Part V: EC Market Integration and Asian NIEs : Comment on Chapters 9, 10 and 11

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Comment on Chapters 9, 10 and 11

Hiroshi Osada

The approaches taken in the literature of the economic impacts of the EC integration on the non-member countries are broadly divided into two; a macroeconomic approach and a sector-wise approach. The macro approach gives the base of the analysis, but at the same time it should be supplemented by sectoral analysis since the relative price effects of the integration vary among industries. In other words, the macro approach seems to have tendencies to underestimate the relative price effects (trade diversion effects) because of the technical reason that the commodity classification for estimating the export function can not be detailed enough, while the sector-wise approach usually has the inclination to highlight the would-be severely affected industries. Therefore, well balanced application of the two approaches is imperative for the accurate assessment of the impacts of the EC integration. The paper on Taiwan by Liang in Chapter 10 is well organized in this sense. The Korean paper by Pyo in Chapter 9 is unique in making use of the survey result made by Korean Foreign Trade Association on the anticipated impacts, covering 245 firms. Unfortunately, any sectoral consideration is not given in the Hong Kong paper by Chou and Lin in Chapter 11, but it tries to partly compensate it by the application of sub-divided export functions in the macro model.

While the impacts of the EC integration basically channelled to each Asian economy through foreign trade, exchange rates, and foreign direct investment (FDI), it can not be accused that the three papers quantify the impacts only through foreign trade if we take account of the difficulty in setting the assumptions on exchange rate development and FDI under the on-going uncertainty. The assumptions made for the model simulation of the three economies are more or less same, since they referred for the figures to the well-known studies on the quantitative assessment of the EC's future. Roughly speaking, EC's GDP is assumed to increase approximately one percentage point and the EC's price level to decrease one to two percentage points from those of the baseline simulation. The simulation by Taiwan and Hong Kong models in Chapters 10 and 11 respectively, gave slightly positive overall effects on the GDP growth as a combination of the positive income effects and negative price effects. In contrast, the Korean model in Chapter 9 gave slightly negative effects on the GDP growth. Though the simulation results of the three models are not provocative, some peculiarity in the structure of the Korean model should be pointed out. First, the total exports (eq. 4 in the Appendix) are estimated as a linear function of the exports to the EC. This is a too strong assumption when the share of exports to the EC was only 12.1%, the third place after the US and Japan as of 1992. The same applies to its import function (eq. 3). Second, the specification of the export function to the EC (eq. 6) seems to be too ad hoc. It gives two overlapping assumptions on

the EC's demand for Korean goods, i.e., GDP and imports of the EC. Also, the treatment of the relative prices is different from the standard methods. Instead of dividing the left-hand variable (exports to the EC) by the Korean export price (PX) and the right-hand variables (GDP and imports of the EC) by CPI of the EC (CPIEC), the relative price (PX/CPIEC) had better be explicitly used as an explanatory variable. Third, some treatment should be taken to avoid the effect of autocorrelation commonly seen in most of the equations.

The sector-wise analyses given in both papers by Pyo and Liang in Chapters 9 and 10 respectively, reveal that the strategic and prospective industries of these countries basically coincide with the EC industries whose efficiency is estimated to improve in most of the previous studies. They are, for example in case of Taiwan, electrical goods, motor vehicles, and mechanical engineering. The sectoral analysis made by the Taiwan paper is convincing. It measures revealed comparative advantage (RCA) and trade specialization index for each industry, and compares the figures with the efficiency gain of the corresponding EC industries. However, since the indicator of the impacts on the EC industries (ECI) is not directly comparable with the RCA index, it might be more convincing if the RCA of the EC is also estimated for direct comparison. Also, since the trade specialization index can be interpreted as an intra-trade index if the absolute value is taken and very much dependent on the level of the classification, we need some caution in its interpretation. In Chapter 11, Lin pointed out that for Hong Kong such sectoral analysis is not so valid since the economy is now heavily biased on the tertiary sector in the discussion. However, the Hong Kong economy might get influence through the change in the manufacturing exports from the hinterland. In addition, Liang warned the possibility of more non-trade barriers on the EC side in Chapter 10.

The overall assessment of the impacts on Korea and Taiwan by the authors was concluded as negligible or slightly negative, and we need a close watch of the development in the EC since there still remains a lot of uncertainties.