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Book Review

Leonard Bierman

BOOK REVIEW

Trade Policies and Developing Nations. By Anne O. Krueger. Washington: The Brookings Institution, 1995.

*Leonard Bierman**

This book is part of a 22-volume series published by the Brookings Institution dealing with the issue of "Integrating National Economies." The goal of the series is to examine problems which can ensue from economic globalization in a world of sovereign nation-states. More specifically, the series focuses on the lowering of world trade barriers and the lowering of economic distances between nations due to increased technology which has occurred since World War II. The result is that the line between "international" and "domestic" policies is today often blurred, and there are considerable "cross-border spillovers" (*i.e.*, pollution). Among nations, problems such as these are generally best dealt with through inter-governmental cooperation including the formation of regional pacts such as the European Community (EC). All of this, of course, threatens the autonomy and sovereignty of individual nation-states.

This particular volume in the series deals with the issue of world economic integration from the perspective of developing countries. It is written by Professor Anne O. Krueger of the economics department at Stanford University. Professor Krueger was formerly vice president of economics and research at the World Bank and is well known for her research and writing regarding developing countries. Reviews of other volumes in this Brookings Institution series have been published previously in this *Journal*.[1]

Professor Krueger begins her analysis by focusing on the "import substitution" policies of developing countries in the early post-World War II era. While industrialized countries were removing trade barriers and lowering tariffs during this period, developing countries were

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* Leonard Bierman is a Professor of Management at Texas A&M University.

1 *See, e.g.*, Book Review, 15 Nw. J. Int'l L. & Bus. 698 (1995).

trying to insulate their economies from the rest of the world. At the heart of this developing country strategy was the replacement or substitution of imported goods with domestically produced goods protected by government mandates—hence the term "import substitution" policies. Developing countries adopted these policies, in large measure, in response to their colonial pasts. The countries felt that they had suffered economically because of prior economic dependence on richer countries and wanted a break from this past. The idea was to attain economic growth and prosperity through economic independence.

The entire thrust of Professor Krueger's book is that such "import substitution" policies did not and do not work. Krueger maintains that the only way for developing countries to make economic progress is through "outer-oriented" economic and trade policies. She illustrates this point by discussing at some length the situation of the East Asian newly industrializing countries (NICs), namely Hong Kong, Korea, Singapore, and Taiwan.

Krueger notes that per capita incomes in Taiwan and Korea, for example, were extremely low in the early 1950s and that each of these countries had experienced severe economic difficulties. However, by shifting from insular "import substitution" economic policies to outer-oriented, export-driven trade policies, these countries experienced phenomenal economic growth. Korea, for example, increased its exports from $31 million in 1960 to $882 million in 1970 and more than doubled its real GDP in the same period. Debunking assertions that economic growth in East Asia represented a special situation, she points to Chile and Turkey as more recent examples of how trade openness led to improved economic performance.

She concludes the first portion of her book by arguing that an economic strategy of "import substitution" cannot sustain growth. She notes that such policies may work for some period of time and that there will be a variety of vested interests wishing to keep the given domestic economy sheltered. Over time, though, she argues that economic growth in such a construct is extremely difficult to maintain and that, for developing countries to continue to grow, they need to rely on the international market.

Part Two of her book deals with the role of developing countries in the international economy, particularly the General Agreement on Tariffs and Trade (GATT). She notes that GATT made special provisions for developing countries, especially Article XVIII: B. This Article allowed developing countries to more easily adopt quantitative and other restrictions on imports and to both be members of GATT and pursue "import substitution" trade policies. In addition, in the mid-1970s, the developing countries formulated the Generalized System of Preference (GSP), which subjected exports from developing countries to lower rates of duty than comparable exports from other developed countries. However, despite these provisions, Krueger notes that developing countries played no major role in GATT until the 1980s and the recently concluded Uruguay Round of negotiations.

Krueger then goes through an excellent and very useful discussion of the impact of the Uruguay Round of GATT negotiations on developing countries. During the Uruguay Round, developing countries, for the first time, sought to influence the outcome of the trade negotiations rather than simply wait for reciprocal tariff reductions among developed countries and then, as Krueger puts it, "free ride" on those reductions. Numerous provisions of the Uruguay Round directly impact developing countries.

First, the Uruguay Round commits nearly all GATT countries to phase out all quantitative restrictions such as import quotas. The only exception is for "least developed countries," defined as countries with per capita incomes under $1,000. The Uruguay Round creates different rules and timetables for "developed countries," "developing countries," and the "least developed countries" noted above.

With respect to the phaseout of quantitative restrictions, Krueger notes that perhaps the most important is the ten-year phaseout of the Multifiber Arrangement (MFA). The MFA has, since the 1950s, imposed quantitative limits on the amount of textile and apparel imports into industrialized countries. Krueger cites statistics that the tariff equivalent of MFA quotas was 48 percent for textiles and 23 percent for apparel for the United States in 1990. Because of this, U.S. consumers annually paid over $8 billion more for apparel and textiles than they would have without the MFA. The phaseout of the MFA will, thus, be a major boon for developing countries exporting low-cost textiles and apparel. Krueger cites statistics that world trade in textiles and apparel may increase between 34 and 60 percent once the MFA phaseout is completed.

Krueger also points out that the Uruguay Round will greatly liberalize trade in agricultural commodities, benefiting developing countries that are net exporters. The agreement also reduces government export subsidies and support for agriculture. Krueger cites estimates that world trade in agricultural commodities should increase by approximately 20 percent once the Uruguay Round's mandates are fully phased-in.

While reductions in quantitative restrictions and in agricultural subsidies were generally changes sought by developing countries, another major Uruguay Round change, increased intellectual property rights, was clearly sought by the *developed* countries. Krueger presents a good discussion of the genesis of this Uruguay Round provision which provides protection for: copyrights, trademarks, industrial designs, geographical indications, patents, layout designs of integrated circuits, and undisclosed information. Developed countries have one year from the effective date of the Uruguay Round to adopt necessary protective legislation, while most developing countries have five years to adopt national provisions protecting such intellectual property.

Krueger notes that, in the short-run, many developing countries will be hurt by these new intellectual property provisions, paying considerably more for pharmaceuticals, reprinting rights for books, and other items. Of course, in the long-run, better protection of intellectual property rights should help spur creative research and development of a kind which should help these countries. Nevertheless, there will be short-run costs.

One exception Krueger notes, however, may be the East Asian NICs. She points out that these countries are probably already far enough advanced technologically to benefit immediately from the Uruguay Round's stronger intellectual property protections.

A final point in this regard that Krueger highlights, although perhaps not enough, is the administrative capacity of some of the developing countries to properly enforce intellectual property laws. She is concerned that, to the extent scarce administrative resources are allocated to this endeavor, they will be taken away from perhaps more "worthy" concerns (imposing even greater costs on the given developing country). This seems to be a very valid point. Moreover, allocation issues aside, one might question whether the requisite administrative infrastructures exist at all in some developing countries.

Krueger ends her discussion of the impact of the Uruguay Round negotiations on developing countries with a discussion of the issue of trade in services. She accurately notes the increasing importance of this area and the fact that the Uruguay Round provides for further negotiations under the GATT/World Trade Organization (WTO) umbrella. She notes that the resistance of developing countries against further negotiations in this area diminished as they realized they held comparative advantages in various service areas — for example, construction — and would thus benefit from greater market access.

In concluding her discussion, Krueger notes other aspects of the agreement, such as the new dispute settlement procedures of the WTO. She asserts, however, that these other aspects will not significantly affect trade policies and administration in developing countries. This contention seems open to some dispute. Indeed, some observers have maintained that the new WTO dispute settlement mechanism may well be the most important gain for developing countries in the whole agreement. Under the former set of rules, it was very easy for any country to block a GATT panel ruling, and, as a result, developing countries did not view the process as having much credibility. Under the WTO, however, dispute settlement rules have been enhanced considerably — for instance, it is now extremely difficult to block a panel ruling. This could ultimately prove a boon to developing countries since they will be able to register complaints under the GATT on a more equal footing.

In the last part of the volume, Professor Krueger goes beyond the Uruguay Round and looks at issues surrounding even deeper economic integration of developing countries. In this regard, she gives considerable attention to developments in both the EC and the North American Free Trade Agreement (NAFTA).

Her core point here is that it may be easier for advanced developing countries to achieve deeper economic integration than commonly thought. In particular, she points to the successful accession of Spain and Portugal into the EC and to the fact that there was very little opposition in Mexico to its joining the NAFTA. She notes that the primary opposition was in the United States. This suggests it may be resistance in developed countries, rather than difficulties in developing countries, which constrain deeper world economic integration.

In discussing the EC accessions, Krueger downplays the role that transfers of funds from richer EC countries have played in smoothing EC integration. She perhaps, however, dismisses this contention too hastily. Under the European Union's structural fund formulas, Spain receives approximately $3 billion annually, and Greece and Portugal both receive over $1 billion per year. Moreover, these countries receive considerable inflows of private capital associated with their membership in the European Union. Neither of these sources of capital is likely to be available to other, lesser developed countries venturing into deeper economic integration.

In her discussion of the NAFTA and EC accession, Krueger issues a sharp cautionary note regarding the subject of labor standards. She forcefully points out that, for many developing countries, cheap labor is their primary "comparative advantage." If more developed countries impose worker safety and other labor standards on these countries, they rob them of this comparative advantage and, in a sense, "kill them with kindness." The idea is that, while intentions may be good, these regulations increase the cost of labor and goods, and ultimately decrease the number of jobs.

An analysis of this issue, however, should be more thorough. First, what about workers in developed countries who lose jobs due to greater integration with low-wage developing countries? This clearly was and is the concern of both the AFL-CIO and Ross Perot regarding Mexico's entry into the NAFTA. Formulating meaningful worker adjustment programs in the United States and Canada is not easy.

Second, the Mexican situation is, in many ways, an easy one because Mexico already has a rather comprehensive set of laws protecting basic worker rights. Thus, the goal of the labor side agreement to the NAFTA between the United States, Canada, and Mexico is simply to require each of the signatory countries to enforce its own labor laws. The idea is that Mexico simply needs to enforce its own labor laws. However, at present, many developing and semi-developing countries do not have comprehensive laws protecting worker rights, which creates rather stark differentials in national treatment.

As Krueger closes her text with a general valedictory about the need for greater economic integration or lberalized trade, the word "trust" comes to mind. Developing countries initiated insular "import substitution" trade policies because they did not trust their former colonial masters. Over the years, some of that distrust has melted away, in some cases aided by billions of dollars of financial assistance. Nevertheless, the trust issue still seems to be highly relevant. For example, developing countries are trusting that large developed countries will abide by the decisions of the new WTO dispute settlement mechanism, and that they will fulfill their Uruguay Round commitment to completely dismantle the Multifiber Arrangement by the year 2005. Should this trust on the part of developing countries turn out to be misplaced, we may well be back to square one.