Geo Factsheet

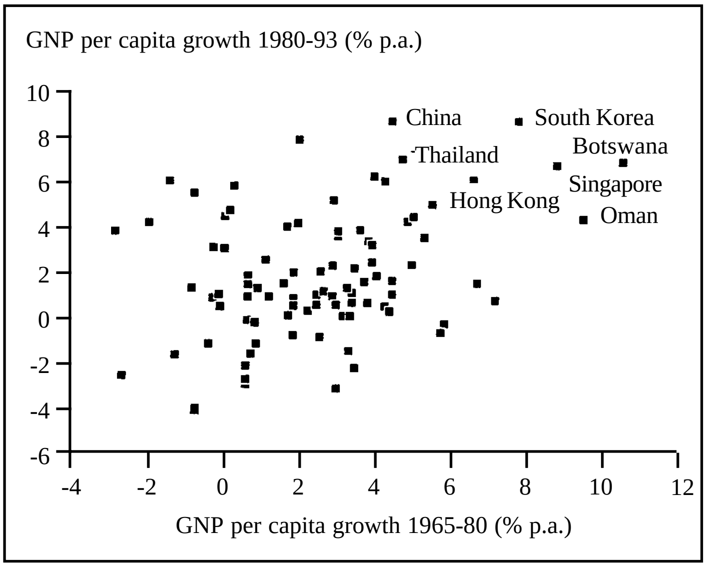
Number 34

# Opportunities and Threats in NICs

**This Factsheet will examine the causes and consequences of the outstanding economic growth of Asian Newly Industrialising Countries (NICs). The article will focus primarily on the original Four Tigers - Singapore, Hong Kong, South Korea and Taiwan but, as we shall see, these first generation NICs are now being replaced by second tier NICs - Malaysia, Thailand, The Philippines and Indonesia.**

In terms of GNP per capita, the original Four Tigers achieved outstanding success (Fig 1); countries such as South Korea and Singapore achieved outstanding growth in GNP per capita over the period 1965-80 and over the period 1980-93. Despite very different population sizes, land areas and very different political systems, each of the Tigers managed to sustain high average annual growth rates in terms of both GNP per capita and in manufacturing output.

**Fig 1. GNP per capita growth in two periods**




### Why have Asian NICs been so successful?

The success of the NICs of the Asian Pacific Rim has been put down to a combination of factors:

1. **Appropriate industries**
   None of the Asian Tigers had any real wealth in terms of their natural resources. Indeed, apart from a natural harbour, the island state of Singapore had none at all and still has to import water from neighbouring Malaysia. However, the Tigers benefited from a large, flexible and very cheap labour supply and each country developed low-skilled and labour-intensive industries. Hence, in Hong Kong, South Korea and Singapore, garment and toy manufacturing was established using cheap, female labour and this process - with the addition of products such as plastic and leather luggage and footwear - has been repeated in Malaysia and Thailand.

2. **Government intervention**
   In each country, the government has intervened to encourage and help the development of export manufacturing. The World Bank refers to this process as market-friendly development or '**command capitalism**'. In South Korea, grain prices were held down in the cities to help keep wages down. Rural incomes were then accordingly depressed and between 1967 and 1976, seven million people left agriculture to become industrial labourers. Cheap, ex-agricultural and predominantly female labour allowed rapid development of textiles, clothing, rubber footwear and the electronics industries.
   Similarily in Indonesia, between 1965 and 1980, per capita GNP increased annually by 4%. Dramatically improved productivity and profitability of agriculture helped Indonesia achieve self-sufficiency in basic foodstuffs such as rice, and in the 1970s, the country used its windfall profits from world oil price rises to embark upon huge public expenditure on its social and physical infrastructure.

3. **Foreign capital**
   The Asian NICs have also been extremely successful in attracting foreign investment. Much of this has come from Transnational Companies (TNCs).

TNCs have been attracted to the region because of:

a) Cheap labour, giving reduced production costs. In the 1960s this proved particularly attractive to U.S. and Japanese firms.

b) The growing affluence of the Asian market. All of the Asian Tigers used their soaring GNP to dramatically raise living standards and aspirations.

c) The lack of organised trade union activity.

d) The region's proximity to the huge and developing Chinese market.

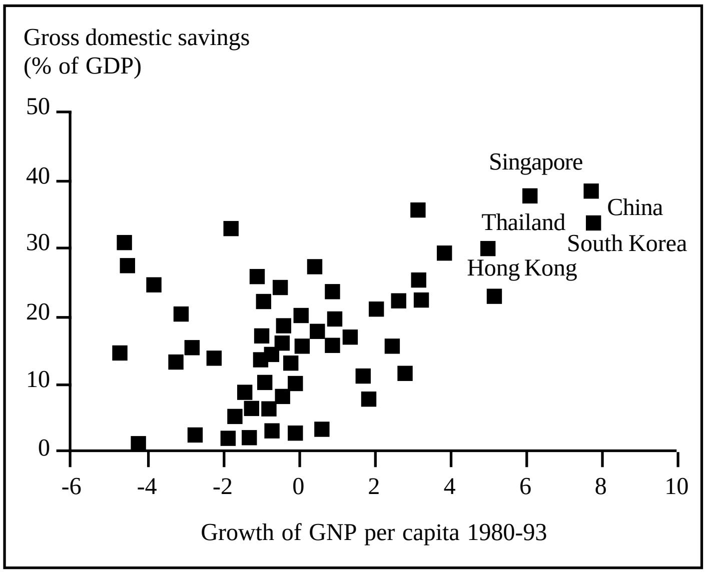
e) The ability to exploit economies of scale by merging or taking over local firms.

f) Inducements from the governments of the Tigers. For example, special Export Production Zones (EPZs) were established in which TNCs were given reliable and cheap access to electricity, along with an efficient infrastructure (eg. roads). In addition, laws on foreign ownership of companies were relaxed and concessions on pollution regulation and import taxes were offered. Such inducements proved spectacularly attractive. By 1980, 79% of Malaysia's manufactured exports came from foreign-owned firms within EPZs and by the early 1990s, 33% of Singapore's GDP was produced by foreign-owned firms.

Japanese TNCs have been major investors in the region. By 1993, nearly 75% of Japan's overseas production of electrical components was located in East and South-East Asia. The major reason for this was the availability of relatively cheap labour but this also allowed Japanese TNCs to get around U.S. import restrictions by producing semi-conductors and televisions in countries which were not covered by these restrictions. Thus, in the 1970s, Sony developed television plants in Singapore, Taiwan, Malaysia and South Korea.

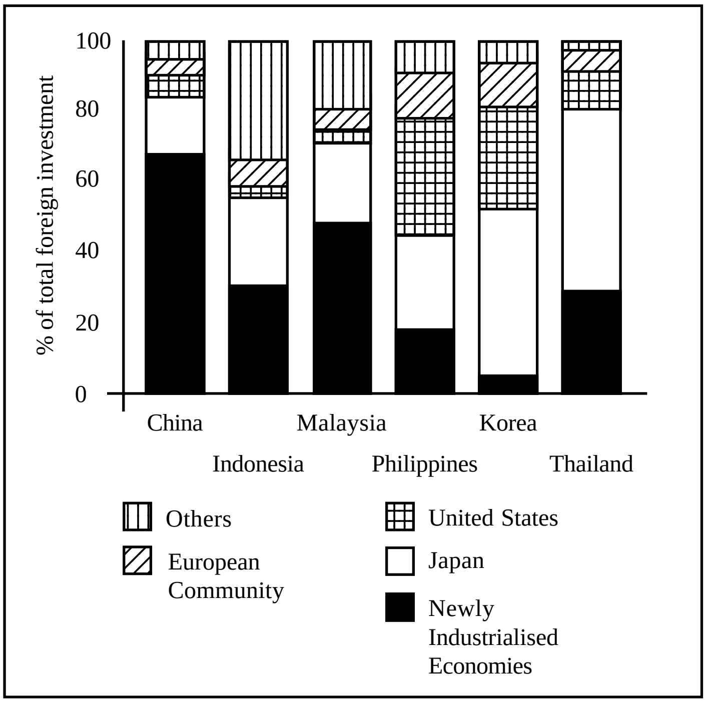
4. **Amassing of Capital**
   The Tiger economies amassed huge capital from their growth between 1960 and 1990. In Singapore in 1993, gross domestic savings accounted for 47% of GDP - the highest savings ratio of any country in the world (Fig 2).

**Fig 2. Growth and savings**




Again, this was directly encouraged by central government. This allowed the Asian NICs to become major investors in their own region (Fig 3).

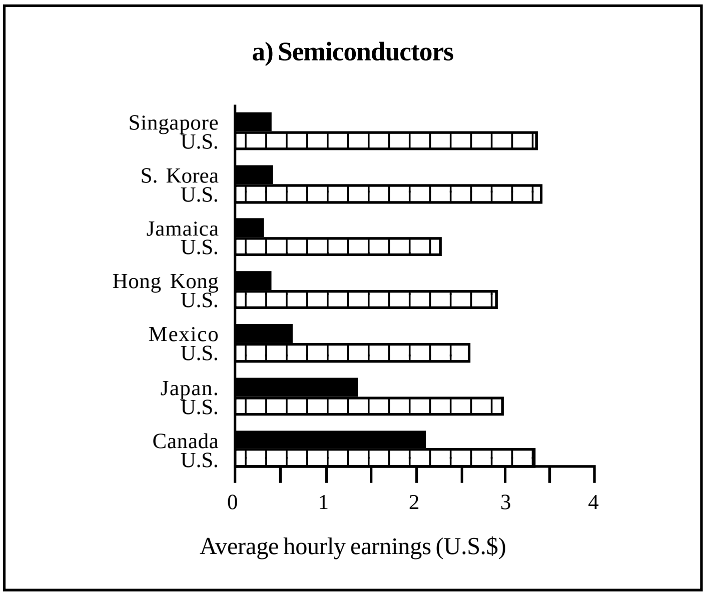
**Fig 3. Sources of investment in Asia**




5. **Increasing Value of Products**
The NICs used the profits from the manufacture and export of low quality products to develop increasingly sophisticated and valuable new products. In the 1960s, semi-conductors were produced on an integrated global assembly line. US companies developed integrated circuits in Japan which were then sent to Malaysia for packaging, to Singapore for testing and then to Hong Kong for final assembly into a PCB. This was all economically sensible, given the difference in labour costs between the USA and the Asian NICs. (Fig 4).

> ***Exam Hint*** *- Candidates knowledge often appeard dated .... few appeared to realise that NICs have their own multinational companies.*

**Fig 4. Labour costs in the US and developing countries**




In South Korea, Samsung began the first production of semi-conductors in 1976 and were quickly followed by Goldstar, Hyundai and Daewoo. However, by the early 1990s, each of these producers had rapidly developed more sophisticated products by closing the high technology gap between them and their Japanese and US competitors. By 1992, each had established their own production facilities in the United States.

## Negative Consequences

However, economic growth has brought social, environmental and economic problems.

### 1. Social problems

Availability of cheap labour has been central to the success of the Asian and other NICs. However, lack of enforcement of minimum wage legislation has led to the exploitation of women and has prolonged inequality amongst the sexes. In Malaysia, for example, women make up 75% of the workforce but, on average, receive only 75% of their male counterparts' pay. Cheap labour has also resulted in the widespread use of illegal immigrants or illegal child labour. Thailand is still thought to have around one million 13 to 14 year olds employed in agriculture or child prostitution. In Singapore, imported, illegal immigrants have allowed the maintenance of industries which would otherwise have relocated to areas of greater comparative advantage, i.e. areas with cheaper labour. It is estimated that 24% of the Singapore workforce is made up of illegal immigrants. In South Korea, immigrant workers receive 50% of the weekly wage of citizens and end up in what are known as **3-D jobs** - dirty, dangerous and difficult - sewing, leather processing, dyeing, plastics, plating and casting. The export of labour is, however, seen as one way of attracting foreign capital - it is estimated that 5 million Filipinos are engaged in overseas employment, including 650,000 construction workers and maids in Saudi Arabia.

In more general terms, it has been suggested that TNCs erode national identity and introduce 'westernised' values: coke-drinking, CD-playing, jean-wearing individuals etc. which all adds up to the destruction of a way of life.

### 2. Environmental Problems

Of all the developing regions, East Asia has the highest rate of deforestation, the highest intensity of energy use per capita of GDP and the highest emissions of carbon dioxide per unit of GDP. 20% of all vegetated land is degraded, compared to a world average of 17%. TNCs have been accused of ruthlessly exploiting the natural environment of NICs. Rapid industrial development has destroyed agricultural land, and destruction of tropical rain forests has occurred either through clearance or through conversion to plantation monoculture.

Urban areas have usually concentrated on the increasing provision of adequate quantities of water rather than cleanliness and in many Asian cities, large sections of the population receive drinking water which contains concentrations of bacterial contaminants or heavy metals which are well above World Health Organisation (WHO) levels. However, there has been some progress. In Indonesia, South Korea, the Philippines and Thailand, taxes have been introduced on vehicles, fuels, parking and road use and in residential areas of Seoul, financial incentives have been offered to persuade residents to switch from coal to gas. Legislation regarding fuel upgrading is pending.

### 3. Economic Problems

Most Asian NICs still lack adequate infrastructure. Traffic problems are continuing to cost Thailand US $2-6 billion annually and in Indonesia and Malaysia, new industries are still often unable to obtain guaranteed access to constant electricity.

Ironically, the economic success of the NICs is now beginning to work against them. As the first generation NICs become accepted as developed counterparts, they no longer qualify for favourable trading agreements and this favours the second generation NICs such as the Philippines, Thailand, Pakistan, Indonesia and China. Differential wages between first and second generation NICs means that TNCs from the developed world, and from the original NICs, now favour the second generation countries. Most of these are adopting the proven model - initially developing labour-intensive export manufactures of low quality goods but then developing increasingly sophisticated labour and information-intensive industries as their prosperity increases. This, in turn, leaves opportunities for other emerging NICs.

Many TNCs have been accused of draining profits from the host country and of recruiting the host country's best young entrepreneurs. It is also clear that the presence of TNCs has not always encouraged the development of domestic industry - a large percentage of exports in EPZs are actually made up of imports. Japan has recently decreased the number of technical transfer agreements which it has with South Korea and this has merely exposed the lack of home-grown R&D which has taken place in that country over the last fifteen years. Similarly, Thailand, Malaysia and Indonesia have relatively little R&D capacity (in all cases, less than 1% of GDP has been allocated to this sector) and attempts to develop advanced technological industries have proved expensive and problematic - the Indonesian aerospace and ship-building industries have been termed **"bonsai industries"**, meaning that they need obsessive attention and never grow. Partly as a result of this, there has been a progressive transition from secondary to tertiary industries such as financial services, investment in tourism and from manufacturing such as textiles and footwear to the heavy and chemical industries (HCI) - iron, steel and petroleum.

### Positive Consequences

The phenomenal economic growth of the Asian NICs has brought clear benefits. TNCs have brought in valuable foreign currency which has been used to increase domestic production, reduce imports and fund infrastructural and social development. Old and new technologies have been introduced and, in turn, this has allowed the development of Asian TNCs in these fields. The complexity of industrial relations in the micro-electronics manufacturing industries is increasing. Japanese firms routinely sub-contract the manufacture of components to first generation NICs such as South Korea, who will then sub-contract out to firms in second generation NICs. This creates many potential spin-offs in terms of training and, at least potentially, in research and development (R&D).

With increased prosperity Asian NICs rapidly improved their essential infrastructure such as roads and airports and then set about improving the quality of basic life - access to clean drinking water, development of sanitation, pest control and public health. In East Asia, the percentage of the population below the absolute poverty line had fallen to 10% by 1990 and has fallen by one percentage point a year for the last 25 years. Some countries have implemented tough family planning measures designed to reduce further population growth. In all of the NICs, education has also been prioritised and illiteracy rates have fallen as school enrolment rates have improved (Table 1).

**Table 1. Basic indicators in East Asia and the Pacific**

| | East Asia and Pacific region | | High-income countries |
|---|---|---|---|
| Indicator | 1965 | 1990 | 1990 |
| Daily calory supply (per capita) | 1,939 | 2,617 | 3,416 |
| Enrolment rate in primary school (%) | 88 | 100 | 100 |
| Adult illiteracy rate (%) | 37 | 24 | 4 |
| Infant mortality rate (per thousand) | 95 | 34 | 8 |
| Total fertility rate (per woman) | 6.2 | 2.7 | 1.7 |
| Life expectancy at birth (years) | 51 | 68 | 77 |

### Summary

By 1990, only 23% of employment in Hong Kong was based in the manufacturing sector and there was a parallel increase in the size of the service sector. In July 1997, Hong Kong reverted to Chinese rule and the break-up of the Hong Kong financial services sector is expected to increase the importance of the Singapore sector which is, nevertheless, inherently limited by the fact that the city state has simply run out of land. Regional expansion - for example to Shanghai - is now prioritised.

All of the Asian NICs - both first and second generation - are putting increasing reliance on the developing Chinese market and Taiwan, in particular, is selling itself as an off-shore regional operation centre for TNCs keen to exploit the Chinese market. Already several European and Japanese owned car manufacturers have established themselves in the country.

The second generation NICs have appreciated the dangers of over-reliance on TNCs and governments are aware of the need to maintain a wide manufacturing base and some independence from foreign investment. Countries such as Singapore which, through the efforts of the Singapore Trade Development Board, have successfully encouraged many of their local firms to go regional, are viewed by many second or third generation TNCs as an ideal model. Since the early 1990s, foreign direct investment in countries such as Malaysia, Indonesia, South Korea and Thailand has dramatically fallen.

Finally, in 1997 the Asian bubble burst. Firstly, several South Korean banks and insurance companies declared themselves bankrupt and revealed huge debts to financial institutions in Japan. The South Korean won was devalued and this dramatically increased the competitiveness of South Korean electronic goods in relation to the same Japanese goods-both countries directly compete in trying to export a range of electronic gadgets, cars and semi-conductors to the US. Economists now predict that Japan's GDP will increase by only 0.6% and GDP in South Korea and Thailand - which had been expected to grow as usual by 6-7% - is now expected to crash. Asian NICs are expected to drastically cut their imports and this, in turn, will effect the economies of countries which rely upon the Asian economy for their exports - Australia, New Zealand, Japan and the US in particular.

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