTS

One of the main reasons why international trade based on the principal of comparative advantage has been opposed by a few economists and by many statesmen is that it can lead to export concentration in a few commodities. The narrow range of goods exported may cause instability in export earnings; and, if export earnings constitute a significant percentage of national product, a fall in export earnings would have serious downward multiplier effect on the domestic economy.[6]

The view that developing countries tend to concentrate on the export of a few commodities, no matter how one defines concentration, is supported by the facts. Table II-8 provides two measures of concentration, where countries are ranked in descending order of the 1984 "concentration index." Both indices range between zero and one,

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[6]A second reason for disliking comparative advantage theory is that an exchange rate that places a country outside its comparative cost limits (extremely over-valued home currency) may lead one to conclude that the home country is undersold in everything.

Table II-8 Export Concentration and Diversification Indices, 1970-84

	Diversification Index[a]		Concentration Index[b]	
	1970	1984	1970	1984
Sri Lanka	0.935	0.837	0.584	0.456
Bangladesh	..	0.897	..	0.326
Burma	0.918	0.860	0.499	0.341
Malaysia	0.792	0.620	0.371	0.276
Philippines	0.855	0.752	0.324	0.298
Pakistan	0.823	0.795	0.264	0.207
Thailand	0.834	0.741	0.262	0.182
India	0.653	0.588	0.139	0.183

Source: UNCTAD, Handbook of International Trade and Development Statistics (New York: UN, various issues).

Notes: ".." means not available.

with one representing the most extreme concentration. The table shows a general tendency for both indices to decline during 1970-84, indicating that countries are expanding the range of goods that they export. India was at the bottom of the list in both indices in both years, while Sri Lanka was at the top of the list for "concentration index" in 1970 and 1984 and for the diversification index in 1970. Based on these two indices, we can conclude that Indian exports were more diversified than those of any other country in the region. The table also reveals that the countries with higher indices in 1970 were more successful in lowering their indices than the countries with lower indices in 1970, likely because of opportunities available to countries with higher indices.

A common feature of developing countries' exports is their high degree of concentration on primary products. The Pearson Committee concluded that:

> almost 90 per cent of the export earnings of the developing countries derive from primary products. Moreover, nearly half of these countries earn more than 50 per cent of their export receipts from a single primary product. As many as three-quarters of them earn more than 60 per cent from three primary products.[7]

Table II-9 shows exports of primary commodities as percentages of all merchandise exports during 1970-85, the countries being ranked by 1985 figures. The evidence in this table supports the view that

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[7]Lester B. Pearson, Partners in Development: Report on the Commission on International Development (New York: Praeger, 1969), p. 81.

Table II-9 Exports of Primary Commodities as Percentages of All Merchandise Exports, 1970-85

	1970	1975	1980	1985
Burma	96.6	100.0	83.5	81.7
Sri Lanka	95.0	88.5	65.9	59.3
Thailand	87.7	75.0	70.3	59.1
Philippines	84.6	77.8	63.1	46.6
Malaysia	85.7	72.1	55.9	40.6
India	47.1	54.3	39.8	38.3
Bangladesh	42.3	28.3	30.5	32.6
Pakistan	32.0	47.6	38.5	29.0
Major Country Groups				
Developing Countries (Excluding Major Petroleum Exporters)	66.1	52.5	40.0	31.2
Developing Countries	48.4	25.4	18.8	20.9
World	27.0	21.0	18.7	16.5

Source: UNCTAD, Commodity Yearbook 1987 (New York: UN, 1988).

primary exports as a percentage of all merchandise exports declined in developing countries in general, and in our cases in particular. However, it increased at least once in one of the sub-periods for three of the five South Asian countries.

A further indication of commodity concentration is provided in Table II-10, which shows the percentage contribution of three major primary commodities in total merchandise exports. The countries are listed in descending order of 1980 values. Three commodities accounted for over one-half of merchandise exports for six countries in 1960 (Sri Lanka, 85 percent; Burma, 80 percent; Malaysia, 70 percent; the Philippines, 70 percent; Thailand, 63 percent; and Bangladesh, 55 percent). However, by 1970 they accounted for a half or more for only four countries (Sri Lanka, 83 percent; Burma, 78 percent; Malaysia, 68 percent; and the Philippines, 56 percent); and by 1980 for only two countries (Burma, 81 percent; and Sri Lanka, 51 percent). This supports the position, derived from Table II-8, that there were clear signs of deconcentration throughout the period (with Burma the lone exception, and only by this measure), especially between 1970-1980.

COMMODITY COMPOSITION OF EXPORTS

Any investigation into the commodity composition of exports of developing countries is complicated by problems of classification

Table II-10 Commodity Concentration Expressed as Percentage Contribution of the Three Major Commodities to Total Merchandise Exports, 1960-80

	1960	1970	1980
Burma	79.5	78.4	80.6
Sri Lanka	85.4	83.0	50.6
Malaysia	70.4	66.7	47.8
Pakistan	28.5	23.5	38.3
Thailand	63.4	44.7	31.0
Philippines	70.1	56.3	26.4
Bangladesh	55.4	42.0	20.8
India	26.5	20.7	16.4

Source: World Bank, World Tables, 3rd edition, vol. I, Comparative Economic Data, Table 8 (Baltimore: John Hopkins University Press, 1984).

of goods. For analytical convenience, we will focus our analysis on major categories of exports. Table II-11 presents five main categories of exports for individual countries: (1) all food items, (2) agricultural raw materials, (3) fuels, (4) ores and metals, and (5) manufactured goods. The remaining exports are grouped under the heading "unallocated," which was very small for all countries except the Philippines. The manufacturing goods category has been divided into three parts: chemical products, machinery and equipment, and other manufactured goods. Depending on the availability, data have been presented for 1970, 1975, 1980, and 1985 or any year close to these years.

Several interesting points emerge from the data presented in Table II-11. First, the leading export category for eight individual countries remained the same throughout the study period. The only exception was Malaysia, where fuels took the lead for the first time in 1982, replacing agricultural raw materials. For Burma, the Philippines, Sri Lanka, and Thailand the leading export category was food items. For Bangladesh, India, and Pakistan, it was manufactured goods. Although the traditional leading export category maintained its position, a significant structural change in the commodity composition of exports can nevertheless be observed.

All Southeast Asian countries--Malaysia, the Philippines, and Thailand--and Sri Lanka achieved a spectacular increase in manufacturing exports. For example, they increased from 6 percent to

Table II-11 Value of Exports by Broad Categories of Goods Expressed as Percentages of Each Country's Total Exports (Selected Years)

	All Food Items	Agricultural Raw materials	Fuels	Ores and Metals	Manufactured Goods				Unallocated
					All	Chemical Products	Other Manufactured Goods	Machinery and Equipment	
	0+1+22+4	2-22-27-28	3	27+28+67+68	5+6+7+8-67-68	5	6+8-67-68	7	
Bangladesh									
1975	7.2	24.6	0.1	0.0	67.85	0.7	67.0	0.2	0.4
1980	12.5	18.7	0.0	0.0	67.7	1.4	65.0	1.3	1.2
1985	17.9	13.3	2.6	0.0	65.8	0.2	64.1	1.6	0.5
Burma									
1970	65.8	25.8	1.2	5.7	1.5	0.1	1.5	0.0	0.0
1975	58.9	30.2	1.0	6.8	3.1	1.6	1.6	0.0	0.0
India									
1970	29.7	5.6	0.8	18.5	45.1	2.3	38.1	4.7	0.3
1975	37.8	4.0	0.9	15.0	42.2	2.7	32.2	7.3	0.2
1980	28.2	5.0	0.4	8.6	47.5	4.2	45.0	8.3	0.3
1982	26.8	3.4	14.8	6.4	48.5	4.4	37.0	7.1	0.2
Malaysia									
1970	12.6	50.1	7.4	22.8	6.3	0.7	4.0	1.6	0.9
1975	23.2	34.1	10.9	14.0	17.1	0.9	10.1	6.2	0.7
1980	15.1	31.0	24.7	10.3	18.6	0.6	6.5	11.5	0.3
1984	19.2	20.2	29.9	4.2	26.4	1.1	6.4	18.9	0.2
Pakistan									
1970	10.6	30.2	1.2	0.7	57.2	0.8	55.9	0.5	0.1
1975	24.7	18.8	1.1	0.5	54.3	1.1	52.5	0.6	0.7
1980	23.5	20.5	7.1	0.4	48.2	0.8	46.1	1.3	0.3
1985	17.3	18.0	1.4	1.2	61.2	3.4	56.8	1.0	0.9

Table II-11 Continued

	All Food Items	Agricultural Raw materials	Fuels	Ores and Metals	Manufactured Goods				Unallocated
					All	Chemical Products	Other Manufactured Goods	Machinery and Equipment	
Philippines									
1970	44.0	25.8	1.6	22.1	6.4	0.5	5.8	0.1	0.1
1975	57.4	10.0	1.7	13.3	11.6	0.9	10.1	0.5	6.0
1980	35.9	6.1	0.7	21.4	20.3	1.6	16.5	2.2	15.7
1985	26.9	4.9	0.8	11.6	25.9	3.5	15.8	6.7	30.0
Sri Lanka									
1970	72.6	25.3	0.0	0.7	1.4	0.3	1.1	0.0	0.0
1975	63.8	19.5	0.1	5.3	3.8	1.9	1.7	0.3	7.5
1980	47.0	18.1	15.4	0.9	18.6	3.1	15.1	0.4	0.1
1984	52.4	10.7	9.0	0.9	27.0	0.5	25.1	1.4	0.1
Thailand									
1970	52.3	24.7	0.3	14.9	4.4	0.2	4.8	0.1	3.3
1975	62.8	12.3	0.6	7.7	14.4	0.6	12.6	1.3	2.2
1980	47.0	11.2	0.1	14.4	24.4	0.8	17.8	5.6	2.9
1985	46.2	9.2	1.3	5.4	37.1	1.3	26.9	8.8	0.8

Source: UNCTAD, Handbook of International Trade and Development Statistics (New York: UN, various issues).

26 percent for Malaysia and the Philippines; from 4 percent to 37 percent for Thailand; and from 1 percent to 27 percent for Sri Lanka. India and Pakistan achieved only a modest growth in manufactured exports, and only late in the period.

In the manufactured goods category exports of "other manufacturing goods"--which includes textile and cotton (including garments), leather, pearls and precious and semi-precious stone--went up during 1970-85. However, Malaysia and Thailand achieved a spectacular growth in exports of "machinery and equipment", consisting of light machinery and equipment. For example, from a low 1 percent it increased to 19 percent for Malaysia and 8 percent for Thailand. The contribution of chemical products in total exports was insignificant.

The spectacular increases in manufactured exports of developing countries was achieved in spite of protectionist measures against them. While industrial countries are the major markets, developing countries impose much higher protection on each others' exports than industrial nations impose on imports from developing countries. A recent study by the OECD found that the proportion of imports of manufactured exports from developing countries to major industrial countries subject to non-tariff barriers alone increased

from 20 percent in 1980 to 30 percent in 1983.[8] Although we do not have exact information about the extent of protection against the countries under review, we can still be fairly sure that manufactured exports would have increased more if new protectionist measures had not been imposed on these countries.

A detailed explanation of the causes of this spectacular increase in manufactured exports cannot be provided here. It is sufficient to say that abundance of low wage labor, ability to penetrate foreign markets, and domestic policies to encourage exports facilitated the expansion of manufactured exports from these countries. At the same time, demand for light manufactures increased in the industrial countries. The unit value of manufactured exports rose every year, averaging an increase of 12 percent per annum.[9] The Generalized System of Preference (GSP) schemes of industrial nations partly accounted for the high manufacturing exports from our countries. For example, in 1985 our countries exported over $3 billions under preferential treatment terms to the U.S. and Japan. To some extent, specific bilateral trade policies of importing countries also contributed to the increase in exports from these countries. Thailand, the Philippines, and Pakistan received preferential treatment from the U.S.A for

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[8]Quoted in David Goldsbrough and Iqbal Zaidi, "Transmission of Economic Influences from Industrial to Developing Countries," World Economic Outlook (July 1986), p. 168.

[9]IMF, "Primary Commodities," World Economic and Financial Surveys (Washington, D.C.: IMF, 1986), p. 2.

political reasons. Malaysia also obtained preferential treatment in the United Kingdom. These political factors undoubtedly facilitated exports from these countries in the hostile world of protectionist measures.

The Spearman rank order correlation coefficients between per capita GNP and the ratio of manufactured exports to total exports in 1985 was 0.64.[10] Interestingly, manufacturing provided a larger share of exports from those countries where the contribution of the manufacturing sector to GDP was lower. Spearman rank order correlation coefficients between manufactured exports and the ratio of manufacturing production to GDP was -0.55.

The share of food items in total exports remained relatively stable for India (tea, coffee, and fresh fish), Burma (rice and fresh fish), Thailand (rice, vegetables, sugar and honey, and fresh fish), and Pakistan (rice and fresh fish). It fluctuated for Malaysia (vegetable oil), and declined for Sri Lanka (tea, fruits, spices, and oil) and the Philippines (sugar and honey and fruits).

The contribution of agricultural raw materials in total export earnings showed a declining trend in general. Malaysia (wood and rubber), Bangladesh (jute), the Philippines (wood), Sri Lanka

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[10]For lack of comparable data Burma is excluded from the calculations.

(rubber), and Thailand (rubber) showed clear signs of a declining trend. For example, it declined from 50 percent to 20 percent for Malaysia, from 35 percent to 13 percent for Bangladesh, from 25 percent to 9 percent for Thailand. It showed marked fluctuations for Pakistan (cotton), but relative stability for Burma (wood and rubber).

Fuel was not an export item from this region except for Malaysia, and only recently for Sri Lanka. Between 1970 and 1985, fuel's share for Malaysian exports (crude petroleum) went up from 7 percent to 30 percent. It became an important source of export earnings for Sri Lanka (petroleum products) from 1978.

Ores and metals were important for Malaysia (tin), India (iron ore), the Philippines (nonferrous ores, silver and platinum ores), and Thailand (tin). There was a marked declining trend in the shares of ores and metals for India, Malaysia, and the Philippines. No clear trend was evident for other countries.

The major point that can be derived from the analysis in this section is that traditional export items still dominate the export composition of our countries but several countries did succeed in increasing the share of manufactured goods exports.

COMMODITY COMPOSITION OF IMPORTS

Broadly speaking, the composition of imports depends on population growth and the level and patterns of past and present development efforts of a country. Countries at a lower stage of development usually import a large amount of capital goods and industrial supplies for development purposes. A high population pressure in food deficit countries leads to large food imports. When imports must be curtailed because of decline in export earnings or a rise in import prices, developing countries with high rates of population growth are in a difficult situation. If they reduce imports of essential capital goods and intermediate goods, economic growth is hampered. If they reduce food imports, serious social and political tension develops. Usually food imports get preference over other types of imports in cases of BOP difficulties.

Table II-12 shows the composition of imports by end-use: capital goods, intermediate goods, and consumption goods.[11] The intermediate goods category in turn is divided into food and beverages mainly for industry; fuels; industrial supplies; and parts and accessories. Consumption goods are divided into food and beverages (hereafter food)--mainly for household consumption--and other consumer goods. The remaining imports were very small for all

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[11]For classification system see United Nations, Classification by Broad Economic Categories, statistical papers, series m, no. 53, Rev. 1 (New York: UN, 1976).

Table II-12 Composition of Imports by End-Use, 1970-85

	1970	1975	1980	1985[a]	1970	1975	1980	1985[b]
	Bangladesh				**Burma**			
Capital Goods	..	5	18	12	24	23	..	..
Intermediate Goods	..	82	72	72	67	69	..	..
Fuels	..	8	9	16	6	7	..	..
Food & Beverage	..	45	17	14	3	2	..	..
Industrial Suppl.	..	27	39	38	52	47	..	..
Parts & Accessor.	..	3	7	4	7	13	..	..
Consumer Goods	..	9	9	14	9	7	..	..
Food & Beverage	..	7	6	9	3	2	..	..
Other Cons. Goods	..	2	3	5	5	5	..	..
	India				**Malaysia**			
Capital Goods	17	13	9	9	20	21	20	24
Intermediate Goods	74	87	88	87	55	56	63	59
Fuels	8	23	45	44	12	12	15	10
Food & Beverage	15	24	7	6	4	5	4	3
Industrial Suppl.	44	35	32	34	33	32	30	28
Parts & Accessor.	7	6	5	4	6	8	14	18
Consumer Goods	7	2	3	4	23	19	13	14
Food & Beverage	5	2	2	2	14	11	6	6
Other Cons. Goods	2	1	1	1	9	8	7	8
	Pakistan				**Philippines**			
Capital Goods	23	16	19	20	24	24	17	8
Intermediate Goods	66	74	72	69	65	63	66	64
Fuels	6	18	27	24	12	22	28	28
Food & Beverage	15	18	7	13	4	3	3	3
Industrial Suppl.	39	33	32	27	39	30	28	28
Parts & Accessor.	6	6	5	5	11	8	7	6
Consumer Goods	9	8	9	9	10	7	5	6
Food & Beverage	5	5	5	5	6	5	3	4
Other Cons. Goods	4	3	4	4	4	2	2	2

Table II-12 Continued

	1970	1975	1980	1985[a]	1970	1975	1980	1985[b]
	Sri Lanka				**Thailand**			
Capital Goods	12	6	17	17	23	23	18	19
Intermediate Goods	51	63	65	67	57	66	70	69
Fuels	13	17	24	26	9	21	30	23
Food & Beverage	2	22	10	5	1	1	2	1
Industrial Suppl.	30	21	27	31	40	34	31	37
Parts & Accessor.	6	3	5	5	8	10	7	9
Consumer Goods	37	30	16	16	13	8	6	7
Food & Beverage	34	28	11	9	3	2	2	3
Other Cons. Goods	3	2	6	6	10	6	3	4

Source: UN, International Trade Statistics Yearbook, all volumes (New York: UN, various issues).

Notes: Different categories in a given year will add up to less than 100 because 'goods not classified elsewhere (SITC 7)' is not reported in the table; [a]1981 for India; [b]1984 for Malaysia and Sri Lanka. ".." means not available.

Imports classified by end-use and corresponding SITC numbers are as follows:

Capital Goods: 41 + 521

Intermediate Goods: 3 + 111 + 121 + 2 + 42 + 53
- Fuels: 3
- Food & Beverages: 111 + 121
- Industrial Supplies: 2
- Parts & Accessors: 42 + 53

Consumer Goods: 122 + 122 + 6 + 522
- Food & Beverages: 112 + 122
- Other Consumer Goods: 6 + 522

Goods not Classified Elsewhere: 7

countries except the Philippines in the late 1970s and 1980s, and are therefore not reported in the table.

The share of capital goods imports ranged from 8 to 24 percent of total imports in the region. The need to increase capital goods imports in the poorest countries of the region is obvious. For Bangladesh, Sri Lanka, and Malaysia the share increased; for rest of the countries it declined. Not inconsistently, the decline in capital goods imports in the relatively high income countries and in India could be the result of increased domestic production of these goods.

The trend in intermediate goods imports was mixed, but did not change much during 1975-85. The shares increased by at least 10 percentage point for Thailand, India, and Sri Lanka; remained about the same for Burma, Pakistan, Malaysia, and the Philippines; and fell for Bangladesh.

Industrial supplies were the major imports in the intermediate goods category throughout the period, except for India, where fuel became the largest share of imports in the late 1970s. It rose significantly for Bangladesh--from 27 percent to 39 percent. It declined for all Southeast Asian countries and Pakistan and India.

The share of fuel imports went up dramatically for all countries except Malaysia. It should be noted that a substantial

amount was re-exported from Sri Lanka. In Bangladesh and Malaysia, the two countries with the lowest and the highest per capita GDP respectively, the increases in the share of fuel imports were small compared to other countries.

A general pattern of a declining trend in food imports for industries can be observed in the region.[12] The share of food imports was low in Burma, the Philippines, and Thailand; and high in Bangladesh, India, Malaysia, Pakistan, and Sri Lanka. The share of food imports remained almost the same in traditionally low food-import countries. Traditionally high food-import countries reduced the share of food imports by a third to two-thirds during the period: for examples, from 51 percent to 24 percent for Bangladesh and from 20 percent to 8 percent for India. The major reason for the decline was increased domestic production. The World Report 1986 stated that the increased domestic production was the result of "efficient adoption of new crop varieties and technique by Asian farmers and improved polices for agriculture."[13]

The share of parts and accessories was low for all countries, except Malaysia where it rose sharply from 6 percent 18 percent.

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[12]According to UN classification, any food imports, such as wheat, that must be processed by industrial sector before it is ready for final use is considered as intermediate goods.

[13]World Bank, World Report 1986, p. 78.

The changing pattern of intermediate goods imports is related to the structure of the economies. As income rises, the value added coefficient declines gradually, thus reflecting an increase in intermediate goods intensity and consequent rise in intermediate imports.[14] In our case the countries with higher per capita GDP were also the countries that increased their shares of intermediate goods imports.

In general the share of consumer goods imports was low and declining. Bangladesh was the only exception: it went up from 9 percent to 14 percent.

In short, we see that when imports are classified by end-use (capital goods, intermediate goods, and consumption goods), the share of intermediate goods imports ranged from 60 to 85 percent, followed by capital goods imports. This also speaks for the effectiveness of these countries in pursuing their development objectives.

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[14]Yuji Kubo, "A Cross Country Comparison of Interindustry Linkages and the Role of Imported Inputs," World Development, vol. 13, no. 12 (December 1985), pp. 1287-1298; Moshe Syrquin, "Alternative Approaches to Industrialization," mimeo (Washington, D.C.: World Bank, 1981).

DIRECTION OF EXPORTS

Ten leading export partners of individual countries during 1970-84 are shown in Appendix A. While I will concentrate on these countries, my observations and comments will not be restricted to these countries only. Burma is excluded because of lack of comparable data. The partner countries are ranked in descending order of percentage of exports going to the partners in 1984. Table II-13, derived from Appendix A, summarizes the information for 1984.

The direction of a country's trade is the result of interaction of historical, political, and economic forces. Historically, metropolitan or imperial countries have been an important outlet for exports of colonies and the current direction of trade reflects economic and institutional structures developed during the colonial period. In our cases we find that the United Kingdom appeared as one of the leading export partners of Bangladesh, Burma, India, Pakistan, Sri Lanka, and Malaysia; the U.S.A. of the Philippines; and Pakistan of Bangladesh. However, exports to these former metropolitan countries were declining. For example, the percentage of exports going to the United Kingdom from India fell from 12 percent to 7 percent; from Pakistan from 10 percent to 6 percent; from Malaysia from 7 percent to 3 percent. For Sri Lanka the change was even more dramatic: exports to the U.K. declined from 23 percent to 6 percent. However, exports from Bangladesh to Pakistan increased over the period, perhaps because of the results of

Table II-13 Three Most Important Trading Partners, 1984

	Export Partners	Import Partners
Bangladesh	USA, Belgium, Pakistan	USA, Japan, Singapore
India	USA, Japan, USSR	USA, Japan, USSR
Malaysia	USA, Japan, Singapore	USA, Japan, Singapore
Pakistan	USA, Japan, Iran	USA, Japan, Saudi Arabia
Philippines	USA, Japan, Singapore	USA, Japan, Saudi Arabia
Sri Lanka	USA, Iraq, Egypt	USA, Japan, Saudi Arabia
Thailand	USA, Japan, Netherlands	USA, Japan, Saudi Arabia

Sources: Appendices A and B.

Note: Trading partners are not ranked according to their importance.

complementarity of both economies during the united Pakistan period (1947-71).

Industrial countries were the largest purchasers of exports for the region. Industrial countries as a group absorbed more than 50 percent of the exports of Bangladesh, India, Malaysia, the Philippines, and Thailand; and more than 40 percent of the exports of Sri Lanka and Pakistan. This geographic concentration of exports made the region vulnerable to the cyclical fluctuations of industrial countries. Some alteration of this direction towards other groups of countries can be observed in the tables presented in Appendix A. For example, 93 percent of exports from Thailand, 90 percent from the Philippines, and 60 percent from Burma went to industrial countries in 1973. By 1984 the numbers had fallen to 57 percent from Thailand, 73 percent from the Philippines, and 22 percent from Burma. There are a few exceptions also. An increasing percentage of Pakistan's exports went to towards industrial countries. Trade with centrally planned economies was at best minimal, except for India and, to a lesser extent, Bangladesh. The centrally planned economies, including the U.S.S.R., absorbed almost one-fifth of India's exports.

Exports from the region to the western hemisphere (excluding the United States) was insignificant, and to Africa was small. Only Bangladesh, Pakistan, and recently Burma exported in any significant amount to Africa. Export to Middle-Eastern countries grew substantially for some South Asian countries, especially Pakistan,

Bangladesh, and Sri Lanka. Intra-regional trade among the countries of the study was low. For example, 4 percent of the Philippines exports went to Malaysia in 1982, 4 percent from Malaysia to India, and 9 percent from Sri Lanka to Pakistan.

As for other points of interest, the United States emerged as the top export partner for five countries: Bangladesh, India, the Philippines, Sri Lanka, and Thailand. The Philippines sent almost 40 percent of its exports to the U.S.A. Over the study period, exports from the Philippines to Japan declined from 40 percent to 20 percent. The emergence of Iran as the top export partner of Pakistan was striking. In 1970, only about 1 percent of Pakistan's export went to Iran; by 1984, that number rose to 10 percent. India's dependence on planned economy countries for export markets has already been mentioned.

ORIGINS OF IMPORTS

Ten leading import partners of each country are shown in Appendix B, where countries are listed with their importance in the latest year shown. Burma is again excluded for lack of comparable data. Table II-13 again present summary information of Appendix B. One of the main features of the sources of imports of the region is the dependence on industrial countries. In 1984 at least 40 percent of imports of each country came from industrial countries. It is

hardly surprising that industrial countries were major import partners since developing countries usually import a large amount of capital goods and raw materials for their development purposes from industrial countries. However, there appeared to be a trend to replace industrial countries with other countries as sources of imports. For example, in 1970 more than 75 percent of imports to Thailand, the Philippines, and Pakistan came from the industrial countries; in 1984, less than 60 percent. However, the proportion of Malaysian imports coming from industrial countries rose. Sixty-four percent of Malaysian imports came from industrial countries in 1984, as against 52 percent in 1970.

The oil-exporting countries emerged as major import partners for many countries, for the obvious reason that oil prices rose. The Philippines, Pakistan, and Sri Lanka increased their imports from oil-exporting countries significantly during 1970-84. However, imports to Malaysia (net oil producer) and Burma and Bangladesh (poorest countries) remained relatively stable.

Perhaps more significant in the long run was the striking increase in the imports from the non-oil exporting countries. For Pakistan, the Philippines, and Thailand the increase was dramatic. Imports from the planned economy countries, including the U.S.S.R., declined. They continued to fall for the Philippines, Pakistan, Malaysia, and India during 1970-84. For Bangladesh and Burma, they fell till 1980, then rose slightly. The centrally planned economy

countries as a source of imports were significant to only India and Burma and, to a lesser extent, to Bangladesh.

Like exports, imports from Africa, the Western Hemisphere (excluding the United States), and other European countries were insignificant. Only Burma imported in any significant amount from these regions. Imports from Middle Eastern countries continued to rise till 1980, whereupon they fell. For all countries, the increase in imports from the Middle-Eastern countries was dramatic. Imports from other Asian countries rose for Bangladesh, the Philippines, Sri Lanka, and India; remained stable for Malaysia; and declined for Pakistan.

India appeared as one of the ten import partners of Bangladesh and Sri Lanka. Imports from India were high in 1972-73 in Bangladesh, and in 1970-72 and 1978-79 in Sri Lanka. Similarly, Malaysia appeared as one of the ten import partners of Thailand, the Philippines, and Pakistan. The importance of imports from Malaysia to Thailand and Pakistan rose in recent years. Thailand also appeared as one of the ten import partners of Malaysia.

As for individual countries, Japan was the top import partner in 1984 for Bangladesh, Malaysia, Pakistan, Sri Lanka, and Thailand. The U.S.A. was the top partner for the Philippines and India. Some curiosities may be mentioned here. During 1972-84, Singapore emerged as an important import partner for Bangladesh. From 1 percent in

1972, imports from Singapore went up to 12 percent in 1984. Imports from the U.S.A. to India declined substantially between 1970-84. From 29 percent in 1970, they dropped to 12 percent in 1984. A similar pattern can be seen in Pakistan's imports from the U.S.A. Imports from former colonial powers were declining, and the decline was sharp for Sri Lanka and Malaysia. Saudi Arabia emerged as a major import partner for many countries.

The main feature of the geographic composition of trade was that the industrial countries, led by the U.S.A. and Japan, were the major trade partner for our countries. However, developing countries were slowly gaining importance. Increased trade with developing countries may be an viable alternative for our countries if developed country markets fail to expand or protectionist measures are not restrained.

CHAPTER III

SERVICES AND TRANSFER PAYMENTS

For a representative picture of the evolution of the BOP patterns, the analysis must extend to the services and the transfer payments accounts, collectively known as the invisible account. In most analyses of the BOP problem of developing countries, the invisible account, particularly the Other Goods, Services, and Income Accounts (services account), receive less attention than the merchandise trade account. There are a number of reasons for this tendency to avoid the invisible account. First, it is argued that reliable, detailed, and consistent statistics on many items of the invisible account are not available. In fact, the major reason for global discrepancies in current accounts mainly arises from the discrepancies in the services and the transfer payments accounts.[1] Some items in these accounts "are invisible literally as well as metaphorically, and the further back in time the analysis reaches the

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[1]A troublesome aspect of the global analysis of the payments problem is that, although in principle the world current account balance should sum to zero, in reality, it climbed to $20 billions in the late 1970s from an approximate balance in the early 1970s. It reached a record high of $107 billions in 1982 before receding in the mid-1980s. A Working Party commissioned by the IMF finds that the greatest discrepancies are in the services accounts, particularly in statistics on portfolio income, followed by shipping. Another area of major discrepancy is the official transfers account. See Shuja Nawaj, "Why the World Current Account Does Not Balance," Finance and Development (September 1987), pp. 43-45 and IMF, World Economic Outlook (Washington, D.C.: World Bank, April 1987), pp. 103-106.

less visible the 'invisible' part of the balance of payments is."[2] The extent of the poor quality of data is not confined to the invisible account only; it is a part of a more general problem of the quality of data available on all accounts of the BOP of developing countries. Consequently, results of the present chapter should be taken as indicative, not conclusive. Second, items in these accounts are normally considered less volatile from year to year than are items in the trade account and that these therefore do not reflect cyclical fluctuation unless the fluctuation is extreme. However, over the long run the trends in the services and the transfer accounts can influence the payments problem as much as the trade account.

CONCEPTUAL PROBLEM OF DEFINING SERVICES

Trade in services has become increasingly important in recent years, but issues relating to it remain as complex and heterogeneous as before. The difficulty starts with the lack of a general consensus on the definition of services. Some define it as "the goods that can not be stored, re-used, or transported,"[3] while others prefer to list the activities that they consider to be services

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[2]A. E. Holmans, "Invisible Earnings" in D. J. Robertson and L. C. Hunter (eds.), The British Balance of Payments (London: Oliver & Boyd, 1966), p. 43.

[3]UN, World Economic Survey, 1986: Current Trends and Policies in the World Economy (New York: UN, 1986), p. 94.

(instead of providing a definition), and thus avoid the problem of definition. A broad list of such activities will include banking; transportation and communication; construction and engineering; tourism; and professional and technical services.[4] The diverse nature of the services transactions, together with the paucity of data, make it difficult to study the underlying patterns of international trade in services.

The importance of the services transactions in the BOP analysis varies depending on which definition of services is adopted. If it is narrowly defined to include shipping, passenger services, and other private transactions, services amounted to 12 percent of the value of the world merchandise trade in 1980.[5] However, if it is broadly defined as services narrowly defined plus travel, port services, and direct and other investment income, then services amounted to 39 percent of the value of the world merchandise trade.[6] Thus, "depending on the definition chosen, international service transactions vary by a factor of three, and in case of the world's largest exporter, the United States of America, the variation is by a

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[4]UNCTAD lists following 18 core service sectors: accounting; advertising; air transportation; automobile and truck rental and leasing; banking; building, construction and engineering; communications; computer services; educational employment; equipment leasing; franchising; health; hotel and motel; insurance; legal; maritime transportation; and motion pictures; See UNCTAD, Production and Trade in Services: Polices and their Underlying Factors Bearing Upon International Service Transactions (New York: UN, 1985), p. 20f.

[5]Ibid., p. 21.

[6]Ibid., p. 21.

factor of over seven."[7] In order to be consistent with previous chapters, we will follow the broad definition as used by the International Monetary Fund.

STRUCTURE OF THE SERVICES ACCOUNTS

In 1984 world services exports totalled $724 billions, while merchandise exports totalled $1,700 billions. Over the past seventeen years the share of world services exports in total trade remained almost the same. As expected, industrial countries are the major exporters of services. However, their dominant position is slipping slowly. For example, industrial countries accounted for 74 percent of the world services exports in 1984 compared to 81 percent in 1975.[8] Developing countries accounted for only 26 percent of the world services trade in 1984, despite a remarkable 27 percent average growth rate per year over the previous decade.[9]

Although the merchandise trade (13 percent) and the services trade (14 percent) grew at almost the same rate in the world during 1970-85, individual countries in our case went through different

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[7]Ibid., p. 21.

[8]Jeffery J. Schott and Jacqueline Mazza, "Trade in Services and Developing Countries," Journal of World Trade Law (May:June 1986), p. 256.

[9]Ibid., p. 256.

experiences. The growth in the services trade (credits + debits) was higher than the growth in the merchandise trade (exports + imports) for all countries, except Thailand (where the difference was negligible) as is shown in Table III-1. The countries are ranked in descending order of the value of the differences between growth in merchandise and services trade. The growth in the services trade was the highest for Malaysia, which also had the highest growth in the merchandise trade. Burma had the lowest growth in services trade as well as in the merchandise trade.

Table III-2 shows the credits, debits, and credits plus debits for services as percentages of GDP during 1970-85. The countries are ranked in descending order of the 1985 values. Services credits as a percentage of GDP increased for all countries during 1970-85. Services debits expressed as a percentage of GDP also showed a rising trend, but did not rise as much as the ratios of services credits to GDP did. Based on the importance of services trade we can classify the countries into two categories. Three Southeast Asian countries and Sri Lanka belong to one category, where the values of services trade averaged 22 percent of GDP. Services trade as percentages of GDP doubled for these countries during the study period. Four South Asian countries belong to the other category, where values of services trade averaged 6 percent of GDP. Services trade was thus important for Southeast Asian countries, perhaps because of higher level of per capita income.

Table III-1 Annual Average Growth in Total Merchandise and Services Trade (credits + debits), 1970-85

	Growth in Merchandise Trade 1	Growth in Services Trade 2	Difference 2-1
Philippines	10.58	16.47	+5.89
Bangladesh[a]	8.38	12.21	+3.83
Malaysia	15.91	19.44	+3.53
Sri Lanka	10.89	14.02	+3.13
Pakistan[b]	14.16	15.98	+1.82
India	13.07	14.23	+1.16
Burma	7.60	8.69	+1.09
Thailand	15.27	15.07	-0.20

Source: Computed from IMF, International Financial Statistics (Washington, D.C.: IMF, various issues).

Notes: [a]Growth rate for 1973-85; [b]Growth rate for 1972-85.

Table III-2 Services Credits and Debits as Percentages of GDP, 1970-85

	1970[a]	1975	1980	1985
Services Credit as Percentages of GDP				
Philippines	3.6	5.6	6.3	10.1
Malaysia	4.8	4.5	8.0	8.5
Thailand	7.4	5.6	5.2	8.3
Sri Lanka	1.7	2.1	6.9	5.5
Pakistan	1.9	2.6	3.0	3.2
India	0.7	1.1	2.4	2.0
Bangladesh	1.1	0.7	2.2	1.7
Burma	0.5	0.8	1.1	1.0
Services Debits as Percentages of GDP				
Malaysia	11.9	10.7	18.9	22.2
Sri Lanka	4.2	3.7	10.5	11.2
Philippines	5.5	6.0	7.4	9.7
Thailand	4.9	5.7	7.5	9.2
Pakistan	4.9	5.3	5.1	6.2
Bangladesh	2.4	2.1	4.3	3.8
India	1.6	1.6	2.2	2.7
Burma	2.4	1.1	2.3	2.3
Services Credit + Debit as Percentages of GDP				
Malaysia	16.7	15.2	26.9	30.7
Philippines	9.1	11.6	13.7	19.8
Thailand	12.3	11.3	12.7	17.5
Sri Lanka	5.9	5.8	17.4	16.7
Pakistan	6.8	7.9	8.1	9.4
Bangladesh	3.5	2.8	6.5	5.5
India	2.3	2.7	4.6	4.7
Burma	2.9	1.9	3.4	3.3

Source: Computed from IMF, International Financial Statistics and Balance of Payments Yearbook (Washington, D.C.: IMF, various issues).

Notes: [a]1972 for Pakistan and 1973 for Bangladesh.

The countries with higher ratios of services credits or debits to GDP also had higher ratios of exports or imports to GDP. The rank order correlation coefficients between the ratios of exports to GDP and the ratios of services credits to GDP was 0.79. The correlation was even stronger (0.86) for the ratios of imports to GDP and services debits to GDP. The strong correlation coefficients supports the commonly held view that services transactions rise as merchandise exports and imports rise.

REASONS FOR RECENT SURGE IN SERVICES TRANSACTIONS

There are a number of reasons for growing attention to international trade in services in recent years. First, of course, is the dramatic increase in 'tradeability' of services, made possible by revolutionary developments in information, communication, and transportation technologies. These inventions have opened up new opportunities for internationally provided services. Second, the interlinkages among production, marketing, and services have increased greatly and resulted in increased demand for services. Third, the integration of the capital markets across countries also contributed to the increased demand for services. A striking shift in the investment income for many countries, and the consequent impact on the BOP, has heightened interest in the services transactions. Fourth, some developing countries--such as India,

South Korea, Brazil--have emerged as exporters of services to other developing countries.

MAJOR COMPONENTS OF SERVICES ACCOUNT

The major components of the services account are presented in Table III-3. The net services balances were consistently negative for all countries, except for a few isolated years for India in the 1980s and Thailand in the 1970s. The highest credit amount for any country was $4 billion for India in 1980, while the highest debit amount was $7 billion for Malaysia in 1985. Malaysia also had the highest deficit in the services account among all countries--$4 billion in 1985.

Shipping

The existence of transport systems, prospects for expansion of trade, and economic development are intimately related. Generally speaking, a "transport system influences economic development but at the same time is influenced by it."[10] That international trade is an

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[10]UNCTAD, Shipping in the Context of Services and the Development Process, Report by the UNCTAD Secretariat, TD/B/1013 (New York: UN, 1984), p. 5.

Table III-3 Structure of Other Goods, Services, and Income Account, 1970-85

	1970[a]	1975	1980	1985	1970	1975	1980	1985
	Bangladesh				**Burma**			
Services Bal.	-77	-147	-263	-353	-40	-10	-68	-84
Credit	65	74	288	280	12	30	66	69
Debit	-143	-221	-551	-633	-52	-39	-134	-153
Shipment Bal.	-86	-146	-289	-259	-5	-3	-9	-5
Credit	0	0	0	2	1	3	13	3
Debit	-86	-146	-289	-261	-7	-5	-22	-8
Other Trans. Bal.	-3	-1	-10	-23	-5	-5	-20	-8
Credit	9	16	39	29	2	4	5	8
Debit	-12	-17	-49	-52	-8	-9	-25	-16
Travel Bal.	-4	-4	0	-23	-1	3	7	6
Credit	2	2	16	23	1	4	10	13
Debit	-6	-6	-16	-46	-2	-1	-4	-7
Investment Bal.	13	-5	7	-112	-4	-7	-47	-70
Credit	17	17	77	42	3	6	14	2
Debit	-4	-21	-70	-154	-7	-14	-61	-72
Other Bal.	2	8	30	64	-25	4	1	7
Credit	37	39	157	184	4	14	23	43
Debit	-35	-32	-128	-120	-29	-11	-22	-50
	India				**Malaysia**			
Services Bal.	-493	-467	523	-1,364	-282	-576	-2,671	-4,296
Credit	378	973	4,028	3,908	190	418	1,968	2,642
Debit	-871	-1,440	-3,505	-5,272	-472	-994	-4,639	-6,928
Shipment Bal.	-166	-379	-1,199	-1,423	-99	-259	-819	-747
Credit	83	209	370	422	2	29	200	352
Debit	-249	-588	-1,568	-1,845	-101	-289	-1,019	-1,099
Other Trans. Bal.	-10	-89	-263	-433	-7	40	-26	25
Credit	69	112	113	137	24	137	372	457
Debit	-79	-200	-376	-570	-31	-96	-398	-432
Travel Bal.	14	172	1438	533	-35	-44	-406	-538
Credit	39	197	1551	887	10	144	317	621
Debit	-25	-24	-113	-354	-45	-188	-724	-1,159

Table III-3 Continued

	1970[a]	1975	1980	1985	1970	1975	1980	1985
Investment Bal.	-297	-256	561	-801	-116	-230	-836	-2,309
Credit	63	130	1,056	525	77	137	739	591
Debit	-362	-386	-495	-1,326	-193	-368	-1,575	-2,900
Other Bal.	-32	181	-18	760	-25	-51	-584	-717
Credit	124	325	935	1,937	77	3	339	621
Debit	-156	-242	-953	-1,177	-102	-53	-923	-1,338
	Pakistan				**Philippines**			
Services Bal.	-186	-297	-498	-952	-81	-45	-413	106
Credit	120	302	731	995	258	910	2,209	3,297
Debit	-306	-599	-1,230	-1,947	-399	-955	-2,621	-3,191
Shipment Bal.	-74	-208	-462	-510	-78	-302	-467	-174
Credit	1	1	8	40	29	23	100	167
Debit	75	-209	-470	-550	-107	-325	-567	-341
Other Trans. Bal	7	73	161	186	-13	37	-87	-1
Credit	42	127	268	357	8	67	105	38
Debit	-35	-54	-107	-171	-21	-30	-193	-39
Travel Bal.	-12	-16	64	-25	68	83	215	473
Credit	11	33	148	184	95	110	320	510
Debit	-23	-49	-85	-209	-27	-27	-105	-37
Investment Bal.	-90	-128	-272	-419	-130	-126	-832	-2,003
Credit	10	37	86	117	10	171	341	360
Debit	-100	-164	-358	-537	-140	-296	-1,173	-2,363
Other Bal.	-17	-18	10	184	12	263	629	1,811
Credit	56	105	221	297	116	540	1,342	2,222
Debit	-73	-123	-211	-481	-104	-277	-583	-411
	Sri Lanka				**Thailand**			
Services Bal.	-56	-62	-146	-339	163	-24	-760	-372
Credit	40	80	279	328	485	817	1,749	3,164
Debit	-96	-142	-424	-667	-322	-842	-2,509	-3,536
Shipment Bal.	-39	-77	-199	-162	-122	-309	-867	-756
Credit	1	2	4	11	15	61	189	340
Debit	-40	-79	-203	-173	-137	-370	-1,056	-1,096

Table III-3 Continued

	1970[a]	1975	1980	1985	1970	1975	1980	1985
Other Trans. Bal.	10	18	10	-13	5	31	17	0
Credit	14	27	40	63	14	62	118	131
Debit	-4	-8	-30	-76	-9	-32	-102	-131
Travel Bal.	1	16	65	37	43	85	625	-890
Credit	4	18	99	83	104	221	868	1,171
Debit	-3	-2	-34	-46	-61	-136	-243	-281
Investment Bal.	-23	-16	-23	-127	19	5	-570	-1,400
Credit	2	7	47	83	79	192	260	245
Debit	-25	-26	-73	-210	-60	-187	-830	-1,653
Other Bal.	-9	-1	4	-74	218	164	33	902
Credit	33	26	88	88	273	281	314	1,277
Debit	-24	-27	-85	-162	-55	-117	-281	-375

Source: Computed from IMF, International Financial Statistics and Balance of Payments Yearbook (Washington, D.C.: IMF, various issues).

Notes: [a]1972 for Pakistan and 1973 for Bangladesh;

Due to conversion from SDRs to dollars and rounding, there may be some discrepancies and the net amount may not be equal to the difference between credits and debits.

The components of services accounts cover the followings:

(a) "Shipment" covers freight, insurance, and other distributive services performed during the course of shipping.
(b) "Other Trans." = "Other Transportation" covers passenger services, port services, and charters not classified in "shipment" or "travel."
(c) "Travel" includes all tourism receipts and expenditure excluding international transport (e. g., lodging, meals, etc. within the country visited) as well as business travel and student exchange.
(d) "Investment Income" includes income from financial assets.
(e) "Other Bal." = "Other Goods, Services, and Income" covers transactions not included above.

For a detailed discussion about the individual items see IMF, Balance of Payments Manual, 4th edition (Washington, D.C.: IMF, 1977).

"engine of economic growth"[11] is stressed by many; however, the fact that an effectively functioning transport system is a prerequisite for the growth in international trade is often ignored. The importance of shipping for developing countries can be realized if one looks at the commodity composition and the geographic direction of trade of these countries. The export items of developing countries require bulk carrying. Their trade is concentrated on trade with distant countries of North America, Europe, and Japan, and very little with neighboring countries, where land transport may be possible. It is evident from the geographic and the commodity composition of trade of the countries under review, as shown in Chapter II, that exports and imports of these countries, like other developing countries, depend heavily on shipping.

Total freight payments in the world amounted to $90 billions in 1982. In the same year, deficits of developing countries in the seaborne transport balance amounted to $33 billions. Deficit of this magnitude create considerable payments problems for developing countries. Table III-3 shows that shipping constituted the major component of the services account for most countries. In 1985, the share of shipping balance accounted for 80 percent to 200 percent of the services balances for Bangladesh, India, the Philippines, and Thailand; 50 percent for Pakistan and Sri Lanka; and 17 percent and 5

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[11]Dennis H. Robertson was probably the first to say this; see Dennis H. Robertson, "The Future of International Trade," The Economic Journal (March 1938), pp. 1-14.

percent for Malaysia and Burma. One common pattern, which is consistent with the experience of developing countries as a group, is that the shipping balance was consistently negative for all countries for all years. For Bangladesh, Burma, Pakistan, and Sri Lanka, earnings from shipping were very small. For India and Malaysia, and to a lesser extent for Thailand and the Philippines, credits from shipping increased only in recent years.

The reasons for such a poor performance in the shipping transactions are difficult to ascertain. One reason is indicate in Table III-4. The shares in the merchant fleets of the world for these countries were, in six of the eight cases, higher than the shares of goods loaded. Quite the opposite is true for developing countries, which, as a group, generated 37 percent of the world seaborne cargo but owned only 16 percent of deadweight tonnage.[12] Thus lack of shipping capacity cannot be blamed for deficits in the shipping account. The higher shares for India, Malaysia, and the Philippines were probably due to their large domestic coastal trades.

One reason for large deficits in the shipping accounts is the traditional trading practices. "There is a consistent tendency for developing countries to have to accept f.o.b. terms for their exports and C&F terms for their imports. This effectively shuts them out from engaging in downstream export activities."[13] This practice

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[12]UNCTAD, Review of Maritime Transport, 1984 (New York: UN, 1985), p. x.

[13]UNCTAD, Shipping in the Context of Services, p. 16.

Table III-4 Shares in Merchant Fleets of the World by Flag of Registration (gross registered tons) and World Seaborne Trade (metric tons) in Terms of Goods Loaded and Unloaded (Percentages), 1984

	Merchant Fleets[a]	Goods Loaded[a]	Goods Unloaded[b]
Bangladesh	0.089	0.046	0.209
Burma	0.026	0.037	0.016
India	1.490	1.189	1.203
Malaysia	0.403	0.379	0.619
Pakistan	0.123	0.099	0.376
Philippines	0.834	0.415	0.523
Sri Lanka	0.181	0.060	0.167
Thailand	0.125	0.499	0.529

Source: UNCTAD, Review of Maritime Transport, 1984 (New York: UN, 1985) Annex II; UN, Statistical Yearbook for Asia and the Pacific (New York: UN, various issues).

Notes: [a]1983 for Burma and India; [b]1983 for Burma and 1982 India.

causes the incidence of freight to fall adversely on imports as well as on exports of developing countries. Over the years, the situation has remained mostly unchanged for our countries, although some countries now possess a larger shipping capacity. One indication of the extent of the problem can be seen in Table III-5. It shows the difference between c.i.f and f.o.b. import values as percentages of c.i.f. import values. Bangladesh, India, and the Philippines were able to reduce cost, insurance, and freight share of imports but only India was able to reduce the share significantly. For other countries, the share remained remarkably stable throughout the period.

Further, the level and the structure of freight rates are also weighted against the developing countries. For example, the index of liner freight rates increased from 100 in 1965 to 321 in 1982 and 407 in 1983.[14] This not only adversely affects the shipping account, but it also affects the merchandise trade account indirectly. Higher freight rates cause export prices to rise and thereby make exports of developing countries less competitive, with a consequent adverse impact on the merchandise trade account. On the other hand, imported goods are needed for development purposes so that any shortage of developmental goods, resulting from higher imports prices, have detrimental effects on the economy. Summarizing an UNCTAD study, Alexander J. Yeats states that "an ocean freight

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[14]UNCTAD, Review of Maritime Transport, 1984, Table 21, p. 40.

Table III-5 Differences Between C.I.F. Imports and F.O.B. Imports as Percentages of C.I.F. Imports, 1970-84

	1970[a]	1975	1980	1984
Bangladesh	12.20	11.07	10.00	9.97
Burma	9.10	9.09	9.09	9.09
India	15.12	11.65	10.46	10.47
Malaysia	7.16	8.46	9.84	9.58
Pakistan	7.83	8.67	8.68	8.68
Philippines	9.91	7.91	6.85	7.82
Sri Lanka	9.98	9.99	10.00	10.00
Thailand	9.79	9.65	10.07	9.88

Source: Computed from IMF, International Financial Statistics (Washington, D.C.: IMF, various issues).

Notes: [a]1972 for Bangladesh and Pakistan; C&F for Bangladesh.
C.I.F. = Cost, Insurance, and Freight
F.O.B. = Free on Board

rate which caused even a 2 percent export price disadvantage for a particular product might inhibit growth of the producing industry."[15] Table III-6 indicates the extent of this problem. The table, of liner freight rates as percentages of prices of selected commodities, shows, for instance, that jute, a major export item from Bangladesh, carried a burden of 21 percent in 1984.

Other Transportation

Bangladesh, Burma, and India registered deficits in the "other transportation" (passenger services, port services, and charters not classified in shipping or travel) account in all years. The amount of deficits were small for Bangladesh and Burma, although it rose rapidly over the period. For India, the increase in the deficit was the most dramatic: it increased from a low of $10 millions in 1970 to a high of $400 millions in 1985. Except for a few years in the mid 1970s, both Malaysia and the Philippines experienced deficits in this account. Sri Lanka, Thailand, and Pakistan registered surpluses in this account over the study period. Sri Lanka's surplus, which was small, was largely due to net earnings from port services. Pakistan's surplus was only $7 millions in 1972, but it did increase to $186 millions in 1985.

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[15]Alexander J. Yeats, Trade Barriers Facing Developing Countries: Commercial Policy, Measures, and Shipping (Great Britain: Macmillan Press, 1979), p. 178; and UNCTAD, Level and Structure of Freight Rates, Conference Practices, and Adequacy of Shipping Services (New York: UN, 1969), p. 94.

Table III-6 Ratio of Liner Freight Rates to Prices of Selected Commodities, 1970-1984

Commodity	Route	1970	1980	1984
Rubber	Singapore/Malaysia-Europe	10.5	8.9	5.9
Tin	Singapore/Malaysia-Europe	1.2	1.0	0.9
Jute	Bangladesh-Europe	12.1	19.8	21.4
Coconut Oil	Sri Lanka-Europe	8.9	12.6	11.0
Tea	Sri Lanka-Europe	9.5	9.9	8.1

Source: UNCTAD, Review of Maritime Transport (New York: UN, various issues).

Travel

The travel account provides an important source of foreign exchange earnings for several countries (Table III-3, pages 74-76), contributing positively to the services account for Thailand, Sri Lanka, the Philippines, India, and Burma but negatively to the accounts of the other countries. International tourism played an important role in many countries. In 1985, the shares of travel credits in total import values ranged from 6 to 13 percent for the Philippines, Sri Lanka, and Thailand. Table III-7 indicates that the contribution of travel credits went up dramatically for all the countries, except the Philippines, where the political disturbances may have discouraged tourists. While the importance of travel credits doubled for all countries during 1970-85, it fell more than two-fold for the Philippines. In 1985, travel credit accounted for one-sixth of services credits all countries, except Bangladesh, and to more than one-fifth for half of the countries.

International tourists mainly came from the industrial countries, particularly from the United States, the United Kingdom, Japan, Australia, Germany, and France.[16] A large percentage of tourists to Bangladesh and Sri Lanka came from India, while a significant percentage of tourists to India came from Sri Lanka.

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[16]United Nations, Statistical Yearbook for Asia and the Pacific (New York: UN, various issues).

Table III-7 Travel Credits as Percentages of Other Goods, Services, and Income Credits, 1970-85

	1970[a]	1975	1980	1985
Thailand	21.4	27.1	49.6	37.0
Sri Lanka	10.0	22.5	35.5	25.1
Malaysia	5.3	34.4	16.1	23.5
India	10.3	20.2	38.5	22.7
Burma	8.3	13.3	15.2	18.9
Pakistan	9.2	10.9	20.2	18.5
Philippines	36.8	12.1	14.5	15.5
Bangladesh	3.1	2.7	5.6	8.3

Source: Computed from IMF, Balance of Payments Yearbook (Washington, D.C.: IMF, various issues).

Notes: [a]1973 for Bangladesh and 1972 for Pakistan.

There also appeared to be a large tourist movement between Thailand and Malaysia.

Investment Income

Table III-3 (pages 74-76) also shows the contribution of investment income to the services account. All countries in our study experienced deficits on investment income account, a pattern common to developing countries in general. For Thailand there was a small surplus early in the 1970s; and for Bangladesh in 1973 and in the 1980s. The debits in investment income account was an important reason for deficits in the services accounts. This is evident in Table III-8, which shows the investment debits as percentages of services debits. The countries are ranked in descending order of the 1985 values. In 1985, the share of investment income debits accounted for one-fourth to three-fourth of services debits. In most countries a rising trend in debits could be observed. For Sri Lanka, the Philippines, and Pakistan it rose after an initial decline. For India it fell from 42 percent in 1970 to 14 percent in 1980, and then climbed to 25 percent in 1985. For Malaysia, it remained almost the same, although it declined slightly in 1980.

The only startling changes in rank order were India and Burma. The major changes in the share of investment debits in services were for the Philippines, Burma, Thailand, and Bangladesh (all up), and India down.

Table III-8 Investment Income Debits as Percentages of Other Goods, Services, and Income Debits, 1970-85

	1970[a]	1975	1980	1985
Philippines	35.9	31.0	44.8	74.0
Burma	13.5	35.9	45.5	47.1
Thailand	18.6	22.2	33.1	46.7
Malaysia	40.9	37.0	34.0	38.2
Pakistan	32.7	27.4	29.1	37.0
Sri Lanka	26.0	18.3	17.2	31.5
Bangladesh	2.8	9.5	12.7	24.3
India	41.6	26.8	14.1	25.1

Source: Computed from IMF, Balance of Payments Yearbook (Washington, D.C.: IMF, various issues).

Notes: [a]1973 for Bangladesh and 1972 for Pakistan.

Other Balances

The catch-all category "Other Balances" covers the transactions not classified elsewhere. Bangladesh, Thailand, and the Philippines registered surpluses in this account over the study period. For Bangladesh and Thailand the surpluses were small. For the Philippines, the surplus rose sharply from $12 millions to $1,811. On the other hand, Malaysia went through just the opposite experience; its deficit rose quite sharply from $25 millions to $717 millions. Pakistan and Burma registered small deficits in the early part of the 1970s and surpluses in the remaining period. For India and Sri Lanka, net balances were in surpluses in some years and deficits in other years.

The major points of this section can now be summarized. The growth in services trade was rapid in our countries and exceeded growth in merchandise trade (except for Thailand). The values of services trade as percentages of GNP were higher for the three Southeast Asian countries and Sri Lanka than for the other four countries of South Asia. Shipping accounted for the most deficits in the services balance in six countries (but not in the balances of Malaysia and Burma) despite growing domestic shipping capacity. This may be an indication that traditional shipping practices and charges were detrimental to the services balances of our countries. Travel accounts show encouraging trends in five countries. All countries experienced deficits in investment income, again a pattern common to

developing countries. Overall the services trade contributed negatively to the external payments problems of our countries.

DIRECTION OF SERVICES TRADE

While statistics on the direction of merchandise trade are readily available from the standard sources, no such statistics can be found for trade in services. All we can say is that the industrial countries were the main suppliers of services to the developing countries, and that a few developing countries (such as India, Korea, Taiwan, Brazil) were also emerging as suppliers of services to developing countries.

UNREQUITED TRANSFER PAYMENTS

There are two broad types of transfer accounts, namely, private and official. Both accounts played important roles for several countries of our study. Unfortunately, a further breakdown of these accounts is not possible because statistics on individual items are not available for all countries. Therefore our analysis can deal only with the broad categories of private and official transfer payments. For private transfers, the major item was remittance earnings; migrants' earnings or other types of earnings were virtually nil or insignificant. Consequently we will use both

the terms (private transfers or remittance earnings) in our analysis since quantitative differences between them are insignificant. The remarks about on official transfer payments will be brief since, again, detailed information is not available. However in chapter V I shall discuss in detail the patterns of official flow when discussing the financing of the BOP.

Private Transfers

Table III-9 shows net private, official, and total transfer payments for individual countries during 1970-85, where countries are ranked in descending order of the 1985 values. Private transfer payments, mainly remittances of earnings, show two clear patterns. First, their contribution to the BOP was negligible for the Southeast Asian countries and Burma. The highest amount received by the Philippines was $323 millions in 1982. For Malaysia, where the net amount was small, outflow was actually larger than inflow for most of the time, except for a few years in the 1980s. This was to be expected since Malaysia hosts migrant labor from other countries, particularly from Thailand.

The second pattern can be seen in the four South Asian countries, where remittances rose to a significantly higher level in the 1980s from a low level in the 1970s. Table III-10 shows remittances as percentages of exports and imports. By 1985 Pakistan's remittance earnings exceeded its export earnings and paid

Table III-9 Net Unrequited Transfers Payments, 1970-85

	1970[a]	1975	1980	1985
	Net Private Transfers			
Pakistan	133	276	2,219	2,709
India	162	535	2,743	2,475
Bangladesh	23	31	301	450
Sri Lanka	-1	3	136	266
Philippines	29	166	230	181
Thailand	3	66	75	47
Burma	1	2	7	6
Malaysia	-65	-67	43	-46
	Net Official Transfers			
Bangladesh	251	379	765	655
Pakistan	46	128	233	355
India	79	195	590	324
Philippines	90	154	135	207
Sri Lanka	13	77	136	175
Thailand	46	24	142	119
Burma	17	15	73	74
Malaysia	6	15	22	19
	Net Total Transfers			
Pakistan	179	404	2,452	3,064
India	260	746	3,347	2,799
Bangladesh	274	410	1,066	1,105
Sri Lanka	12	80	272	411
Philippines	119	320	365	388
Thailand	49	90	217	166
Burma	18	17	80	80
Malaysia	59	-52	65	-27

Source: IMF, Balance of Payments Yearbook (Washington, D.C.: IMF, various issues).

Notes: [a]1973 for Bangladesh and 1972 for Pakistan.

Table III-10 Remittances as Percentages of Exports and Imports, 1970-85

	1970[a]	1975	1980	1985
	Remittances as Percentage of Exports			
Pakistan	20.6	26.3	86.4	102.3
Bangladesh	6.4	9.6	37.4	45.0
India	8.6	11.5	33.0	26.1
Sri Lanka	0.3	0.5	12.8	20.4
Philippines	2.7	7.3	4.0	3.9
Burma	0.9	1.2	1.6	1.9
Thailand	0.4	3.0	1.0	1.0
Malaysia	-4.0	-1.8	0.3	-0.3
	Remittances as Percentage of Imports			
Pakistan	15.0	12.5	40.8	46.1
Bangladesh	2.6	2.6	12.8	19.7
India	8.0	10.8	19.0	16.4
Sri Lanka	0.3	0.4	7.4	13.6
Philippines	2.3	4.8	3.0	3.5
Burma	0.6	11.6	0.9	1.2
Thailand	0.3	2.3	5.4	1.0
Malaysia	-5.0	-1.9	0.4	-0.4

Source: Computed from IMF, Balance of Payments Yearbook (Washington, D.C.: World Bank, various issues).

Notes: [a]1973 for Bangladesh and 1972 for Pakistan.

half of the import bill. This amounted to a five fold increase in the percentages of its exports and a three fold increase in the percentages of its imports after 1972. For Bangladesh, remittance earnings (45 percent of exports values and 20 percent of imports values in 1985) increased seven fold as percentages of the values of exports and of imports in 1973. For India these earnings tripled to 26 percent of its exports and more than doubled to 11 percent of its import values in 1985, up from 9 percent and 8 percent in 1970. These statistics show that in the absence of remittances, our countries would have faced much more severe payments difficulties. Table III-10 also shows the relative insignificance of private transfers in terms of exports and imports for Southeast Asian countries and Burma.

A shift in the traditional sources of remittance earnings can be seen for several countries in the early part of the 1970s. Before 1973, the main source of remittance earnings for Bangladesh, Pakistan, and India were the United Kingdom. However, after 1973 oil exporting Middle Eastern countries became the main source of remittances for these countries. A general expansion of economic activity in the Middle Eastern oil exporting countries in the 1970s required a larger number of migrant laborers. The South Asian countries, mainly Pakistan and India but to a lesser extent Bangladesh, sent large numbers of laborers as early as 1975.[17] While

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[17]Ibid., p. 699.

South Asian countries continued to send an increasing number of workers, other Asian countries (Thailand, the Philippines, Korea, and Taiwan) also increased their presence in the Arab world toward the end of the past decade.[18]

Clearly the number of migrants abroad and their wages are the most important determinants of remittance flows. These, in turn, depend both on the absolute level of and cyclical fluctuations in the economic activities of the host countries.[19] Some economists believe that since the economies of oil exporting countries are heavily dependent on oil revenues, the recent fall in oil prices will definitely reduce the demand for migrant workers, and hence earnings from remittances can be expected to fall in future. Some economists argue that "the period of phenomenal rates of growth in remittances is probably over" for most of the countries.[20] Still others believe that while the decline in oil price is detrimental to the continued inflow of remittances, the demand for migrant workers will still rise in future because "investment set in place will generate a continued

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[18]Ibid., p. 699.

[19]G. Swamy, "International Migrant Worker's Remittances: Issues and Prospects," World Bank Staff Working Papers, no. 481 (Washington, D.C.: World Bank, 1981)

[20]See Sharon Stanton Russel, "Remittance from International Migration: A Review in Perspective," World Development, vol. 14, no. 6 (1986), p. 680; J. S. Birks and C. A. Sinclair, "Migration and Development: The Changing Perspective of the Poor Arab Countries," Journal of International Affairs, vol. 33, no. 2 (1979), pp. 285-309.

demand for labor as a crucial input"[21] and, therefore, the inflow of remittances is probably not going to fall.[22]

While remittance flows may be declining for developing countries as a group, we can not say the same thing for our countries since the pattern of remittances appears to be upward. Bangladesh earned the highest amount in 1983; Pakistan and the Philippines in 1982. For India the highest amount received was in 1980. It did fall for a couple of years, but then picked up again in 1983. Sri Lanka experienced the highest amount of transfer receipts in 1984.

The effect of remittances on the BOP was positive for developing countries--especially for three and perhaps for five of our countries--but no general consensus can be found about the effects of remittances on the domestic economy. Studies on this aspect of the flow of remittances show that cash remittances were largely spent on unproductive personal consumption, social ceremonies, and real estate.[23] Some studies even pointed out that

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[21]Nazli Choucri, "The Hidden Economy: A New View of Remittances in the Arab World," World Development, vol. 14, no. 6 (1986), p. 699.

[22]Naiem A. Sherbiny, "Labor and Capital Flows in the Arab World: A Critical View," Finance and Development (December 1984), pp. 34-74.

[23]For a review of the literature emphasizing the negative aspect of the remittances, see Anand B. Chandavarkar, "Use of Migrant's Remittances in Labor Exporting Countries," Finance and Development (June 1980), pp. 36-39. Also, I. Gilani, M. F. Khan, and M. Iqbal, Labor Migration from Pakistan to the Middle East and its Impact on the Domestic Economy, Final Report, Research Project on Export of Manpower from Pakistan to the Middle East (Washington, D.C.: World Bank, June-July 1981) and Zafer Ecevit and Kunniparampil C.

the remittance earnings caused growing demand for imported consumer goods and thus caused imports to rise.[24] While remittances sent by migrant labor may cause consumer goods imports to rise in labor exporting countries, it is often forgotten that a large migrant labor force also causes exports to host countries to rise. One reason for the dramatic increase in the level and shift in the geographic direction of exports from our countries toward the Middle Eastern countries is the large number of migrant laborers. Further, even if the overall pattern of expenditure was consumption oriented, it "should not be interpreted as being mainly unproductive; in an economy in which levels of living are low, consumption expenditure may often be functional and may induce significant improvements in labor productivity."[25] In addition, expenditure on land (if it involves improving the land) and upon housing also created new jobs in the economy. Thus the net effect of remittances on the domestic economy was definitely positive.

Zachariah, "International Labor Migration," Finance and Development, vol. 15, no. 4 (December 1978), pp. 32-37.

[24]See Ismail Serageldin *et al.*, Manpower and International Labor Migration in the Middle East and North Africa (Oxford: Oxford University Press, 1983).

[25]A. S. Oberai and H. K. Manmohan Singh, "Migration, Remittances, and Rural Development: Findings of a Case Study in the Indian Punjab," International Labor Review, vol. 119, no. 2 (March-April 1980), pp. 236-237. In a different context, Myrdal points out that "in poor countries a change in the levels of living affects the contribution men make to production." See Asian Drama, vol. III, Appendix 2, p. 1912.

Recapturing the main points, private transfers were helpful in financing the trade and services deficits. Two clear patterns emerged: private transfers had only a minor impact on the Southeast Asian countries and Burma, but a marked positive impact on the remaining South Asian countries, particularly India, Pakistan, and Bangladesh. In the absence of private transfers these three countries would have experienced extreme difficulties in maintaining imports. The sudden rise in inflows of private transfers were a new development for these countries. Temporary labor migration from these countries to the oil-exporting countries in the Middle East after the rises in oil prices were the main reason why private transfers, mainly remittance earnings, rose to a dramatic level. While some economists doubt whether remittances will continue to flow toward the developing countries, there is no evidence that this will be the case for our countries.

Official Transfers

The official transfer accounts cover official transactions such as grants of technical assistance and scholarships, subsidies to current and defence budgets, cancellation of debts, governments' contributions to international organizations, and so on. All countries in our study registered surpluses in this account (Table III-9, page 91), a pattern common to developing countries in general. Bangladesh, the country with the lowest per capita GNP, registered the highest surplus; while Malaysia, the country with the highest per

capita GNP, registered the lowest surplus. Official transfer receipts were always higher for Bangladesh than for any other countries in the study. India experienced a rise in transfer receipts during 1980s.

Several major events affected this account for our countries. A debt cancellation by Germany in 1979 helped Bangladesh's surplus to rise substantially in that year: from $363 millions in 1978 it jumped to $821 millions in 1979. A large percentage of Burma's official transfer payments came from Japan as grants and goods received under the Japan-Burma Economic and Technical Cooperation Agreement. India received a substantial amount in the U.S. government Rupee Grant of 1974. India also received grants of various amounts from Canada and the United Kingdom on numerous occasions. A large percentage of official transfer receipts to Pakistan came from the United States. For Pakistan, grants received by the Terbela Development Fund and the Indus Basin Development Fund were registered in this account. The Philippines received reparations from Japan through 1977. A substantial amount of transfer receipts in the Philippines came from the United States as pension funds and grants.

CHAPTER IV

EXPLAINING THE BALANCE OF PAYMENTS PROBLEM

Building on the discussion of the structures of merchandise trade and services and transfer accounts in the last two chapters, this chapter will deal mainly with the nature, causes, and consequences of BOP problems in our countries. But first we will briefly discuss the movements of the trade and current account balances and the implications of development and trade strategies for the BOP problem.

MOVEMENT IN CURRENT ACCOUNT BALANCES

The movement of the current account balance excluding exceptional financing, expressed as percentages of exports (CAX), and the merchandise trade balance, also expressed as percentages of exports (TBX), are shown in Figure IV-1. Several interesting points emerge from this figure. First, there was a remarkable stability in the direction of change in CAX and TBX. Both moved in the same direction for all the countries for almost all years. The main reason for this was the dominant position of the trade balance in the current account balance, a feature common to developing countries in general. Out of a total of 128 observations, there were only five

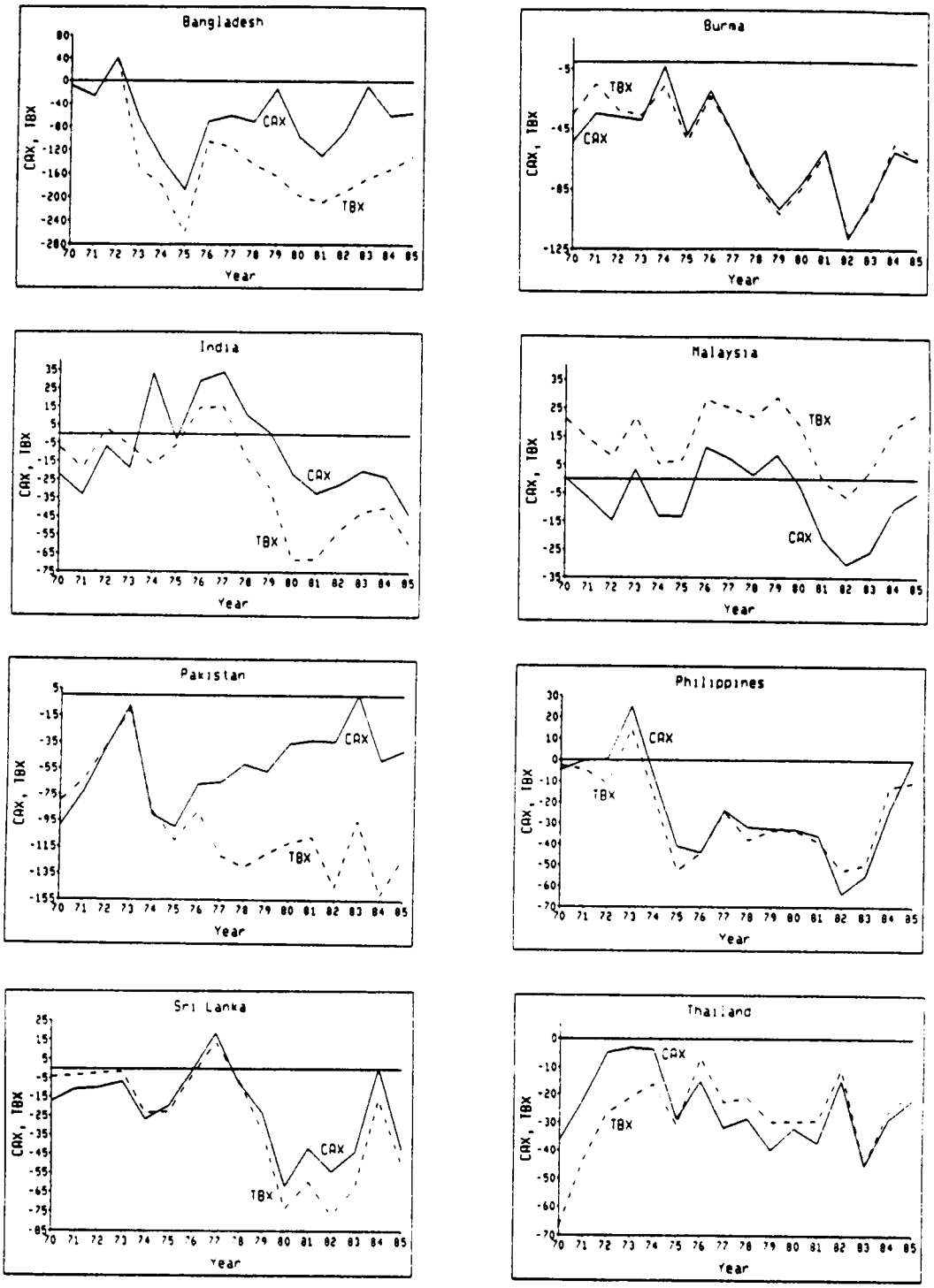

Figure IV-1 Current Account Balance and Trade Balance as Percentages of Exports (CAX and TBX), 1970-85

Source: IMF, International Financial Statistics (Washington D.C.: IMF, various issues).

cases when the current account balance improved while the trade balance deteriorated--twice in Bangladesh and once each in India, Pakistan, and the Philippines. In only 4 cases did the current account balance deteriorate while the trade balance improved--once each in Bangladesh, India, Thailand, and the Philippines. For most of the countries the CAX curve was above the TBX curve, indicating a relatively favorable services and transfer balance--mainly due to remittances from abroad--offsetting an adverse trade balance. There were two exceptions: the TBX curve was above the CAX curve throughout the period for Malaysia, and for Thailand for 1975-85. For four South Asian countries--Bangladesh, India, Pakistan, and Sri Lanka--the difference between the CAX and the TBX widened over the period, but the same did not happen for the Southeast Asian countries. The main reason for the contrast was (as explained in Chapter III) the South Asian countries' success in earning large remittances.

Deficits in the trade and the current account balances appear to be common characteristics of our countries. Burma and Thailand never had trade surpluses during 1970-85. Similarly, Burma, Pakistan, and Thailand never had current account surpluses. Both India and Malaysia experienced current account surpluses during 1976-79. In 1976 and 1977 favorable merchandise trade balances contributed to the current account surpluses for both the countries. However, in 1978 and 1979 India's current account surplus mainly resulted from the surplus in the transfer account. Only rarely did

resulted from the surplus in the transfer account. Only rarely did the Philippines, Sri Lanka, Bangladesh, and Pakistan experience either a trade or a current account surplus during the period.

Based on CAX averages for the period, the countries can be grouped into two categories. The first group includes all Southeast Asian countries and India and Sri Lanka, where CAX deficits averaged between zero and 30 percent. The second group comprises the rest of the South Asian countries, where CAX deficits averaged between 50 and 80 percent. In general, the average TBX deficit was higher than the CAX deficit for the period for all countries except Burma and Malaysia, and Thailand during late 1970s. In Burma, the difference between the CAX and the TBX was small, indicating the insignificance of the services and transfer accounts for the BOP position. In Malaysia, the average TBX was positive but the CAX was negative. Malaysia's results can be largely attributed to its oil exports and Burma's to its oil self-sufficiency.

Movements in the current account balance and the trade balance, both expressed as percentages of GDP and imports, are broadly similar to the movements of TBX and CAX shown in Figure IV-1. Figure IV-1 thus basically summarizes the evolution of the trade and the services and transfer accounts as described in Chapters II and III.

TRADE AND DEVELOPMENT STRATEGIES

"The balance of payments is a synthetic category, and enormous deficits in it are only a mirror in which the true difficulties of a particular development phase and subjective weaknesses and mistakes of a particular economic policy are reflected in aggregate."[1] The BOP pattern of a developing country depends, to some extent, on its long term development and trade strategy. An underdeveloped country undertaking an accelerated development of its economy "almost always faces balance-of-payments difficulties that may last for decades after its initial takeoff."[2] In short, BOP difficulties are typical of the early stage of development effort.[3]

Rapid economic growth has been a priority target of the newly independent developing countries of Asia and Africa in the 1950s and 1960s. They required a large volume of capital goods for a "Big Push", but their export earnings were not sufficient to finance all the capital goods they required. Consequently they relied on foreign aid to fill the "Savings Gap". The strategy made sense since foreign aid was easily available. This strategy has some implications for the BOP position in that, at an early stage of development, a country

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[1]Branko Colanovic, "Balance of Payments Policy," Eastern European Economics, vol. XX, no. 3-4 (Spring-Summer 1982), pp. 121-122.

[2]Ibid., p. 128.

[3]Ibid., p. 127.

may experience deficits in the current account and surpluses in the capital account. The Balance of Payments Stages Hypothesis (discussed in Chapter I) clearly argues along this line.

Foreign trade strategies play a crucial role in determining the BOP position of a country. Broadly speaking, there are two types of trade strategy, namely, import-substitution and export promotion. Import-substitution, which is also known as an inward-looking strategy, attempts to replace imported goods with domestic sources of production behind protective tariff and non-tariff barriers. Import-substitution policy is justified on the basis of the infant-industry argument. However, critics of import-substitution policy point out that benefits from this strategy are questionable because, in most cases, it causes negative impacts on the economy and the BOP position of a country. On the import side, import-substitution policy leads only to a shift in the composition of imports instead of to reductions in imports; and, far from removing the dependence on imports, it causes countries to depend more on imports. On the export side, goods produced in the import-substitution industries "are hopelessly uncompetitive in the world market"[4] and thus can not be exported. More importantly, artificially overvalued home currency discourages agricultural output and both traditional and nontraditional exports. In these circumstances, "any attempt to accelerate growth thus faces increased imports beyond the likely

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[4]Tibor Scitovsky, "Comments on Adelman," World Development, vol. 12, no. 9 (September 1984), p. 953.

growth of exports."[5] An external payments problem may evolve from these characteristics of import-substitution industrialization.

In contrast to an import-substitution strategy, an export promotion strategy (also known as an outward-looking strategy) eliminates bias against exports and encourages--through pricing policies and incentives--exports, particularly of nontraditional commodities in which the country has a potential comparative advantage. An export promotion strategy may have a favorable impact on the BOP, but critics point out that an export promotion policy may generate little benefit in the long run because the price and income elasticities of demand for the primary and light manufacturing exports of developing countries (the major export items from these countries) are relatively low. Further, these commodities usually face threats of protectionist measures in industrial countries. Thus export promotion policy may not be "conducive to growth because external factors can or will exert constraining influences."[6]

The implications of trade strategy for the BOP position of a country become important in the case of external shocks. While the immediate impact of may be higher in the outward-looking countries than the inward-looking countries, the outward-looking countries can

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[5]Malcom Gills *et al.*, Economics of Development, 2nd edition (New York: W. W. Norton & Company, 1987), p. 451.

[6]Hans W. Singer and Patricia Gray, "Trade Policy and Growth of Developing Countries: Some New Data," World Development, vol. 16, no. 3 (March 1988), p. 395.

adjust more quickly than the inward-looking group in responding to external shocks. Consequently, adjustment costs, in the sense of forgone potential output, in response to external shocks are lower in the outward-oriented countries. Taiwan's and Korea's experiences in the 1970s clearly support this view.[7] According to Balassa, writing about the years 1974-78, the BOP effect of external shocks--expressed as percentages of GDP--was 7.5 percent for outward-looking countries in contrast to 3.8 percent for inward-looking countries.[8] However, during the same period, the export market shares of outward-looking countries experienced an average gain of 14 percent, while that of inward-looking countries suffered an average loss of 8 percent. Further, economic growth was 7.9 percent in outward-looking countries in 1973-79 compared to 4.8 percent in inward-looking countries despite the large shock suffered by outward-looking countries. Broadly similar results were obtained for 1978-82 also.

A classification of our countries based on their trade orientation is presented in Table IV-1, which has been adopted from the World Development Report 1987.[9] Malaysia and Thailand pursued a moderately outward-oriented strategy during 1963-85. Bangladesh, India, Pakistan, and Sri Lanka pursued a determinedly inward-oriented

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[7]Hang-Sheng Cheng, "Alternative Balance-of-Payments Adjustment Experiences: Korea and Taiwan, 1973-77," Federal Reserve Bank of San Francisco Economic Review (Summer 1978), pp. 37-48.

[8]Balassa, "Structural Adjustment Policies in Developing Economies," passim, pp. 4-7.

[9]World Bank, World Development Report 1987, p. 83.

Table IV-1 Classification of Countries by Trade Orientation, 1963-73 and 1973-85

	Moderately outward-orientated	Moderately inward-oriented	Strongly inward-oriented
1963-73	Malaysia Thailand	Philippines	Bangladesh India Pakistan Sri Lanka
1973-85	Malaysia Thailand	Pakistan Philippines Sri Lanka	Bangladesh India

Source: World Bank, World Development Report 1987 (New York: Oxford University Press, 1987), Figure 5.1, p. 83.

Note: Burma is not listed in the source.

strategy in 1963-73. However, in 1973-85 Pakistan and Sri Lanka changed their trade strategy to moderately inward-looking while Bangladesh and India continued to follow strongly inward-looking strategies. Burma's case (not listed in the table) is peculiar; it remained isolated throughout the period, pursuing its own brand of socialization.

Table IV-2 shows some comparative data for our countries. Sri Lanka and the Philippines are listed as moderately inward-oriented since they pursued a moderately inward-oriented strategy for most of the 1970s and 1980s. The performances of outward-oriented Malaysia and Thailand were better than the inward-oriented countries in every category. Within the inward-oriented countries, growth in per capita GNP and exports were better in moderately inward-looking countries. For 1970-85, average trade balances as percentages of exports--a rough indicator of the BOP performance--were also better in outward-oriented countries. Based on these statistics and our earlier discussion on import-substitution and export promotion strategies, we can say that the countries following an import-substitution policy experienced more severe BOP difficulties than those following an export promotion strategy.

Table IV-2 Comparative Economic Growth, 1970-85

	Real GNP Per Capita 1970-82[a]	Value Added in Manufacturing 1970-83[a]	Exports 1973-83[a]	Trade Balance as Percenatge of Exports 1970-85[b]
Moderately outward-oriented				
Malaysia	5.2	9.2	7.5	-1.6
Thailand	4.9	8.4	10.4	10.2
Moderately inward-oriented				
Pakistan	2.6	5.8	7.4	-31.9
Philippines	3.2	5.5	5.6	-14.2
Sri Lanka	3.0	2.2	3.5	-22.2
Strongly inward-oriented				
Bangladesh	2.5[c]	5.0	2.9	-67.2
India	1.5	3.7	3.3	-19.9
Other				
Burma	2.4	4.5	3.2	-26.2

Sources: Per capita real GNP data from UN, National Accounts Statistics: Analysis of Main Aggregates, 1982 (New York: UN, 1985); manufacturing value added and export growth data from World Bank, World Development Report 1986 (New York: Oxford University Press, 1986); trade balance data from IMF, International Financial Statistics (Washington D.C.: IMF, various issues).

Notes: [a]Average annual growth rate, percent per year; [b]Simple average; [c]1972-82 for Bangladesh.

CAUSES OF THE BALANCE OF PAYMENTS PROBLEMS

While the trade and development strategies may influence the general direction of the current account balance, the evolution of the current account balance depends upon more than the trade and development strategies alone. For analytical purposes, these other considerations can be divided into external (beyond the influence of individual developing countries) and domestic or internal (within the control of individual developing countries). The major external factors include terms of trade, growth in real GNP in industrial countries, and the real foreign interest rate. The major internal factors include the exchange rate and the fiscal balance. It should also be recognized that the distinction between external and internal is not always clear-cut in practice since many inter-relationships exist among the various factors. Nevertheless, the distinction into external and domestic does help to understand the relative importance of the various factors in causing BOP problems. In addition, it allows to design appropriate policy measures in response to BOP problems.

The impact of external shocks and policy responses to these shocks can be analyzed by counterfactual analysis--studying the impact of a shock by comparing an actual situation with a hypothetical, non-disturbance situation. External shocks can be decomposed into the effects of terms of trade, export volume

(recessions in industrial countries), and the interest rate (burden of accumulated debt).

According to Seiji Naya, D. H. Kim, and W. James, during 1974-82 adverse external shocks ranged from $2 billion to $4 billion for four countries (India, the Philippines, Thailand, and Pakistan); $1/2 billion for Sri Lank; and only $50 million for Burma (Table IV-3).[10] Malaysia experienced a $0.7 billion favorable shock during the same period.[11] Table IV-4 provides estimates of external shocks as percentages of GNP. The table is based on three studies done by Balassa and McCarthy; Naya, Kim, and James; and Helleiner (the original tables are in Appendix C). It should be noted that some countries are missing because the writers did not cover all of our countries. External shocks are categorized into positive and negative; negative shocks are again divided into low (less than 5 percent of GNP) and high (more than 5 percent of GNP). The table shows that, with the exception of Malaysia, all countries suffered adverse shocks. While the estimates vary, it is still clear that India's shock was small and Sri Lanka's shock large according to all three studies.

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[10]Seiji Naya, D. H. Kim, and W. James, "External Shocks and Policy Responses: The Asian Experience," Asian Development Review, vol. 2, no. 1 (1984), Table 5, p. 11.

[11]Ibid., p. 11.

Table IV-3 External Shocks, Balances of Trade, and Effects of Terms of Trade and Volume of Trade (millions of $) 1974-82

	External Shocks	Balance of Trade	Terms of Trade Effects	Volume of Trade Effects
Burma	-51	-141	-81	-60
India	-3,809	-3,143	-2,772	-371
Malaysia	+679	+1,117	+499	+618
Pakistan	-3,153	-1,601	-1,472	-371
Philippines	-2,532	-1,884	-1,900	+16
Sri Lanka	-529	-391	-404	+31
Thailand	-2,394	-1,539	-2,158	+619

Source: Seiji Naya, D. H. Kim, and W. James, "External Shocks and Policy Responses: The Asian Experience," Asian Development Review, vol. 2, no. 1 (1984), Table 5, p. 11.

Notes: Data for Bangladesh is not available in the source. Balance of Trade = Exports minus Imports; Volume of Trade Effects = Balance of Trade minus Terms of Trade Effects.

Table IV-4 External Shocks as Percentages of GNP

	Positive Shocks	Negative Shocks	
		Below 5 Percent	Above 5 Percent
Balassa (1974-82)	Malaysia (1.5)	India (-2.6) Thailand (-4.2)	Bangladesh (-7.4) Pakistan (-5.4) Philippines (-6.1) Sri Lanka (-26.8)
Naya, Kim, & James (1974-82)	Malaysia (6.4)	Burma (-1.8) India (-4.6)	Pakistan (-26.8) Philippines (-14.5) Sri Lanka (-23.5) Thailand (-15.2)
Helleiner (1973-82)		India (-1.5)	Pakistan (-5.4) Philippines (-6.1) Sri Lanka (-31.5) Thailand (-10.1)

Sources: Bela Balassa and F. Desmond McCarthy, "Adjustment Polices in Developing Countries, 1979-83: An Update," World Bank Staff Working Papers, no. 675 (Washington, D.C.: World Bank, 1984); Seiji Naya, D. H. Kim, and W. James, "External Shocks and Policy Responses: The Asian Experience," Asian Development Review, vol. 2, no. 1 (1984), Table 4, p. 8; Gerald K. Helleiner, "Balance-of-Payments Experience and Economic Growth Prospects of Developing Countries: A Synthesis," World Development, vol. 14, no. 8 (August 1986), Table A2 and A3, pp. 906-907.

Changes in Terms of Trade

The annual percentage change in terms of trade for our countries for the period 1971-85 is shown Figure IV-2. As can be seen from the movement of the curves, terms of trade show large fluctuations, particularly in the early part of 1970s, for all countries. The coefficient of variation of the terms of trade ranged from a low 9 for Burma to a high 34 for the Philippines. The coefficient of variation of export price indices ranged from 28 to 51, with a mean of 35; and of import price indices from 36 to 51, with a mean of 46. Except for Malaysia, the coefficient of variation of import price indices were higher than that of the export price indices. Thus the higher fluctuations in the terms of trade were largely the result of fluctuations in import price indices.

The terms of trade declined for all countries with the exception of Malaysia. Higher average declines were experienced by the Philippines (6.1 percent), India (5.2 percent), and Pakistan (5.1 percent).[12] The declines were moderate for Thailand (3.9 percent), Sri Lanka (2.7 percent), and Bangladesh (1.7 percent). Malaysia's improvement (2.5 percent) can be largely attributed to the increase in oil prices.

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[12]The growth rates of terms of trade were estimated by ordinary least square regressions on the equation:

$$\log (\text{terms of trade}) = \alpha_0 + \beta_1 \text{ time}.$$

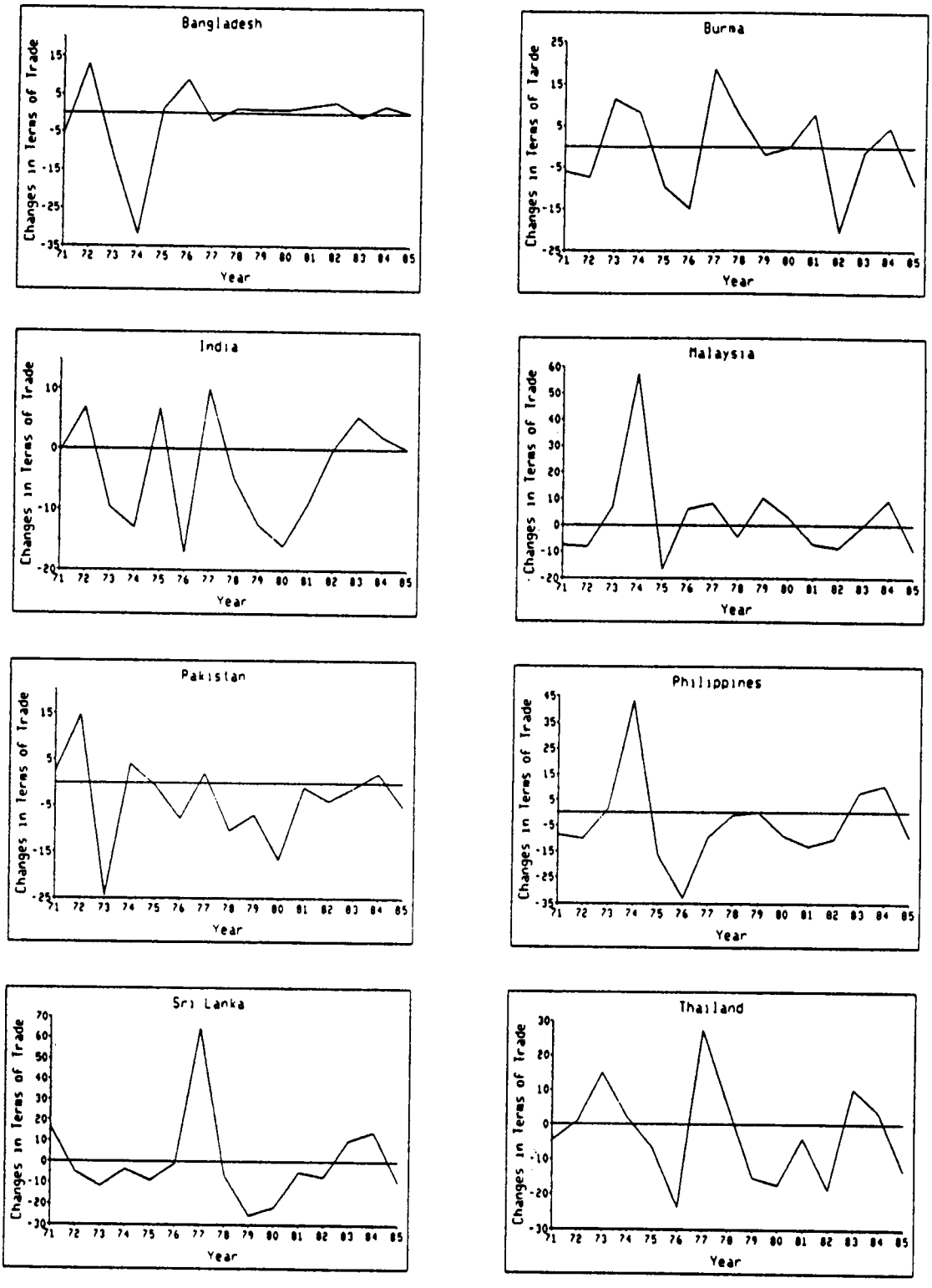

Figure IV-2 Annual Percentage Change in Terms of Trade, 1971-85

Source: UNCTAD, Handbook of International Trade and Development Statistics (United Nations: New York, various issues).

However, average declines mask substantial year-to-year fluctuations. For example, Bangladesh's terms of trade fell by 32 percent between 1973 and 1974, then improving by only 1 percent between 1974 and 1975. For Malaysia, these improved by 57 percent between 1973 and 1974 but declined by 17 percent between 1974 and 1975. For most countries the changes in terms of trade was substantial during one of the years between 1973 and 1976. The markedly low points--for Bangladesh (1974), Burma (1976), Malaysia (1975), Pakistan (1973), Philippines (1976), and Thailand (1976)--coincided with two related events. One was the sudden rise in oil prices and the other was the end of the boom in commodity prices. For example, the Philippines experienced a decline in its export prices of several commodities during 1974-75: the prices of coconut oil fell by 61 percent, of copra by 57 percent, of logs by 17 percent, and of plywood by 20 percent. The price of rubber fell by 25 percent for Malaysia and Thailand, and of rice by 55 percent for Thailand and Burma. Conversely, India and Sri Lanka benefited from a 103 percent rise in the price of tea during 1975-76.

To show that the changes in terms of trade is strongly related with the changes in current account balances (excluding official transfer and exceptional financing) and in trade balances, Figure IV-3 presents these three variables together for 1971-85. A strong positive correlation is obvious for all countries. There were only isolated cases when these curves did not move in the same direction.

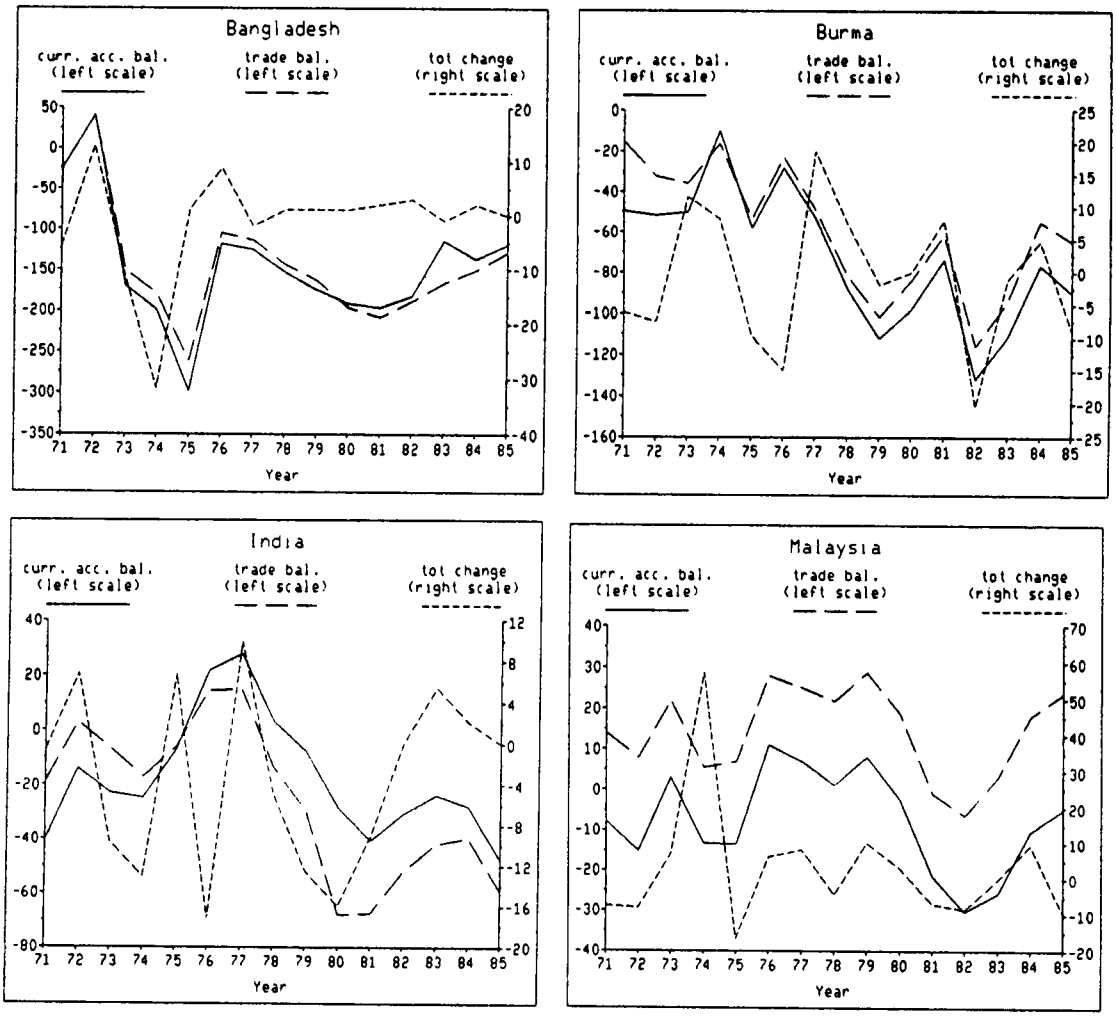

Figure IV-3 Current Account Balance and Trade Balance as Percentages of Exports and Annual Percentage Change in Terms of Trade, 1971-85

Sources: Current account balance, trade balance, and export data from IMF, International Financial Statistics (Washington D.C.: IMF, various issues); annual percentage changes in terms of trade are calculated from UNCTAD, Handbook of International Trade and Development Statistics (New York: United Nations, various issues).

Note: Current account balance data exclude official transfer and exceptional financing.

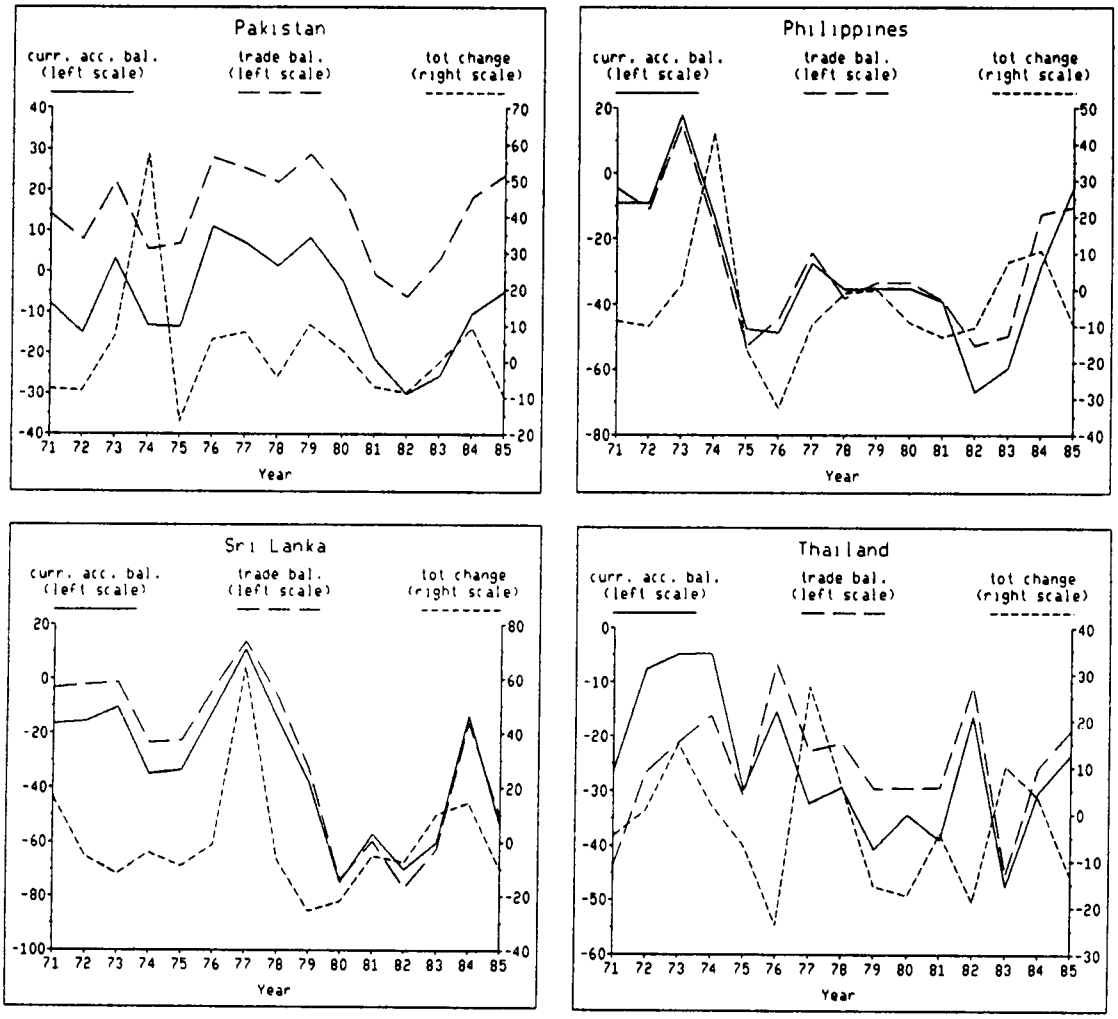

Figure IV-3 Continued

Impact of the Rise of Oil Prices

A significant part of the deterioration of the terms of trade of non-oil developing and industrial countries during the last decade can be attributed to the historic rises in oil prices, first in 1973-74 and again in 1979-80. As mentioned earlier, the terms of trade of developing countries as a group declined by 7.6 percent in 1973-74 and by 7.3 percent in 1980-81.[13] However and fortunately for LDC, export prices of primary commodities also rose on both occasions, which helped to mitigate the adverse movement in import prices. William R. Cline showed that 15 out of 25 sample countries in his study experienced deterioration in terms of trade between 1971-72 and 1975; but that 19 countries showed an improvement in terms of trade if the cost of oil was excluded from their import prices.[14] The favorable impact of the rise in primary commodity prices would have been larger had there not been a slowing of growth in the industrial countries. The empirical evidence suggests a positive association between the economic activity in industrial countries and the primary commodity export prices of developing countries. While the precise size of the estimated elasticity varies, a median estimate is 2.[15]

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[13]Khan and Knight, "Determinants of Current Account Balance," p. 824.

[14]William R. Cline, *et al.*, World Inflation and the Developing Countries (Washington D.C.: Bookings Institution, 1981).

[15]For example, according to Ke-Young Chu and Thomas K. Morrison, Rudiger Dornbusch, and Sewder van Wijnberger, the estimated elasticity of non-oil primary commodity prices with respect to economic activity of industrial countries are 2.0, 1.0, and 4.5

While the increase in oil price affected both the developing and the industrial countries, the impact was particularly devastating for the non-oil developing countries. The sudden jump in oil prices affected the developing countries through various channels.[16] First, of course, is the immediate rise in the import bill for oil. Second, a weakening in export markets resulted from oil-induced recessions in industrial countries. Third, non-oil import prices also rose because of oil-induced inflation in industrial countries. Fourth, access to private capital became difficult once the trade balance deteriorated significantly. And, finally, the flow of concessional aid to developing countries declined resulting from recycling of petrodollars from non-oil developing countries to OPEC countries and from there to private banks in industrialized countries.

The impact of oil price shocks on the trade balances for the years immediately after the energy shocks are shown in Table IV-5. Both the changes in the trade balances and in the net energy imports

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respectively. See Ke-Young Chu and Thomas K. Morrison, "World Non-Oil Primary Commodity Markets: A Medium-Term Framework of Analysis," International Monetary Fund Staff Papers, vol. 33 (March 1986); Rudiger Dornbusch, "The effects of OECD Macroeconomic Policies on Non-Oil Developing Countries: A Review," cited in David Goldsbrough and Iqbal Zaidi, "Transmission of Economic Influences from Industrial to Developing Countries," World Economic and Financial Surveys (July 1986); and Sewder van Wijnberger, "Interdependence Revisited: A Developing Countries Perspective on Macroeconomic Management and Trade Policy in the Industrial World," Economic Policy: A European Forum, vol. 1 (November 1985).

[16]Edward R. Fried and Charles L. Schultze, Higher Oil Prices and the World Economy: The Adjustment Problem (Washington, D.C.: Brookings Institution, 1975), p. 6.

Table IV-5 The Contribution of Net Energy Imports to Trade Deficits, 1973-74 and 1979-80[a]

	Change in Trade Balance		Change in Net Energy Imports		Change in Net Energy Imports as a Percent of Change in Trade Balance
	US $ mns.	Percent	US $ mns.	Percent	
1973-74					
Bangladesh	-85	-16	-58	-400	68
Burma	+22	39	-25	-397	116
India	-434	-227	-699	-99	161
Malaysia	-428	-66	-61	-424	14
Pakistan	-787	-779	-85	-153	11
Philippines	-725	-263	-465	-271	64
Sri Lanka[b]	-108	-986	-88	-1,720	81
Thailand	-68	-21	-392	-190	576
1979-80					
Bangladesh	-627	-36	-32	-23	5
Burma	-57	-8	..	..	..
India	-3,422	-154	-2,611	-64	76
Malaysia	-751	-24	+536	-51	71
Pakistan	-535	-23	-432	-91	81
Philippines	-398	-26	-836	-61	210
Sri Lanka	-460	-142	-173	-109	38
Thailand	-352	-23	-1,267	-79	360

Sources: Trade balance data from IMF, International Financial Statistics (Washington D.C.: IMF, various issues); energy data from ESCAP, Statistical Yearbook for Asia and the Pacific (New York: UN, various issues); Malaysia's energy data from UNCTAD, Handbook of International Trade and Development Statistics (New York: UN, various issues).

Notes: [a]Energy data relate to "Mineral Fuels and Related Materials" (SITC 3) and thus include not only crude oil and petroleum products but also coal and its products. Net energy import is defined as energy import minus energy export. A "-" sign indicates deterioration and a "+" sign indicates improvement; [b]1971-74 for Sri Lanka; ".." means not available.

between 1973-74 and 1979-80 varied across the countries. Except for Burma in 1973-74, the trade balances deteriorated dramatically for all countries in both occasions, oil import bills increasing by more than 100 percent for the seven other countries. Although the impact of net oil imports was less severe in 1979-80, the energy import bill still dominated the changes in trade balances for most countries. In contrast to other countries, Malaysia in fact gained from the oil price rise in 1979-80.

Table IV-6 provides some indication of dependence on imported energy for the period 1970-81. A clear pattern of rise in expenditure on imported energy, expressed either as percentages of GDP, exports, or imports, can be observed for all countries. For example, energy imports as a percent of GDP increased by 3 to 17 fold during 1970-73 and 1979-81. For every country the increase in energy imports/GDP was higher than in energy imports/exports. While the energy consumption/GDP ratio (not shown in the table) rise in developing countries as development proceeds, the dramatic rise in energy expenditure in the 1970s and 1980s was significantly higher than the usual proportionate rise in the energy consumption/GDP ratio.

One way to see the impact of oil import costs is to evaluate incremental cost over a base year. Using this approach, Ching-yuan Lin found that change in the current account balances relative to incremental oil import costs for the period 1974-77 compared to 1973

Table IV-6 Indicators of Oil Dependence, Averages for Selected Periods 1970-81

	Energy Import Expenditures as Percentages of GDP			Energy Import Expenditures as Percentages of Export Receipts			Energy Import Expenditures as Percentages of Total Import Expenditures		
	1970-73	1973-79	1979-81	1970-73	1973-79	1979-81	1970-73	1973-79	1979-81
Bangladesh	0.2[a]	1.3	1.2	4.3[b]	23.6	23.1	4.5[b]	11.6	10.8
India	0.5	1.8	5.1[c]	11.5	30.0	70.1[c]	9.0	20.9	30.4[c]
Pakistan	0.6	2.4	4.2	9.3	26.8	42.8	7.2	14.7	21.9
Sri Lanka	0.6	4.2	10.3	4.3	21.1	38.5	4.2	18.6	22.5
Philippines	1.9	4.9	6.7	12.1	28.8	38.1	12.0	20.7	26.9
Thailand	1.9	4.6	7.5	15.0	26.6	40.1	10.0	20.0	29.1

Source: William E. James, "External Shocks, Energy Policy and Macroeconomic Performance of Asian Developing Countries: A Policy Analysis," Asian Development Bank Economic Office Staff Paper, no. 17 (Philippines: Asian Development Bank, 1983), Table 18, p. 124.

Notes: [a]1973 only; [b]1972-73 only; [c]1979-80 only. Burma and Malaysia are not listed in the source.

was above the global average in Malaysia, India, and Burma and below the global average in Sri Lanka, Thailand, Bangladesh, and the Philippines.[17] Lin also estimated cumulative change in the current account balance and decomposed the change into oil and non-oil components for the period 1974-77 compared to 1973. His estimates are shown in Table IV-7, where countries are listed in descending order of total current account deficits for the period 1974-77. Total current account balances (column 1) showed large deficits for Pakistan, the Philippines, Bangladesh, and Thailand. Sri Lanka and Burma also showed deficits, but not as much as the above countries, while Malaysia and India showed surpluses. The cumulative change (column 2) appeared to be highly negative for Pakistan and the Philippines and a highly positive for India. However, incremental net oil imports (column 3) were high in India, Thailand, and the Philippines. While cumulative oil deficits were negative for all countries, non-oil deficits (column 4) were negative only in three countries--Bangladesh, Pakistan, and the Philippines. This suggests that, in the absence of a very high price of oil India, Malaysia, Burma, Sri Lanka, and Thailand would have experienced BOP surpluses. For example, India's surplus would have been a significant amount--$7.2 billion.

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[17]Ching-yuan Lin, Developing Countries in a Turbulent World: Patterns of Adjustment Since the Oil Crisis (New York: Praeger, 1981), Table 2.8, p 31.

Table IV-7 Cumulative Changes in Current Account Balances and Estimated Oil and Non-oil Components (Billions of $), Ratios of 1974-77 to 1973

	Current Account Balance, 1974-77[a]		Cumulative Increments in Net Import Payments Attributable to Oil Price Increases, 1974-77 Over 1973[b]	Cumulative Increments in Non-oil Deficits if No Change Occurred in Net Oil Import Volume, 1974-77 Over 1973[c]	Percentage Share of Incremental Deficits	
	Total	Cumulative Changes Over 1973			Oil[d]	Non-Oil[d]
Pakistan	-3.94	-3.50	-0.70	-2.80	-20	-80
Philippines	-3.40	-5.00	-2.20	-2.80	-44	-56
Bangladesh	-2.80	-0.80	-0.20	-0.60	-25	-75
Thailand	-2.00	-1.70	-2.00	0.30	-118	18
Sri Lanka	-0.39	-0.23	-0.28	0.05	-122	22
Burma	-0.30	0.02	-0.06	0.08	-300	400
Malaysia	0.73	0.37	-0.15	0.52	-41	141
India	0.86	3.10	-4.10	7.20	-132	232

Source: Ching-yuan Lin, Developing Countries in a Turbulence World: Patterns of Adjustment Since the Oil Crisis (New York: Praeger, 1981), Table 5.5, pp. 103-108.

Notes: [a]Balance on goods, services, and private transfers; [b]Measured on net imports of crude oil and refined products in 1973, with incremental oil import cost over 1973 estimated at $7.27, $7.83, $8.52, and $9.61 per barrel, for the years 1974, 1975, 1976, and 1977 respectively; [c]Columns 2 minus column 3; [d]Ratio of column 3 and 4, respectively, to column 2.

External Shocks and Terms of Trade

Decomposing external shocks into terms of trade and export volume provides a hypothetical picture of the BOP position. It is assumed that terms of trade remain at base year level; that real GNP and export volume continue to grow at the previously prevailing rates; and that export market shares do not change. The difference between the hypothetical and the actual BOP position is then calculated. Following this method, Naya, Kim, and James came to the conclusion that terms of trade effects for the period 1974-82 ranged from $1.5 billion to $2.8 billion for four countries (India, Pakistan, the Philippines, and Thailand); $400 million for Sri Lanka; and $80 million for Burma (Table IV-3, page 112).[18] Again Malaysia enjoyed a $0.5 billion favorable effect.[19]

To show that the terms of trade effect was the major reason why our countries experienced adverse external shocks we present Table IV-8 which shows external shocks and their composition. Again this table is based on Balassa and McCarthy; Naya, Kim, and James; and Helleiner. Changes in terms of trade accounted for three-fourths or more of total shocks for all countries except Pakistan and even in Pakistan's case the export volume effect was only slightly higher than the terms of trade effect. A broadly similar conclusion can be

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[18]Seiji Naya, D. H. Kim, and W. James, "External Shocks and Policy Responses: The Asian Experience," Table 5, p. 11.

[19]Ibid., Table 5, p. 11.

Table IV-8 External Shocks and Their Composition (percent)

	Bang	Burm	Indi	Mala	Paki	Phil	Sri	Thai
Naya, Kim, and James (1972-84)								
External Shock/GNP	..	-1.8	-4.6	6.4	-26.8	-14.5	-23.5	-26.8
Composition of External Shocks (as percent of external shocks)								
Terms of Trade Effects	..	-185.5	-72.8	71.6	-46.7	-75.1	-76.5	-90.1
Export Volume Effects	..	58.8	-27.2	28.4	-53.3	-24.9	-23.5	-9.9
Helleiner (1974-82)								
External Shock/GNP	..	..	-1.5	..	-5.4	-6.1	-31.5	-10.1
Composition of External Shocks (as percent of external shocks)								
Terms of Trade Effects	..	..	-83.3	..	-76.9	-58.2	-88.4	-66.3
Export Volume Effects	..	..	-10.0	..	-21.3	-32.8	-11.0	-31.7
Interest Rate Effects	..	..	0.0	..	-0.9	-8.2	0.5	-2.5
Balassa and McCarthy (1979-82)								
External Shock/GNP	-1.1	..	-3.0	-5.3	-2.8	-6.4	-25.1	-6.4
Composition of External Shocks (as percent of external shocks)								
Terms of Trade Effects	-31.8	..	-81.3	20.7	-61.0	-37.9	-93.0	-69.7
Export Volume Effects	-46.2	..	-21.3	-132.7	-12.0	-35.7	-4.0	-5.2
Interest Rate Effects	-21.1	..	2.4	11.9	-26.9	-26.3	-3.0	-25.1

Sources: Seiji Naya, D. H. Kim, and W. James, "External Shocks and Policy Responses: The Asian Experience," Asian Development Review, Vol. 2, No. 1 (1984), Table 4, p. 8; Gerald K. Helleiner, "Balance-of-Payments Experience and Economic Growth Prospects of Developing Countries: A Synthesis," World Development, vol. 14, no. 8 (August 1986), Table A2 and A3, pp. 906-907;. Bela Balassa and F. Desmond McCarthy, "Adjustment Polices in Developing Countries, 1979-83: An Update," World Bank Staff Working Papers, no. 675 (Washington, D.C.: World Bank, 1984).

Notes: ".." means not avialable.

derived from Helleiner's study. Balassa and McCarthy's study, which is an analysis of 1979-82 (a period of recession in industrialized countries), show that more than three-fifths of total shocks for India, Pakistan, Sri Lanka, and Thailand were accounted for by the terms of trade. The implication is clear: changes in terms of trade had a more serious impact on the BOP positions than did the recessions in industrial countries.

Economic Growth in Industrial Countries

Economic growth in industrial countries affects the current account balances of developing countries indirectly through changes in the terms of trade and directly through changes in the exports of developing countries. A high economic growth rate in industrial countries improves the BOP position of developing countries through increasing imports from developing countries. The impact of economic growth in industrial countries on the BOP positions of developing countries usually manifests itself through changes in the export volume.

The average growth rate for each of our countries was higher than the average growth rate of real GNP of 2.8 percent in the industrialized countries during 1970-85. The mean year-to-year differences between the real GDP growth rate of our countries and that of industrial countries are positive for all countries.

To test the hypothesis that the economic growth rate in industrial countries is positively correlated with the current account balance of our countries, I calculated correlation coefficients between (i) the real GDP growth rate of industrial countries and the current account balance expressed as a ratio of exports of our countries, and between (ii) the real GDP growth rate of industrial countries and the current account balances expressed as a ratio of GDP of our countries (Table IV-9). In every case, correlation coefficients were positive. However, strictly speaking, economic growth should be treated as a relative term when investigating its impact on the BOP. A higher growth rate in the home country relative to foreign countries would increase imports in the home country and, consequently, the current account balance would deteriorate, and vice versa. In an attempt to discover the relationship between the differential growth rates and the current accounts, I also calculated correlation coefficients between these two variables. Except for Pakistan, the correlation coefficients were negative, as expected (Table IV-9).

The fact that the economic growth rate in industrialized countries affects the BOP position of developing countries can be seen from Table IV-10. The industrial countries went through recessions during 1974-75 and 1980-82 (Table IV-10). The last row of the table indicates this. When the growth rates of real exports of our countries are compared with the real GDP growth rates in industrialized countries for the periods 1977-79 and 1980-82 it

Table IV-9 Table of Correlation Coefficients

	CAX and IGNP	CAGDP and IGNP	CAX and RELATIVE	CAX and FP
Bangladesh	0.64	0.50	-0.70	-0.27
Burma	0.27	0.34	-0.46	-0.63
India	0.10	0.18	-0.19	0.46
Malaysia	0.56	0.57	-0.02	0.83
Pakistan	0.30	0.40	0.29	0.48
Philippines	0.52	0.51	-0.15	0.48
Sri Lanka	0.64	0.57	-0.08	0.74
Thailand	0.20	0.20	-0.18	0.17

Notes: CAX = current account balance as percentages of exports;
IGNP = real GNP growth of OECD countries;
CAGDP = current account balance as percentages of GDP;
RELATIVE = real GDP growth rates of South and Southeast Asian Countries as ratios of real GNP growth of OECD countries; and
FP = central goverment's fiscal balance as percentages of national income.

Table IV-10 Annual Growth Rates of Real Exports and Real GDPs, Industrialized Countries, Selected Years

	1968-73	1974-76	1977-79	1980-82
Annual Growth Rates of Real Exports				
Bangladesh	..	-5.3	5.2	3.6
Burma	-3.5	1.5	13.8	-1.3
India	3.4	11.4	0.1	-1.1
Malaysia	10.2	6.4	12.4	0.4
Pakistan	16.5	-3.8	3.1	2.2
Philippines	8.6	0.7	8.6	1.5
Sri Lanka	-3.8	-0.1	7.3	0.1
Thailand	7.8	13.4	8.1	7.7
Real GDP Growth Rates				
Industrial Countries	4.4	1.8[a]	3.7	0.9

Sources: Real exports data from Asian Development Bank, Key Indicators of Developing Member Countries of ADB (Philippines: Asian Development Bank, various issues); real GDP data from IMF, International Financial Statistics, Supplement on Output Statistics, no. 8 (Washington, D.C.: IMF, 1984).

Notes: Real exports are defined as nominal exports deflated by the index of unit values of exports from industrialized countries. [a]Growth rate is only 0.15 for 1974-75.

becomes clear that real export growth rates declined for all countries with the decline in economic activity in industrialized countries. For most countries the decline was important; and even negative for some countries. Export growth rates went up for most countries between 1974-76 and 1977-79 when real GDP went up in industrialized countries.

Various studies have attempted to estimate the sensitivity or elasticity of export growth in response to economic activity in the industrial countries. According to the IMF, "every reduction of 1 percentage point in the growth of industrial countries for a one year period typically reduces the exports of non-oil developing countries by about 1 1/2% or more than $2 billion."[20] Marvin E. Bond estimated that elasticity of export volume (total exports) of non-oil developing countries with respect to GNP in industrial countries is 2.4.[21] Elasticity in fact varies from country groups to country groups. Exporters of manufactures usually have a higher elasticity than non-manufactures. The calculated elasticity of our countries' export volumes with respect to the real GNP of OECD countries ranged from -0.5 to 3.0 (Table IV-11).[22] It is interesting to note that

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[20]IMF, World Economic Outlook (Washington D.C.: IMF, 1980), p. 8.

[21]Marvin E. Bond, "Export Demand and Supply for Groups of Non-Oil Developing Countries," International Monetary Staff Papers, vol. 32 (March 1985), pp. 56-77.

[22]The elasticities were derived from ordinary least squares regression on equation:

Table IV-11 Elasticities of Export Volumes with Respect to Real GNP Growth of OECD Countries

	Time Period	Elasticities
Bangladesh	1970-85	1.5
Burma	1970-85	0.5
India	1970-85	0.5
Malaysia	1970-85	3.6
Pakistan	1970-85	1.6
Philippines	1970-85	1.5
Sri Lanka	1970-85	1.7
Thailand	1970-85	2.8
Major Country Groups[a]		
Non-fuel Exporters	1967-81	2.3
Primary Product Exporters	1968-84	2.4
Services and Remittances Earnings	1968-84	0.4

Sources: [a]David Goldsbrough and Iqbal Zaidi, "Transmission of Economic Influences from Industrial to Developing Countries," World Economic and Financial Surveys (July 1986), Table 60, p. 166.

the countries with higher export/GDP ratios or higher trade ratios have higher export elasticities in general then countries with lower export/GDP or trade ratios.

External Shocks and Volume of Trade Effects

According to Naya, Kim, and James four of our countries experienced favorable and three experienced adverse export volume shocks during 1974-82 (Table IV-3, page 112). For Malaysia and Thailand favorable shocks were valued at $600 million, while for India and Pakistan $370 million. The Philippines and Sri Lanka had only small favorable shocks (less than $30 million), while Burma's adverse shock amounted to $60 million. Table IV-8 shows that, while export volume shocks may not be as important as terms of trade shocks, they were still important factors in the deterioration of the BOP of several countries. According to Balassa and McCarthy's study, export volume effect was the major reason why Bangladesh and Malaysia had BOP problems.

Real Foreign Interest Rate

Another major cause of BOP problems from the late 1970s is the sharp rise in interest rates in the international capital markets

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$$\log (\text{export volume})_t = \beta_0 + \beta_1 \log (\text{OECD real GNP})_t.$$

and the consequent rise in debt service payments. International capital markets were favorable in the 1960s and, in addition, a large proportion of outstanding debt was lent by foreign official institutions to developing countries at fixed concessional rates. The inflation rate was low in industrialized countries and real interest rates were low or negative for developing countries in general. But the situation changed dramatically in 1978, when interest rates increased significantly as a result of tight monetary policy in the industrialized countries. For example, the six-month London interbank offer rate on the U.S. dollar deposits rose from 6.37 percent in 1977 to 9.20 percent in 1978, and eventually climbed to an all time high 16.72 percent in 1981. Real interest rates were even higher for many countries. A world wide recession during 1980-83 led to a fall in the volume of world trade for the first time since the end of Second World War.[23] Exports and/or prices declined for many developing countries. Faced with this situation, many developing countries decided to borrow more (instead of making domestic adjustments) from whatever sources (private or official) to what they had access, and did so at a time when their debt burden was already high. Consequently their debt service obligations became higher in the late 1970s and 1980s.[24]

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[23]Anne O. Kruger, "Developing Countries Debt Problems and Economic Growth Prospects," Atlantic Economic Journal, vol. 14, no. 1 (March 1986), p. 11.

[24]Ibid., 11.

While this is the general picture of the debt problem of developing countries, it must be remembered that "developing-country debt problems are not all the same, and not all developing countries have debt problems."[25] Countries with a large amount of borrowing from official sources had lower average interest costs than countries with similar amounts of borrowing from private sources. The terms and conditions of new loans to Southeast Asian countries became increasingly harsh in the late 1970s and 1980s.[26] While South Asian countries continued to receive highly concessional loans--they remained close to 90 percent of total outstanding debts--Southeast Asian countries experienced a drop in such favorable loans, and the proportion of concessional loans in their total outstanding debt fell to 33.[27]

Table IV-12 shows the debt obligations of our countries for 1970-85. Between 1980 and 1985 total debt services and interest payments as percentages of exports of goods and services increased for all countries, but no particular pattern can be seen in the 1970s. In 1985 total debt service ranged from 13 to 17 percent in five countries, and over 20 percent in three countries. If debt service ratios of 20 percent or higher are dangerous (meaning

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[25]OECD, External Debt of Developing Countries: 1983 Survey (Paris: OECD, 1984), p. 14.

[26]Seiji Naya, "Economic Performance and External Debt in Asian Developing Countries," Energy, vol. 11, nos. 4/5 (1986), p. 368.

[27]Ibid., p. 368.

Table IV-12 Total Debt Service and Interest Payments as Percentages of Exports of Goods and Services, 1970-85

	1970	1975	1980	1985[a]
	Total Debt Service as a Percent of Exports of Goods and Services			
Bangladesh	..	18.4	7.1	16.7
Burma	17.2	17.4	22.6	37.4
India	23.7	13.3	8.4	13.3
Malaysia	3.7	3.3	2.5	22.3
Pakistan	23.4	18.5	17.9	29.5
Philippines	7.3	7.0	7.4	15.8
Sri Lanka	10.8	21.7	6.3	13.9
Thailand	3.4	2.4	1.3	14.7
	Interest Payments as a Percent of Exports of Goods and Services			
Bangladesh	..	4.3	4.3	6.9
Burma	2.1	5.0	9.2	14.6
India	8.7	4.4	3.0	5.6
Malaysia	1.2	1.4	1.7	6.3
Pakistan	9.5	7.6	7.5	8.4
Philippines	1.8	2.2	4.7	10.5
Sri Lanka	3.2	3.2	2.5	6.6
Thailand	1.4	1.2	3.1	5.9

Source: World Bank, World Debt Tables: External Debt of Developing Countries (Washington D.C.: World Bank, various issues).

Notes: ".." means not available; [a]1984 for Burma.

difficult to service) then Malaysia's, Burma's, and Pakistan's debts were causes of concern. However, it must be remembered that debt service ratio alone may be a misleading indicator of the problem because other factors (for examples, import level, economic growth, and so on) need to be taken into account when the impact of debt service is considered. Further, countries with lower debt service ratios may also have difficulty also in servicing debts. Malaysia had traditionally maintained a low debt service ratio; its high ratio of 22.3 percent in 1985 was the result of a "bunching" of debts. Bangladesh, Burma, Pakistan, the Philippines, and Thailand have external debt situations worse than the other Asian countries including our sample countries, although their position is better than that of some Latin American and African countries.

Changes in the current account balances and the real interest rate are shown in Figure IV-4. The real interest rate is defined as six-month London interbank offer rate (LIBOR) on U.S. dollar deposits minus export price changes. In general, an opposite movement between the current account balance and the real interest rate can be observed for our countries during the later years when the real interest rate became highly positive for many countries, although there does not seem to be consistency between leads and lags. However, when the real interest rate was negative, as in the 1970s, the pattern is less obvious.

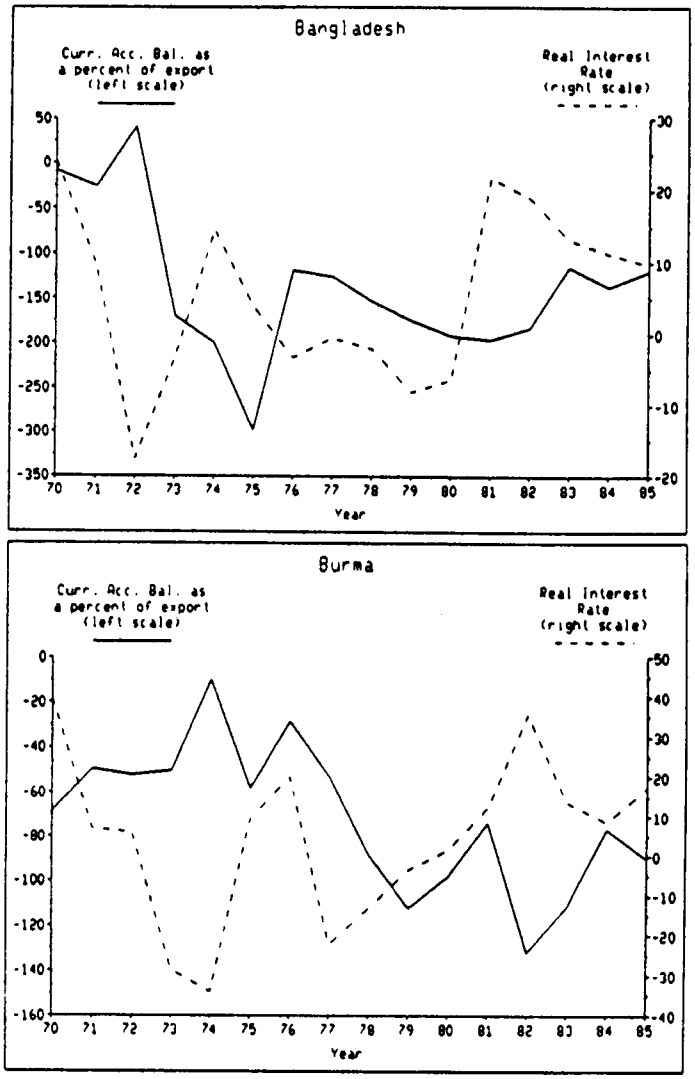

Figure IV-4 Current Account Balance as Percentage of Exports and the Real Foreign Interest Rate, 1970-85

Source: IMF, International Financial Statistics (Washington D.C.: IMF, various issues).

Notes: Current account balance data exclude official transfer and exceptional financing. Real foreign interest rate is calculated as six-month London interbank offer rate (LIBOR) on U.S. dollar deposits minus annual percentage change in export price index.

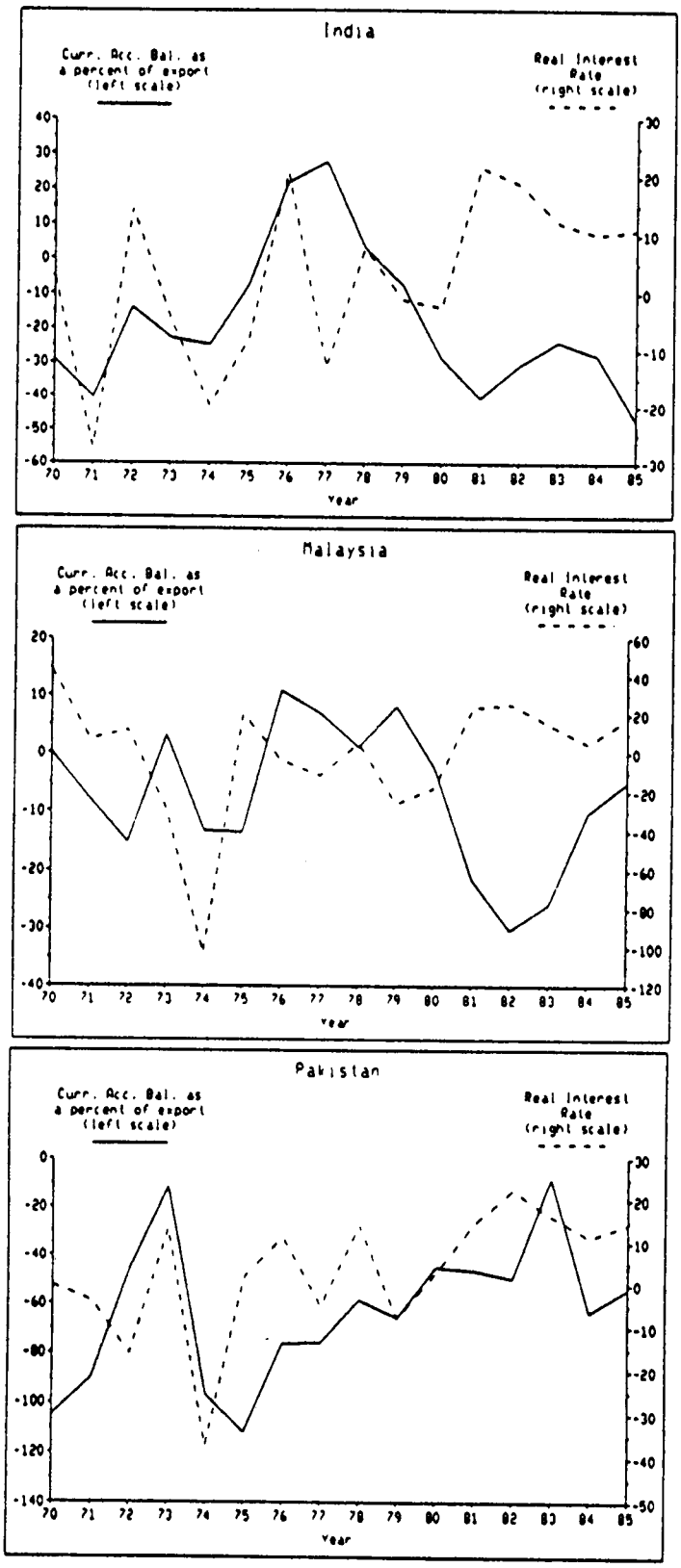

Figure IV-4 Continued

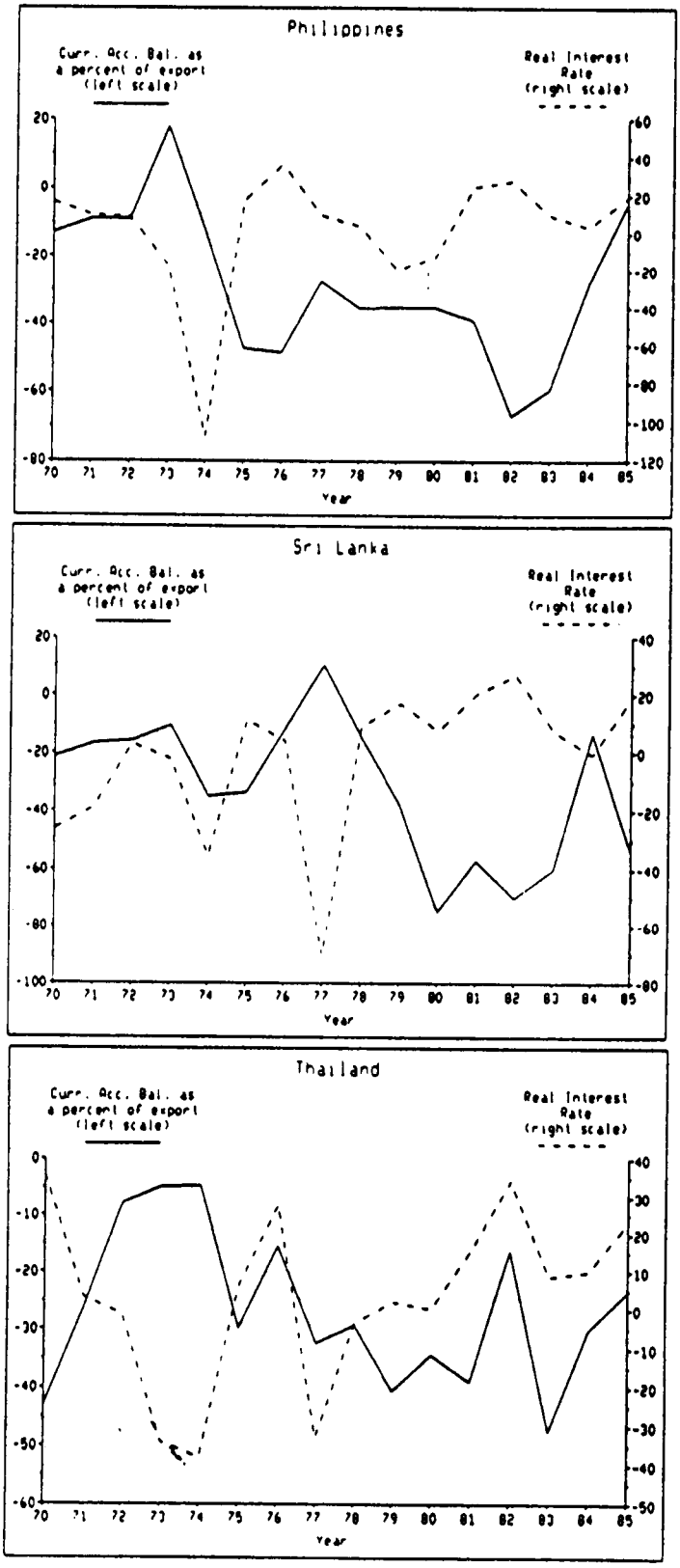

Figure IV-4 Continued

External Shocks and Real Foreign Interest Rate

The impact of interest rate shocks can be observed in Table IV-8 (page 127). The interest rate effect became important only after the second oil shock, i.e., after 1978-79. For this reason the impact of interest rates was small for the average figures of 1974-82 as shown by Helleiner. However, according to Balassa and McCarthy's study, during 1979-82 the interest rate effect accounted for one-fifth of total external shocks for Bangladesh and one-fourth of external shocks for Pakistan, Thailand, and the Philippines. Only India and Malaysia enjoyed small favorable interest rate shocks.

Fiscal Balance

According to the World Bank, "virtually every major payments crisis in the 1970s and 1980s was preceded by large and growing budget deficits."[28] The IMF stabilization programs for the countries facing BOP crises typically call for reductions in fiscal deficits. The policy prescription that improvement in fiscal position improves the current account balance is popular in industrial countries too. A recent Economic Report of the President, transmitted to the U.S. Congress, states that "the persistence of federal deficit ... is one of the most important factors contributing to the growth of the trade

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[28]World Bank, The World Development Report 1985, pp. 62-63.

deficits."[29] A number of studies have found a significant positive correlation between fiscal deficits and current account deficits, with the direction of causation running from the fiscal deficits to the current account deficits.[30]

How budget deficits affect the BOP can be explained quite simply within the national income accounting framework that relates expenditure to the difference between saving and investment. Increased fiscal deficits (public sector dissaving) cause domestic absorption to rise and, consequently, demand for imports rises. A part of increased government expenditure may go directly to imports. Furthermore, a higher domestic demand may cause the diversion of some production from the export market to the domestic market, thereby causing further deterioration in the current account balance.[31]

The average fiscal balance for each of our countries was negative for the study period. In India, Malaysia, Pakistan, and Sri Lanka, government budgets were consistently in deficit in all years. It was in surplus only once in Thailand and twice in the Philippines. The average fiscal balances--where fiscal balance is measured as the

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[29]United States Government, "Economic Report of the President," transmitted to the Congress (Washington D.C.: Government Printing Office, 1987), p. 111.

[30]Ibid., p. 63; Khan and Knight, "Determinants of Current Account Balance," p. 828.

[31]Jennifer Sharpley, "The Potential of Domestic Stabilization in Developing Countries," in Tony Killick (ed.), The Quest for Economic Stabilization, p. 56.

central governments deficits or surpluses as percentages of GDP--were small for Bangladesh (-1 percent), Burma (-1 percent), and the Philippines (-1.5 percent). India's deficit (-5 percent) remained stable through out the period. For Malaysia (-8 percent), Pakistan (-7 percent), and Sri Lanka (-9 percent), the average deficits were not only higher, but year-to-year fluctuations, particularly toward the end of the period, were greater too. For example, fiscal deficits as percentages of GDP averaged 13 percent in Sri Lanka during 1978-83 and 15 percent in Malaysia during 1981-83.

The relationship between fiscal imbalance, measured as above, and external imbalance, measured as current account balances (excluding official and exceptional financing) as percentages of GDP, is shown in Figure IV-5. The figure clearly shows that years with higher levels of current account deficits were associated with higher levels of fiscal deficits. Calculated correlation coefficients were positive for all countries except Burma. The movements in the fiscal balance and the current account balance depicted in Figure IV-5 and the calculated correlation coefficients clearly suggest that both variables move in the same direction for most of the countries. Thus we find a strong support for the hypothesis stated earlier, that fiscal deficits contribute to the current account deficits.

The fact that the correlation coefficient was negative for Burma should not be surprising. Other studies have found mixed results too. For example, in a causality test between these two

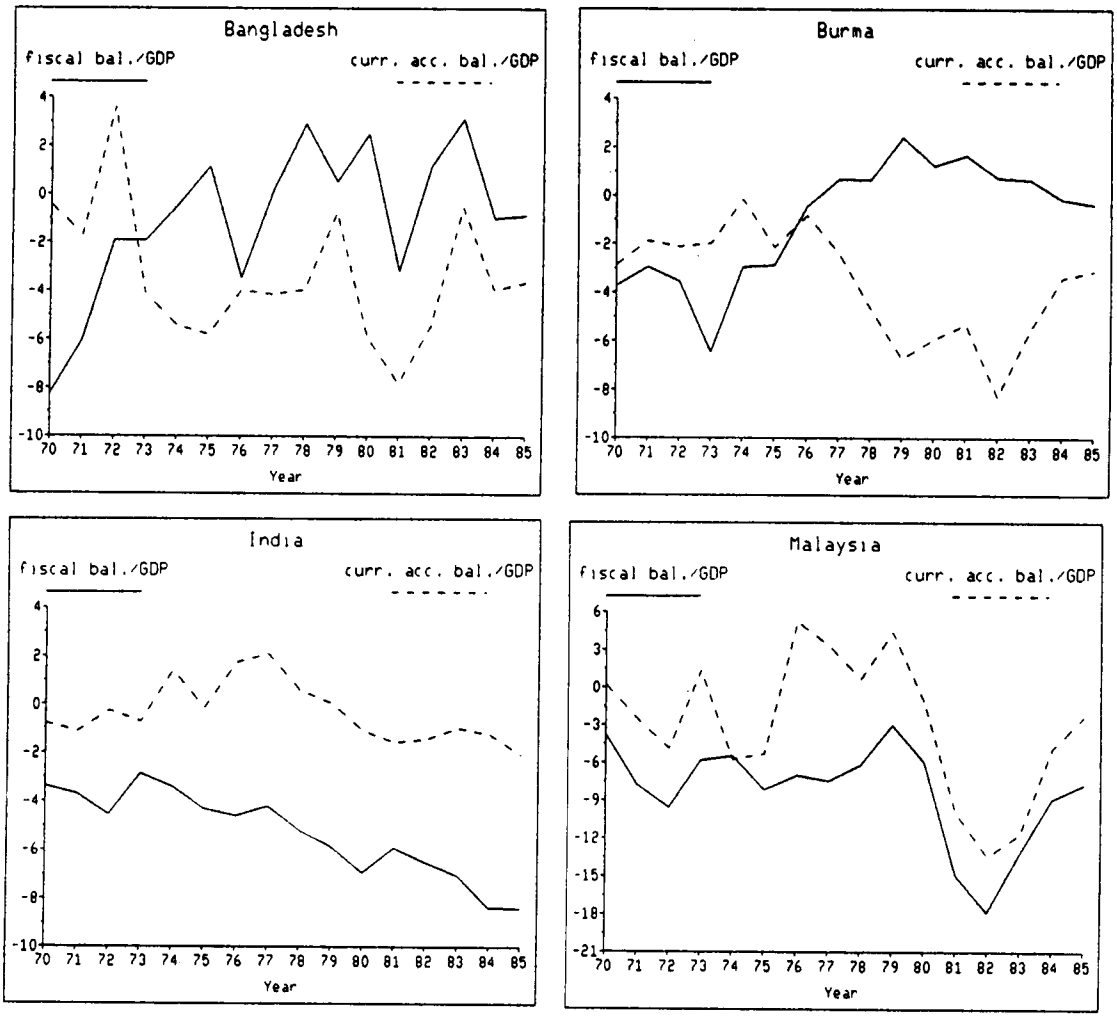

Figure IV-5 Current Account Balance and Fiscal Position as Percentages of GDP, 1970-85

Sources: IMF, International Financial Statistics (Washington D.C.: IMF, various issues). For Bangladesh and Pakistan FP/Y is equal for 1970-71. For Burma, 1970-73 data from World Bank, World Tables (Washington D.C.: World Bank, 1976). For Burma, 1985 data is average of 1982-84.

Notes: Current account balance data exclude official transfer and exceptional financing. Fiscal position is defined as the difference between central government's revenue minus expenditure.

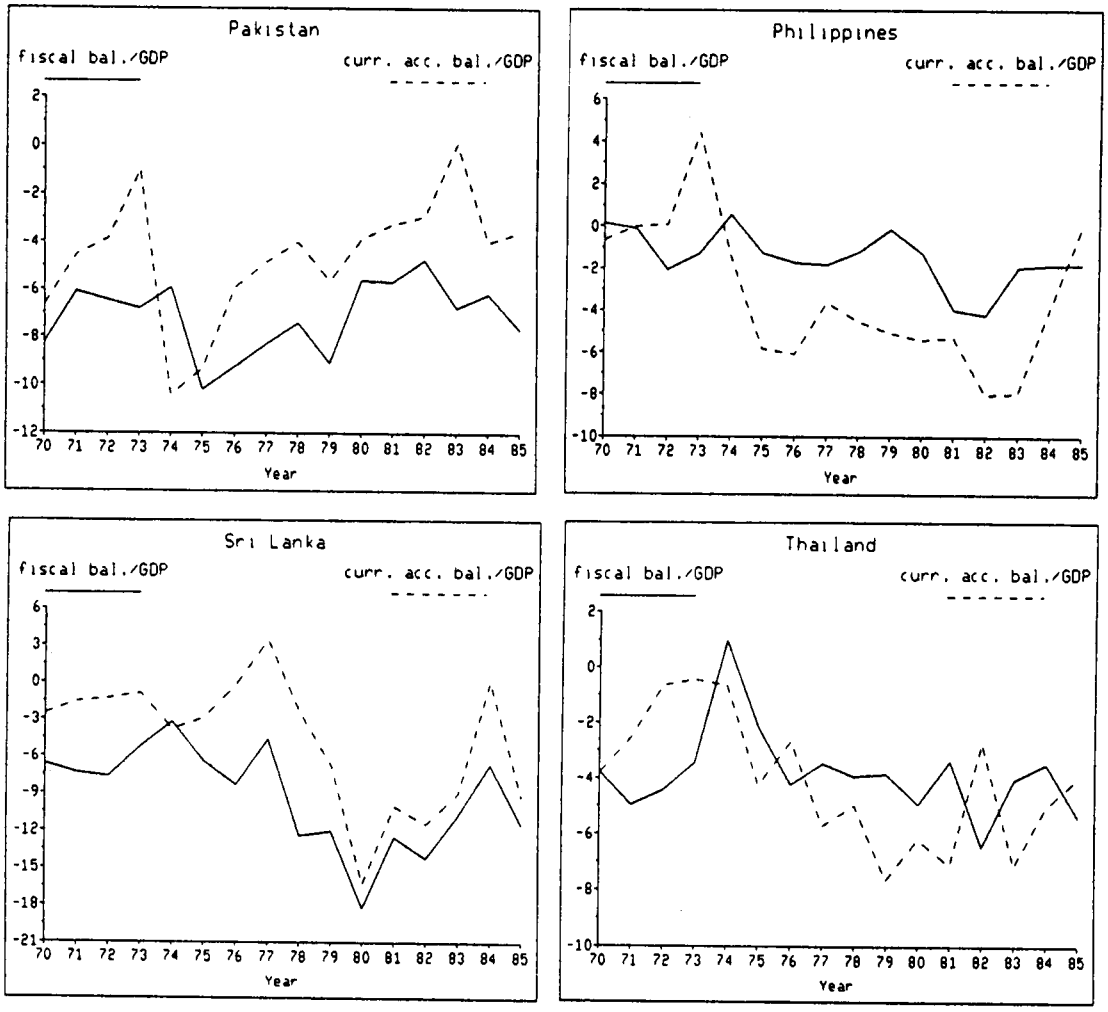

Figure IV-5 Continued

variables for developing countries, Iqbal Zaidi found bidirectional results.[32] It is quite possible that budget deficits, being partly endogenous, may be the result, not the cause, of payments deficits. For example, BOP pressure may force a country to cut down its imports, and this in turn may lead to fall in revenue collection. Further, external developments such as oil price increases or wars can also contribute to both fiscal and BOP deficits.

Real Effective Exchange Rate

Exchange rate changes play an important role in the external payments position of a country. They affect the current account balance directly through changes in relative prices and indirectly through changes in rates of inflation.[33] In one sense "exchange rate changes are direct channel through which international divergences in economic policy are transmitted to domestic economic performance."[34] Other things being equal, an appreciation of the home currency (hereafter exchange rate) causes domestic demand for imports to rise and foreign demand for exports to fall. The opposite happens when

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[32]Iqbal Zaidi, "Saving, Investment, Fiscal Deficits, and the External Indebtedness of Developing Countries," World Development, vol. 13, no. 5 (May 1985), pp. 573-588.

[33]Andrew Dean and Val Koromzay, "Current Account Imbalances and Adjustment Mechanisms," OECD Economic Studies, no. 8 (Spring 1987), p. 24.

[34]United States Government, Economic Report of the President, 1987, p. 113.

the exchange rate depreciates. Consequently, current account balance tends to deteriorate when the exchange rate appreciates and improve when the exchange rate depreciates.

An exchange rate may be fixed, adjustable peg, or crawling peg in terms of its chosen benchmark, or it may float. Before any discussion of the impact of exchange rate on the balance of payments one has to decide which exchange rate--nominal, real, or effective--to use in the analysis. As a measure of competitiveness, the nominal exchange rate may be a misleading indicator. It is possible that the nominal exchange rate of rupees per dollar remain unchanged when the major world currencies--to which rupees is pegged--fluctuate substantially. To overcome this problem, it is common to calculate nominal effective exchange rates, which are the averages of bilateral exchange rates, with some "proper weighting."

The real exchange rate is more appropriate in considering international competitiveness. The real exchange rate takes into account international inflation differentials. This is important because, "when domestic inflation is higher than world inflation, a country must devalue its currency if it wishes its prices to remain competitive abroad."[35] However, as a measure of average competitiveness, it is a common practice to calculate real effective exchange rate.

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[35]Word Bank, World Development Report 1987, p. 100.

The real effective exchange rate can be constructed differently, depending on one's purpose. The most common definition is

$$r = eP^*/P$$

where r = real exchange rate,

e = nominal exchange rate (domestic currency per unit of foreign currency),

P^* = foreign price index, and

P = domestic price index.

Following this definition, bilateral real exchange rates were calculated using consumer price indices, and then averaged using 1980 partner imports for the weighting (see Appendix D for weights). When defined this way, a fall in the real effective exchange rate means an appreciation and a rise means a depreciation.

Figure IV-6 shows the indices of nominal exchanged rate (R) and real effective exchange rate (REER). In general, both R and REER show an upward trend, indicating a steady depreciation throughout the period for most countries. In Malaysia R in fact appreciated as a result of what is sometimes called the "Dutch Disease." The Philippines also shows a slight appreciation of its REER over the period. While both R and REER depreciated steadily for the rest of the countries, the depreciation of REER was not sufficient to

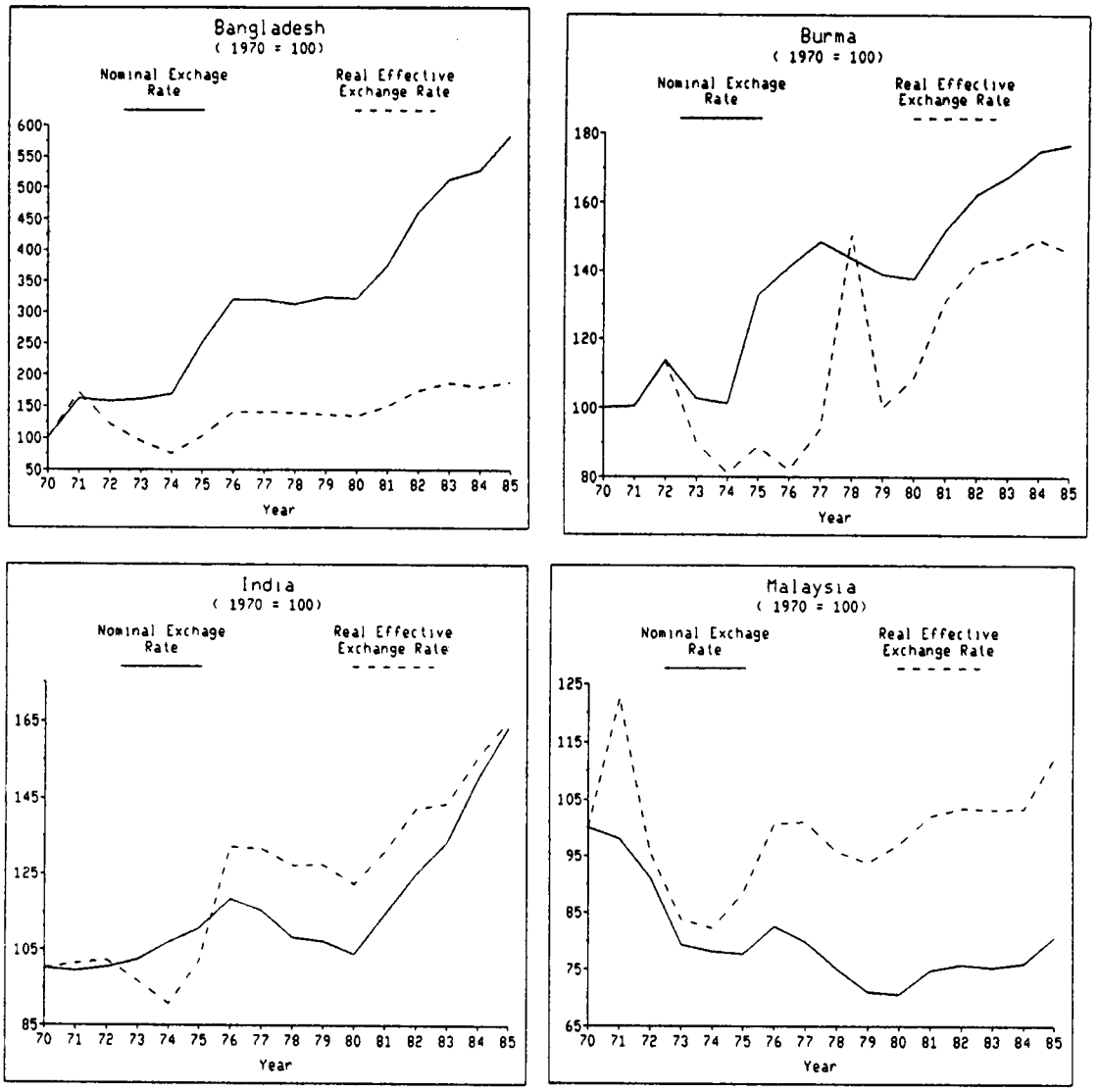

Figure IV-6 Nominal and Real Effective Exchange Rate Indices, 1970-85

Source: Calculated from IMF, International Financial Statistics, (Washington D.C.: IMF, various issues).

Notes: A higher value of either index means a depreciation and a lower value means an appreciation. The real effective exchange rate is calculated using the 1980 major import partner for weights.

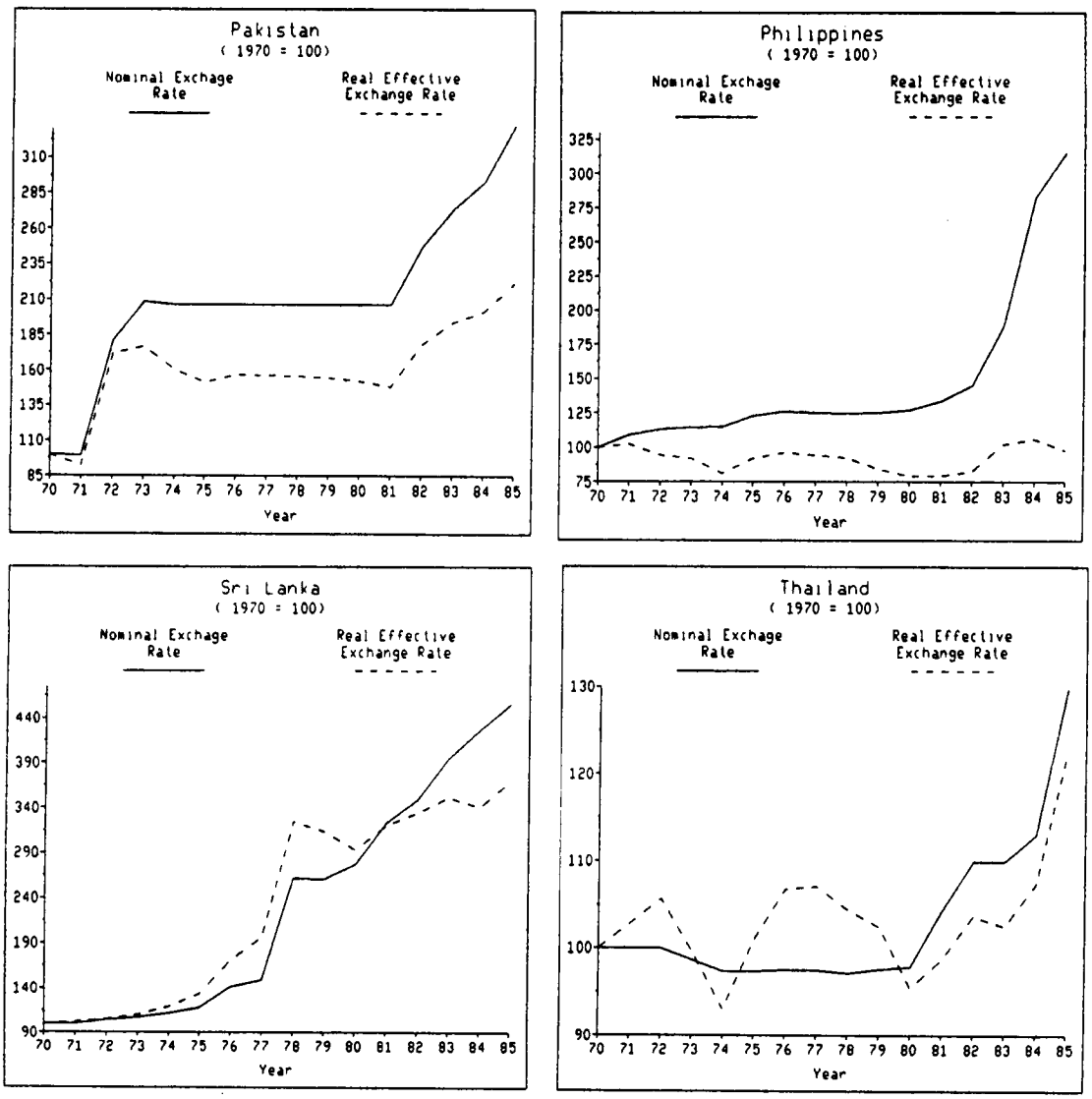

Figure IV-6 Continued

maintain international competitiveness. Average REER depreciation lagged behind average R depreciation for all countries for the period 1970-85. The difference is particularly large for Bangladesh, Pakistan, and the Philippines. However, contrasting behavior can be observed during the sub-periods. The annual average depreciation in R was more than REER for all countries except for Sri Lanka in 1970-75 period. Many countries experienced appreciation in 1974 as a result of the commodity price boom.[36] The situation changed during 1975-80. Nominal exchange rates were realistic for many countries. In five countries--Bangladesh, Burma, India, Malaysia, and Pakistan--REER depreciated more than R. At the same time, REER in fact appreciated at an annual rate of 2.5 percent and 1 percent in the Philippines and Sri Lanka respectively. However, the situation reversed again in 1980-85, when REER declined more than R only in Burma and Malaysia.

Both R and REER show large fluctuations for our countries. Such large fluctuations are also reported by other studies. For example, Helleiner found that, with the exception of Pakistan, all countries in our study experienced increased variability of the REER in 1973-79 compared to 1971-73.[37] More importantly, the major source

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[36]Pradumna B. Rana, "Sources of Balance of Payments Problem in the 1970s: The Asian Experience," Economics Office Report Series, no. 30 (Philippines: Asian Development Bank, 1985), p. 6.

[37]Gerald K. Helleiner, "The Impact of the Exchange Rate System on the Developing Countries," in Sidney Dell (ed.), The International Monetary System and its Reform, Part II (New York: North-Holland, 1987), pp. 407-510.

of instability is the fluctuations among major world currencies to which our currencies are pegged. However, it should be remembered that, since our currencies are pegged to baskets of currencies (except for the Philippines), such fluctuations in exchange rates are unavoidable.[38] Externally caused exchange rate fluctuations have made the macroeconomic management and development problems more difficult for our countries. For example, a background paper for the World Development Report 1986 found that a 10 percent average increase in real exchange instability is associated with a 4.8 percentage point reduction in the net investment ratio.[39] While the precise impact of variability of exchange rates on the BOP is difficult to estimate, it can be said that "uncertainty regarding the real exchange rate tends to discourage exports."[40]

An important consequence of exchange rate changes is change in market shares in world trade. An appreciation of REER leads to declines in export market shares in world trade and a depreciation to rising shares. Balassa and McCarthy have demonstrated this for our countries.[41]

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[38]Ibid., p. 492.

[39]Domingo F. Cavallo, Joaquin Cottani, and M. Shahbaz Khan, "Real Exchange Rate Behavior and Economic Performance in LDC's," cited in World Development Report 1986, p. 32.

[40]Bela Balassa, "Effects of Exchange Rate Changes in Developing Countries," Indian Journal of Economics, vol. LXCVII, part II, 269 (October 1987), p. 207.

[41]Balassa and McCarthy, "Adjustment Polices in Developing Countries, 1979-83: An Update."

The impact of exchange rate changes on the BOP depends, among other things, on the elasticity of exports with respect to REER. A recent study found this elasticity to be in the range of 1.3 to 3.3 for developing countries with a median of 2.9.[42] In our case elasticity of REER with respect to export volume ranged from 1.1 to 3.9. Interestingly, elasticity of exports with respect to the exchange rate was higher in those countries with lower per capita incomes. Bela Balassa reports that a one percent change in the real exchange rate is associated with a 0.8 percent change in the export/output ratio for merchandise exports and a 0.5 percent change for goods and services.[43]

The relation between exchange rates and current accounts is both complex and often difficult to interpret. Both can be affected by other macroeconomic variables. It is quite possible that developments in the current account balance itself may cause exchange rates to change. A government may devalue its currency in response to a payments crisis, as did several countries of our study. The effect of exchange rate changes on the current account also depends on the response of the domestic economy. The countries with higher trade ratios may well be more directly affected than countries with

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[42]R. M. Bautista, "Exchange Rate Change and LDC Export Performances Under Generalized Currency Floating," Weltwirtschaftliches Archiv, 3 (1981), Table 2, pp. 454-455.

[43]Quoted in Bela Balassa, "Effects of Exchange Rate Changes in Developing Countries," Indian Journal of Economics, vol. LXCVII, part II, 269 (October 1987), p. 209.

lower trade ratios. Other external factors such as terms of trade may systematically influence REER so that it may not always be possible to isolate the impact of exchange rate changes on the BOP. For example, a deterioration of terms of trade due to a rise in the prices of import may cause domestic prices to rise and, if offsetting policy measures are not taken, REER may appreciate.

ECONOMETRIC ANALYSIS OF THE FACTORS AFFECTING THE CURRENT ACCOUNT BALANCE

An econometric analysis of the origins or proximate causes of payments imbalances was tried for our countries for 1970-85. The empirical model specified to examine the determinants of the current account balance was similar to that of Khan and Knight.[44] The general form of the equation was:

$$CA/X = f(\underset{+}{TOT}, \underset{+}{DGNP}, \underset{-}{RI}, \underset{-}{REER}, \underset{+}{FP/Y}, \underset{?}{T}) \qquad (1)$$

where

CA = current account balance,

X = merchandise exports,

TOT = terms of trade,

DGNP = growth of real GNP in industrial countries,

RI = real foreign interest rate,

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[44]Khan and Knight, "Determinants of Current Account Balances", pp. 819-42.

REER = real effective exchange rate,

FP = fiscal balance (revenue minus expenditure),

Y = nominal GDP, and

T = linear time trend.

The expected sign of the coefficients are shown on top of the variables. Thus current account balances improve if terms of trade improve or if the growth rate of real GNP of industrial countries increases. It worsens if real interest rates in the international market rise or real effective exchange rates of our countries appreciate. And, lastly, the current account balance deteriorates if the fiscal balance declines. The linear time trend is included to capture the influence of other factors such as protection in industrial countries, weather, war, and trade and development strategies. Thus "T" can take either a positive or a negative value.

I estimated equation (1) for each country separately and also for pooled time-series cross-section data for three country groups--All Countries, South Asia, and Southeast Asia (country dummies were included to account for cross country differences but time dummies were not introduced since the time trend was included in each case). For estimation purposes the following semi-log linear specification was used:

$$(CA/X)_t = \beta_0 + \beta_1 \log TOT_t + \beta_2 DGNP_t + \beta_3 RI_t + \beta_4 \log REER_t + \beta_5 FP/Y_t + \beta_6 T + u_t \qquad (2)$$

where u is a random disturbance term and t refers to the time period (t = 1, 2, ..., 16). Appendix E describes in detail the sources and definitions of the variables.

Results

Table IV-13 shows the results of ordinary least squares analysis for individual countries. Several interesting results emerge from the table, but results do not give support to standard doctrines:

1. The value of adjusted R^2--the usual measure of goodness of fit--is 0.8 for Malaysia and Burma; and 0.5 for Bangladesh, Burma, India, Pakistan, and the Philippines; and only 0.06 for Thailand. The model thus fails to explain a large percentage of variation in the current account balances.

2. The signs of the parameters are opposite to what one should expect in one out of every four cases (excluding time trend). The only variable that yields the expected sign for all countries is economic growth in industrial countries.

3. Standard errors of the parameters are large. These in fact exceed the magnitudes of the parameters almost half of the time.

The results of ordinary least squares regression of pooled cross-section time-series data are reported in Table IV-14.

1. The adjusted R^2 is low for all three country groups. It ranges from 0.23 for South Asia to 0.34 for All Countries.

Table IV-13 Regression Results for Current Account Balances, 1970-85
(All Countries)

	Terms of Trade (log TOT)	Growth in Industrial Countries (DGNP)	Real Foreign Interest Rate (RI)	Real Effective Exchange Rate (log REER)	Fiscal Position (FP/Y)	Time Trend (T)	$\bar{R}^2$	SEE	DW
Bangladesh	2.14	0.10	-0.006	-0.88	-0.05	0.15	0.54	0.56	2.17
	(1.87)	(0.12)	(0.02)	(0.89)	(0.09)	(0.14)			
Burma	-0.90	0.02	-0.005	-0.18	0.005	-0.03	0.53	0.22	1.77
	(0.81)	(0.03)	(0.002)	(0.75)	(0.04)	(0.04)			
India	0.08	0.04	-3.34	-0.56	0.11	0.04	0.50	0.15	2.25
	(0.69)	(0.02)	(1.29)	(0.37)	(0.06)	(0.05)			
Malaysia	0.35	0.04	0.001	-0.19	0.02	-0.01	0.77	0.05	2.48
	(0.18)	(0.01)	(0.0006)	(0.26)	(0.006)	(0.009)			
Pakistan	0.36	0.01	-0.007	0.29	0.02	0.07	0.48	0.21	2.90
	(0.65)	(0.05)	(0.005)	(0.51)	(0.06)	(0.05)			
Philippines	1.65	0.05	0.002	-0.92	-0.04	0.04	0.48	0.16	2.40
	(0.87)	(0.02)	(0.003)	(0.86)	(0.05)	(0.04)			
Sri Lanka	0.52	0.03	0.0005	-0.42	0.02	0.04	0.86	0.09	2.82
	(0.26)	(0.02)	(0.001)	(0.19)	(0.008)	(0.02)			
Thailand	-0.29	0.01	-0.004	0.65	0.0004	-0.005	0.06	0.13	2.10
	(0.38)	(0.04)	(0.003)	(1.21)	(0.03)	(0.03)			

Notes: The dependent variable is the ratio of the current account balance to merchandise exports. $\bar{R}^2$ is the adjusted coefficient of determination. Figures in parentheses are standard errors of the respective coefficients. SEE is the standard error of the estimated equation. For Pakistan and Sri Lanka results are after correction for first order autocorrelation using the Cochrane-Orcutt method.

Table IV-14 Regression Results for Current Account Balances, 1970-85
(Country Groups)

	Terms of Trade (log TOT)	Growth in Industrial Countries (DGNP)	Real Foreign Interest Rate (RI)	Real Effective Exchange Rate (log REER)	Fiscal Position (FP/Y)	Time Trend (T)	$\bar{R}^2$	SEE	DW
All Countries	0.15	0.05	-0.003	0.12	-0.02	-0.003	0.34	0.52	1.60
	(0.30)	(0.03)	(0.002)	(0.20)	(0.02)	(0.01)			
South Asia[a]	0.16	0.07	-0.004	0.03	-0.03	0.004	0.23	0.65	1.69
	(0.59)	(0.05)	(0.003)	(0.39)	(0.02)	(0.05)			
Southeast Asia[b]	0.23	0.02	-0.0002	0.27	0.02	0.004	0.28	0.17	1.57
	(0.17)	(0.01)	(0.001)	(0.32)	(0.01)	(0.009)			

Notes: The dependent variable is the ratio of the current account balance to merchandise exports. $\bar{R}^2$ is the adjusted coefficient of determination. Figures in parentheses are standard error of the respective coefficient. SEE is the standard error of the estimated equation.

[a]South Asia includes Bangladesh, Burma, India, Pakistan, and Sri Lanka.

[b]Southeast Asia includes Malaysia, the Philippines, and Thailand.

2. The signs of all three external variables as are expected, but only in one case do the internal variables yield the expected sign.
3. Standard errors of the parameters are again large. This time in one out of every three cases the standard errors exceed the magnitude of the parameter.

The results of this empirical examination provides more questions than answers. The explanatory power of the model is poor and the parameters have wrong signs almost as often as they have correct signs. Large standard errors make any conclusions about the magnitudes of the parameters or elasticities meaningless. One can certainly provide possible reasons (or rationalizations) for such disappointing results, but it is sufficient to say that with the presence of various government interventions in the traded goods sector, restrictions in capital and financial flows in our countries, and the dominant influence of weather (especially the monsoon) in the domestic economies, the results of any econometric examinations of standard trade and balance of payments model will have limited use. The main conclusion that can be derived from this econometric examination is that the data do not support the model as specified in equation (1).

CHAPTER V

THE PATTERN OF RESPONSE TO IMBALANCES IN EXTERNAL PAYMENTS

Imbalances in external payments must be financed. There are a number of possible ways a country can respond to payments difficulties. It can (i) finance the imbalance through net external financing and/or by using its accumulated foreign reserves ("live above its means"), (ii) lower the economic growth rate ("living within one's means"), or (iii) restructure the economy towards export expansion and import substitution ("reallocation of resources"). The choice, of course, depends on the nature and magnitude of the difficulties, the availability of foreign reserves, access to foreign capital markets, the level of development, and so on.

The analysis in this chapter will mainly concentrate on external financing--its nature, sources, and composition--since it was the predominant mode of response for our countries.

USE OF INTERNATIONAL RESERVES

"International reserves form an integral part of a nation's overall portfolio of foreign assets and liabilities."[1] A temporary

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[1]World Bank, World Development Report 1985, p. 83.

measure to finance the current account deficits is the use of international reserves. However, a continued use of reserves will use these up and create a liquidity problem. Fluctuations in reserves thus indicate a temporary policy taken to finance the current account deficits.

Table V-1 shows non-gold reserves as ratios of imports expressed in number of weeks of imports that the reserves can cover. Economists generally agree that reserves less than the value of three months imports is a sign of weakness in the external payments situation.[2] Based on this criterion, the Southeast Asian countries and Burma and India performed better than other three countries. The Southeast Asian countries had reserves less than the value of three months imports mainly in the 1980s, and Malaysia's reserves never fell below that level. The Philippines has had reserves for less than six weeks of imports during the first two years and the last five years. Bangladesh, Pakistan, and Sri Lanka consistently experienced very low reserve/import ratios. Reserves were more than the value of three months imports in only three years for Pakistan, two years for Bangladesh, and four years for Sri Lanka. Reserves came down to less than three weeks imports for Bangladesh in 1981 and for Pakistan in 1979.

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[2]Evelyn M. Go, "Patterns of External Financing of DMC," Asian Development Bank Economic Staff Paper, no. 126 (Philippines: Asian Development Bank, 1985).

Table V-1 Ratio of Non-gold International Reserves to Imports Expressed in Number of Weeks of Imports they Can Cover, 1970-85

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
Bangladesh	..	..	21	6	7	6	16	10	11	11	6	3	4	13	7	6
Burma	9	13	13	34	44	27	32	20	11	19	17	14	13	17	14	6
India	19	20	21	14	10	9	26	38	43	39	24	16	15	18	20	22
Malaysia	23	27	29	27	20	21	33	32	29	26	21	18	16	15	14	21
Pakistan	10	10	17	22	12	8	11	10	7	3	5	7	9	19	9	7
Philippines	8	12	18	29	22	18	21	18	18	18	18	13	6	5	5	6
Sri Lanka	6	7	8	11	6	4	8	22	21	19	6	9	9	8	14	12
Thailand	33	32	34	31	29	27	26	20	20	13	9	9	9	8	10	12

Source: IMF, International Financial Statistics Yearbook (Washington D.C.: IMF, various issues).

Notes: ".." means not available.

One interesting thing to notice is that reserves as proportions of imports have not particularly fallen and risen with the commodity price boom of 1973-74 and 1978-79. For some countries they went up right after the oil price rises. This indicates that some of our countries partially responded with drawing down on reserves to "cushion the impact of external pressure on the domestic economy."[3]

It should be pointed out that there were marked declines in reserve/import ratios for India and Bangladesh before the first oil shock of 1972-73. Faced with the famine in 1973 and America's refusal to provide aid (because of its trade with Cuba) Bangladesh had to use its reserves to finance its imports. India had to use its reserves to import a large quantity of food in 1973 because of the poor harvest resulting from bad monsoon.[4]

NET EXTERNAL FINANCING

The external financing gap can be defined as the current account deficits plus additions to international reserves, as shown in Table V-2. Current account deficits include private transfers

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[3]Dell and Lawrence, The Balance of Payments Adjustment Process in Developing Countries, p. 45.

[4]Bimal N. Jahan, The Balance of Payments Adjustment Process in Developing Countries: The Experience of India, UNCTAD/UNDP, INT/75/015 (New York: United Nations, 1979), p. 3.

Table V-2 Current Account Financing, 1970-85

	1970[a]	1975	1980	1985	1970	1975	1980	1985
	Bangladesh				Burma			
Current Account Deficits	-610	-969	-1521	-1200	-81	-95	-420	-276
Change in Reserves and Related Items	153	37	260	102	55	45	-94	18
Total to Finance	-457	-932	-1261	-1098	-26	-50	-514	-258
Non-Debt Financing								
a. Direct Investment	.	.	.	.	.	.	.	.
b. Official Transfers	370	355	767	658	17	15	73	74
c. SDR Allocations and Gold Monetization	.	.	21	.	9	.	10	.
Debt Financing								
a. Long-Term Borrowing	118	613	520	460	1	41	391	130
b. Short-Term Borrowing	-21	2	-24	-33	-3	-8	..	15
c. Errors and Omissions	-10	-40	-24	13	2	2	40	40
	India				Malaysia			
Current Account Deficits	-531	-325	-2378	-4508	2	-512	-307	-753
Change in Reserves and Related Items	-312	-362	-833	321	-35	-64	-501	-1146
Total to Finance	-843	-687	-1545	-4187	-33	-576	-808	-1899
Non-Debt Financing								
a. Direct Investment	6	-11	.	.	94	351	935	695
b. Official Transfers	137	196	590	324	6	15	22	19
c. SDR Allocations and Gold Monetization	143	.	155	14	21	.	34	.
Debt Financing								
a. Long-Term Borrowing	578	925	1347	3352	2	371	85	829
b. Short-Term Borrowing	-5	11	-181	-51	-6	-66	414	350
c. Error and Omissions	-16	-455	-366	548	-84	-95	-682	-52

Table V-2 Continued

	1970	1975	1980	1985	1970	1975	1980	1985
	Pakistan				**Philippines**			
Current Account Deficits	-705	-1177	-1152	-1449	-138	-1077	-2049	-234
Change in Reserves and Related Items	85	216	-130	159	-112	16	-1117	-101
Total to Finance	-620	-961	-1282	-1290	-250	-1061	-3166	-335
Non-Debt Financing								
a. Direct Investment	23	26	59	134	-25	98	-107	15
b. Official Transfers	38	125	292	381	90	153	148	207
c. SDR Allocations and Gold Monetization	32	-	39	12	37	-	156	222
Debt Financing								
a. Long-Term Borrowing	472	732	889	483	155	419	1034	3102
b. Short-Term Borrowing	-6	87	-68	250	141	577	1812	-3873
c. Error and Omissions	61	-11	70	29	-148	-186	122	660
	Sri Lanka				**Thailand**			
Current Account Deficits	-71	-188	-793	-589	-296	-650	-2207	-1672
Change in Reserves and Related Items	-14	27	265	111	82	52	139	-43
Total to Finance	-85	-161	-528	-478	-214	-598	-2068	-1715
Non-Debt Financing								
a. Direct Investment	..	..	43	26	43	22	190	161
b. Official Transfers	13	77	138	175	46	24	142	119
c. SDR Allocations and Gold Monetization	13	-	16	-	-	-	25	-
Debt Financing								
a. Long-Term Borrowing	30	90	198	304	67	169	1952	1445
b. Short-Term Borrowing	34	-4	117	16	54	215	-61	-127
c. Error and Omissions	-5	-3	16	-43	4	168	-180	117

Source: UN, Handbook of International Trade and Development Statistics (New York: UN, various issues).

Notes: [a]1973 for Bangladesh. ".." means not available.

but exclude official transfers, which are considered a financing item. Thus financing categories include all capital account items plus official transfers. For accounting purposes any addition to reserves is considered as requiring external finance rather than as financing. Grouping the components of external finance into non-debt (direct investment; official transfer; and SDR allocations and gold monetization) and debt financing (long-term borrowing; short-term borrowing; and errors and omissions) show that the shares of debt and non-debt financing fluctuated considerably, and debt-financing exceeded non-debt financing for all countries. The only exception was Malaysia.

Non-Debt Financing

Direct Investment: Direct investment as a means to fill the gap was virtually non-existent in South Asia--only Pakistan had some direct investment toward the end of the period. In Southeast Asia Thailand had some direct investment. Only in Malaysia was the share of direct investment in total financing the major form of financing.

Official Transfers: In non-debt financing, official transfers were the largest, and often the only, source of finance for the external gap. It was an important means to finance the external gap for all the South Asian countries except India, covering 30 to 50 percent of current account deficits in 1985.

SDR Allocations, Gold Monetization, and Others: The flow of resources from the IMF (Oil Facility, Extended Fund Facility, SDR Allocations, Gold Monetization, and Other Related Items) were small, if sometimes crucial, for some countries. A break down of the use of IMF resources into its principal components shows that our countries drew primarily from the facilities that carry low levels of conditionality. For example, use of Trust funds loans was popular among the countries during 1978-80.

Debt Financing

Long-term Borrowing: The share of long-term financing was not only the highest in debt-financing, it was also typically the largest form of financing in both debt and non-debt financing categories for most countries. In some cases long-term borrowing accounted for as much as 94 percent of total financing.

Short-term Borrowing: Short-term borrowing played a minor role in South Asia, but in Southeast Asia it was important and in some years crucial. It was even negative for some countries, particularly the Philippines and Thailand, indicating that long-term borrowing was used to finance the outflow of short-term resources. A large negative amount for the Philippines during 1980s (particularly 1983-85) was the result of calling on short-term loans and halting further loans by the international banks because of unsettling political events.

Errors and Omissions: Errors and omissions, which are really balancing items, were small for most countries. They became higher for India, Thailand, and the Philippines toward the end of period.

Main Sources of Resource Flows

Three main sources are identified--Development Assistance Committee (DAC) members of OECD, multilateral agencies (MULTI), and members of OPEC. Flows from centrally planned economies are not included, partly because consistent data are not available and partly because resource flows from these countries to our countries are of minor significance.

The Flow from the Development Assistance Committee (DAC): The main sources of flow for our countries were DAC member countries (Table V-3). During 1970-85 DAC member countries provided from one-half to three-fourth of the resources: 70 to 75 percent of total resource flows to Burma, Malaysia, Sri Lanka, and the Philippines; 63 percent to Bangladesh and Thailand; and 53 percent to Pakistan and India.

The share of DAC resource flows to our countries declined over the period. In 1970 the share of DAC was at least three-fourths of total flows. In 1985 it ranged from one-half to three-fourths. The decline was substantial for some countries. For example, the DAC share of total financing declined from 92 percent to 51 percent for India, from 83 percent to 46 percent for Pakistan, and from 95

Table V-3 Distribution of Sources of Net Total External Resources (Percentages), 1970-85

	1970[a]	1975	1980	1985	1970	1975	1980	1985
Bangladesh					**Burma**			
DAC	72.9	65.3	68.3	53.5	100.0	44.9	80.6	71.4
MULTI	27.1	28.9	27.9	45.7	0.0	55.1	19.4	28.6
OPEC	0.0	5.7	4.0	0.8	0.0	0.0	0.0	0.0
India					**Malaysia**			
DAC	91.6	48.0	33.7	51.3	77.8	77.5	83.2	79.9
MULTI	8.8	39.5	67.5	50.2	22.2	21.9	15.4	13.7
OPEC	0.0	12.0	-1.2	-1.5	0.0	1.0	1.5	6.4
Pakistan					**Philippines**			
DAC	82.6	29.0	40.0	46.2	94.7	65.1	63.2	60.8
MULTI	17.4	16.6	36.8	59.9	5.7	34.9	36.1	39.4
OPEC	0.0	54.4	23.1	-5.9	0.0	0.0	0.7	-0.2
Sri Lanka					**Thailand**			
DAC	88.0	20.3	77.2	74.0	84.0	57.7	70.1	55.6
MULTI	11.9	36.6	20.7	25.0	16.0	45.3	28.9	43.2
OPEC	0.0	42.6	2.1	1.0	0.0	0.0	0.9	1.3

Sources: OECD, Geographical Distribution of Financial Flows to Developing Countries (Paris: OECD, various issues); UNCTAD, Handbook of International Trade and Development Statistics (New York: UN, various issues).

Notes: [a]1973 for Bangladesh; DAC = Development Assistance Committee of OECD; MULTI = Multilateral Agencies; OPEC = Organization of Petroleum Exporting Countries.

percent to 61 percent for the Philippines. The flows from DAC declined for all countries during 1970-75. For most countries the share went up again in 1975-80.

The main reason for the decline in the flow of resources to our countries was the sudden rise in oil prices that channeled a huge amount of resources from industrialized countries to the OPEC countries.

The United States and Japan was the two most important donors to our countries. Resource flows from Japan were traditionally important in Southeast Asian countries and Burma. Japan's donation became important in South Asian countries toward the end of the period.

The Flow from the Multilateral Agencies (MULTI): Multilateral agencies were the next important sources of external resources. The decline in DAC resource flows were compensated by the increased flow from the MULTI agencies. This change in the source of resource flow was a new event for our countries. The share of MULTI roughly equals or exceeds the share of DAC in 1985. Of all the multilateral agencies, the flows from IDA were the most important in South Asian countries. The Asian Development Bank also provided significant amount of resources to most countries. The World Bank loans were important for most countries, particularly India, Malaysia, Thailand, and the Philippines.

The Flow from the Members of OPEC: A notable feature of the resource flows of the 1970s was the emergence of OPEC (mainly Arab members) nations as donors. The flow from members of OPEC was nonexistent at the beginning of the 1970s. After the oil price shock OPEC started to provided resources to developing countries. But this flow also declined with the decline of oil price in the 1980s. The share of OPEC resource flows in total flows was small compared to DAC or multilateral agencies. Only three countries--Bangladesh, Pakistan, and India--were the main beneficiaries of resource flows from members of OPEC. In many cases OPEC flows were used for deferred payments on oil imports. Southeast Asian countries and Sri Lanka and Burma did not receive any significant amount from OPEC except in a few isolated years.

The proportion of flows from the OPEC countries fluctuated over the study period. For example, for Bangladesh OPEC accounted for less than 10 percent of total resource flows; the only exception was in 1977 when it was 22 percent. For India it was high during 1978-80 when OPEC accounted for 18 percent of the total flow. The resource flow from OPEC to Pakistan fluctuated a lot: 80 percent in 1974, down to 9 percent in 1977, then up to 23 percent in 1980. For Sri Lanka OPEC funding was a significant source of net external financing in 1976 and 1977 and for Thailand in 1977.

Resource flows from OPEC went mainly to the countries with which the Arab members had a long cultural, historical, and religious

affinity: Bangladesh, Pakistan, and India.[5] It is likely that a large Muslim population in Bangladesh, Pakistan, and India was an important reason why these countries received more funds from OPEC than other countries in our study.

Composition of Financial Flows

The composition of net resource flows to our countries can be categorized under two main headings:

1. Official Development Finance from official bilateral and multilateral institutions and consists of:

(a) Official Development Assistance (ODA). Each ODA transaction contains a grant element of at least 25 percent. ODA can be subdivided into Grants (gifts--in money or in kind--for which no repayment is required or repayment is required in recipient's currency) and Loans with maturities of over one year.

(b) Other Official Flows that are less concessional or non-concessional public flows.

2. Private Flows that consist mainly of direct investment and export credits.

The breakdown of net financial flows into these categories is shown in Table V-4. Several interesting patterns emerge from this table. With the exception of Malaysia, official flows were

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[5]George Abbott, International Indebtedness and the Developing Countries (London: Croom Helm Ltd., 1979), p. 57.

Table V-4 Composition of Net Financial Flows (Disbursements), 1970-85

	1970[a]	1975	1980	1985	1970	1975	1980	1985
	Bangladesh				**Burma**			
Official	225	1,094	1,253	1,136	22	55	314	356
ODA	224	1,018	1,262	1,151	23	58	309	356
Grants	210	373	1,160	641	21	33	98	107
Loans	14	645	103	641	2	25	211	249
Other Official	·	76	·9	·15	·1	·4	6	·
Private	·2	·10	6	·17	8	·6	89	1
	India				**Malaysia**			
Official	823	1,666	2,260	1,807	45	160	217	380
ODA	825	1,708	2,127	1,527	27	99	135	229
Grants	204	588	798	630	17	32	61	103
Loans	622	1,120	1,329	897	9	66	75	127
Other official	·2	·43	132	280	18	61	82	150
Private	19	33	129	653	45	152	472	·145
	Pakistan				**Philippines**			
Official	472	750	1,112	908	146	293	534	882
ODA	27	892	1,040	735	46	180	304	486
Grants	17	221	602	429	32	105	123	245
Loans	9	672	438	306	14	75	180	242
Other official	18	·142	72	173	100	113	230	396
Private	45	·91	114	·47	172	106	442	·247
	Sri Lanka				**Thailand**			
Official	57	208	396	503	127	157	731	806
ODA	49	175	393	485	74	90	418	481
Grants	21	81	221	206	55	53	178	264
Loans	28	94	171	279	20	37	240	217
Other official	8	34	4	18	52	68	313	325
Private	2	·65	38	82	73	31	382	74

Sources: OECD, Geographical Distribution of Financial Flows to Developing Countries (Paris: OECD, various issues); UNCTAD, Handbook of International Trade and Development Statistics (New York: UN, various issues).

Notes: [a]1972 for Bangladesh; ODA = Official Development Assistance.

consistently the major ones. The share of net official flows exceeded private flows by a wide margin for all countries, but there were wide variation among countries. South Asian countries depended more on official flows than Southeast Asian countries.

While official flows grew for all countries, private flows fluctuated during the period. Private flows, mainly for South Asian countries, were small or even negative in some years. For example, in Pakistan official flows increased from $472 million to $908 million between 1970 and 1985 but private flows declined from $45 million to a negative $47 million. As is to be expected, the share of ODA flows was the largest in official flows. Other official flows were important for Southeast Asia but not South Asia. Except for Bangladesh, Burma, and India, the shares of grants and loans in ODA were roughly equal. For South Asia concessional flows ranged from 80 to 98 percent of total flows, but for Southeast Asia they were only 20 to 45 percent.

The forgoing analysis shows that our countries (except Malaysia) preferred debt financing over non-debt financing as a means to finance the external imbalances. Foreign direct investment (a component of non-debt financing) played no role or a minimal role in six or perhaps seven countries. While Pakistan, Bangladesh, the Philippines, and Sri Lanka tried (and failed) to attract foreign investment, India and Burma preferred not to pursue the policy. Only Malaysia was successful in pursuing this policy.

Initial responses to the external payments pressures were to draw funds from the IMF. While the absolute amount of IMF funds covered only a small portion of the deficits, nevertheless it was important because it enabled many countries to obtain financing from other sources. It should be mentioned that the attitudes towards borrowing from the IMF were mixed. For example, between 1974 and 1977, the Philippines had no problem in reaching agreements with the IMF to secure commercial loans. However, India did not want any outsider controlling their economy and was cautious in borrowing. During 1973-75 India borrowed only 3 billion rupees from the IMF's Extended Fund Facility and regular credit tranches although it could have borrowed a maximum of 24 billion rupees.[6]

The financing problem of current account deficits were met mainly by reliance upon long-term borrowing (another component of debt financing). The South Asian countries were particularly more dependent on long-term borrowing than the Southeast Asian countries. Despite huge current account deficits after the first round of rises in oil prices, the availability of external financing helped to moderate the BOP pressures, and in some cases even shored up the level of reserves, at least until 1980. This is one reason why countries like India, Bangladesh, the Philippines, and Sri Lanka

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[6]Dell and Lawrence, The Balance of Payments Adjustment Process in Developing Countries, p. 45.

experienced high level of reserves during late 1970s.[7] However, after the second round of rises in oil prices, long term concessional flows, which had traditionally been the main sources of financing, were difficult to obtain. The Philippines, and to a lesser extent Malaysia, turned to short-term loans to cover the payments imbalances. Even India resorted to commercial borrowing to supplement financing available from traditional sources.[8]

Net total resource flows grew significantly for all countries in nominal terms but, then declined as percentages of GNP. After picking up in the late 1970s net total resource flows as percentages of GNP averaged 5.3 percent for South Asia, but only 1.7 percent for Southeast Asian countries in 1985. At the beginning of the period, the main sources were DAC member countries; but flows from MUTLI agencies increasingly became important towards the end of the period. OPEC emerged as the important sources of funds for three Muslim populated South Asian countries. The share of official flows exceeded private flows, and the South Asian countries depended more on official flows than did the Southeast Asian countries.

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[7]Eli M. Remolona, Mahar Mangahas, and Filologo Pante, Jr., "Foreign Debt, Balance of Payments, and the Economic Crisis of the Philippines in 1983-84," World Development, vol 14, no. 8 (August 1986), pp. 993-1018.

[8]Montek Singh Ahluwalia, "Balance-of-Payments Adjustment in India, 1970-71 to 1983-84," World Development, vol 14, no. 8 (August 1986), pp. 937-962.

EXPORT PROMOTION AND IMPORT SUBSTITUTION

Although our countries relied mostly on external financing, this does not mean that they did not take other adjustment measures. Export promotion (defined as the change in 1972 export market shares, in turn estimated as the difference between the constant-price value of actual and hypothetical exports) and import substitution (defined as the savings in imports associated with the decrease in the import elasticity of demand for imports) were also important. This is shown in Appendix C (particularly Table C-1). Southeast Asian countries were successful in increasing their export market share, with Malaysia doing better than Thailand and the Philippines. In South Asia, only India had some success in increasing its export market share, while others in fact lost some. The poor export market penetration of Burma, Pakistan, Sri Lanka, and Bangladesh (not listed in the table, but analysis applies equally it) was the result of sagging external demand, rising costs, and stagnating productivity.[9] For example, jute exporting countries (Bangladesh, India, and Pakistan) experienced a rise in the cost of production at a time when industrialized countries were substituting synthetic products. Recall that in chapter II (Table II-7, page 37) I had produced evidence of declining export market shares for six countries (except Malaysia and Thailand).

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[9]Naya, Kim, and James, "External Shocks and Policy Experiences," p. 8.

Import-substitution policy was also applied as a long term measure to counter adverse BOP problems; but, countries generally associated with pursuing an import-substitution development strategy (India, Burma, Pakistan) had poorer records than export-oriented countries.

Helleiner also shown that both export promotion strategy and import-substitution strategy were pursued during 1973-82 with more success in 1978-82 than 1973-78 (Appendix C). Similar results were obtained by Balassa.

TEMPORARILY LOWER ECONOMIC GROWTH

One way to adjust to external pressure is to reduce imports by lowering the rate of growth of GNP. This was a common approach for the highly indebted countries that experienced BOP problems in the 1980s. For example, Khan and Knight reports that during 1982-86 volume of exports grew at an average annual rate of just over 1 percent but imports fell at an average rate of nearly 10 percent for the fifteen most heavily-indebted developing countries.[10] A similar pattern was evident for most other developing countries. However, Khan and Knight also reports that the only exception was Asian

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[10]Mohsin S. Khan and Malcolm D. Knight, "Import Compression and Export Performance in Developing Countries," Review of Economics and Statistics, vol. LXX, no. 2 (May 1988), p. 315.

countries. According to Naya, Kim, and James this mode of adjustment was not a particularly popular policy (Appendix C). South Asian countries and the Philippines either maintained or increased their growth rates during 1974-82, suggesting that contraction of domestic demand was not used as a means to cushion the external payments imbalance. Investment/GDP ratio either increased or remained stable for all countries during the period. Only exception was the Philippines where it increased from 21 percent in 1970 to 31 percent in 1981, then fell to 14 percent in 1985. However the decline in investment ratio there was in fact the result of political disturbances rather than response of balance of payments crisis.

To see to what extent our countries resorted to reductions in import volumes during the crucial years, simple percentage changes of import volumes were calculated for the years between 1973 and 1975, between 1978 and 1981, and between 1982 and 1985. The volume of imports did not fall during those sub-periods. On the contrary, India, Sri Lanka, Pakistan, and the Philippines liberalized their imports at a time when their external payments positions were not favorable.[11] Thus import reduction to lower GNP growth rate was not a popular policy for our countries.

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[11]David Greenway, "Characteristics of Industrialization and Economic Performance Under Alternative Development Strategies," Background paper for Chapter 4, World Development Report 1987 (New York: Oxford University Press, 1987), Table 7.

CHAPTER VI

CONCLUSIONS

The purpose of this study was to examine the trade and balance of payments problems of selected countries of South and Southeast Asia, from 1970 to 1985. Eight South and Southeast Asian countries were selected for the study: five from South Asia (Bangladesh, Burma, India, Pakistan, and Sri Lanka) and three from Southeast Asia (Malaysia, the Philippines, and Thailand). These countries were selected because recent trade and development literature has largely ignored the area, dealing mainly with the success stories of East Asia, the debt problems of Latin America, or stagnation in Sub-Saharan Africa. Together these countries have a population of over a billion and, within the group, per capita GNP varies from a low of $150 in Bangladesh to a high of $2000 in Malaysia.

The salient points made can be summarized under the headings: structure of trade; structure of services and transfer accounts; balance of payments pressures; trade and development strategies and the balance of payments; empirical examination of the causes of BOP problem; and financing of external payments imbalances.

STRUCTURE OF TRADE

1. The foreign trade of the region was marked by rapid growth. Between 1970 and 1985 exports increased by at least three to four times or more and imports increased at even a higher rate. The countries with higher levels of per capita GNP also had higher levels of per capita exports and imports. While the secular trend of exports and imports was upward in the region, its growth was not evenly spread and also the growth rate was higher in the 1970s than in 1980s.

2. The major contributor to growth of trade was increasing unit values; volume growth played only a minor role. Most countries lost some export share in world markets even though world trade increased as a whole during the study period.

3. The exports of our countries, like those of most developing countries, are highly concentrated in a few commodities, but there were clear signs of deconcentration throughout the period.

4. The commodity composition of trade varied among countries. Food (Burma, Sri Lanka, Thailand, and the Philippines) and manufacturing goods (India, Pakistan, and Bangladesh) were the two leading export items from the region, but fuel became a leading export category for Malaysia toward the end of 1970s. Although the traditional export items (i.e., food and manufactured goods) remained

the same for each country all of them achieved a marked increase in the manufacturing exports. Although the successes were not as spectacular as those of East Asian countries, nevertheless Southeast Asian countries and Sri Lanka's achievement were particularly spectacular. "Textile and Cotton including Garments and Leather" category of manufactured goods, a labor intensive category, largely accounted for the increased manufacturing exports.

5. The commodity composition of imports also experienced important changes. In general food imports declined in the region as a result of increased food production. Capital goods imports increased in the three poor countries--Bangladesh, Burma, and Sri Lanka--while it declined for rest of the countries. Industrial supplies were the major import items in the intermediate goods category.

6. The direction of trade shifted to some extent. While industrial countries are still the largest purchasers of exports from the region, in a number of cases the importance of industrial countries as trading partners declined over the study period. A notable feature of the geographic composition of trade was that exports from our countries to Middle East countries increased significantly for most countries. Trade among the sample countries of the study was low, and with the centrally planned economies was, at best, minimal (except for India).

The countries were dependent on the industrial countries to a large extent for imports. However, there was a tendency to replace industrial countries with the newly industrializing countries and other developing countries as sources of imports for light consumer goods, and even for some intermediate goods.

STRUCTURE OF SERVICES AND TRANSFER ACCOUNTS

1. The study also examined the pattern of services and transfer account of our countries. Again a significant change can be observed for most countries. The growth in services trade (credit + debit) was higher than merchandise trade for all countries over the period. A contributing factor to the increased service trade was the result of a dramatic increase in "tradeability" of services, made possible by revolutionary developments in information, communication, and transportation technologies. In general the countries with higher ratios of exports or imports to GDP also had higher ratios of services credits or debits to GDP.

2. The shipping balances were consistently negative for our countries and were mainly responsible for the deficits in the total services accounts. The traditional practice of the shipping business, where developing countries accept f.o.b. terms for their exports and c.i.f. terms for their imports, was one reason why our countries, like other developing countries, experienced deficits in

this account despite their growing shipping capacity. Further, the level and structure of freight rates militated against our countries, thus affecting not only the services accounts but also the trade accounts.

3. In the services accounts only the travel accounts show some encouraging trend, and only for some countries. All countries in the study show deficits in investment income account, a pattern common to developing countries in general.

4. Unrequited transfer payments, both private and public, played and important role for several countries. Private transfer payments, mainly remittance earnings, were important for three of the South Asian countries--Bangladesh, India, and Pakistan. The amount of remittance earnings ranged from one-fifth to one-half of their import bills. In addition, the traditional source of remittance earnings changed for these countries during the period. The United Kingdom was the traditional source of remittance earnings, but Middle Eastern countries became the main source of remittances after the first oil shock. All countries in our study registered surpluses in the official transfer accounts, a pattern common to developing countries in general.

BALANCE OF PAYMENTS PRESSURES

1. The deficits in the trade and the current accounts was a common characteristic for our countries (except Malaysia). Many countries experienced trade and BOP deficits of unprecedented magnitudes during the period. The ratios of current account deficits to exports were as high as 80 percent for some countries. The BOP pressure was more serious for the poor countries of South Asia.

2. Except for Malaysia, all countries suffered from adverse external shocks. For some countries the shock was as high as one-fourth of GNP. The shocks, not surprisingly, were higher for countries with higher trade ratios.

3. While a significant part of the external payments problems could be attributed to domestic mismanagement, the principal reasons for deficits in the trade and current accounts were external, i.e., the factors beyond the control of the deficit countries.
The external factors responsible for the external payments problem were adverse movements in terms of trade, recessions in industrial countries, and a rise in real interest rate. While hardly responsible for these developments, our eight countries nevertheless had tremendous burdens imposed upon them.

4. The terms of trade showed a declining trend over the period for most countries. A significant part of the deterioration in the

terms of trade was caused by increasing import prices that resulted from the historic rises in oil prices in 1973-74 and 1978-79. While all eight countries rode out of the crises the net oil import bills doubled in 1973-74. Although the impact was not as severe in 1979-80, still the net energy import bill dominated the changes in trade balances in most countries.

5. The effects of the oil price rises were further aggravated by recessions in industrial countries in 1974-75 and 1980-83, each time followed by a relatively slow recovery. These resulted in decline in growth of exports from our countries. Consequently, industrial countries were able to shift a part of their balance of payments pressure to our countries.

6. Sharp increases in real interest rates in the international capital market in the late 1970s and 1980s were another factor causing balance of payments problems. However, the problem from this source was not so serious as it was for some Latin American and African countries, largely because our countries mainly relied on official sources rather than on private sources for their external financing.

7. Domestic factors may also have contributed to the BOP problem: average fiscal balance for each country was negative for the period. The continuing rise in real effective exchange rates

caused demand for imports to rise and foreign demand for exports to fall, further contributing adversely to the BOP.

TRADE AND DEVELOPMENT STRATEGY AND BOP

1. Trade and development strategies played important roles in determining the BOP position of a country: current account deficits were higher in countries pursuing import-substitution strategies and lower in countries pursuing export-oriented strategies.

EMPIRICAL EXAMINATION OF THE CAUSES OF BOP PROBLEMS

1. An econometric analysis of the proximate causes of the BOP problems was also presented. The empirical model specified was a reduced form model. The dependent variable was the ratios of current account balance to exports and the independent variables were terms of trade, growth of real GNP in industrial countries, real interest rates, real effective exchange rate, ratios of fiscal balance to nominal GNP, and a linear time trend. The ordinary least squares analyses for both individual and pooled time-series and cross-section had poor results. The regression results generally show moderate explanatory power for individual countries but not so good for the pooled model. The signs of the variables were often perverse and/or the magnitudes too low. Except for the real effective exchange rate,

the signs of all independent variables had the expected sign in the pooled model. The low value of the parameters indicate the difficulty in modeling the standard trade theories for developing countries. Many non-economic factors--political situation, war, weather, and so on--play important roles in developing countries.

FINANCING OF IMBALANCES IN THE EXTERNAL PAYMENTS

1. Imbalances in the external payments were financed mainly through the net external borrowing. The main component of external financing was debt-finance. In non-debt financing official transfer was the largest means to finance the BOP gap.

2. The main sources of external borrowing were the DAC member countries of OECD, followed by multilateral agencies. The flow from the OPEC countries was important during the 1970s, but only for the Muslim populated countries: Bangladesh, India, and Pakistan. South Asian countries depended on official flows more than did the Southeast Asian countries.

3. Southeast Asian countries were more successful in export promotion than were South Asian countries. Reducing imports through lower GNP growth was not a popular policy.

THOUGHTS FOR FUTURE

It is unlikely that the character of trade and current account deficits will change in the near future. The eight countries will continue to experience BOP deficits. Without a favorable international environment our countries will not be able to improve external payments situation. Such an environment implies improvement in the terms of trade of our countries coupled with strong economic growth, high import growth rates in industrial countries, and few protectionist or discriminatory measures against the exports of our countries. In addition, real effective exchange rates (home currency) need to depreciate if the countries are to remain competitive in international markets. Finally, a larger and steady flow of long term capital at concessional rates will also be needed to allow the eight countries to make necessary structural changes in the domestic economy so that they have the capacity to respond to external payments problems of both external or internal origin.

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APPENDICES

Appendix A Destination of Exports (Percentage of Total Value of Exports), 1970-84

Table A-1 Bangladesh

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
USA	..	..	14.8	20.3	18.1	15.8	17.0	14.3	15.2	13.9	11.7	11.6	11.2	12.0	15.2
Belgium-Lux	..	..	..	5.1	3.9	2.5	3.5	3.4	2.8	3.2	3.2	2.7	3.3	4.6	7.5
Pakistan	..	..	..	0.0	0.0	0.0	0.0	6.5	8.7	5.3	9.5	6.7	9.7	7.8	7.4
Japan	..	..	2.2	2.9	4.0	1.7	2.6	2.5	3.7	6.5	3.1	4.2	6.1	6.6	7.2
Italy	..	..	..	3.2	3.2	2.8	6.7	5.9	5.3	7.2	4.2	4.6	3.9	6.6	6.6
UK	..	..	..	12.1	7.1	6.0	7.4	13.1	6.1	7.7	4.0	4.9	5.0	5.5	5.9
Iran	..	..	..	2.2	1.9	5.1	0.0	3.5	2.7	3.4	5.4	6.2	2.5	11.4	5.9
USSR	..	..	..	4.4	4.8	7.8	3.5	4.4	7.2	8.4	5.1	5.5	5.5	5.0	3.3
Mozambique	..	..	..	3.4	6.3	6.1	0.0	0.0	3.6	3.7	4.1	10.5	4.2	1.5	1.5
China	..	..	..	0.0	0.0	0.0	1.2	1.6	5.0	2.8	5.0	2.5	3.9	2.6	1.1

Table A-2 India

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
USA	13.5	16.2	15.3	13.6	13.0	11.1	11.9	11.9	13.3	11.5	11.3	9.6	14.8	23.2	26.3
USSR	13.4	13.8	15.2	13.2	12.0	11.7	9.0	11.4	8.8	8.6	16.8	19.5	15.1	17.0	17.3
Japan	14.0	11.5	11.2	13.6	10.1	10.3	11.0	9.9	9.8	10.4	9.7	6.9	10.9	11.2	10.9
UK	11.6	10.2	9.9	9.9	9.9	9.6	10.4	10.0	8.4	9.1	6.1	4.7	6.5	5.5	7.4
Germany, F R	2.2	2.2	3.0	3.4	3.1	3.0	4.2	4.5	4.5	5.4	5.7	4.1	5.1	4.9	4.8
Saudi Arabia	1.0	0.7	0.8	0.8	1.2	1.4	1.6	2.2	2.3	2.7	2.7	2.2	3.1	2.8	2.7
Netherlands	0.9	0.9	1.6	2.4	2.5	1.9	3.1	2.9	2.8	3.7	2.4	1.5	1.1	1.7	2.6
France	1.2	1.4	2.2	1.9	2.3	2.5	2.5	2.8	2.9	2.9	2.2	1.6	6.4	2.3	2.2
Arab Emirates	0.3	0.4	0.5	0.6	1.4	1.5	2.7	3.1	2.5	2.3	2.4	2.3	2.5	2.3	2.1
Belgium-Lux	1.3	1.4	1.5	1.6	1.9	1.0	1.7	3.1	3.9	2.8	2.4	1.0	2.1	2.6	1.8

Table A-3 Malaysia

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
Japan	18.3	18.2	17.1	18.1	16.9	14.5	21.1	10.4	21.6	23.4	22.8	21.1	20.4	19.7	22.9
Singapore	21.6	22.5	23.3	23.2	21.7	20.3	18.3	15.9	16.2	17.4	19.1	22.8	25.0	22.5	20.5
USA	13.0	12.7	13.8	10.8	14.0	16.1	15.6	18.2	18.6	17.3	16.3	13.0	11.5	13.2	13.5
Korea R	2.6	2.6	1.6	2.2	1.8	1.7	1.8	1.7	1.8	1.9	2.0	3.7	3.7	4.7	5.0
Netherlands	3.2	3.3	5.1	3.7	5.5	8.4	6.6	6.6	5.6	5.6	6.0	5.9	6.0	5.5	4.1
India	0.4	0.6	0.9	1.0	0.6	0.7	0.6	2.6	3.3	2.1	2.2	2.6	1.8	2.4	3.6
Germany F R	3.1	2.7	3.1	3.8	3.9	4.3	4.3	3.7	3.6	3.7	3.6	2.9	2.9	3.2	3.1
Thailand	0.9	1.5	0.8	0.5	0.9	1.5	1.3	1.4	1.3	1.3	1.5	1.7	3.7	4.1	2.8
U.K.	6.6	6.5	7.0	7.9	6.6	6.0	4.9	5.1	4.8	3.9	2.8	3.0	2.7	2.7	2.6
USSR	4.1	3.0	2.1	3.4	4.1	2.6	2.2	2.0	1.9	2.3	2.2	2.2	2.0	2.1	1.3

Table A-4 Pakistan

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
Iran	0.7	1.1	0.9	1.5	6.3	1.8	3.1	7.8	2.7	2.8	7.6	5.5	4.2	16.0	10.3
USA	11.8	10.1	5.0	4.2	5.0	4.4	5.9	5.0	6.3	5.8	5.3	7.1	7.1	6.3	10.1
Japan	5.9	8.3	16.3	13.9	5.7	6.8	7.9	7.2	10.3	8.2	7.8	7.2	9.0	8.0	9.3
Saudi Arabia	0.8	1.7	2.1	2.1	5.2	6.3	5.5	5.2	4.5	5.4	5.4	6.8	8.4	8.6	7.3
UK	10.4	9.8	8.1	7.4	6.3	6.2	6.3	7.5	6.3	6.3	4.2	4.8	5.6	4.4	6.2
Germany F R	3.6	3.3	3.6	3.7	4.6	5.0	5.5	6.0	5.9	6.2	5.5	4.1	4.2	4.4	5.5
Arab Emirates	0.8	1.5	1.6	2.2	3.9	4.0	4.4	3.8	3.4	5.5	5.1	6.1	6.5	9.4	5.3
Italy	2.9	2.8	5.5	4.4	3.8	2.9	4.3	2.8	3.4	4.0	3.2	2.9	3.4	2.9	4.3
China	5.4	4.5	2.5	1.5	1.0	1.3	1.5	1.5	2.2	1.2	8.5	6.1	6.0	4.7	1.6
Hong Kong	5.3	8.7	13.7	13.3	6.4	11.1	8.3	4.5	8.9	6.9	6.5	3.4	5.0	3.1	1.5

Table A-5 Philippines

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
USA	41.0	40.3	41.8	37.2	43.0	29.8	36.8	35.8	34.3	30.2	27.5	30.9	31.6	36.0	38.0
Japan	39.6	35.6	33.8	37.3	35.3	37.4	23.5	22.5	22.9	26.4	26.6	21.9	22.9	20.5	19.4
Singapore	0.7	1.4	0.8	0.8	0.7	1.4	2.2	2.1	2.1	1.4	1.9	2.3	2.2	2.8	6.0
Hong Kong	1.1	1.3	1.3	2.1	1.2	1.2	1.6	1.7	2.7	3.4	3.3	3.9	3.9	3.4	4.4
UK	1.0	0.9	1.1	1.1	1.3	2.7	2.2	1.9	2.7	3.0	2.5	3.4	3.8	4.6	4.2
Germany F R	1.9	2.9	3.7	3.5	2.5	3.0	4.2	4.4	4.3	4.9	4.4	4.2	6.5	4.0	3.3
Malaysia	0.0	0.0	0.0	0.3	0.2	0.2	0.2	1.0	1.1	1.2	1.6	1.8	3.5	3.2	3.3
Netherlands	4.1	6.9	7.3	5.0	5.9	7.9	8.4	9.1	8.4	7.8	6.3	5.6	3.8	6.1	3.1
Korea R	3.0	2.5	1.4	1.5	0.7	0.7	1.0	0.8	1.9	3.1	3.5	3.5	3.0	3.0	1.8
USSR	0.0	0.0	0.1	0.4	0.7	0.5	3.5	4.2	1.2	1.8	3.3	3.0	2.3	1.7	1.0

Table A-6 Sri Lanka

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
USA	7.3	8.5	6.7	6.9	7.0	5.6	7.0	7.5	7.0	10.4	11.1	14.0	14.1	17.4	19.3
Iraq	2.8	5.2	0.0	0.0	3.3	4.8	3.0	5.4	3.5	3.0	3.5	2.9	4.6	4.6	7.1
Egypt	2.7	2.6	0.0	2.0	0.5	3.1	2.1	4.6	4.2	2.8	3.3	3.1	4.0	6.8	6.3
UK	22.8	17.2	12.7	11.1	10.3	8.0	9.7	8.0	7.9	8.1	7.4	6.5	6.7	5.0	5.9
Gremany F R	4.1	3.8	3.4	4.5	5.7	3.0	3.4	3.9	4.3	5.9	5.3	6.0	5.5	6.1	4.9
USSR	4.1	5.0	3.1	2.4	2.9	2.6	3.2	1.9	1.5	3.1	3.0	2.3	2.2	3.7	4.4
Japan	2.9	3.4	2.8	4.6	3.8	4.6	4.5	4.9	5.8	6.8	3.2	4.9	5.0	4.5	4.3
Saudi Arabia	0.0	0.0	0.0	0.0	1.8	2.4	2.5	2.6	4.7	2.9	3.5	3.2	2.7	3.2	3.5
Pakistan	2.1	5.7	7.4	8.2	7.7	8.8	7.5	8.0	5.2	4.5	3.3	5.4	3.8	2.8	2.4
Netherlands	1.7	1.2	0.0	2.2	2.9	1.8	2.4	2.8	2.8	3.2	2.7	2.3	3.3	3.0	2.3

Table A-7 Thailand

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
USA	13.4	13.0	12.6	9.5	7.9	10.6	10.0	9.7	11.0	11.2	12.7	12.9	12.8	15.0	17.2
Japan	25.5	24.7	20.7	26.9	25.5	27.8	25.8	19.7	20.3	21.2	15.1	14.2	13.7	15.1	13.0
Netherlands	8.6	8.0	8.0	9.4	8.6	10.2	13.3	13.4	14.7	11.3	13.2	12.2	13.1	10.8	10.0
Singapore	6.9	7.0	8.7	7.7	8.2	9.1	6.8	6.3	8.1	8.5	7.7	7.8	7.3	8.1	8.4
Malaysia	5.6	4.3	5.0	6.2	4.8	4.7	4.2	5.3	5.2	4.4	4.5	4.6	5.2	4.5	4.7
Hong Kong	7.5	6.9	7.4	7.5	7.1	6.1	5.0	4.7	5.3	4.9	5.1	4.8	5.0	5.0	3.8
Germany F R	3.6	3.7	2.5	2.4	2.2	2.5	3.2	3.5	4.1	4.1	4.1	3.2	3.3	3.5	3.3
Saudi Arabia	2.2	1.3	0.7	1.3	1.5	1.4	1.3	1.0	1.4	1.7	1.7	2.0	2.7	2.9	2.6
China	0.0	0.0	0.0	0.0	0.0	0.9	2.1	2.9	1.8	1.5	1.9	2.7	4.4	1.7	2.5
USSR	0.0	0.7	0.3	0.2	0.9	0.4	0.1	0.1	0.2	0.8	2.5	4.4	2.6	1.0	1.0

Source: IMF, Direction of Trade Yearbook (Washington D.C.: IMF, various issues); UN, Yearbook of International Trade Statistics (New York: UN, various issues).

Note: ".." means not available.

Appendix B Origins of Imports (Percentage of Total Value of Imports), 1970-84

Table B-1 Bangladesh

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
Japan	..	..	8.9	9.0	7.5	7.4	2.5	21.6	11.7	13.3	13.7	16.0	12.6	12.9	13.2
Singapore	..	..	1.4	0.9	1.3	2.3	1.8	0.1	4.8	5.4	9.4	10.4	13.5	12.8	12.4
USA	..	..	27.6	21.3	21.5	28.4	28.5	10.3	19.3	12.5	15.3	10.3	11.5	13.2	11.1
China	..	..	0.0	0.1	0.1	0.8	0.9	2.2	3.2	4.6	5.1	6.9	5.1	5.3	5.6
Australia	..	..	1.1	1.8	7.1	3.9	1.8	0.0	2.0	5.5	2.7	3.3	2.8	2.1	4.7
Korea S	..	..	0.0	0.4	0.9	0.3	0.5	0.8	3.6	2.6	4.1	3.8	3.7	4.7	4.5
India	..	..	17.1	13.1	6.5	5.0	8.0	8.7	2.8	4.6	5.1	4.5	3.7	4.1	4.1
Germany F R	..	..	3.5	4.5	11.6	6.0	6.0	4.1	3.8	5.9	4.3	5.6	3.8	4.2	4.0
Canada	..	..	..	4.8	9.7	6.4	9.7	3.6	4.8	4.1	2.1	3.4	5.2	5.2	3.9
UK	..	..	..	7.1	5.1	2.7	4.9	4.7	6.5	7.2	8.4	6.5	4.8	4.8	3.7

Table B-2 India

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
USA	29.0	22.9	14.2	17.8	13.7	22.4	24.9	12.9	12.0	10.4	11.5	9.3	11.9	14.3	11.5
USSR	7.9	4.3	4.6	3.8	9.5	4.1	3.3	3.0	3.2	5.5	4.0	5.3	8.0	9.3	9.1
Japan	4.6	8.3	9.3	9.2	9.3	8.1	5.9	7.4	7.6	8.3	5.0	5.9	10.4	11.2	8.5
Saudi Arabia	0.9	2.1	0.1	0.1	0.1	0.1	0.1	0.1	2.3	4.5	4.6	5.0	11.2	9.5	7.9
Iran	4.6	6.6	0.3	0.3	0.4	0.3	0.2	0.3	5.1	4.4	10.4	12.2	11.1	9.3	7.8
UK	6.7	11.6	12.6	10.2	5.2	5.1	5.9	7.5	7.4	8.5	5.4	5.7	10.5	9.5	7.6
Germany F R	6.5	6.7	8.7	7.2	6.6	7.2	6.1	9.0	8.9	7.4	5.3	6.0	6.4	6.5	6.7
Belgium-Lux	0.6	1.5	2.7	2.7	1.6	2.2	1.1	2.1	5.2	3.4	2.4	3.8	4.8	4.5	4.8
Canada	7.0	5.8	4.8	5.8	3.1	3.9	3.0	3.1	3.3	2.9	2.3	2.1	1.8	1.7	2.7
Iraq	0.2	0.2	0.2	0.3	0.2	0.3	0.2	0.3	6.2	9.6	7.7	1.6	1.4	1.2	1.0

Table B-3 Malaysia

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
Japan	17.5	19.5	20.5	22.7	22.3	20.1	21.3	23.4	23.1	22.4	23.0	24.6	25.1	25.4	26.3
USA	8.6	6.6	9.0	8.6	9.4	10.7	12.6	12.3	13.9	14.9	15.0	14.5	17.5	16.1	16.3
Singapore	7.5	8.2	8.0	7.8	8.3	8.5	8.6	8.4	8.5	9.1	11.7	13.0	14.3	13.9	13.1
Germany F R	4.9	4.6	4.5	5.5	6.3	5.1	5.6	5.6	6.1	5.9	5.4	4.5	4.2	5.2	4.2
Australia	5.7	5.8	7.5	7.1	7.2	7.8	7.1	6.1	6.4	6.1	5.4	5.5	4.6	4.1	4.0
UK	13.5	14.0	12.5	10.2	9.4	10.0	7.4	7.6	7.4	6.4	5.4	4.5	4.1	3.5	3.6
Saudi Arabia	1.7	1.4	1.7	1.5	3.2	2.3	2.2	4.3	4.0	3.1	6.2	4.7	3.3	4.3	3.4
Thailand	3.6	3.0	4.3	4.5	3.5	4.0	4.2	4.6	4.3	3.6	3.0	3.4	3.7	3.0	3.4
France	1.4	1.6	1.4	1.6	1.8	2.0	1.6	1.4	1.5	2.0	1.8	1.8	1.3	2.6	2.4
China	5.3	4.6	4.3	6.2	5.0	4.2	3.5	3.1	3.7	2.8	2.4	2.4	2.2	2.0	0.0

Table B-4 Pakistan

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
Japan	11.1	10.7	8.4	9.0	10.5	12.9	11.9	15.2	10.0	12.6	10.3	12.1	12.9	14.4	14.8
USA	30.8	25.1	22.3	25.9	22.7	13.3	18.7	11.6	12.4	12.7	14.1	8.6	10.2	9.5	10.8
Saudi Arabia	0.7	1.1	3.9	4.6	6.3	8.0	7.5	5.6	9.5	5.3	9.6	15.1	13.6	13.0	9.7
Kuwait	0.2	1.4	2.4	2.6	5.9	4.1	4.8	4.9	6.3	8.1	9.5	4.7	9.9	6.8	8.4
UK	10.2	11.1	9.2	7.5	6.6	6.3	7.9	8.3	6.8	7.0	5.7	6.1	6.7	6.0	6.5
Arab Emirates	1.2	1.5	0.4	0.0	0.2	3.4	4.0	4.8	3.7	2.4	6.3	6.8	6.1	5.9	5.7
Germany F R	10.2	8.8	8.8	8.6	8.4	6.1	6.5	7.7	6.1	5.4	4.5	5.6	5.7	6.7	5.6
Malaysia	0.5	0.4	0.5	0.6	2.3	2.7	1.3	2.5	2.1	2.0	3.1	3.1	2.7	3.5	5.5
Italy	3.6	5.1	3.6	2.3	2.8	3.1	2.8	3.1	3.0	4.0	3.4	2.9	2.7	3.4	2.6
China	2.4	3.8	3.9	5.0	3.1	2.5	2.9	2.2	2.6	3.0	3.1	3.3	2.8	2.7	2.5

Table B-5 Philippines

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
USA	29.3	24.8	25.4	28.3	24.1	22.2	22.2	20.6	21.1	22.9	23.6	22.9	22.6	23.3	27.4
Japan	30.5	29.5	30.6	31.4	27.0	27.9	27.1	25.2	27.5	22.8	19.9	19.0	20.1	17.2	13.6
Saudi Arabia	1.1	1.6	4.9	6.3	10.8	10.3	7.6	7.9	5.4	5.8	10.0	12.6	11.4	10.5	6.9
Kuwait	2.3	2.7	1.8	3.2	4.6	4.0	5.9	3.4	3.3	4.6	5.1	5.1	3.6	3.7	6.2
Malaysia	2.3	2.3	1.3	0.9	0.8	1.5	2.3	1.5	1.1	1.4	2.0	2.2	1.5	2.0	5.7
Hong Kong	1.0	1.0	1.0	1.0	0.8	0.9	1.3	1.5	2.2	2.4	2.4	2.6	2.7	3.3	3.9
China	0.0	0.0	0.1	1.2	0.8	1.3	1.4	1.9	2.3	1.9	2.7	2.5	2.7	1.6	3.6
Germany F R	5.7	6.9	4.8	4.7	3.9	3.8	3.5	3.3	3.8	4.5	4.2	4.0	4.3	4.8	3.2
Indonesia	2.5	2.5	0.7	0.1	0.1	1.7	3.0	3.7	3.0	2.9	2.3	2.7	1.8	2.2	3.2
Australia	4.7	4.1	4.8	4.2	4.4	3.8	3.5	4.7	3.8	3.5	2.9	2.9	3.1	2.5	2.4

Table B-6 Sri Lanka

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
Japan	8.8	8.7	9.0	8.7	7.8	8.5	8.1	7.0	11.0	13.4	12.8	14.4	15.2	17.7	16.6
Saudi Arabia	0.0	0.0	0.0	0.0	9.8	12.1	12.7	12.1	9.4	7.0	10.5	15.2	12.4	4.4	16.6
USA	5.7	5.2	7.0	9.0	3.2	6.4	8.1	9.0	8.2	5.4	4.4	7.2	6.3	6.4	8.9
India	9.8	9.9	4.5	2.9	4.8	2.9	3.9	6.0	9.2	10.3	4.7	4.2	4.1	6.4	6.0
Singapore	1.3	0.6	0.0	0.0	3.0	2.3	1.7	2.1	2.8	6.0	4.5	5.5	6.0	8.3	5.5
UK	14.1	12.5	9.8	6.8	3.8	4.3	5.9	5.8	9.8	9.0	9.5	6.2	6.6	6.9	4.9
Germany F R	0.8	0.2	4.8	4.2	3.8	4.8	3.9	3.8	5.7	5.4	3.5	5.0	4.3	4.2	4.8
Hong Kong	0.6	0.1	0.0	0.0	0.2	0.2	0.5	0.7	1.5	2.3	2.1	2.9	2.3	3.0	3.2
Iran	0.8	0.2	0.0	0.0	3.8	4.1	10.6	9.8	5.8	3.3	5.4	6.8	11.6	10.5	2.9
France	2.7	3.9	3.2	6.6	7.6	8.2	6.3	3.9	4.7	2.1	3.9	2.2	2.1	2.7	1.2

Table B-7 Thailand

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
Japan	37.6	37.7	36.9	35.7	31.4	31.5	32.5	32.4	31.0	25.8	20.7	24.0	23.5	27.4	26.9
USA	14.9	14.2	15.7	14.0	13.5	14.4	13.4	12.4	13.8	15.7	16.6	13.5	13.3	12.6	13.4
Saudi Arabia	2.0	2.8	3.1	2.3	4.8	9.0	7.6	8.3	5.6	6.5	9.9	13.4	15.2	10.3	8.5
Singapore	1.0	0.8	1.4	0.9	1.6	2.0	2.5	3.0	4.1	4.7	6.3	6.8	6.3	6.2	7.9
Malaysia	0.5	1.7	1.6	0.7	0.3	0.4	0.5	1.0	1.3	1.7	1.8	2.7	5.2	5.4	4.9
Germany F R	8.5	7.8	7.4	7.6	7.3	5.2	4.8	5.5	5.2	5.2	4.2	4.3	3.9	4.7	4.2
China	0.0	0.0	0.0	0.0	0.1	0.5	2.0	1.5	1.6	3.4	4.4	3.2	2.7	2.6	3.0
Korea S	0.5	0.4	0.4	0.9	0.6	0.7	0.8	1.0	1.5	1.6	2.1	1.4	1.8	2.4	2.8
UK	7.5	7.7	5.2	6.4	4.6	4.5	3.6	4.0	3.8	3.2	2.6	2.7	2.6	2.3	2.3
Qatar	0.0	0.0	0.0	0.0	6.0	3.7	5.7	5.3	4.4	4.5	5.3	3.2	2.2	1.2	0.1

Source: IMF, Direction of Trade Yearbook (Washington D.C.: IMF, various issues); UN, Yearbook of International Trade Statistics (New York: UN, various issues).

Note: ".." means not available.

Appendix C

External Shocks and Adjustments

Table C-1 Balance of Payments Effects and Adjusments (percentages), 1974-82

	Balance of Payments Effects			Direct Adjustment				Net External Finance
	Terms of Trade	Export Volume	Total External Shocks	Export Market Penetration	Import Subs-titution	Import Redirection Through Lower GNP Growth	Total[a]	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Burma	-185.5	58.5	100.0	-153.9	-0.8	111.4	-43.3	143.3
India	-72.8	-27.2	100.0	8.3	-2.3	2.2	8.2	91.9
Malaysia	71.6	28.4	100.0	39.9	-25.4	4.3	18.8	118.8
Pakistan	-46.7	-53.3	100.0	-8.1	0.8	-5.6	-12.9	112.9
Philippines	-75.1	-24.9	100.0	17.5	2.3	-2.6	17.2	82.9
Thailand	-90.1	-9.9	100.0	25.5	8.6	2.6	36.7	63.4
Sri Lanka	-76.5	-23.5	100.0	-8.6	14.8	-17.5	-11.3	111.3

Source: Seiji Naya, D. H. Kim, and W. James, "External Shocks and Policy Responses: The Asian Experience," Asian Development Review, vol. 2, no. 1 (1984), Table 4, p. 8.

Notes: [a]7=(4)+(5)+(6). Data for Bangladesh is not available in the source.

Table C-2 Sources of External Shock and Domestic Policy Response (Percent of GNP), 1973-82

	External Shocks[a]					Domestic Policy Spending[b]					
							Domestic Spending[c]		Trade Ratios[d]		
	Observed Deficit Increase	Total	Terms of Trade	Interest Rate	World Trade	Other[e] External Variables	Total	Gross Investment	Consumption	Export Ratio[f]	Import Ratio[g]	Residual
1973-78												
India	-1.6	1.4	1.1	-0.0	0.3	-1.3	-1.7	0.1	-0.2	-1.5	-0.1	0.0
Pakistan	0.5	3.1	2.3	0.2	0.6	-5.7	3.3	-0.2	0.2	2.4	0.9	-0.2
Philippines	10.5	7.3	4.9	0.4	2.0	0.6	2.1	1.7	-0.8	-0.1	1.3	-0.0
Sri Lanka	2.9	-3.0	-4.2	-0.1	1.3	-0.6	8.3	2.1	-0.5	23.5	-16.9	-1.8
Thailand	4.2	10.6	7.3	0.2	3.2	1.7	-8.2	0.8				
1978-82												
India	2.4	1.5	1.4	0.0	0.0	-0.7	1.6	0.0	0.1	-0.8	2.4	-0.0
Pakistan	-0.8	7.6	6.0	-0.1	1.7	-1.3	-5.4	-0.1	-0.1	-2.9	-2.3	-0.1
Philippines	3.0	4.8	2.2	0.6	2.0	1.1	-2.8	-0.3	0.2	-2.9	0.2	-0.1
Sri Lanka	7.6	65.9	59.9	0.4	5.6	-7.1	-57.9	5.7	-10.7	-11.4	-42.1	6.6
Thailand	-3.4	9.5	6.1	0.3	3.2	0.3	-13.2	-1.7	0.4	-8.8	-3.2	-0.0

Source: Gerald K. Helleiner, "Balance-of-Payments Experience and Economic Growth Prospects of Developing Countries: A Synthesis," World Development, vol. 14, no. 8 (August 1986), Table A2 and A3, pp. 906-907.

Notes: [a]A "+" sign denotes an adverse and a "-" sign denotes a favorable external shock; [b]A "+" sign denotes a deficit-increasing and a "-" sign denotes a deficit-reducing policy actions; [c]A "+" sign denotes an expansion of domestic spending, which increases the deficit. A "-" sign denotes a contraction of domestic spending, which reduces the deficit; [d]A "+" sign denotes a movement of the trade ratios which increases the deficit. A "-" sign denotes that the trade ratios moved to reduce the deficit; [e]A "+" sign denotes a favorable movement. A "-" sign denotes a favorable movement; [f]A "+" sign denotes a reduction and a "-" sign denotes an increase of the exports to world trade ratio; [g]A "+" sign denotes an increase of the import content of domestic spending. A "-" sign denotes a reduction of the import ratio.

Table C-3 External Shocks and Performance Indicators, 1979-82 (Ratios, Percentages)

	Bang	Indi	Mala	Paki	Phil	Sri	Thai
External Shocks/GNP (1974-78)	13.6	2.2	-8.3	7.9	5.7	28.5	1.9
External Shocks/GNP (1979-82)	1.1	3.0	5.3	2.8	6.4	25.1	6.4
Composition of External Shocks (as percentages of external shocks)							
Terms-of-Trade Effects	31.8	81.3	-20.7	61.0	37.9	93.0	69.7
Export Volume Effects	46.2	21.3	132.7	12.0	35.7	4.0	5.2
Interest Rate Effects	21.1	-2.4	-11.9	26.9	26.3	3.0	25.1
Policy Responses (as percentages of external shocks)							
Add. Net External Financing	142.9	157.3	115.6	116.2	70.7	116.6	42.1
Export Promotion	-54.6	-55.0	115.4	28.0	43.0	1.1	44.0
Import Substitution	103.2	-4.0	-97.4	-45.2	-9.5	-20.7	-11.0
Fuel	139.3	-18.4	3.2	-11.0	16.2	-15.1	-0.2
Non-Fuel	-36.1	14.4	-100.6	-34.2	-25.7	-5.5	-10.8
Macroeconomic Policy Effects	-91.4	1.8	-33.5	1.1	-4.1	3.1	25.0
Policy Response Ratios							
Export Promotion/Exports	-10.7	-33.5	-12.8	8.6	17.9	1.1	14.0
Import Substitution/Imports	8.2	-2.0	-12.0	-7.5	-2.9	-22.0	-2.9
Fuel/Fuel Imports	161.5	-27.2	3.8	-10.0	25.9	-62.1	-0.2
Non-Fuel/Non-Fuel Imports	-3.0	10.8	-13.9	-6.9	-9.7	-8.0	-3.5
Macropolicy effects/Imports	-7.2	0.9	-4.1	0.2	-1.2	3.3	6.6

Source: Bela Balassa and F. Desmond McCarthy, "Adjustment Polices in Developing Countries, 1979-83: An Update," World Bank Staff Working Papers, no. 675 (Washington, D.C.: World Bank, 1984).

Appendix D Weights (1980 Partner Imports) Used in Calculating Real Effective Exchange Rates

Bangladesh		Burma		India		Malaysia	
USA	15.3	Japan	43.7	USA	11.5	Japan	23.0
Japan	13.7	U.K.	8.8	Iran	10.4	USA	15.0
Singapore	9.4	Germany, F. R.	7.4	U.K.	5.4	Singapore	11.7
U.K.	8.4	Singapore	6.1	Germany, F. R.	5.3	Saudi Arabia	6.2
India	5.1	USA	5.0	Japan	5.0	Australia	5.4
Germany, F. R.	4.3	Norway	4.0	Saudi Arabia	4.6	Germany, F. R.	5.4
Korea	4.1	Canada	2.0	Belgium	2.4	U.K.	5.4
Malaysia	2.7	Malaysia	1.9	Canada	2.3	France	1.8
Canada	2.1						

Pakistan		Philippines		Sri Lanka		Thailand	
USA	14.1	USA	23.6	Japan	12.8	Japan	20.7
Japan	10.3	Japan	19.9	Saudi Arabia	10.5	USA	16.6
Saudi Arabia	9.6	Saudi Arabia	10.0	U.K.	9.5	Saudi Arabia	9.9
Kuwait	9.5	Kuwait	5.1	Iran	5.4	Singapore	6.3
U.K.	5.7	Germany, F. R.	4.2	India	4.7	Germany, F. R.	4.2
Germany, F. R.	4.5	Australia	2.9	Singapore	4.5	U.K.	2.6
Italy	3.4	Indonesia	2.3	USA	4.4	Korea, South	2.1
Malaysia	3.1	Malaysia	2.0	Germany, F. R.	3.5	Malaysia	1.8
				France	3.9		

Source: Derived from IMF, Yearbook of Direction of Trade Statistics (Washington D.C.: IMF, various issues).

APPENDIX E Sources and Definitions of Date Used in Estimation of Regression Equations

There are 16 observations for each of the variable for the period 1970-85. The sources and the definitions of the variables are:

Current Account Balance as a Ratio of Exports (CA/X): The variable CA and X are in millions of U.S. dollars. CA data exclude official transfer and exceptional financing. The source of the data is the IMF, International Financial Statistics (IFS), various issues. For Bangladesh, 1970-72 data are from the ESCAP, Statistical Yearbook for Asia and the Pacific, various issues.

Terms of Trade (TOT): TOT is defined as the ratio of unit value of exports to unit value of imports, both expressed in U.S. dollars. The source of the data is UNCTAD, Handbook of International Trade and Development Statistics, various issues. There are slight differences between the IMF and UNCTAD data. I decided to use UNCTAD data for two reasons. First, as is common in empirical research, terms of trade data on a consistent basis for all countries are not available. UNCTAD publishes consistent time series data on terms of trade for a large number of developing countries, including our countries. Second, UNCTAD data takes into account transportation charges and is therefore a better measure of price changes among traded goods.

Growth of Real GNP in Industrial Countries (DGNP): The annual average growth in real GNP in industrial countries data is from IFS, various issues.

Real Interest Rate (RI): The RI is defined as the six-month London Interbank Offer Rate (LIBOR) on U.S. dollar deposits minus individual country's export price changes. LIBOR is taken from IFS, various issues, and U.S. dollar export price changes are calculated from export price index data reported in UNCTAD, Handbook of International Trade and Development Statistics, various issues.

Fiscal Position (FP/Y): The FP/Y is defined as the ratio of a central government's revenue minus expenditure as a percent of nominal GDP. The main source of the data is IFS, various issues. Since no separate data for Bangladesh and Pakistan exist for 1970-71, the heroic assumption is made that the 1970-71 ratio for Pakistan would also have been the ratio for Bangladesh. which may not be unrealistic since both were within the united Pakistan till the December of 1971. For Burma, 1970-73 data are from the World Bank, World Tables, 1976 and 1985 data are, by assumption, the average of 1982-84.

Real Effective Exchange Rate (REER): The REER index shows domestic currency per U.S. dollar. REER was calculated because no

consistent indices are available for our countries. First, I calculated bilateral real exchange rates for major import partners of each country in our sample, defining the real exchange rate as

$$r = eP^*/P$$

where r = real exchange rate,
e = nominal exchange rate (domestic currency per unit of foreign currency),
P^* = foreign price index, and
P = domestic price index.

To obtain REER, geometric averages of these bilateral exchange rates were calculated with 1980 partner imports as weights. For partner imports, as many countries as possible were used for which "P", "P^*", and "e" are available for the ten major import partners of our countries in 1980. Appendix D shows the countries and corresponding weights used. P and P^* refer to consumer price indices of respected countries. P, P^*, and e are from IFS, various issues. Partner import data are from the IMF, Yearbook of Direction of Trade Statistics, various issues.

VITA

Baban Hasnat was born in Dhaka, Bangladesh, on February 9, 1956. He received his secondary education at the Dhaka University Laboratory School and higher secondary education at the Dhaka College. He earned the Bachelor of Science degree in 1978 and the Master of Science degree in 1980, both in economics, from the Jahangirnagar University, Dhaka. He then worked as a research fellow at the National Foundation for Research on Human Resource Development, Dhaka, and joined the Jahangirnagar University as a lecturer in economics in 1981.

In January, 1982 he entered the graduate program in economics at The University of Tennessee, Knoxville, Tennessee. As a doctoral student, he served as a research and teaching assistant during the subsequent years. From 1986-1989 he worked as a graduate assistant at the Oak Ridge National Laboratory, Oak Ridge, Tennessee. He was awarded the Master of Arts degree with a major in economics in December, 1987 and the Doctor of Philosophy degree with a major in economics in August, 1989. He will join the Morehead State University, Morehead, Kentucky in August, 1989.

Baban married Kumkum Chowdhury in June, 1984. They have a two year old son Abir.