How Support Services Can Expand Manufactured Exports

New Methods of Assistance

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and
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This paper offers proposals to make support services more effective through outside assistance. Especially recommended are packages of assistance and promotion built around grant funds that pay firms half the cost of commercial service suppliers, such as consultants, and/or half of their initial marketing expenses.
This paper—a product of the Trade Policy Division, Country Economics Department—is part of a larger effort in PRE to study export development and supply response. Copies are available free from the World Bank, 1818 H Street NW, Washington, DC 20433. Please contact Sheila Fallon, room N10-017, extension 37947 (44 pages).

Assistance to support services for exports has rarely boosted manufactured exports from developing countries whose export policies were less than fully satisfactory. This is particularly true of services that involve consultant advice, export promotion, marketing assistance, and provision of export-related information.

Keesing and Singer make four recommendations for improving such services:

- Emphasize services that improve firms’ know-how and performance in overcoming supply difficulties, which are the biggest obstacle to expansion of promising manufactured exports. Provide consultant assistance to promising firms with strong export prospects to help them improve their supply capabilities and performance. Advice from consultants with export know-how can substitute for learning from buyers and may be better. Most manufacturing firms in developing countries are unaware of how far behind they are in current practices in systems engineering, productivity, quality control, and other aspects of production management. When they have been cut off for years from international “best practice,” help from outside consultants can provide dramatic results.

- Give exporters ready access to commercial service suppliers abroad. As exports develop, systematically favor the development within the national economy of competing (primarily private) service suppliers. Encourage the establishment of local branches or affiliates of multinational service firms. Dismantle policy obstacles to the use of consultants and other service suppliers from abroad and encourage a policy environment that supports vigorous, diversified export growth. Abolish protection of, and monopolies in, services for exporters. Insist that public service organizations, if they continue to function, charge commercial prices for most of their services and compete with private services. Encourage private suppliers to compete in providing information services, each with telephone access to many online databases and other commercial information services abroad.

- Rely on specific, time-limited projects or project components involving temporary infusions of specialized resources, where and when needed, to channel external assistance to services supporting manufactured exports. Direct each project component at expanding exports within that time-frame. Any project to expand exports should include specific measures directed at turning passive or nonexporters into active exporters.

- Create packages of assistance built around one or more grant funds. Through these funds, provide cost-sharing grants to firms to help pay the costs of services from suppliers of their choice. The institutions or banks that administer these funds assist firms in preparing export expansion plans and grant applications, and help identify suitable service suppliers. In funds set up with World Bank assistance in India, grants come with all necessary government approvals and are complemented by funds for term lending.

See also companion paper, WPS 543.
How Support Services Can Expand Manufactured Exports:
New Methods of Assistance

by
Donald B. Keesing and Andrew Singer

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Assistance to support services for exports has almost never proved effective in systematically expanding manufactured exports from developing countries that have less than fully satisfactory policies toward such exports. This conclusion applies particularly to services that involve consultant advice, export promotion, marketing assistance, and provision to enterprises of export-related information.1/ Despite this disappointing conclusion, we are fully convinced that assistance to these and related support services can be an effective instrument for expanding manufactured exports in countries with partly satisfactory policies toward exports if countries make bold, imaginative use of new instruments and techniques.

This chapter discusses effective methods of assistance and puts forward recommendations for policy as well as external assistance in this area. These are intended above all for World Bank operations, but also for other organizations providing assistance in this field and for the

1/ See our companion paper "Development Assistance Gone Wrong"
developing countries themselves. To go with these recommendations, we present suggestions concerning key details of the design of projects or project components using the new techniques.

We do not want to exaggerate what can be achieved. At best, support services have much less impact on a developing country manufactured exports than its policy and physical environment. Suitable services cannot compensate for unsatisfactory policies. Indeed, services for exports yield no return unless the exports assisted can soon be made profitable. Appropriate services are thus a complement and not a substitute for suitable policies, resources, infrastructure, and all the other facilities that manufactured exports require. However, with help from consultants or other experts working directly with enterprises, developing countries can overcome a wide range of difficulties in exporting.

We have four main recommendations:

1. Emphasize support services that overcome supply difficulties holding back otherwise potentially profitable exports. Provide consultant assistance to promising firms in products with strong export prospects, to help them improve their supply capabilities and performance.

2. Provide exporters with ready access by exporters to commercial service suppliers abroad. As exports develop, systematically favor the development within the national economy of a number of competing service suppliers, primarily in the private sector. Facilitate and encourage the establishment of local branches or affiliates of multinational service firms.
3. Rely on specific, time-bound projects or project components involving temporary injections of resources to channel external assistance to services supporting the expansion of manufactured exports. Direct each project component specifically toward the one overriding objective of expanding exports within the project's time frame, avoiding premature and unrealistic institution building.

4. Create packages of assistance built around one or more grant funds. By means of these funds provide cost sharing grants to firms to help pay the costs of services from suppliers of their choice.

Inexperienced exporters have a pressing need for assistance from experienced service suppliers. Thus, fostering support services in the ways discussed here is especially crucial for developing countries that expect to rely primarily on exports by local firms with little previous export experience.

Alternatively, small developing countries may choose to develop manufactured exports primarily through investment promotion that encourages existing manufacturer exporters from abroad to set up satellite production units inside the country. Because the foreign firm already has the marketing links, know-how, and experience to make such a unit a success, investment promotion aimed at such firms can greatly reduce the need for the support services discussed here. This has been the main route followed in such small countries as Ireland, Malta, Mauritius, and Singapore.

In larger economies, investment promotion can contribute to export development, but it is not a substitute for the services discussed
here. Even if foreign investment on a large scale is politically acceptable, promotion of foreign investment is likely to prove a good way to get started only in exceptional export industries. For all developing countries taken together, exports by firms owned by the countries' nationals are several times larger in value than those by foreign owned firms, and in most industries, foreign-owned firms have no lasting advantage. Thus, the services discussed here are likely to be crucial for accelerating the growth of manufactured exports in large or medium-sized economies.

**Primary Emphasis on Supply**

Once governments have reformed policies sufficiently to make at least some manufactured exports feasible and potentially profitable, experience shows that supply difficulties are generally the most important obstacle to expanding promising manufactured exports. Indeed, the marketing difficulties of developing country exporters are generally rooted in unsatisfactory supply capabilities, typically combined with unfamiliarity with what distant target markets require. These deficiencies are aggravated by a lack of service suppliers to perform, supervise, or advise on the various steps of the export supply process. In advanced economies, exporters have access to a wide range of suitable consultants and other service suppliers, but these are rarely available in a developing country in transition toward satisfactory policies for exports, except in products that have already been exported successfully for many years.

Thus, within a project seeking to expand manufactured exports, a particularly effective method of assistance is to offer promising firms expert consultant assistance and advice centered on supply-related task
in product groups with strong export potential. This assistance will often include guidance on what is required or in demand in the target market.

The Underlying Challenge

Export marketing is a three-stage process. The first stage is selecting an export market (or markets) on which to concentrate, and exploring those markets to find out what they require. The second stage is adapting the supply package (and the various links in the supply chain) to suit the target market's preferences. The third stage is actively finding (or attracting) customers and getting orders; in other words, selling exports to the target market.

In the typical case, a locally owned enterprise in a developing country exports to buyers' orders and detailed specifications. The firm receives orders principally on the basis of its production capabilities. Learning to market these capabilities better is one way to improve results. Even more effective is to improve and broaden the supply capabilities themselves. Poor supply performance can quickly undo the entire export marketing effort. Supply is always crucial.

Buyers and customers usually provide developing country export manufacturers with some useful advice on the details of their supply tasks. Export manufacturers typically learn a lot this way, but buyers only provide systematic assistance in a sustained relationship, especially if, in return, they are able to buy the product at very low prices. Moreover, buyers are always eager to find suppliers already competent to handle all or most tasks unassisted. While a few buyers specialize in finding and teaching new suppliers in return for low prices, most buyers shun would-be suppliers that need a lot of instruction and assistance.
A firm producing to order must learn to make exports according to the designs, materials, stylings, and specifications called for, suitably documented, labeled, packaged, and ready for shipment to the ultimate customer. The firm has to adapt and modify its production and associated processes, as well as its management and training methods, to meet specific but frequently changing product specifications. The firm must also continually improve its production methods to reduce costs, increase product reliability, and achieve strict quality control, and it must learn to deliver exports dependably on schedule. Exporting on the basis of the firm's own designs and distribution usually calls for even greater supply capabilities.

Advice from expert consultants, with know-how and experience comparable to that of the best informed buyers, can substitute for learning from buyers. By accelerating and reinforcing the learning process, such assistance makes the firm more attractive to buyers. Prior instruction from consultants holds down buyers' risks and costs. This leads them to place more orders and to pay higher prices. To be effective for these purposes, however, consultant advice has to be customized to the firm's production equipment and methods, technical capabilities, and management practices.
The Supply Gap and Consultant Advice

Most manufacturing enterprises in developing countries are unaware of how far they lag behind the best current practices in advanced countries in systems engineering, productivity, quality control, and other aspects of production management. Only after policies become favorable for exports do they begin to learn, as the buyers show them how to reorganize their production or as they begin to use international consultants.

The amount of catching up required is generally enormous. Developing country plants are typically badly out of date, not only in their more obvious visible features, such as their equipment, but also in less obvious areas, for instance, the way this equipment is arranged, how they measure quality, and production practices. In richer countries, output attainable from a given plant and equipment has often increased enormously in recent years through advances in management practices in such areas as plant layout, machine arrangement, work flow, inventory management, and quality control. These changes have greatly reduced the work force required and the costs of production. Large gains have also taken place in the output attained from a given input of raw materials. At the same time, product quality, production scheduling, and the product options offered to buyers have all improved.

The resulting gap is graphically illustrated by the findings from follow-up interviews with Indian firms to determine the impact of and returns from matching grant assistance provided by the Productivity Fund and Export Marketing Fund, which were set up in 1986 under a World Bank export development loan. The firms that benefited were mainly private
firms in engineering industries. Most were already well managed, competitive, and rather large by Indian standards. A number already had significant export experience.

One firm, with a large output even by world standards, was surprised when after an introductory plant visit, a foreign consultant said that he could guarantee a 50 percent increase in output from the existing plant and equipment within one year with almost no new investment. During the eight months it took to finalize the consultancy arrangement, the firm's head challenged its managers to increase productivity in every way they could. By the time the consultant returned, the firm had achieved a 15 to 20 percent increase in output. After taking a more careful look at how production was organized, the consultant said to the head of the firm, "Make that 100 percent." By reorganizing production methods, the machinery layout, work flow, and other systems engineering aspects of production, he guaranteed that output would double within a year.

In another enterprise with insufficient output to meet domestic demand and only a small volume of exports, a consultant zeroed in on the 20 to 25 percent rejection rate in the foundry, which was the first stage in the production process. With the consultant's help, the rejection rate was reduced to 5 to 6 percent. This translated to a 20 percent increase in final output and resulted in a large saving in materials. The result was a dramatic reduction in the unit costs of production, making exports more competitive. Now the firm is meeting all its domestic demand and exporting half its output, compared to 3 percent two years earlier. The
firm now intends to establish a second production line exclusively for exports. (In this instance, the cost to the Productivity Fund of the Japanese consultant was less than US$25,000.)

These examples illustrate a general principle. When a developing country has for years been cut off from international best practice, the returns from outside consultancy assistance can be dramatic.

**Growing Recognition of the Importance of Supply Assistance**

Until very recently, most outside assistance for export promotion and marketing support had neglected supply problems. However, donors have now begun to rectify this neglect, with promising results. Several external donors have started to provide supply-related assistance to firms before or along with final-stage marketing assistance.

The International Trade Center (ITC) of UNCTAD and GATT, the largest provider of assistance and advice in this area, has begun to experiment with what it calls the "enterprise-oriented approach," which involves providing individual firms with systematic consultant advice.

The European Community (EC) in its assistance in this area to nonassociated developing countries, which is the second largest program in this field after ITC's, has recently begun to include supply-related assistance to firms in its major export promotion and marketing projects. The EC now generally undertakes integrated projects lasting three to five years focused on specific product groups. It conducts regular intermediate evaluations to guide the adjustment of projects to new circumstances and information.
Assistance to firms in adapting their supply capabilities has also become an important element in some projects by other agencies: the Developing Country Trade Agency (DeCTA) of the United Kingdom, the Center for the Promotion of Imports from Developing Countries (CBI) in the Netherlands, and the U.S. Agency for International Development (USAID). The World Bank has been one of the leading pioneers in assistance in this area and is believed to be the only donor to set up grant funds. The World Bank has given supply-related assistance through the Export Marketing Fund and Productivity Fund in India, as well as technical assistance in design in the Philippines. Four new export development funds have been created in India and an export support fund has begun to help exporters in Indonesia.

Access to Services

In any developing country just beginning to export manufactured products, the support services most needed will come primarily from abroad, from economies that already have well-developed and up-to-date versions of the industries and exports that are beginning to emerge. To make use of service suppliers overseas, exporters require ready access to foreign exchange as well as to government approvals, such as travel visas needed to import services. Access to services abroad is generally blocked or uncertain until the country attains a convertible currency or, like India or Morocco, facilitates exports by giving exporters the right to foreign exchange up to the equivalent of the value of a specified small percentage of their exports in the previous year, usable for a wide range of service transactions, and eases its restrictions on business-related
Actions to facilitate the use of services abroad deserve priority attention.

The development within the country of support services for manufactured exports tends to come about later, following export successes made possible by a promising policy framework and industrial capacity, at least for some export products. When exports first emerge, local service suppliers understand little of what exporters need. Only as experience is acquired by all concerned does the situation become ripe for developing suitable service suppliers within the country.

The government's overall objective at each stage ought to be to expand exports rapidly by making available to exporters high-quality services that reflect the best advice and knowledge available internationally. This calls for facilitating access to service suppliers abroad, then as experience cumulates, fostering the development within the country of a number of competing service suppliers, some of them foreign owned, predominantly in the private sector. Vigorous competition in services will then ensure that service suppliers respond to exporters' needs and that the country gradually develops a full array of local services.

Actions to further the objective described should be supported by external assistance and advice. For example, every World Bank loan or credit aimed at expanding manufactured exports should consider such actions.

Policies Toward Private Services Suppliers

The actions required are likely to involve new or revised legislation and regulations together with new procedures for administering
existing laws and regulations. Services to support export expansion
deserve a high priority wherever resources (such as foreign exchange) are
rationed. New tax breaks, temporary subsidies, or other inducements may
be required to foster the provision of services, not only by private
firms, but also by organizations such as exporters' associations and
chambers of commerce.

Governments should abolish protection and monopolies in services
for exporters and avoid restrictions on imports of services and on the use
of service suppliers abroad. Entry and exit (closing down or bankruptcy)
of service firms need to be facilitated.

Services for exporters are among the activities in which foreign
participation deserves to be welcomed and encouraged. A foreign ownership
presence in these services may be essential for eliciting a strong
performance by locally owned firms. Multinational service firms, after
all, have a wealth of experience and are strongly influenced by
international best practice in services.

These recommendations are based in large part on the favorable
results of lively competition in services in nearly all developed market
economies and in leading East Asian industrializing economies. Typically
this competition includes numerous foreign owned firms, including both
subsidiaries within the country and services supplied from abroad.

In the long run, the vigorous expansion of manufactured exports;
with all the learning that it engenders, will be infinitely more valuable
than any initial loss of business or local control in services to
foreigners. Moreover, a foreign owned services firm will be strongly
motivated to train local nationals to take over key jobs in its local
branch offices, since local nationals can learn to do the work just as
well as people from developed countries, but typically require much lower salaries and rewards. The long-run result is that many of these local managers will later set up their own service firms or acquire full or part ownership of the branch offices, thus eventually indigenizing the services.

The Role of Public Sector Service Suppliers

In contending that export-related service suppliers should be predominantly private, we do not rule out service organizations funded largely by government, but in which the private sector plays a large role in direction and decision making. Nor do we rule out all service provision in this area by public sector organizations. We do recommend, however, that as a rule, publicly funded service organizations charge commercial prices for services and face private competitors.

The positive influence that charging for services has in improving the services and expanding the resources available has recently become widely recognized in export promotion in industrial countries. As

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2/ Tasks relating to export marketing that may well deserve subsidies, if not direct government support, include (a) providing commercial representatives abroad to help local nationals transact business abroad and to gather economic information; (b) publishing and disseminating trade statistics and other relevant information on the country's economy; (c) gathering and disseminating information that is useful to exporters and not readily available from alternative sources about the situation in other countries; and (d) helping to arrange for local exporters to participate in trade fairs, particularly when trade fair participants are grouped by country. One corresponding task relating to supply is setting uniform industrial standards and measurements in consultation with the relevant industries.
one respondent in a Western European, governmental service supplier put it, "Charging is the only way to justify our services." Australia's trade promotion organization, Austrade, introduced general charges for services in 1986 as a means "to test the relevance and quality of services, and to put our resources to the best use."

Whether service suppliers are actually privately owned probably matters less than whether they are in a competitive situation and act much like private firms. What is important is that these entities provide the services in a helpful manner similar to that of private suppliers in a competitive buyers' market. The government can try to achieve this environment through the composition of the organization's governing board and its legal status, salary scale, recruitment efforts, and working style, but this may be impossible in an economy afflicted by vast excess aggregate demand that is reflected in high inflation or widespread shortages. It may also be difficult to achieve in an economy in which private enterprise does not play a predominant role overall.

Multiple Suppliers of First- and Third-Stage Marketing Assistance

Assistance in the supply aspects of exporting includes help in the second stage of marketing: adapting supply to target market preferences and requirements. A useful complement to assistance in strengthening supply is helping enterprises in the first and third stages of export marketing.

Firms and nascent industries may well need help in the first stage, namely, selecting and exploring the most promising markets for their exports and identifying suitable products. This may call for travel to these markets. It may also extend to detailed market research with the help of service suppliers located in the target market.
For the third stage of marketing, that is, actually selling exports, firms often look for outside help in finding buyers and customers, countertrade or buyback partners, agents, representatives, or distributors. A consultant who helps a firm to adapt its supply package may also help it get orders based on its new capabilities. Exporting firms also often require advice on how to support sales with brochures, advertising, point-of-sale material, samples, and other evidence of their capabilities.

Assistance in third-stage marketing is most effective when combined with advice relating to supply and geared to the supply capabilities, orders already received, and learning stage of each individual firm. A high payoff is likely if marketing assistance is concentrated on firms with strong or much-improved export supply capabilities that are not yet reflected in their exports.

Meeting Exporters' and Buyers' Information Needs

A useful supplement to consultant advice to exporting firms is facilities to meet exporters' information needs. However, exporters' information needs are extremely diverse and quickly become very specific. Usually even a good library is insufficient as is the typical official trade promotion organization (TPO).

Exporting firms require information on markets, in much comparative detail; on the supply package required in a selected market and how to supply it; on competitors' technologies, equipment, and management systems; on potential buyers, what they generally buy, and
details of their businesses; and much else. But while one entrepreneur is trying to learn about the U.S. market for men's leather shoes, another is trying to learn about the German and British markets for ladies' blouses, and a third is looking at export prospects in smaller countries for hand-operated pumps. One is searching for information on product designs and the supply package required, another wants to know about details of documentation and nontariff barriers, and a third is looking for distributors and potential customers. Every exporter wants different details, most of them specific to narrow product groups.

Meeting these varied information needs in a timely fashion is not a task suitable for a public monopoly supplier of information. What is needed is a large number of competing information suppliers, each armed with telephone access to many on-line data bases and other commercial information sources abroad, and many of them experienced and active in providing similar types of information in many different countries and settings. Thus, private suppliers are likely to form the backbone of successful information services in this area.

Foreign buyers looking for local suppliers require much more than an up-to-date list of firms in each product group and information on how to reach them. They seek extensive information on each firm, including its experience and past performance, production capacity, supply capabilities, finances, creditworthiness, and the ambitions and motivations of the people who own and run it. To start with they need enough information to focus quickly on the firms of appropriate size and experience for their needs or a reliable short-list of two or three firms most suitable for them, with poor performers omitted.
A developing country has a strong interest in pointing buyers in the right direction, both to facilitate their finding a suitable supplier in the country rather than elsewhere, and to reduce the risk of a bad outcome that would harm the reputation of the whole country and the industry as a source of supply. This calls for liberal disclosure of very basic relevant information, for example, numbers of workers employed in each firm; the value of its sales, or turnover or shipments; the value of its exports in each year, and a precise description of the products it manufactures or exports. However, because data about individual firms is usually considered confidential and because governments are reluctant to appear to be favoring individual companies or supplying negative information about particular firms, they will typically provide only lists of firms that claim to be qualified.

A publicly funded body or, for that matter, a membership organization, faces considerable difficulties in providing information that fully reflects the greater suitability of one exporter over another for a particular buyer's purposes. This can be done verbally in some circumstances, particularly if the organization offers buyers face-to-face advice in this area. Yet many of the weaker firms will likely resist the collection and maintenance of partly negative information and its use as the basis of recommendations. Vigorous competition among independent private information suppliers can, however, fill this need.

Support services important for exports are numerous. A list of private service suppliers within a country that are potentially valuable for expanding manufactured exports follows below. Many of these suppliers can provide important export-related information as well as necessary services. An asterisk marks service categories in which foreign or
multinational firms can make a major contribution because of their wide experience and connections compared to the typical local enterprise.

- Accounting and auditing firms*
- Bonded warehouses
- Business publications*
- Commercial banks*
- Credit rating and credit checking firms*
- Customs expedite
- Design and product development consultants*
- Engineering and production consultants*
- Export market research and analysis firms*
- Foreign firms' buying offices and agents*
- Foreign trade consultants*
- Insurance companies (export insurance)*
- Investment and development banks
- Management consultants*
- Marketing consultants*
- Procurement and purchasing agents
- Product inspection and quality control firms*
- Shipping agents and freight forwarders*
- Testing and certification laboratories*
- Trading (export- import) firms*
- Warehousing and storage firms
- Wholesalers and distributors

The information, know-how, and advice these suppliers and others, for instance, exporters' associations and chambers, provide frequently overlaps. However, as long as inward-looking policies predominate, many of these private service suppliers remain concerned almost exclusively with the country's domestic market. Only after policies change decisively do they invest in developing services and training staff to meet the needs of export-oriented manufacturing industries. Thus improvements in policies toward manufactured exports are generally essential for the development of suitable support services.
Following policy improvements, a program designed to facilitate and speed the development of export-oriented private services might well accelerate export expansion. How best to implement such a program under different circumstances is a matter for surmise and experimentation. As far as we know, experience in actually doing this is still practically nonexistent.

**Assistance Through Time-Bound Projects or Project Components**

In proposing that aid be given through time-bound project components, we reject the alternative assumption that has thus far dominated development thinking in this area, namely, that support for export expansion is a matter of establishing, supporting, or reforming permanent public sector institutions devoted to and in control of the various aspects of this support.

Building institutions to support export expansion is not like building an electric power company or a central bank that will be organized and operated in much the same way throughout the country's development. Rather, experience in this area shows that institutions created in the early stages of a policy transition remain unsatisfactory and start to hinder export development as the country policies toward manufactured exports improve. Only by staying flexible during a policy transition can a developing country hope to make the most of its export opportunities and attain suitable institutions in the longer run.

Because of this, we favor a temporary infusion of specialized resources when and where they are most needed to achieve rapid increases
in exports. Where the need cannot be fully met through one such infusion, it could be pursued through another somewhat different infusions.

A project component directed at assisting export expansion through support services needs to address three interrelated tasks: (a) correcting exporters' weaknesses particularly in supply; (b) fostering service suppliers to meet a wide range of export-related needs, including assistance required within the time-bound project component; and (c) instigating a promotion campaign to "sell" exporting to local business people.

Who to Subsidize and How

Success in fulfilling three tasks outlined above usually depends on finding appropriate ways to subsidize the crucial services required. The leading alternatives are subsidizing or paying selected service suppliers directly or -- generally preferable -- giving cost sharing grants to exporters to help them pay for the services they need most. Box 1 presents practical and theoretical justifications for subsidizing support services to help enterprises expand manufactured exports.
Box 1. Justifications for Subsidizing Support Services for Manufactured Exports

Subsidizing services valuable for expanding manufactured exports can be justified in terms of economic theory as well as in practical terms, particularly if it is undertaken only for a limited period of time. Subsidies to services in support of exports are an internationally permitted means (and there are very few) of subsidizing manufactured exports that have powerful spillover or side benefits (what economists call positive externalities) for the overall economy. Side benefits can also be expected from the development of support services. The use of imported services appears, moreover, to have much larger positive results than most enterprises expect.

In a developing country, the export of manufactured goods leads to huge potential external benefits that cannot be internalized in the earnings of the exporting firm or those of the service suppliers helping this firm. These benefits involve, above all, technology acquisition, learning, and training. For example, people who gain experience in an exporting firm and then go to work for another firm or set up their own firm take with them the know-how and technology they have acquired. External benefits also come as a result of buyers' and customers' learning; imitation of successful firms; economies of agglomeration, including a more suitable division of labor; and improvements of products and technology in the domestic economy. Despite these large and numerous positive externalities, direct subsidies to manufactured exports are against the rules of international trade.

A pioneer service supplier may generate spillover benefits not only by expanding exports, but also by contributing to the emergence of desirable service activities and know-how benefiting the economy as a whole. Many of the eventual returns from the pioneer firm's efforts inevitably spill over to competitors and imitators and to firms in other activities, so its pioneer role may be thoroughly unprofitable without subsidies.

A different justification for subsidies is that exports (and hence services assisting them) are seriously underrewarded in developing countries that have only partially satisfactory policies toward manufactured exports. In particular, protection, exchange controls, depressed investment, and slow growth keep the exchange rate much less attractive for exports than would otherwise be the case. This justification disappears when policies and exchange rates become fully suitable for rapid expansion of exports, high growth, high investment, currency convertibility, and reduced protection.

Firms with substantial capacity and export potential, but still at a learning stage, often derive very large benefits many times what they pay for the services, even at the full market rate from effective support services of international quality. A further justification of subsidizing some services is that these services tend to be inadequately valued by potential exporters, while yielding benefits far exceeding what users are at first ready to pay. Providing subsidies to reduce the cost of these services may be essential to persuade exporters to use them and learn their value.
What forms of subsidy or equivalent assistance are cost-effective in promoting these export-related services in the early years of export development is an empirical and administrative question and a central issue for this study. Subsidies that promote competition within services and do not distort the pattern of services provided are obviously preferable.

Cost-sharing assistance to service users appears to be particularly suitable. Temporary direct subsidies to two or more pioneer firms (perhaps local branches of experienced international firms) to allow them to demonstrate the feasibility and value of a new service activity may be justified, but subsidizing only one demonstration service firm would be difficult to justify.

Importance of a Strong Promotional Package

Several studies in industrial economies illustrate the differences between firms that export and those that do not. Particularly useful is one by Bannock and his colleagues (1987) that highlights the following differences between active exporters and passive exporters or non exporters (see also Schwarting 1982; Cavusgil 1981):

- Active exporters view exporting as contributing significantly to overall profitability; the others do not.
- Top management in active exporters has a strong commitment to exporting and persists despite obstacles; exporting is seen as a board-level responsibility.
- In all active exporting firms, a board director spends several months each year overseas.
• Passive exporters and non exporters are daunted by the added complexity of exporting; active exporters use service suppliers liberally at the start of their exporting experience.

• Only passive exporters and nonexporters see language as a problem.

• Of nonexporters, 55 percent have never tried to export.

These findings have important implications for external assistance for export development, since increasing the ranks of active exporters is one key to the systematic expansion of manufactured exports. Any project to expand exports should include specific promotion measures directed at turning passive exporters and nonexporters into active exporters. Thus a project generally requires a promotion campaign that will reach the top management of firms in the product groups the project is targeting or those considered most promising. It may also reach out to entrepreneurs in all industries.

Top management need to be convinced that exporting can contribute significantly to overall company profitability, even if unit price realizations may be lower than in the domestic market. The promotion effort should also show management that the added complexity of exporting need not be daunting, and that using service suppliers liberally at the start of the process is the way to handle this complexity. Management needs to be made aware that the government and the team managing the promotion are making active efforts to make the support services needed to assist the export take-off accessible and available, and to provide firms with sources of advice and help in identifying suitable service suppliers.
An Integrated Package of Assistance Around One or More Grant Funds

In India and Indonesia, the World Bank has pioneered the use of cost sharing grants as the core of promotional and service-fostering packages aimed at encouraging and assisting businesses into active exporting. These grants cover up to half the cost of a firm's programs to improve and adapt its supply, market development, and related export development operations. Firms can use the grants to help pay for expert services and travel associated with market exploration and initial marketing. Matching grants are the rule to ensure that the firm has a financial stake in getting value for money. The availability of the grants serves as one inducement in a powerful promotional and service-fostering assistance package. In India, the first two grant funds started in 1986 were followed by another four in a 1989 project, including successors to the first two managed by the same institutions.

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3/ Grant funds are also proposed as components in other World Bank projects now being prepared. Somewhat similar grant assistance for services is given in a less public fashion by many successful exporting countries, most of them in Western Europe. An openly publicized grant program, through the Market Development Fund of Singapore's Trade Development Board, was started over a year before the World Bank's first use of grant funds in India. Ireland's CTT started a grant fund for marketing in 1961 and another for design assistance in 1962. However, the World Bank's grant funds have been the first major ones set up through external assistance and are unusual in their emphasis on consultant assistance relating to supply.
Active Firm-Level Promotion

Efforts to promote exporting face strong resistance among businesses. After experience with import substitution, entrepreneurs tend to mistrust profoundly any approach from a publicly funded operation trying to persuade them to invest their time and money in new directions. A persuasive promotional package is needed to overcome this resistance.

The promotional package in India is particularly comprehensive. Free advice is given initially to back up the sales message. Salespeople for the Export Marketing Fund have learned to undertake library research in preparation for this first visit to find out more about the company's products and potential export markets. By doing this, salespeople are able to stimulate initial interest and to make their program very different from the publicly funded operations that management has come to mistrust.

While discussing the firm's export development plan and offering help in drawing it up, the salesperson encourages the firm to use commercial support services in carrying out the plan. Experience has shown that firms new to exporting are generally slow to recognize the value of external advisory services. Reducing this resistance early on is important, since the support provided by external services at an early stage can make a huge difference.

The firm's leaders are told that not only will advice be available on identifying appropriate service suppliers, but also that cost
sharing grant assistance will be available to cut the initial cost of these services. Loans may also be available to help fund the costs of upgrading production. Moreover, the grant fund administrators stand ready to help firms design and prepare their grant applications.

Perhaps the most attractive element in the promotional package, especially in India, where controls abound, is that the unit delivering the promotional package is able to ease the firm through a wide range of important government clearances, which have been delegated to the committee that approves grant applications. The availability of this "one-stop" facility often makes all the difference in persuading firms to start taking exporting seriously.

Other Important Features of Grant Fund Schemes

In the grant schemes already under way, matching grants are given for a range of export marketing and supply-related activities, so long as they are undertaken as part of a properly planned export expansion program by an individual firm. This mechanism is designed above all to encourage firms to improve their supply capabilities and engage in appropriate preparation prior to actual selling.

In a setting where initial resistance to using services is particularly strong, the first two or three days of assistance might be fully grant funded to expose firms to the services consultants can provide.

As Ireland's experience has shown, however, not going on too long with grants is important, else a "grant culture" will develop, in which exporting becomes dependent on receiving a continuing stream of grants.
Applying the infant industry principle to subsidies, we suggest that firms are made aware from the start that grants will only be offered for an initial fixed period to launch exports. A second grant will not be given except in certain exceptional circumstances. When further grants are given, we are in favor of increasing the firm's percentage contribution to ease the eventual transition away from grants.

Rules and procedures must be established to prevent grants from being diverted into activities that would have been undertaken anyway or being used for unproductive purposes. By way of example, the Export Marketing Fund in India is restricted to providing assistance only in difficult and highly competitive markets, and then only to firms marketing products that are new to them, entering markets that are new to them, or making a major change in the marketing of an existing product in an existing market. In its first years, the fund was further restricted to exports of 11 engineering product groups.

Rules such as these also have the advantage of focusing the promotional effort. The Export Marketing Fund team actively promoted exporting and the use of the fund to virtually all competent firms in each eligible product group. Sitting back and waiting for applications is unlikely to prove effective, whatever the rules.

Complementary Loans

Another part of the package can be a loan fund for export-oriented investments, administered by the same body as the grant fund.
Loans are made available for activities that complement the recipient firms' grant programs but do not qualify for cost sharing grants, such as purchasing testing and quality control equipment or data processing equipment, or expanding or re-equipping an existing plant.

Using matching grants or other subsidies for such purposes would be contrary to World Bank practice and open to objections and possible countervailing duties under GATT trade rules. Subsidies for services exporters use do not normally meet with such objections, unless the subsidies are linked in a one-to-one relationship with the direct costs of producing a particular item.

The World Bank has set up complementary loan funds along with its four new export development grant funds in India.

Provision of Services by Donors

As an alternative to the grant fund method, an increasingly common method for achieving a temporary injection of resources to assist export expansion involves giving assistance in the form of specific donor-organized support services that help selected firms in promising product groups. This substantially reduces the choices available to users, so that we consider it inferior to the grant fund method in most circumstances. However, some bilateral donors and the European Community tend to favor this alternative method. One reason is that the aid can easily be tied to specific national suppliers of services.

Examples of this alternative method can be found in some EC trade promotion projects in recent years, such as one in Egypt being run by the
Trade Development Institute of Ireland, and in an integrated project that one of the authors (Singer) designed and is helping to implement in India for DeCTA.

The essence of the method is that a project or project component is contracted out to a private firm, typically a consultancy firm, that organizes and arranges consultant assistance to selected firms with promising export potential in a small number of product groups with strong export prospects. In each of these product groups the firms assisted face similar problems. Thus one consultant can stay on the job for a considerable period and work individually with each firm, minimizing the travel costs for each visit. In the more effective schemes of this type, charges to the firms cover a substantial share of the costs. Assistance is mainly in supply-related aspects of exporting, but assistance in selling may also be provided once firms are ready for it. With the help of mid-course evaluations and corrections, resources are concentrated in the export activities that show the best prospects or best results.

The export activities assisted are chosen because they have recently become or are expected to become profitable, and a large expansion of these exports appears likely once the firms learn the necessary techniques and supply skills. Thus this method is best suited to a populous country with low labor costs in which policies toward exports are improving rapidly for several industries at once.

As with a grant fund, spillover benefits are likely to occur as key people from the assisted firms move to rival firms or set up their own
businesses, and as firms imitate successful export activities. Local firms generally collaborate in providing the services and may gain useful training as a result, but the main consultants are brought in from abroad. No significant permanent addition is made to the institutions in the national economy.

Guidelines for Detailed Design of a Project Component

Complementary to our four major recommendations are further proposals concerning detailed the design of a project component in this area.

Duration of a Project Component

Present practice suggests project components that last three to five years, but there is plenty of scope for further experimentation. For instance, the initial analysis and preparation phase could constitute one project component, followed later by a more extended component.

Institutional Consequences

Actions aiming at a rapid expansion of exports within a few years contribute to the creation of suitable support service suppliers through a creative process of learning and experimenting. Such a gradual, interactive process avoids the problems that result from freezing the institutional structure or recruiting permanent staff prematurely. A donor such as the World Bank can follow a first project component with a second that amends and improves the delivery mechanism.
Investment Promotion and Support Services for Exporters

Project components for promoting investment and providing support services for exports should almost certainly be kept separate. There is essentially no overlap in business customers or concerns between investment promotion and the support services discussed here. Experience suggests that when export promotion services to locally owned firms are combined with investment promotion, one task nearly always dominates to the detriment of the other.

Targeting Exports and Monitoring Results

We strongly favor specifying the impact each unit of expenditure in a project component should aim at, measured in terms of the value of the exports that result, and then carefully monitoring the exports generated. All activities under the project component should lead to additional annual exports of at least a specified multiple, such as ten times the once-off project costs incurred, with these exports expected to continue for at least five years. Projects in India for DeCTA and the World Bank are using this approach. Experience with it indicates that it

4/ In the case of a matching grant, from the exporter's point of view, the discounted stream of profits from additional exports has to exceed the enterprise's half share of the costs of the consultant. From the government's point of view, the half it contributes (generally borrowed from a donor) ought to be more than offset by the value to it of positive spillover benefits (externalities) from these same exports, and/or additions to revenue generated. This is a more subjective and problematic calculation. A simple practical rule such as we suggest here is meant to ensure that these conditions are met. If the time profile of returns is unusual, a discounting procedure or another rule may have to be used.
is a highly effective management tool for running such projects. However, monitoring may have to continue for, say, two years beyond the commitment of the funds to be able to judge the results.

**Built-In Flexibility and Mid-Course Corrections**

In a period of policy transition, the realities of exporting change quickly as policies are improved with the help of feedback from exporters and as firms take up new profit opportunities. Accurately anticipating what will happen and what the results will be for exports is not possible.

A project design fixed in stone for three or more years cannot allow for unexpected changes, as EC assistance now recognizes. The three-year DeCTA project in India has incorporated an annual progress review into the project design, which leads to an annual redistribution of resources among separate activities, depending on relative progress in different subsectors and changing circumstances.

This means that the World Bank's continuing insistence on fixing the design of a project component for its entire duration is inappropriate to the assistance under discussion and should be modified. It may work well for large fixed-investment projects, but it works less well, in our view, for support for export expansion.5/

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5/ We know that in practice, some World Bank projects are modified during implementation as part of the supervision process, but too often the original legal documents set tight limits on the degree of modification possible. The paucity of resources devoted to supervision constitutes a further constraint on mid-course corrections.
A useful element of project components in this area is the inclusion of built-in flexibility. Thus, if the project component provides support for three to five preselected subsectors, the allocation of resources among them could be only partly fixed in advance, and the subsectors could compete for the remaining resources based on their export results or firms' detailed proposals. In some instances it will be useful to include one separate, open-ended activity for assisting subsectors that emerge as successful exporters during the life of the project. Or some part of the funding can be preassigned to the chosen subsectors and another part set aside for a wider set of manufactured exports.

Concentrating on Promising Product Groups

A grant fund may be limited to certain product groups or industries. The first two grant funds in India were initially limited to selected engineering products, but were later extended to all manufactured products. The more open the grant fund, the less likely it is to exclude unique products with export potential, and the less the need to pick winners. However, the promotion that accompanies the fund should be targeted first at the firms considered likely to give the best returns in terms of additional exports per dollar of grant expenditure. Selecting the most promising product groups can be an important aspect of choosing firms to be targeted. In the case of a project component that provides specific support services directly, concentrating on particular product groups is a central part of the design of this component.

Modern thinking treats the concept of comparative advantage as dynamic rather than static, recognizing that although the starting point
in exporting may be low labor costs, before long, successful exporting units will depend on acquired advantages for much of their success, including skills acquired from previous export experience. The existing manufacturing base is an unsatisfactory starting point for analyzing export expansion. Typically this base has been developed specifically to substitute for imports, and most of it has little prospect of becoming internationally competitive. Analyzing it, even using sophisticated concepts, may reveal little about where the country's manufactured export opportunities lie.

Searching for elements of uniqueness in factor supplies, the availability of inputs, labor skills, relative factor costs, location, and transport costs can be more useful as a starting point. Also important is searching for what we call "attributes with uniqueness," such as promising exports or export potential in unusual products. One way to do this is to examine export flows to discover the existing strengths they indicate.

Attention should be paid to the opportunities offered and the limits set by the system of bilateral textile and garment quotas in force in leading OECD countries, as well as preferential arrangements in these products. Under the Multifiber Arrangement, the amounts of particular garments and the specific textile products that will be acceptable as imports in a major market without the imposition of quotas, and the approximate levels attainable if quotas are imposed, are known in advance. Thus a developing country can design a strategy to develop these export industries based on its right to quotas.

The person doing this analysis should also carefully examine the effects of recent policy reforms in the country since, in a transitional policy situation, the latest policy improvements may open the way to exciting new profit opportunities in exports. India, for example.
exported much good-quality leather in the form of shoe uppers and more as finished leather. Then, within the last three or four years, reforms made imported shoe machinery, shoe components, and materials accessible to firms making shoes. This has created an opportunity for firms to move from making uppers into full shoe production wholly for export. The DeCTA project is concentrating on helping firms manage the move from simple sewing of shoe uppers into more fully mechanized, flow-line assembly of finished shoes. Already it is clear that the export returns on this technical assistance expenditure will be dramatic.

Evaluating Constraints

To facilitate and expand the export of particular products, project planners must examine the present state of each link in the export chain for the product, to ascertain whether it is acceptable to large buyers. This evaluation requires interviewing exporters, potential exporters, buyers, and others. The assistance under the project can then be designed to address the particular constraints to export expansion. Unless assistance addresses the main constraints affecting each product or product group, it is unlikely to have any impact on the expansion of exports.

Selecting Firms to be Assisted

Scarce and expensive new services need to be directed at firms that will make the best use of them in expanding exports. This inevitably implies some mechanism for selecting firms.
In the first selection round, promotion efforts, and perhaps the services themselves, are targeted specifically on selected subsectors or product groups, and on the more promising firms within each group. If service development is supported through cost sharing grants to exports, grant recipients can largely be left to do their own selection within these subsectors on a first come, first served basis.

If specific services are to be provided through the project component, further selection rounds are needed. In the second round, trying to preempt the ruthless selection that the market will eventually make is desirable. This can be done by using a surrogate for the community of buyers in selecting the firms to receive scarce services. Such preselection can improve overall cost-effectiveness by concentrating services on the eventual winners.

One method for doing this is to send an expert familiar with the target market's preferences on a tour of applicant (or eligible) firms to select firms "on behalf" of buyers. CBI and DeCTA are already using this approach. Another mechanism CBI uses is to conduct a market test on buyers using product samples from applicant firms. The buyers' responses are used as the basis of selection for further assistance.

Even when a buyer-surrogate approach to selection is used, we strongly favor charging for the services. Thus the final selection criterion is willingness and ability to pay. Charging for services also improves the motivation and attitude of firms being assisted. They take much more interest in the details of the assistance provided to ensure that they get value for their money. Charging also adds to the resources available for assistance. We believe that ITC's enterprise-oriented
Additional Measures to Expand Service Supply

A time-bound project component typically requires the importation of suitable support services for export expansion in the product groups targeted. Development of a local supply of suitable services may sometimes be a feasible additional objective. The choice of how to bring forth the supply of needed services depends above all on what is possible in the given context. Firms in India supported by the World Bank's Productivity Fund and Export Marketing Fund have relied for the most part on consultants and services provided by experienced international service firms overseas, including Japan, Singapore, and other Asian countries as well as countries in Western Europe and North America.

DeCTA's India project provides services entirely in the form of temporary outside injections of British technical assistance to meet the temporary needs of export expansion. Thus, for example, British production management experts helping Indian firms get started in shoe assembly provide their services only in the short term.

Developing Export-Oriented Services

The potential exists of offering grants from a grant fund not only to prospective exporters, but also to service suppliers interested in offering suitable services to exporters. These enterprises could be asked to submit plans for reorienting their services. Key elements of these plans could then be funded through cost-sharing grants.
This was attempted in each of the first two grant funds in India. The World Bank tried to induce local service suppliers to provide services for exporters by offering generous grants to support set-up costs, including training; however, this attempt failed. The grants were directed to the management consultancy segment of the consultancy services subsector, which at that time did not view export consultancy as a profit making opportunity. No grants were applied for. The timing was probably too early, and the idea is worth trying again.

Grant Funds and State-Provided Services

The use of grant funds for services provided by public sector institutions presents certain dangers. The grants are likely to be misused in one way or another. In our view, such assistance should be conditional on the full commercialization of these services within a set period, and on the state extending no special privileges or advantages to its own service providers.

Selecting a Local Institutional "Hook-Up"

Choosing an institution to manage and implement a project allows considerable scope for experimentation. Part of the challenge is to select an arrangement where the individuals involved are strongly motivated to achieve the results desired. Managing a grant fund and carrying out the necessary promotion campaigns calls for people with a strong business background in marketing and production management. To attract and motivate such skilled people, offering them permanent positions in an ongoing organization with an assured future may be necessary.
We see two options here. One is giving the management task to one or more permanent local institutions, such as development, investment, or commercial banks. The second is to give the task to a consultant firm (generally from abroad) operating under a term management contract.

In India the World Bank has had good results from directing its grant fund assistance through an industrial development bank (ICICI) and the country’s export-import bank. Both are well managed and strongly concerned with exports. Some of the skilled people required to manage these funds were recruited from private businesses. Two leading state-owned commercial banks now also manage export development funds. Through managing a grant fund, financial institutions such as these have an opportunity to identify new lending opportunities and extend new loans. They can also acquire valuable information and insights that allow them to expand and improve their services to customers. Staff in such institutions can thus be strongly motivated to manage and promote the grant fund effectively and to help make grant recipients succeed in exporting and in expanding their businesses.

An alternative being proposed in World Bank projects now being prepared is to delegate the administration of the grant fund, under a management contract, to a suitable firm of management consultants. The terms of this contract would include bonus payments related to specific measures of performance, such as additional exports directly generated.

In Indonesia, the World Bank helped establish a new organization to take charge of a grant fund. The Export Support Board (ESB) was intended to be independent and run by people from the private sector. However, its newness and a need to comply with public sector budget and
expenditure procedures have weakened its initial effectiveness. So has pressure from the Ministry of Trade and the official trade promotion organization, which is a directorate of the ministry. As a result, the World Bank has had to defend ESB's independence. The staff's concern about ESB's and their own future, after the grant fund is spent has also caused a variety of difficulties. Yet despite these institutional difficulties and the consultants' unfamiliarity with the grant fund concept, the exports generated, particularly by supply-related assistance to firms, have (as in India) been very large relative to the grants given.

When designing grant fund schemes, World Bank staff typically find themselves under pressure to delegate implementation to the existing trade promotion organization. We definitely do not favor this approach. If the TPO both provides support services and approves grant applications, serious conflicts of interest will inevitably arise. The body approving grant proposals should have no vested interest in the supply of paid services. Moreover, these organizations are typically ineffective and do not enjoy the confidence of the business community. Motivating their staff to do this task well would be likely to prove extremely difficult.

As an alternative, experiments using nongovernmental organizations to deliver the promotional package could prove fruitful. A private bank would almost certainly be suitable. In some developing countries, chambers of commerce or exporters' or industry associations may be sufficiently strong to handle this function. An altruistic not-for-profit foundation might be another alternative. Motivating the staff involved to do the task well while avoiding undue favoritism may well be feasible in all or most of these arrangements. However, government resistance to the concept of delegating the responsibility for
administering government funds borrowed from the World Bank to a private organization would need to be overcome. Investing the authority to approve grant applications in a committee dominated by government representatives would almost certainly be necessary.

Under the alternative method of providing support services directly, a consultancy firm based abroad generally undertakes management functions.

Discontinuing Unsatisfactory Arrangements

Our recommendation to rely on time-bound projects, while intended to apply to external assistance, can also be implemented by a developing country in its own programs in this area.

As new delivery mechanisms are created, we recommend that the use of methods and institutions that have proved unsatisfactory be systematically discontinued. Public or mixed public-private organizations providing export-related services are likely to perform better if they know that their future success and survival depend on the demand for their services, or at least their association with successful export expansion. Service quality can usually be improved by eliminating institutional arrangements that work badly.

Summing Up the Strategy

Our four main recommendations, in their simplest forms, combine to form a strategy for swiftly expanding manufactured exports by improving the export capabilities and performance of enterprises with strong potential in the most promising export industries.
We recommend that donors build project components around grant funds and direct each time-bound project component toward the overriding objective of expanding exports within the project's time frame. At the same time, we recommend that the country be persuaded to dismantle policy obstacles to the use of consultants and other service suppliers from abroad, and that the country and aid donor both concentrate primarily on improving firms' know-how and performance in the supply aspects of exporting.

To accelerate exports further, we also recommend fostering competing, predominantly private service suppliers based within the country as well as abroad. What is needed for this, most of all, is a favorable policy environment on all relevant fronts and vigorous, diversified export growth. Subsidies to service users through a grant fund are likely to contribute to the growth of the market for commercial services.

The World Bank's Potential for Popularizing These Approaches

The World Bank now has a unique opportunity to develop effective instruments of assistance in the field of export promotion. Many developing countries are in desperate need of foreign exchange. The Bank wants to use policy reforms to encourage outward orientation, boost economic efficiency in the industrial sector, and contribute to growth through export expansion. Policy reform is undoubtedly central, but attention to services in support of export expansion represents a unique opportunity to sustain the reform process and boost exports faster.

The Bank is well positioned to adopt and popularize the approaches proposed here. It is not committed to any particular approach
in this area. Its concern is typically to encourage developing countries to undertake sensible policy improvements to foster export and industrial development. Its loans are generally conditional on progress in this direction. The Bank is not restricted by a narrow mandate preventing it from giving policy advice. Revising its activities in this field requires no prior complex negotiation among numerous recipient countries and donors.

As the world's leading development assistance agency, moreover, the World Bank exerts much influence on other donors and on developing countries' economic policies and strategies. It has long used this leadership to encourage the adoption of outward-oriented policies. Encouraging new initiatives relating to export support services would be a natural extension of this active role.
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<td>Donald B. Keesing, Andrew Singer</td>
<td>November 1990</td>
<td>S. Fallon 37947</td>
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