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Chapter IV

TOWARDS A NEW FORM OF GLOBAL INTERDEPENDENCE

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TOWARDS A NEW FORM OF GLOBAL INTERDEPENDENCE

A. Introduction

In the past, developing-country trade relied mainly on primary commodity exports to developed countries in exchange for imports of manufactures. The comparatively small proportion of developing-country manufactured exports tended to be in resource- and labour-intensive products.

It has long been argued that such a trade pattern provides insufficient support to economic growth in developing countries. Both the productivity potential and the income elasticity of demand for primary commodities are usually lower than for most manufactured products, with the result that the global demand potential and the growth stimulus of primary commodity exports remain limited.

Furthermore, growth in demand for primary commodity imports from developed countries has weakened over the past three decades due to both the slowdown in their growth and their move away from raw-material-intensive industrial production activities towards an increasingly service-based economic structure. Long-standing market-access barriers, combined with difficulties and high costs

of market entry, have also hampered developing-country exports to developed countries.

Trade among developing countries, also called South-South trade, has sometimes been promoted as an alternative to this traditional trade pattern. On this view, South-South trade can shield against a decline in demand of developed countries for primary commodity exports, as well as provide an opportunity for export diversification away from a narrow dependence on primary commodities. In particular, manufactures with a relatively high skill content could be more important in manufactured trade among developing countries than in their manufactured exports to developed countries.

During the 1970s, some progress in this direction was made, as South-South trade was growing considerably faster than both world trade and trade among developed countries. It is true that much of the increase in South-South trade as a share of total world trade during the 1970s was related to the rise in commodity prices, particularly of petroleum, and it quickly dissipated fol-

lowing the price declines during the 1980s. But some of it also resulted from a rise in intra-regional trade of manufactures, particularly in East Asia and Latin America. However, the economic and financial crises in much of the developing world, including many Latin American countries, during the early 1980s had a strong adverse effect on South-South trade.

The emergence of a number of Asian developing countries to form a new growth pole in the world economy has renewed hopes that South-South trade could provide additional momentum to development. Indeed, trade statistics since the mid-1980s reveal three striking features: (i) a dramatic increase in the value of manufactured exports from developing countries; (ii) a rising share of developing countries in world trade; and (iii) a strong increase of South-South trade in both primary commodities and manufactures. Taken together, these three features have sometimes been referred to as the “new geography of trade” (UNCTAD, 2004c).

Table 4.1 provides an illustration of the evolution of these three features over the period 1965–2003.¹ It shows that, as a share of developing countries’ total exports, South-South exports increased from 25 per cent in 1965 to 43 per cent in 2003. This was accompanied by a decline in the share of their exports to developed countries, from 69 per cent in 1965 to 54 per cent in 2003. At the

same time the share of the first-tier NIEs and China in South-South imports rose from about one fifth (\$1.3 billion out of \$6.4 billion) in 1965 to almost

two thirds (\$586 billion out of \$921 billion) in 2003, and their share in developing-country exports to developed countries rose from 8 per cent (\$1.5 billion out of \$17.6 billion) in 1965 to almost 50 per cent (\$545 billion out of \$1,142 billion) in 2003. The increase in their share of developing-country exports to developed countries has been

particularly pronounced for manufactures, which rose from 45 per cent (\$0.9 billion out of \$2.0 billion) in 1965 to 58 per cent (\$512 billion out of \$879 billion) in 2003.² The table also shows that the shares of developing-country exports of primary commodities to developed countries fell from 72 per cent in 1965 to 53 per cent in 2003, while the share traded between them rose from 22 per cent in 1965 to 41 per cent in 2003. Yet, again, the NIEs and China accounted for more than half of this growth.

These figures raise the following questions: (i) What are the reasons for the rising importance of developing countries in world trade? (ii) How widespread is this

phenomenon? (iii) What are the prospects for a further expansion of developing countries’ trade in world trade and of its role in stimulating economic development? Sections B–D of this chapter focus on these questions.

Developing countries’ traditional reliance on developed-country markets and primary commodities for their exports cannot adequately support growth. ...

... South-South trade has been promoted as an alternative.

Table 4.1

MATRIX OF WORLD MERCHANDISE TRADE BY MAJOR PRODUCT CATEGORY, 1965, 1985 AND 2003						
Exporters	Importers					
	<i>Developed countries</i>		<i>Developing countries</i>		<i>of which: First-tier NIEs and China</i>	
	<i>Value (\$ billion)</i>	<i>Share^a (Per cent)</i>	<i>Value (\$ billion)</i>	<i>Share^a (Per cent)</i>	<i>Value (\$ billion)</i>	<i>Share^a (Per cent)</i>
1965						
Developed countries						
All merchandise	87.0	67.2	29.3	22.6	2.8	2.2
Manufactures	55.3	64.5	22.6	26.4	2.0	2.3
Primary commodities	30.4	75.2	6.2	15.2	0.8	2.0
Developing countries						
All merchandise	17.6	68.9	6.4	25.1	1.1	4.3
Manufactures	2.0	53.4	1.6	43.8	0.2	5.1
Primary commodities	15.6	71.7	4.7	21.8	0.9	4.1
<i>of which:</i>						
First-tier NIEs and China						
All merchandise	1.5	53.7	1.3	47.1	0.2	7.7
Manufactures	0.9	55.5	0.7	47.2	0.1	6.7
Primary commodities	0.6	51.9	0.5	46.3	0.1	9.3
1985						
Developed countries						
All merchandise	851.3	67.5	279.2	22.1	79.1	6.3
Manufactures	616.9	67.0	221.2	24.0	63.6	6.9
Primary commodities	213.8	71.6	50.5	16.9	13.8	4.6
Developing countries						
All merchandise	217.8	60.3	97.0	26.9	38.3	10.6
Manufactures	74.3	58.3	43.0	33.7	17.0	13.3
Primary commodities	131.9	59.4	40.3	18.2	12.7	5.7
<i>of which:</i>						
First-tier NIEs and China						
All merchandise	59.5	54.7	45.7	42.0	23.3	21.4
Manufactures	42.5	58.0	24.8	33.8	12.2	16.6
Primary commodities	6.7	25.5	7.9	30.1	2.8	10.7
2003						
Developed countries						
All merchandise	3 555.1	74.7	1 033.4	21.7	418.0	8.8
Manufactures	2 829.7	74.0	864.3	22.6	349.7	9.1
Primary commodities	614.3	78.0	136.2	17.3	53.9	6.8
Developing countries						
All merchandise	1 141.7	53.8	921.4	43.4	510.4	24.1
Manufactures	879.1	54.4	714.3	44.2	429.2	26.5
Primary commodities	258.3	52.6	200.2	40.8	79.1	16.1
<i>of which:</i>						
First-tier NIEs and China						
All merchandise	545.4	47.5	586.0	51.0	385.1	33.5
Manufactures	511.6	48.6	526.8	50.1	350.6	33.3
Primary commodities	31.6	35.6	54.6	61.6	33.7	37.9

Source: UNCTAD secretariat calculations, based on UN COMTRADE.

Note: The table is derived from data that countries report to the United Nations (see also text note 1). First-tier NIEs comprise Hong Kong (China), the Republic of Korea, Singapore and Taiwan Province of China.

a Share in group's total exports of the product group. The shares of South-East Europe and the Commonwealth of Independent States (CIS) are not included in this table, which explains why the shares do not add up to 100.

B. The growing importance of developing countries in global markets

The share of developing countries in world merchandise trade has strongly increased over the past few decades. Their export share has almost doubled since 1970 and has stood at more than 30 per cent over the past few years, while their import share has risen less rapidly, reaching 29 per cent. Developed countries, on the other hand, have experienced a decline in their share of world merchandise trade by about 10 percentage points since 1970, but they still account for about two-thirds of such trade (table 4.2).

The growing importance of developing countries in world merchandise trade has been neither a continuous process nor uniformly spread across the various developing regions. Their exports grew very rapidly during the 1970s, but this was largely due to the temporary hike in international oil prices. Thus, the major oil exporting countries, many of which are located in West Asia, were responsible for a significant part of the rise in developing-country exports during the 1970s. The subsequent sharp fall in oil prices, combined with the effects of the debt crisis of the early 1980s, led to the shrinking of developing countries' share in world trade during the 1980s. As a result, in 1990 the shares of many developing countries, particularly in Africa and Latin America and the Caribbean, were lower than their shares in 1970. Despite a strong rebound during the 1990s, the average shares in world trade of these two regions have not recovered to the levels reached in 1980.

Contrary to the experience of the other developing regions, East Asia's share in world trade

has grown at a consistently rapid rate since the early 1960s, except for a temporary decline in the immediate aftermath of the Asian crisis in 1997–1998. The share of the first-tier NIEs has grown three- to fourfold since 1970, and China's share has risen more than fivefold since 1980. Indeed, over the period 1970–2003 as a whole, the NIEs and China together have been responsible for almost the entire rise in the share of world exports of developing countries taken as a group.

The rapidly growing South-South trade has often been identified as a major driving force behind the rising share in world trade of all developing countries taken as a group. Indeed, between 1970 and 2003, South-South trade rose considerably faster than both world trade and trade among developed countries (table 4.3). The share of South-South exports in total developing-country exports roughly doubled, increasing from about 23 per cent in the 1970s to over 40 per cent in the period 2000–2003. Moreover, South-South exports as a percentage of developing-country exports to developed country markets (South-North trade) have also more than doubled, reaching a level of about 74 per cent on average during the period 2000–2003 (and exceeding 80 per cent in 2003).

Manufactures have been the most important product category in South-South trade relative to both developing countries' total exports and their exports to developed countries. The only exception to this was a transitory period following the Asian crisis when agricultural products overtook

Table 4.2

THE ORIGIN AND DESTINATION OF MERCHANDISE TRADE, 1970–2003									
(Per cent)									
	Market share					Average annual growth in value			
	1970	1980	1990	2000	2003	1970–1980	1980–1990	1990–2000	2000–2003
A. World merchandise exports by region/country									
Developed countries	75.0	65.3	72.0	65.7	64.8	18.8	7.3	5.9	4.6
Developing countries	19.2	29.5	24.3	31.6	32.1	25.6	3.1	8.9	5.8
<i>of which:</i>									
Latin America and the Caribbean	5.5	5.5	4.1	5.5	5.0	20.8	1.7	10.3	1.6
Developing Asia	8.5	18.0	16.9	23.8	24.7	29.6	4.6	9.5	6.7
South Asia	1.1	0.7	0.8	1.0	1.1	16.1	6.9	9.1	8.6
<i>of which: India</i>	0.6	0.4	0.5	0.7	0.8	17.3	7.3	9.5	10.7
East Asia	4.2	7.1	12.0	18.6	19.4	26.6	11.7	10.4	6.9
First-tier NIEs	2.0	3.8	7.6	10.3	9.4	28.2	14.4	8.8	2.6
China	0.7	0.9	1.8	3.9	5.8	20.0	12.8	14.5	20.8
West Asia	3.1	9.9	3.9	4.1	4.1	34.5	-6.3	5.8	5.2
Africa	5.0	5.9	3.2	2.3	2.4	21.6	-1.2	2.8	6.9
North Africa	1.6	2.2	1.2	0.8	0.9	23.7	-2.3	2.2	5.8
Other Africa	3.4	3.7	2.0	1.4	1.5	20.5	-0.5	3.2	7.5
Memo item:									
Developing countries, excl. first-tier NIEs and China	16.5	24.8	14.8	17.5	16.8	25.5	-0.9	8.1	3.8
B. World merchandise imports by region/country									
Developed countries	75.6	70.8	73.1	69.5	68.4	19.4	6.9	6.2	4.3
Developing countries	18.8	24.0	22.5	28.7	29.0	23.6	4.0	8.3	5.4
<i>of which:</i>									
Latin America and the Caribbean	5.7	6.1	3.7	5.9	4.8	20.6	0.1	11.5	-2.5
Developing Asia	8.4	13.1	15.8	20.8	21.9	26.6	6.5	8.2	7.1
South Asia	1.3	1.3	1.1	1.2	1.4	20.0	3.7	8.6	9.2
<i>of which: India</i>	0.6	0.7	0.7	0.8	0.9	20.7	4.2	10.1	11.5
East Asia	5.1	7.2	11.7	16.7	17.6	24.4	10.9	8.9	7.0
First-tier NIEs	2.7	4.3	7.4	9.8	8.7	25.7	11.9	8.1	1.2
China	0.7	1.0	1.5	3.4	5.4	23.7	13.5	13.0	22.3
West Asia	2.0	4.6	2.9	2.8	2.9	33.6	-2.4	5.2	7.1
Africa	4.4	4.6	2.9	2.0	2.2	21.0	-0.2	3.5	8.8
North Africa	1.2	1.5	1.2	0.7	0.8	25.6	2.7	2.8	6.1
Other Africa	3.3	3.1	1.6	1.2	1.4	18.9	-2.1	4.0	10.3
Memo item:									
Developing countries, excl. first-tier NIEs and China	15.4	18.8	13.6	15.5	15.0	23.2	0.7	7.7	3.5

Source: UNCTAD *Handbook of Statistics*, various issues, table 1.1

Note: The group of first-tier NIEs comprises Hong Kong (China), the Republic of Korea, Singapore, Taiwan Province of China. East Asia comprises China, Cambodia, Indonesia, Malaysia, Myanmar, the Philippines, Thailand, Viet Nam and the first-tier NIEs. South Asia comprises Afghanistan, Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri Lanka. The shares of South-East Europe and the Commonwealth of Independent States (CIS) are not included in this table, which explains why the shares do not add up to 100.

Table 4.3

SOUTH-SOUTH TRADE IN WORLD TRADE, 1970–2003

	1970–1980	1980–1990	1990–2000	2000–2003	<i>Memo item:</i> 1970–2003
South-South trade					
<i>(Average annual percentage change)</i>					
Total merchandise exports	26.7	5.8	10.9	7.9	13.3
Agricultural products	20.5	4.9	7.9	7.3	9.4
Fuels, minerals and metals ^a	30.2	-8.8	7.8	-0.9	7.6
Manufactures	26.4	16.9	12.1	9.6	18.3
South-South trade as a percentage of total developing-country exports					
<i>(Period averages)</i>					
Total merchandise exports	22.9	29.5	39.1	40.9	31.6
Agricultural products	22.3	30.6	39.6	43.1	32.0
Fuels, minerals and metals ^a	20.1	21.1	30.7	36.2	25.2
Manufactures	34.5	36.5	41.6	41.9	37.9
South-South trade as a percentage of developing-country exports to developed countries					
<i>(Period averages)</i>					
Total merchandise exports	35.3	48.0	71.2	74.3	53.8
Agricultural products	34.5	52.5	71.6	80.9	55.5
Fuels, minerals and metals ^a	30.9	32.4	60.9	71.5	44.4
Manufactures	60.1	64.4	74.3	73.8	66.8
South-South trade as a percentage of total developing-country imports					
<i>(Period averages)</i>					
Total merchandise imports	26.1	32.4	37.8	43.9	33.1
Agricultural products	37.9	36.3	42.0	44.9	39.4
Fuels, minerals and metals ^a	74.1	72.9	67.2	66.8	70.9
Manufactures	11.6	20.1	33.1	39.8	23.3
South-South trade as a percentage of developing-country imports from developed countries					
<i>(Period averages)</i>					
Total merchandise imports	38.0	51.5	64.7	85.1	54.4
Agricultural products	65.7	62.2	76.8	87.1	70.4
Fuels, minerals and metals ^a	394.2	396.2	261.3	327.9	344.3
Manufactures	13.8	27.4	51.8	69.6	34.7
Memo items:					
Total world exports					
<i>(Average annual percentage change)</i>					
Total merchandise exports	20.2	6.7	7.4	4.5	9.2
Agricultural products	17.1	4.6	3.9	6.7	6.6
Fuels, minerals and metals ^a	27.1	-3.7	6.7	-1.6	6.5
Manufactures	19.0	10.1	7.9	5.2	10.3
Trade among developed countries					
<i>(Average annual percentage change)</i>					
Total merchandise exports	17.2	9.5	6.8	5.0	9.2
Agricultural products	15.4	6.4	3.6	8.1	6.8
Fuels, minerals and metals	19.9	1.0	5.1	2.8	7.3
Manufactures	17.1	11.2	7.4	4.9	9.8

Source: See table 4.1.

Note: The table is derived from data that countries report to the United Nations (see also text note 1).

^a Developing-country exports of fuels are underreported for recent years due to missing data.

manufactures. But a comparison of South-South trade with that of developing-country exports to developed countries also reveals that primary commodities have been much more dynamic than manufactures: the percentage share of agricultural products and of fuels, minerals and metals in South-South trade relative to developing-country exports to developed countries has more than doubled since 1970, their increase being particularly strong since the early 1990s.

Table 4.3 also shows that the importance of trade among developing countries relative to their trade with developed

countries has risen more strongly for imports than for exports. This is the most apparent for manufactures, as their average share in South-South trade relative to developing-country imports from developed countries increased from about 14 per cent during the 1970s to about 70 per cent in 2000–2003. As discussed in more detail below, much of this is due to the rising importance of production-sharing within East Asia, resulting in a “triangular trade” pattern. This means that, rather than exporting directly to developed countries, the industrially relatively more advanced countries such as the Republic of Korea export intermediate production inputs to China, for example, where these inputs are used in production for export to developed countries. On an accounting basis, triangular trade leads to a rise of similar dimensions in both South-South and South-North exports, while in terms of imports it results in a rise only in South-South trade, but not in a rise of developing-country imports from developed countries. Thus the statistical effect of triangular trade is that trade in manufactures among developing countries relative to such trade with developed countries rises much more for imports than for exports. This mechanism also explains the different performance of trade in primary commodities and manufactures noted in the preceding paragraph: triangular trade by and large causes South-South manufactured exports to move *pari passu* with South-North manufactured exports, while this is not the case

South-South trade, especially in manufactures, has risen faster than both world trade and trade among developed countries.

South-South trade is concentrated in a few economies, mainly in East Asia.

for primary commodities in which there is no triangular trade.

The rapid rise in the importance of South-South trade, particularly over the past two decades, reflects a number of factors. First, it reflects an upswing after the downturn of such trade during the 1980s. Table 4.3 shows that growth in South-South trade during the 1980s was significantly slower than that of either world trade or trade among developed countries. While the global recession of the early 1980s affected the trade performance of both developed and devel-

oping countries, it had a particularly damaging impact on South-South trade. This is because it was associated with economic and financial crises in many developing countries, particularly in Latin America and Africa, caused by the collapse of commodity prices, the rising cost of servicing soaring external debts and the ensuing sharp contraction of the supply of commercial credit that reduced their capacity to import. Combined with slow or negative economic growth, the outcome was a substantial fall in the volume of these countries’ imports, including those from other developing countries (*TDR 1993*).

The impetus from Latin America and Africa to South-South trade also weakened considerably in the wake of the debt crisis, because many of these countries shifted the direction of their exports, particularly of manufactures, towards developed countries. This shift was partly motivated by the slowdown of economic activity in developed countries being much less sharp than in developing countries. Combined with the large size of developed-country markets, the relatively faster growth of demand in those markets provided better

opportunities for developing-country exporters. Another reason was that foreign-exchange-starved countries, particularly those in Africa, sought export revenues in convertible currencies in order to service their debt and to import, as far as possible, on credit.

The second reason for the rapid rise in the importance of trade among developing countries, particularly over the past two decades, has been trade liberalization. The move towards the adoption of more outward-oriented development strategies, along with trade reform and regional trade agreements, in a wide range of developing countries has significantly improved access to their markets, including for imports from other developing countries. More generally, average tariffs in developing countries fell to about one third their level of the mid-1980s, and this decline was accompanied by even larger reductions in non-tariff barriers and in exchange rate overvaluation. The reduction of developed-country tariff and non-tariff barriers during the same period of time was smaller (World Bank, 2004b: 76).

But the most important reason for the rapid growth of South-South trade is probably a combination of three factors: the widening growth differential between developing and developed countries; the large size of the rapidly growing developing countries; and the growing importance of intraregional specialization and production-sharing that has been closely linked to these countries' buoyant growth performance. Over the past three decades, developing countries as a group have recorded more rapid average real income growth than developed countries, and this difference has become increasingly larger over the past two decades. During the 1980s developed and developing countries grew at a pace of 3.1 per cent and 3.7 per cent, respectively; during the 1990s economic growth in developed countries slowed down to 2.4 per cent, but in developing countries it accelerated to 4.8 per cent; and during the period 2001–2004, average real income growth in developing countries was more than double that in developed countries (chapter I, table 1.1; and UNCTAD *Handbook of Statistics*, various issues, table 7.2).

Apart from relatively weak economic growth, developed countries (the traditional destination of developing country exports of primary commodities) have increasingly undergone structural change away from raw-material-intensive indus-

trial activities. This has limited their import demand for non-food primary commodities. Moreover, given only little change in the level and composition of per capita food consumption and stagnating or declining populations, developed country markets have shown little dynamism with respect to food imports from developing countries. This contrasts with those developing countries that have grown rapidly in the past few years. Given their generally lower levels of per capita income and rapidly increasing populations, as well as their still relatively low levels of industrialization, the income elasticity for food and

raw materials in these countries exceeds that in developed countries (chapter II). Thus, once economic growth and industrialization had gathered sufficient momentum in developing countries, many primary commodities that had previously displayed lacklustre performance in the world market for an extended period of time recovered their dynamism on the basis of the rapid growth and industrialization of some developing countries.

The impact on trade flows of the rising importance of developing countries as a growth pole in the world economy is largely due to the fact that this growth performance has been concentrated in the NIEs, China and India. Combined, these economies account for about one fifth of total world income (in terms of purchasing power parity) and two-fifths of the total world population.

Rapid economic growth and industrialization in East Asia have been accompanied by a marked trend towards greater integration and specialization in the region, which has led to a rapid expansion of trade within production networks. As discussed in some detail in *TDR 2002*, lower transport and communication costs, and reduced trade and regulatory barriers have facilitated production-sharing on a global basis. Production-sharing is generally concentrated in labour-intensive products; but it can also involve the location at different sites of labour-intensive segments of otherwise technologically complex production processes. It allows firms to exploit the comparative advantage of different locations specific to the production of particular components, including scale econo-

Much of the increase in South-South trade in manufactures, as shown in trade statistics, is due to double-counting ...

mies, and differences in labour costs across countries. Firms operating in East Asian economies have been particularly successful in spreading production activities in clothing, footwear and electronics across this subregion, taking advantage of labour-cost differentials.

International production networks promote a new pattern of trade, in which goods travel across several locations before reaching final consumers, and the total value of trade recorded in such products exceeds their value added by a considerable margin. As illustrated in figure 4.1, trade of such products within production networks can cause a very substantial increase in recorded trade among developing countries, without any increase in final consumption in developed countries. This rise in recorded South-South trade is higher the larger the import content of a good assembled in a developing country and exported to another developing country. Recorded South-South trade increases particularly fast if the trade within production networks involves passing through transshipment ports, such as Hong Kong (China) and Singapore.

Figure 4.2 illustrates how triangular trade leads to a rise in recorded South-South trade. It shows that the strong rise in manufactured exports from the Republic of Korea and Malaysia to China since the early 1990s has been accompanied by an almost equally strong rise in China's exports to the United States. This has two important implications for South-South trade. First, the magnitude of South-South trade in manufactures depends to a considerable extent on United States import demand for products for which production-sharing within East Asia plays an important role. Thus the recent rise in South-South trade is partly the result of strong growth in the United States economy, which, combined with increased competitiveness brought about by currency devaluations in the aftermath of the Asian crisis, provided an independent export stimulus; at the same time, the trade impulse was amplified by strong intra-regional trade linkages. But it also means that slower economic growth in the United States

... associated with triangular trade within international production networks and indirect maritime trade through regional hub ports.

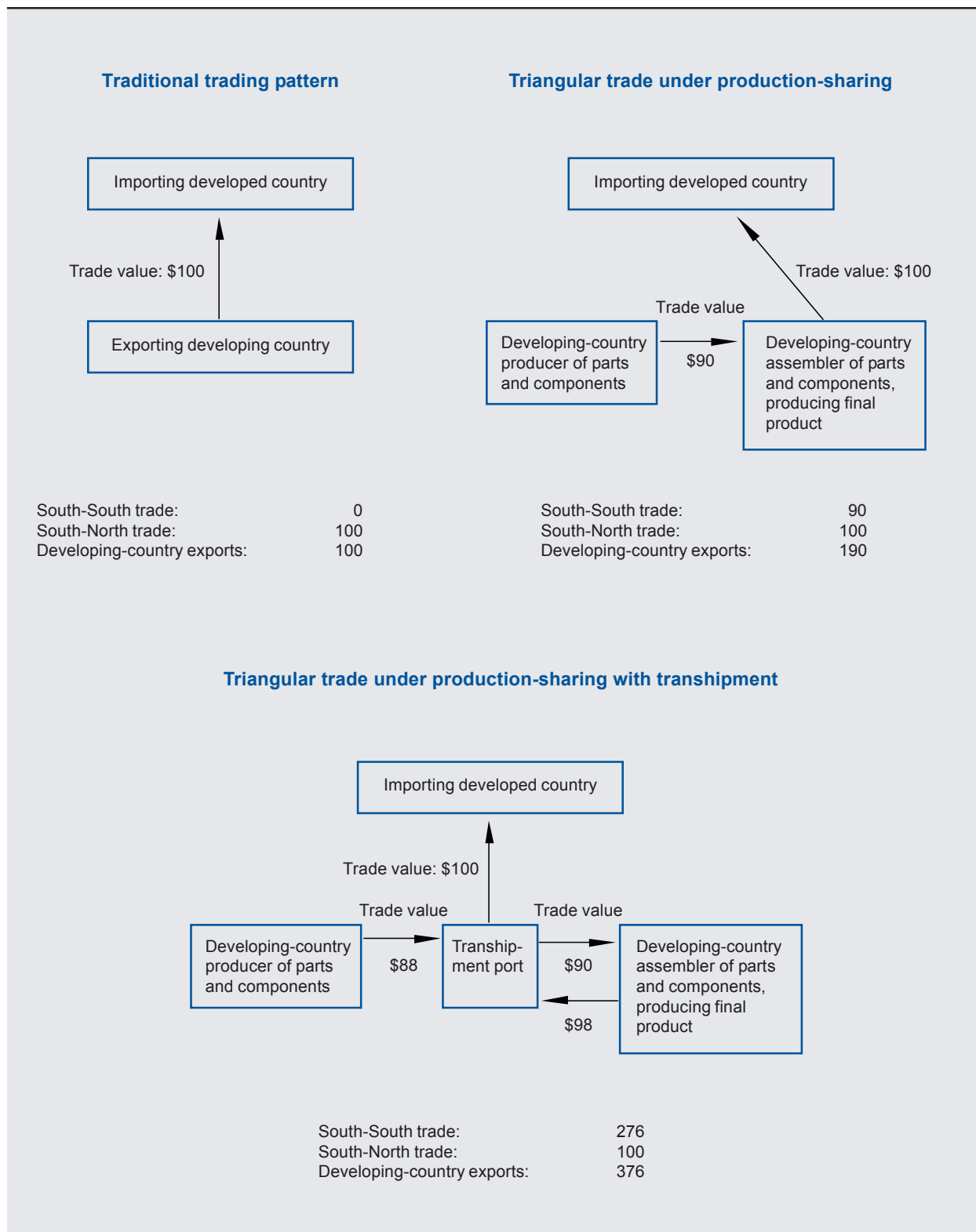
would reduce not only United States imports of finished products, but also China's imports of parts and components from which the finished products are assembled. Second, the magnitude of South-South trade in manufactures will decline to the extent that China succeeds in reducing the import content of its exports. As discussed in chapter II, there are indications that China is indeed reducing the share of imported parts and components in its electronics exports, many of which are directed to the United States.

The new pattern of international trade resulting from international production networks, and the strong involvement of East Asian economies in these networks, goes a long way in explaining two main new features of South-South trade, relative to the 1970s: its much larger size, already mentioned, and its narrow concentration among East Asian economies. In 2003, trade among East Asian economies accounted for about two thirds of total South-South trade (up from 21 per cent in the 1970s), while trade between East Asia and other developing countries accounted for about another 14 per cent (table 4.4). Intra-East Asian trade in manufactures has grown particularly rapidly. In 2003, trade among East Asian economies was responsible for 72 per cent of total South-South trade in manufactures, up from 26 per cent in 1970. But even for primary commodities, trade among East Asian countries now represents about one third of total South-South trade – broadly double the share in 1970. The bulk of this increasing importance of intra-East Asian trade as a share of total South-South trade occurred during the 1980s, when rapid growth and industrialization in the NIEs were accompanied by increasing intra-regional specialization of production and rapid trade integration by China.

South-South trade is concentrated in a few individual economies, mainly in East Asia. In 2003, the top 10 economies in South-South trade jointly accounted for about 84 per cent of total South-South exports and for about 78 per cent of total South-South imports. Brazil (as an exporter and as an importer) and Mexico (as an importer)

Figure 4.1

SCHEMATIC ILLUSTRATION OF THE IMPACT OF PRODUCTION-SHARING ON THE STATISTICALLY RECORDED VALUE OF SOUTH-SOUTH TRADE



Source: UNCTAD secretariat.
Note: The numbers used are fictitious.

are the only non-Asian countries that feature among these top 10 economies. The top two economies, China and Hong Kong (China), taken together, are responsible for more than one third of South-South trade (table 4.5).

The concentration of South-South trade is particularly strong in exports of manufactures in which the top 10 economies account for over 90 per cent – and China and Hong Kong (China) for about 40 per cent – of total South-South exports. It is less concentrated in primary commodities than in manufactures. This is especially true for exports where the top 10 economies account for roughly two-thirds to three-fourths of total South-South trade, and where countries from all developing regions rank among the top 10 traders. The fact that Singapore features among the leading countries in South-South trade of fuels, minerals and metals reflects its function as a regional hub port for transshipment of goods in this category to neighbouring countries.

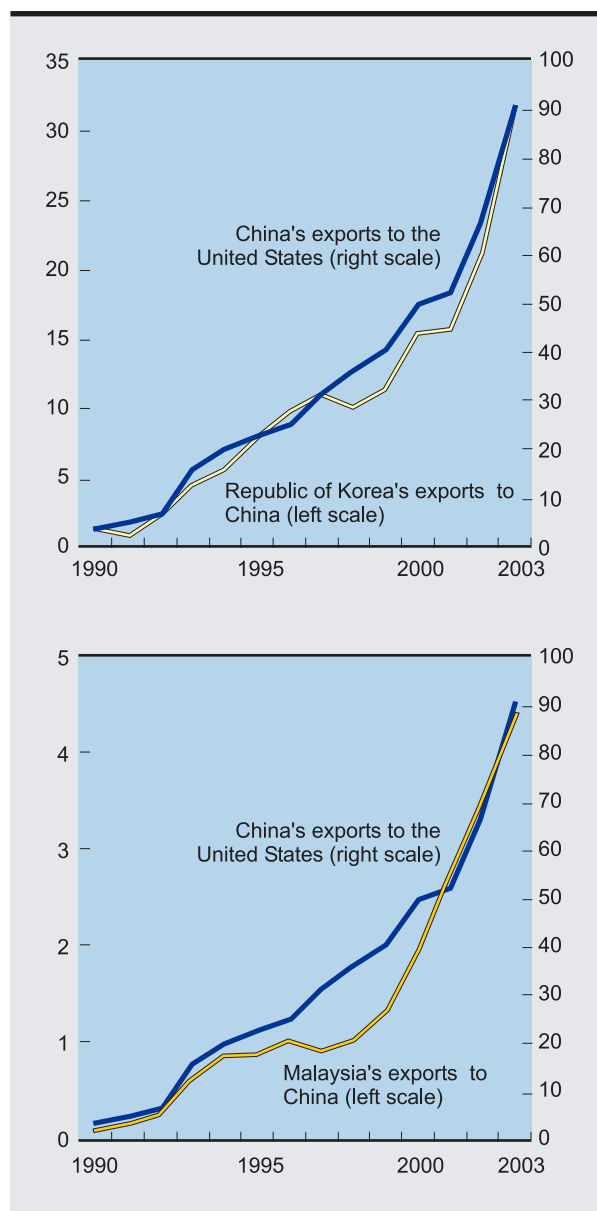
The function of Hong Kong (China) as a transshipment port for China's external trade alone is responsible for a substantial share of overall South-South trade. More than 40 per cent of China's exports to other developing countries go to Hong Kong (China) and about three quarters of the exports from Hong Kong (China) to other developing countries go to China. More specifically, exchanges between China and Hong Kong (China) represent about 20 per cent of total merchandise trade – and almost 25 per cent of manufactured trade – among developing countries.³

There are marked differences across individual developing countries regarding both the current reliance on developing-country markets and the change in this reliance since the early 1990s (table 4.6). Among the developing countries for which comprehensive data are available, Eritrea, Paraguay and Sudan rely more than 80 per cent on other developing countries for their exports. The landlocked situation of Paraguay and Sudan, and transshipment in the case of Eritrea, probably explain these high levels.⁴ By contrast, exports to other developing countries account for only 5 per cent of Mexico's total exports, and for 10–15 per cent of the total exports of a range of countries such as Bangladesh, Fiji, Jamaica, Madagascar, Mauritius, Morocco and Papua New Guinea.

Figure 4.2

TRIANGULAR TRADE IN MANUFACTURES BETWEEN EAST ASIA AND THE UNITED STATES, 1990–2003

(Billions of dollars)



Source: See table 4.1.

Strong reliance on a single export item (such as clothing, sugar, or a metal) and/or preferential access to developed-country markets are probably the main reasons, although they do not seem to have played such a strong role for other developing countries.

Table 4.4

SOUTH-SOUTH MERCHANDISE EXPORTS, BY GEOGRAPHICAL REGION, 1970–2003

	Share in total South-South exports of the respective product category (Per cent)					Average annual percentage growth in value (Per cent)				Memo item: Value (\$ million)	
	1970	1980	1990	2000	2003	1970– 1980	1980– 1990	1990– 2000	2000– 2003	1970	2003
	Asia										
<i>Asian exports to other developing countries</i>											
Total merchandise	9.7	11.8	4.8	8.4	8.1	29.8	-2.2	15.5	5.9	1 077	74 260
Manufactures	18.7	12.8	7.2	8.9	8.1	21.2	9.9	13.7	4.6	595	58 013
Primary commodities	6.2	11.2	0.1	6.8	7.0	34.7	-26.3	41.2	7.4	477	13 993
<i>Intra-Asian exports</i>											
Total merchandise	49.3	56.1	80.0	76.0	77.9	27.9	9.8	10.3	8.9	5 452	717 882
Manufactures	49.4	59.7	82.5	82.4	84.6	29.0	20.7	12.0	10.8	1 568	604 404
Primary commodities	50.1	55.3	74.9	56.8	54.5	27.5	-1.1	5.0	0.4	3 838	109 047
<i>East Asian exports to other developing countries</i>											
Total merchandise	11.3	11.7	14.1	14.1	14.2	28.4	7.9	11.0	7.7	1 249	130 628
Manufactures	19.4	24.1	16.3	16.0	15.3	31.6	11.6	11.8	7.4	616	109 113
Primary commodities	8.0	6.4	9.8	8.3	9.0	24.4	1.3	7.1	5.0	614	18 076
<i>Intra-East Asian exports</i>											
Total merchandise	21.0	20.1	57.5	62.1	64.4	25.6	19.5	11.6	9.6	2 326	593 650
Manufactures	26.5	31.5	67.2	70.5	72.1	27.1	27.5	12.5	10.7	842	514 702
Primary commodities	19.0	15.4	38.4	37.2	38.1	24.4	7.9	7.6	3.3	1 456	76 244
<i>South Asian exports to other developing countries</i>											
Total merchandise	7.0	3.5	2.5	2.6	3.6	20.4	3.7	10.9	20.0	778	33 128
Manufactures	14.2	5.7	2.4	2.7	3.2	18.0	5.8	13.2	15.8	452	23 186
Primary commodities	4.2	2.7	2.8	2.3	4.8	23.0	1.2	5.6	33.7	323	9 541
Latin America and the Caribbean											
<i>Latin American and Caribbean exports to other developing countries</i>											
Total merchandise	9.8	9.6	4.2	2.6	3.5	25.4	-2.3	7.2	19.4	1 084	32 166
Manufactures	2.5	4.4	2.8	0.9	1.3	33.2	11.7	1.3	21.7	79	8 967
Primary commodities	13.1	12.0	7.2	7.5	11.6	24.6	-7.5	10.4	18.5	1 004	23 182
<i>Intraregional exports</i>											
Total merchandise	18.7	13.6	8.5	8.3	6.6	22.7	1.6	11.6	-1.3	2 071	60 973
Manufactures	22.5	20.5	6.0	5.9	4.4	25.2	4.5	13.2	-2.4	714	31 094
Primary commodities	17.5	11.2	13.5	15.5	14.9	21.1	-0.7	10.0	-0.2	1 342	29 723
Africa											
<i>African exports to other developing countries</i>											
Total merchandise	5.4	6.0	1.1	2.8	2.3	29.8	-10.4	19.6	1.2	599	21 006
Manufactures	1.6	1.1	0.7	0.7	0.7	20.6	10.4	11.2	8.6	50	4 851
Primary commodities	7.2	7.0	2.0	9.1	8.0	28.1	-13.9	23.9	-0.7	550	16 112
<i>Intraregional exports</i>											
Total merchandise	5.7	1.2	1.2	1.9	1.6	13.5	0.1	17.0	4.8	629	14 506
Manufactures	4.9	1.4	0.9	1.1	0.9	13.5	6.7	16.1	7.0	157	6 620
Primary commodities	4.1	1.2	1.9	4.1	3.9	15.6	-3.6	18.6	2.9	315	7 817

Source: See table 4.1.

Note: See note to table 4.2 for country groupings. Total merchandise includes SITC 0 to 9, manufactures includes SITC 5 to 8 less 68, primary commodities includes SITC 0 to 4 plus 68.

Table 4.5

TOP 10 ECONOMIES IN SOUTH-SOUTH TRADE, 2003

(Percentage shares of total South-South trade)

Rank	Total merchandise	Manufactures	Fuels, mineral and metals	Agricultural products
Leading exporting economies				
1	China (19.7)	China (22.4)	Singapore (9.8)	China (11.5)
2	Hong Kong (China) (14.2)	Hong Kong (China) (17.2)	China (9.7)	Argentina (10.6)
3	Rep. of Korea (11.1)	Rep. of Korea (13.2)	Indonesia (7.3)	Brazil (10.2)
4	Singapore (9.4)	Taiwan Prov. of China (11.2)	Nigeria (6.4)	Malaysia (9.6)
5	Taiwan Prov. of China (9.3)	Singapore (9.7)	Iran, Islamic Rep. of (6.2)	Thailand (8.2)
6	Malaysia (6.0)	Malaysia (5.6)	Venezuela (5.9)	Indonesia (6.5)
7	Thailand (4.1)	Thailand (3.9)	Malaysia (5.8)	India (5.5)
8	India (3.4)	India (3.0)	Rep. of Korea (5.0)	Hong Kong (China) (5.1)
9	Brazil (3.3)	Brazil (2.4)	India (4.4)	Chile (2.6)
10	Indonesia (3.1)	Indonesia (2.1)	Chile (3.6)	Singapore (2.5)
Memo item:				
Share of top 10	83.5	90.7	64.2	72.3
Leading importing economies				
1	China (21.0)	Hong Kong (China) (23.3)	Rep. of Korea (20.4)	China (17.9)
2	Hong Kong (China) (17.7)	China (21.9)	China (19.1)	Hong Kong (China) (7.4)
3	Rep. of Korea (8.9)	Singapore (8.1)	Taiwan Prov. of China (8.7)	Rep. of Korea (7.2)
4	Singapore (7.7)	Rep. of Korea (5.7)	Singapore (8.2)	India (6.1)
5	Taiwan Prov. of China (5.9)	Taiwan Prov. of China (5.4)	Thailand (5.2)	Malaysia (4.2)
6	Malaysia (4.6)	Malaysia (5.0)	Indonesia (4.1)	Brazil (3.9)
7	Thailand (4.0)	Mexico (4.4)	Brazil (4.0)	Thailand (3.6)
8	Mexico (3.5)	Thailand (3.6)	Hong Kong (China) (3.3)	Saudi Arabia (3.6)
9	India (2.5)	India (2.3)	Turkey (3.2)	Singapore (3.4)
10	Brazil (2.2)	Philippines (1.9)	Malaysia (2.9)	Indonesia (3.0)
Memo item:				
Share of top 10	77.8	81.7	79.2	60.4

Source: See table 4.1.

There have also been wide cross-country variations of shifts in the importance of South-South trade in total exports. Since the early 1990s, the importance of other developing countries as a destination for their exports has halved for Bangladesh and Mexico, whereas it has more than tripled for the Dominican Republic, Honduras and Nigeria. Most importantly, on a country-specific basis, the importance of South-South trade for Africa and Latin America and the Caribbean has grown much more than for Asia, and it now accounts for a similar share in all three developing regions: for the countries included in table 4.6,

the unweighted average of the share of developing countries in total exports increased from 26 per cent to 39 per cent for Africa and from 29 per cent to 41 per cent for Latin America, compared to the much smaller increase from 34 per cent to 38 per cent for Asia.⁵

Indeed, many of the relatively small countries for which exports to other developing countries accounted for a sizeable share of their total exports over the past few years are located in West Africa, such as Benin (79 per cent), Niger (60 per cent), Senegal (53 per cent), and Togo

Table 4.6

IMPORTANCE OF SOUTH-SOUTH TRADE FOR DEVELOPING ECONOMIES, 1990–2003

(Share of exports to developing economies in total exports, per cent)

Africa			Asia			Latin America and the Caribbean		
Exporting economy	1990–1992	2000–2003	Exporting economy	1990–1992	2000–2003	Exporting economy	1990–1992	2000–2003
Algeria	6.7	15.6	Bangladesh	21.9	10.4	Antigua and Barbuda	..	53.4
Benin	47.2	79.1	China	60.4	41.0	Argentina	46.0	63.2
Cameroon	13.2	24.8	Fiji	22.2	13.7	Barbados	35.7	48.8
Côte d'Ivoire	..	36.5	Hong Kong (China)	47.3	54.3	Bolivia	45.9	58.5
Egypt	23.4	35.4	India	28.0	44.5	Brazil	33.3	38.1
Eritrea	..	83.3	Indonesia	33.7	45.5	Chile	27.6	39.3
Ethiopia	..	43.1	Iran, Islamic Rep. of	..	31.1	Colombia	24.0	33.4
Kenya	45.9	56.5	Jordan	70.4	58.9	Costa Rica	20.5	29.0
Madagascar	18.1	12.8	Macao (China)	22.4	22.1	Dominican Rep.	4.5	21.7
Malawi	9.6	26.1	Malaysia	48.6	50.2	Ecuador	31.7	37.2
Mali	73.5	27.7	Nepal	21.2	52.5	El Salvador	34.8	68.0
Mauritius	6.6	10.2	Oman	27.8	37.8	Honduras	11.0	37.5
Morocco	24.1	14.5	Pakistan	38.3	40.3	Jamaica	13.1	11.1
Niger	..	59.6	Papua New Guinea	17.3	10.4	Mexico	8.2	5.0
Nigeria	7.3	31.4	Philippines	20.8	38.6	Montserrat	..	52.7
Senegal	37.4	53.1	Qatar	21.0	49.1	Nicaragua	28.8	43.0
Sudan	..	83.2	Rep. of Korea	34.6	49.8	Panama	18.7	26.5
Togo	42.7	72.5	Saudi Arabia	38.2	27.1	Paraguay	57.4	80.8
Tunisia	16.8	13.8	Singapore	49.2	58.8	Peru	31.4	32.7
United Rep. of Tanzania	..	31.0	Sri Lanka	25.7	20.7	Trinidad and Tobago	34.2	37.5
Zambia	..	16.0	Syrian Arab Rep.	24.6	30.1	Uruguay	53.4	60.7
Zimbabwe	23.7	36.2	Taiwan Prov. of China	34.1	50.2	Venezuela	22.0	29.7
			Thailand	31.6	43.5			
			Viet Nam	..	40.6			
Memo item:								
Unweighted group averages	26.4	39.2		33.6	38.4		29.1	41.3

Source: See table 4.1.

Note: Includes all developing countries for which data are available.

(72 per cent), or Central America and the Caribbean, such as Antigua and Barbuda (53 per cent), Barbados (50 per cent), Honduras (38 per cent), and Montserrat (53 per cent). This is similar to the countries listed by Andriamananjara, Arce and Ferrantino (2004: table 3) as small transshipment countries for which re-exports account for a large share of their gross exports. The emergence of a worldwide hub-and-spoke system of shipping routes that is discussed in some detail in box 4.1, and that has proved to be an efficient way of servicing smaller countries and of providing many more port-to-port connections than direct services, is probably the main reason for this high share for many of these countries. The use of *entrepôt* trade to facilitate tariff evasion may explain some of it for the other countries in the list.

However, given that, as discussed above, the absolute level of trade in Asian developing countries is on average much higher than in Africa and Latin America and the Caribbean, this has not altered the predominance of Asian countries in South-South trade. Indeed, the strong role of trade among East Asian economies in the rise of South-South trade also partly explains the observed inverse correlation between the number of regional trade arrangements (RTAs) and intraregional trade shares.

Asia has only one major RTA while Latin America and the Caribbean as well as Africa have a large number of RTAs (WTO, 2003: 26–28). Regional economic and trade cooperation, including through bilateral and regional trade agreements, has been a major mechanism employed by an increasing number of developing countries to expand mutual trade and investment. Regional arrangements offer participating countries significant opportunities to enlarge economic space and pool economic, human, technological and infrastructural resources. Where complementarities exist, regional cooperation enables the participants to expand trade in specific sectors. However, intraregional trade within existing RTAs has suffered from continuing trade barriers, infrastructural problems in transport and information technology, and, often, few complementarities because of similar resource endowments. Recently, developing

countries have reinvigorated their regional liberalization programmes and entered into initiatives aimed at deeper integration. These changes, if implemented, may further boost intra-group trade (UNCTAD, 2005d).

Relatively weak trade performance within RTAs such as MERCOSUR in Latin America, has also been due to the volatility in the economic performance of its member States more generally. For example, the sizeable fluctuations in real income growth rates and in the real exchange rates of Argentina and Brazil during much of the period since the early-1990s have prevented industry in these countries from taking a long-term view. They have also impaired the investment in production capacity needed for restructuring industry and improving productivity and competitiveness following the economic crisis in the 1980s. In particular, during the second half of the 1990s, considerable fluctuations of the exchange rate

between the Argentinean and Brazilian currencies hampered trade within MERCOSUR. Nevertheless, the expansion of the automobile industry in Argentina and Brazil, based on increased specialization and production complementarity, which was one of the objectives of MERCOSUR, has contributed significantly to the growth of South-South trade in

automotive products (*TDR 2002*). Moreover, the acceleration of economic growth in MERCOSUR in 2004 and 2005 has been accompanied by a rise in intra regional trade in Latin America. For example, according to Argentina's National Statistics and Census Institute (Instituto Nacional de Estadística y Censos),⁶ the dollar value of Argentina's imports from MERCOSUR of the first five months of 2005 exceeded that of the same period in 2004 (2003) by 44 (149) per cent, the respective numbers for Argentina's exports to MERCOSUR being 9 per cent and 27 per cent.

Over the past few years, interregional trade between developing countries has lacked the dynamism it had in the 1970s, and it has also been less dynamic than intraregional trade. However, the earlier performance was mainly a reflection of the sharp increase in the value of oil shipments from

The rise of South-South trade in primary commodities, though modest, is more widespread, and probably more resilient.

Box 4.1**TOWARDS A NEW STRUCTURE OF GLOBAL MARITIME TRADE**

The rapidly growing importance of East Asian economies in international trade has been closely associated with the emergence of a new structure of global maritime trade. While there is a continuation of traditional maritime shipping patterns, based on shipments of manufactures among developed countries, and from developed to developing countries in exchange for primary commodities, the greater participation in world trade of the NIEs and China has been accompanied by the emergence of a triangular shipping pattern: these countries import much of their raw materials in the form of bulk cargo from other developing countries and export much of their manufactured goods in the form of containerized cargo to developed countries.

The development of global shipping networks, the move towards containerization in maritime transport, as well as port and customs reforms and increased investment in transport infrastructure by developing countries, have occurred at the same time as greater developing-country trade. In particular since the early 1990s, the global exchange of goods has benefited from the establishment of global liner shipping networks that connect regional, North-South and East-West shipping routes via transshipment ports. Thus regular, albeit indirect, maritime transport connections have enabled even countries that are not directly connected through liner shipping services to trade with each other. Moreover, the greater time efficiency of port, customs and shipping services, including through investment in information and communication technologies, has facilitated developing countries' participation in global production networks and the associated requirement to comply with "just in time" delivery. Hummels (2001), for example, estimates that each additional day spent in transport reduces the probability that the United States will source from a particular country by 1–1.5 per cent, and that each day saved in shipping time is worth 0.8 per cent of the traded manufactured good's value. He also estimates that the advent of fast transport (through air shipping and faster ocean vessels) was equivalent to a reduction in tariffs on manufactured goods from 32 per cent to 9 per cent between 1950 and 1998.

The mode of maritime transport differs between manufactures and primary commodities. Most inter-continental trade of manufactured goods and components is containerized and transported by regular, so-called "liner shipping" services. Access to such services is therefore a crucial aspect of competitiveness in the international trade of such goods. The highest liner shipping connectivity has been measured for Hong Kong (China), followed by Singapore, China, the United States and the Netherlands. The main determinant of a country's liner shipping connectivity is the volume of its containerized trade – greater volume attracts better liner shipping services. At the same time, ports that are located in favourable geographic locations (i.e. at the crossroads of shipping routes), and that provide fast and reliable transshipment services to shipping lines, tend to attract far more shipping services than they would on the basis of "national" trade alone. The main examples of such transshipment centres include Hong Kong (China), Panama and Singapore. This has contributed to the fact that, today, 20 of the 30 busiest container ports are located in Asia and Asian companies account for 46 per cent of global container ship operations. Moreover, between 2003 and 2004, operations in the two top Chinese container ports of Shanghai and Shenzhen grew by 28 per cent. It is estimated that in 2005, China will account for about one fourth of the world's containerized exports (measured in container units); the next biggest Asian exporters will be Japan (5.8 per cent of world containerized exports), the Republic of Korea (4.1 per cent), Taiwan Province of China (3.9 per cent), Indonesia (3.3 per cent) and Thailand (2.6 per cent).

By contrast, primary commodities are shipped in the form of bulk cargo, which requires large carriers that tend to be chartered for complete shiploads. Since East Asian countries, particularly China, have become the world's leading importers of many primary commodities, they account for a large share of bulk cargo; for example, in 2003 their share was 57 per cent of world trade in the three major dry bulk cargo commodities: iron ore, coal and grains. Over the past decade, Chinese seaborne trade in bulk cargo has grown by 17 per cent annually, compared to a growth rate of just 5.4 per cent for Japan, 2.3 per cent for Europe and negative growth for the United States.

Box 4.1 (concluded)

Although maritime transport of containerized trade and bulk cargo involves two separate markets, both of them saw record price levels in 2004 and 2005. The cost of chartering a medium-sized container ship was \$40,000 per day at the beginning of 2005, compared to around \$7,500 three years earlier. The index of chartering a dry bulk vessel was 2.6 times higher than the previous historical high of 1995. Between January 2003 and January 2005, prices for oil tankers doubled, and those for dry bulk vessels and container ships even increased by two and a half times.

One reason for the price increase in containerized maritime transport is the fact that China sources much of its manufactured imports from its trading partners in the region, while its manufactured exports are shipped mainly to North America and Europe. This has contributed to a strong imbalance of demand for containers and container ships, with a shortage of space for containerized cargo exports in Asia and a surplus in North America and Europe. As a result, container freight rates are two to three times higher for exports from China to North America or Europe than for trade in the opposite direction.

Another reason for the recent surge in the cost of maritime transport is the fact that the supply of ocean vessel capacity is very price-inelastic in the short term. This is because of the relatively long time lag between a rise in freight prices and the ordering of new vessels on the one hand, and new vessel construction and delivery on the other. Two to three years ago, owing to expectations of low growth in trade volumes, there were very few orders for new ships, which led to insufficient new vessel deliveries in 2003 and 2004. Today, shipyards are working at full capacity to deliver in 2007 or 2008; thus ample new vessel capacity is scheduled to enter the market in the coming years. For example, the combined container carrying capacity of new vessels expected to enter the market in 2006 will exceed the deliveries of 2003 and 2004 taken together. In January 2005, the order book of new container vessels registered 4 million container units, equivalent to 55 per cent of existing capacity (up from just 20 per cent in January 2002). This represents a historical record, more than double the previous record of mid-2001. About 80 per cent of container ships are being built in China, Japan and the Republic of Korea, with the latter country alone accounting for two thirds of global container-ship-building capacity.

Given the scheduled entry of new vessel capacity into the market, the present record freight and charter levels will likely decline to more normal levels in the foreseeable future. In the meantime, however, some developing countries are beginning to suffer from the adverse effects of high transport costs and scarce vessel capacity. Some African, Latin American and South Asian shippers have complained about export cargo not being carried on time, and, globally, the high transport costs have led to a measurable increase in freight payments by developing countries. In Latin America, for example, between the first six months of 2003 and the same period of 2004, the ratio of the cost of shipping to the total value of exports increased by 39 per cent.

Indeed, the mutual reinforcement of traded volumes and the availability of transport services has prevented many developing countries from benefiting from the tighter network of global shipping lines, in addition to contending with the current shortage of vessel capacity and high freight costs. For example, the average number of liner services to least developed countries (LDCs) is only one seventh of the average number provided to other countries, and more than half of the world's least connected non-landlocked countries are LDCs. The challenge for policy-makers in many of these countries is to initiate a virtuous cycle between improved connectivity to international maritime transport services and greater trade volumes.

Note: The data in the box are based on UNCTAD, *Review of Maritime Transport*, Geneva, various issues; UNCTAD, *Transport Newsletter*, Geneva, various issues; Clarkson Research Studies, *Container Intelligence Monthly*, London, various issues; ECLAC, *The costs of international transport and the integration and competitiveness of Latin America and the Caribbean*, Bulletin FAL 191, Santiago, 2002.

West Asia; and when oil prices declined during the 1980s, interregional trade tapered off. More recently, interregional South-South trade has shown signs of a recovery. As in the 1970s, this recent growth is due mainly to primary exports. But this time, Africa and Latin America and the Caribbean have benefited most from its rise. Growth in Africa's primary commodity exports to other developing country regions, of almost 20 per cent per annum between 1990 and 2003, has helped increase the share of Africa's primary exports in total South-South primary exports to levels not seen since the mid-1980s. A similar evolution can be observed for Latin America and the Caribbean where primary commodity exports to other developing regions grew by over 10 per cent between 1990 and 2000, and by almost 20 per cent between 2000 and 2003 (table 4.4).

To sum up, the most rapid growth of South-South trade has been among a small number of economies, mainly in East Asia, and primarily in manufactures. However, a substantial part of this increase in South-South trade in manufactures shown in trade statistics is actually due to double-counting associated with intraregional production-sharing for products eventually destined for export to developed countries as well as to double-counting associated with the function of Hong Kong (China) and Singapore as transshipment ports or regional hub ports. The rise in South-South trade of primary commodities, which in trade statistics is apparently much more modest, has been more widespread and has allowed Africa and Latin America and the Caribbean to recoup some of the market shares in total South-South trade that they had lost in the 1980s.

C. Shifts in the composition of developing-country exports

As noted above, one reason for the promotion of South-South trade has been the expectation that manufactures in general, and manufactures with a relatively high-skill content in particular, will be more important in South-South trade than in developing-country exports to developed countries. This expectation is based on the assumption that developing-country consumers are mainly interested in cheaper manufactured consumer goods, and are less demanding than consumers in developed-country markets in terms of a wide range of differentiated consumer manufactures – often having the same basic characteristics – and the consistent high quality of such goods. Thus, tapping developing-country markets is expected to facilitate export diversification away from a nar-

row focus on primary commodities. It is generally agreed that the production and export of manufactures, particularly high-skill-intensive goods, have greater developmental effects owing to the higher potential for demand and productivity growth in such products.

To analyse the shifts in composition of developing-country exports, nine categories of products have been selected. The primary commodities are classified according to their natural-resource content (agricultural products; minerals, ores and metals; and mineral fuels, lubricants and related materials) and the manufactures according to the mix of different skill- and technology intensities (labour- and resource-intensive manu-

factures; and low-, medium- and high-skill- and technology-intensive manufactures⁷); parts and components of electrical and electronic goods, and electronics excluding parts and components constitute two separate categories.⁸ As discussed in some detail in *TDR 2002*, although the skill and technology intensity of a product does not necessarily indicate the productivity growth potential of the sector producing it, the relationship is close enough to focus the analysis on product categories based on their skill and technology intensity.

Over the past two decades, the shifts in the composition of South-South trade have strongly differed from those of developing-country exports to developed countries.⁹ In developing-country exports to developed countries, medium-skill manufactures (such as road motor vehicles) registered the most dynamic growth in terms of export value between 1976 and 2003, followed by electronics excluding parts and components; parts and components of electrical and electronic goods; and high-skill manufactures (fig. 4.3). Imported high-skill intermediate production inputs in the context of international production networks clearly have played a crucial role in shaping this pattern. Thus findings based on trade statistics that rely on gross exports cannot be taken at face value. Nonetheless, they broadly indicate that relatively higher skill- and technology-intensive manufactured product categories have also played some role in the growth of developing-country exports to developed countries.

By contrast, regarding shifts in the composition of South-South trade over the period 1976 to 2003, the value of labour- and resource-intensive manufactures (such as clothing) increased the most strongly, followed by parts and components for electrical and electronic goods, medium-skill manufactures and agricultural products (fig. 4.3). Hence, in the dynamism of South-South trade, primary commodities have played a more important role than in South-North trade, and the most dynamic manufactured product categories in South-South trade tend to be less skill- and technology-intensive than those in South-North trade. This implies that the pattern of export dynamism by broad product

categories has not met the expectations for South-South trade.¹⁰

Examining the dynamism of South-South trade at a more disaggregated level shows that all four product groups within the category “parts and components of electrical and electronic goods” ranked among the seven most dynamic products in South-South trade during the period 1990–2003; combined, they accounted for about one fourth of total South-South trade in 2003 (table 4.7). But the table also shows that several goods in all product categories have experienced rapid growth in such trade. For example, 10 primary commodities (fur skins, briquettes, vegetable oils, ores and concentrates of precious metals, synthetic rubber, nickel, coal, residual petroleum products, aluminium, and pulp and waste paper) were among the 30 most dynamic products in South-South trade during the period 1990–2003, even though their growth began from a low base. This,

again, demonstrates the dynamism of primary commodities in South-South trade.

A second major difference in the compositional shifts in South-South trade compared to South-North trade is that the sensitivity of the results to changes in the base year in South-North trade is much lower. Changing the base year for the calculation of export dynamism (from 1976 to 1985, 1990, 1995 or 2000) affects the ranking of these four product categories in South-North trade only for the period 2000 to 2003; parts and components for electrical and electronic goods rank last of all nine categories. Indeed, shifts in the share of the nine product categories in total developing-country exports to developed countries show a clear trend away from primary commodities towards medium-skill manufactures and electronics, as shown in the top panel of table 4.8.

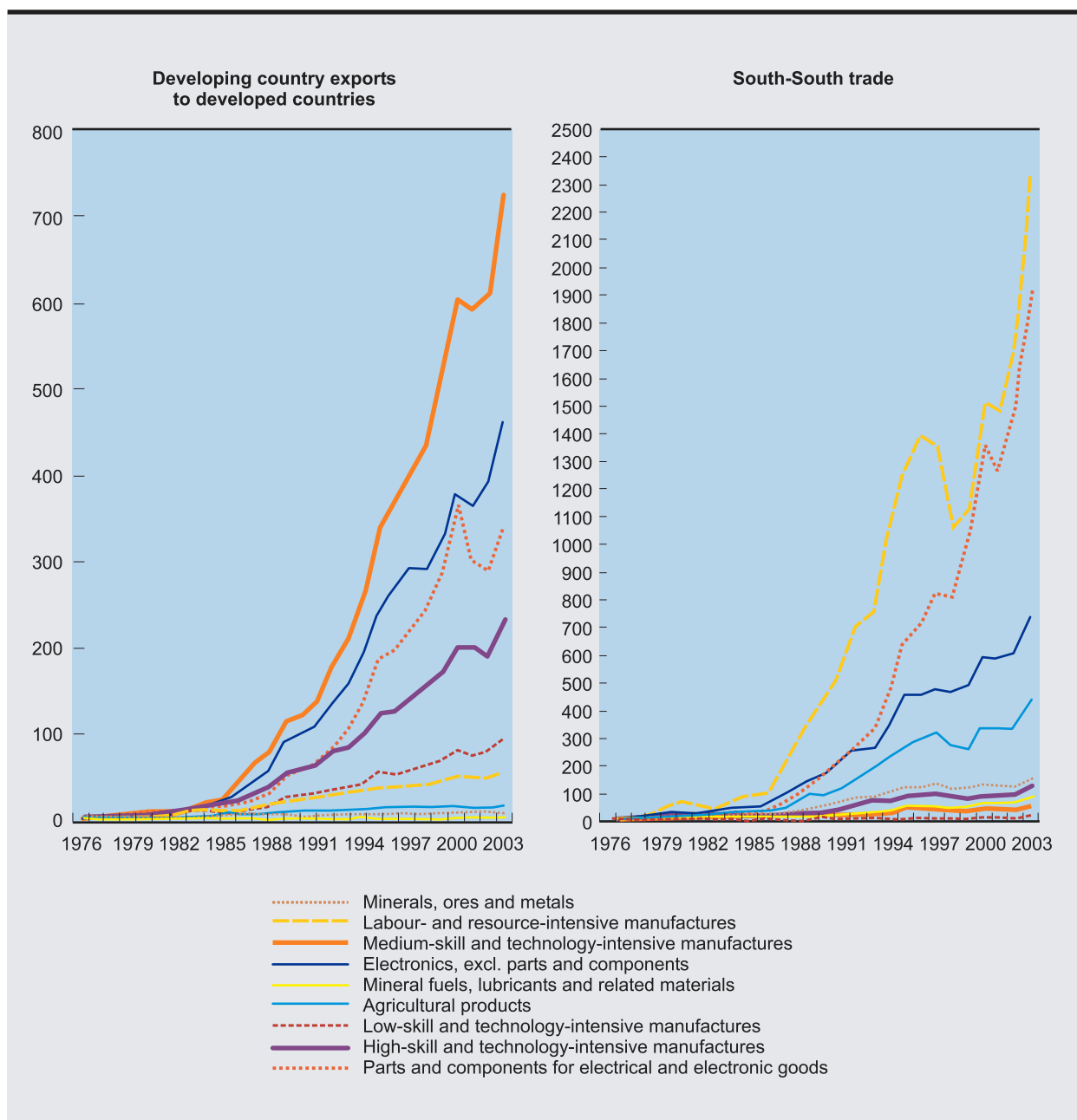
The ranking of broad product categories by dynamic export growth in South-South trade varies significantly with changes in the base year. Growth in terms of export values of labour- and resource-intensive manufactures in South-South trade had already taken off in the late 1970s, but was particularly dynamic between the mid-1980s

Primary commodities have played a more important role in the dynamism of South-South trade than in South-North trade.

Figure 4.3

EVOLUTION OF DEVELOPING-COUNTRY EXPORTS, BY BROAD PRODUCT CATEGORY, 1976–2003

(Index numbers, 1976 = 1)



Source: See table 4.1.

and mid-1990s and between 2000 and 2003. The first of these three periods broadly coincides with the beginning of production-sharing in the textile and clothing industry between the NIEs and the ASEAN-4 (Indonesia, Malaysia, the Philippines

and Thailand). The second period broadly coincides with China's participation in production-sharing in this sector. The third period probably reflects an intensification of China's involvement following its accession to the WTO and quota

Table 4.7

SITC code Product group		EXPORT VALUE GROWTH AND SHARE IN TOTAL SOUTH-SOUTH EXPORTS OF THE 30 MOST DYNAMIC PRODUCTS, ^a 1990–2003				
		(Per cent)				
		Average annual value growth of South-South exports	Share in total South-South exports		Memo item: Share in total exports from developing countries	
		1990–2003	1990	2003	1990	2003
871	Optical instruments and apparatus	32.4	0.1	1.0	0.1	0.6
759	Parts of computers and office machines	22.1	1.6	5.3	1.6	4.3
681	Silver and platinum	22.0	0.0	0.1	0.1	0.3
752	Computers and office machines	21.5	0.9	3.6	2.6	5.7
776	Transistors and semiconductors	21.3	3.8	12.5	3.5	8.0
212	Fur-skins, raw	19.1	0.0	0.1	0.0	0.0
772	Electrical apparatus such as switches	17.4	0.9	2.0	0.7	1.8
884	Optical goods nes	17.3	0.1	0.3	0.2	0.3
714	Non-electric engines and motors	17.2	0.0	0.1	0.1	0.1
718	Other power-generating machinery	16.8	0.0	0.0	0.0	0.0
323	Briquettes; coke and semi-coke; etc	16.7	0.0	0.1	0.0	0.1
511	Hydrocarbons, nes, and derivatives	16.4	0.4	0.7	0.3	0.4
222	Seeds and oleaginous fruit	15.9	0.3	0.5	0.5	0.4
764	Telecommunications equipment, and parts	15.8	2.7	5.6	2.3	5.2
873	Meters and counters, nes	15.8	0.0	0.0	0.0	0.0
289	Ores and concentrates of precious metals	15.7	0.0	0.0	0.1	0.1
513	Carboxylic acids, and their derivatives	15.5	0.3	0.6	0.2	0.4
582	Condensation products	15.2	0.5	0.9	0.3	0.6
778	Electrical machinery and apparatus, nes	15.0	1.1	2.1	0.8	1.9
771	Electric power machinery, and parts thereof	14.6	0.5	0.9	0.5	0.8
233	Synthetic rubber, latex, etc	14.4	0.1	0.1	0.1	0.1
874	Measuring instruments	14.4	0.3	0.5	0.3	0.6
683	Nickel	14.2	0.0	0.0	0.0	0.0
872	Medical instruments and appliances, nes	14.1	0.1	0.1	0.1	0.3
322	Coal, lignite and peat	13.9	0.2	0.4	0.2	0.4
335	Residual petroleum products	13.7	0.2	0.2	0.2	0.2
716	Rotating electric plants and parts thereof, nes	13.3	0.4	0.7	0.3	0.6
684	Aluminium	13.2	0.5	0.7	0.7	0.6
251	Pulp and waste paper	13.0	0.2	0.2	0.2	0.2
781	Passenger motor vehicles (excluding buses)	13.0	0.4	1.0	1.0	2.1
	Total for 30 most dynamic products	18.3	15.8	40.5	16.9	36.1
	Parts and components of electronics ^b	19.7	9.0	25.4	8.0	19.2
	Memo items:					
	Total merchandise exports	9.8	100.0	100.0	100.0	100.0
	Manufactures	10.5	72.8	81.7	70.7	82.1
	Fuels, minerals and metals	9.1	11.2	8.6	12.1	8.3
	Agricultural products	6.1	16.1	9.6	17.2	9.6
	Total world exports	6.1	-	-	-	-
	Total developing-country exports	9.2	-	-	-	-

Source: See table 4.1.

a Includes SITC 0 through 8, except product groups 286, 351, 675, 688 and 333 because of poor data reporting for these categories.

b Includes SITC 759, 764, 772 and 776.

Table 4.8

**COMPOSITION OF DEVELOPING-ECONOMY EXPORTS TO DEVELOPED COUNTRIES,
BY BROAD PRODUCT CATEGORIES, 1980–2003**

<i>Exporting economies</i>	Shares (Per cent)				Value change up to 2003 (Index numbers)	
	1980	1990	2000	2003	1976 = 1	1990 = 1
<i>All developing economies</i>						
Agricultural products	13.2	15.1	8.9	9.2	18.9	1.7
Minerals, ores and metals	4.7	4.6	2.7	2.5	10.6	1.5
Mineral fuels, lubricants and related materials	65.0	23.7	14.2	12.2	4.4	1.4
Labour- and resource-intensive manufactures	9.4	24.6	20.3	20.7	56.9	2.4
Low-skill and technology-intensive manufactures	1.6	5.1	5.3	5.6	96.0	3.1
Medium-skill and technology-intensive manufactures	1.0	7.4	14.1	15.6	724.8	5.9
High-skill and technology-intensive manufactures	1.7	5.0	6.3	6.9	235.8	3.9
Electronics excluding parts and components	1.4	7.7	11.2	12.9	470.6	4.7
Parts and components of electrical and electronic goods	1.9	6.8	17.0	14.4	339.3	5.9
Total merchandise exports	100.0	100.0	100.0	100.0	25.7	2.8
<i>Developing economies, excl. NIEs</i>						
Agricultural products	13.8	20.9	11.7	11.5	20.1	1.8
Minerals, ores and metals	5.2	7.0	3.7	3.2	10.3	1.5
Mineral fuels, lubricants and related materials	75.2	36.3	19.1	15.5	4.2	1.4
Labour- and resource-intensive manufactures	3.8	19.1	21.4	22.0	274.2	3.8
Low-skill and technology-intensive manufactures	0.3	2.9	4.3	5.0	218.3	5.7
Medium-skill and technology-intensive manufactures	0.3	5.3	14.0	14.9	4 200.9	9.5
High-skill and technology-intensive manufactures	0.6	4.1	5.8	5.8	611.1	4.8
Electronics excluding parts and components	0.1	1.7	8.3	11.7	29 632.9	23.4
Parts and components of electrical and electronic goods	0.7	2.8	11.6	10.3	4 388.3	12.4
Total merchandise exports	100.0	100.0	100.0	100.0	22.0	3.4
<i>Developing economies, excl. NIEs and China</i>						
Agricultural products	..	20.9	12.8	14.0	17.6	1.8
Minerals, ores and metals	..	7.3	4.2	4.0	9.2	1.4
Mineral fuels, lubricants and related materials	..	38.1	22.9	20.9	4.0	1.4
Labour- and resource-intensive manufactures	..	17.3	18.1	19.1	171.8	2.9
Low-skill and technology-intensive manufactures	..	2.6	3.4	3.7	117.4	3.7
Medium-skill and technology-intensive manufactures	..	5.3	14.3	15.8	3 193.8	7.8
High-skill and technology-intensive manufactures	..	3.7	5.3	5.5	413.2	3.9
Electronics excluding parts and components	..	1.7	7.1	7.6	13 943.7	11.7
Parts and components of electrical and electronic goods	..	3.0	12.1	9.5	2 902.6	8.3
Total merchandise exports	..	100.0	100.0	100.0	15.5	2.6

Source: See table 4.1.

Note: Data for 1980 in the third panel of the table are not provided, as data for China for that year are not available.

elimination associated with the implementation of the second stage of the Agreement on Textiles and Clothing (ATC) at the beginning of 2002. By contrast, production-sharing in the electronics sector, mainly among the East Asian economies, broadly began in the mid-1980s. As a result, parts and components of electrical and electronic goods have been the most dynamic product category in South-South trade in terms of export value growth for the period 1985–2003. Hence, changes in the pace of export dynamism of labour- and resource-intensive manufactures and of parts and components of electrical and electronic goods broadly coincide with different waves of production-sharing among developing countries in these sectors. Taken together, these results further support the above finding, that the statistical effects associated with production-sharing have been a key determinant of the growth of South-South trade in manufactures as reflected in trade statistics.

However, the fact that in most products, rapid growth of South-South trade started from a relatively small base in the late 1970s has also played a role in both the rapid rate of growth in export values and the variety of broad product categories that have driven growth in South-South trade over the past three decades. For example, in 1976 the value of developing-country exports of labour- and resource-intensive manufactures to developed countries was about 200 times higher than the value of their exports of such products to other developing countries, and that of agricultural products was about 20 times higher, while the same magnitudes were 4 and 2 for parts and components of electrical and electronic goods, and electronics excluding parts and components, respectively.

A characteristic common to the evolution of both South-South and South-North trade is that a few Asian developing economies have a strong in-

fluence on shifts in the broad export patterns of developing countries taken together. If the exports from the NIEs – whose production and export patterns have become very similar to those of developed countries, as mentioned above – are excluded

from South-North trade, the most dynamic product categories are electronics (both finished products and parts and components), as shown in the second panel of table 4.8. If China is excluded as well (third panel of table 4.8), the dynamism of finished electronics drops by more than half, even though it remains the most dynamic product category. This,

of course, reflects the statistical effects of triangular trade. Taken together, it indicates that much of the expansion of relatively skill- and technology-intensive manufactured exports from developing to developed countries is closely linked to successful economic growth and industrialization in East Asia.

Table 4.9 shows that in the segment of South-South exports which excludes the NIEs and the ASEAN-4, the two electronics categories recorded the most dynamic growth. However, irrespective of whether this growth performance is measured over the period 1976–2003 or 1990–2003, it occurred from a very low base, so that the share of these two categories remains low.

Turning to interregional trade, the growth in the value of developing country exports to Asia stands out for two reasons (third panel of table 4.9). First, it expanded by more than 155 times between 1976 and 2003, signifying that the dynamism of this segment of South-South trade has been

more than double the already impressive expansion of South-South trade overall. Second, for the period 1990–2003, primary commodities have been of crucial importance in this expansion, as their various categories rank much higher here than in the other segments of South-South trade shown in the table.

The most dynamic manufactures in South-South trade tend to be less skill- and technology-intensive than those in South-North trade ...

... but industrialization in East Asia accounts for much of the expansion of skill- and technology-intensive exports from developing to developed countries.

Table 4.9

**COMPOSITION OF TRADE AMONG DEVELOPING ECONOMIES,
BY BROAD PRODUCT CATEGORIES, 1980–2003**

	Shares (Per cent)				Value change up to 2003 (Index numbers)	
	1980	1990	2000	2003	1976 = 1	1990 = 1
<i>Exporting economies</i>						
Importing economies: all developing economies						
<i>All developing economies</i>						
Agricultural products	5.6	11.6	12.6	13.0	445.8	4.5
Minerals, ores and metals	10.0	22.5	16.8	15.2	153.2	2.7
Mineral fuels, lubricants and related materials	2.6	3.3	3.3	3.3	87.9	4.0
Labour- and resource-intensive manufactures	1.8	4.2	4.6	5.6	2 360.3	5.3
Low-skill and technology-intensive manufactures	47.3	16.6	13.2	9.6	8.8	2.3
Medium-skill and technology-intensive manufactures	19.3	15.1	9.5	9.5	55.2	2.5
High-skill and technology-intensive manufactures	5.2	7.1	5.9	6.6	129.8	3.7
Electronics excluding parts and components	5.4	10.9	11.6	12.1	775.0	4.4
Parts and components of electrical and electronic goods	2.7	8.5	22.5	25.0	1 921.5	11.7
Total merchandise exports	100.0	100.0	100.0	100.0	67.4	4.0
<i>Developing economies, excl. NIEs and ASEAN-4</i>						
Agricultural products	12.4	18.6	15.4	14.5	112.8	2.9
Minerals, ores and metals	2.4	4.7	5.0	5.2	59.9	4.1
Mineral fuels, lubricants and related materials	71.9	24.7	22.9	14.9	5.6	2.2
Labour- and resource-intensive manufactures	4.6	19.8	19.1	20.3	678.0	3.8
Low-skill and technology-intensive manufactures	1.9	7.7	6.8	7.9	692.1	3.8
Medium-skill and technology-intensive manufactures	3.5	10.5	11.0	11.6	572.6	4.1
High-skill and technology-intensive manufactures	2.8	10.1	10.3	9.9	555.5	3.6
Electronics excluding parts and components	0.3	2.7	2.9	5.7	6 860.7	7.7
Parts and components of electrical and electronic goods	0.1	1.1	6.6	10.0	5 263.8	32.7
Total merchandise exports	100.0	100.0	100.0	100.0	34.9	3.7
Importing economies: Asia						
<i>Developing economies, excl. Asia</i>						
Agricultural products	48.6	31.6	31.2	35.3	174.9	4.6
Minerals, ores and metals	15.5	15.0	15.8	15.7	44.1	4.3
Mineral fuels, lubricants and related materials	11.4	12.0	30.4	22.7	535.1	7.7
Labour- and resource-intensive manufactures	3.5	4.9	4.7	4.4	294.3	3.7
Low-skill and technology-intensive manufactures	3.6	20.1	6.0	9.6	2 259.5	2.0
Medium-skill and technology-intensive manufactures	0.7	3.7	3.0	4.2	1 134.5	4.6
High-skill and technology-intensive manufactures	16.1	11.9	6.3	5.5	259.4	1.9
Electronics excluding parts and components	0.5	0.4	0.2	0.1	8 471.0	1.3
Parts and components of electrical and electronic goods	0.1	0.3	2.5	2.5	36 396.0	33.0
Total merchandise exports	100.0	100.0	100.0	100.0	155.9	4.1

Source: See table 4.1.

D. What has changed? An assessment

While increased South-South trade is a fact, recent developments for the developing countries as a whole require a careful assessment of the statistical data. Indeed, such an assessment leads to a number of qualifications to the *prima facie* impression that trade among developing countries has grown massively over the past decade or so, and that exports of manufactures account for much of this rise.

The trend towards a “new geography of trade” appears to be the result, above all, of the above-average growth performance of a few Asian developing economies, and the associated shifts in the level and composition of their external trade. The fact that most developing countries outside East Asia do not appear to have participated significantly in the emerging “new geography of trade” suggests that interpretations of this trend need to be treated with caution in order to avoid unrealistic expectations of its ultimate scope and impact.

The outstanding growth performance of the NIEs and China has had a significant impact on international trade flows because it has further increased the already sizeable weight of these economies, which account for about 16 per cent of world income (in terms of purchasing power parity) and 22 per cent of the world population. Perhaps most importantly, the production structures of some of the NIEs, namely the Republic of Korea and Taiwan Province of China, have become increasingly similar to those of the major developed countries in terms of both production and export of manufactures (*TDR 2003*). As a re-

sult, the rise in South-South trade has occurred in a hierarchical way. On the one hand, the Republic of Korea and Taiwan Province of China trade skill-intensive manufactures directly with developed countries. On the other hand, both domestic firms and affiliates of foreign TNCs located in these economies (and, to a lesser extent, in South-East Asian countries such as Malaysia) take advantage of increased intraregional cooperation and specialization among the East Asian economies. For example, the Republic of Korea and Malaysia export intermediate production inputs to China where these inputs are assembled for export to developed countries (i.e. in a triangular trade pattern). The rising specialization of all these Asian economies in manufacturing activities is, in turn, associated with their growing import demand for products with a high natural-resource content, such as energy and industrial raw materials, required for industrialization. Many of these products are sourced from other developing countries.

The important role of triangular trade in the measured rise of South-South trade in manufactures implies that the bulk of such trade has not reduced the dependence of developing countries’ manufactured exports on aggregate demand in developed-country markets. As long as demand from developed countries – notably the United States, which is East Asia’s most important export market – remains high for products for which production-sharing within East Asia plays an important role, triangular trade and, thus, South-South trade, will remain strong. But this also implies that a drastic reduction in United States imports of such products may lead to a major decline

in South-South trade of manufactures. A similar outcome may result from an adjustment of the current trade imbalances between the United States and East Asian economies which would be associated with at least a partial offsetting of the gains in competitiveness of East Asian exporters in recent years.

For South-South trade in manufactures, other than that related to triangular trade, developing countries' pace of economic growth and the soundness of their liquidity situation are of key importance. In particular, instead of rapid capital accumulation and technical progress, Latin America has recorded low investment performance in industry over the past two decades, which has caused productivity growth to be cyclical and related to labour shedding (*TDR 2003*). Thus industrial upgrading has been limited, and progress in certain industries, such as aerospace and automobiles, has not been deep enough to establish a dynamic momentum in industry. The macroeconomic environment of high interest and exchange rates and volatile capital flows has done little to support the new investment required for sustained industrial upgrading. Moreover, the tendency towards sharp real currency appreciations, particularly during the early 1980s and the 1990s, has been a major factor in the deterioration of the international competitiveness of these countries' manufacturers, including their competitiveness vis-à-vis East Asia. However, the recent improved growth performance of a range of Latin American countries probably improves the scope for intra regional trade in manufactures, as well as for their trade with other developing regions.

The growth of South-South trade has not reduced the strong reliance of the vast majority of developing countries on primary commodity exports. However, the rise in their exports of primary commodities to the rapidly growing Asian developing countries is likely to evolve into the most resilient feature of the "new geography of trade". Since two of the

While the increase in South-South trade is a fact, this trend requires a careful assessment to avoid unrealistic expectations.

The promotion of South-South trade remains a desirable objective for a variety of reasons.

most rapidly growing Asian developing countries – China and India – still are in the early phases of industrialization, they will continue to source their imports of primary products from the group of natural-resource-abundant countries. Thus there is significant potential for cooperation between China and India, on the one hand, and other developing countries, on the other, for strategic resources such as energy products and minerals (e.g. iron ore and copper). Indeed, Chinese and Indian FDI in such resources has gained in importance over the past few years and evolved as a complement to trade-related South-South cooperation.

The promotion of South-South trade remains a desirable objective for a variety of reasons. Firstly, sluggish growth in developed countries and their continued trade barriers against products of export interest to developing countries implies that developing countries need to give greater attention to each other's markets to fill the gap in export growth consistent with achieving their economic growth targets. This concerns both primary commodities and manufactures. In the case of primary commodities, structural change away from raw-material-intensive industrial production continues to reduce the intensity of raw material use in the major developed countries; for manufactures, the case for greater skill intensity in manufactures traded among developing countries remains intact. Secondly, the vast size of the rapidly growing Asian economies reduces the need for developing countries to seek developed country markets in order to benefit from economies of scale. Thirdly, continued dependence on developed-country markets exposes developing countries to possible pressure that link better access to those markets with binding commitments to rapid trade and financial liberalization, protection of intellectual property and open-door policy for FDI. More generally, it also entails the risk of increasingly narrowing the policy space for developing countries.

To the extent that trade barriers present a major impediment to the growth of South-South trade, lowering tariffs and non-tariff barriers is a priority. This holds within RTAs among developing countries, as well as for stimulating inter-regional trade based on the Global System of Trade Preferences among Developing Countries (GSTP). However, attention needs to be given also to other trade barriers, including inadequate transport facilities and the absence of established business and banking linkages.

Indeed, the issue of finance remains of crucial importance to the prospects for South-South trade growth. For example, the absence of efficient financing not only increases transaction costs for South-South trade, but may also act as an effective

barrier to trade if neither of the two Southern partners has access to adequate financing. Developed-country export credit agencies can provide credits and credit insurance for exports to most developing countries; but there are only a few such agencies in developing countries and those that do exist often are only able to cover exports to developed countries (UNCTAD, 2005e). Moreover, regional financial arrangements and cooperation frameworks can support the stabilization of the exchange rates of developing country currencies with respect to each other. In particular, mechanisms of intra-regional support against currency runs – such as the Chiang Mai Initiative (*TDR 2001*) – can bring considerable benefits to intraregional trade, as they reduce exchange rate spreads and commissions in currency trading associated with regional trade.

E. Policies for managing the new forms of global interdependence

A new form of global economic interdependence is taking shape, primarily as a result of the increasing weight of the rapidly growing Asian developing economies, in particular the large ones of China and India, in the global economy.

The first-tier NIEs and China are already playing a crucial role in global trade flows, not only as suppliers of manufactures to the world market and importers of primary commodities from other developing countries, but also as importers of developed countries' manufactures. Moreover, through their large current-account surpluses and their accumulation of foreign exchange reserves, they have also become influential actors in international financial and monetary relations. India is set to join this group of East Asian economies as a major importer of primary

commodities; its export growth has so far been concentrated in services, but in the future this may also extend to manufactures of similar kinds as those produced in the East Asian economies when they were at the earlier stages of their industrialization process.

The analysis in this and the preceding chapters shows a complex and nuanced picture of the new features of global interdependence, which pose new challenges for policy-makers in different countries, depending on their stage of development and their position in the global economic landscape. The smooth integration of large and rapidly growing economies into global economic relationships has the potential to benefit all countries. However, this will depend to a considerable extent on how the new forms of interde-

pendence between these rapid industrializers, the advanced industrialized countries and other developing countries is managed. Coherent policies are required at both the international and national levels.

Despite their rapid growth over the past two and a half decades, both China and India still have relatively low levels of per capita income. However, due to their size – with a combined population representing two fifths of the world population and a combined GDP accounting for one fifth of the world total – their economic performance will inevitably have repercussions on international trade patterns and global output growth. Given their increasing dependence on imports of primary commodities for industrial output growth, in particular fuels and industrial raw materials, the growth performance of these large Asian economies will have greater repercussions on other developing countries as their catching up process advances. This inevitably raises the question of the sustainability of the pace of growth of these two economies in the medium and long term. Problems could arise from their heavy dependence on exports, insufficient domestic demand, and a sharply rising bill for imported raw materials, especially energy.

As discussed in chapter I, section E, China has already acquired a solid manufacturing base, and it has been able to maintain a broad balance between growth impulses from domestic demand and those from foreign demand. It should therefore be able to maintain GDP growth at a pace that will permit a considerable further rise in per capita income, and at the same time induce growth in other developing countries. In India, it is the services sector that has so far been leading economic growth, but it is unclear for how long this can be maintained. Historically, there has been no case of economic catch-up based on the development of the services sector (perhaps with the exception of a few small island economies that depend on tourism or financial offshore centres), where the scope for productivity gains is more limited than in manufacturing. The IT-revolution has

certainly changed the potential for the services sector to support rapid growth in developing countries, as has been the case in some developed countries. However, the size of the world market for IT-based services is smaller than that for manufactures, especially when the rising demand for manufactures from developing countries themselves, not least as a result of poverty reduction efforts, is taken into account. Thus there can be little doubt that India will substantially improve its growth prospects if it succeeds in accelerating the development of its manufacturing industry.

In both China and India it will be crucial to ensure that all segments of the population participate in income growth.

This is not only essential for accelerating the eradication of poverty and gaining broad-based social acceptance of the enormous structural changes required; wage increases throughout the economy, in line with rising productivity, are also key to the expansion of domestic consumption and, thus, to the sustainability and stability of output growth. Fixed capital formation depends on favourable demand expectations in general, and not just on exports, which are subject to the vagaries of the world market and to changes in international competitiveness. Among final demand, private consumption is the most important stabilizing factor of private investment.

Policy options for China and India may be identified by drawing on the successful experiences of earlier catching up episodes in Asia, taking account of both the difference in the current international environment relative to that prevailing during these earlier episodes, and the difference in the sizes of the Chinese and Indian economies relative to those of the first-tier NIEs. The effects of growth and changing trade patterns in China and India are having a much stronger impact on world markets, and thus on the terms of trade of the two countries themselves. In any case, a sustained growth process will require a rapid and well sequenced upgrading of manufacturing production and exports, and a greater emphasis on the domestic market for outlets of labour-intensive production activities as well as

China and India need to ensure further productivity gains in manufacturing, and the participation of all segments of their population in income growth.

for the supply of intermediate goods. In China, in particular, an increase in labour productivity in the rural areas and rising incomes in the agricultural sector would contribute to generating the demand needed to absorb greater domestic-oriented production; it would also help secure a higher degree of food self-sufficiency.

The availability of raw material imports, and their prices, will be another critical factor for the sustainability of the current pace of development in the rapidly growing Asian economies. Domestic policies in this regard will need to focus on the provision of incentives to raise the efficiency of raw material use, in particular of fuels. This is a challenge that all countries, developed and developing alike, are facing, and it also has important implications for global environmental sustainability. But the supply of primary commodities depends to a large extent on responses by producers to the rise in the volume of global commodity consumption and to the favourable price changes that have occurred recently.

Other developing countries should seek to adopt policy measures that will enable them to derive the most benefits from the rising import demand from the Asian industrializers, and to translate the eventual gains into stronger domestic investment in support of greater diversification and faster industrialization. Continuing growth in East and South Asia and recovery in other developing regions is likely to sustain the demand for primary commodities. However, depending on the pace of reduction in the intensity of use of raw materials, the extent and speed with which new supply capacities come on-stream, and the size of possible changes in primary commodity demand of the developed countries, the rise in primary commodity prices may come to a halt, or may even be reversed.

Thus the basic problems of instability in primary commodity prices and of their long-term deteriorating trend vis-à-vis the prices of manufactures – especially those exported by developed countries – cannot be considered as resolved. With

the boom in the fuels and mining sectors there is a tendency for investment to shift into these sectors, at a risk of neglecting further development and upgrading of the manufacturing sector, including the processing of locally available natural resources. Exporters of primary commodities that have recently benefited from higher prices and, in some cases, from higher export volumes, would be well advised to seek greater diversification, not only within their primary commodity sector, but also, and more importantly, by developing their manufacturing and services sectors. Gains from recent improvements in the terms of trade and higher export earnings should be translated into greater investment in infrastructure, education and productive capacity with a view to accelerating productivity growth and reducing commodity dependence. This is not the time for complacency, either at the national or at the international level, with regard to the commodity issue.

In many developing countries, the recent gains in the terms of trade have also led to renewed attention to the long-standing issue of the sharing of export revenues, and especially rents from the extraction of non-renewable fuels and minerals. Increasing global demand and higher international prices for fuels and mining products have been attracting additional FDI to these sectors in a number of developing countries. However, government revenues from taxes on profits in these sectors have typically been very low. Since the beginning of the 1990s, there has been increasing competition among developing countries to attract FDI by offering fiscal incentives. Some potential host countries have sometimes risked engaging in “a race to the bottom”. In order to ensure that the considerable rents accruing in the extractive industries are used in a way that maximizes the gains for development and social welfare, governments need to strike a balance between the use of fiscal incentives for stimulating investment, including FDI, and realizing public revenue from these industries.

Additional means of obtaining fiscal revenues from primary export-oriented activities may be

Oil and mineral exporting countries should cooperate in the formulation of agreed principles relating to the fiscal treatment of foreign investors.

through royalties, the conclusion of joint ventures, or full public ownership of the operating firms. However, efforts to obtain adequate fiscal revenue should not deprive the operators, private or public, of the financial resources they need to increase their productivity and supply capacity, or their international competitiveness. Recent upward trends in world market prices of fuels and minerals and mining products provide an opportunity to review the existing fiscal and ownership regimes. Such a review – already under way in several countries – and possible strategic policy adjustments, could be more effective if oil and mineral exporting countries were to cooperate in the formulation of some generally agreed principles relating to the fiscal treatment of foreign investors. But it is crucial to ensure that the higher income accruing to the public sector or to domestic consumers from the rent generated by extractive industries be used for purposes that enhance development and progress towards the MDGs. Measures to increase the domestic share of the rent from non-renewable natural resources should be taken in the context of a comprehensive strategy that ensures the use of the proceeds for physical and human capital formation.

Despite the fast pace of the catching up process in Asian economies, and their growing importance in world output and trade, the performance of most developing countries continues to depend on growth as well as on macroeconomic and trade policies of the major industrialized countries. The role of the fast growing Asia has added another dimension to these linkages: in addition to their direct trade relations with the developed countries, indirect relations, via exports to the Asian suppliers of manufactures to the North, are gaining in importance. Thus, the benefits that other developing countries will be able to reap from further industrialization in East and South Asia would be enhanced by further trade liberalization in the developed countries, including in the agricultural sector. Moreover, the attitude in these countries towards increasing competition from Asia in the markets for certain types of manufactures will

The international community should review mechanisms to reduce price instability of a wider range of commodities, not just oil, so as to minimize its adverse impact on national income.

have important repercussions not only for the Asian exporters of such products, but also for those developing countries that are exporters to the latter. Instead of giving in to protectionist pressures, developed countries should adopt proactive policies to accelerate structural adjustment towards high-technology-intensive sectors and a greater share of services in GDP. Obviously, such adjustments are much easier to achieve in a context of growth (as in the United States) than in a context of stagnation (as in much of Western Europe and Japan).

At the international level, the main challenge is to find a global approach to manage the integration of the rapidly growing, large, low-wage countries in Asia in a way that is beneficial for all countries. One aspect is to ensure that the boom in the markets for a number of primary commodities translates into real gains for development in those countries that depend on the exports of these commodities. The inherent volatility of commodity markets, combined with the economic dependence of many developing countries on a small number of primary commodities, continues to be a major obstacle to development.

Over the past few decades, most internationally traded commodities have experienced a long-term decline in prices as well as a high degree of short-term price volatility. Even though prices for a number of commodities have surged recently, productivity increases and low elasticity of demand are likely to support the downward trend of commodity prices in the long run. Overall price volatility also appears to have declined since the price shocks of the 1970s. Nonetheless, there are several commodities, important to developing countries' export earnings, for which price instability has remained very high. In addition, commodity export dependence and export concentration have not decreased significantly in most developing countries.

Wide fluctuations in commodity prices are not in the interests of either producers or consumers. This has also been recognized by the International

Monetary and Financial Committee of the International Monetary Fund (IMF): at its April 2005 meeting, it underscored, *inter alia*, “the importance of stability in oil markets for global prosperity” and encouraged “closer dialogue between oil exporters and importers”. Although instability in markets for commodities other than oil may be less of a problem for the developed countries, they are equally, if not more, important for those developing countries that depend on their exports. And since in many of these developing countries extreme poverty remains a pressing problem, the issue is of crucial importance for global prosperity, particularly for attaining the MDGs. Consequently, in the spirit of a global partnership for development, the international community might consider reviewing mechanisms at the global as well as the regional level to reduce commodity price instability, thereby mitigating its impact on national income in the exporting countries.

Commodity price risk management through market-based instruments can offer some protection against price uncertainty; yet it has clear limitations as far as developing countries are concerned. Therefore, producer countries and international commodity organizations might reconsider the practical and political feasibility of supply management systems (based on information networks), commodity-specific arrangements among producers, and international cooperation among producers and consumers. This could be accompanied by a system of low-conditionality finance to compensate for shortfalls in commodity export earnings, which responds to the needs of developing countries better than the instruments that have been available in the past (see also UNCTAD, 2003).

Another area for strengthened international cooperation and policy coherence is the search for an appropriate macroeconomic solution to the large current-account imbalances that have shaped the world economy in recent years. Such imbalances represent the greatest short-term risk for stable growth in the world economy and for the sustainability of the recent growth performance of the developing countries. These imbalances are closely linked not only to the growth differential

between the United States and other major industrialized countries, but also to the expansion of United States imports from the highly competitive suppliers in East and South Asia. Yet it would be a mistake to treat these imbalances as bilateral problems. Given their global dimension and the repercussions of any adjustment on the world economy as a whole, it appears that the safest way to redress the global imbalances lies in an adequate sharing of the adjustment burden between the deficit countries – especially the United States – and the surplus economies of Western Europe, Japan and the rapidly growing developing economies of East Asia, including China.

A solution sought exclusively through a further sharp depreciation of the dollar and lower absorption in the United States would imply a reduction of exports from the rest of the world, with attendant effects on primary commodity export earnings and fiercer competition in the markets for certain manufactures. This would risk pushing out of the market those developing-country producers whose productivity growth has been slower than that of the fast growing Asian economies.

Similarly, correcting global imbalances, or the external deficit of the United States, mainly through massive exchange rate appreciation and lower absorption in China and other developing economies in Asia would have a strong deflationary effect on the world economy as a whole. It would not only render more difficult China’s attempts to integrate a vast pool

of rural workers and, more generally, to reduce poverty in the country, it would also imply a setback to the efforts of other developing countries to make progress towards the MDGs. Most of the surplus countries in East Asia, and in particular China – on which

international pressure for revaluation has been the strongest, from both financial markets and policy-makers – have actively managed the floating of their currencies or have pegged them to the dollar. The sizeable revaluation of any single currency vis-à-vis the dollar could destabilize regional trade and financial relations, in particular, in light of China’s bilateral deficits with its trading partners

It would be a mistake to treat the global current-account imbalances as bilateral problems.

in Asia. It is essential to prevent greater exchange rate flexibility vis-à-vis the dollar from causing higher intraregional volatility. Therefore, if a revaluation of China's renminbi is deemed inevitable as a contribution to an internationally coordinated solution to the global imbalances, it should be sought in the context of a multilateral or regional arrangement.

The stronger the contribution of faster growth in the euro area and Japan, the less deflationary the correction of the global imbalances will be. Indeed, both the euro area and Japan have compelling reasons to stimulate domestic absorption with a view to solving their unemployment problems, especially since this entails a minimal risk of overheating or accelerating inflation. Such an action would also greatly help reduce their trade

surpluses, while at the same time supporting growth momentum in the world economy.

Thus a well coordinated international macro-economic approach would considerably enhance the chances of the poorer countries to consolidate the recent improvements in their growth performance. The Plaza Agreement of 1985, which was a joint political effort among the major industrialized countries, provides an example of how a correction in large current-account imbalances can be achieved at the global level. The world economy has changed in the past 20 years, and a new agreement of a similar kind would certainly need to involve the developing countries that have come to play a major role in the performance of the entire world economy and in its stability. ■

Notes

- 1 Table 4.1, as well as tables 4.3–4.9 and figure 4.3, are derived from data that countries report to the United Nations. The UN COMTRADE is the most comprehensive database available for the purposes of this chapter. However, given that some countries do not (or not comprehensively) report trade data, the tables are not an exhaustive listing of developing-country trade. This is the case mainly for the early periods shown in the tables, when non-reporting countries accounted for a very small share in world trade, and for recent years for some of the major fuel exporters in West Asia. The latter has led to an underrepresentation of developing-country exports of fuels for recent years. However, these data constraints do not affect the overall pattern of the findings discussed in this chapter.
- 2 The strong involvement of transnational corporations (TNCs) in international production networks, and the associated rise in intrafirm trade and transfer pricing, has increased the difficulties in correctly

accounting for international trade in manufactured goods. This is because the prices set by TNCs for intrafirm transfers (i.e. transfer prices) are often not the prices that would be negotiated between arm's-length parties. Rather, TNCs tend to set transfer prices in a way that minimizes tax and tariff payments, as discussed, for example, by Eden (2001).

- 3 UNCTAD secretariat calculations, based on UN COMTRADE database.
- 4 Sudan's exports to other developing countries have also been boosted by the surge in oil exports to China.
- 5 Taking averages only for those countries for which data for both periods are available slightly reduces the numbers for Africa and Latin America for the period 2000–2003.
- 6 Data available at www.indec.gov.ar.
- 7 In what follows, these latter categories are called low-, medium- and high-skill manufactures.
- 8 See *TDR 2002*, table 3.A1 for a complete list detailing which products are included in each category.

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- 9 The following analysis complements the examination in *TDR 2002*, chap. III of dynamism in world trade and dynamism in total developing-country exports. Its main findings were that (i) manufactures have been the sector in which values have grown the most rapidly both in world trade and in developing-country exports, and (ii) the higher the skill and technology content of exports, the faster is the growth of exports of developing countries compared to growth in world trade. This latter finding was attributed to the fact that rapid growth in developing-country exports of skill- and technology-intensive goods started from a relatively low base
- 10 in the early 1980s, and, more importantly, that such exports usually have stemmed from the involvement of developing countries in international production networks, where the most skill-intensive parts of the exported product have often been imported from developed countries.
- 10 These findings are based on trade flows at a high level of aggregation and, therefore, may mask substantial variation across individual developing countries in terms of the contribution of South-South trade in skill- and technology-intensive manufactures to the dynamism of their exports. However, country-specific analyses are beyond the scope of this *Report*.

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