4[4]

Improving Supply Responses in ACP Countries
Complementarities Between Government and the Private Sector, with Particular Reference to SMEs

Summary

The conventional wisdom regarding structural adjustment is that to 'get your prices right' is both a necessary and sufficient condition for growth. This report takes the view that 'getting prices right' is necessary but not sufficient. It suggests that some interventions are also required. These can be divided into two categories functional and selective (Lall 1994a). The former are those interventions which address market failures without favouring any specific activity (e.g. provision of infrastructure, institutional capacity, education), whereas the latter 'are designed to favour individual activities or groups of activities in order to remedy specific failures or externalities that would lead to sub-optimal resource allocation either in a static or dynamic sense' (Lall, 1994b p.65). Selective interventions address market failures concerning the creation of a dynamic capacity within an economy in particular information and technology upgrading, and skills formation.

Governments also have important roles to play in the co-ordination and timing of policies. This ensures that the skill creation, technological capacity and know-how are developed in line with requirements. However 'government failures' exist in developing countries, and assistance is required to help overcome resulting problems.

An example of this approach is seen in Taiwan ROC where the complimentarities between market mechanisms and government interventions have been very successfully exploited. The case study of Taiwan provides many important lessons for other developing countries.

Increased globalisation means that growth must be private sector led. This requires greater emphasis being placed on micro, small and medium-sized enterprises (SMEs).

The second part of this chapter examines the importance and potential benefits of small firm development in developing countries, and stresses the need for a strategy rather than ad hoc development. This is particularly important since small firms experience greater efficiency when they operate in clusters or groups. Under such conditions horizontal and vertical links develop between enterprises. These, together with subcontracting, result in a network of formal and informal relationships which greatly enhance flexibility and speed of reaction time.

Any post Lomé agreement needs to target assistance towards overcoming 'government failure', and to provide assistance to support small enterprise development.

4.1 Introduction

The discipline imposed on economies by globalisation and liberalisation requires countries to adopt forward looking and outward oriented policies. However many developing countries are characterised by low growth, political instability, weak and fragmented industrial bases, and low and unstable export earnings that are highly concentrated in primary products. Under such conditions economies are vulnerable to both exogenous and endogenous shocks. Their problems are exacerbated when governments pursue weak macro policies which result in inflation,

4 The authors would like to thank Mr. Carl Greenidge for his helpful comments on Chapters 4 and 5.

low levels of private and public savings and investment, overvalued exchange rates, and balance of payments problems.

Faced with such problems governments often engage in indiscriminate protection, the results of which resonate throughout the industrial and manufacturing sectors, causing increased costs and uncompetitiveness, low levels of productivity, and rent seeking behaviour. Under these conditions countries are clearly unable to meet the levels of efficiency required for successful participation in world trade. Adherence to a sound macro policy, together with the rule of law and a degree of political stability are necessary conditions for participation in the global economy, and for economic growth and development.

Many ACP countries, through structural adjustment programmes, are implementing macro policy reforms in terms of financial and trade liberalisation, exchange rate policies, and reductions in public sector expenditure. Some still have a way to go.

The conventional wisdom, however, is that this 'getting your prices right' is both necessary and sufficient for growth. The alternative view put forward in this report is that 'getting your prices right' although a necessary condition for growth is not in itself a sufficient one. Efficient selective intervention in both product and factor markets to facilitate market entry, to support industrial and export expansion and the formation of a technological capacity, and to create new markets, is also necessary for sustained growth.

To understand this controversy it is necessary to understand the implicit assumptions of the conventional approach to structural adjustment. This assumes:

1 Goods markets will provide the correct signals for investment if allowed to operate freely.

2 Markets for factors of production are free to respond to these signals.

3 As a result, the economy will make the most efficient use of the country's resources. The 'guiding hand' of the market with its constant flow of information can never be improved upon by government.

4 The acquisition of technological capabilities and knowledge does not enter into this analysis because it is assumed to be available throughout the world and can be easily obtained by a developing country. Indeed, it is often claimed that latecomers can grow more rapidly because they can acquire the hard won knowledge of today's more developed countries. Increasing the technological capacity of a country is therefore seen as an engineering problem, not an economic one.

In this view of the world, the role of government is solely to provide basic public institutions and a legal framework and pursue macro policies which will ensure a stable and predictable economic environment. It may be accepted that some factor and product markets may not operate efficiently where there is a public goods issue. An example would be education, where the social benefit may be greater than the private benefit captured through increased lifetime earnings and where the time horizon of individuals may be less than that of society, in which case there will be private under-investment in education. Similarly, firms may under-invest in training workers because other firms may 'free ride', not train workers, and simply poach them away with higher wages. In these cases the conventional wisdom would be that government intervention is potentially beneficial provided the intervention is *general* and *neutral*, that is it is not selective between different economic activities or economic agents(for example policy should be neutral as between foreign and local firms). Also, such limited interventions should be *indirect*, utilising the market, for example, through a system of taxes and subsidies. The general conclusion of the conventional structural adjustment approach is that there is no need for policies to support, protect, and induce the acquisition of

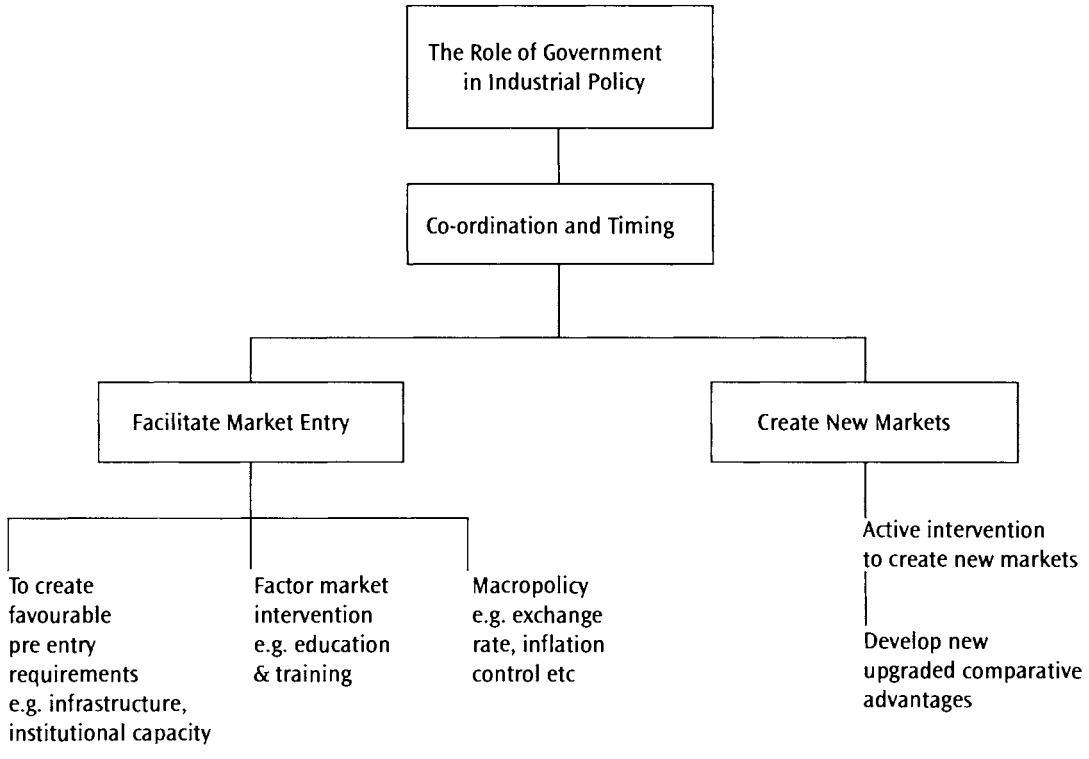
technological capabilities and knowledge in developing countries (Pack and Westphal 1986), or to create new industries and upgrade existing industries from which new dynamic comparative advantages will result (Biggs and Levy 1990), and that where governments have done so, for example in the NICs, these policies have had few positive structural effects (as discussed for example, in World Bank 1993. This conventional view is also largely implicit in the thinking underlying the policy prescriptions of the Commission, as outlined in the Green Paper.

The alternative view, forwarded by this report, strongly supports Lall's analysis (1994a and 1997), and that discussed in the Industrial Development Report (UNCTAD 1996). As stated earlier, globalisation means that countries must adopt outward oriented policies, this has necessarily resulted in the need for governments to adopt the discipline of appropriate macro policies. This approach strongly endorses the conventional view that sound macro policy and structural change are fundamental prerequisites for industrial and export-led growth. It also recognises that globalisation has changed, and to some extent reduced, the role of governments in formulating economic policies. However, this report advocates that the development of sound and efficient industrial and trade sectors, which are capable of acting as a platform for export-led growth requires that further interventions be undertaken. The nature of such interventions will be discussed in subsequent paragraphs. Within this approach we can distinguish clear and decisive roles for governments in co-ordination, the timing of policy executions, and in planning and implementing interventions designed to assist the development of industrial and trade sectors.

4.2 The Role of Government

The role of government in this approach is outlined in diagram 4.1 below.

Diagram 4.1 **The Role of the State in Industrial Policy**



Consider first the role of government in policy co-ordination. As countries begin to develop, industries and markets do not necessarily develop in a well co-ordinated and logical manner. Pockets of economic or entrepreneurial activities may arise, but their future development may well be thwarted by insufficient physical and business infrastructure, and underdeveloped financial markets or export channels. The timing and co-ordination of policies aimed at developing these support systems is crucial. Similarly in the early stages of industrialisation, output consists primarily of low-tech, labour-intensive commodities such as wood manufactures, garments and footwear, together with agricultural output. In order for industrialisation to proceed smoothly the development of strategic processing and heavier industries must be planned for and not merely allowed to develop in an ad hoc fashion. Future skill requirements need to be anticipated so that education and training keep pace with industrialisation. The conventional approach relies heavily on market mechanisms to provide the necessary stimulus for new industries to develop. However, the private sector in general, and entrepreneurs in particular, are motivated by profits. Profits act as a signal to entrepreneurs attracting new investments in relatively high performance industries. These profits arise out of the differences between private costs and private returns, and accrue to individual firms. For an economy as a whole however, the focus must be on social costs and social returns. Given externalities, private sector investment may, in some areas, be sub-optimal and poorly-timed.

Also, as economies develop some industries will naturally decline whilst new industries will spring up. There is a critical need to forecast, with some accuracy, both sunrise and sunset industries, and formulate policies both to mitigate the impact of shutdowns, and to train workers in the necessary skills and techniques required for the new sunrise industries (UNCTAD 1996).

The second, and equally important, role of the state involves intervention. Lall (1994) stated that interventions can be divided into two categories – functional and selective. 'Functional interventions' are those interventions which address market failures without favouring any specific activity over another whereas 'Selective Interventions' are designed to favour individual activities or groups of activities in order to remedy specific failures or externalities that would lead to sub-optimal resource allocation either in a static or dynamic sense (Lall 1994b p.65). Examples of functional interventions can be seen in the provision of transport, telecommunications, education and health services. Other general interventions may also include supporting and restructuring the private sector, regional policies, and policies aimed at increasing overall export competitiveness.

Selective interventions address the more subtle types of market failure described by Stewart and Ghani (1991) concerning the creation of dynamic capacity within an economy. This has particular importance with respect to information and technology upgrading and skill formation. In the neo-classical model, from which the conventional approach is derived, knowledge and technology are freely, instantaneously, and costlessly available to all. In practice, in developing countries, nothing is further from the truth. One of the problems of Sub-Saharan Africa is the weakness of its technological capacity, a problem that does not appear to be abating. Also it is not sufficient for a nation or a firm to have knowledge of or acquire a technology; they must also be able to use it efficiently and adapt it effectively to their best advantage (Fransman 1986). However in developing countries local managers may not be familiar with, or fully understand the skills that are required to use imported techniques or technologies effectively, or the skills available to them in the workforce may not match those required for new technologies. These problems need to be addressed.

An integral part of developing long-term technological capacity is the need, as industrial-

isation proceeds, to develop an indigenous R&D capability. This takes time and must be carefully planned for in terms of skill developments and specialisms in specific areas such as engineering, material science and bio-technology. Most R& D undertaken in developing countries is informal and incremental, and generally falls into the 'development' category – but in order to incrementally upgrade both products and processes, firms must have a firm grasp of underlying technology. Research institutions can help adapt and develop appropriate industry-specific techniques and technologies so that firms can in turn utilise them as they stand, or modify them to suit their particular market demands. While some techniques and technologies may be mastered quickly and relatively costlessly, others may involve substantial outlays in both monetary and resource terms, and involve long time lags.

Under such conditions there are large potential social returns to be gained from the development of research institutes and programmes which, once operational, will provide an important channel through which firms and industries can upgrade. Without intervention these channels will simply not develop in sufficient numbers. However, most ACP countries do not have the capacity for such development, and there is a critical need for assistance in this area.

Another related, and well known, cause of market failure lies in the under-provision of education and training. Primary and secondary education may, to a large extent, be viewed as general training. Further education and skill training may be regarded as more specific. As has already been mentioned, there is a critical need for education policy to be co-ordinated with industrial development thus ensuring that skills are matched to requirements. Whilst primary and secondary education provide many of the skills required for shop floor supervision, many technologies are industry specific or process specific. With the ever accelerating pace of technological change the need for ongoing training is heightened. Individual firms, for reasons discussed earlier, have on aggregate a lower propensity to invest in training employees than is socially optimal, and therefore intervention is required to ensure its provision.

When developing technological capacity governments also have a role to play in decisions involving licensing agreements and joint ventures. In Japan, the Republic of Korea and Taiwan ROC, the state played an active role in searching for and introducing new technologies (Amsden 1985). It also played a key role as a regulatory body, and took the lead role in bargaining with TNCs (Taylor 1993).

Ongoing industrialisation requires a level of institutional capacity which is lacking in many ACP countries, and governments have a key role to play in expanding and co-ordinating its development.

The final role of governments in the area of intervention concerns market creation. Twenty five years ago Kaldor (1972) distinguished the allocative function of markets from the second, less frequently focused-on function, which he called the creative function:

> *'a creative function – as an instrument for transmitting impulses of economic change.'*

Here intervention focuses on the creation of new markets. This can be done, for example, via the state taking the lead in the creation of key upstream enterprises if the private sector is not forthcoming in their provision. The establishment of such large enterprises acts as a catalyst for the development of a host of smaller, downstream firms. This can be done either as a joint venture or, if necessary, as a state-owned enterprise. As industrialisation proceeds, or once such firms are well established, it is important that ownership and control are divested to the private sector. Such a policy, as will be discussed later, proved to be very successful in South Korea and in Taiwan ROC in the 1970s and 80s.

The case for selective interventions is strengthened if, following Bruton's analysis (1989), which may be viewed as an extension of the standard infant industry argument, developing countries in

general, particularly the least developed countries, may themselves be considered to be infant economies, and need to be protected whilst they undergo the transition period of industrialisation. This argument is heightened in a global world as these infant economies have little or no experience as global players and their fragile economies are extremely vulnerable when exposed to world markets. Under present WTO rules countries with per capita income less than US$1000 are exempt from regulations regarding selective subsidies. However some countries, e.g. Mauritius, do not fall into this category but, because of their small size and narrow range of export commodities, still need support as they attempt to upgrade and diversify.

It is worth noting that the distortions of government policies in Sub-Saharan Africa were no worse than many other developing countries and that levels of protection and weaknesses in macro policies were probably worse in Latin America. What has made the Sub-Saharan African situation so serious is the combination of these problems with a very weak technological and skill capacity in these countries, and this will not improve significantly without government intervention, both generally in factor and product markets, and selectively in clusters of related activities, increasing collective efficiency.

4.3 Government Failure

As has already been mentioned, a great deal of government failure also exists in developing countries, both in terms of failing to eliminate market failures, and in failing to create new markets and market capacity. For example, attempts by governments of developing countries to fill the gaps in financial markets with specialist development and finance institutions have a poor record of achievement both in financial terms and in terms of poverty relief (Hulme and Mosley, 1995). If governments actively engage in promoting credit to 'favoured' industries, e.g. by subsidised interest rates, distortions can be very large. Similarly if governments do not have enough information to calculate the true relative social costs/benefits of the formation of different industries, or of undertaking various projects, or enough knowledge of the existence of certain technologies, then they cannot play an effective role in co-ordinating industrial and private sector development.

Given the high potential for 'government failure' in ACP countries, there is a need for EU policy to be aimed at attempting to overcome this by concentrating their efforts in specific areas.

The present EU mandate here is wide. By reducing it, the Commission's strength and EU funds have the potential to be used more effectively. This is particularly important at this time when Europe is increasingly concerned with value for money, and when the percentage share of EU funds appropriated to ACP countries is being squeezed as Europe is expanding and strengthening links with the transition economies. The opportunity cost of not undertaking the required selective interventions is high, and more work is needed to establish priorities in these areas.

4.4 The Development of SMEs

This section will focus, using examples from Taiwan ROC, on the development of SMEs, and the role of governments in supporting their ongoing proliferation. If successfully implemented, such a policy has the potential to reduce dependence on primary commodities and help integrate an economy into the world trading system without heavy reliance on TNCs. However, the growth of manufactures by SMEs does not provide an 'easy quick-fit solution' for low income countries, and attempts to minimise the problems facing countries undertaking such an approach must be avoided. Nevertheless small firms offer potential entrepreneurs the opportunity to enter business activities without being faced with prohibitively high initial levels of investment and skills.

Traditionally, small firms have been viewed as less efficient than their large counterparts. Indeed

neo-classical economic theory only considers large firms which have the potential to benefit from scale economies and to produce under conditions of constant returns. However, industrialisation led by large-scale, assembly-line technology, together with its highly developed division of labour and stratification, is not always optimal in a developing country. Large firms, and in particular MNEs, have their place in industrialisation in developing countries, but the role of SMEs has not always been fully recognised and exploited. Over the last decade, increased awareness has led to changing consumer tastes and the need for differentiated products, and it is here that small firms are able to capitalise on their flexibility and fast response times.

Small scale production has many advantages including the potential to:

(i) combat rural depopulation and migration, thus reducing the problem of dualistic development;

(ii) enable firms to set up and develop in sectors and industries not suitable for large production i.e. in sectors where there are few scale economies;

(iii) have a large and positive effect on the distribution of income;

(iv) provide local employment, particularly for women, and give them the opportunity to enter the labour market either as employees or entrepreneurs;

(v) induce potential entrepreneurs to start up businesses on an on-going basis;

(vi) turn local savings into local investments;

(vii) absorb and adapt technology, particularly when backward linkages between larger national firms and MNEs are established, (under such conditions small enterprises are able to incrementally upgrade using appropriate technology); and

(viii) upgrade and enhance skills over a wide range of production activities.

With the help of government, support agencies and other private organisations these small firm advantages can be harnessed to play a major role in creating a manufacturing base. However, small size means that individual firms are vulnerable. Inexperienced entrepreneurs do not have the range of skills or the knowledge or information available to larger enterprises. If they are to operate successfully in global markets they need to have channels through which to sell their exports and acquire knowledge and technology.

Internationalisation and changing consumer tastes have resulted in the creation of niche markets which SMEs, with their enhanced flexibility and fast response times, are able to exploit. Deregulation has also, in some areas, had a positive influence on market penetration for SMEs, but many small firms still have problems in identifying new markets.

The gains from small-scale production are amplified when individual firms form part of a 'cluster', or co-operative, both in terms of employment and information flows (Pyke 1992). Industries such as footwear, clothing, furniture and mechanical and electrical engineering all lend themselves to small firm production, and by operating and interacting at differing levels the industry can together achieve what Schmitz (1995) called 'collective efficiency'. Collective efficiency may thus be viewed as the competitive advantage that agglomerations of small firms within a sector can derive from interaction and from local external economies. Such agglomerations are usually referred to as 'clusters', and can be both sectorally and geographically concentrated. Probably one of the most widely discussed European examples of the successful development of a cluster is the Italian footwear industry. Less well known, and more pertinent to the requirements of developing countries, is the ongoing and very successful development of industrial clusters in the Asian NICS, and particularly in Taiwan ROC, during the 1970s and 80s.

4.5 The Case Study of Taiwan ROC

No blue print for industrialisation exists. Different countries require different policies at different stages to cope with changing economic conditions. But the example of Taiwan ROC provides a host of important messages for developing countries. It demonstrates quite clearly that a manufacturing sector comprised almost entirely of SMEs can successfully lead the industrialisation process via its export success.

Taiwan ROC, is a small island located in the South China Sea. It has relatively few natural resources, and yet achieved such high levels of growth during the 1970s and 80s that many authors referred to Taiwan's growth as an 'economic miracle'. The SME sector, which accounted for over ninety five percent of Taiwan's manufacturing outlets in the 1980s has been described as the backbone of Taiwan's manufacturing and export industries. Yet, contrary to what was first believed by Western scholars and institutions in the 1980s, Taiwan's 'economic miracle' was not achieved solely by the operation of market forces, or 'get your prices right policies', but by a subtle mix of market forces and efficient and flexible government intervention.

Under the auspices of an entrepreneurial, and somewhat authoritarian government, Taiwan's industrial development was achieved via flexible planning undertaken by the government using a series of four and ten year development plans which were modified and changed in line with changing economic and political climates (see Wade 1990, Phillips 1994). Starting with the targeting of simple labour intensive exports in the 1960s, new, more advanced target industries and technically sophisticated ones were introduced over time, and comparative advantages established in the fields of electronics and computer technology. As industrialisation proceeded, the proportion of government-owned enterprises declined, and that of agriculture as a percentage of GDP gradually, yet substantially, reduced. The authoritative nature of the state enabled the government to pursue a sound and flexible macro policy and develop markets and infrastructure – thus overcoming market failures.

In the 1950s Taiwan adopted import substituting policies but, unlike so many developing countries at that time, these were relatively light, and post 1960 a vigorous outward-oriented policy has been pursued. Nevertheless some I-S industries were developed alongside export industries, this was particularly so in the post-oil shock years when export and import industries were developed in tandem, primarily to counter negative exogenous forces, and to deepen their industrial base, thus reducing outside dependence. In the 1970s, the first of currently over seventy industrial parks and three export processing zones was developed along with the establishment of science and technology research centres. These provided a major stimulus to the industrial upgrading process and, ultimately, to Taiwan's export success. This success was augmented by the government's policy with respect to foreign direct investment (Amsden 1985, Haggard 1993). The Government restricted foreign investment to key industries where the technology was vital to industrial development.

Indeed although FDI was welcomed in designated areas such as electronics, chemicals, textiles and optical instruments, other areas were screened from foreign influences (Amsden 1985). Where large scale investment was deemed necessary, and FDI unforthcoming, the government itself set up large up-stream enterprise (which it subsequently divested, partly or fully, to the private sector). These large upstream plants provided the incentive for the proliferation of smaller, downstream enterprises. At the same time there was heavy investment in education and training and latterly in research and development, to support the upgrading process. Over time Taiwan's industrial base widened and deepened and during the 1970s, 1980s and 1990s more complex technologies have been introduced, existing industries upgraded, and new ones developed. This has resulted in the creation of new dynamic comparative advantages, and export successes that are the envy of many developing and industrialised countries.

Taiwan's experience sheds light on the importance of the government in providing systematic, planned, yet flexible polices, and the need for long and medium term goals and strategies. During its developing years macro policy was tight – for example interest rates and energy prices were swiftly and substantially raised in response to the two oil price shocks (see Kuo 1983 for details). Massive investment in education was undertaken. However, expenditure on further education was co-ordinated and targeted to development needs. For example during the period 1960-69 the average percentage of students in higher education enrolled in engineering was 18%; this rose to 33.2% during 1980-89 (MOEA 1989). The number of students in social sciences followed a similar trend until 1983 when, due to a shift of emphasis, there was a dramatic fall in numbers. The late 80s and 1990 show increases in the number of students under taking management training; there has also more recently been a re-emphasis on agriculture.

A similar involvement by government in creating technological capacity can also be observed. At the beginning of 1980 government spending accounted for 60.4% of total expenditure on R&D; by 1987, as firms and private institutions began to undertake more of their own R&D (with particular emphasis on development) this figure had fallen to 50.8% (MOEA 1989).

The government also set up research institutes, and encouraged the development of both public and private organisations to support developing and upgrading industries and entrepreneurs including: The Metals Industry Development Centre (1963), The China Youth Career Organisation (1979), the Industrial Design and Packing Centre, the China External Trade Development Council (which now has offices all over the world), the China Productivity Centre, and many more.

However, perhaps the most remarkable achievement of the Taiwanese government was their ability to recognise the complimentarities between government intervention and market mechanisms. This is nowhere more apparent than in their policies directed at supporting SME development. Selective intervention may be said to have been a necessary condition for Taiwan's industrialisation and export success; it was not a sufficient one. Market forces have played a crucial and dominant role in the development of the manufacturing sector.

For historical reasons many Taiwanese businesspeople have a dislike of too much government interference, and a strong desire for independence. Cultural factors mean that strong loyalties exist between families and friends. These factors together with the lack of employment opportunities in the 1960s and the targeting of exports, provided the potential for the growth of entrepreneurship.

The role of the government here can best be described as that of facilitating, supporting and guiding market forces. By providing the necessary physical and business infrastructure, it helped create an environment in which enterprises could flourish. However selective interventions were also employed, for example, the government played an active role in creating new industries by investing in upstream enterprises and thus facilitating the development of small downstream firms, and ensuring that certain key or target industries were developed. Skill centres were developed to provide training and the changing skill requirements as industries and firms upgraded.

An array of support agencies and supply and export channels were provided by the government and the private sector enabling clusters of small firms to develop. Over time networks developed and strengthened. The government also actively engaged in promoting target industries via the provision of subsidised product development research, training, finance, and by assisting with factory designs and upgrading. Support for SMEs operating existing target industries was reduced as they developed, and new, more sophisticated industries were developed and targeted. The development of firms operating in non targeted industries was generally left to market forces, and most

of these SMEs received no specific government assistance.

Taiwan's policy towards SMEs is, however, not unique. South Korea and Japan operate a similar strategy in terms of the support systems and networking services they provide for small enterprises.

4.6 Lessons for ACP Countries

Taiwan ROC ensured that policies affecting the growth of manufacturing and exports were well co-ordinated and anticipated future needs. The government adopted an entrepreneurial attitude. It prioritised export growth and sought out and established new markets where future dynamic comparative advantages could be developed. Conditions were established, and constantly upgraded, so that the private sector could thrive. Any long term planning was flexible, allowing for upgrading and changing international conditions. The key element in Taiwan's success is that markets were allowed to work efficiently – but their establishment was managed. In short, the market sector and the government worked together in a complementary way.

4.7 Summary and Conclusions

This chapter has discussed the important and complementary roles of ACP governments, the private sector and the EU in ACP countries. It has presented the case for efficient intervention by governments, which rests on the belief that the existence of market failures means that the private sector will not develop, in the medium and long term, without some form of selective, as well as functional intervention. Globalisation has increased the pressure on ACP countries to establish a thriving private exporting sector to act as an engine of growth. This has led to changing, and to some extent reduced roles for governments and public sectors. But governments still have a vital role to play in the co-ordinating and timing of policies, particularly in education and skill training, in the development of infrastructure and institutional and technological capacity and in creating new markets. However, in many ACP countries 'government failure' also occurs, and there is a need for support in this area to overcome market failure. A new convention may wish to examine ways in which specific support can be developed for individual countries. One of the criteria for developing such capacity is the establishment of an equal working partnership between ACP governments, the Commission and the private sector. This would enable a policy framework, binding to all parties, to be jointly established and agreed on. Policies need to be forward looking and flexible, and geared towards ensuring that the private and public sectors assume their correct role in industrial development. To do this priorities must be established and targeted. Under the 'alternative approach' forwarded by this report, selective interventions would assume a high priority. However regardless of the approach taken by different countries it is necessary to target assistance, as was done in Taiwan ROC, so that SMEs can develop in sufficient numbers as to lead export growth. Policy instruments that have a high potential to facilitate small firm growth need to be employed. To achieve the greatest effectiveness, the number of policy instruments must be limited and bureaucratic procedures minimised.

References

Amsden, A. (1985), 'The Division of Labour is Limited by the Rate of Growth of the Market: The Taiwan Machine Tool Industry in the 1970s', *Cambridge Journal of Economics*, Vol 9, pp.241-54.

Biggs, T. and Levy, B. (1991), 'Strategic Interventions and the Political Economy of Industrial Policy in Developing Countries', in Perkins, D. and Roemer, M. (eds.), *Reforming Economic Systems in Developing Countries*, Harvard Institute for International Development, Cambridge, Ch.14, pp.365-401.

Brock, W., and Evans, D. (1989), 'Small Business Economics', *Journal of Small Business Economics*, Vol.1, pp.7-20.

Bruton, H. (1989), 'Import Substitution' in Chenery, H. and Srinivasan, T., *Handbook of Development Economics*, Vol.2, Ch.31.

Cawthronne, P. (1995), 'Of Networks and Markets: The Rise and Rise of a South Indian Town: The Example of Tiruppur's Cotton Knitwear Industry', *World Development*, Vol.23, No,1, pp.43-56.

Development Merit (1990, 1994), Medium and Small Business Administration Publication, Ministry of Economic Affairs, Taiwan Republic of China.

European Centre for Development Policy Management, (1996), *Beyond Lomé IV: Exploring Options for Future ACP-EU Co-operation*, Policy Management Report Number 6, European Centre for Development Policy Management: Maastricht.

European Commission, (1996), *Green Paper on Relations between the European Union and the ACP Countries on the Eve of the 21st Century: Challenges and Options for a New Partnership*, European Commission, Brussels.

Fransman, M. (1986), 'International Competitiveness, Technical Change and the State: The Machine Tool Industry in Taiwan and Japan', *World Development*, Vol.14, No.12, pp.1375-1396.

Gibb, A.A. (1993), 'Key factors in the design of small and medium enterprises (SMEs): An overview', *Entrepreneurship and Regional Development*, Vol.5, No.1, pp.73-84.

Greenaway, D. and Milner, C. (1995), *The Uruguay Round and Commonwealth Developing Countries: An Assessment*, A Report prepared for the Commonwealth Secretariat, Commonwealth Secretariat, London.

Greenidge, C. (1996), 'The African, Caribbean and Pacific Group of States: Experience of Partnership with the European Union', briefing paper, Secretariat of African, Carribean and Pacific Group of States, Brussels.

Greenidge, C. (1997), 'Return to Colonialism?: The New Orientation of European Development Assistance', *European Development Policy Study Group Discussion Papers*, Development Studies Association.

Haggard, S. (1993), *Pathway from the Periphery: The Political Growth in the Newly Industrialising Countries*, Ph.D. thesis, Cornell University Press.

Harris, J. (1990), 'Linkages between the formal and informal sectors in Developing Countries: A Review of the Literature', *Working Paper WEP 2-19/WP50*, Geneva, International Labour Organisation.

Hulme & Mosley (1996), *Finance Against Poverty*, Routledge.

Hunt, D. (1989), *Economic Theories of Development*, Harvester Wheatsheaf.

Kaldor, N. (1972), 'The Irrelevance of Equilibrium Economics', reprinted in *Economic Journal*, Dec.1982.

Kuo, S. (1983), The Taiwan Economy in Transition, (West Press/ Boulder, Colorado).

Lall, S. (1994a), 'The East Asian Miracle: Does the Bell Toll for Industrial Strategy?', *World Development* Vol. 22, No.4, pp.645-54.

Lall, S. (1994b), 'Industrial Policy: The Role of Government in Promoting Industrial and Technological Development', *UNCTAD Review*.

Lall, S. (1997), 'Coping With New Technologies in Emerging Asia', for the Asian Development Bank's 'Emerging Asia' Study.

Lall, S. and Wignaraja, G. (1997), *Mauritius: Dynamising Export Competitiveness*, Report for the Ministry of Finance, Government of Mauritius: Economic Affairs Division, Commonwealth Secretariat.

Levy, (1989), 'Export Traders, Market Development and Industrial Expansion', *Research Memorandum*, Williams College, No. 114, Williamstown, Massachusetts.

Ministry of Economic Affairs (MOEA) (1989), National Service Council, *Annual Statistics*, Taiwan Republic of China.

Pack, H. (1984), 'Productivity and Technical Choice', *Journal of Development Economics*, Vol.16, pp.153-176.

Pack, H., and Westphal, L. (1986), 'Industrial Strategy and Technological Choice', *Journal of Development Economics*, Vol.22, pp.87-128.

Pedersen, P.O., Sverrisson, A., and van Dijk, M.P., (eds), (1994), *Flexible Specialisation: The Dynamics of Small-scale Industries in the South*, London: Intermediate Technology.

Phillips, C. (1994), *Managing Markets: A Case Study of the Industrialisation of Taiwan*, unpublished Ph.D. thesis, University of Reading.

Pomp, M. and Burger, K. (1995), 'Innovation and Imitation: Adoption of Cocoa by Indonesian Smallholders', *World Development*, Vol. 23, No.3, pp.423-431.

Pyke, F. (1992), *Industrial Development Through Small Firm Co-operation*, Geneva, ILO.

Schmitz, H. (1995), 'Collective Efficiency: Growth Path for Small-Scale Industry', *Journal of Development Studies*, Vol.31, No.4, pp.529-566.

Stewart, F. and Ghani, E. (1991), 'How Significant are Externalities for Development?', *World Development*, Vol.19, No.6.

Tambunan, T. (1995), 'Rural Small-Scale Industries in a Developing Region: A Sign of Poverty or Progress, a Case Study in Ciomas Subdistrict, West Java Province, Indonesia', *Entrepreneurship and Regional Development*, Vol.6, pp.1-13.

Taylor, L. (1993), 'The Rocky Road to Reform: Trade, Industrial, Financial and Agricultural Strategies', *World Development*, Vol.21, No.4, pp.577-90.

UNCTAD, (1996), *Industrial Development Report*.

Wade, R. (1990), *Governing the Market: Economic Theory and the Role of Government in East Asian Industrialisation*, Princeton University Press: Princeton.

World Bank, (1993), *The East Asian Miracle: Economic Growth and Public Policy*, Policy Research Report, The World Bank: Washington DC.