

# The Challenge of the South

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# The Challenge of the South

KHALIL HAMDANI

## ABSTRACT

The rise of the South poses three broad challenges. The first challenge is for developing countries to seize the momentum for accelerating human development. Nearly all of the fastest-growing economies in this century are in the South, and many have an opportunity to rise from their low rankings on human development. The second challenge is to ensure that South-South trade does not replicate the traditional asymmetric pattern of North-South trade. Trade based on the import of commodities and export of manufactures can set back the industrial ambitions of Africa. The pitfalls of commodity dependence can be avoided through smart government and proven industrial policy—fostering linkages, entrepreneurship and productive capabilities – and a developmental state supportive of human development. The third challenge involves development cooperation. South-South cooperation should expand and complement North-South cooperation. The United Nations can and should make a special effort to enlist the South as a leader on development cooperation.

## INTRODUCTION

A prominent feature of our changing world is the increasing role of developing countries in the global economy. They are reshaping North-South relationships towards greater balance, and are creating new South-South linkages that open untapped opportunities for growth and development. Brazil, China and India are ubiquitous, but other developing countries too are fast catching up.

The rise of the South is not unprecedented: All geographic regions have hosted economic growth poles at some point in history. But the rise of the ‘new’ South is particularly timely, providing a much needed boost to the global economy at a dismal juncture, and sustaining progress in the developing world, which otherwise faces an uncertain prospect.

This paper examines the rise of the new South and its potential to contribute towards more equitable and sustainable human development. It traces the origins of this shift, which go back several decades, resulting in southern economies becoming dynamic drivers of trade and investment flows, and world economic growth. The paper then highlights how new technologies have facilitated the South’s rise; it is a familiar story of catch-up through cross-border exchange and learning, but the impact is proving transformational. Increasing numbers of entrepreneurs are innovating through

assimilation and adaptation to meet the needs of an expanding middle class, sustaining rapid growth in subregional markets. A concluding look at policy implications explores a major challenge to the South: seizing momentum to accelerate human development. Nearly all of the fastest growing economies are in the South; many have an opportunity to rise from their low rankings on human development.

## 1. THE RISE OF THE ‘NEW’ SOUTH

Investment, trade and economic growth in recent years have been more rapid in the South than in the developed world. A global rebalancing—a new geography—is emerging. Developing countries’ share of world trade increased from 22 percent in 1965 to 42 percent in 2010.<sup>1</sup> Their share of world exports of services rose from 18 percent in 1990 to 30 percent in 2010, and of information and communication technology (ICT) goods from 43 percent in 2000 to 67 percent in 2010. Their participation in foreign direct investment (FDI) jumped

1 The expression ‘new geography’ was used by UNCTAD Secretary-General Rubens Ricupero in 2004; ‘rebalancing’ was used by World Bank President Robert Zoellick in 2010. Trade, investment and ICT data are available on line from <http://unctadstat.unctad.org>.

from 18 percent of global inflows in 2000 to 46 percent in 2010, while FDI outflows rose from 8 percent to 25 percent.

In world manufacturing value added, their share grew from 17 percent in 1980 to 32 percent in 2010.<sup>2</sup> They accounted for two-thirds of all new researchers from 2002 to 2007,<sup>3</sup> and for more than 70 percent of the expansion in trade of intermediate products, the most dynamic component of world trade.<sup>4</sup> Their contribution to world output rose from 33 percent in 1980 to 43 percent in 2010, and they currently account for two-thirds of global growth.<sup>5</sup>

Realignments in North-South trade, investment and production have been accompanied by greater economic activity among developing countries. Trade increased among them by 12 percent and investment by 20 percent, annually, from 1996 to 2009.<sup>6</sup> South-South trade now comprises a fifth of the world total, and is the largest component of the exports and imports of the least developed countries (LDCs).<sup>7</sup> South-South FDI comprises a tenth of the global total and is a particularly important source of capital for the LDCs.<sup>8</sup> Overall, economic growth in developing countries—whether low or middle-income, or oil-exporting—is more dependent on the South than the North.<sup>9</sup>

## TRADE

Trade among developing countries has increased steadily over the past 50 years, initially within their respective regions and later across continents. The share in total exports rose from 25 percent in 1965 to 55 percent in 2010 (see Figure 1). Today, developing countries export more merchandise and manufactured goods to each other than they do to developed countries. Moreover, manufactured exports to each other are more skill and technology intensive than those to developed countries (see Figure 2). South-South exports in 2010 were 62 percent manufactured, and half were high-skill- and technology-intensive products such as cathode valves and tubes, telecommunications equipment, automatic data-processing machines, parts and accessories, optical instruments and complex chemical products.

South-South trade is largely driven by Asia, where 84 percent originates and 82 percent is marketed; 74 percent is

Figure 1: South-South trade. (Percentage share of total exports of developing countries)



Source: <http://unctadstat.unctad.org>

entirely within Asia. Latin America and Africa account, respectively, for 10 percent and 6 percent of South-South exports. The regional market is important in Latin America, however, particularly for its manufactured exports; South-South trade accounted for 39 percent of total exports in 2010. In Africa, South-South trade the same year was also significant at 41 percent of total exports; 70 percent of trade with southern countries is interregional. The LDCs in 2010 marketed 54 percent of their total exports, mainly primary commodities, in developing countries, and sourced 66 percent of their total imports, mostly manufactured goods, from the South.

Primary products account for the bulk of Asian imports from Africa and Latin America, up from 59 percent in 1990 to 80 percent in 2010, which has revived the trade and growth prospects of commodity producers. Sub-Saharan Africa is presently sustaining real GDP growth above 5 percent, with the lower income commodity exporters growing 50 percent faster than their middle-income neighbours.<sup>10</sup> Hopefully, governments have learned the lesson of ‘Dutch disease’, and will recall that commodity booms are short-lived, and can leave economies and peoples worse off without smart policies.<sup>11</sup>

10 IMF 2011b.

11 This issue is taken up again in the next section under growth spillovers and in the final policy section. Farooki 2009 suggests that the current commodity boom will be long lived.

2 UNIDO database.

3 OECD 2010.

4 Athukorala and Menon 2010, p. 8.

5 World output and growth refer to gross domestic product (GDP) measured in terms of purchasing power parity (PPP), as compiled by the World Bank and International Monetary Fund (IMF).

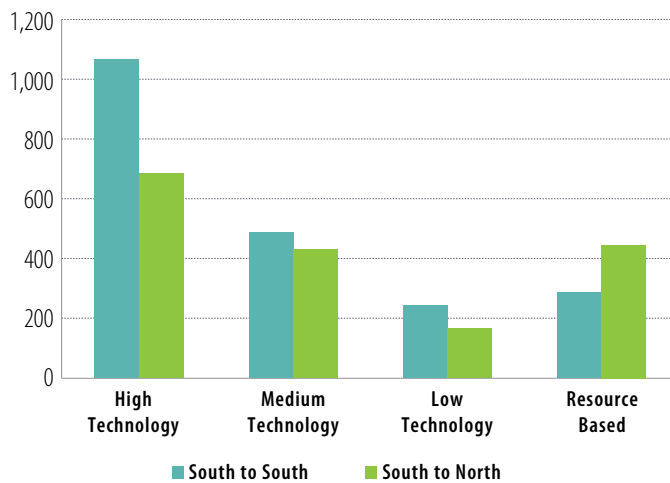
6 UNCTAD 2011b.

7 UNCTAD 2011a, chapter 2.

8 UNCTAD 2006b.

9 Garroway et al. 2010, p. 18.

Figure 2: Technology in the manufactured exports of the South (US \$ billions, 2010)



Source: <http://unctadstat.unctad.org>

## INVESTMENT

Sizeable investment flows to a greater number of developing countries in the past quarter century—expanding at a 16 percent compound annual growth rate from 1985 to 2010—have facilitated capital accumulation, technology transfer, industrialization and economic growth. FDI is not necessary or sufficient for development, but it has been catalytic in many developing countries.<sup>12</sup> Whatever their development strategy—export- or inward-oriented, state-led or market-driven—all large or fast-growing developing countries have attracted and benefited from FDI.<sup>13</sup> Investment has also flowed to resource-abundant economies, but there the impact has been uneven.<sup>14</sup>

FDI has helped propel many developing countries into world markets, diversify their exports and raise their share in global trade. A hallmark of globalization is the link between trade and investment: Two-thirds of world trade involves transnational corporations, and half of their trade occurs entirely within their corporate networks, between parents and affiliates, and among affiliates.<sup>15</sup> In this way, export-oriented FDI in developing countries has expanded their global exports and nurtured South-South trade with affiliates in neighbouring countries (see Box 1). In Asia, intra-industry

12 There is a vast literature on this subject. See, for instance, UNCTAD 1999.

13 From 1985 to 2010, the compound annual growth rates of FDI inflow were: Brazil, 15 percent; China, 17 percent; Chile, 20 percent; Hong Kong, China (SAR), 15 percent; India, 24 percent; Malaysia, 11 percent; Republic of Korea, 14 percent; Singapore, 15 percent; Thailand, 15 percent; and Turkey, 20 percent. For developing regions, the rates were: Africa, 13 percent; Asia, 18 percent; and Latin America, 14 percent.

14 UNCTAD 2007b.

15 UNCTAD 1996b.

## Box 1: Production sharing through regional networks of transnational corporations

In the 1980s, Toyota established a regional network of affiliates in Indonesia, Malaysia, the Philippines and Thailand to manufacture specific and different automobile components (i.e., transmissions, engines, electrical equipment, stamped parts and steering assemblies). These were then traded among the affiliates or with the parent for assembly and sale in local and global markets, all coordinated from regional headquarters in Singapore. Later, in 2005, Toyota opened a research and development (R&D) centre in Thailand. Production-sharing networks are popular in the automobile, electrical and electronics industries, and are not unique to developing countries (e.g., Ford manufactured its world car largely in Europe).

Regional networks transform parts and components into intermediate goods that fill out the product space and allow developing countries to trade their way up to higher value production that otherwise is typically beyond reach. Affiliates start at the labour-intensive and low-skill segment of production. Over time and with appropriate policy support (see Box 2), the more dynamic affiliates move up the value chain or acquire additional functions (e.g., R&D) and establish affiliates of their own in other relatively lower cost locations (e.g., China, Indonesia and Viet Nam). Malaysian and Thai enterprises did this by emphasizing technological learning, skill development and supplier linkages with local enterprises.

For more background on regional networks, see UNCTAD 1993b and 2005a; and on product space, see Hidalgo et al. 2007.

trade in manufactured goods, such as components for motor vehicles, electronics and electrical goods, was largely an outgrowth of industrial specialization and the regional spread of international production integrated through transnational corporations.<sup>16</sup> Initially, manufacturing in affiliates involved standardized production and assembly operations, but over time it has involved more sophisticated process technologies. One estimate of the impact is illustrative: “The surge of integrated international production networks in electronics within East Asia resulted in a high-technology export boom of nearly \$320 billion between 1995 and 2005.”<sup>17</sup>

Production sharing through intra-Asian trade enabled countries to create jobs and diversify their industrial and export

16 UNCTAD 1993b.

17 UNIDO 2009, p.115.

structures, and, importantly, to participate in technologically complex production processes of dynamic products, albeit initially in the labour-intensive segments. The benefits included learning through the knowledge network of the parent company and the buyer-supplier relationships between affiliates. National institutions and regional arrangements and associations evolved to facilitate such interactions, and collective capabilities were enhanced. The total recorded value of trade<sup>18</sup> may well have exceeded the value added of the final product, but the production-sharing business model was highly successful for the firm, the nation and the region. Countries competed for FDI and market share, even as the paramount mantra was not ‘beggar thy neighbour’ but ‘prosper thy neighbour’.

The internationalization of manufacturing was followed by the offshoring and outsourcing of services.<sup>19</sup> Traditionally, services have been non-tradable and required a physical presence in the foreign market through migration or FDI, and non-equity ties by mainly developed country multinationals (e.g., in banking, insurance, construction, air transport, shipping, and hotel and restaurant chains). Services comprised only 20 percent of world exports in 2010, and much of that was in the affluent consumer markets. But developing countries have steadily increased their share in services trade, to 30 percent in 2010. They have cashed in on the demographic dividend and serviced their own expanding consumer markets, and seized possibilities from new technologies for IT-enabled trade in services. Services range from data entry and those offered in call centres (low-skill); to back-office accounting, programming, ticketing and billing (medium-skill); to architectural design, digital animation, medical tests and software development (high-skill).

India is a big player, but others include Argentina; Bangladesh; Brazil; Chile; China; Costa Rica; Egypt; Hong Kong, China (SAR); Kenya; Malaysia; Mexico; Morocco; Pakistan; Panama; the Philippines; Republic of Korea; Singapore; South Africa; Taiwan Province of China; Thailand; Turkey and the United Arab Emirates, plus others. Many got started through the offshoring of functions within transnational corporate networks, but homegrown enterprises are active in South-South investment and trade in services, and in competing globally for the outsourcing of production from the developed countries. Enterprises there are cutting costs and improving quality by concentrating on core activities while sending non-core activities overseas.

18 Trade statistics record the value of cross-border transactions, so trade in parts and components, final products and trans-shipments are all considered separate imports/exports.

19 Offshoring takes place within corporate networks, while outsourcing involves a transfer of production to other enterprises. For more background, examples and data, see UNCTAD 2004.

The high end of services trade and investment is the internationalization of R&D to the South.<sup>20</sup> This trend is recent but indicates the South has penetrated the R&D domain of the North. The share of developing countries in the R&D expenditures of US majority-owned affiliates increased from 7.6 percent in 1994 to 18 percent in 2009.<sup>21</sup> The share of developing countries in the geographic distribution of R&D bases of Japanese manufacturing companies rose from 24 percent in 2000 to 53 percent in 2011.<sup>22</sup>

FDI in developing countries has been a forerunner to outward FDI from them (see Figure 3). In 1980, there were fewer than a thousand companies from developing countries investing overseas.<sup>23</sup> Today, one out of every four transnational corporations worldwide is based in the South.<sup>24</sup> The early pioneers were mainly Latin American (e.g., Argentines) though now these enterprises are overwhelmingly Asian.<sup>25</sup>

Although very different in size and capacity, in terms of sheer number, there are now more transnational corporations from the Republic of Korea than from Japan. China has more than the United States. China and India produced 111 new multinationals each in 2008; China added another 141 in 2009. Relative to earlier years, the new entrants are less concentrated in extractive industries and more in business services and higher value manufacturing.<sup>26</sup>

The bigger players in the South include: in mining, Vale (Brazil); in chemicals, SABIC (Saudi Arabia); in petroleum refining, Sinopec (China), Petrobras (Brazil), Petronas (Malaysia) and Indian Oil (India); in cement, Cemex (Mexico); in automotive, Hyundai and Kai (Republic of Korea); in electronics, Samsung and LG (Republic of Korea); in telecommunications, China Mobile (Hong Kong, China [SAR]) and MTN (South Africa); in port logistics, DP World and Hutchison Whampoa (Singapore); and diversified across industries, CITIC (China), SK (Republic of Korea), Tata (India) and Orascom (Egypt). There are many more (see Annex Table A). Overall, the presence of southern companies on the Fortune Global 500 ranking of the world’s biggest corporations rose from 4 percent in 1990 to 22 percent in 2011 (see Figure 4).

20 UNCTAD™ 2005b.

21 UNCTAD 2005b and [www.bea.gov](http://www.bea.gov).

22 UNCTAD 2005b and [www.jbic.go.jp](http://www.jbic.go.jp).

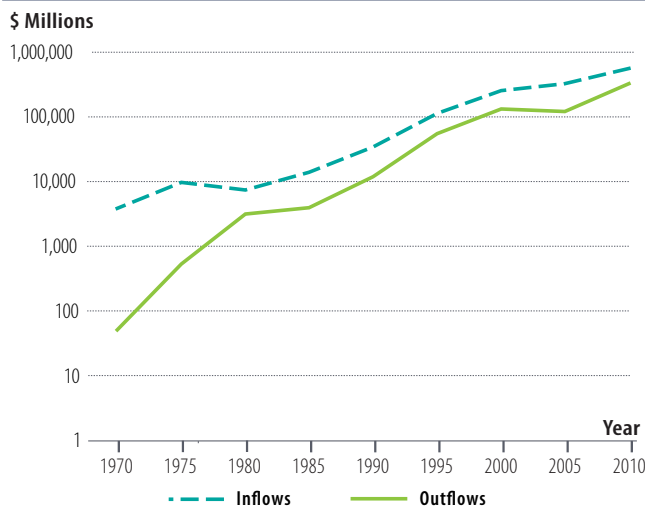
23 Wells 1983.

24 Developing countries are home to 20,238 of the estimated 77,175 transnational corporations worldwide. See UNCTAD 2006b, Annex Table A.I.6.

25 Among the largest developing country transnationals, 14 of the top 30 in 1977 were Latin American and 10 were Asian; in 2003, 40 of the largest 50 were Asian and 7 were Latin American (e.g., Brazilian and Mexican). See ECLAC 2005, p. 55.

26 PricewaterhouseCoopers LLP 2010.

Figure 3: FDI flows of developing countries



Source: <http://unctadstat.unctad.org>

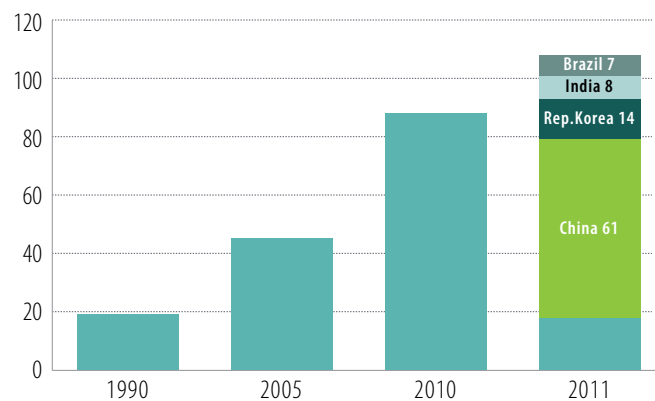
Southern enterprises are going global earlier than firms from developed countries did at a similar stage of development. They are augmenting their competitive advantages (e.g., competencies in manufacturing parts and components, and in ICT products and services) by acquiring strategic assets (e.g., brands, technology and distribution networks). The success of global buy-outs is at best an even chance,<sup>27</sup> but can provide quick learning and fast entry into world markets. A number of firms are entering niche markets, adapting products and services for affordable, mass consumption in developing countries. Indian firms are supplying medicines, medical equipment, and ICT products and services to countries in Africa; Brazilian and South African companies are doing the same in their regional markets.<sup>28</sup> Turkish firms supply Central Asian and Arab firms that are investing in their regions and Islamic countries elsewhere.

South-South FDI, like trade, is mainly intraregional and concentrated in Asia at 80 percent. Regional investments in Latin America are led by Argentina, Brazil, Chile and Mexico; South Africa is the dominant investor in Africa, accounting for more than half the total inward FDI of Botswana, the Democratic

27 The 1998 Daimler-Chrysler merger failed, but the subsequent 2009 Fiat-Chrysler partnership appears to be holding. Japanese acquisitions in America in the late-1980s have proved costly (e.g., the Mitsubishi purchase of Rockefeller Center and the buying spree by Sony in Hollywood). Luedi (2008) finds that half of 56 Chinese acquisitions from 1995 to 2007 involved some overpayment, and, on average, lost 3 percent of shareholder value; however, strategic objectives can override cost and value. The Lenovo purchase of the IBM personal computer division in 2005 was quite successful. Indian companies paid relatively high prices for European acquisitions but have managed to make these profitable (e.g., the Tata purchase of Land Rover).

28 Reddy 2011, Chapter 10.

Figure 4: Number of southern Fortune Global 500 companies



Source: Fortune Global 500, *Fortune*.

Republic of the Congo, Lesotho, Malawi and Swaziland, much in extractive industries. The major interregional flows are from Asia to Africa, with Chinese, Malaysian and Indian firms playing a prominent role. Investment flows from Asia to Latin America have risen rapidly in recent years, and in 2010 China was the third largest investor in the region and the top investor in Brazil, with investments mainly in extractive industries, but also in manufacturing, agriculture and utilities.<sup>29</sup>

South-South FDI accounts for more than 40 percent of the total inward FDI of many LDCs. There is some evidence that its impact on the host economy, through linkages with local firms, intensive use of labour, and local content and technology transfer, can be more beneficial than FDI from developed countries.<sup>30</sup>

China's role in Africa is noteworthy. The stock of Chinese FDI there rose from \$49 million in 1990 to \$1.6 billion in 2005, or by 26 percent per year.<sup>31</sup> Chinese investment flows to sub-Saharan Africa have exceeded a billion dollars annually from 2007 to 2009, much of it in resource extraction, but also in infrastructure and manufacturing. It has been accompanied by increased bilateral trade and development assistance, and the recipient countries have experienced rapid economic growth. An estimate for 13 countries comprising 78 percent of sub-Saharan Africa's GDP and absorbing 92 percent of China's FDI flows to the region from 2003 to 2009 suggests that Chinese FDI contributed to growth (see Table 1).<sup>32</sup> The

29 China invested \$15 billion in Latin America in 2010, and has FDI in Argentina, Brazil and Peru, as well as in smaller countries such as Costa Rica, Ecuador and Guyana.

30 See Kumar 1982, Wells 1983 and UNCTAD 2006b.

31 Malaysian and Indian investment grew equally fast, though much was to Mauritius. See UNCTAD 2007a.

32 Weisbrod and Whalley 2011.



Table 1: GDP growth from Chinese FDI in Africa, 2003-2009

Country	Percentage points of additional GDP growth
Angola	0.04
Botswana	0.05
Congo, D.R.	1.0
Ethiopia	0.2
Ghana	0.1
Kenya	0.07
Madagascar	0.5
Niger	0.5
Nigeria	0.9
South Africa	0.04
Sudan	0.3
Tanzania	0.1
Zambia	1.9

Source: Weisbrod and Walley 2011, Table 5.

boost of half a percentage point or more that some countries realized was significant, particularly from 2008 to 2009, when other growth impulses were dissipating.

While the rise of the new South may be most apparent in the advancement of a few large and fast-growing countries, the phenomenon is widely spread and germinating in a number of second- and third-tier developing economies. The universe of emerging economies is continuously expanding.<sup>33</sup> The new South is still in its infancy.

## 2. THE NEW SOUTH

The rise of the new South, at first glance, seems to stem from catch-up through cross-border exchange and learning from the North. In the 19th century, the backward economies of Europe caught up by borrowing technology and replicating the industrial processes of their more advanced neighbours.<sup>34</sup> This was followed by the rise of the United States and Japan. In the second half of the 20th century, the catch-up process began to

play out globally, through trade and investment flows.

Catching up is not path dependent. Its speed and character are shaped by natural potentials, institutions, social capability<sup>35</sup> and states; development paths can therefore differ fundamentally.<sup>36</sup> The new South is seemingly gravitating towards its own economic growth pole with an internal locus of control responsive to the emerging demands and circumstances of developing countries. This augurs well for global rebalancing and human development.

### THE ASIAN NEWLY INDUSTRIALIZING ECONOMIES

The Asian catch-up experience is particularly notable.<sup>37</sup> The resource-based economies of East and Southeast Asia transformed themselves from commodity producers into newly industrializing economies (NICs) in relatively short time spans, shifting their export structure from primary to manufactured goods in a decade, and towards higher-skill exports in another decade or so (see Table 2). Their success was driven by technology, though achieved in a variety of different ways.<sup>38</sup> The Republic of Korea and Taiwan Province of China fostered technology acquisition by building the capabilities of export-oriented enterprises in textiles and electronics, with differing emphasis on types of enterprise: large conglomerates (chaebols) in the former, and small and medium-size enterprises in the latter. Malaysia, Thailand and other members of the Association of Southeast Asian Nations (ASEAN) relied more on technology transfer through FDI, and on integrated international production in textiles, electronics and automotive components.

A common feature was the acquisition of technology from developed countries to establish manufacturing industries, supplemented with a full array of measures to support technological learning and upgrading (see Box 2). Such measures provided the social capability for enterprises to move up the technology ladder, from low-skill production to medium and higher-skill manufacturing, including within transnational company networks or through original equipment manufacturer (OEM) and other subcontracts. That graduation—from product assembly to component fabrication and equipment

33 In 2001, Goldman Sachs identified four BRICs (Brazil, the Russian Federation, India and China). In 2005, it expanded its scenarios to include the Next Eleven (Bangladesh, Egypt, Indonesia, Iran, Mexico, Nigeria, Pakistan, the Philippines, Republic of Korea, Turkey and Viet Nam). Ernst & Young and Oxford Economics target 25 rapid-growth markets (Argentina; Brazil; Chile; China; Colombia; Czech Republic; Egypt; Ghana; Hong Kong, China (SAR); India; Indonesia; Kazakhstan; Malaysia; Mexico; Nigeria; Poland; Republic of Korea; the Russian Federation; Qatar; Saudi Arabia; South Africa; Thailand; Turkey; United Arab Emirates; Ukraine and Viet Nam). McKinsey identifies Africa as the next growth market.

34 The classic reference is Gerschenkron 1962.

35 The importance of social capability in catching up was emphasized by Abramovitz 1986.

36 Several decades before the debate on the Washington Consensus and 'one-size-fits-all', Gerschenkron (1962) wrote: "Capitalist industrialization under auspices of socialist ideologies may be, after all, less surprising a phenomenon than would appear at first sight."

37 The Asian experience is examined in World Bank 1993, UNCTAD 1993a and UNIDO 2005, among others.

38 Country experiences are presented in Ernst, Ganiatsos and Mytelka 1998, and Lall and Urata 2003.



Table 2: Manufactured exports of Asian NICs, 1965 to 2010 (as percentage of total exports of non-oil merchandise)

Economy	1965	1975	1985	1995	2010
<i>Korea, Republic of</i>					
All manufactures	57	82	94	95	95
Medium and high-skill manufactures	4	18	27	55	72
<i>Taiwan Province of China</i>					
All manufactures	40	81	91	93	95
Medium and high-skill manufactures	10	26	36	58	72
<i>Singapore</i>					
All manufactures	39	63	77	90	96
Medium and high-skill manufactures	21	42	61	81	86
<i>Hong Kong, China (SAR)</i>					
All manufactures	92	97	96	95	96
Medium and high-skill manufactures	10	23	36	44	73
<i>Malaysia</i>					
All manufactures	5	19	36	80	80
Medium and high-skill manufactures	4	13	27	65	65
<i>Thailand</i>					
All manufactures	2	14	37	71	79
Medium and high-skill manufactures	0	3	13	42	61
<i>Indonesia</i>					
All manufactures	3	4	24	58	53
Medium and high-skill manufactures	3	3	7	11	27

Source: UNCTAD (1996a), pp. 118-119 and <http://unctadstat.unctad.org>

manufacture—encouraged outward investment and relocation of less complex production to less advanced neighbouring economies,<sup>39</sup> bolstering South-South investment and sequential growth in the new host countries of domestic firms for supplying inputs and producer services. Malaysia and Thailand became assembly and export platforms, and Singapore emerged as a regional headquarters and R&D hub for transnational corporations. Korean and Taiwanese industry produced global players like Acer, Hyundai and Samsung; the last planned to invest \$41 billion at home and abroad in 2012.<sup>40</sup>

### THE SOUTHERN BRICS

The leaders of the new South are Brazil, China, India and South Africa, or the southern BRICS.<sup>41</sup> China already has the second-largest economy in the world, Brazil the sixth-largest and India the ninth-largest; the three contributed 31 percent to world output growth in 2010. In terms of purchasing power parity, China is projected to overtake the United States

39 The flying geese (*ganko keitai*) paradigm was proposed by Kaname Akamatsu in the 1930s. For more background, see Kasahara 2004.

40 In 2011, Samsung invested more than Japan's Sony, Toshiba, Hitachi and Sharp in combination (Reuters, 17 January).

41 The leaders of Brazil, the Russian Federation, India, China and South Africa (the BRICS) meet annually. The fourth BRICS summit took place in India in March 2012.

### Box 2: Improving technological capabilities

Technological capability determines how well domestic producers *catch up* by acquiring existing technology; *keep up* by learning to use and adapt it to local demands and supplies; and *get ahead* by creating new products and process technology. Successful strategies to develop technological capabilities have emphasized:

- *Education and training*, particularly science and engineering;
- *Enterprise development*, ranging from encouraging entrepreneurship and providing small and medium-size enterprise support services, to setting up and later privatizing public enterprises;
- *Technology diffusion* through research institutions, industrial clusters, science parks and business linkage programmes; and
- *Policy support* with a broad scope, including tax incentives, financial subsidies, accounting standards and business friendly regulations, investment and export promotion, and government procurement. The mix, sequence and duration of policies also matter.

Policy support can be:

- *Vertical* (e.g., picking winners, targeted incentives and preferential schemes for choice industries) and
- *Horizontal* (e.g., competition policy, industry standards, privatization, streamlined regulations and overall improvement of the business environment).

For a review of country experiences see, among others, UNCTAD 1996a; Ernst, Ganiatsos and Mytelka 1998; Lall and Urata 2003; and UNIDO 2005.

as having the largest economy within the next five years, and India is expected to have the third-largest.<sup>42</sup> The performance of these countries is especially impressive as they are all relative latecomers. It was only in the 1990s that they began to emerge on the world economic scene, and they have done so in different ways: Brazil on the strength of natural resources, China through manufacturing and India via services.

China's industrial performance is unrivalled: Its share of world industrial output tripled in the 1990s, rising from 2 percent to almost 7 percent. This was largely driven by investment, with significant inward FDI in special zones

42 IMF (2011b) projections indicate that China could overtake the United States in 2016; World Bank (2008) projections indicate that this could occur in 2018.

and ‘flying geese’ investments from the NICs.<sup>43</sup> FDI from developed countries was more market-seeking, while FDI from Asian economies was more export-oriented with lower capital intensity.<sup>44</sup> China’s exports boomed in the 1990s, and their composition shifted towards manufactured and more skill-intensive products (see Table 3); indeed, China is now the world’s largest exporter of high-technology goods,<sup>45</sup> though these have high import content reflecting China’s emergent role as final assembler in East Asia’s production-sharing networks.<sup>46</sup> Industrial growth is increasingly technology-driven, as China is promoting technology diffusion and R&D in its state enterprises, and is acquiring process technology and corporate brands through global buy-outs.<sup>47</sup> As production has moved up the technology scale, labour-intensive manufacturing has begun to relocate to other Asian countries (e.g., Pakistan and Viet Nam) and also to Africa.

In comparison, India’s performance has been driven more by the services sector, entrepreneurship and domestic markets. While manufacturing expanded (in output, exports, productivity and skill intensity), the services sector did better. Productivity in services—which generally include activities with low productivity potential—grew by 5.6 percent annually in the 1990s, and exports of services grew by 26 percent. Services accounted for a third of total exports in 2010, twice the share in comparator countries (see Table 4). ICT and graduates from the Indian Institutes of Technology enabled sizeable offshoring of professional and business services from developed countries. The spontaneous rise of high-tech ICT clusters in Bangalore, formed by entrepreneurs and the private sector, attracted significant FDI, including for skill-intensive R&D activity. More than half of current FDI inflows are from developing countries, with, for example, Singaporean firms active in telecommunications, shipping and oil refining, and Malaysian companies involved in construction and utilities. Indian companies have ventured overseas since the 1960s, initially in textiles and trading in developing countries but now

Table 3. Manufactured exports of southern BRICS, 1990–2009 (Percentage of total exports of merchandise)

Economy	1990	2000	2009
<i>Brazil</i>			
All manufactures	75	77	65
Medium and high-skill manufactures	30	37	26
<i>India</i>			
All manufactures	80	84	88
Medium and high-skill manufactures	14	17	25
<i>China</i>			
All manufactures	76	92	96
Medium and high-skill manufactures	26	41	58
<i>South Africa</i>			
All manufactures	26	61	68
Medium and high-skill manufactures	8	24	32

Source: UNIDO (2005, 2009, 2011), Annex tables.

in a broad range of industries,<sup>48</sup> with strategic acquisitions in developed countries,<sup>49</sup> and acquisitions and greenfield investments in developing countries, particularly in Africa. On current trends, India could overtake China, from 2018 onwards, as the largest source of new multinationals from the South.<sup>50</sup>

Already in 1990, Brazil was producing 2.5 percent of world industrial output—more than China or any other developing country—due to a large market, ample natural resources, a diversified manufacturing base and significant FDI (being the largest host developing country in the 1970s). But its promise as a global player is based on its performance since then. In the 1990s, Brazil initiated key policy measures such as constitutional amendments that fully opened the domestic market to the private sector; liberalization of the trade regime, which encouraged large companies and foreign subsidiaries to be more efficient, upgrade and subcontract to local suppliers; privatization to revive public utilities and infrastructure; and the creation (with Argentina, Paraguay and Uruguay) of the Mercosur customs union.

There was a surge of investment inflows into services (e.g., telecommunications and electric utilities); manufacturing,

43 Manufacturing absorbed 60 percent of FDI inflows, and manufacturing productivity (i.e., output per worker) grew at 14.7 percent annually from 1997 to 2000. See UNCTAD 2005a, p. 31.

44 Wang 1997 and Yao 2003.

45 Woo 2012.

46 The import content of China’s high-technology exports was estimated at 48.5 percent in 2005. See Riad et al. 2012, Figure 10.

47 Examples include the 2005 purchase by Lenovo of the IBM personal computer division, and the 2010 acquisition of Volvo by Geely. In 2006, Lifan bid for an entire BMW-Chrysler engine factory in Brazil, with the intent to take it apart and ship it home for reassembly in China.

48 These include ICT (e.g., Infosys, WIPRO and Tata Consultancy Services), pharmaceuticals (e.g., Ranbaxy, Sun Pharmaceuticals and Biocon), food and beverages, consumer goods, automotive (e.g., Tata Motors), metals (e.g., Tata Steel), energy (e.g., Tata Power and the state Oil and Natural Gas Corporation), finance and insurance, entertainment and broadcasting (e.g., Reliance Entertainment), construction and telecommunications (e.g., Bharti Airtel and Essar). See Satyanand and Raghavendran 2010.

49 For example, Tata Motors purchased Jaguar and Land Rover from Ford in 2008.

50 PricewaterhouseCoopers LLP 2010.

Table 4: Services exports of southern BRICS, 1990 to 2010 (merchandise and services percentage of total exports)

Economy	1990	2000	2010
<i>Brazil</i>	11	15	14
<i>India</i>	20	28	36
<i>China</i>	9	11	10
<i>South Africa</i>	13	14	14

Source: <http://unctadstat.unctad.org>

including in integrated international production and the manufacture of medium and high-technology exports (e.g., motor vehicles and digital equipment); and the primary sector (e.g., petroleum and mining). A number of state-owned and later privatized enterprises became global players, such as the mining giant Vale and the aircraft manufacturer Embraer.<sup>51</sup> Brazilian companies have production in some 80 countries, mainly in Latin America, with the major southern investments being in Argentina and Uruguay.<sup>52</sup>

South Africa underwent a similar transformation in the 1990s, but under very different circumstances, given the challenge of shaping a post-apartheid economy. Today, South Africa is a major investor in Africa in a range of industries, including mining, metals, chemicals, paper, retail and trade, finance, media, telecommunications, transport and utilities). South African investments in banking (e.g, Standard Bank), telecom (e.g, MTN) and infrastructure (e.g., Eskom, Transnet) have energized entrepreneurship, subregional markets and trade in East and Southern Africa, and also drawn Indian and Chinese investment there.

### THE OTHER SOUTH

The rising South, of course, encompasses countries beyond the NICs and the southern BRICS. In Asia, there are the ASEAN countries, and in West Asia, there are Kuwait, Saudi Arabia, Turkey and the United Arab Emirates. Latin America has Argentina, Chile, Colombia, Mexico and Venezuela; Africa has Egypt and Nigeria. All of these countries had sizeable investment and trade activity in the past decade, within their regions and globally (see Table 5). With one exception, they all had a medium or higher ranking on human development.

Even in countries with low levels of outward investment, firms, generally small enterprises, invest in other developing

Table 5: Largest development economy investors, 2010 (all developing economies with outward FDI stock over \$5 billion)

Economy	Outward FDI (\$ billion)	Share of world exports (%)	Share of world manufacturing value added (% 2009)	HDI
<i>Hong Kong, China (SAR)</i>	948	2.6	0.08	0.862
<i>Singapore</i>	300	2.3	0.45	0.846
<i>China</i>	297	10.4	14.45	0.663
<i>Taiwan Province of China</i>	201	1.8	1.68	0.663
<i>Brazil</i>	180	1.3	1.66	0.699
<i>Korea, Rep. of</i>	138	3.1	3.16	0.877
<i>Malaysia</i>	96	1.3	0.54	0.744
<i>India</i>	92	1.5	1.69	0.519
<i>South Africa</i>	81	0.6	0.40	0.597
<i>Mexico</i>	66	2.0	1.42	0.750
<i>United Arab Emirates</i>	55	1.3	0.24	0.815
<i>Chile</i>	49	0.5	0.24	0.783
<i>Panama</i>	31	0.0	0.02	0.755
<i>Argentina</i>	29	0.5	0.93	0.775
<i>Qatar</i>	25	0.5	0.03	0.803
<i>Thailand</i>	25	1.3	0.93	0.654
<i>Turkey</i>	23	0.8	1.04	0.679
<i>Colombia</i>	22	0.3	0.28	0.689
<i>Venezuela</i>	19	0.4	0.37	0.696
<i>Kuwait</i>	18	0.4	0.09	0.771
<i>Saudi Arabia</i>	16	1.6	0.42	0.752
<i>Libya</i>	13	0.3	0.02	0.755
<i>Bahrain</i>	7	0.1	0.03	0.801
<i>Lebanon</i>	7	0.0	0.04	0.737
<i>Philippines</i>	6	0.3	0.34	0.638
<i>Egypt</i>	5	0.2	0.39	0.620
<i>Nigeria</i>	5	0.5	0.05	0.423

Source: For FDI and trade data, <http://unctadstat.unctad.org>; for manufacturing value added, UNIDO 2011; for the HDI, UNDP 2010.

countries, mainly those that are close by or culturally familiar (see Table 6).

The overall picture is of an increasingly vibrant and interconnected South. Moreover, these changes are happening much faster than ever before, as the new South eases the rise of other developing countries by enlarging their opportunities for growth and development through growth spillovers and market multipliers.<sup>53</sup>

51 UNCTAD 2001.

52 The biggest investments are in developed countries (Denmark, Spain, the United States and others). See Lima and Barros 2009.

53 Conceptually, growth spillovers are from a country or group to another, while market multipliers occur within a country or group; these processes are concurrent in practice.

Growth spillovers occur as South-South trade, investment, financial flows and technology transfer augment growth and productivity in partner economies.<sup>54</sup> Asia's growth and import demand for natural resources has sustained a prolonged commodity boom since 2003, benefiting exporters in Africa and Latin America, and particularly contributing to their above-average economic growth rates in recent years.<sup>55</sup> Asian FDI in Africa has been accompanied by industrial technology and expanded utility infrastructure and telecommunications, the essential backbone for ICT connectivity and use. Mobile phone penetration in the South is approaching saturation, and Internet use is rising fast.<sup>56</sup> Official financial flows and public-private partnerships have reinforced developmental effects.<sup>57</sup>

Estimates suggest that these growth spillovers are positive, significant, increasing and robust in the face of global shocks. One IMF staff study of long-term growth trends over 1988 to 2007 finds positive growth spillovers from China to other countries, particularly for close trading partners; a 1 percentage point increase in Chinese growth correlates, on average, with an increase in growth of 0.5 percentage points in other countries.<sup>58</sup> Another IMF study that encompasses Brazil, China and India also finds significant positive spillovers, and estimates that growth in low-income countries would have been 0.3 to 1.1 percentage points lower from 2007 to 2010 if growth in the southern BRICS had fallen at the same rate as in the developed economies.<sup>59</sup>

Market multipliers can result from technology diffusion; economies of agglomeration in consumer demand; network externalities from entrepreneurship; and emulation effects in public policy. Technology, as discussed earlier, was essential to the manufacturing and export success of the new South, and its diffusion through South-South investment in

54 Negative effects are also possible and include competition in import industries, exchange rate movements adverse to the nontradable sector and crowding out of indigenous enterprises.

55 Ademola, Bankole and Adewuyi (2009) argue that the negative effects can outweigh the positive effects for many African countries, as the underlying trade pattern does not contribute to industrial development in the absence of accompanying policy measures. This is discussed in the next section.

56 UNCTAD 2009.

57 Benefits in Africa include a 35 percent increase in the supply of electricity, a 10 percent improvement in rail capacity and lower telephone costs. See IMF 2011a, p. 27.

58 Arora and Vamvakidis 2010. Similar results are reported by Garroway et al. 2010.

59 IMF 2011a. The study defines the BRICS as Brazil, the Russian Federation, India and China; however, the Russian Federation has relatively minor trade and investment links with low-income countries, and the focus is on the southern BRICS.

Table 6: South-South investment of developing countries with low outward FDI (\$ million, stock of outward FDI in 2009 or 2010)

Country	Investment to (main destinations)	Amount
<i>Bangladesh</i>	India, United Arab Emirates, Sri Lanka, Pakistan	98
<i>Botswana</i>	South Africa, Zimbabwe, Tanzania, Lebanon	400
<i>Costa Rica</i>	Guatemala, Panama, El Salvador	313
<i>El Salvador</i>	Nicaragua, Guatemala, Costa Rica, Honduras	7
<i>Mauritius</i>	Seychelles, Madagascar, Mozambique, South Africa	72
<i>Mozambique</i>	Kenya, Zimbabwe, Malawi, South Africa, Mauritius	2
<i>Pakistan</i>	United Arab Emirates, Bangladesh, Qatar, Sri Lanka	555
<i>Peru</i>	Chile, Brazil, Bolivia, Panama	1,200

Source: IMF, Coordinated Direct Investment Survey, <http://cds.imf.org>. The selected countries include all developing country participants in the survey with low levels of outward investments (\$1.5 billion or less).

ICT connectivity infrastructure and trade in affordable ICT products (see Box 3) is lowering the threshold for economic activity, unleashing the entrepreneurial spirit across income classes and cultivating subregional markets, particularly in Africa. Affordable, Asian-built mobile phone handsets allow leapfrogging over landlines and have multiple uses. Cellular banking is cheaper and easier than opening a bank account; farmers can obtain weather reports and check produce prices; and entrepreneurs can provide business services through kiosks. Mobile phone diffusion is so rapid that IBM predicted in 2011, "The digital divide will cease to exist in 5 years: on current trends, 80 percent of the current world population will have a mobile device."<sup>60</sup>

Economies of agglomeration in consumer demand occur in countries with large populations and wide disparities in income. Foreign companies enter the market at the high end with products designed for their home market, neglecting the consumer market on the low end that innovative domestic companies can capture with affordable versions of the products, re-engineered and adapted for local tastes and incomes.<sup>61</sup> The consumer markets in China and India have adequate mass for the production of both luxury and affordable goods, and, indeed, these flourish side by side in a range of industries—food and beverages, clothing, home appliances, motor vehicles, hotels and others. The domestic companies create consumer surplus for the 'bottom billion'. They also generate jobs and develop producer capabilities,

60 IBM 2011.

61 This can give rise to intellectual property disputes when the local product is an outright imitation or sold (even exported) under unlicensed brands. Standards are also an issue.

### Box 3: Product development for markets in developing countries

- Companies based in the South are developing innovative, technology-intensive products for large consumer markets with low purchasing power:
- In 2004, TI India, an R&D centre of Texas Instruments (TI) in Bangalore, designed a single-chip prototype for manufacturing high-quality, low-cost mobile phones in large volume by the Indian companies BPL and Primus.
- In 2005, Nokia, in cooperation with TI, began to market the Indian-made one-chip handsets in India and Africa, achieving sales of 20 million in the first nine months.
- Single-chip designs have also emerged from the Philips, Qualcomm and National Semiconductor R&D centres in India, and are used for other devices, including affordable digital display monitors and medical ultrasound machines. Intel India developed, and a Taiwanese OEM is manufacturing, a handheld device to enable door-to-door rural banking in villages.
- In 2007, WIPRO Infotech marketed a low-power desktop for basic computing and Internet connectivity.
- In 2008, Tata announced the ultra-low-cost Nano family car based on 34 new modular-design and manufacturing patents. It will be exported to developing countries in kits to be assembled and serviced by local entrepreneurs, requiring basic mechanical skills comparable to those for a bicycle.

Source: Reddy 2011, Chapter 10

with the more productive firms emerging as exporters and investors overseas.<sup>62</sup> India's pharmaceutical industry has spawned cheap but quality generic medicines and also global players (e.g., Ranbaxy).

This pattern of technological diffusion across income classes and consumer groups represents a shift in the traditional techno-economic paradigm.<sup>63</sup> In North-South relations, the NICs developed technological capabilities for export success in developed country markets, and focused on manufacturing complex products efficiently. In South-South relations, southern companies have found opportunities to adapt and innovate so that products and manufacturing processes better suit the needs of their own and other emerging

markets. Thus, companies like Tata Motors are manufacturing complex automobiles (e.g., Jaguar) for northern markets and an affordable car (e.g., the Nano) appropriate for southern ones.

The built-up R&D capabilities in the southern BRICS make them natural hubs for absorbing existing technologies, and engineering new products and uses for application at home and export to other southern markets (see Figure 5). Under the 2005 GSM Emerging Markets Initiative, manufacturers in India reduced the price of mobile handsets by more than half, and expanded the GSM (global system for mobile communications) subscriber base by 100 million connections per year; this in turn has stimulated investments in telecommunications networks. In 2007, mobile operators (including South Africa's MTN and Kuwait's Zain) announced a five-year plan to invest an additional \$50 billion in sub-Saharan Africa to improve and expand mobile coverage to 90 percent of the population, or some 670 million persons. This could raise annual GDP growth by as much as 2 percentage points.<sup>64</sup> The South-South pattern of technology diffusion often entails firms pursuing business models based on low margins but aimed at reaching large numbers of lower income communities in markets with weak support infrastructure. At home and abroad, this model empowers people, creates additional investment opportunities and raises living standards.

Network externalities can arise from the dynamic interaction of technology, entrepreneurship and markets. People tend to be self-organizing, creating buyer-seller relationships, becoming entrepreneurs to fill unmet needs and spontaneously sprouting markets. People with cell phones do these things more easily and rapidly, and when they do, network externalities result in larger welfare gains for all users and non-users. For example, fishermen with mobile handsets in Kerala, India, rationalized the delivery of their catch to local markets with information on demand-supply conditions, leading to better market functioning for all fishermen and adding to collective social welfare.<sup>65</sup> The use of cell phones in Niger has improved the performance of the grain market, the behaviour of traders and consumer welfare;<sup>66</sup> Ugandan farmers have used mobile phones to get higher prices for their perishable bananas.<sup>67</sup> Commercial service providers are

<sup>64</sup> See: Reddy 2011, Chapter 10, and [www.gsma.com](http://www.gsma.com) for growth projections.

<sup>65</sup> Jensen 2007.

<sup>66</sup> Aker 2008.

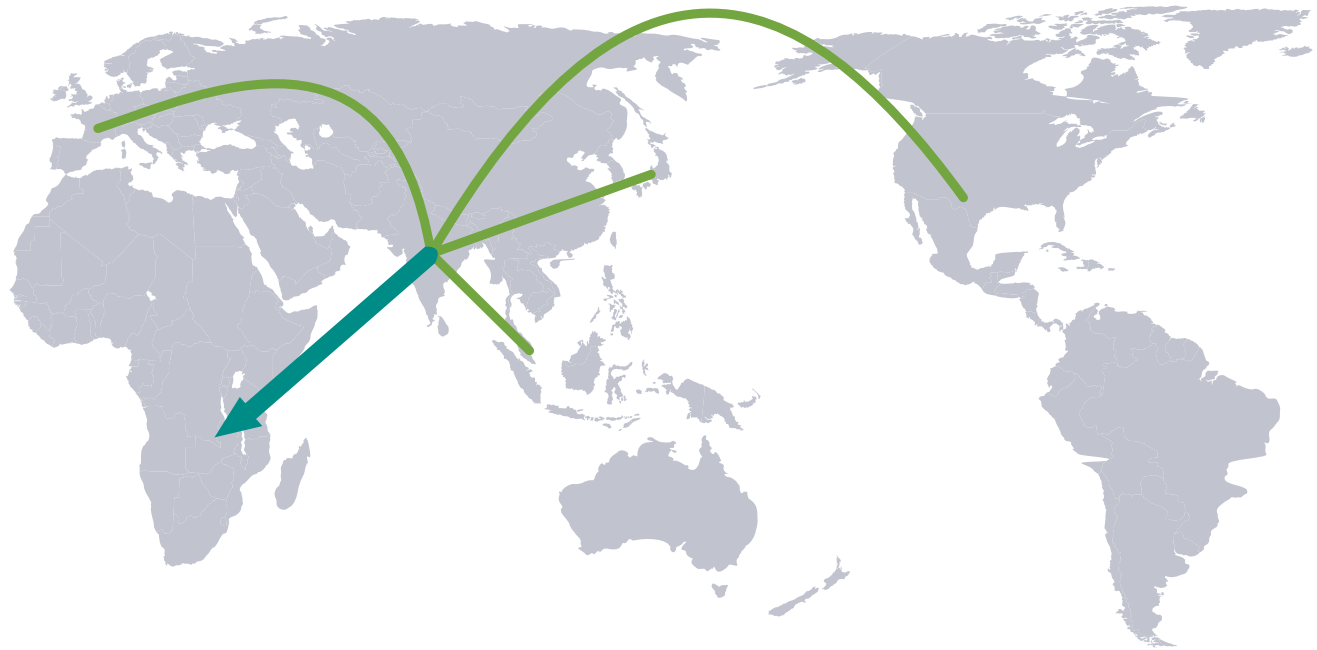
<sup>67</sup> For a review of these and other studies, see Jensen 2009, and Aker and Mbiti 2010.

<sup>62</sup> See Demirbas, Patnik and Shah 2010.

<sup>63</sup> The extensive literature on technological diffusion includes Freeman and Perez 1988, and Perez 2001.



Figure 5: Technology diffusion to Africa via India



The emerging pattern of global technology diffusion involves assimilation, adaptation and innovation in southern technology hubs, and onward diffusion in products more suited to the demands and circumstances of developing countries. Brazil and China are also technology hubs, as well as other developing countries.

profitably offering market information to smallholder farmers through low-cost mobile subscriptions.<sup>68</sup>

Network externalities also arise from interactions between companies and community stakeholders to create shared value.<sup>69</sup> Innovation and its benefits spread quickly and widely among communities and within regions, spawning faster change.<sup>70</sup> These transformations multiply the possibilities of what people can do with technology in areas that include: participation in decisions that affect their lives; quick and low-cost access to knowledge; the spread of cheaper, often generic medicines, better seeds and new crop varieties; and new

employment and export opportunities. These possibilities cut across income classes, reaching down to grass-roots levels.<sup>71</sup>

Improved public policy helps ensure that best practices spread and have significant multiplier effects. For example, many African governments have adopted policies to emulate Mauritius's early success in attracting Asian FDI by creating export processing zones. Malaysia's investment promotion policies have been widely replicated, including such concepts as 'win-win', 'public-private dialogue' and 'smart partnerships'. In a number of countries, 'client charters' adopted by state institutions have improved the quality, cost and administration of public services. Generally, there is greater worldwide appreciation of a broader role of the state in stimulating R&D and nurturing synergies from tripartite cooperation among private, university and public research institutions, and also of the importance of an effective state. Shared experiences broaden options for public policy and development strategies, and foster pragmatic leadership.

68 More than 200,000 Indian farmers subscribe to Reuters Market Light for \$1.50 per month, collectively generating income of \$2-3 billion and additional savings on agricultural inputs; for this and other examples, see the World Bank site [www.infodev.org/en/index.html](http://www.infodev.org/en/index.html).

69 Examples include the social business enterprise initiatives by Grameen, which worked with companies in Bangladesh to tap the latent demand of poor consumers for basic nutrition and footwear. For a review of the literature on social business enterprise, see Edwards 2009.

70 Network externalities can also impede change. For example, India's caste system has restricted men to working in traditional occupations, even as wider opportunities have opened up for women in the same cohort. See Munshi and Rosenzweig 2006.

71 UNDP 2001.

### 3. POLICY IMPLICATIONS

The new South is a promising force for more equitable and sustainable human development. The gap in human development between developed and developing countries narrowed by 25 percent from 1970 to 2010, with much of the catch-up since 1990.<sup>72</sup> Poverty is declining in all developing regions.<sup>73</sup> The faster growth of developing countries is an opportunity for quicker progress, particularly in the least developed economies.

The global prospect is uncertain, however, and the economic downturn in the North affects the South. It depresses North-South exchanges as well as South-South trade, which to a large extent depends on final demand in developed countries.<sup>74</sup> At the same time, there is potential to sustain growth and better leverage it, internally and globally.

#### SUSTAINING GROWTH

The economic slowdown in developed countries is an opportunity for the new South to shift gears, and rely more on regional and domestic demand to sustain future growth. Already, developing countries trade more among themselves than with the North. Regional trade is growing faster than world trade, is generally more dynamic (i.e., involving manufactures and greater technological content), and has the potential to expand further if recent initiatives bear fruit (see Box 4). There is scope to strengthen regional trading and investment arrangements—there are more than a dozen regional integration groups in Africa alone—by practical measures such as streamlining transit, transport and customs procedures, and harmonizing national regulatory schemes. There is also scope to lower tariffs on South-South trade in final products, which are higher than for North-South trade, with significant reward: a welfare gain for the South of \$59 billion.<sup>75</sup> A more ambitious proposal involves the recycling of Asian savings into African investments (see Box 5).

Perhaps the most important engine of growth for the South is the domestic market. The middle class in Asia is large, and rapidly growing in size and income. One indicator of rising prosperity is the dramatic growth in Asian tourism.<sup>76</sup>

72 As measured by the HDI. See UNDP 2010, p. 29.

73 World Bank 2012.

74 The final demand for South-South trade in parts and components through production sharing is set in developed countries (Athukorala 2011).

75 OECD 2010 estimates a welfare gain for the South of \$59 billion if South-South tariffs were lowered to North-South levels.

76 UNWTO 2006 predicts that China, by 2020, will be the world's fourth-largest tourist-generating country, with some 100 million outbound tourists.

Another is the trend among transnational corporations to target developing countries for global revenue growth.<sup>77</sup> Since 2008, Chinese, Indian and Turkish firms in the apparel sector have been shifting production from shrinking global markets to expanding domestic ones.<sup>78</sup> Kharas (2010) suggests an optimistic scenario of global recovery led by the middle classes of China and India, which are seen as sufficiently large to make up for the slack in external demand from the weakening developed economies.<sup>79</sup> Regardless, the changeover in growth strategy towards greater reliance on domestic markets would further boost internal dynamism and contribute to more inclusive growth. For these reasons alone, the time may be ripe to accelerate institutional changes and public services to promote aggregate consumption.<sup>80</sup> A number of Asian economies, in the words of the IMF, “can afford to deploy additional social spending to support poorer households.”<sup>81</sup>

#### LEVERAGING GROWTH

Sustained, rapid growth of Asian economies should continue to spill over to other developing countries in Latin America and Africa, where the major policy challenge is to capture the full benefits through market multipliers among suppliers and consumers.

Sub-Saharan Africa is projected to maintain real GDP growth above 5 percent in 2012-2013.<sup>82</sup> Commodity producers could continue to enjoy high prices and demand for their exports, and consumers are expected to benefit from increased imports of affordable Asian products such as household appliances, mobile phones, electrical goods and vehicles. Flourishing local markets could breed entrepreneurs and attract large Asian investment, in extractive industries as well as infrastructure, telecommunications, finance, tourism and manufacturing, particularly light manufacturing industries in which African countries have latent comparative

77 “For those companies that derived more than 5 percent of their revenues from emerging markets, the share reporting better financial performance than that of their peers was 39 percent. By contrast, among the companies that derived less than 5 percent of their total revenues from activities in emerging markets, only 28 percent reported their financial performance as being better than that of their peers.”

78 See Cattaneo et al. 2010.

79 Kharas (2010), maintains: “I suggest that this new Asian middle class is large and growing rapidly, and that it is of sufficient size to provide the impetus for demand growth that the world needs” (p. 38).

80 Since 2009, new investment in China has been higher, on average, in the domestic nontradable sectors, with increased public expenditures on infrastructure and services (health, education, housing and social security). See World Bank 2011. A similar emphasis is placed in the 2012 budget of Hong Kong, China (SAR).

81 IMF 2012, p. 7.

82 Ibid., Table 1.



**Box 4: Recent regional arrangements in the South**

The Asia Free Trade Zone became operational on 1 January 2010. It encompasses 1.9 billion people in 11 countries: Brunei, Cambodia, China, Indonesia, Lao People's Democratic Republic, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Viet Nam. It aims at 100 percent tariff-free trade by 2015. Initially, the more developed member countries (Brunei, China, Indonesia, Malaysia, Philippines, Singapore and Thailand) are removing duties on 90 percent of their imports from other members in the zone. Tariffs on the remaining 10 percent, involving products in agriculture, auto parts and heavy machinery, will be removed subsequently. The less developed countries

(Cambodia, Lao People's Democratic Republic, Myanmar) have until 2015 to lower tariffs gradually. Trade in this new Asian zone amounted to \$192.5 billion in 2008, third in value and volume after the European and North American free trade zones.

The East African Common Market was launched on 1 July 2010, and encompasses Burundi, Kenya, Rwanda, Tanzania and Uganda. It allows free movement of capital, people and goods within their collective borders. The common market aims to become a monetary union by 2012, with a common currency by 2015.

The South Asian Free Trade Area was agreed on 6 January 2004 and encompasses Afghanistan, Bangladesh, Bhutan, India, the Maldives, Nepal, Pakistan and Sri Lanka. Trade is limited, but could expand dramatically with the 2011-2012 commitments between India and Pakistan to grant each other most-favoured nation status and allow cross-border investment.

advantages.<sup>83</sup> In this scenario—which has already played out in the past decade and in other regions—host economies would undergo structural changes, and indigenous industry would need to respond to competitive pressure from imports and investment inflows by upgrading production. This process is proving difficult in Africa,<sup>84</sup> however, more so than in Asia or Latin America, where technological capacities, infrastructure and social capability are relatively better developed.

83 Dinh et al. 2012 suggest that light manufacturing has the potential to create millions of productive jobs in Africa.

84 Ademola et al. 2009 review various studies and conclude that there is a strong consensus that African producers of manufactured products are severely threatened by competition from Chinese exports in the domestic, intra-African regional, and global market spheres, in spite of import barriers in the domestic market and special trade preferences offered in both regional and global markets.

**Box 5: Recycling Asian savings into African investments**

“Asia has to find new sources of growth,” says Changyong Rhee, Chief Economist of the Asia Development Bank, adding: “Industrial countries are unlikely to drive global demand and growth any time soon. In addition to increasing domestic consumption in Asia, strengthening South-South links through recycling of savings to investment in the less affluent South can take up the slack.”

He elaborates: “Hosting manufacturing industries, which the North previously exported to Asia, could be a new stimulus for African growth, for example. Using savings from the South for investment through industry migration rather than holding them in safe assets in the West will contribute to the stability of the global economy by promoting global rebalancing.”

Source: Rhee 2011.

Therefore, future growth will need to be leveraged with policies to deepen linkages between trade and the wider economy, and promote human development.

A major hurdle is the enclave character of extractive industries, which for the host country reduces potential gains from South-South trade and investment to economic rents, and poses the risk of Dutch disease.<sup>85</sup> However, industry and country experiences—in Brazil, Chile, Indonesia, Malaysia, and Trinidad and Tobago, among others<sup>86</sup>—suggest that the primary sector is amenable to extensive and sizeable backward and forward linkages, and can generate sustained, widespread growth.<sup>87</sup>

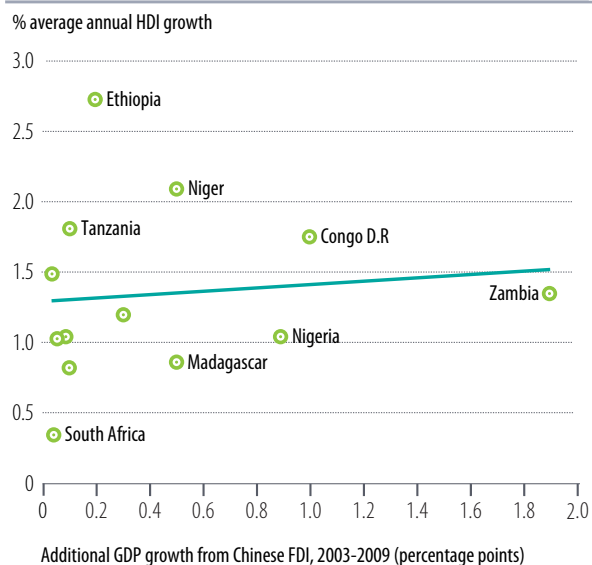
In addition, the trend in global value chains is for transnational companies to source inputs locally, by providing credit and technology to upstream suppliers to improve quality, and ensure adequate and timely supply, and in the process to create shared value within the community. Agro-industry, upstream suppliers, logistics infrastructure and demand for a variety of services (e.g., food, construction, repair and maintenance) can create jobs, income and learning, as well as entrepreneurs who jumpstart a new cycle of innovation

85 Nigeria was afflicted by Dutch disease during the 1970s oil boom, when large inflows of dollars appreciated the naira and made exports of cocoa, groundnuts and other non-oil products uncompetitive. In addition, the rents on oil flowed out in capital flight rather than into productive investment, an aspect of the so-called resource curse.

86 Including developed countries such as Australia, Canada, Finland, New Zealand, Norway, Sweden and the United States.

87 Kaplinsky 2011 presents the synergies between commodity specialization and industrial development, and also a critique of the literature on the resource curse.

Figure 6: Human development and growth spillovers



and economic activity, and additional investment inflows. The extent of value added depends on local capacities. In Zambia, the copper mining industry has local supply chains of service providers. In Ghana, gold mining has created more extensive linkages and industrial districts. In South Africa, domestic mining companies have become regional and global industry players.<sup>88</sup> An encouraging sign is that increasing Asian investment in African commodities has fewer enclave characteristics; another is that the new generation of African leaders is more aware and supportive of a developmental state.

Africa's new leadership is increasingly pragmatic and proactive. Pragmatism is evident in the many governments with sound macroeconomic policies and institutions, and open regimes. Proactive approaches can be found in the emerging priorities of industrial policy: promoting entrepreneurship and private sector development; strengthening institutions for technological upgrading, education and skill formation; creating finance and credit facilities for small and medium-size enterprises; providing support for industrial clusters and economic zones; and expanding regional trade and investment.<sup>89</sup> Sound macroeconomic policy helps manage the dangers of large foreign exchange inflows (i.e., Dutch disease), while smart industrial policy helps deepen linkages and enhance market multipliers. These policy trends, coupled with continuing growth spillovers from within the South, if not from the North, are also conducive to accelerating human development.

88 Kaplinsky 2011, Figure 11.

89 UNIDO and UNCTAD 2011.

Human development policies can play a special catalytic role in the current trade and investment interaction in the South. On the one hand, all the beneficiaries of growth spillovers rank low on human development. On the other hand, human development deepens absorptive capacity.<sup>90</sup> While growth spillovers contribute to human development through additions to income, the initial benefits are small. To the extent that policies enhance non-income components of human development, the fuller potential of growth spillovers can be captured. A virtuous circle is set in motion for achieving greater future benefits. A cursory look at recent experience suggests that countries could improve policies in this area (see Box 6).

#### Box 6: Human development and growth spillovers

Asian growth spillovers mean faster GDP growth in Africa, but progress depends on how well countries convert additional GDP into human development. To illustrate, all 13 countries that had growth spillovers from Chinese FDI in Africa from 2003 to 2009 (see Table 1) also advanced in human development (see Figure 6). But the dispersion in the trend is wide. The Democratic Republic of the Congo, Ethiopia, Niger and Tanzania all ranked at the bottom of the HDI in 2002, but were able to achieve higher HDI growth with less additional GDP growth than other economies. Many factors are at play—such as low initial level, other sources of growth (or obstacles to it, like HIV). One of these is policy. By sharing and learning from their respective policy experiences, countries could improve benefits from growth spillovers.

#### SOUTH-SOUTH COOPERATION

The singular policy lesson in the rise of the new South is the importance of building domestic productive capacity, namely, infrastructure, the technological capabilities of firms and human development. This enabled the NICs and the southern BRICS to harness the growth of advanced countries in their catch-up phase, and then gravitate to their own long-term growth paths. The accumulation of capabilities may precede, but more importantly can co-evolve with economic activity, particularly through institutions and policies that bring out the learning and diffusion potential in trading, investing and

90 Human capital can have threshold effects on FDI spillovers. See Fu and Li 2010.

partnering processes in all industries, even commodities.<sup>91</sup> This policy lesson is directly relevant to countries of the South as a whole: Building domestic productive capacity is the only sure way of catching up while avoiding ‘the commodities trap’ that could hold back long-term growth. Much of the onus rests on individual countries, but South-South cooperation can support their efforts and be a ‘win-win’ for all.

The main types of cooperation are already underway and could be scaled up, including:

- Complementing investment flows and trade arrangements with development assistance and finance (e.g., loans, grants and credit lines for local enterprises). China has pioneered partnership packages involving bundling natural resource extraction projects with infrastructure, technology and productive capacity expansion. India, Kuwait, Saudi Arabia and the United Arab Emirates have also financed infrastructure. Such investments are expanding roads, railways and utilities. Given Africa’s infrastructure deficit, such financial partnerships could be more widespread and comprehensive. The interest shown by the regional development banks and sovereign wealth funds in organizing and participating in investment consortia is indicative of the potential for scaling up finance.
- Closer cooperation in creating jobs and industrial linkages. Host and home governments can encourage investors to employ and train greater numbers of local workers, including by removing regulatory obstacles and strengthening social infrastructure. There is considerable Asian experience in building links among firms and establishing industrial clusters that could be applicable to Africa.<sup>92</sup> Cooperation of this type could also help address cultural conflicts that often arise in interregional investment.<sup>93</sup> Bilateral programmes are the main modality, along with technical assistance from regional and international agencies supported by voluntary funds of developing countries, as this approach to cooperation is not necessarily a priority of traditional donors.
- Encouraging sequential investment outside natural resource industries, in agriculture, manufacturing, and services such as in finance and telecommunications. These sequential investments can be cross-border within the African region,

and also by small and medium-sized enterprises that follow large investors to form industrial clusters. Such patterns are prevalent in East Asia and applicable to Africa.

- Promoting the ‘flying geese’ relocation of manufacturing to Africa as industry upgrades in China and other Asian economies. This has happened within Asia and could be more interregional, contributing to Africa’s industrialization (see Box 5).
- Fostering technology partnerships and alliances among R&D institutions, particularly tapping into the sizeable capabilities in Brazil, China, India, Turkey and other countries. Such alliances can leverage technological congruence among developing countries, and create products and processes applicable to their situation and needs (e.g., new crop varieties; tropical medicines and vaccines; affordable health treatments and diagnostic kits; alternative energy sources; and innovative ICT applications).
- Sharing policy experience and best practices in handling economic issues arising in similar growth contexts and developing country environments. These range from practical procedures for investment facilitation to institutions for microfinance, public-private dialogue and government-business risk partnerships. UN organizations can also do more to programme peer learning into technical assistance.

South-South cooperation has considerable potential, but collective action requires a shared vision. The 1990 report of the South Commission—*The Challenge to the South*—is a seminal analysis, still relevant two decades later. It mentions, for example, climate change as a priority, and challenges that stubbornly persist (poverty, exclusion) or are re-emerging (the widening gap between rich and poor, even with convergence in growth). At the same time, the world has changed dramatically, and if the report were to be rewritten today, it could well be re-titled “The Challenge of the South”.

The new South of the 21<sup>st</sup> century has economies growing at double-digit rates, and nations with trillions of dollars of foreign exchange reserves and more trillions to invest outside their borders. Southern businesses number among the world’s largest. The possibilities for collective action have never been greater, but cannot be taken for granted. The institutions for South-South cooperation—the Group of 77, the Non-Aligned Movement and South Summits—grew from the decolonization experience. This was a strong political, economic, social and cultural bond, but it is increasingly distant to the new generation. There is growing differentiation among countries, and the pursuit of national interest remains paramount.

91 Enterprises that have diversified out of resource-based production include Nokia, which once made rubber boots in Malaysia, and Orascom (Egypt), which started in cement and is now the seventh-largest telecom company in the South.

92 Dinh et al. 2012 provide various examples.

93 UNDP 2004.

South-South cooperation needs a compelling case for collective action. A new South Commission could initiate a fresh vision based on common understanding of how the diversity of the South can be a force for solidarity (see Box 7). The elements are there: different endowments basic for exchange; diverse experiences ripe for sharing; the need to collaborate to compete in world markets; and, above all, the need to learn to collaborate on a 'win-win' basis. The global context is right; the time for renewal has come.

#### Box 7: The challenge of the South

South-South trade should not replicate the traditional asymmetric pattern of North-South trade. The new South is sustaining growth and counteracting the decline in demand from the North, but trade based on the import of commodities and export of manufactured goods (even capital goods) could set back the industrial ambitions of many southern countries.

Commodity producers, instead of once again being on the losing end of trade, could take full advantage of the prolonged commodity boom, while sidestepping the inherent problems of Dutch disease and resource curse. The pitfalls of commodity dependence can be avoided through smart government, proven industrial policy that fosters linkages, entrepreneurship and productive capabilities, and a state supportive of human development.

South-South cooperation and 'win-win' partnerships could facilitate industrial diversification through FDI and joint ventures; technology sharing through peer learning; and meeting the needs of the emerging entrepreneurial class and 'bottom billion' with affordable products and innovative applications. This is already happening and can be scaled up substantially in the years ahead

Developing countries are already playing a greater role in the Bretton Woods institutions and global dialogue through the Group of 20 leaders summits, and are active in the Organisation for Economic Co-operation and Development. They are prominent in emergency relief and peacekeeping; consideration is underway to enlarge the United Nations Security Council. Their enhanced role should be welcomed by developed countries, as the success of the South earns dividends for the North and advances prosperity for all.

## GLOBAL COOPERATION

A forward-looking new South can provide timely impetus to development cooperation, which is under threat from the global downturn and its undertow of austerity. Emerging states could invigorate the intergovernmental process of development cooperation, providing new solutions and political will to foster strategic use of the now substantial new South investments, technology and new business models for human development. Emerging states could be leaders in tackling the global challenges of the Millennium Development Goals, climate change and conclusion of the Doha development round of trade talks.

## ANNEX

Table A1: Major Transnational Corporations based in the South, 2009 (ranked by size of foreign assets)

Corporation	Home Economy	Industry
<i>Hutchison Whampoa Ltd</i>	Hong Kong, China (SAR)	Diversified
<i>CITIC Group</i>	China	Diversified
<i>Cemex S.A.B. de C.V.</i>	Mexico	Non-metallic mineral products
<i>Vale SA</i>	Brazil	Mining & quarrying
<i>Samsung Electronics Co., Ltd</i>	Korea, Republic of	Electrical & electronic equip.
<i>Petronas - Petroliam Nasional Bhd</i>	Malaysia	Petroleum
<i>China Ocean Shipping (Group) Company</i>	China	Transport and storage
<i>Hyundai Motor Company</i>	Korea, Republic of	Motor vehicles
<i>LG Corp</i>	Korea, Republic of	Electrical & electronic equip.
<i>Singapore Telecommunications Ltd</i>	Singapore	Telecommunications
<i>Zain</i>	Kuwait	Telecommunications
<i>Qatar Telecom</i>	Qatar	Telecommunications
<i>Tata Steel Ltd</i>	India	Metal and metal products
<i>Formosa Plastics Group</i>	Taiwan Province of China	Chemicals
<i>Hon Hai Precision Industries</i>	Taiwan Province of China	Electrical & electronic equip.
<i>Petroleo Brasileiro SA</i>	Brazil	Petroleum
<i>MTN Group Ltd</i>	South Africa	Telecommunications
<i>Abu Dhabi National Energy Co PJSC</i>	UAE	Utilities
<i>Jardine Matheson Holdings Ltd</i>	Hong Kong, China (SAR)	Diversified
<i>Gerdau SA</i>	Brazil	Metal and metal products
<i>Petróleos de Venezuela SA</i>	Venezuela	Petroleum
<i>China National Petroleum Corporation</i>	China	Petroleum
<i>Wilmar International Ltd</i>	Singapore	Food, beverages and tobacco
<i>Tata Motors Ltd</i>	India	Automobile
<i>América Móvil SAB de CV</i>	Mexico	Telecommunications
<i>Noble Group Ltd</i>	Hong Kong, China (SAR)	Wholesale trade
<i>Flextronics International Ltd</i>	Singapore	Electrical & electronic equip.
<i>Oil and Natural Gas Corp Ltd</i>	India	Petroleum
<i>CapitaLand Ltd</i>	Singapore	Construction and real estate
<i>Hindalco Industries Ltd</i>	India	Diversified
<i>DP World Ltd</i>	UAE	Transport and storage
<i>First Pacific Company Ltd</i>	Hong Kong, China (SAR)	Electrical & electronic equip.
<i>New World Development Ltd</i>	Hong Kong, China (SAR)	Diversified
<i>Axiata Group Bhd</i>	Malaysia	Telecommunications
<i>Genting Bhd</i>	Malaysia	Other consumer services
<i>CLP Holdings Ltd</i>	Hong Kong, China (SAR)	Utilities
<i>Orascom Telecom Holding SAE</i>	Egypt	Telecommunications
<i>Sinochem Group</i>	China	Petroleum
<i>China Resources Enterprises Ltd</i>	Hong Kong, China (SAR)	Petroleum
<i>Shangri-La Asia Ltd</i>	Hong Kong, China (SAR)	Other consumer services
<i>STX Corporation</i>	Korea, Republic of	Other equipment goods
<i>Ternium SA</i>	Argentina	Metal and metal products
<i>Sasol Ltd</i>	South Africa	Chemicals
<i>China National Offshore Oil Corp</i>	China	Petroleum

Corporation	Home Economy	Industry
<i>Pou Chen Corp</i>	Taiwan Province of China	Other consumer goods
<i>ASUSTeK Computer Inc</i>	Taiwan Province of China	Electrical & electronic equip.
<i>Sun Hung Kai Properties Ltd</i>	Hong Kong, China (SAR)	Other services
<i>Doosan Corp</i>	Korea, Republic of	Diversified
<i>Quanta Computer Inc</i>	Taiwan Province of China	Electrical & electronic equip.
<i>Li &amp; Fung Ltd</i>	Hong Kong, China (SAR)	Wholesale trade
<i>Naspers Ltd</i>	South Africa	Other consumer services
<i>Acer Inc</i>	Taiwan Province of China	Electrical & electronic equip.
<i>Yue Yuen Industrial Holdings Ltd</i>	Hong Kong, China (SAR)	Other consumer goods
<i>Steinhoff International Holdings Ltd</i>	South Africa	Other consumer goods
<i>Fomento Economico Mexicano SAB</i>	Mexico	Food, beverages and tobacco
<i>Netcare Ltd</i>	South Africa	Other consumer services
<i>Fraser and Neave Ltd</i>	Singapore	Food, beverages and tobacco
<i>Grupo Bimbo SAB de CV</i>	Mexico	Food, beverages and tobacco
<i>POSCO</i>	Korea, Republic of	Metal and metal products
<i>Gold Fields Ltd</i>	South Africa	Metal and metal products
<i>Sappi Ltd</i>	South Africa	Wood and paper products
<i>Suzlon Energy Ltd</i>	India	Diversified
<i>Medi-Clinic Corp Ltd</i>	South Africa	Other consumer services
<i>Tata Consultancy Services</i>	India	Other services
<i>Sime Darby Bhd</i>	Malaysia	Diversified
<i>Swire Pacific Ltd</i>	Hong Kong, China (SAR)	Business services
<i>Reliance Communications Ltd</i>	India	Telecommunications
<i>Lenovo Group Ltd</i>	China	Electrical & electronic equip.
<i>Compal Electronics Inc</i>	Taiwan Province of China	Other consumer goods
<i>Taiwan Semiconductor Manufacturing</i>	Taiwan Province of China	Electrical & electronic equip.
<i>China Railway Construction Corp Ltd</i>	China	Construction
<i>City Developments Ltd</i>	Singapore	Other consumer services
<i>United Microelectronics Corp</i>	Taiwan Province of China	Electrical & electronic equip.
<i>Agility Public Warehousing Company</i>	Kuwait	Construction and real estate
<i>Enka Insaat ve Sanayi AS</i>	Turkey	Construction and real estate
<i>ZTE Corp</i>	China	Other consumer goods
<i>Turkcell Iletisim Hizmetleri AS</i>	Turkey	Telecommunications
<i>Wistron Corp</i>	Taiwan Province of China	Other equipment goods
<i>TPV Technology Limited</i>	Hong Kong, China (SAR)	Wholesale trade
<i>Advanced Semiconductor Engineering</i>	Taiwan Province of China	Electrical & electronic equip.
<i>Lee &amp; Man Paper Manufacturing Ltd</i>	Hong Kong, China (SAR)	Wood and paper products
<i>National Industries Group Holdings SAK</i>	Kuwait	Diversified
<i>Inventec Co Ltd</i>	Taiwan Province of China	Electrical & electronic equip.
<i>Skyworth Digital Holdings Ltd</i>	Hong Kong, China (SAR)	Electrical & electronic equip.
<i>China Minmetals Corp</i>	China	Metal and metal products
<i>Galaxy Entertainment Group Ltd</i>	Hong Kong, China (SAR)	Other consumer services
<i>Cheng Shin Rubber Industry Co</i>	Taiwan Province of China	Chemicals
<i>Esprit Holdings Ltd</i>	Hong Kong, China (SAR)	Other consumer goods
<i>Neptune Orient Lines Ltd</i>	Singapore	Transport and storage
<i>Techtronic Industries Co Ltd</i>	Hong Kong, China (SAR)	Other equipment goods
<i>Asia Food &amp; Properties Ltd</i>	Singapore	Food, beverages and tobacco



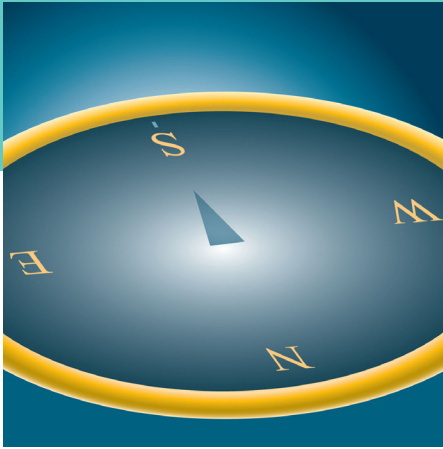
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