

BY ALICE H. AMSDEN

If enthusiasm for globalism nose-dived immediately after Sept. 11, the bargaining power of developing countries rose in ways that are just beginning to be understood. Their new strength derives from the realization that globalism requires international political stability, while poverty breeds unrest. And now that the message is out, poor countries with greater leverage haven't been shy about making their wishes known. Exhibit A: One of Pakistan's demands for cooperating in Afghanistan was a higher quota for its textile exports.

The enlightened self-interest driving America's new enthusiasm for aiding Pakistan seems to have spilled over elsewhere, too. At the World Trade Organization's meeting in Doha, Qatar in November, members agreed to make drugs for epidemics available to poor countries at below-average-cost prices. But this may have been the high-water mark in the altruism department; the big pharmaceutical companies are already balking at the concession. And since nothing much else happened at Doha, no change is likely in the developing world's hostility toward yet another round of trade liberalization.

That puts the spotlight on the WTO's core problem. The agenda is supposed to move beyond trade to the broader issues of managing global markets – in particular, protecting intellectual property rights and freeing multinationals from parochial regulation. Yet with

China now at the table to buttress the *dirigiste* views of Brazil and India, the developing countries' demands are likely to gain clout.

What, precisely, are their demands? And if their wishes were granted by the advanced economies, would the world economy be better or worse off? Read on.

THE CULT OF POVERTY

A big blue sky separates what Southern countries have long demanded and what Northern anti-globalists and pro-globalists alike have seen as their just deserts. From the anti-sweatshop movement to the World Bank, a cult of poverty colors advanced-country thinking. Allegedly, the South is hopelessly destitute and corrupt. Whatever economic gains it makes, debt crises are bound to erode. Poverty is thus recurrent, and the appropriate policy thrust is poverty alleviation. Anti-poverty measures have thus tended to crowd out policies aimed at development.

The gist of the anti-sweatshop movement's approach is to alleviate poverty by raising minimum labor standards. The resulting

ALICE AMSDEN teaches political economy at MIT and is the author of *The Rise of "The Rest": Challenges to the West from Late-Industrializing Economies* (Oxford University Press, 2001).



increase in wages is supposed to bolster domestic demand. With demand rising at home, the pressure to export will taper off, thereby sparing workers in advanced economies a “race to the bottom” in the production of labor-intensive goods.

Alas, the movement’s argument doesn’t stand up to analysis on its own terms. For one thing, rising wages in developing countries can’t create markets comparable in purchasing power to those of advanced economies. Consider an old colonial couple, the Netherlands and Indonesia. The population of Indonesia is about 13 times greater than that of the Netherlands, but the market in the Netherlands, measured by its GNP at current exchange rates, is almost three times greater than Indonesia’s.

Instead of labor and environmental standards, which many disparage as protection-

ism in disguise, the developing countries want room to grow through exports of agricultural products, textiles and steel. If the South can export more, this is bound to trigger capital formation, especially in the poorest countries – developmentalism par excellence. Yet anti-globalists in rich countries, keen on holding together political coalitions that include import-vulnerable labor unions, are silent when it comes to opening their markets.

For the World Bank, by contrast, poverty alleviation means aiming loans for health, education, nutrition and infrastructure at poor countries, as well as prying open these countries’ markets to give the little guy a fair shake and the multinational an incentive to invest. The Bank’s commitment to poverty alleviation started after the Vietnam War under the presidency of Robert McNamara, who made it a top priority.

TRENDS

But the McNamara approach works better on paper than on the ground. Most developing countries can't attract enough foreign direct investment to make a big difference, even if their markets are wide open. Those that can want to regulate markets in order to ensure that multinationals act responsibly and that space is freed for nationally owned companies – many of which have demon-

estimates that the 40 least-developed countries account for only 13 percent of the population of the developing world (consisting of 152 countries). The lowest level of development is suffered by 36 economies, many with exceptionally small populations and domestic markets. Seventy-eight poor countries have graduated to what is considered by the UN to be a medium level of human development. Poor people abound in these countries, but

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strated more entrepreneurship than the foreign fogies. Small-scale enterprises, for their part, seem to be forever marginalized unless they can cluster around growth poles created by large companies, as shown in Taiwan.

The current vogue in development research is to tease out cause and effect between growth and a variety of factors by looking at data from a wildly diverse group of economies. Not surprisingly, growth is found to be faster the greater a country's investment, ethnic homogeneity, political stability, expenditures on education and proximity to the sea. Absent altogether from the equations are policy-sensitive developmental variables such as the degree of local ownership of enterprises, technological skills or industrial transformation. Presumably these factors are ignored because manufacturing is assumed to be beyond the pale of the South.

In fact, this view ignores the wide variability in economic cultures in what is casually labeled the developing world. The United Nations' 2001 Human Development Report

generally only around 20 percent to 40 percent of the population falls below the poverty line. Most are ready to supplement policies that fight poverty with policies that build globally competitive industries – the heart of modern economic growth.

The cult of poverty not only over-generalizes from the poorest countries, but also ignores the lessons from numerous success stories of the past three decades. Countries including China, Korea, Taiwan, Brazil, Chile, Mexico, Malaysia, Thailand and Turkey began catching up without the benefit of cutting-edge technologies or wide-open trade and investment policies. Indeed, the rise of these late-developing economies involved a mixture of foreign and indigenous enterprises, along with the acquisition of technological capabilities by nationally owned companies like Hyundai Motors (Korea), Usiminas Steel (Brazil), Giant Bicycle (Taiwan), Legend Computer (China), Vitro Glass (Mexico), Siam Cement (Thailand) and Dr. Reddy's Labs (India).

Under the more tolerant General Agree-

ment on Tariffs and Trade (GATT), established 50 years before the WTO, investment in these countries boomed and per capita incomes sometimes doubled within a decade. Although most latecomers paid a price in periodic financial crises, debt debacles did not come close to erasing the gains.

Thus, three sets of developing countries now exist: what I call “the rest” (the successful latecomers), “the residual” (the poorest) and a large number of middle-income countries in between – “the remainder.” “The rest” all had experience in manufacturing before World War II, which seems to have been critical in curbing corruption and enabling developmental policies to work. Experience in the textile and machinery industries, for example, created a supply of local entrepreneurs and managers to run modern companies and state bureaucracies. Experience also led to expectations that new industries would become profitable, which lured capital from proverbial mattresses. With high expectations of profits, it became rational for entrepreneurs to use subsidies from the government to create productive capacity rather than to increase personal consumption.

Since the 1960s, comparable manufacturing experience has been accumulated in UN-defined middle-income countries, including Vietnam, the Philippines, South Africa, Nigeria, Mauritius, Egypt, Morocco, Tunisia, Puerto Rico and Peru. These economies, I would argue, are ready for a big push to modernize selective industries and services. And they are likely to use their newfound bargaining power on the global stage to make the case for industrialization measures along the lines of those used by “the rest.”

DEVELOPMENTALISM

The poverty alleviation approach would give poor countries drugs at below-patent prices.

The developmental approach is to give them cheap drugs that are produced locally by indigenous companies. India built its drug industry with policies typical of those used to industrialize by “the rest.” First, the Indian government recognized only process patents so that national companies could legally copy the product innovations of foreign companies. Second, public sector organizations jump-started local manufacturing by training a cadre of employees who later played a prominent role in private-sector companies. Third, the structure of tariffs promoted learning and movement up the ladder of technological complexity.

By contrast, the Indian software industry strictly upholds international patents in order to attract outsourcing from foreign clients. Software pirates operate openly only in the “informal” sector. Like the pharmaceutical industry, software innovation was jump-started by government organizations (one, for example, trained hundreds of engineers to computerize India’s railway reservation system). Nevertheless, by Indian standards, government support for software has been minimal because local companies have been able to compete at world prices.

“The rest,” it is important to note, succeeded by tying subsidies to performance standards. The Indian government’s price controls on drugs, for example, provided makers with incentive to cut costs and to export. The protection of foreign process patents pressured manufacturers to maximize the efficiency of their own production.

In the Brazilian automobile industry, domestic content rules required foreign assemblers to buy parts and components locally, which gave them an incentive to raise the productivity and quality of local suppliers, typically small- and medium-size companies. Import protection in Korea and Taiwan

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carried with it the obligation to meet export targets. Development banks lent at below-market interest rates to a wide array of industries, in exchange for which clients had to meet standards pertaining to professional management – for example, hiring a non-familial chief financial officer, not exceeding a specified debt-equity ceiling and introducing modern cost-accounting techniques.

Free market ideologues feast on stories of “the rest’s” failed experiments. Price controls succeeded in India’s pharmaceutical industry but doomed its steel industry to obsolescence. One Brazilian steel mill was first-rate, but another was highly politicized. Certainly, “efficiency” is unlikely to have been maximized to the extent that it would have been had free markets been allowed to work. But then again, free markets might well have been slower to generate the conditions for local enterprise and industrialization.

THE PROGRESS OF NO PROGRESS

The South should be allowed to use some of the same developmental policies that were once tolerated by the GATT on the condition that they do not undermine global prospects for raising economic welfare. This condition would almost certainly not be met if the economic integration agreements already fully implemented by the GATT and WTO were abrogated. A rollback would create a nightmare of uncertainty and declining trade. A further reduction in Southern countries’ tariffs could be pegged to a rise in their per capita incomes. The North should increase its quotas for Southern exports of agricultural and labor-intensive products.

Trade barriers aside, the WTO would be wise to see the pragmatic potential in moving neither backward nor forward for a while. It would not be a sin, for example, to give devel-

oping countries a breather on issues linked to intellectual property rights and to foreign investors’ rights. By the same token, it would probably make sense to give the developing world a de facto veto on other major globalization initiatives as long as they are making good-faith efforts to jump-start their economies. Standing still is difficult in cultures that associate change with progress, but arguably a stationary state would raise welfare in the post-September 11 world.

In the case of trade-related investment property rights (TRIPs) for pharmaceuticals, the world’s leading multinational companies argue vociferously that patent piracy in India, China and Brazil reduces their revenues, expenditures for research and development and, hence, the production of new life-saving drugs. For their part, Southern drug makers argue that patent piracy increases international competition and, hence, world welfare.

According to this argument, mergers and acquisitions have raised the market power of the big drug companies, which were losing market share in the South because they are inefficient. In India, imports and locally produced drugs by multinationals’ affiliates or subsidiaries accounted for 75 percent of India’s market in 1975. Two decades later, they accounted for only 32 percent. The decline in the multinationals’ market share was due to both their slowness to market and high prices. A top drug like Ciprofloxacin was priced by a multinational corporation in India at \$40, compared with \$2.42 by a locally owned company.

In the case of trade-related investment measures (TRIMs), bitter opposition from the South led the Paris-based Organization for Economic Cooperation and Development to abandon its controversial Multilateral Agreement on Investment, which would have given MNCs a free hand to buy into whatever coun-

try or whichever industry they liked (excluding defense and culture). The European Union and Japan are now promoting a similar measure under the WTO. If it is tabled in response to the South's newfound bargaining power and volubility, multinationals operating in their midst will continue to face performance standards pertaining to technology transfer, local content and trade balancing (whereby they must export an amount equivalent to what they import to conserve foreign exchange). MNCs will also continue to be restrained from engineering hostile takeovers of national companies and from crowding out national competitors before they learn the ropes. (Taiwan gave national companies a five-year head start in telecommunications.)

It's not as though advanced economies are being asked to do more for the poor countries than they do for their own. Liberal rhetoric notwithstanding, loopholes have enabled the WTO to keep its rich constituents happy without breaking treaty obligations. If an industry is threatened by foreign competition, a WTO member can protect it for eight years or invoke antidumping measures. Subsidies are strictly verboten when it comes to exports by the South. But they are strictly kosher when it comes to science and technology, and regional development – otherwise the United States, European Union and Japan might abandon the WTO. American pharmaceutical companies enjoy large indirect subsidies from the National Institute of Health, and American manufacturers of aircraft get large indirect subsidies from the Department of Defense. Analogous support is available from the European Union and Japan.

With ingenuity, “the remainder” can use such measures to strengthen their own industries and companies, just as “the rest” is now doing. The South's demands for heterogeneous developmental policies could be met by

freezing TRIPs and TRIMs and by exploiting existing WTO loopholes. It is still unclear, though, how well its economies would fare under so tolerant a global regime.

Much depends on whether “the remainder” can create control mechanisms that carve out a corruption-free development zone in which subsidies are tied to concrete, monitored performance standards. Much also depends on growth in the international economy. When “the rest” rose, they did so during a golden age of capitalism, with growth rates still unmatched. Tariffs started from a high base and reductions made a big impact. The attention of the United States and Europe was riveted on each other's trade barriers, and the developing world was benignly neglected – or given a break to keep its sympathies with the anticommunist West.

Now the developing world is regarded as an “emerging market,” and competition among countries within this world is fierce.

The major agent of globalization has been the multinational company. Multinationals account for most foreign direct investment and a rising share of foreign trade – maybe as much as two-thirds in the case of manufacturing. Virtually all the world's leading multinational companies are from a dozen or so Northern countries; in part, this explains the North-South divide. If Northern negotiators to the WTO can finesse the sectoral demands of their own multinationals, big drug companies, farmers, steel workers and textile mills, and if the South's demands for developmental policies succeed in creating world-class locally owned companies, the upshot will be globalism with a kinder, gentler face. If they can't, existing multinationals will remake the whole world in their own image, with inflammatory effects. It is in the interests of peace and prosperity to give the entrepreneurial upstarts a fighting chance. **M**