Chapter 2

EXPORTS OF MANUFACTURED GOODS AND ECONOMIC DEVELOPMENT

2.1 Introduction

In this Chapter, the significance of the exports of manufactured goods for economic development will be discussed.

As background to this main theme, the theoretical and historical relationship between exports and economic development will be briefly reviewed in section 2.2. Section 2.3 presents a bird’s eye view of the general export performance of developing countries over the last two decades and comments on its achievements and shortfalls. The role of manufactured exports in the export structure of these economies is discussed in section 2.4. The final section summarizes the main conclusions of the present Chapter.

2.2 Exports and Economic Development

Historically, exports have played a crucial role in quickening the pace of economic development of the countries that are now among the highly developed and have high levels of income per head. The classic example in this respect is that of Great Britain where expanding exports
of wool and textiles played a leading role in providing stimulus to the growth of the economy in the 19th century. Over the years 1870-1913 Britain exported roughly a fifth of its national income and a third of its industrial output. Since the first world war, however, the proportion of gross product exported declined from around 18.8 percent in 1909-13 to 8.4 percent in 1944-45. Subsequently it picked up to a level of 16 percent during 1949-53 but dropped again to 13.8 per cent during 1957-63.  

These movements in exports were found to have a parallel effect on the growth of Britain's industrial output and its national product. Another example can be found in the case of Japan where the contribution of exports in fostering economic development has been very considerable in its early stages of development. Japan exported as high as 22 percent of her gross domestic product during 1914-17 which was the crucial stage of Japan's development. Similarly other cases of export-led growth could be found in the U.S.A. from 1790 to 1860; Canada and Switzerland during 1900-1913 and Sweden and Denmark after 1880.

In most of these countries, an expanding export trade gave a conspicuous momentum to the economy and helped it on its way to industrialisation. The dormant or idle resources were drawn into economic activity for export production; increasing labour force or capital stock.

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1 All the figures have been taken from National Council of Applied Economic Research (NCAER), *Export Strategy for India*, New Delhi, June, 1969, pp. 2-3.

2 Ibid., p. 3.

were gainfully allocated and thus the benefits from specialisation and economies of scales were fully derived. These benefits were mainly derived by the primary producing countries which were still in the process of being settled. Trade enabled them to bring into use their great unexploited natural resources and freed them from the limitations of their own domestic markets. Further the areas that had natural resources whose products were in growing demand abroad also received an increasing amount of foreign capital to exploit those resources and to increase the supply of products. This, along with expansion of exports, led to a cumulative process of development in these countries. Thus for most of these countries trade was an "engine of growth".

In recent years, however, two divergent opinions have emerged on trade being an engine of growth in the 20th century, that it was a century ago. They are reflected, for example, in the positions taken by Ragnar Nurkse and A.K. Cairncross on this issue. Nurkse is of the opinion that the 19th century trade-growth nexus cannot be as effective for the present day developing countries of the world for the simple reason that "the 19th century conditions were different: they happened to be such that the growth of the dominant economy, Great Britain, did tend to transmit itself to the periphery through an even more than proportional expansion in demand for crude materials and foodstuffs....

This mechanism of growth transmission is now in comparatively low gear. And the reasons which he advances to establish his case are:

- the low elasticity of demand for foodstuffs, agricultural protection in the industrial countries, the increased share of services in the consumer's budget,
- the shift towards less material-intensive products in manufacturing, the substitution of synthetics for natural materials,
- and the reduction of input requirement in individual industries.

On the contrary, A.K. Cairncross considers the contribution that foreign trade can make to economic development of the developing countries today as unique. To him "Trade is no mere exchange of goods least of all when it takes place between economies at different stages of development. As often as not, it is trade that gives birth to the urge to develop, the knowledge and experience that make development possible, and the means to accomplish it."

The truth, perhaps, lies somewhat in between. Exports, by themselves, will not guarantee economic development unless accompanied by complementary policies conducive to growth. Similarly, exports can be neglected only at the cost of economic development.

As is well known, economic development of almost every developing

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6 Ragnar Nurkse, op. cit., p. 27.
7 Ibid., p. 23.
country calls for a substantial amount of investment in a wide range of productive facilities. But as production in a developing country is initially confined to a limited range of products, it has to look to the imported inputs of technical know-how and capital equipment. Often economic growth also requires imports of raw materials and consumer goods. These imports have to be paid for through foreign loans or grants, foreign investment in the country, withdrawals from the accumulated holdings of foreign exchange, current export earnings or a combination of these. Of these, it needs hardly any argument to demonstrate that exports are economically a better means of financing imports provided that they are feasible. If imports are financed by foreign loans, the loans apart from being inadequate and guided by various motives, both political and economic, carry interest and the principal has to be repaid. Similarly foreign investment involves remittance of profits and eventual repatriation of foreign capital. All this means foreign exchange, which can only be acquired through increased export earnings. No doubt payments for these may also be made by contracting further loans, but that only means putting off the day of reckoning and building up more massive liabilities for the future. Likewise, withdrawals from reserves is not an unlimited process and most of the developing countries seem to reach this limit in the very early stage of their development. Ultimately, it is, therefore, exports and more exports that can be used to finance the expanding needs of imported supplies and thus to foster economic development quickly and at an uninterrupted rate. Financing of imports through exports has, however,
other benefits also. It provides an opportunity to the importer to buy in the market of his choice and at competitive prices. This freedom is more or less restricted when imports are financed by foreign aid. The donor nations limit the sources of supply to their respective markets where prices generally tend to be high. Further, an expanding export trade, apart from providing the wherewithal to import from the most preferred sources, also enables the exporting nations to take greater advantage of the international division of labour, procuring desired goods from abroad at considerable saving in terms of inputs of factors of production. This helps in increasing the efficiency of industry which is a major factor in economic growth. The country also gains from economies of large scale production. When a country exports, its market is enlarged and this permits large-scale operations. Export development makes it necessary for a country to remain competitive in prices as well as quality of its exportables in international markets. This in turn entails the export industries to keep costs low and to constantly strive for more efficient operations. As a result, efficient export industries are established. Other benefits that may follow from the development of exports include increased investment and consumption, inducement to foreign capital in the country and the flow of technological and market innovations as well as managerial skills. All these factors are conducive to a faster rate of growth of the economy.

It follows then that exports are of strategic importance for economic development of developing countries. Failure on this front may
lead to cuts in imports and investment and the pace of economic development may slow down. As a matter of fact it is not very difficult to find the cases where in the absence of growth in exports at a satisfactory rate, the countries concerned have been facing difficulty in financing imports in spite of large foreign aid. They have often been forced to eliminate "non-essential" imports by severe trade restrictions which have made resource allocation less efficient, and, in periods of extreme difficulty sharp cuts have been necessary in imports of capital goods and raw-materials as well. This has led economies to work below capacity. The most striking example in this respect is perhaps that of India.

Moreover, a developing country needs to expand its exports even at later stages of economic development. History is replete with instances which show that economic development leads to a greater degree of inter-dependence rather than self-sufficiency. This can be seen in the fact that the developed countries are the best customers for one another. Thus an expanding export trade is a dynamic factor in the development of a country and needs to be encouraged.9

9 The existence of a significant correlation between exports and economic development has been fairly established by a number of empirical studies. For example, R.F. Eady finds in his study that relates to a group of 50 countries and covers the period 1953-63 a positive relationship between the rates of economic growth and the rates of export growth and concludes that "as a rule of thumb countries ought to aim at 2.5 percent expansion of exports to obtain a 1 percent expansion of per capita real GNP". See his, "The Relation of Exports and Economic Growth", Kyklos, Vol. XX-1967-Fasc. I, pp. 470-486.
2.3 Export Performance of Developing Countries

Looked at in the context of our discussion on the role of exports in economic development in the preceding section, expansion in the exports from developing countries (DE) during the past two decades has not been reassuring. In fact it has been rather depressing. There is considerable evidence to show this.

As may be seen from the data given in statement 2.1,10 exports from developing market economies in the period 1950 to 1970 rose from about $19 billion to $55 billion giving a compound rate of growth of 6.4 per cent per annum.11 Excluding the major oil exporting countries, the rise in exports of DEs in this period was from $15.4 billion to about $40 billion only. This amounts to an increase of 4.8 percent per annum. As against this exports from developed market economies (DME) over the same years rose at an annual compound rate of 9.4 percent and those from the centrally planned economies (CPE) at 10.1 percent. In absolute terms the rise in their value of exports during 1950-70 was from

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10 All Statements can be found in the Appendix.
11 Throughout this study, the terms "developing market economies" and "developing countries" are used interchangeably and unless otherwise specified the Developed Market Economies (DME), Developing Market Economies (DE) and the Centrally Planned Economies (CPE) refer to the groups of countries referred to by the UN as Economic class I, II, and III respectively. According to this classification Economic Class I includes Canada, United States of America, Western Europe, Australia, New Zealand, South Africa and Japan; Economic Class II includes all countries in Asia, Africa and Latin America except Japan and the CPE; and Economic Class III includes Eastern Europe (Albania, Bulgaria, Czechoslovakia, Eastern Germany, Hungary, Poland, Romania, USSR), China (mainland), Mongolia, North Korea and North Viet-Nam.
$37.2 billion to about $224 billion and from about $5 billion to $33.4 billion respectively. Thus the export trade of DEs has not fared well in comparison with the exports of the DNEs and CPEs. This is equally evident if one looks at the quantum of goods exported from DEs (Statement 2.2).

On the other hand imports into the DEs rose from $17.5 billion in 1950 to $56.2 billion in 1970 recording an increase of 6.0 percent per annum (Statement 2.3). This rate of growth was in excess of the 5.4 per cent annual rate of growth of exports in these countries in the same period as noted earlier. As a result, the trade balance of DEs steadily worsened over the period. In 1950, the DEs enjoyed a surplus of exports over imports to the extent of about $1.4 billion; this turned into a permanent negative balance of trade for them in the period after 1951. In 1951 the value of their exports matched the value of imports. On this account also, it is the group of DEs, excluding the major oil exporters, that have suffered most. For example, while the growth registered in their value of exports in the period under review was just 4.8 per cent a year, the value of their imports in the same period progressed at a rate of 5.9 per cent per annum. Consequently their trade deficit recorded a substantial increase and in 1970 amounted to $8,520 million as against a small amount of $10 million in 1950 (Statement 2.4).

The divergence between exports and imports is only one aspect of the problem encountered by the DEs. The problem has been further accentuated by the deterioration in their terms at which their exports,
mostly primary products, are exchanged for their imports, mainly manufactures. The average price of goods exported by the DEs has lagged behind their price of imports, with the result that the terms of trade have declined over the period (Statement 2.5).

These developments in exports of DEs were, however, not equally spread over the whole period. As is shown by Table 2.1, exports from DEs rose at a faster rate during 1960-70 than in 1950-60.

TABLE 2.1
ANNUAL RATE OF GROWTH OF WORLD EXPORTS
BY MAJOR REGIONS: 1950-70
(Percent)

<table>
<thead>
<tr>
<th></th>
<th>1950-70</th>
<th>1950-60</th>
<th>1960-70</th>
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</thead>
<tbody>
<tr>
<td>Developing market economies</td>
<td>5.4</td>
<td>3.7</td>
<td>7.3</td>
</tr>
<tr>
<td>Developing market economies - excluding major oil exporters</td>
<td>4.8</td>
<td>2.6</td>
<td>7.0</td>
</tr>
<tr>
<td>Developed market economies</td>
<td>9.1</td>
<td>8.7</td>
<td>10.1</td>
</tr>
<tr>
<td>Centrally planned economies</td>
<td>10.1</td>
<td>11.8</td>
<td>8.6</td>
</tr>
<tr>
<td>World</td>
<td>8.5</td>
<td>7.6</td>
<td>9.3</td>
</tr>
</tbody>
</table>

Source: Statement 2.1

There are many factors that account for this acceleration of the growth of exports of DEs during the sixties. In the first place, it could be related to the generally higher level of economic growth of the world especially that of the DMEs during the sixties as compared with the fifties. In consequence, world demand for the products exported by the DEs accelerated. Secondly, it could also be attributed to a rise in the prices or unit value of exports of DEs. Thirdly the
increased exports of manufactures from DEs have also contributed, although in a small way, in speeding up the exports from them.

Table 2.1 also shows that despite the faster rate of growth in exports during the period 1960-70, exports from DEs lagged behind the world exports in general and those of the DMEs and CPEs in particular. In view of this, it is not surprising to find that the share of DEs in world exports steadily declined over the period under review. In 1950 the share of DEs in world exports was 31.0 percent; in 1960 it was 21.3 percent and by 1970 it had fallen to 17.6 percent. This decline in the share is more rapid if major oil exporting countries are left out account: from 25.3 percent in 1950 to 15.7 percent in 1960 and to just 12.7 percent in 1970. During the same period the share in world exports of both the DMEs and CPEs increased considerably.

Several factors account for such a depressing performance of the DEs in world exports. Underlying these, however, is the very structure of their exports, which largely consist of foodstuffs and agricultural raw materials or what is more popularly known as primary products. And it is for this group of products that the world demand especially the demand of the DMEs has been either stagnant or increasing at a very slow pace. The high levels of per capita income and consumption in

12 For the relative share of "primary products" and "manufactured goods" in total exports of the different economies see Chapter 3.

the DMEs have transformed the whole structure of their demand. The demand for cereals and other foodstuffs has lagged behind the rise in incomes and the consumption of manufactured goods and of the products of service industries. Further, the significant increases in the domestic output of agricultural products in the DMEs and increasing protection of agricultural output put these economies have added to the gravity of problem for the DEs. As regards the natural raw materials, it is the changes in the industrial structure of DMEs that have adversely affected the demand for industrial raw materials of the DEs. Industrial structure in DMEs has tended to shift in favour of engineering goods and chemicals where the share of raw materials per unit of value added is much smaller. For example between 1953-54 and 1965-66 the growth of the industrial countries' textile and footwear industries, for which the share of raw materials used per unit of value added is particularly important, was only one-third of the growth in the chemical industry and about one-half of that of engineering. Added to this has been the problem of synthetic materials produced in industrial countries.

Exports from the DEs have also suffered due to the shrinking exportable supplies, inflation and the relatively high prices for their goods. With the initiation of the process of economic development,

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15 Ibid., p. 43.
domestic demand in most of the DEs has been rising at a greater speed than the increase in domestic output. As a result of it, the available supplies for export have been naturally affected and it is not very difficult to find the cases where a few of them have had to import instead of exporting primary commodities. Also, the internal policies followed by the respective governments have also contributed to the depressed export earnings of these countries. 17

2.4 Significance of Exports of Manufactures

We have noted that in general exports are indispensable for any programme of economic development of DEs. We have also seen that their actual export earnings have not been satisfactory. The causes for this depressing performance of exports of DEs are both the declining demand for their major exports — mostly foodstuffs and raw materials — and shrinking exportable supplies, though the intensity of these factors may vary in different countries and for different products. Of these the demand factors are not likely to change in future in any significant manner. It means that exports of primary products from DEs can be expected to grow only slowly. On the other hand imports in most of the DEs can be assumed to grow slowly only at the cost of a slow pace of economic development. This most of the DEs cannot afford. Their urge for

quick economic development is very intense. In view of this, it is imperative for DEs to expand their exports of manufactures rapidly to the world in general and to the DMEs in particular. The size of the markets of the latter for manufactured goods is very wide and ever expanding. They have ample purchasing power and their needs are always growing. Labour is scarce and expensive. DEs can take advantages of this opportunity and increase their exports of manufactures to them. This will increase their export earnings and provide an additional momentum to their drive for industrialisation. We are not suggesting that the DEs should develop their exports of manufactures at the cost of their primary products. It would be in their own interest if they not only maintained their exports of primary products at the present level but also registered some increase; otherwise the gains in exports of manufactures will be wiped out by short-falls or stagnation in exports of the former. But as the prospects for expansion in exports of primary products are limited the DEs should increasingly look upon manufactured goods to fill the gap between their export receipts and import requirements.

As we shall see in the following Chapter, manufactured goods enjoy a buoyant demand in world markets. In the markets of the DMEs it has been found that the import elasticity for manufactures is higher than for most of the primary products. Therefore, it may be possible for DEs to

10 According to one estimate, an increase of 1 percent in the gross domestic product of the DMEs normally raises their demand for imports of foodstuffs and agricultural raw materials from DEs only by 0.5 to 0.6 percent. But the demand for fuels goes up by 2.4 percent and of manufactures by 1.0 percent. See U.N. World Economic Survey, 1969, Part I, pp. 57-58.
gain a greater share of world trade by orienting their production and trade in favour of manufactured items.

In addition to the factors mentioned in section 2.2, others can be adduced in favour of manufactured exports from the DEs. For instance, in most of them expansion of exports of manufactures is essential for further advances in the process of industrialisation. Industrialisation in the DEs has been generally carried out through substitution of domestic production for imports. Substitution cannot be carried on too long without exposing the economy to the danger of high costs.19 Besides, many import replacing industries contribute little to net savings of foreign exchange because they themselves depend heavily on imports for intermediate materials and capital equipment.20 Sometimes, industries of this sort also face the threat of shutdown whenever imports have to be curtailed to deal with an exchange stringency. In such a situation further advances in the process of industrialisation depend on expansion into foreign markets.

Apart from these benefits of exports of manufactures by DEs, there are other benefits that will follow from an expanded exports of these goods.

19 The defects of the policy of industrialisation based on import substitution have been well listed by Raul Prebisch. See his Towards a New Trade Policy for Development, UN, New York, 1964, pp. 21-22.

20 The strength of this factor is suggested by A. Wajiszals. According to him, capital goods and intermediate products represented only 40 percent of the imports of a group of semi-industrial countries in 1929, while the comparable figure for these countries in 1955 was 69 per cent. See his, Industrial Growth and World Trade, Cambridge: Cambridge University Press, 1963, pp. 70, 76.
To quote Keesing "New high-quality human resources will be created through industrial experience that could not be obtained under heavy protection. Outside competition will spur adoption of new technology and efficient methods. A more rational and efficient allocation of scarce resources will emerge than under inward-looking policies, and gross error will be avoided.... The result will be to sow the seeds for a flourishing growth of industry that will soon far outstrip the blighted product of an inward-looking strategy".  

2.5 Concluding Remarks

This Chapter has emphasised the vital role of exports of manufactured goods for economic development. Exports are of strategic importance for economic development of DEs. But actual exports from them in the past have not been reassuring. The reasons for the unfavourable trends in exports of these economies are rooted in the structure of their trade. Their exports are heavily dominated by primary products for which world demand, especially the demand of the DMEs - their major customers, has been growing at a slow rate. Besides, the shrinking exportable supplies and the policies of the governments in DEs have also affected exports from these countries. The demand factors, by and large, are not likely to reverse themselves in future and therefore the exports of primary products from them can be expected to grow only slowly on this count. Of course, oil exports will grow.

rapidly as there exists a booming world demand for it but they are likely to make a substantial contribution to the export earnings of a very limited number of countries. For most of the DEs, therefore, manufactured goods appear to be the most promising source of export earnings. This will enable them to exploit the booming international markets in manufactures, will reduce their dependence on the structural weaknesses of primary commodity markets and the vagaries of individual commodities, and will also help them in quickening the pace of industrialisation.