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INSTITUTIONAL FRAMEWORK AND POLICY DIALOGUE FOR THE PROMOTION OF INDUSTRIAL RESTRUCTURING IN THE ASIAN AND PACIFIC REGION

(Item 6 of the provisional agenda)

SUMMARY

The Seoul Plan of Action for Promoting Industrial Restructuring in Asia and the Pacific, adopted by the Commission in 1992, spelled out recommendations and proposals for action in sustaining the region's industrial and technological dynamism. One of these recommendations urged the secretariat to examine the feasibility of a regional forum to promote industrial restructuring.

Industrial restructuring is becoming a challenging task in the face of a fast-changing global economic order. In recent years, several important issues and concerns have come to shape the pace and direction of industrial restructuring. In particular, the globalization of the world economy, the growing nexus between foreign direct investment, manufacturing production and technology flow, the transition of several centrally planned economies to market-based systems, the widespread adoption of privatization and liberalization measures, the emergence of regional and subregional arrangements, the unprecedented upsurge in external capital flows, rapid technological innovations, and the successful conclusion of the Uruguay Round agreements, are beginning to have profound implications for industrial restructuring in the region.

In this emerging environment, an informal regional forum to bring together policy makers, professional experts and private sector representatives could play a vital role in facilitating industrial restructuring in the region. The Seoul Plan of Action recommended the formation of such a forum, and the secretariat continued to examine the issue through meetings and discussions with policy makers, professional experts and private sector representatives. The Committee for Regional Economic Cooperation, at its fifth session, held at Bangkok on 2 and 3 April 1996, commended the secretariat initiative in that regard. The Commission, at its fifty-second session in 1996, endorsed the recommendation of the Seoul Plan to establish the forum. This document, after analysing some of the more important trends and events, suggests that an informal regional forum to promote policy dialogue in industrial restructuring and development should be formed.

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I. BACKGROUND

1. The Seoul Plan of Action for Promoting Industrial Restructuring in Asia and the Pacific, adopted by the Commission at its forty-eighth session in 1992, contains several recommendations and proposals for action.[1] One of the recommendations[2] relates to the creation of a specialized facility for conducting dialogue amongst the policy makers, private sector representatives and professional experts to promote industrial restructuring in the region. This recommendation was extensively deliberated at a regional meeting held at Kuala Lumpur from 6 to 10 December 1993, which reiterated the need for such a forum. Both prior to and since that meeting, extensive consultations have been held with several countries of the region about the feasibility of establishing such a forum.

2. The eighth meeting of the Steering Group of the Committee for Regional Economic Cooperation, held at Seoul from 13 to 16 March 1996, in reviewing the progress of the implementation of the Seoul Plan of Action and the necessity to include some additional areas of focus in the Plan, commended the secretariat initiative towards the establishment of a regional forum for industrial development and restructuring in the region. The Committee for Regional Economic Cooperation, at its fifth session, held at Bangkok on 2 and 3 April 1996, also commended the secretariat initiative in that regard. The Commission, at its fifty-second session in 1996, endorsed the recommendation of the Seoul Plan to establish the forum.

3. In pursuance of that recommendation and the subsequent endorsement by the Commission, the secretariat has prepared this document on the institutional framework and policy dialogue in promoting industrial restructuring, with particular emphasis on the needs of the countries in the light of emerging issues and concerns at the dawn of the twenty-first century.

II. EMERGING ISSUES AND CONCERNS OF IMPORTANCE FOR INDUSTRIAL RESTRUCTURING IN THE ASIAN AND PACIFIC REGION

A. The cascading pattern of industrialization continues but challenges loom

4. An increasingly competitive and outward-oriented manufacturing sector has continued to sustain the high level of economic growth in the Asian and Pacific region. This is being achieved at a time when the global economy could be entering a new phase of synchronized growth, possibly for the first time since the beginning of the First World War.[3] World real gross domestic product (GDP), which grew by 3.5 per cent in 1995, is projected to grow by 3.8 per cent in 1996 and by 4.1 per cent in 1997, with a four-year average of 4.4 per cent from 1998 to 2001.[4] The industrial

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[1] *Seoul Plan of Action for Promoting Industrial Restructuring in Asia and the Pacific* (ST/ESCAP/1182).

[2] Ibid., para. 58.

[3] *The Economist*, 4 January 1997, p. 69.

[4] International Monetary Fund, *World Economic Outlook: October 1996* (Washington DC), p. 41.

countries grew by 3.5 per cent in 1995 and are expected to increase that rate to 2.3 per cent in 1996 and 2.5 per cent in 1997. Their real GDP is expected to grow by an average of 2.6 per cent in 1998-2001. The developing countries are expected to recover their previous trend and grow by 6.3 per cent in 1996 and 6.2 per cent in 1997 with the average reaching 6.3 per cent for the 1998-2001 period. For the first time since 1986, the countries in transition are expected to break out of their negative growth rate. After experiencing a modest growth of 0.4 per cent in 1996, this group of countries are expected to grow by 4 per cent in 1997 and reach a four-year average of 5.2 per cent for 1998-2001.

5. This synchronized growth pattern, in which all the regions and groups of countries are expected to register positive high growth rates in the coming years, has a significant implication for the Asian and Pacific region. Being one of the most outward-oriented segments of the world economy, the Asian and Pacific region as a whole can look towards sustained demand for its manufactured exports and obtain capital and intermediate industrial inputs from diversified and competitive sources.

6. The real GDP of the Asian region (excluding Japan) grew by 8.6 per cent in 1995 and is estimated to have grown by 8 per cent in 1996, with a projected growth rate of 7.5 per cent in 1997.[5] Among the high performers, China continued to grow at double-digit rates at 12.6 per cent in 1994 and an estimated rate of 10.2 per cent in 1995, a mild slowdown compared with previous years. The economy of the Philippines appeared to break out of its long period of sluggish growth in the early 1990s and achieved an estimated output growth rate of 4.4 per cent in 1994. Indonesia, Malaysia, the Republic of Korea, Singapore and Thailand grew by a simple average of 8.6 per cent in 1994. Indonesia, Malaysia and the Republic of Korea are estimated to have grown by 8.1, 9 and 9.5 per cent in 1995 respectively, with Singapore and Thailand experiencing a slight moderation in their performance in 1995 compared with 1994. In South Asia, India grew by 5.7 per cent in 1994 and is expected to have achieved a 6.8 per cent growth rate in 1995. Pakistan's growth rate, at 3.8 in 1994, is expected to have picked up, reaching 4.5 per cent in 1995. Sri Lanka's growth rate declined from its 1993 level to reach 5.6 per cent in 1995 and is expected to have declined further to 5.4 per cent in 1995. Among the least developed countries, Bangladesh continued to grow sluggishly, at 4.8 per cent in 1993 and 4.7 per cent in 1994, with the expected growth rate in 1995 remaining at the previous year's rate. Bhutan continued to perform well with an expected growth rate of 7 per cent in 1995. Growth is expected to have picked up in Cambodia and the Lao People's Democratic Republic to 7.6 and 7.1 per cent respectively in 1995. Nepal is expected to have grown by 5.8 per cent in 1995 after a setback in 1994. Among the Pacific island developing countries, Fiji, Papua New Guinea and Solomon Islands grew by an average of 5.2 per cent in 1994. Among the economies in

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[5] Ibid., p. 173.

transition, Viet Nam continued its strong performance with growth reaching 8.1 per cent in 1993 and 8.8 per cent in 1995, with a projection of 9.5 per cent for 1996.

7. The above pattern of growth reflects the cascading nature of industrialization, which continues to shape the changing competitive advantage of the countries in the region. First Japan and then the Asian newly industrialized economies (NIEs) have emerged as new centres of industrial power. Japan lost its comparative advantage in labour-intensive manufacturing production decades ago. It was able to establish its competitive edge quickly in a wide range of exportables and successfully restructured its economy towards the production of human capital-intensive and technology-intensive manufactured goods. A vast number of its manufacturing enterprises have been relocated abroad, a process which is still in progress. This has allowed greater rationalization and restructuring of its domestic industrial structure, with new products and services appearing in the market.

8. This pattern set by Japan has also been followed by the Asian NIEs. Faced with growing labour costs and intense competition to penetrate overseas markets, the NIEs are gradually restructuring their industries away from an overdependence on labour-intensive production techniques. A new range of skill- and technology-intensive manufacturing activities are accounting for an increasing share of manufacturing value added in these economies, although the industrial restructuring process will have to be continued on an ongoing basis. While the Republic of Korea and Singapore have emerged as powerful manufacturing countries, Hong Kong has virtually shifted all its resources out of declining manufacturing industries and has created a vibrant service sector.[6] As a consequence, the share of the manufacturing sector in its GDP had declined to 11 per cent by 1993.

9. The continuation of this pattern of industrialization to proceed unhindered and the possibilities for other countries of the region to fill the vacuum created by the progressive graduation of the NIEs will critically depend on a number of factors. Countries like China, India, Indonesia, Malaysia, the Philippines and Thailand have already been able to establish a broad-based manufacturing base. The majority of them remain attractive destinations for foreign direct investment (FDI) and other forms of external resource flows and have acquired a strong foothold in export markets, but they could easily be embroiled in fierce competition for the same export markets with declining prices for their goods. This could adversely affect their ability to generate the needed income and investment to graduate to higher levels of industrial production. To avoid this happening, the NIEs will have to find the resources for industrial restructuring and move up the production ladder, creating the space for other developing countries to enter into higher value-added production lines. Under the prevailing conditions, one of the most promising options which could be pursued to achieve this goal and

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[6] Henry Wai-chung Yeung, "Sectoral specialization and competitive advantage", ASEAN Economic Bulletin (Jakarta), July 1996.

thereby sustain the cascading pattern of economic development of the region would be to strengthen cooperation towards exploiting the growing industrial complementarities on a regional and subregional basis.

10. The other developing countries, for example, the least developed countries, the Pacific island countries and the economies in transition, stand to benefit from this process at least on two grounds. First, cost and locational advantage could make it profitable for them to undertake an increasing number of manufacturing activities, particularly certain processes like production of parts and components. Second, as the NIEs and other dynamic countries liberalize their economies, they would potentially have a larger market for their exports, in addition to access to developed country markets.

11. However, the full utilization of this potential can only be realized if countries of the region continue to pay increased attention to economic fundamentals, including restructuring their industries on a continuous basis to remain internationally competitive. The recent slowdown of export demand for a number of manufactured goods from some countries of the region underlies the importance of the changing nature of international competitive conditions. Although most observers are agreed that the more dynamic countries of the region continue to display strong economic fundamentals and the recent reverses in exports are merely adjustments to stresses built up during the years of high growth, the trend towards reallocation of export demand from rising cost centres to low-cost production centres does indicate the need for restructuring to cut production costs and improve productivity. Industrial restructuring also needs to shift progressively away from input-intensive to productivity-led growth strategies. In these circumstances, countries with clear goals for integrating into the global movements of manufactured goods, services and financial capital are expected to do better in the changing environment.

B. Globalization, regionalization and future industrial restructuring

12. Since the Plaza Accord in 1985, the region has witnessed a turning point in its drive for industrial and technological development. The world economy has entered into a new phase with increased interdependence. The widespread resort to liberalization and deregulation measures has brought both opportunities and challenges in achieving higher manufacturing competitiveness and securing new market niches. Financial markets have expanded rapidly with transnational corporations and fast changes in technological innovations exerting a profound impact on the globalization process. The impetus towards greater interdependence and integration has been further strengthened by moves in harmonizing trade and investment policies, as embodied by the successful conclusion of the Uruguay Round of multilateral trade agreements and the rapid strides made in giving more operational meaning to several regional and subregional arrangements. The establishment of the World Trade Organization validates the underlying trend towards further globalization of trade, investment and manufacturing production.

13. With the successful conclusion of the Uruguay Round agreements, a new set of opportunities as well as challenges face the developing countries of the region to sustain their growth momentum.[7] As trade and investment barriers come down under the agreements, the nature of international competition could be significantly altered, with a significant impact on the course of industrial development in the signatory countries. Many countries will have to reform and restructure their existing investment and trading regimes with increased competition for FDI, export markets and technology. The most important aspects of the Uruguay Round agreements which are expected to have an impact on industrial restructuring in the region are embodied in the Multifibre Arrangement (MFA), trade-related aspects of intellectual property rights (TRIPs) and trade-related investment measures (TRIMs).

14. The planned reintegration of world trade in textiles through the phasing out of MFA over a ten-year period represents one of the most important achievements of the Uruguay Round agreements.[8] As textiles play a key role in the industrial development strategies of many countries, the phasing out of MFA will alter their export shares in significant ways. Once the restrictions on textiles exports are removed, it is expected that the developing countries will be able to gain a significant advantage in securing and maintaining external markets. The impact of the integration of MFA is likely to be felt over time as it is implemented in a staggered manner. International trade in textiles will become more competitive, with consumers in the developed countries benefiting through lower prices. It will mean that many developing countries will have to invest more in and restructure their textiles and apparel industries, in terms of upgrading technology and developing appropriate skills.

15. The agreements on TRIPs represent by far the most comprehensive international agreements on intellectual property rights. The new rules governing TRIPs are expected to lead to strengthened protection of intellectual property rights, and a non-restrictive framework for FDI, thus promoting the transfer of technology and foreign investment to developing countries, two critical factors in carrying out industrial restructuring successfully. Enhanced protection of intellectual property rights will encourage innovation in developing as well as developed countries.

16. The TRIMs agreement specifies "measures related to trade in goods only" and prohibits the adoption and utilization of investment-related measures (legislative or otherwise) which may give rise to "trade restrictive and distortive effects". It excludes foreign direct investment in services such as communications, transport, advertising and financing. The various provisions of the agreement on

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[7] See United Nations Conference on Trade and Development, *The Outcome of the Uruguay Round: An Initial Assessment* (New York, United Nations, 1994) for a comprehensive discussion of the various implications of the agreements.

[8] See Will Martin and L. Alan Winters, *The Uruguay Round: Widening and Deepening the World Trading System* (Washington DC, World Bank, 1995) for a detailed discussion.

TRIMs will become effective over an extended period, giving many developing countries time to adjust their trade and investment practices. The gradual abolition of export performance requirements, one of the most frequently used trade-related measures in many developing countries, along with provisions relating to restrictions on access to foreign exchange, mean that no member will be allowed to apply trade-related measures which are inconsistent with the obligations of national treatment and with the general movement towards elimination of quantitative restrictions. All the exceptions granted under the General Agreement on Tariffs and Trade (GATT) 1994 will also apply, as appropriate, to the provisions of the TRIMs agreement.

17. Although regulations on FDI, including TRIMs, have been significantly liberalized since the 1980s, the new rules governing performance requirements and domestic contents are expected to require significant restructuring, the direction and impact of which are yet to be defined. However, one question which is likely to receive considerable attention in coming years is the extent to which the implementation of the TRIMs agreement may promote FDI in the countries of the region, or to alter the patterns of trade associated with it. Another difficult question is whether the application of TRIMs will alter the export-import policies by foreign affiliates, thereby adversely affecting industrial restructuring in developed as well as developing countries. Finally, it should be noted that the possible recourse to exceptions under GATT 1994 may allow countries to use some of the trade-related investment measures without violating the TRIMs agreement.

18. The trends towards globalization of trade and investment have seen a parallel increase in the rise of regional and subregional arrangements, a phenomenon which has been termed "regionalism". Although there is no conclusive evidence to suggest that the regional and subregional arrangements could dangerously lead to fragmentation of world trade and investment,[9] the emergence of various regional arrangements could be viewed as an intermediate step towards full globalization. In that context, synchronizing and dovetailing regional cooperation efforts such as the Association of South East Asian Nations (ASEAN), the Asia-Pacific Economic Cooperation forum, the South Asian Association for Regional Cooperation with the various provisions of the Uruguay Round agreements could become a major task, particularly in terms of different time-frames and the scope of various provisions envisaged in liberalizing different sectors.[10]

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[9] See K. Anderson and H. Norheim, "History, geography and regional economic integration", in K. Anderson and R. Blackhurst, eds., *Regional Integration and Global Trading System* (New York, Harvester Wheatsheaf, 1993).

[10] The decision of the World Trade Organization to set up the Committee on Regional Trade Agreements in February 1996 illustrates the importance attached by the world body to studying and handling the relationship between regionalism and globalism in a more systematic manner.

C. Foreign direct investment, borderless production and industrial complementarities

19. The world economy has witnessed an unprecedented surge in FDI flows, with the total reaching an all-time high of US$ 240.3 billion in 1995.[11] The developing countries received net US$ 90.35 billion, of which the Asian region accounted for US$ 55.75 billion (excluding Central Asia). Among the countries in the Asian and Pacific region, China remained the most important destination for FDI, receiving an estimated US$ 38 billion in 1995, followed by Malaysia with US$ 5.8 billion, Indonesia with US$ 4.5 billion and Thailand with US$ 2.3 billion. In South Asia, India received roughly two-thirds of the US$ 2 billion which went to that subregion in 1995.

20. These flows have contributed significantly to the industrial restructuring of the recipient countries through structural change, graduation to the production of higher value added products, technology transfer and maintenance of export competitiveness. The United States of America, some European Community countries, Japan and the capital-surplus NIEs such as Hong Kong, the Republic of Korea and Taiwan Province of China remained the major suppliers of FDI to the developing countries of the Asian and Pacific region.

21. FDI flows, focusing on investments in new plant, equipment, roads, transport and other forms of fixed capital, have boosted the recipient countries' industrial productivity and facilitated the release of scarce domestic resources from declining industries to profitable industries. This process, anchored on FDI, has already taken root in the more dynamic economies of the region, particularly in the ASEAN-4, and has the potential to do so in the larger economies such as China and India.

22. FDI flows to the least developed countries and the transitional economies, although very limited in size, are beginning to have similar effects in restructuring their industries so that they are more profitable and competitive. FDI is helping to replenish their existing industrial capital stock and complementing domestic resources in undertaking more investment in physical and social infrastructure such as schools, health facilities, housing, and transport and communications.

23. A strong nexus has developed between FDI, manufacturing production, international trade and technological innovations. This nexus is beginning to shape the industrial scene of the region and extending itself beyond the traditional triangle linking the United States, Japan and the European Community to include the NIEs, the dynamic economies of South-East Asia such as Indonesia, Malaysia, the Philippines and Thailand, and China and India. This trend has reinforced incentives for industrial restructuring in other developing countries of the region so that they can also benefit from this nexus.

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[11] World Bank, *World Debt Tables 1996: External Finance for Developing Countries* (Washington DC, 1996), p. 93.

24. Centred around FDI, this emerging nexus has enabled enterprises based in the developed countries to use overseas investments as a vehicle for rationalizing and restructuring their own industries in line with their changing competitive advantage. In particular, FDI, anchored on relocation of production and sourcing of industrial goods, products and processes, has increased the flow of industrial capital and technology more in line with emerging complementarities and globalization of production to meet the challenges of an increasingly unified international market. In this context, FDI-related relocation and industrial complementation could serve to reduce significantly trade friction between developed and developing countries.

25. Segmentation of production processes has also brightened prospects for charting out a new pattern of specialization in the region. The ability to separate out some key manufacturing products/processes according to their factor intensity and base those products/processes in different countries has already set in motion a new pattern of borderless production which could be further strengthened. For instance, enterprises based in developed countries have separated out the production of labour-intensive products/processes to labour-abundant countries. However, in order to utilize the full potential of this trend, the developing countries would have to study more thoroughly the sectoral specialization of investing enterprises.[12] This would call for more cooperation and exchange of information between the investing and recipient countries, requiring regionwide coordination of industrial restructuring measures. In that regard, rationalization of entry and exit policies regarding mobility of factors across industries and over national boundaries could make a significant contribution in promoting industrial restructuring. Countries which are losing comparative advantage in certain industries could expedite the speed and scope of the restructuring of those industries.

26. The ASEAN experience in this respect shows what could be pursued in other parts of the region. To foster greater industrial cooperation, ASEAN began with three programmes: ASEAN industrial projects (essentially large-scale government-owned projects); the ASEAN Industrial Complementation Programme, aimed at promoting vertical integration of production activities to be undertaken by several member countries with brand-to-brand complementation receiving 50 per cent tariff preference on investments in automobile parts; and the ASEAN Industrial Joint Ventures Programme which gave 90 per cent margin of preference for trade with participating countries and allowed up to 60 per cent foreign participation.

27. Some discussions have taken place within ASEAN to replace or reshape the investment cooperation schemes under the ASEAN Industrial Joint Ventures Programme and brand-to-brand complementation as the introduction of the Common Effective Preferential Tariff scheme would

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[12] Yeung, loc. cit.

reduce the attractiveness of the preferential tariff granted under these schemes. One proposal which has been under discussion relates to the granting of automatic privileges to investors in ASEAN from the Board of Investment of the member countries.[13] This proposal is likely to bring more investment to the subregion. The investors would be allowed to bring their own technology. The proposed scheme would grant a preferential tariff of 0-5 per cent during the years leading to year 2000 or 2003, the target date for the completion of the ASEAN Free Trade Agreement. The private sector would also like to see that the new scheme grants privileges in other fields such the development of technology and the promotion of investment in products which can be manufactured in all the member countries.

D. Macroeconomic stability: a prerequisite for successful industrial restructuring

28. Maintenance of macroeconomic stability has appeared as one of most important prerequisites for effecting successful industrial restructuring. The remaining part of the 1990s will demand a greater degree of skill and alertness on the part of policy makers to maintain that stability, particularly in a world rapidly brought together by unprecedented financial flows and investment liberalization. Continuous attention to economic fundamentals, including those factors which determine industrial competitiveness, will be required. A systematic divergence from those fundamentals will necessitate an immediate response, including industrial restructuring and other adjustment measures to restore a country's international competitiveness. Structural or cyclical changes, as currently experienced by many countries of the region, require an appropriate response, often involving restructuring of industrial production and redirection of exports from oversaturated markets.

29. The growing reliance on monetary instruments in maintaining macroeconomic stability could encounter limits under the present circumstances. Many countries of the region, using interest rates as a key policy variable, have succeeded in taming inflation and providing stability in investment expectations. However, an interest rate that is too high to contain inflation could lead to increased demand for offshore borrowing and unsustainable pressure on the exchange rate and the current account with serious implications for industrial competitiveness. In so far as these types of interest and exchange rates movements reflect economic fundamentals, timely industrial restructuring can be one of the options to avoid some of their negative consequences. Some industrial enterprises (for instance, from Hong Kong, Japan, the Republic of Korea and Taiwan Province of China), particularly the small and medium-scale enterprises which are labour-intensive and highly sensitive to price changes, have tried to avoid the loss of their international competitiveness by relocating production abroad.

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[13] See E/ESCAP/SREC(8)/3, p. 8.

30. Macroeconomic stability is also needed to generate a sufficient supply of domestic resources, a key factor in successfully carrying out industrial restructuring. The success with which the ASEAN countries and the Asian NIEs continue to restructure their industries is due largely to the ample supply of domestic savings and channelling of those savings to industrial use. Although access to international savings, especially FDI, remains the only option for many developing countries to restructure their industries successfully, domestic savings will have to assume an increasingly important role in the long run.

31. As the supply of savings at levels, terms and conditions conducive to successful industrial restructuring requires the maintenance of monetary growth at non-inflationary rates, a high degree of fiscal responsibility will also have to be ensured. Persistent budget deficits discourage the flow of savings needed to restructure industry. Such deficits incurred as a result of subsidizing loss-making industrial enterprises not only compound difficulties in pursuing prudent fiscal management, but they also take away the incentive from those industrial enterprises to restructure and become efficient.

E. Privatization, deregulation and enterprise reform

32. The potential benefits of privatization, deregulation and enterprise reform, as industrial restructuring measures, are well recognized in most countries of the region. Many of these countries have also put in place ambitious privatization programmes to improve efficiency in resource allocation, reduce budget deficits and allow their private sector to play a bigger role in the industrialization process.

33. Privatization as a means to mobilize external resources and restructure industry has appeared as a strategic option in many countries of the region. In East Asia and the Pacific, a total of US$ 10,138 million of foreign exchange was raised through privatization during the period 1988-1994. In South Asia, it amounted to US$ 1,070 million during the same period, with US$ 997 million being raised by India alone in 1994.

34. Several transitional economies of the region have embarked on a market-based and private sector-led industrial development strategy.[14] This has entailed significant and far-reaching restructuring of their industries, a process which is still in progress. These transitional economies, which comprise the Central Asian republics of the Commonwealth of Independent States, Cambodia, Mongolia and Viet Nam, have put in place a wide range of restructuring policies and programmes to revitalize their industries as part of their preparation to open their economies to international competition. Among them, Viet Nam, Turkmenistan and Azerbaijan have made impressive gains in attracting FDI. The admission of Viet Nam into ASEAN as a full member should facilitate its gradual integration into the regional flows of trade and investment.

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[14] See Pradumna B. Rana and Naved Hamid, eds., *From Centrally Planned to Market Economies: the Asian Approach* (Hong Kong, Oxford University Press, 1995) for a comprehensive treatment of some of the issues raised here.

35. Many developing countries of the region, especially the least developed countries and the transitional economies, continue to face a challenging task in carrying out industrial restructuring measures and in developing a private sector which will eventually become the prime engine of their industrial development. They need access to information and draw lessons from successful examples of privatization, deregulation and liberalization measures. In most of the countries in these subgroups, property rights continue to remain fragile with weak enforcement mechanisms which discourage investment and the development of a market-based system to coordinate investment and consumption decisions.

F. Changing skills requirements, work organization and well-functioning labour markets

36. The ability to carry out industrial restructuring effectively depends critically on the supply and availability of a well-qualified human resource base. Technologies embodied in products and processes like computers, telecommunications and microelectronics have given rise to demands for new skills. The competitive advantage of nations can largely be determined by investments made on such skills and the ways in which such skills are used.

37. As competition intensifies, many countries of the region are looking for ways to move away from resource-based manufacturing production processes. As new generations of production processes begin to replace natural-resource and labour-intensive processes, demand for multi-skilled managers and a multi-skilled workforce to run competitive industrial enterprises is sharply increasing. Many developing countries lack the resources to develop such skills. In that context, the potential offered by transnational corporations in improving and upgrading the level and composition of industrial skills deserves more attention, particularly as countries of the region become more integrated with the global production networks.[15]

38. Labour and product market rigidities could hold back attempts to restructure industries. As many countries begin to display features of matured economies, they also accumulate these rigidities, which can complicate the implementation of restructuring strategies. These rigidities include high non-wage labour costs, restrictions on changing the level of employment at enterprise levels, entry barriers to new firms and restrictions on the introduction of new products and processes.

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[15] United Nations Industrial Development Organization, *Industrial Development: Global Report 1996* (Vienna, 1996), pp. 82-83.

III. A POLICY FRAMEWORK FOR PROMOTING INDUSTRIAL RESTRUCTURING IN THE ASIAN AND PACIFIC REGION: ITS NEED, FORM AND SUGGESTED FUNCTIONS

39. The sequential pattern of Asian industrial development experience indicates that industrial restructuring, either policy-led or driven by market forces, will remain a key factor in promoting and sustaining the dynamic performance of the region. The industrial restructuring policies and programmes so far pursued in the region have involved the achievement of the following broad goals: (a) to reduce excessive dependence on external demand for growth and avoid trade friction; (b) to remain internationally competitive; (c) to graduate to the production of higher value-added manufactured goods/products; (d) to shift resources, for example, labour, capital and technology to industries/products/processes in which enterprises have a dynamic comparative advantage; (e) to upgrade production technology commensurate with factor endowment; and (f) to achieve social objectives of employment generation and minimization of adjustment costs.

40. The specific modalities or strategies can be divided into two categories: policy-led measures and market-led restructuring. Policy-led measures could include (a) industrial complementation, relocation and sourcing schemes; (b) realigning national policies with international agreements and regional arrangements; (c) deregulation, liberalization and privatization; (d) reform of public sector enterprises; (e) incentive schemes for right-sizing/abandoning declining industries and shift resources to expanding ones; (f) training and retraining schemes; and (g) social safety measures to minimize restructuring costs. Market-led restructuring modalities could include (a) right-sizing/abandoning industries or products which have lost their international competitiveness and shift resources to more profitable ones; (b) enterprise-to-enterprise cooperation to seek out new markets and acquire new technology; (c) shifting production to overseas locations to take advantage of relative differences in cost and productivity; (d) entering into industrial complementation schemes or joint ventures as strategic options to acquire new markets and expand production; and (e) technology tie-ups to acquire competitive advantage. In reality, all these goals and modalities could be pursued in various combinations. However, in achieving the goals of industrial restructuring, close and ongoing cooperation between the private sector and the government would remain a vital precondition.

41. Industrial restructuring is a process which entails changes in ownership, shifts in production technology, alterations in market structure, diversification of outputs, and changes in the composition of skills towards utilizing scarce resources efficiently to remain internationally competitive. Industrial enterprises go through this process in an environment characterized by changes in relative prices, real exchange rates, liberalization and deregulation measures, investment policies, technological innovations and production complementarities. Strategic competition for resources and markets, enterprise-to-enterprise cooperation, transfer of manufacturing production abroad and sourcing of

industrial goods from geographically dispersed locations also have an important bearing on the pace, speed and direction of industrial restructuring.

42. The increasingly globalized production systems have blurred the age-old distinction between the domestic market and the international market. This implies that a fundamental symmetry of economic interests is developing between the countries of the region. Industrial enterprises everywhere need to take full cognizance of this new economic paradigm and acquire the ability to restructure swiftly in order to remain competitive. This emerging paradigm requires that the enterprises operating in developing countries with predominantly market-based systems become more flexible in terms of their response to internal and external imperatives. Operating on a "real-time" basis, they face far greater demands on their survival skills than at any time before. The need for coordinated responses to such complex imperatives has never been so compelling.

43. Conformity to new international agreements and regional arrangements, greater volatility in capital flows, uncertainties in retaining established markets, and unprecedented advances in production and information technologies are manifestations of this emerging paradigm. National policies would have to rhyme well with events and trends outside one's own economy, implying a continuous attention to opportunities for restructuring. The more developed and dynamic economies of the region are likely to be more successful than others in doing so. In the less dynamic economies, particularly in the least developed countries and the transitional economies, strong public policy in support of market-based instruments will be needed.

44. The wide differences in national capabilities to cope with the emerging economic paradigm create a basis for enhancing regional economic cooperation, centring around FDI, debt and equity financial flows, joint industrial complementation schemes, and increased intra- and interindustry trade. In particular, the prospects for geographically contiguous countries to forge greater economic cooperation and exploit industrial complementarities are bright.

45. In this context, the task of developing coordinated responses to future challenges has become highly urgent, underscoring the need for a specialized framework which will be able to draw and retain the attention of the countries of the region to promote industrial restructuring. In an integrating global economic system, disjointed actions and reactions to events and trends at the national level and beyond could seriously complicate matters in promoting and sustaining industrial development. In particular, some of the less dynamic countries of the region, which are yet to integrate themselves fully with the regional flows of trade and investment, lack the requisite information and expertise to respond in an effective manner to the changing global situation. Even for the more successful countries of the region, the need has become all the more acute as many of them continue to be taken aback as rapidly changing global market conditions dramatically alter their industrial and export

performance. Anticipatory response to unexpected and steep declines in FDI flows and export demand for manufactured goods is illustrative of the nature of policy vigilance that the forum could endeavour to foster.

46. The secretariat, in consultation with relevant government officials, private sector representatives and professional experts, has examined the possible institutional form that such a forum could assume. The thinking on this area has evolved over time and the consensus seems to be that there is no need for a new institutional mechanism or body to perform the function of a regional forum and that the forum function should be carried out by the ESCAP secretariat within its existing resources, augmented by focused extrabudgetary assistance over an extended period of time.

47. In arriving at the above conclusion, two distinct options were examined: (a) the establishment of a new institutional set-up, outside the ESCAP secretariat, to act as the forum; and (b) an informal forum, consisting of focal points at the national level, to be serviced by the ESCAP secretariat. The emerging consensus pointed towards the second option.

48. The regional forum could have the following terms of reference:

(a) The regional forum should meet periodically on an ad hoc basis and focus on a specific area of crucial importance as a theme and report its findings to the Committee for Regional Economic Cooperation either directly or through the Steering Group of the Committee. The meeting should also review all activities in promoting industrial restructuring as envisaged under the Seoul Plan of Action;

(b) The regional forum should assist developing countries of the region in organizing national forums to facilitate and promote industrial restructuring with a focus on the needs of the least developed countries, the Pacific island economies and the economies in transition;

(c) The regional forum should assist the developing countries of the region in promoting industrial restructuring, with special emphasis on the creation of a vibrant private sector through the mobilization of all internal and external resources for industrial development;

(d) The regional forum should actively promote cooperation on a regional and subregional basis to harness industrial complementarities, and foster foreign direct investment, enterprise-to-enterprise cooperation, skills development, private sector development and the growth of export-oriented small and medium-sized enterprises;

(e) The regional forum should assist in institutional developments and promoting interministerial and interdepartmental linkages and coordination for industrial restructuring;

(f) The regional forum should undertake studies and provide advisory services on macro policy issues related to industrial development and restructuring;

(g) The regional forum should undertake periodic benchmark studies on the state of industrialization in the region and disseminate the information to all interested parties;

(h) The regional forum should, in cooperation with national forums, carry out periodic assessments of industrial investment opportunities and make that information available to interested foreign investors;

(i) The regional forum should undertake training and advisory programmes in promoting foreign direct investment and other external capital flows, particularly in the least developed countries, the Pacific island countries and the economies in transition;

(j) The regional forum could organize exchange visits and study tours for policy makers, private sector representatives and professional experts to facilitate exchange of information and expertise on industrial restructuring;

(k) The regional forum should assist national forums to carry out periodic assessments of investment opportunities in the countries concerned, and disseminate such information as widely as possible;

(l) The regional forum should assist national forums to organize trade and investment fairs, when possible, by enlisting the support and involvement of national chambers of industry and commerce and by inviting the participation of other countries;

(m) The regional forum should assist national forums to enlarge the role of the private sector in the industrial development and restructuring policies and programmes of the countries concerned;

(n) The regional forum should assist national forums to "corporatize" and "internationalize" public sector enterprises, wherever needed;

(o) The regional forum should assist national forums to develop policies and programmes to professionalize and upgrade the skills of the Boards of Investment and national chambers of commerce and industry and foster greater cooperation amongst them through networking and exchange of information;

(p) The regional forum should assist national forums to undertake studies of successful cases of privatization and then disseminate these to other appropriate countries through their own national forums.

49. The terms of reference of the regional forum would be reviewed from time to time in order to retain its effectiveness in promoting industrial restructuring in the region.