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*Chervinski Y.A.***IMPORT SUBSTITUTION POLICY:  
CONCEPTS, METHODS  
OF ANALYSIS AND MAIN AREAS  
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The article analyzes the existing methodology of import substitution, investigates the mechanisms and objectives of its implementation, suggests possible directions of improvement of this economic strategy.

**Keywords:** substitution of import; import substitution policy; national goods transitive economy; technological innovation; the dynamics of domestic demand; quantitative import quotas; changes in the structure of the economy.

*Червинский Е.А.***ПОЛИТИКА ИМПОРТОЗАМЕЩЕНИЯ:  
ПОНЯТИЕ, МЕТОДИКА АНАЛИЗА  
И ОСНОВНЫЕ НАПРАВЛЕНИЯ  
СОВЕРШЕНСТВОВАНИЯ****Червинский Евгений Александрович,***научный сотрудник Центра мировой экономики и внешнеэкономических исследований**Институт экономики Национальной академии наук Беларуси,**ул. Сурганова, д. 1, корп. 2, Минск, 2220072, Республика Беларусь**E-mail: e.chervinski@gmail.com***АННОТАЦИЯ**

Анализируется существующая методология политики импортозамещения, исследуются механизмы и задачи ее реализации, предлагаются возможные направления совершенствования данной экономической стратегии.

**Ключевые слова:** политика импортозамещения; национальные товары; транзитивная экономика; технологические инновации; динамика внутреннего спроса; количественное квотирование импорта; изменение структуры экономики.

## 1. Introduction

The current stage of development of the world economy is characterized by the increasing role of trade. Trade is an important element in the dynamic development of the national economy. However, the prospects of imbalance between exports and imports are a negative aspect of the process. International division of labor provides countries with opportunities to increase exports, but increasing dependence on imports and negative trade balance.

An integrated approach is necessary to support the export potential; for rational use of imports in the country; to ensure the competitiveness of national products on the world market in the long term. The results of the global financial and economic crisis actualized the problem. The crisis provoked reduction of national economies and increased competition in international markets. Import substitution policy is a means of solving this problem. It involves the gradual replacement of imported goods by the domestic goods. But there is a need for specialization in production, which has raw materials, energy, territorial priorities. [1, p. 100-106].

## 2. Research findings

The first attempts of import substitution take place due to the crisis of the western economy known as the «Great Depression». During this crisis the decline of purchasing power of foreign markets led to a drop in the world trade. The crisis affected Latin America the most, where economies are dependent on exports of raw materials to the United States and Europe. To overcome the gap in these countries a new economic policy was adopted, known as «import substitution industrialization».

Southeast Asia is another region, which used the policy of import substitution. It began in the middle of the previous century, that is the later period in comparison with Latin America. Currently there is an interest in import substitution policy from countries with transitive economy. The interest is determined problem of balance of foreign trade and a need to change economic systems.

Analysis of practice of import substitution in the transition economies helps to classify its main objectives, modalities and mechanisms for implementation, to determine the results.

### a) Aims

The main objectives of the policy of import substitution in Latin America and Southeast Asia were industrialization and catching the

economically developed countries. Currently in the countries with transitive economy the import substitution policy aims to improve the trade balance and reduce imports. This is determined by the decrease in the competitiveness of industry and agriculture. This fact determines the value of import substitution in the system of economic policy. In the past it was the dominant component of the economy. Now it is a subsidiary mechanism of diversification of production and optimization of foreign trade.

### b) Conditions for

The specificity of «import substitution industrialization» in Latin America is justified by the objective prerequisites. Significant resources helped to provide their own raw materials for industry. Large volumes of domestic markets kept demand for domestic goods at a high level. This created conditions for economic development at the expense of domestic consumption. Products the new industries replaced foreign goods, which reduced the cost of imports and to supported modernization of domestic economy. This is the specificity of import substitution policies in Latin America.

In South-East Asia the background of import substitution policy was less favorable. This is due to the small size of the domestic market countries such as Singapore, Taiwan, South Korea. Lack of natural resources reduced the competitive advantage. They were not allowed to develop at early stage due to the export of raw materials. Therefore, the import substitution strategy was focused on a limited number of goods. The production of such goods does not require large investment costs, it is not a high-tech and it provides a stable demand.

In the Commonwealth of Independent States (Azerbaijan, Kazakhstan, Russia and Ukraine) decided to develop import substitution industries was adopted. Some of them are commodity exporters with significant domestic markets. And in the long term this economic strategy can be success. In these countries import substitution policy is not seen as a central element in the development. It is a complementary mechanism for diversification of production and optimization of foreign trade relations. This policy promotes restoration of industry which stagnated after the collapse of the Soviet Union.

### c) Implementation details

In the structure of import substitution policies of Latin America there can be two main phases:

– the first phase of import substitution, which came in the middle of the 20<sup>th</sup> century, was oriented to the development of the national branches of food and light industry;

– the second phase, which began in the sixties of the previous century, provided import substitution of heavy industry.

In the early stages this policy led to the rapid growth of the Latin American economy, but later the growth slowed down, the macroeconomic problems aggravated. Under these conditions neoliberal economic reforms were implemented in Latin America. They included: the opening of domestic markets, reduction of social spending, reduction of the state control and debt restructuring. The result was a long crisis: the gross domestic product reduced, the standard of living fell, unemployment increased [1, p. 67-70].

The first stage was the most productive period of import substitution industrialization for Latin America. At this time there was organized a new production of consumer goods of medium-term and short-term use. This kind of product is not capital intensive and allows you to adjust its output in the short term. The volume of the labor force in Latin America was sufficient, and production technologies were low. Such conditions do not require large expenditures on training and scientific and technical base. The problem of formation of light and food industry as a whole was successfully solved. However, the manufactured products were not competitive in comparison with the imported analogues.

In the second stage of import substitution difficult problem was to organize production for production purposes. It demanded to increase investment spending, to strengthen the costs of preparing of qualified professionals to enter the technological innovations. Reduction of dependence on imports of consumer goods in the Latin American region determined the dependence on foreign equipment and technology. This eliminated the savings of foreign currency obtained in the process of import substitution. Foreign currency earnings from exports were insufficient. There is an active attraction of foreign capital in the form of equity and loans. This led to increase in external debt. Heavy industry became not profitable, it focused on the domestic market. Slight demand for their products is not possible to achieve cost savings in the volumes. It's not possible to achieve a high level of competitiveness.

Implementation of the policy of import substitution in Southeast Asia was held later than in Lat-

in America. This helped to use the experience and avoid mistakes.

In the first phase there were formed the branches of food and light industries. The main emphasis was placed on the diversification of production. There was been a saturation of the domestic market products and increased demand for foreign currency funds. This caused a shift to the export-oriented economic policy.

In the process of export strategy there was increased demand for machinery and industrial equipment. This caused increase in imports and wage growth. The ability of import substitution industries to compete reduced gradually. The next step was industrialization. There began the creation of heavy industry.

The transition to export-oriented economic policy was complemented by the reduction in imports and restrictions on the import of goods from abroad. Liberalization of legislation occurred only after ensuring the rapid growth of exports. National production capacity was achieved to compete in world markets.

Post-Soviet countries with economies in transition developed industry. They do not have the need to implement the first and the second stage of import substitution. Making the new products is determined by competitive advantages, the dynamics of domestic demand and imports. For example, in the countries with large reserves of natural resources the priority vector of import substitution is manufacturing. In countries with a tradition of cotton the growing development of light industry is a priority. For transitive economy the production of various labor, capital- and knowledge-intensive should be completed.

#### d) Mechanisms

The means of tariff and non-tariff barriers were used in Latin America during the import substitution industrialization to support young plants. There were used high tariffs and strict import quotas. There took place artificially low exchange rate for the maintenance of domestic and foreign producers of discrimination [2, c. 60-62]. Funding was provided from the own sources of commodity export. Foreign direct investment and financial resources in developed countries were also attracted. The reserves of the International Monetary Fund and other credit institutions were used [3]. Large support costs of the manufacturing sector and social programs provoked imbalances in the macroeconomic sphere and large budget deficits. Hyperinflation in the 70s reached 1000% per year [4].

In South-East Asia in the early stages the financing of projects of import substitution was done using financial assistance of Western states. The support for Taiwan by the United States in the period from 1951 to 1965 amounted to 1,444 million dollars. [6, p. 31]. It compensated the lack of foreign currency and reduced the state budget deficit. The share of US funding in the national savings of Taiwan until 1961 was 40-68% [5, p. 31]. Such economic policy ensured the development of domestic sources of financing and increased their volume.

To be competitive in the international market and to protect domestic producers in South-East Asia the multiple exchange rates were used. Restrictions were placed on currency exchange of importers, ban on the import of luxury goods, devaluation the national currency. Taiwan was overvalued exchange rate of the national currency. This has a negative impact on the country's export potential, but domestic price increases and the increase of the cost of imported goods were stimulatory. They stimulate the production of goods for the domestic market. The relative prices of import of cotton in relation to export of rice increased by two and a half times. Rice is one of the main export commodities. [5, p. 44].

In the initial stages of import substitution policies there were introduced various restrictions to control the amount of imports. Without governmental approval the enterprise could not be imported to the amount of more than the volume of their exports. There were applied quantitative import quotas, used special permits lists for the imported goods. The lists included raw materials for domestic enterprises products export. Customs tariffs are low or zero. Licensing, tariff and non-tariff measures were restricted for foreign goods. There were used a ban on the import of products that were domestic counterparts with adequate security and quality. There were applied differentiated tariffs: low for raw materials, high and prohibitive for industrial goods and consumer demand luxuries. The restrictions on the import of goods from Asian countries are direct competitors. This stimulated the efficiency of import in the industry.

With the growth of export restrictions the foreign trade gradually declined. The size of import tariffs on finished products consistently reduces. There is a transition from permissive to restrictive lists of goods. Their import is reduced by additional taxation. The government reduced the protective measures for their industries. The industrial sector

is competitive and the products are in demand in foreign markets. Decrease of security developed industrial sectors accompanied by support of growing enterprises. There were imposed the restrictions on imports competing with the products of the young national enterprises. The measures of tariff regulation which used by Taiwan authorities were protectionist. It is noted by many researchers [6, p. 95].

In modern conditions the possibility of restrictive measures significantly reduced. Today in the import substitution policy the priorities are incentives. An important regulatory factor is the use of governmental and industry programs.

In Russia the first stage of import substitution, which took place after the 1998 crisis was caused by the devaluation of the national currency. Decline in real incomes of the population led to higher prices of imported goods in the domestic market. Consumer demand shifted to domestic production [7, p. 117-120]. Now the activation of import substitution policies implemented through sectoral development strategies of industry. The development of heavy engineering, automotive, chemical and petrochemical industry, pharmaceutical and other industries was regulated by the Federal Law «On the National Industrial Policy in the Russian Federation». The draft law is aimed at elimination of technological backwardness of industry, improving the competitiveness of products, expanding the range of manufactured goods. The displacement of foreign competitors in the domestic market is relevant [9]. Under the rules of the WTO the actions to displace foreign goods from the domestic market can be not recognized by the market.

Import substitution policy was also implemented in the Republic of Kazakhstan. Kazakhstan adopted: «The program of import substitution in light and food industries for 2001-2003» [10] and the «State program for accelerated industrial and innovative development of the Republic of Kazakhstan for 2010-2014» [11].

#### e) Results

The results of import substitution industrialization in Latin America are contradictory. It is necessary to recognize the success of the individual elements of the strategy to diversify the national economy and create new industries. There was achieved a high growth of gross domestic product in the medium term and gradual reduction of the export of raw materials. The transition to industrial economy boosted exports of consumer and industrial goods.

However, import substitution policy had negative aspects. The industries were formed under protectionism. They were unable to compete in the open market situation. Orientation to the maximal number of import substitution products led to its horizontal nature. This led to the increase in budget expenditures to support the industry. The closed nature of national markets provoked the emergence of monopolies and reduction of competition. Protection of industry provoked technological backwardness, inefficient enterprises and the growth of prices for their products. Agriculture had no preferences, so there began stagnation.

In Southeast Asia there was another approach. The harmonious combination of export and import policies allowed developing successfully. The industries focused on domestic demand gradually became export leaders. Labor-intensive, capital-intensive and technology-intensive industries developed. An integrated approach to restrictions on the import and export development strategy promoted successful industrialization. This provided the balance of the trade balance figures.

There was the formation of the new industries to develop infrastructure, to create financial institutions and transport. There took place state regulation of export-import operations to ensure the effectiveness of economic modernization. During the formation of the industrial economy the state regulation weakened. It was carried out by financial liberalization and increased competition in the domestic market states. The developed system of light and heavy industry stimulated the production efficiency. The private sector share in the Taiwanese industry in the early fifties was about 40%. And in 1980 it increased to 79.1%. This effect is provided by market reforms and liberalization of economic relations. [6, p. 85]. The negative effects of the conservation industry in the domestic market were overcome. In the countries of the Commonwealth of Independent States the import results are specific. The results are depend on the macroeconomic situation in the country. The volume of domestic and foreign investment determines the specificity of import substitution.

Countries with large reserves of minerals have growth of national output in the manufacturing sector. However, some states do not provide import substitution in agriculture, food and light industries due to price competition and the lowering of customs barriers.

The first phase of import substitution has not resulted in significant economic effect in the Re-

public of Kazakhstan. In Kazakhstan the first phase of import substitution failed to secure economic benefits. At the same time the second phase of import substitution has been successful [12, p. 15-18]. Engineering has developed successfully in countries that are able to ensure the growth of investment in this area due to the export of raw materials. There are primarily the Russian Federation, the Republic of Kazakhstan. One of the distinctive trends in this area is actively attracting foreign direct investment to ensure import substitution. So almost all the leading car manufacturers have their production in the Russian Federation, including Renault, GM, Ford Motors, Volkswagen,

### Conclusion

Import substitution policy is a set of measures aimed at stimulating production and competitiveness of domestic goods, increasing of domestic demand optimization of demand for imports. It is determined by the need to reduce the dependence of transitive economy on economic leaders. The main objective of the policy of import substitution is to encourage national production, to development the new products to stimulate demand and import restrictions. Actual directions: industrial restructuring, the balance of foreign trade, protection of the domestic market during the transition period. In the Commonwealth of Independent states import substitution is a complementary mechanism for diversification of production. Mechanisms for implementation: preferential loans and taxation, overvaluation of the national currency, governmental regulation. Ways to restrict imports: tariff regulation, quotas, introduction of limitation lists and multiplicity of the national currency.

Improving the competitiveness of new production provides vertical strategy of import substitution. It is aimed at meeting the intermediate demand of domestic enterprises. The horizontal structure? oriented to fill the maximum commodity nomenclature? is less effective.

Factors contributing to the policy of import substitution: large capacity of the domestic market, natural resources, ability to provide investments in the industry due to raw materials export.

The main vector of implementation of the import substitution policy:

- Improving the competitiveness of national products;
- Reorientation of industries from the domestic market to foreign markets;
- Effective integration into the global division of labor.

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