Michigan Journal of International Law

Volume 11 | Issue 2

1990

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Linda Y.C. Lim
University of Michigan

U.S. TRADE POLICY TOWARD THE NEW NICS OF SOUTHEAST ASIA

*Linda Y.C. Lim**

As export and economic growth in Korea and Taiwan has slowed since 1988, it has increased dramatically in several countries of Southeast Asia. Thailand, for one, is chalking up a second year of eleven percent real GDP growth in 1989 to become the fastest-growing economy in the world. Malaysia and even the Philippines are not far behind, with growth predicted to reach the six to eight percent range for the second or third year in a row. Even Indonesia's growth is rising above five percent for the first time since the oil price slump of the early 1980s. Manufactures now account for over half, in some cases well over half, of merchandise exports in all four of these ASEAN countries. This has caused them to be referred to by the international business press, with varying degrees of enthusiasm, as the next newly industrializing countries ["NICs"] — the next Koreas and Taiwans, only bigger (with the exception of Malaysia).

U.S. trade policy towards Japan, Korea, and Taiwan is, in part, responsible for the recent rapid growth in export manufacturing in the ASEAN countries. These include Singapore, which like Thailand grew at eleven percent in 1988 and will probably reach nine percent growth in 1989, outstripping the Northeast Asian NICs. Unlike Korea and Taiwan, Singapore has actually benefited from recent U.S. trade policy, largely because of its close links with the other ASEAN economies. The appreciation of the won and the NT$ under U.S. pressure and the removal of GSP privileges for the NICs have — together with their rising wages, labor shortages, and unrest — shifted international competitiveness to the near-NICs of Southeast Asia. Together with the appreciation of the Japanese yen, these factors have, since 1987, brought about a huge influx of Asian foreign investment, relocating export industries to the ASEAN countries. Taiwan now rivals Japan as the largest foreign investor in Thailand, Malaysia, and the Philippines, and last year tied with West Germany as the largest foreign investor in Indonesia. Together with increased investment from Hong Kong, Singapore, and South Korea, this influx has pushed

* Assistant Professor, University of Michigan; Research Director, Southeast Asia Business Program; Acting Director, Center for International Business Education.

the U.S. down to third or fourth place in the region's foreign investment stakes.

The trade flows already emanating from these investment flows suggest some of the issues that arise for U.S. trade policy and trade relations with Southeast Asia.

First, since 1986, the Southeast Asian countries' trade balances with the U.S. have turned from chronic deficits to persistent surpluses. Still, by Korean and Taiwan standards, these are still small. Unlike Korea and Taiwan, these countries mostly run global trade deficits. Discounting oil, a very important factor in the trade of Malaysia and Indonesia especially, Southeast Asian trade with Japan, Korea, and Taiwan is also in deficit. What this adds up to is the familiar "triangular pattern of trade," whereby Southeast Asian countries, like Korea and Taiwan, import capital goods and manufactured inputs from Japan (and increasingly also from the NICs), process them locally, and then export the final products to the U.S. and other countries.

From the U.S. point of view, this investment and trade pattern has several undesirable implications. The fact that many Japanese, Korean, and Taiwanese companies manage to maintain their international competitiveness and market share by relocating to or sourcing from cheaper Southeast Asian locations reduces the benefits to U.S.-based industry of the worldwide currency realignment since 1985. Their East Asian competitors may actually become more, rather than less competitive. Japan, Korea, and Taiwan are in effect diverting part of their bilateral trade surpluses with the U.S. through cheaper third countries, from which they then "attack" U.S. industry in its home market. What's more, these countries offer them a host of investment incentives which reduce their local costs of operation, such as tax holidays, subsidized industrial estates and utilities, and preferential tariff treatment of imported inputs.

As Japan, Korea, and Taiwan open their domestic markets to imports, these may come from their own relocated factories abroad, or from independent local manufacturers in Southeast Asia rather than from U.S.-based firms. Location in Southeast Asia also gives Japanese, Taiwanese, and Korean manufacturers an advantage in supplying the rapidly growing Southeast Asian markets, which might otherwise be good markets for U.S. exports. In the absence of commensurate U.S. investment, the Southeast Asian markets may become "locked up" for good by the Japanese in particular, as they transfer entire vertically integrated production structures and distribution networks there, replicating the tight supplier-customer linkages that make the Japanese market so difficult to penetrate at home. This may make it difficult, if not impossible, for U.S. producers to penetrate these markets in the future, despite declining tariff barriers in the region and the absence of a Europe-1992-style Pacific regional economic bloc — which, for various reasons, is unlikely to emerge.

Thus, the "Southeast Asian solution" for Japanese, Korean, and Taiwanese firms relocating there in the face of the U.S. trade policy actions does more than simply limit the positive impact of the worldwide currency realignment on the U.S. trade balance. It also spawns second-generation Koreas and Taiwans and knits them more tightly together as Japanese-dominated economic territories, shutting out U.S. industry from promising growth markets. At the same time, this process is stimulating the development of new NIC multinationals. Forced by rising currencies and the loss of GSP privileges to "go international," companies from the NICs may eventually become sophisticated enough to be major players on the world competitive stage. In short, U.S. trade policy towards Korea and Taiwan has done a very good job of promoting the competition in Southeast Asia.

From the Southeast Asian point of view, U.S. trade policy towards Japan, Korea, and Taiwan has been a bonanza, bringing a windfall of foreign investment and manufactured exports, and spurring economic and industrial growth. This has not come without costs in terms of a worsening trade policy relationship with the U.S. The removal of GSP privileges for the NICs, for example, immediately made Thailand the largest recipient of U.S. GSP in Asia and the third largest in the world, thereby bringing it to the unwelcome attention of U.S. policymakers.

Of all the Southeast Asian countries, Thailand is the most like Korea and Taiwan in the nature of the U.S. trade policy actions that it is attracting. Its GSP eligibility has been challenged on grounds of inadequate protection of intellectual property rights, for which it has been put on the USTR's Super 301 priority watch list. It is also facing an investigation of inadequate labor rights. The Thai cigarette market is the controversial target of USTR market-opening measures. The country has faced antidumping actions on steel, ball-bearings (made by a Japanese company), and other products. As it exports more manufactures to the U.S. — made by Japanese, Taiwanese, Korean, Hong Kong, and Singaporean as well as Thai companies — it may become the target of more U.S. trade policy actions.

Yet, Thailand cannot retreat to exporting the simpler products of an earlier time: witness the U.S. Farm Act of 1985 which dumped U.S. surplus rice on the world market, undercutting the poor Thai farmer who is otherwise the most efficient producer in the world. This was an important psychological, as well as economic, event which drove home to the Thai that they cannot rely on market forces and primary product exports to develop, but need to accelerate their industrialization. Within the manufacturing sector, U.S. trade policy actions have also caused the Thai to lose their enthusiasm for cheap, labor-intensive products like garments and textiles which are subject to import quotas that limit their growth. Today, what the Thai are exporting or gearing up to export, with the help of their Asian investor friends and some U.S. companies, are cars and computer equipment, rather than rice and shirts, all within the space of two to three years.

Elsewhere in Southeast Asia, many of the same trade policy issues arise, though nowhere as concentrated or acrimonious as in the case of Thailand. A couple of years ago following the Korea-Taiwan model, the U.S. tried to get Singapore to appreciate its currency, claiming it was undervalued by ten percent. This pressure has ceased and the U.S. now generally praises Singapore for its open market, recognizing it as clearly the best of the NICs with respect to trade practices and, indeed, as a model for the whole world. However, Singapore, like Thailand, has also been the target of various antidumping actions, including the same one against Minnebea ball-bearings.

Malaysia is next to Singapore in terms of the openness of its trade and investment policies, and much more open than Korea and Taiwan. The Malaysian dollar is widely regarded to be undervalued, but the U.S. has not put a great deal of pressure on Malaysia to appreciate its currency. The main source of trade tension was the AFL-CIO petition in 1988-89 for Malaysia to be denied U.S. GSP privileges on grounds of labor rights violations because of restrictions on unionization in the (U.S.-multinational-dominated) electronics industry. This petition was denied after a USTR investigation which concluded that, not only had Malaysia "made progress" in the area of labor rights, but that labor conditions in the country were good and in some cases even superior to those in the U.S. Regarding Indonesia, the chief trade friction has been over intellectual property rights protection, a field in which Indonesia has recently passed legislation.

There is no question that as the ASEAN countries move up to NIC status in the footsteps of Korea and Taiwan, the U.S. will increasingly focus its trade policy attention on them. This is the main reason why Malaysia vigorously denies that it even aspires to NIC status, and goes about frequently and publicly proclaiming all the reasons that it is "not a NIC." Though there are similarities in the trade policy situations of the established and the new NICs, there are also some differences that may influence their policy relationship with the U.S.

First, with the partial exception of Malaysia, the Southeast Asian next-NICs are very much poorer than Korea and Taiwan are today, or even than they were ten years ago. Thailand's per capita annual income is about $1,000, the Philippines' per capita annual income about $700, and Indonesia's less than $600 a year. As still-poor developing countries, they will retain developing-country designation and treatment — including GSP privileges — for a long time yet to come. Many of the arguments which underlie these countries' resistance to U.S. pressure on trade issues also reflect concern about the welfare effects on their poor populations who, for example, cannot afford to pay for brand-name pharmaceuticals or expensive copyrighted textbooks, videos and computer software, but can afford cheaper generic medications, copies, and imitations.

Second, these economies have been rapidly liberalizing their trade and foreign investment regimes. With the exception of Indonesia, they have always been more open economies than were Korea or Taiwan. The U.S. is anxious not to jeopardize this process of economic liberalization, although it has, thus far, been Japan and the other Asian NICs, not the U.S., which have most availed themselves of the new opportunities presented by liberalizations.

Third, because of their past relative openness, the Southeast Asian countries host substantial amounts of U.S. foreign investment — much more than Korea and Taiwan. In cumulative terms, U.S. investment is probably still close to that of the Japanese in most countries. Thus, unlike Korea in particular, these countries have many friends in America — U.S. multinationals located here, particularly in oil and high-tech, who would be hurt by some U.S. trade policy actions and who can lobby effectively against them in the U.S. itself.

Fourth, the ASEAN countries are long-time friends and important Third World allies of the U.S. They have supported U.S. positions on many international issues and in many international fora, from Cambodia in the United Nations to free trade in agriculture and services at GATT. They also have the capacity to act together on regional or international issues of mutual interest, and thus possess some bargaining power, both individually and collectively, with the U.S.

Fifth, related to this is the lesser direct dependence of the ASEAN countries on the U.S. than either Korea or Taiwan. Their exports are more diversified, with no country sending more than a quarter — in most cases, less than a fifth — of its exports to the U.S. market. The U.S. has also declined in relative terms as a foreign investor and aid donor in Southeast Asia, and wields much less leverage with governments of the region than it did before. Japan, on the other hand, is now the region's largest foreign investor and aid donor as well as its first or second most important trade partner. The U.S. has to be careful that its actions do not push the Southeast Asians ever deeper into the arms of the Japanese, to the detriment of the long-run competitive position of U.S. firms themselves. U.S. trade policy actions in the last few years have already alienated many of its friends in the region, with the Singapore National Trades Union Congress, for one, publishing and circulating throughout the international labor movement a pamphlet entitled, "U.S.A. — Big Brother or Bully?"

Finally, unlike Korea or Taiwan, the Southeast Asian new NICs cannot be accused of being mercantilist. Despite their bilateral surpluses with the U.S., they run global trade deficits, and exports are, to them, a means to industrial development and material prosperity for their people, not an end in themselves. They have also not repressed domestic wages or consumption levels to promote exports and restrict imports. And they are restrained by domestic politics from pursuing such a strategy of high tariffs and artificially low wages.

What then, can or should the U.S. do to improve its trade position in Southeast Asia, if not by employing the somewhat heavy-handed methods which have only been partly successful in Korea and Taiwan? The one answer that all Southeast Asians give is, "Invest more in our countries" — to diversify their dependence on Japan, to make their local markets more competitive, and to generate trade flows which could even reverse the "triangular pattern of trade" and reduce their trade deficits with Japan. In other words, U.S. firms should locate in Southeast Asia not only to supply the local and regional markets, but also to penetrate the Japanese, Korean and Taiwanese markets themselves — in the case of Japan, perhaps even benefitting from expanded Japanese GSP. Unfortunately, American business does not appear to be about to take this course of action on a large enough scale. With Southeast Asian markets rapidly filling up with Japanese, and to a lesser extent Korean and Taiwanese, capacity, it may already be too late.