

Economic Adjustments of Asian NIEs & Implications for Japan

By S. L. Wan

Instead of falling into the vicious cycle of poverty forcefully argued by Gunnar Myrdal in the book *Asian Drama* a quarter of a century ago, the Asia-Pacific region is demonstrating a virtuous cycle of economic development. Newly industrializing economies (NIEs) in Asia, which started their processes of industrialization by serving as subcontractors of labor-intensive products for advanced countries, are plowing back the wealth they created to meet the challenges of the next stage of productivity and economic development. Faced with the situation in which their competitiveness is no longer based on low-cost labor and the accelerated pace of competition from other developing economies, NIEs in the region are in the midst of reformulating their economic development strategies.

In the late 1980s, there was pessimism concerning the future industrial development of NIEs. New foreign investment from advanced countries, especially from Japan, was bypassing these NIEs, the once favored investment spots, and investing directly in countries like Thailand, Malaysia and Indonesia. It was generally believed at that time that NIEs would soon completely lose their pre-eminent positions

in low-end products in light of heightened competition from developing countries. On the other hand, NIEs were finding it difficult to compete with advanced countries in the high-end products due to their lack of original technologies and a general lack of their own direct sales channels and brand names.

Such perception began to change in the early 1990s. NIEs were responding favorably to the challenges posed and returning to the international business platform with renewed vigor and competitiveness. As a result of these efforts, foreign direct investment in NIEs, after experiencing drawbacks in 1989 and 1990, was picking up and/or accelerating again in 1993 and 1994, clearly indicating that economic restructuring of NIEs was creating new opportunities for advanced countries. Let us take a look at how these NIEs have responded to the challenges posed in the last few years.

Economic adjustment strategies of NIEs

Singapore, for instance, rather than trying to delay multinationals or MNCs relocating investment to other low cost

countries, encouraged these MNCs to restructure their operations on a regional basis, i.e., make Singapore their regional administrative headquarters and/or regional marketing/distribution/services/R&D centers to support manufacturing and sales in Southeast Asia. To promote such restructuring, new incentives such as the Operation Headquarters (OHQ) scheme and the International Logistics Centre (ILC) scheme were introduced. In the meantime, efforts were made to create more high value-added jobs through accelerated efforts to develop key technologies and manpower. Furthermore, in recent years, the Singapore government pushed state-owned enterprises such as Keppel Group and Singapore Telecommunications to invest in emerging economies such as China, Vietnam, India and Myanmar, a change of strategy that can categorically be described as diversifying from "Singapore Inc." to "Singapore International." This was a wise bet for sustaining the economic future of the country.

In contrast to the government-led development strategy of Singapore, Hong Kong relied primarily on the dynamics of its entrepreneurship and its excellent business infrastructure to meet the challenges. Needless to say, the opening up of China enabled Hong Kong's economy to move to a new horizon and the opportunities presented were unprecedented and multi-dimensional. For Hong Kong, the opening up of China presented a low-cost production base nearby and a vast market for products and financial services. For China, Hong Kong's role grew stronger everyday as a trans-shipment center for its products to international markets and for catering to incoming and outgoing travellers. For MNCs and overseas Chinese investors, Hong Kong was, and still is, an ideal base to tap the business opportunities in mainland China. For the future, it is no exaggeration to say



Managers from Asian countries receive training at a factory in Japan.

that Hong Kong's economy will depend primarily on the healthy economic development of China, especially by this year, when Hong Kong sovereignty returns to the mainland. As such, although Hong Kong's economic future could be even more prosperous, fostered by an increasingly modernized and progressive China, there is a possibility, however slight, that Hong Kong's future could be jeopardized by adverse political and economic events in China. Foreign investors should factor in these two possibilities when formulating their investments in Hong Kong.

Taiwan and South Korea adopted strategies different from that of the city-states of Singapore and Hong Kong in facing development challenges. The essence of their strategies was: rigorous investment by both government and private companies in technology, together with concerted efforts to build up their own brand names in international markets. They understood fully that these were the areas upon which their economic futures depended. While Taiwan has crafted its strength in personal computers and its peripherals, semiconductors, and increasing attempts at developing its own liquid crystal display and digital camera industries, South Korea has been successful in the product areas of automobiles, semiconductors, optical fibers and shipbuilding. To acquire the technologies in these and future industries, conscious efforts were made to diversify their source of technology from Japan to the United States. Instead of suffering from the problem of brain drain as in many other developing countries, Taiwan and South Korea benefitted from inbound brain drain. Students from these two countries graduated and/or worked in the U.S. after graduation and returned to their motherland with exposure to the latest technology, new business ideas and the entrepreneurial spirit of Silicon Valley. Of course, a friendly environment and expanding business opportunities at home were contributing to their return. It should be recalled that in the 1980s, one of the main purposes that the

Taiwan government to establish the Industrial Technology Research Institute (ITRI), a public-funded research institute for electronics and machine tools, was to provide opportunities for these returning graduates to continue their research. Such opportunities were still rare in the private sector at that time. Furthermore, companies were established in the U.S. to undertake R&D and collect marketing and technological information.

However, it is interesting to see that future economic development of the two countries will be governed more by political than by economic factors and hence, it demands more political wisdom than economic wisdom to face their development challenges. For Taiwan, the political question is how to chart a peaceful relationship with mainland China. China's recent military exercises in the Taiwan Strait, an attempt to dampen Taiwan's surging mood of self-determination, could severely damage Taiwan's economy in terms of capital and manpower flights, especially when the promotion of technology-intensive industries, where Taiwan is heading, requires longer recovery periods and heavier capital investment. For South Korea, the question is how to handle a socially and economically devastated North Korea. More specifically, it means reducing the military threat from North Korea in the short run, and assisting its economic reconstruction in the long run. These problems are too formidable to be solved by the governments of Taiwan and South Korea alone. Solutions can only be found through the concerted efforts of four concerned parties, all with vested interest in Northeast Asia. These are the U.S., Japan, China, South Korea and Taiwan. In other words, the future economic development of the two countries demands more political than economic wisdom.

Importance of NIEs for Asian economic growth

The continued economic prosperity of the four NIEs is not just a matter of concern to their own people, but is cru-

cial to the future economic development of the Asia-Pacific region as a whole. Instead of the "Flying Geese" economic development pattern propounded by some Japanese economists and policy-makers, economic development in the region could be better represented by the sequential pattern of "points," "lines" and "faces." After World War II, the first economic bright spot that appeared on the economic map of Asia was Japan, followed by a line linking South Korea, Taiwan, Hong Kong and Singapore. The latter happened in the 1970s and 1980s. All these points served as the core axis in spreading development dynamics to the neighboring areas, by acting as demonstrator, i.e., by a forceful governmental commitment to development, proper economic policies, assimilation of foreign management and technology, that they too can prosper. These NIEs also served as investors, capital providers and, increasingly, as export markets for their products. In 1985, only 26% of exports from east Asian countries, excluding Japan, was exported to other countries in the region, but the figure increased to 39% in 1994 and the trend is increasing. Growing intra-regional investment was one major factor for expanding intra-regional trade, and the presence of NIE investment in other Asian countries is becoming more visible.

Besides manufacturing, the statistics compiled by the World Trade Organization (WTO) reveal that in 1994, Hong Kong and Singapore ranked 10th and 12th position respectively in the global economy in terms of the export of services. The major service export items of both include transportation and communication, tourist revenue, financial services and professional business services such as advertising and legal services. In the case of Hong Kong, another outstanding item of service export is its movies and television programs. WTO statistics also indicate that South Korea and Taiwan were the 14th and 18th major exporting countries in services. If we envisage that these Asian NIEs continue to build upon their strengths in these areas, their importance in the overall development

of the Asia-Pacific region will continue to strengthen.

Implications for Japan

What are the implications of these developments for Japan? First, Japan has to understand that a positive attitude to accept change and to take risks is the only guarantee for the continued economic vitality of any nation. Any retreat to protectionism out of fear of rising domestic unemployment, an aging population, and hollowing out of industry will only provide a temporary reprieve from tackling the genuine necessity to foster a positive restructuring of its economy. Japan has also to understand that due to many artificial reasons, its domestic cost structure is too high to compete with these fast emerging Asian countries, even without *endaka*, and reliance on private companies' efforts in downsizing and rationalization to cut costs is approaching the limit. Deregulation to foster competition from within and abroad is the most efficient means to pull down the cost structure. Consider for instance, the demerits of how expensive domestic travel in Japan scared away foreign tourists, and even local tourists; and the merits of how the deregulation of international telephone services has helped reduce telephone rates in Japan in the last few years.

Second, the fast development of Asia presents Japan not only with challenges but growing opportunities. To benefit from these opportunities, Japan should understand clearly where its strengths lie and make the best use of these advantages in Asia. The competitive edges of Japan are:

(1) Its advanced technology in terms of precision, quality and originality of products such as precision bearings, liquid crystal displays, endoscopes, electro-magnetic memories, ceramic technology, application of bio-technology in farming and food processing, and perhaps, the latest that could be added to this list is digital cameras. In these technological areas, Japan has absolute competitive advantage.

(2) Its sophisticated production systems integrating numerous parts and

components of diverse technology into a single product for mass production. Examples of these are automobiles, machine tools, computer printers and computer games. Also, applying the same principle of systematic integration in retail and department store management. As a matter of fact, Japanese department stores and supermarkets have revolutionized the retailing industry in East Asia in recent years.

(3) Its strength in undertaking large-scale infrastructure and plant-engineering projects, backed by Japan's financial capital. Rapid economic development in Asia has fueled demand for infrastructure projects (especially electricity generation facilities, ports and airports) and demand for raw materials (such as steel and petrochemicals). However, in future, Japanese companies, especially trading companies, can no longer apply leverage merely by their previous strategies and presence, in anticipation that such projects are forthcoming. Faced with an increasingly stringent ODA budget, eroding competitiveness due to a high yen, and the entry of U.S. and European engineering companies, Japanese companies have to realize that such markets in Asia have become more international, open and more competitive. Their success in the future depends on their ability to design finances for such projects, to enhance skills in enlisting support from numerous financial institutions, to identify and team up with international partners with strong competitiveness in price and technology, and to apply legal skills in such methods as "BOT" and "BTO"—all the more important assets for winning future orders in Asia.

(4) Its superb abilities in generating new business ideas. Although many of these ideas like Doutor coffee chain shops and Seven-Eleven convenience chainstores originated in Western countries, it is the Japanese companies that refined them and brought them to perfection. Many of these new business ideas will find their heretofore untapped market in Asia.

(5) Its environmental protection technologies and its experience in social

engineering to promote a clean environment. Environmental deterioration has become intolerable in almost all Asian countries, especially in those mega-cities where all major economic activities that include manufacturing and transportation are heavily concentrated. Proven by its record, Japan's environmental protection and resources recycling technologies would be relevant and welcome in Asia.

Certainly, the leading position of Japan in these technologies is not guaranteed, especially if we consider the growing interest of U.S. and European companies in Asia that could offer alternatives and the "catching-up" of other Asian countries, especially the NIEs. To ensure its leading position, it is imperative that Japan continues to build its strength in these and other areas and to be price competitive.

Furthermore, it is important for Japan to realize that in the 21st century, which is less than three years away, Asia will become more multipolarized in terms of economic diversity and strength. Fostered by their success in economic development, Asian nations will be more self-confident and they will look on Japan as a partner. Asia needs Japan as much as Japan needs Asia. Understanding Asian people's mentality and aspiration, adjusting its management system to enable active participation of talented local staff in company management, a faithful recognition of its historical errors, and willingness and courage to chart the future course of the region's development in a spirit of common prosperity are essential for Japan to be a leader of what may be appropriately called the forthcoming "Pacific Century." ■

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