INDUSTRIAL AND TRADE POLICIES UNDER THE NEW TRADING SYSTEM: TOWARD A COMPARATIVE ANALYSIS BETWEEN EAST ASIA AND LATIN AMERICA

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ABSTRACT

It is generally assumed that as a result of the Uruguay Round and other international accords, developing countries will face more stringent restrictions on their ability to conduct selective trade and industrial policies. On the other hand, the room for manoeuvre has by no means disappeared, and a number of policies can be still exploited by developing countries for industrial and trade pursuits, which conform to the commitments of the Round and other trade agreements. The objective of this paper is to explore the issue of manoeuvrability in trade and industrial policies by developing countries under the new international trade system.

The paper consists of four chapters. The first introductory chapter outlines the need for an "endogenous" development focus, especially from the perspective of Latin America and the Caribbean. Chapter II provides an overview of endogenous industrial and trade policies and the justification for them. The following chapter briefly examines new constraints and room for manoeuvre in trade and industrial policies under the new international trade regime, specifically in the area of fiscal, monetary and exchange rate policies, business facilitation, export subsidies, counter-measures on imports and exports, TRIMs, TRIPs, services and agriculture. Chapter IV describes an ongoing ECLAC project whose objective is to carry out a comparative analysis of some selective East Asian and Latin American countries, their past and present trade and industrial policies and their future evolution, under the legal framework of the new world trading system.
I. INTRODUCTION

One of the principal objectives of public policy in Latin America over the last two decades has been, and will continue to be, structural transformation of the economy based on a deliberate and systemic incorporation of technical progress, which is conducive to upgrading international competitiveness by achieving an authentic insertion in the world economy through increased productivity. The driving force of this process must be the competitiveness and dynamism of the national economy, which create needs for openness, competition, deregulation, privatization, macro-economic stability and structural reforms, not founded solely on export expansion. The endogenous nature of the process of absorbing knowledge through openness generates dynamic economic growth, which later translates into a rapid, diversified offer of exportables. In short, "Structural transformation has a major influence on the evolution of comparative advantage and is a cause of economic growth; however, it should not be considered as an automatic by-product of an outward-oriented strategy and sound macro-economic policies as in free trade orthodoxy."\(^1\)

From the perspective of an endogenously oriented trade expansion, the reduction of the levels of tariff and non-tariff barriers and their dispersion and the elimination of anti-export biases by appropriate exchange rate policies are far from sufficient. As Rodrik puts it, "Trade policy plays a rather asymmetric role in development: an abysmal trade policy can perhaps drive a country into economic ruin; but good trade policy cannot make a poor country rich. At its best, trade policy provides an enabling environment for development.\(^2\) Hence, industries to sustain the economy of the next generation (i.e., dynamic industrial and trade sectors) will not emerge automatically from the adjustment process, but only through the activities of the private sector. Trade liberalization must be accompanied by a strategy of openness, involving a set of policies through which the economy as a whole may achieve international competitiveness and a more dynamic insertion in the world market, as one of the catalysts of sustained growth.

The case for this development thinking is strengthened by the results of economic reforms in Latin America of the last decade and a half. The countries in the region have pursued the goals of macro-economic stabilization based on fiscal discipline, trade liberalization and financial deregulation, the improved functioning of market mechanisms, and greater reliance on private investment. For the majority

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of the countries, these reforms have resulted in moderate growth rates which are inferior to historical performance and unsatisfactory with regard to technological progress, job creation and social equity.

Neither recent economic reforms giving the market a greater role in the allocation of resources nor the large-scale return of capital flows to Latin America that began in the late 1980s has led to a significant improvement in investment performance. Rather, by way of marked exchange rate appreciation and rising interest rates, they have tended to discourage the productive investment required for structural transformation and, at the same time, have deviated investment funds mainly to financial channels and consumption. In addition, structural change which would render the economy more resilient to external shocks and more able to sustain long-term rapid growth has been slow, while macro-economic stabilization and structural reforms have usually reinforced "optimum" allocation of resources under the existing industrial and trade structures and technological level of Latin American countries, specializing in a limited number of primary products and light industry of low value added.

In the past, Latin American development thinking and policy formulation was placed in a false dichotomy. The development of the dynamic East Asian economies was contrasted with the unstable, deteriorating economic performance of Latin America. Some analysts attributed the differences in the two regions' performances to the outward-looking, market-oriented, export growth strategies of East Asia as against the inward-looking, interventionist, import-substitution strategies of Latin America. These false, stylized contrasts contributed to the evolution in Latin America of an economic orthodoxy that emphasized trade liberalization, open economy policies, getting prices right through market forces and a smaller role for the State. In short, the greater importance attached to market signals as the basis for resource allocation has led to the almost total disappearance of sectoral policies, investment promotion schemes, and, above all, industrial policy measures, making the coordination of macro-, meso- and micro-economic policies redundant.

It is now widely accepted that an important part of the East Asian success is mainly attributable to pragmatic and selective government intervention, which resulted in an accelerated pace of capital accumulation, technical progress, structural change and, hence, economic growth, beyond what would have been possible from laissez-faire. In essence, government interventions have been directed at tackling a series of closely interrelated and mutually reinforcing market failures which hold back the process of investment and innovation in a typical late-industrializing country. This argument still holds true, in spite of the severe economic turbulence experienced by the East Asian countries in recent months.

The new disciplines assumed under the various accords at multilateral, plurilateral, sub-regional, regional and hemispheric levels (the Uruguay Round in particular) will not allow Latin America to resort to selective industrial and trade policies of such scope and intensity practiced in East Asia. As a result of the World Trade Organization (WTO) and other international accords whose commitments sometimes go beyond the scope of the WTO (WTO-Plus), developing countries will face more stringent restrictions on their ability to conduct development-oriented trade and industrial policies. The "showcase" countries in East Asia also have to accommodate and innovate their policies in accordance with their regional and

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3 ECLAC maintains that for the region as a whole to grow at an annual rate of 6% (or for per capita income to grow at a rate of 4%), the coefficient of investment as share of gross domestic product (GDP) must rise by 6 percentage points to 28% (ECLAC, Strengthening Development, The Interplay of Macro- and Micro-economics (LC/G.1898/Rev.1-P), Santiago, Chile, 1996. United Nations publication, Sales No. E.96.II.G.2.)
multilateral commitments, including the Uruguay Round, the Asia Pacific Economic Cooperation (APEC) and the ASEAN Free-Trade Area (AFTA). The question of manoeuvrability in industrial and trade policy under the new scenario must be addressed.

On the other hand, it is also clear that the room for manoeuvre has by no means disappeared. Even the area of trade per se still contains policy domains that can be exploited by developing countries. Taking into consideration the "endogenous" focus, developing countries should actively seek to strengthen policy measures to develop endogenous capacities which are consistent with the norms of the Round. Measures could be designed to attack the problems of infant industry protection, externalities, coordination failures and information asymmetry in product and capital markets. How to implement these measures will be a major future concern for Latin America and East Asia. From this perspective, both regions can learn from each other on imaginative intervention to alter the perceptions of economic agents and thereby improve economic performance.

The incorporation of developing countries into the multilateral WTO system implies that these countries have to change domestic legislation in a large number of new areas, including services, intellectual property rights and several new areas of trade policy (e.g., safeguards, subsidies, antidumping, and competition). National institutions have to develop their capacities for enforcement and administration. Formulating trade and industrial policy within the legal framework of the Round commitments will require not only more lawyers but also able bureaucrats and efficient institutions.

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II. JUSTIFICATION FOR AN ENDOGENOUSLY ORIENTED INDUSTRIAL AND TRADE POLICY

A. ENDOGENOUS INDUSTRIAL POLICY

The debate on causality in the relation between growth and exports for East Asia (i.e., export-led growth versus growth-led exports) is far from settled. An increasing number of studies suggest, however, that the development process is led by investment. Investment is a condition for productivity growth, and output per head is related to capital per head. Contrary to the view professed in The East Asian Miracle by the World Bank, the principal determinant of the East Asian miracle seems to be capital accumulation rather than an increase in total factor productivity. It is likely that the causality chain starts with investment, which increases the rate of structural change and productivity improvement, which in turn leads to a supply-driven process of export expansion and international competitiveness. In contrast to the neoclassical view, eventual decreasing returns will not necessarily set in with high rates of investment. Rather, when technical change is regarded as being embodied in new capital goods, high rates of investment lead to faster technical progress, greater learning by doing and a virtuous circle of greater competitiveness and faster economic growth. It is possible that post-war East Asian growth started from the inside outward and is supply-driven, and greater trade growth occurs as a result of rapid GDP growth.

The East Asian countries have had much higher investment rates than Latin American countries in the last 25 years, and the disparity in investment performance has tended to widen. Public investment in East Asia has not declined, and private investment has gone hand in hand with increases in public investment. East Asian governments have managed to engineer a significant increase in the private return on capital not only by removing a number of impediments to investment and establishing a sound investment climate, but more importantly by alleviating the coordination failure which typically blocks sustainable economic growth. Certain industries of high future potential have been promoted by clear criteria for selectivity and incentives of a moderate and finite nature. In sum, the Asian experience has shown that public policies must affect the parameters of the savings and investment functions, promote

\[\text{\textsuperscript{5}}\text{ For an analysis based on this viewpoint, see, UNCTAD, Trade and Development Report, 1996, (UNCTAD/TDR/16), Geneva, 1996, chapter, II. United Nations publication, Sales No. E.96.II.D.6.}\]

\[\text{\textsuperscript{6}}\text{ For this line of argument, see for instance, Paul Krugman, "The myth of Asia’s miracle", Foreign Affairs, vol.73, No. 6, November-December 1994; Dani, Rodrik, "Growth policy. Getting interventions right: How South Korea and Taiwan grew rich", Economic Policy, April 1995; and Ajit Singh, "How East Asia Grew so Fast?: An Analytical Consensus", RIS Occasional Paper, No. 46, Research and Information System for the Non-Aligned and Other Developing Countries, New Delhi, 1995.}\]

\[\text{\textsuperscript{7}}\text{ The debt crisis of the 1980s does not fully explain this difference because the level of capital accumulation in Latin America was far lower than that in East Asia even during the 1970s.}\]
efficient organization of the financial system and establish an adequate institutional framework, making it possible to channel savings to productive investment. The question has yet to be addressed regarding the extent to which the WTO regime would allow such measures to influence the investment and savings parameters of the outward-oriented countries.

As the events of the past few months testify, the savings-investment link is not a settled issue for East Asia. A number of countries (e.g., Malaysia, Indonesia, Thailand, the Republic of Korea and the Philippines) have experienced a severe deterioration of the balance of payments and trade as a likely consequence of trade liberalization and an easier access to foreign credit. The issue of the savings-investment nexus is thus becoming increasingly important for East Asia as well.

Productivity growth is a result of an incremental, long-term process of learning by doing, based on past and present production experiences. But within the economy, some sectors display greater capacity for technological innovation, while others serve as strategic sectors which transmit their strong externalities to the rest of the production system. The tacit, specific, and cumulative nature of technical change can lead to divergent accumulation rates of technological capabilities among countries over time.

The industrial system should be viewed as a series of national networks of interfirm, intra-industry and interindustry linkages: the nature of these relations along the longer production chain—based on efficient firms and a competitive network of research and development (R&D) units, suppliers, producers, distributors, wholesalers, retailers and service centres—is what determines competitiveness. Other crucial factors at the national level include a favourable macro-economic environment, adequate physical infrastructure (especially in transportation and telecommunications), a literate, skilled workforce and adequate institutional infrastructure for the legal system, the financial system, export promotion and technological support. Latin American and East Asian countries face intense competition from competitors inside and outside their own region, arising in part from enormous infrastructure bottlenecks.

From this perspective, trade policy is unlikely to be a first-best instrument for correcting any distortions in factor and capital markets. The problems should be tackled at their roots. In labour markets, for instance, many important skills are acquired on the job. High labour turnover, however, causes enterprises to under-invest in upgrading the skills of their employees. In product markets, the pioneer enterprises which try new technologies or new markets provide valuable information to others in the economy, and when successful, their experiences can be emulated. These informational and technological externalities, especially those of external origin, cannot be readily internalized and are therefore underproduced. In the absence of well-developed capital markets backed by an adequate prudential and regulatory framework, the financial market is unlikely to do a good job in financial intermediation, especially where long-term investments or small- or medium-scale firms are involved. Entrepreneurs thus tend to depend more on funds which are generated internally or by family.

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8 The major determinants of competitiveness increasingly have to do with the following factors: i) the rapid rate of generation and disappearance of new knowledge and innovation; ii) the broad applicability of new information-handling technologies across a broad spectrum of economic activities; iii) the reduction of labour costs as a production process through technological change; iv) shorter process and product life cycles; v) the predominance of the quality of the product over cost competitiveness; vi) the growing importance of responsiveness to customer needs, including quick delivery times; and vii) the need for aggressive marketing and efficient networks.
To assure a faster, more intensive capital accumulation—physical and human alike—it is necessary to act simultaneously on all its components, via the application not only of neutral, horizontal policies (i.e., regardless of the sectors concerned), but also of selective policies, which will have lasting effects on systemic competitiveness. The list of measures is long:

i) promote and/or regulate certain productive sectors or services, especially those which are conducive to international competitiveness, for instance via tax incentives;

ii) restructure and rationalize the sectors which produce importables;

iii) attract foreign direct investment (FDI) to new sectors with future potential, and obtain and diffuse foreign technology in harmony with the country’s process of technological change;

iv) facilitate certain export-oriented industries and services in certain geographical areas;

v) promote physical and social infrastructure (both public investment and private participation), provide general subsidies and credits for R&D and vocational training, and procure know-how;

vi) extend credit facilities to those entities excluded earlier from the formal financial market (small- and medium-sized enterprises, in particular) by way of establishing and/or strengthening national "development" banks;

vii) perfect trade credit facilities;

viii) overcome widening regional income disparities;

ix) provide temporary production subsidies in sectors with economies of scale (e.g., infrastructure, telecommunications and energy);

x) implement effective environmental protection measures and labour legislation consistent with the process of opening up; and

xi) efficiently use Official Development Assistance (ODA) and other foreign credit facilities in accordance with national development priorities.

While some measures are unlikely to lead to reprisals by the international community, others will be subject to severe scrutiny. An urgent task facing the policy makers of Latin America and East Asia is to assess, with certain clarity, to what extent these interventions are permitted under the emerging international trade regime and under what modalities they are to be implemented.

B. ENDOGENOUS TRADE POLICY

In areas more directly related to trade, the government could act as a crucial moderator-cum-facilitator for the initiatives taken by the private sector. For exports and imports to be a cumulative process of learning and technology absorption both for local traders and for the country as a whole, there should exist an appropriate institutional framework to ensure the public good of international insertion.
Government participation will have strong positive externalities, even for countries of a small market size. Such externalities include, for example, the following:

i) trade promotion activities which are provided by governments through information services, market development, assistance in design and packaging, etc., which can be appropriated by firms with ambitions to export;

ii) export externalities which accrue from meeting international market standards, product quality specifications, quality criteria and distribution and marketing challenges, which, once achieved, can be generalized to other products and processes;

iii) import externalities which result from the learning opportunities made possible by importing capital goods and intermediate goods with embodied technologies;

iv) negotiation on market access for specific products to specific markets;

v) strengthening the negotiation capacity on foreign market access in general; and

vi) coordination of these policies with those of other countries, under subregional, regional or hemispheric integration schemes.

The East Asian experience in this field of public policy and their future accommodation should offer useful insights for Latin America.

The recent proliferation of trade accords in Latin America and East Asia has implied realignments of tariff and non-tariff measures, bringing with them both static and dynamic effects on trade and investment flows, the cost structure of production, competition patterns and the creation and diffusion of technology. These agreements should lead to a better articulation of regional capacities in transport, telecommunications, energy, water and other forms of infrastructure. They should also lead to a more homogeneous system of trade-related services, investment, intellectual property rights, factor mobility, rules of origin, antimonopoly laws, antidumping and safeguards, sanitary and phytosanitary regulations, etc. Ongoing negotiations and existing agreements in both regions, will likely play a crucial role in shaping the nature of government intervention acceptable in multilateral relations. For this reason, these agreements should be analysed from the viewpoint of the endogenous model, in a comparative context between Latin America and East Asia.
III. TRADE AND INDUSTRIAL POLICIES AFTER THE URUGUAY ROUND:
NEW CONSTRAINTS AND ROOM FOR MANOEUVRE

Under the commitments of the Uruguay Round and other international accords, developing countries will face more stringent restrictions on their ability to conduct development-oriented trade and industrial policies. The WTO commitments, for instance, will reduce developing countries' freedom in many areas of trade and industrial policy-making, the most obvious being i) the practical elimination of export subsidies and other subsidies which affect export prices; ii) the curtailment of quantitative restrictions for balance-of-payments purposes; iii) pressures to bind and reduce tariffs; and iv) the ban of domestic-content and trade-balancing requirements on foreign investors by the Agreement on Trade-Related Investment Measures (TRIMs). Outward-oriented industrialization strategies will not be able to resort to measures of the size and variety of those applied successfully by the East Asian economies in the past. Now, special and differential treatments for developing countries seem to have largely been limited to longer periods for implementing obligations. Below, the major agreements of the Uruguay Round are briefly analysed to foresee the adjustments and reforms necessary to conform to the commitments and at the same time to assess the possibility for developing countries to formulate endogenously-oriented policies without violating them.

A. FISCAL, MONETARY AND EXCHANGE RATE POLICY OPTIONS

There seems to exist a wide range of fiscal, monetary and exchange rate policies which are acceptable to the WTO. The WTO rules do not impose restrictions on monetary and fiscal policies that would facilitate high savings and investment rates. In the new trading order, developing countries should pay special attention to the enforcement of fiscal discipline in the government sector. They should also adopt suitable interest rate and credit policies so that the contributions of the household and corporate sectors to domestic savings is realized to its full potential in investment. Furthermore, trade and industrial policy instruments, including the investment regime, strongly influence and are heavily affected by exchange rate policy. A stable, realistic real exchange rate can reduce the need to excessively apply measures to compensate the anti-export bias of other policies such as special credit lines, insurance schemes, export subsidies, etc. From this viewpoint, though the post-Uruguay Round trading regime may restrict the use of a number of instruments of industrial policy with respect to the promotion of exports and the control of imports, it should not prevent countries from resorting to policies regarding domestic savings and investment. These are just as crucial to industrial success as trade policy.

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9 With respect to tariff binding, however, some degree of differential treatment remains: though may not be desirable, developing countries have the freedom to raise tariffs up to the bound level (mostly in the range of 25%-30% for developing countries, which are substantially higher than in developed countries).
B. BUSINESS FACILITATION MEASURES

Businesses face numerous difficulties in customs rules and procedures, including non-transparent, inefficient customs infrastructures. Hence, trade promotion could be enhanced through the simplification and harmonization of customs procedures and standard norms.

One interesting example in this area is the "de-bureaucratization" programmes in Uruguay which aims to simplify customs procedures for exporting its major products (e.g., meat, wool and leather) by reducing the number of necessary papers from ten to four, by streamlining bureaucratic procedures, and by speeding up the processes. Uruguay also employs a "single window" system at the Center for Export Documentation (Centro de Trámites de Exportación, or CENTREX) in the Central Bank. Companies first must file an Exporter Registration Card. CENTREX then issues various export documents to registered exporters on presentation of an export application and a commercial invoice, thereby greatly simplifying the paper work involved.\(^\text{10}\)

Some developing countries have taken important steps to simplify trade procedures, and further improvements are expected with the imminent implementation of new computerized systems.\(^\text{11}\) In Brazil, for instance, export procedures and the processing of export documentation have been improved with the introduction of the computerized information system SISCOMEX in 1993. Brazil has also made many improvements in the development and administration of standards, testing and certification since 1992. Indonesia passed a new customs law in 1995 which became effective in April 1996, in order to comply with its Uruguay Round commitments as well as to change the system of inspection. Measures such as can be as effective as other export promotion instruments which are encouraged by the WTO.

C. SUBSIDIES

The WTO Agreement on Subsidies and Countervailing Measures defines a subsidy as a financial contribution by the government (including non-collection of taxes that would otherwise be due) and clarifies the rules on the use of subsidies. They are now classified under three categories: "prohibited", "actionable", and "non-actionable" subsidies. Any developing country with a per capita gross national product (GNP) less than US$ 1,000 is permitted to maintain export subsidies. Once it graduates from this income level, that country has to phase out export subsidies over an eight-year period. This gives an interesting, but not necessarily sufficient, breathing space to lower-middle-income countries where significant industrialization has not yet taken place. The Agreement also contains certain flexibilities however: developing countries are allowed to subsidize exports if their presence in the importing country’s market is modest; the *de minimis* clause indicates the possibility of even applying actionable

\(^{10}\) These examples are cited in Laird, op. cit., p. 19.

\(^{11}\) Export procedures and the processing of export documentation has been improved with the introduction of the computerized information system SISCOMEX in 1993. World Trade Organization (WTO), *Examen de las políticas comerciales: Brasil*, Informe de la Secretaría (WT/TPR/S/21), October, 1996, pp. 79-80.
subsidies (i.e., those that cause injury, nullification or impairment of benefits, or serious prejudice) if they are moderate.  

Prohibited subsidies include non-agricultural export subsidies and subsidies contingent on domestic content requirements. These prohibitions affect a wide range of export performance schemes still in practice, such as the reduction of tariffs on imported inputs up to an equivalent value of exported final goods. A clear example of this would be the Brazilian waiver of the 70% duty on imported components used in automobile assembly, up to the equivalent value of exported automobiles. Similarly, Chile and El Salvador use rebate systems based on the f.o.b. value of exports, which do not conform to the WTO provisions on duty drawback. Such measures indirectly affect the prices of all factors of production, including wages, capital costs and other factor costs, none of which is rebated. Duty drawback schemes, in which the precise amount of duty is rebated on the export of a component incorporated in a final good, are not considered export subsidies. Drawback schemes differ from the export performance schemes mentioned above in that under the former, the precise amount of duty is waived or rebated on the same parts (or identical, domestically produced parts) that are re-exported.

Another important exclusion is the precise exemption or remission of indirect taxes that are normally payable on the production and distribution of like goods sold for domestic consumption. This could include sales taxes or value added taxes, but not direct taxes such as taxes on wages and profits. The reimbursement of indirect taxes, charges and other levies paid by exporters, such as Colombia’s tax reimbursement certificates (Certificados de Reembolso Tributario (CERT)), is not prohibited, though it may contain an element of subsidy.

Export credits and export credit guarantee or insurance programmes below costs are prohibited, but not if the loans are made above cost but below market rates. For example, Brazil’s Export Financing Programme (PROEX) and Finance Programme for Exports of Machinery and Equipment (FINAMEX), take place below market rates but above cost and are thus not considered a subsidy. Concessional taxes and duty provisions covering earnings, profits and imported materials and capital goods, such as Colombia’s Special Import/Export Systems (SIEX), are considered to contain a subsidy element. Therefore, some countries will need to conduct a comprehensive overhaul of the internal taxation system.

Many countries in Latin America and the Caribbean and East Asia provide a number of fiscal incentives for industries located in export processing zones (EPZs). These are often linked to outward processing operations, or maquilas. For some countries in Central America and the Caribbean and China, a major part of their exports originate from these zones. Article 3 and Annex I of the WTO Agreement on Subsidies and Countervailing Measures classifies the fiscal exemptions available under free trade zones.

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12 Serious prejudice occurs when the amount of the total ad valorem subsidy exceeds 5%, when subsidies are used to cover operating costs, or when there is direct debt forgiveness.

13 Agriculture is exempt from the general prohibition on the use of export subsidies.

14 Support for exports of goods and services is available through PROEX. Although interest rates are pegged to the London interbank offered rate (LIBOR), the rate equalization mechanism provides a subsidy to Brazilian exports because the Government pays the difference between the interest charged and the cost of raising funds. The National Economic and Social Development Bank (BNDES) operates FINAMEX, offering financial facilities for exports of capital goods and equipment.

15 Laird, op. cit., pp. 3-4.
and export processing zones as prohibited export subsidies. Developing countries, however, have until 2003 to bring their legislation into line with WTO provisions.\textsuperscript{16}

The \textit{non-actionable} category allows developing countries to subsidize activities with externalities, if they are not specifically oriented to exports and if the subsidies are given to all industries. This permits, in principle, the use of subsidies related to training and retraining, which are essential to upgrading productivity and international competitiveness, as well as R&D related subsidies, including product-quality improvements, local adaptation of foreign technology and studies of consumer preferences. Subsidies that are general in nature (i.e., not "specific" in the sense used for actionable ones) and thus do not have an impact on prices are not actionable. Other examples of general subsidies include assistance to underdeveloped regions,\textsuperscript{17} support for complying with new environmental standards or norms, or even certain types of privatization programmes when applied by developing countries.

For such countries as Malaysia, it will not be difficult to phase out subsidies, as they have already abolished a number of subsidies based on expert performance. Future support for the manufacturing sector will not be based on subsidies but will encourage firms to increase productivity and labour skills. For others, such as the Republic of Korea, it is necessary to replace existing prohibited subsidies for export promotion and domestic product procurement by non-actionable subsidies and to reduce the amount and scope of subsidies during the prescribed grace period. In fact, the Government of Korea has recently announced that subsidies for export promotion such as the Export Industries Equipment Investment Fund, Export Import Loans, the Export Loss Reserve Fund, and Special Depreciation for Foreign-Exchange-Earning Fixed Assets are to be replaced by export insurance, long-term export credit, drawback schemes and a trade bill system which are allowed under the WTO.\textsuperscript{18}

\section*{D. COUNTER MEASURES ON IMPORTS AND EXPORTS}

In the first 20 years of the General Agreement on Tariffs and Trade (GATT), there was little use of the antidumping mechanism, because of high tariffs and extensive use of quantitative import restrictions. Today, it has become the prime trade defense instrument. Domestic producers' preference for this mechanism over other trade control measures, such as safeguards under article XIX of the General Agreement, relates to several factors: i) the injury test is lower; ii) it allows discrimination, with antidumping duties set for each foreign firm; iii) the time-frame is longer; iv) the use of safeguards envisages adjustment by the domestic industry; v) there is no compensation requirement; and vi) a


\textsuperscript{17} For example, in Brazil regional development is promoted through federal and BNDES programmes as well as by the use of free trade zones. By far the most important of these zones is the Manaus Free Trade Zone, from which practically all the production is destined for the Brazilian domestic market.

foreigner can be labeled as "unfair" in the propaganda war.\textsuperscript{19} The Agreement requires that antidumping duties remain in place for no longer than five years, unless a review demonstrates that the removal of injury would lead to continuation of dumping and injury, the so-called sunset clause.\textsuperscript{20}

In the 1990s, developing countries increasingly resort to dumping actions and impose countervailing or dumping duties to ensure fair competition. A number of developing countries have been involved in GATT/WTO consultations and panel reviews, regarding the application of antidumping and countervailing regulations.\textsuperscript{21} Some countries have introduced new laws and regulations to enable them to instigate such actions against exporting countries.\textsuperscript{22} Other countries need to implement changes to existing laws to conform to provisions in the Uruguay Round antidumping agreement.\textsuperscript{23} Still others need to eliminate such measures as domestic goods procurement agreements orderly market arrangements and other import relief measures, since they are not clearly allowed in the agreement. In addition, emergency tariffs, quota tariffs and adjustment tariff systems should be consistent with the WTO Agreement on Safeguards.\textsuperscript{24} It will also be necessary to strengthen administrative and support capacities in order to implement effectively the Uruguay Round commitments.

\textsuperscript{19} Laird, op. cit., p. 11.

\textsuperscript{20} It also contains de minimis provisions relating to the margin of dumping and volume for terminating proceedings: antidumping cases are to be terminated if the margin of dumping is less than 2\%, or if the share of the volume from particular countries in the importing market is below 3\% (or, cumulatively, 7\% among exporters supplying less than a 3\% share).

\textsuperscript{21} For example, Brazil’s use of contingency measures has increased, with 66 antidumping cases and 13 countervailing investigations initiated between 1992 and 1995. In the mid-1996, 25 antidumping and 7 countervailing actions were in force.

\textsuperscript{22} Indonesia, for example, had no legal regulations or institutional mechanism to instigate dumping actions or impose countervailing duties. Thus a number of laws and regulations were introduced in 1995 and 1996 to enable the country to instigate such actions against exporting countries. The elements of these laws and regulations closely follow the new agreement under GATT 1994. The implementing organism is an antidumping committee made up of officials from the Ministry of Trade and Industry, the Ministry of Finance and other relevant ministries or non-ministerial agencies.

\textsuperscript{23} For example, although the Malaysian antidumping and countervailing law is comprehensive, it still needs to be changed to conform to the provisions in the Uruguay Round antidumping agreement. The Malaysian antidumping law needs to be revised: i) to incorporate the legal definition of dumping; ii) to amplify its too-restrictive definition of domestic industry, which does not describe some portion of the industry; and iii) to require that to initiate an investigation, the petition must be supported by at least 25\% of the total production in the domestic industry. Mohamed Ariff, Mahani Zainal-Abidin and Tan Eu Chye, "Study of the Emerging Global Trading Environment and Developing Asia: the Malaysian Perspective", Study of the Emerging Trading Environment and Developing Asia Conference on Countries, Manila, Asian Development Bank, 29-30 August, 1996, pp. 50 and 51.

\textsuperscript{24} Pursuant to Article 4.2(b) of the Agreement on Safeguards, which stipulates that the determination of serious injury to a domestic industry shall not be made unless the investigation demonstrates, "on the basis of objective evidence, the existence of the causal link between increased imports of the product concerned, and serious injury or threat thereof." For instance, it will be necessary for the Government of Korea to amend provisions on safeguards in the Foreign Trade Act accordingly (Hak K. Pyo, Ki-Hwan Kim and Inkyo Cheong, op. cit., p. 18).
With regard to the impact of the antidumping agreement on developing countries' exports, producers do not have adequate resources to appeal antidumping decisions by importing countries. Many are small companies without the legal expertise or financial resources to prepare a case to present their points of view. Many are not even aware of the antidumping agreement and its very detailed provisions and requirements. Furthermore, industry associations in developing countries are not strong lobbying groups, and some are not even active. Thus, affected companies may not have a ready-made mechanism to support their case. The local institutional capacity must be strengthened and expanded, including legal expertise, in order to provide effective support.

E. TRADE-RELATED INVESTMENT MEASURES (TRIMs)

The Uruguay Round agreement on trade-related investment measures (TRIMs) reaffirms existing GATT disciplines relating to national treatment (article III) and the prohibition of quantitative restrictions (article XI). Essentially, TRIMs on local content and trade balancing requirements are inconsistent with the former, while those relating to trade and foreign-exchange balancing restrictions and domestic sales requirements violate the latter. All members had 90 days from the WTO's entry into force to notify measures not in conformity with the provisions of the agreement. Measures not notified had to be eliminated immediately. Developed countries were obliged to eliminate notified measures within two years (i.e., by 1997), while developing countries had five years and least-developed countries had seven years. This agreement could have far-reaching implications for many industries of interest to developing countries, such as the automobile sector, where local content schemes and export-balancing requirements are widespread. In Latin America, for instance, this would affect the automotive industry in the Andean Group, the Southern Common Market (Mercosur) and Mexico.25

The most controversial aspect of the TRIMs Agreement appears to be the provisions of article III and article IV, under which developing countries can deviate from the stipulations of article II, regarding national treatment and general elimination of all quantitative restrictions, only when the WTO Committee on Balance-of-payments Restrictions is "convinced" that the country which is intending to initiate some immediate corrective measure is really in a balance-of-payments crisis. Furthermore, priority will have to be given to "price-based" measures, and quantitative restrictions will have to be kept to the minimum. The concerned member country will also have to prepare a comprehensive document on various aspects of the balance-of-payments situation and policy measures, and will have to undergo continuous monitoring and surveillance by the aforesaid Committee.26

In the last decade, there has been a clear tendency to liberalize foreign direct investment (FDI). Many countries in East Asia and Latin America raised the maximum foreign ownership to 100% in almost all sectors except for sectors of public interest. The divestment period was also increased. At the same time, the conditions for receiving national treatment have been relaxed. There has been a shift from an approval system to an application system.

25 Laird, op. cit., p. 10.
In September 1993, for example, the Government of Korea announced a foreign-investment liberalization plan which converted FDI from an approval system to an application system. Further liberalization measures were introduced in June 1994 by extending industry scope and investment environments. By 1997, the total number of industries in which FDI is allowed will be increased to 95.3%. (At the time of publication, the number was 1,040 out of 1,148 total industries.) Also by 1997, the application of FDI can be made at any foreign exchange bank rather than at the Bank of Korea, and the bank is supposed to reply promptly rather than taking 20-30 days, which is the Bank of Korea’s current customary practice. Financial and tax incentives to foreign investors who are introducing high-technology businesses into the country will include allowing them within-three-year short-term foreign borrowing, above-three-year foreign commercial loans and deductions for corporate and value added taxes. They will also be allowed to acquire larger areas of land, and the Foreign Investment Industrial Complex will be opened in Kwangju and the Chunan area. Each local government is supposed to open a Foreign Investment Assistance Center, and all institutional supports are to be provided to domestic small- and medium-sized firms, including R&D Assistance Funds for foreign investors. These measures are in line with the TRIMs agreement and should enhance the endogenous technological capacity.

As the Korean case illustrates these TRIM restrictions do not prevent developing countries from using special tax incentives or certain types of minimum performance requirements (for instance on exports) to attract multinational firms which would have strong impacts on local competitiveness, technology enhancement, human capital capacitation, etc. Moreover, this agreement does not address the issue of local content requirements (LCRs) related to government procurement. Most developing countries are not signatories to the Uruguay Round agreement on government procurement, and hence face no restrictions on the use of LCRs in the context of government procurement.

Market forces in a competitive environment could ensure the FDI effects of growth diffusion and technology diffusion. It is prudent, however, for host governments to set up a multidisciplinary governmental machinery entrusted with the tasks of examining the various facets of the foreign investment flows and advising the private sector to take corrective actions to make the foreign investment activities conducive to and consistent with the imperatives of development in the national economy.

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27 In Indonesia, maximum foreign ownership was raised in 1986 to 95% for export-oriented firms, investments in East Indonesia, high technology, and ventures requiring large capital (i.e., above US$ 10 million). In 1987, the divestment period was increased to 10 years. Foreign investors are now able to receive national treatment if the venture is at least 75% Indonesian owned; if 51% of its shares are sold on the capital market; or if 51% is Indonesian owned and 20% is sold on the capital market. The conditions for receiving national treatment were further relaxed in 1987 to 51% Indonesian owned or 45% owned and 20% of its shares issued in the capital markets. In 1989, 100% was allowed for firms exporting 100% of their production and located on Batam Island, an export processing zone next to Singapore. Foreign investors were required to divest 5% within 5 years. In 1992 100% foreign ownership was allowed for certain types of investment (i.e., over US$100 million, in East Indonesia, and 100% export oriented). Finally, in June 1994, most of the restrictions were removed to allow 100% foreign ownership in all sectors except for the nine public-interest sectors, which were open for joint ventures. Sherry Stephenson and Mari Pangetsu, “Indonesia and the Emerging Trading Environment”, Study of the Emerging Trading Environment and Developing Asia Conference on Country Studies, Manila, Asian Development Bank, 29-30 August 1996, pp. 34-37).

28 Hak K. Pyo, Ki-Hwan Kim and Inkyo Cheong, op. cit., pp. 4-5.
F. TRADE-RELATED ASPECTS OF INTELLECTUAL PROPERTY RIGHTS (TRIPs)

Exercising a patent is the obligation of the patent-right holder and for this reason many Patent Acts provide for compulsory licensing of the patent for its activation. However, the GATT-1994 Agreement does not provide for this. Article XXVII envisages that patent rights are "enjoyable without discrimination as to the place of invention, the field of technology and whether the products are imported or locally produced". Importation is considered equivalent to local production, thereby indicating that patents can be exercised through importation of the product. The agreement allows compulsory licensing only in limited cases (e.g., educational and research purposes). Article 70, further provides for what is called pipeline protection, under which a country which has not introduced a product patenting regime must provide five years of exclusive marketing rights to a product patent holder of any other country in the case of pharmaceutical and agricultural chemical products. Granting exclusive marketing rights to a foreign patent-right holder tends to thwart local initiatives for innovation and competition.29

Some countries are already reforming their regulations to conform with the TRIPs agreement. Brazil, for instance, has reformulated their regulations: a new Industrial Property Law was approved in May 1996 covering, among others, the granting of patents of invention and of utility models; legislation of industrial designs and trademarks; and repression of false geographic indications. Provisions concerning "pipeline" protection entered into force in May 1996, while other sections came into force in May 1997.30 Similarly, Indonesia will amend its copyright, patent and trademark laws, and it will also introduce implementation regulations on industrial design. In addition, three new laws will be introduced covering industrial design related to integrated circuits, protection of new plant varieties and protection of trade secrets.31

Malaysia is not expected to have a serious problem in meeting the requirements of the TRIPs agreement. In some areas, however, additional provisions must be incorporated to meet all the obligations. For example, patent laws must be amended: i) to incorporate protection for plant varieties; ii) to provide protection for a term of 20 years from the date of filing, instead of 15 years from the date of grant; and iii) to change the compulsory licensing provision in conformity with the article 31 of the TRIPs agreement. Malaysia also has to create specific laws dealing with the protection of layout designs of integrated circuits.32

Other countries are taking positive steps to minimize the effects of the TRIPs agreement. One such step is the dissemination of patent information among firms, research institutes and universities. Another is to help firms develop their own brands and design capacity and to protect their endogenous technology.

29 Phanchamukhi, op. cit., p. 9.
30 WTO, Examen de las políticas ..., op. cit., pp. 121-127.
31 In the late 1980s and early 1990s, Indonesia introduced gradually various laws and regulations on IPR, such as copyright (in 1982 and updated in 1987), patents (1989 and later amended in 1991) and trademark (in 1992 to replace the 1961 law). The new trademark law involved a fundamental change in recognizing the "register system" (i.e., the first to use the product or service is the one entitled to register the trademark) rather than the "first use principle" (i.e., the first to register has the right to the trademark) (Stephenson and Pangentsu, op. cit., pp. 104-108).
32 Ariff, Mahani and Tan, op. cit., p. 46.
Government authorities can also improve the coordination of TRIPs administration among different branches of the Government. For those countries which are already creators and exporters of intellectual property rights and which possess patents in certain crucial areas, the agreement gives better protection for intellectual property rights inside the countries themselves as well as outside. However, it will imply higher administrative and enforcement costs, increased expenses to acquire proprietary knowledge and start-up and incremental costs for monitoring domestic R&D facilities.

Despite the fairly strong limitations placed on TRIPs, developing countries still have some room for manoeuvre. They can use to their advantage the transitory nature of the agreement which has a maximum 10-year grace period for implementation. Royalties on imported technology will not necessarily inhibit its transfer to developing countries. The information embedded in each patent or even in imported goods is public knowledge, and nothing prohibits others from using it as a starting point for other innovations. In fact, all innovations must be adapted to local conditions, and they are receptive to continuous improvements. If, for instance, countries succeed in excluding from their national legislation on patents the large proportion of innovations that is already routine or that constitutes a minor advance, and if they can exclude general scientific principles from copyrights, significant gaps will remain in the international legal system for practicing reverse engineering and adapting existing technology.

G. SERVICES

From the viewpoint of developing countries, the General Agreement on Trade in Services (GATS) is a relatively balanced agreement whose principal merit is to establish a flexible basis for future negotiations. Because the service sector involves the movement of factors of production across national borders, the agreement contains a series of exceptions and positive lists to which countries can resort, hence preserving an important degree of national autonomy. Also, the General Agreement permits developing countries to negotiate specific commitments from foreign firms to strengthen the efficiency and competitiveness of their domestic services, including access to technology, distribution channels and information networks.

Developing countries in both East Asia and Latin America practice a high degree of selectivity in their GATS commitments. They are "standstill" commitments. The majority of the countries attached certain limitations to these commitments related to market access and national treatment. In many sectors, approval will still be required for asset acquisition, merger or take-over of a national entity by foreigners. Certain limits on national treatment are also imposed for reasons of State interest. In most services activities, a commercial presence is allowed through a locally incorporated joint venture. Aggregate foreign shareholding in the joint venture may also have a ceiling. The commercial presence of a foreign

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33 For example, Korea, has designated the Patent Office for handling industrial property rights; the Ministry of Culture for copyrights; the Ministry of Industry and Resources for semiconductor design rights; and the Ministry of Science and Technology for computer program rights.

34 Agosín, "La política comercial ...", op. cit., p. 164.

35 The proportion of sectors (out of 1,240 possible cases) which did not contain any restrictions, in terms of both market access and national treatment, was 6.8% for Latin America and 8.0% for East Asia. (Bernard Hoekman and Carlos A. Primo Braga, "Trade in services, the GATS and Asia", Asia-Pacific Economic Review, vol. 2, No. 1, pp. 5-20, 1996).
financial institution is only allowed through the establishment of a locally incorporated joint venture with aggregate foreign shareholding not exceeding a certain limit. In addition, each country presented a list of most favoured nation (MFN) exemptions for particular sectors (e.g., movement of personnel or semi-skilled workers; construction; government-funded projects). These exemptions are subject to a review every five years, to be conducted by the WTO Council for Trade in Services.

Indonesia practices a high degree of selectivity. Within the GATS framework, the country has made commitments on services under five broad sectors: telecommunications, industrial services, maritime transport, tourism and financial services. Certain limitations on market access and national treatment are attached to these commitments. For instance, the Joint Venture/Representative Office should be a limited-liability enterprise, and not more than 49% of the capital share of that entity may be owned by foreign partners. In addition, there is a list of MFN exemptions for particular sectors, including banking, movement of personnel or semi-skilled workers, construction and government-funded projects.

Similarly, Malaysia made GATS commitments in the areas of finance, insurance, business, communication, construction and related engineering, health-related social services, tourism and travel, recreation, culture and sport, transport and training. When deemed necessary, the government can use the horizontal commitments to limit the market access of foreign services producers. For instance, approval will still be required for asset acquisition, merger or take-over of a Malaysian interest by foreigners, if it exceeds a specific limit. Certain limits on national treatment are also imposed for reasons of State interest. In most services activities, a commercial presence is allowed through the establishment of a locally incorporated joint venture with either Malaysian individuals or Malaysian-controlled corporations, with aggregate foreign shareholding not exceeding 30%. These same limitations apply to the commercial presence of a foreign financial institution.

The principal benefits arising from financial liberalization are the expansion of the range of financial services available to domestic firms (e.g., trade finance and insurance) and the associated organizational, managerial and marketing know-how. Developing countries should therefore apply selectivity and discretion as allowed in the General Agreement to discriminate in favour of long-term capital flows which increase investment and against short-term volatile flows which destabilize the domestic economy.

H. AGRICULTURE

The Agreement on Agriculture provides certain special, differential treatments to exporters from developing countries regarding the de minimis provision, export subsidies and exemptions of certain

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36 For example, incentives are offered only to Malaysian-owned corporations, and there are no limits to the measures that the Government can introduce to help Bumipueras (Malays) under the New Economic Policy (NEP) and the National Development Policy (NDP). Under the general limitation for national treatment, any deals involving land property and real estate must have the approval of the relevant domestic authorities.
subsides. The latter involve, for example, the exemption from commitments to reduce export subsidies on marketing, including those related to their manipulation, improvement and other processing expenses, and international and domestic transport costs. Also, the "green box" measures include government assistance for R&D, fighting pests or diseases, infrastructure, food security, structural adjustment, environmental programmes or regional assistance programmes.

For some countries the Agreement on Agriculture does not imply major changes, while for others it means significant adjustments. Some governments must implement policies to minimize the short-term impacts of the Round and to support farmers' welfare through various means of income assistance. They may have to restructure and streamline existing subsidy-related rules and laws, such as double-price systems, grain-management systems and agricultural subsidies. In addition, they may need to prepare measures for emergency import relief and improve in sanitary and phytosanitary measures for imported agricultural products. In all cases, it is necessary to make progress in restructuring the agricultural sector and raising its productivity.

Both price-based and non-price-based factors such as quality and standards are emerging as the crucial determinants of comparative advantage in this sector. The policy response in the developing world aim to improve productivity, expand the scale of operations and conform to the sanitary and health standards of agricultural products. Since government support for R&D activities and other service programmes is exempt from reduction commitments, governments should seize these opportunities to divert the resources released by subsidy reduction towards programmes to increase R&D activities.

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37 By virtue of the de minimis provision, in developing countries, internal support measures that do not exceed 10% of the production value (threshold of 5% for developed countries) are exempted from the reduction commitments. Export subsidies by developing countries will also be reduced by 21% over a 10-year period from their average levels prevailing in 1986-1990 (36% over six years for developed countries).
IV. ECLAC PROJECT ON "TRADE AND INDUSTRIAL POLICIES UNDER THE NEW TRADING SYSTEM: A COMPARATIVE ANALYSIS BETWEEN EAST ASIA AND LATIN AMERICA"

The foregoing analysis is based on fragmentary information gathered on specific topics, primarily from secondary sources. What is missing is a more detailed analysis of individual countries. To address this insufficiency, ECLAC is now in the process of executing a project, funded by the Japan Fund for International Cooperation for Development, to undertake a comparative analysis of selected East Asian and Latin American countries, focusing on their past and present trade and industrial policies and their future evolution under the legal framework of the new world trading system. The project is designed to extract from the experiences of both regions the essence of the appropriate role of the State in industrial and trade development and to identify its new role and available instruments, in conformity with the post-Uruguay Round trade regime.

This project undertakes six comparative case studies on past and future trade and industrial policies between Asia and the Pacific (Indonesia, the Republic of Korea and Malaysia) and Latin America (Brazil, Argentina and Chile). The selection of the countries is based on the level of industrial development, market size, and corporate and state culture. The basic structure of the six studies is outlined below.

i) Review the recent literature on sources of economic growth for the country in question, covering the last three decades, to discuss the causality between growth and exports in order to characterize the growth pattern as either export-led growth, or growth-led or investment-led exports. The discussion should examine the performance of savings (domestic and foreign), investment (domestic and foreign) and foreign trade (exports and imports) in relation to the national product, detect major changes in their evolution, and identify policies responsible for such changes. Special emphasis should be given to three factors: 1) the role of investment; 2) the incentive structure, the capability-building process and the institutional framework linked to productive investment promotion; and 3) the effective employment of foreign capital for capital formation and technological improvement.

ii) Examine whether the country’s industrial and trade policies were selective or neutral in the period up to the conclusion of the Uruguay Round (December 1993). In either case, specify the policies and their positive or negative impacts. Examine the transformation of the incentive system, the design and control of instruments to improve the competitiveness of the industrial and export sectors and the sequencing and timing of protection or incentives granted.

iii) Analyse in depth the range of future trade and industrial policies under the constraints of the new trading system. Examine possible modifications or changes contemplated, or already introduced in national legislation in a number of new areas, including services and intellectual property rights, and several fields of trade policy (e.g., tariff binding and reduction, reduction or elimination of non-tariff barriers, TRIMs, safeguards, subsidies, antidumping, competition), to conform with WTO agreements.
iv) Identify selective and neutral policy instruments that can still be sought and implemented to enhance endogenous capabilities, yet which are consistent with the WTO agreements. In particular, policies should be developed in the following areas: physical investment; human capital; infrastructure; investment and trade finance; management, technology, and information acquisition and diffusion; manpower training; and quality control and standardization. Identify new incentives, capability-building mechanisms and institutions that can be created for such purposes, as well as measures to soften the effects of trade liberalization and financial deregulation on national firms and instruments to facilitate the structural transformation of infant industries, declining industries and small- and medium-sized enterprises (SMEs).

v) Review the present institutions of industrial and trade policy-making. Analyse the relation between the private sector and the State, bureaucratic autonomy, coordination and articulation (or lack thereof) between macro and micropolicies and networking among government agencies. Discuss possible institutional developments that might enhance the establishment of a coherent, long-term, global development strategy and trade policies, in the context of globalization, regionalization and rapidly changing comparative advantage. Such institutions include not only various governmental ministries and agencies, but also semi-public and private organizations in the areas of industrial and trade promotion, human capital formation, trade finance, investment, technology development, industry and trade associations and Chambers of Commerce. The above also includes the representation of commercial interests and economic diplomacy in foreign countries.

vi) Analyse the role of subregional and regional integration accords in shaping the nature and scope of industrial and trade policy. Study their impact on trade and investment flows, exploitation of economies of scale, the cost structure of production, patterns of specialization, R&D efforts, infrastructure building and regulation of foreign investment (e.g., rules of origin; repatriation of profits and capital) to guide multinational companies in coordinating operations at a regional level.

The commissioned papers are to be completed by the end of 1997. ECLAC will then hold a seminar for the consultants and other interested parties to discuss and diffuse the project results. The seminar will probably take place in the second quarter of 1998 in Santiago, Chile.