

The Need for a Coordinated Industrial Strategy to Boost Pakistani Exports: Lessons from Asia

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Outline

- ▶ Existing literature on export diversification
 - ▶ Lessons from other Asian Economies
- ▶ Specific Industrial Policies in the Asian Context
- ▶ Choosing ‘Winning sectors’ rather than ‘Winners’
- ▶ Empirical Analysis of the Transition from Low to High Value Added Exports
- ▶ Conclusions



Lessons from other Asian Economies

- ▶ Almost all of the growth in the sample of Asian economies has been export led. What is not clear is how this occurred at a micro level?
 - ▶ There are some important lessons one can find from the existing literature on Asian Economies
 1. Export led growth in Asia has followed the extensive margin approach. The successful Asian economies have diversified the base of exports as well as the destinations of these exports.
 2. Manufacturing exports matter more than agricultural based exports for growth
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Lessons from other Asian Economies

3. Third, these economies relied intensively on technology spillovers from foreign manufacturers who began to produce in these economies.

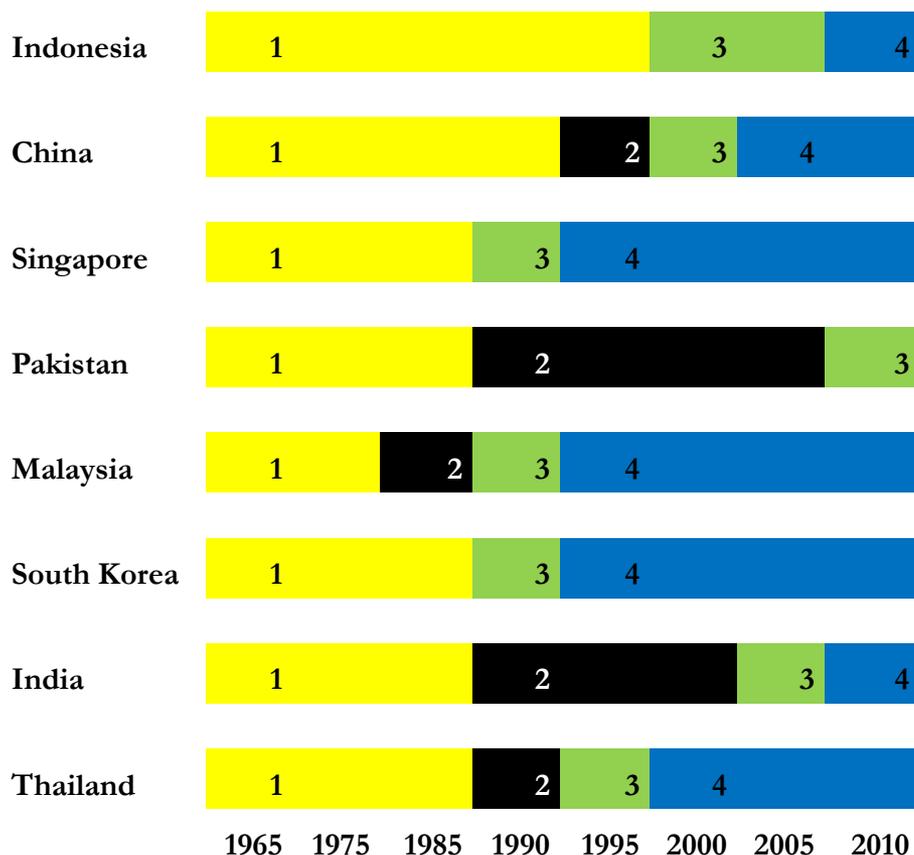
Foreign companies set up manufacturing units →, local engineers learn about the technologies and production techniques → set up their own businesses producing these goods.

This strategy was combined with focused university curricula and incentives for high skilled foreign trained nationals to return home which created the environment for foreign firms to invest in these economies as well a skilled group of individuals to start their own spinoffs.



Moving Up The Export Ladder

Figure 1: Phases of Export Development in a Sample of Asian Economies



- ▶ In the first two phases, economies would be gaining export earnings mainly from low value items such as agricultural products, tobacco and beverages, and simple manufactured items.
- ▶ In phase three, economies ‘take-off’ to high value added items such as chemicals, machinery and transport equipment while in phase four, they continue expansion in both types (the low value and higher value added items).
- ▶ In the last phase (Phase 5), economies would produce more of high value added items at the expense of basic export items.

Moving Up The Export Ladder

Lesson 1

- ▶ Export led growth has to come from existing manufactures moving up the quality ladder. Producing the same type of export commodity in larger numbers simply does not work as a long term growth strategy.

Lesson 2

- ▶ Expertise in producing higher value exports does not translate in expertise in producing higher value added goods in other categories: No technology jumping.



Moving Up The Export Ladder

Here, it seems like Pakistan is finally entering into the early parts of stage 3, which means there is a need for a coherent industrial policy focusing on:

- ▶ Significant investment in higher value added product categories in its existing exports (like textile)
 - ▶ Expansion of other sectors
 - ▶ producing simple low value added goods in other categories (i.e. stick with what they are good at) as the expertise and skills in current areas develop
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‘Winning Sectors’ Or ‘Winners’?

- ▶ The sample of Asian countries have all been based on developing a strong industrial policy.
- ▶ An interesting phenomenon among these countries has been that they chose the ‘winners’ in terms of winning export sectors
 - ▶ Choose sectors and let competition determine individual winners
- ▶ Countries pursued trade policies that supported these sectors, in terms of incentivizing capital investment and creating incentives for local and foreign companies to establish and develop
- ▶ Examples:
 - ▶ Singapore chose electronics
 - ▶ China chose textiles and electronics



Specific Industrial Policies in the Asian Context

- ▶ There is no one policy that each country has adopted to boost exports; rather each country has adopted multiple policies simultaneously.
 - ▶ China has relied heavily on Free Trade Zones and Free Trade Agreements
 - ▶ Korea and Indonesia relied on export insurance and credit
 - ▶ Singapore focused on attracting foreign direct investment and multinational enterprises to boost technological spillovers.
 - ▶ Heavy emphasis on two major components of an export promoting strategy; establishment of Free Trade Zones as well as export insurance, finance and credits.
 - ▶ Successful countries have only signed free trade agreements with countries which have significant markets for their export goods.
 - ▶ So, as is the case with the China-Pakistan Free Trade Agreement, the prime beneficiary may potentially be the Chinese exporters and not the Pakistani exporters.
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Specific Industrial Policies in the Asian Context

- ▶ What is seen in most of the cases is that the Asian economies followed a system of either adjustable pegs or managed floats (within predetermined bands) as they were entering the takeoff period for high value added export growth (or stage 3 represented in figure 1).
- ▶ Also what is seen is that they have tended to pursue the same currency system throughout stage 3 and into stage 4 of their high value export growth push.
- ▶ The message is simple for a country like Pakistan that is just entering the stage of higher value added exports:
It is critical to develop a few key aspects of an industrial strategy and stick to them as well as a coherent exchange rate policy over time, which is a policy prescription that Pakistan has failed to follow



Empirical Analysis of the Transition from Low to High Value Added Exports

- ▶ In our empirical analysis we looked at the factors that affected countries moving up the export ladder from low value added exports to high value added exports.
- ▶ The variables looked at are:
 - ▶ the exchange rate,
 - ▶ lending rate,
 - ▶ level of FDI
 - ▶ level of domestic credit to the private sector
 - ▶ the percentage of the population with tertiary training



Table 1: Fixed Effects Model of High Value Export Growth in a Sample of Asian Economies

Dependent Variable: total amount of high value added exports / total exports

<i>Variable Name</i>	<i>Coefficient</i>
Secondary level attainment in total population	.0320 (.181)
Tertiary level attainment in total population	-.977*** (.418)
Exchange Rate	.0015 (.001)
Domestic credit to private sector as percentage of GDP	.227** (.107)
Foreign direct investment, net inflows (% of GDP)	.885 (.723)
Lending interest rate	.240 (.736)
Total Imports as % of GDP	.523*** (.205)
Number of Observations: 44	
R ² : 0.5374	

Note: *** represents significance at 1%, ** represents significant at 5% and * represents significant at 10%. Standard Errors given in Parentheses.

Table 2: Ordered Logit Model of Stages of Export Growth Between 1965 And 2010 in a Sample of Asian Economies

Dependent variable: scale from 1-4 with 1 showing if a country is exporting low value added goods and 4 showing if a country is exporting high value added goods

<i>Variable Name</i>	<i>Coefficient</i>
Secondary level attainment in total population	-.0122 (.0294)
Tertiary level attainment in total population	.101* (.0578)
Exchange Rate	.0006** (.0003)
Domestic credit to private sector as percentage of GDP	.033* (.0173)
Foreign direct investment, net inflows (% of GDP)	.208 (.2914)
Lending interest rate	-.356*** (-.132)
Personal remittances received (as % of GDP)	1.020** (.472)
Total Imports as % of GDP	.362** (.0177)
Number of Observations: 38	
Pseudo R ² : 0.451	

Note: *** represents significance at 1%, ** represents significant at 5% and * represents significant at 10%. Standard Errors given in Parentheses.

Empirical Analysis of the Transition from Low to High Value Added Exports

- ▶ First, there is a strong case for incentives (in the context of a coherent industrial policy) to promote the import of capital that can assist in the technical upgradation of exports.
 - ▶ Second, this industrial policy has to make aggressive use of credit to certain export oriented (potential high value added export) sectors.
 - ▶ Third is an urgent need to coordinate vocational and technical training in Pakistan to support an industrial policy that can lead to high value added exports.
 - ▶ Fourth, there has to be a coherent strategy which differentiates between the import of intermediate goods that can be used in the manufacturing sector and the wholesale import of all foreign goods that has the potential to damage potential export sectors. This last point is extremely important as Pakistan is in the midst of pursuing free trade agreements without an industrial strategy which helps identify potential export sectors.
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Conclusions

- ▶ Unlike Pakistan, the Asian economies have pursued a set of coherent and consistent industrial policies to promote exports.
 - ▶ The strategy has been simple: a multi-tiered set of policies that help core industries develop from low value added to high valued exporters while identifying secondary industries to develop over the medium term from simple exporters to high quality exporters.
 - ▶ These economies have not just let these sectors develop themselves but rather have identified 'winning sectors' which have the potential to start out slow but expand into major export sectors.
 - ▶ The strategies have been relatively simple in nature: To provide cheap credit to these sectors while providing them with incentives to improve their technology with imported capital and collaborations with foreign investors or multi-nationals.
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Conclusions

- ▶ In addition to these policies, the high growth Asian economies have coordinated other policies with their long term industrial strategies.
 - ▶ Industrial policy was beyond a set of policies to promote industrial exports but rather a coordinated strategy which combined macroeconomic policies, educational policies, financial sector policies and focused sector specific incentives.
 - ▶ So universities were partnered with industrial sectors to develop a workforce that could not only work in chosen industrial sectors but could also learn from foreign technological advances to develop businesses of their own.
 - ▶ A good starting point would be to focus some of HEC scholarships, funding for Pakistani research as well as technical and vocational training towards pre-identified sectors.
 - ▶ Also, incentives were put in place to tempt nationals who were trained abroad in the chosen sectors to return and set up their own enterprises.
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Conclusions

- ▶ The Pakistan case: There is no coherent long term industrial strategy which looks at how to move from low to high value added textile exports.
 - ▶ At the same time there is no one has coherently identified sectors in which Pakistanis can start developing basic exports and expanding these to high value added exports over time.
 - ▶ Finally, there has to be a coherent strategy which differentiates between the import of intermediate goods that can be used in the manufacturing sector and the wholesale import of all foreign goods that has the potential to damage potential export sectors. This last point is extremely important as Pakistan is in the midst of pursuing free trade agreements without an industrial strategy to help identify potential export sectors.
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