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Review

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- Three dots (...) indicate that data are not available or are not separately reported.
- A dash (—) indicates that the amount is nil or negligible.
- A blank space in a table means that the item in question is not applicable.
- A minus sign (-) indicates a deficit or decrease, unless otherwise specified.
- A point (.) is used to indicate decimals.
- A slash (/) indicates a crop year or fiscal year, e.g., 1970/1971.
- Use of a hyphen (-) between years, e.g., 1971-1973, indicates reference to the complete number of calendar years involved, including the beginning and end years.
- Reference to "tons" mean metric tons, and to "dollars", United States dollars, unless otherwise stated.
- Unless otherwise stated, references to annual rates of growth or variation signify compound annual rates.
- Individual figures and percentages in tables do not necessarily add up to corresponding totals, because of rounding.

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Review

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The State and changing production patterns with social equity

*Eugenio Lahera**

This article analyzes the importance of the public sector in Latin America and the Caribbean for the development of the region, although, due to its preliminary nature, it does not explore the differences to be observed between the various national economies.

In the first section, considerations relating to the role of economic agents in the development process are formulated. It is argued that the focus which results from examining the economic participation of the public sector in purely "quantitative" terms should be changed for one which would take into account the characteristics of the economic system as a whole.

The analysis and description of the Latin American and Caribbean public sector that is presented in the second section highlight important differences with respect to the industrialized nations and some developing countries of East Asia, as well as the existence of a considerable degree of heterogeneity within the region. In the same section, it is concluded that there are different patterns of relationship between the public and private sectors, varying according to periods and countries. It is demonstrated that the principal public sector characteristic that is common to the countries of the region is the depth of the fiscal-budget crisis, with its sequel of macroeconomic effects; on the other hand, it becomes apparent that the type of adjustment used tends to weaken the recovery capacity of this sector.

The third section deals with the subject of the State and development in the 1990s. After a description of the present logic of public intervention, there is an analysis of the macroeconomy of changing production patterns, the redefinition of the direct and regulated participation of the State in the economy, social and egalitarian policies, special measures favouring structural change, and public institutions and their performance.

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Introduction

Latin America is submerged in a crisis the gravity of which is comparable only to that unleashed by the Great Depression. Just as occurred then, the internal order of the countries, as well as their insertion in the international economy have been questioned. Perhaps the principal difference lies in the fact that there has been a reversal of the changes considered to be indispensable: whereas in the 1930s and 1940s greater public intervention in the economy became necessary and participation in the world economy underwent an abrupt decline, at present the alternative sought is characterized by amplification of the scope of private activities and a deepening of the financial, commercial and productive insertion of the region in the world economy.

The transition under way shows both creative and destructive components, which can ensure that the resultant institutional structure will be shaped by contradictory forces and tendencies, making it difficult to forecast its design. The State will be, at once, the object and the subject of the economic and social reorganization, given its indisputable importance in both respects. The State must preside over its own reorientation, in spite of the difficulties it faces and in the absence of a consensus and of criteria that are sufficiently well-defined for such a process. The public sector forms part of the problem and, likewise, of the solution: hence the inconsistency of the policies that are frequently proposed. We are witnessing a crisis of the State, which is passing through various dimensions of reality and which manifests itself in social, economic, political and ideological spheres.

From the viewpoint of positive economy, the State is of great significance, both direct and indirect. In fact, some present problems derive from this condition or from some of its properties. From the viewpoint of a regulated economy, the application of a strategy for changing production patterns with social equity involves a vast agenda for the State. If the matter were not so evident for the region, it would be even paradoxical: the State is an essential actor even if there is an effort to diminish the productive participation of the public sector or to alter the level of economic regulation. A public sector role is necessary, not only for the determination, in each

country, of the specific objectives of changing production patterns with social equity, but likewise for the specification, application and evaluation of functional policies. From a different standpoint, it is in the State where the political options required for such a strategy can crystallize and where the

macroeconomic objectives of the foreign debt conditionality are negotiated.

It is probable that the State constitutes the most relevant theme in the Latin American economy. For this reason, it is essential to approach the subject with a pragmatic attitude, that is to say, without ideologies.

I

A general view

1. *The public sector and the private sector in regional development*

Unlike what occurred in other situations considered to be typical, in which a relatively strong and homogeneous civil society organized itself into a national State, in various countries of the region the State has played or is playing the role of keeping the civil society together. The relatively precarious social and political structure of various Latin American countries required the support of the State, which thus became the arbitre and participant in a vast range of economic, political and social transactions, as well as the touchstone of ideologies, political positions and development strategies. The same reasons which led it to assume such important roles eroded, however, its strength: a technocratic vision of the common good had to coexist with strong tensions and sectoral clashes initiated by groups that were fighting to receive privileged attention for their individual problems. This aggregate of relations, in turn, was strongly influenced by ideological views, frequently originating in attitudes that had little to do with local needs.

The discussion of the role of the public sector in Latin American and Caribbean development is an old one; however its elements have been changing and, in recent years, have undergone substantial modification.

The controversy over the virtues and defects of the economic performance of the public and private sectors has traditionally been carried on in ideological and exclusive terms, frequently removed from regional realities. Whereas the public sector appeals to the general interest, the private sector seeks greater efficiency, feeling suffocated by excessive extension of the public sector. Both extremes have ingredients

of objective validity, as well as elements of representation. They share a standard appraisal of the agent for which they plead, while their policy prescriptions are essentially quantitative: more private sector or more public sector.

In practice, however, it has been proved that the public sector does not always serve the general interest most efficiently and that often the private sector does not operate under conditions of perfect competition. It is not customary, in the region, to encounter price wars, the seizure of technological income and firms with high rates of capitalization. Many subsidies lack technical justification; certain incentives originally established as temporary often turn out to be permanent, and internal and external protection goes beyond what is advisable, lasting for excessively long periods; capital markets are small and not very transparent; credit is severely rationed, which, moreover, discriminates against risk or long-term operations; and in several countries capital flight is of considerable magnitude.

The relation between the public and private sectors in Latin America and the Caribbean is far from being unanimous and constant. In some cases and periods it has been one of complementarity and co-determination; in others, of distance and confrontation. Frequently, the public sector has opened up paths for the development of the private sector, through large-scale investments in infrastructure; the granting of subsidies for various cost components, such as financing and labour; or regulations for the protection or encouragement of national industry. Disagreements have been numerous but there has frequently been a mutually-advantageous symbiosis. Thus there has been experience with utilization of the public sector for the benefit of exclusively private interests, as well as

examples of suffocation of private activity by the State; likewise, nationalization of the economy and privatization of the State have often occurred as part of a single process.

The development of the public sector in the region has been, moreover, heterogeneous. In some countries it has promoted the development of private activities; in others it has favoured its own socio-political role. In some countries the State is strong and technocratized; in others, weak, seeing itself periodically flooded by new political waves.

In general, public intervention in the economy has had a favourable effect on several aspects of the region's development, thanks particularly to large investments in areas crucial to growth, in which the private sector did not enter, owing to weakness or aversion to risk, or for both reasons. The broadening and improvement of the physical infrastructure and communications, energy, education, and the solution of various industrial bottlenecks are among the achievements of the public sector. This likewise had a positive, although quite heterogeneous, effect on social welfare (Mesa-Lago, 1985).

Public intervention had, however, a number of shortcomings. In the area of goods and services, projects were often poorly evaluated, had low investment returns, and were subject to non-economic goals, without subsequent evaluation. With respect to incentives and regulations, excessive protection frequently generated revenue problems. Actions oriented towards social development favoured, in a preferential way, sectors with some degree of economic insertion, reaching the poor to a lesser extent. In public administration itself, there was a tendency for inefficiency, bureaucracy and overemployment to prevail. On the other hand, the intervention of the public sector was losing effectiveness as a result of various related processes: while the tax base was eroding, the social and economic functions assigned to the State continued to expand, along with the magnitude of transfers to the different social groups. Although preconditions for transferring State responsibilities to the private sector were reached in an aggregate of areas, the decision to proceed to take such action was lacking. Inadequate regulatory standards restricted the potential contribution of direct foreign investments to regional development, limiting their operations to the respective national markets and granting them an unjustified level of protection.

The private sector, in turn, frequently demonstrated aversion to productive risk and a tendency to transfer capital abroad, to arrange tax havens, and to establish vested-interest relationships with the public sector. On the other hand, it frequently failed to respect its tax obligations, despite the high concentration of income prevailing in the region.

All in all, the public sector and the private sector are, simultaneously, the cause and the effect of the characteristics of the development process in each society, to the extent that in several cases they share virtues and weaknesses. The resultant economic system has, on the whole, been characterized by low levels of productivity, profiteering, price distortions and slow technological progress (Fajnzylber, 1989). The evasion of taxes and of controls, the payment of bribes, and illegal foreign trade activities are illustrative of a strong tendency to seek easy profit.

This summary analysis leads to the conclusion that the cause of the present crisis in the public-private sector relationship is more complex than the mere presence of an inefficient and semi-paralytic State, which has an erosive effect on its surroundings. The public sector is one of the endogenous variables whose interaction make up the pattern of regional development: to isolate it analytically can take us farther away from an understanding of reality instead of bringing us closer to it.

2. The main analytical problem: smaller or better public sector?

The basis for the insertion of the public sector in the economy is the proof that the market reveals several "flaws". Among these are imperfections that make competition difficult, the existence of public goods, the presence of externalities and insufficient information (Stiglitz, 1986). The markets of the countries of the region are characterized by the existence of entry barriers, the lack of apprenticeship opportunities in practice, and the absence of technological income.

Since the beginning of studies on "development economics", there has been agreement that the role of the public sector is naturally greater in the poor countries, given the generalized existence of externalities and distortions, in both financial and

product markets, and the lesser availability, in quantitative and qualitative terms, of information for private economic agents. It is clear that differences between countries of different development levels are related not only to factor endowment but also to basic aspects of economic organization, including the functioning of markets. The aggregate of economic organization is what limits the action possibilities of firms. The "market flaw" is definitely more generalized in developing countries, where imbalances are more extensive and deeper, with frequent cases of high levels of inflation and underutilization of the work force (Stiglitz, 1989).

The above-mentioned deficiencies often correspond to true market flaws, voids, or semi-voids, that the public sector has tried to fill. In the literature, this type of problem is considered to be a "dynamic" flaw (Rees, 1984). By definition, public sector activity in these cases should be purely temporary.

Thus it is apparent that there have been, and are, theoretical bases for "correct" public intervention; consequently, there is no point in seeking the automatic optimum of non-public intervention (Toye, 1987). In some cases, the possibility of making "market" corrections for "market flaws" has been, during long periods, either scarce or non-existent.

There is no doubt that there also exists what could be called "State flaws", since government has various deficiencies, some of which, such as those observed in the matter of information, are shared with the private sector. Occasionally, State intervention can effectively block the development or improvement of various markets. Likewise, it can make important strategic mistakes in the management

of the main macroeconomic variables, as occurred with the management of the foreign debt. It is clear that the public sector can intervene inadequately (Lal, 1985) or for too long, thus impeding or preventing private relief activity. From another standpoint, there is the risk that State regulation may be promoted by private interests, for the purpose of obtaining undue profits (Buchanan and Tullock, 1962; Stigler, 1971; Peltzman, 1976), with the possible result of socially-negative effects (Pera, 1989).

In short, it is a matter of trying to reduce, and at length correct, the adverse effects of market imperfections. For this purpose, we must recognize the potentialities and the limitations of government intervention for correcting market flaws or faults. Since two imperfect entities are involved, each must specialize, although not necessarily exclusively, in those functions which it performs better and for which it is more indispensable. The production function belongs primarily to the market and the private sector; the State should be concerned with promoting macroeconomic equilibria and increasing degrees of equity, as well as with eliminating bottlenecks critically affecting development -availability of foreign exchange and savings and investment processes (Ramos, 1989).

The quality of State intervention is an important subject and therefore the analysis cannot be limited to merely quantitative aspects. Less State, in the abstract, is not always advisable; on the other hand, it is always possible to think in terms of better State intervention.

II

The public sector in Latin America and the Caribbean

1. An overall view

Whether as direct agent or regulatory body, the public sector has influenced, and is influencing, in varying degrees, basic aspects of regional development: financing and investment; income distribution and social development; and foreign trade. In the first of these it has operated through public firms in a variety of sectors, with different agencies serving as financial

intermediaries, through the provision of public services and the transfer of subsidies to the poorer sectors and, occasionally, with domestic and/or international trade institutions. A considerable part of the region's technological research and development efforts has been realized in the public sphere.

On the other hand, the public sector regulates, with different coverage and purpose, various prices that are strategic for the functioning of the economy

and for such micro-economic decisions as those relating to exchange rates, interest rates, tariffs and other foreign trade restrictions, minimum salaries and, at least partially, the readjustability of wages and salaries, among others.

The public sector includes activities of different origin and aim. They correspond *grosso modo* to the State as developer, the welfare State and the State as saviour of private firms with problems: the public sector includes assets transferred, for varying reasons and in different ways, from the national and transnational private sectors.

It is difficult to quantify adequately a role which is so multifaceted and whose characteristics vary significantly between countries and periods. In general the indicator used is the size of public expenditure with respect to the GNP, which fluctuated around 30% between 1982 and 1984 (IMF, 1989). This average disguises an important degree of heterogeneity of the sector in the region, since the range of participation is between 11 and 55% (table 1). While recognizing problems of an accounting and institutional nature, which erode the reliability of statistics, it is unquestionable that the differences between countries are substantial. The heterogeneity of the public sector is a basic datum of the regional situation.

Table 1
EXPENDITURES OF THE GENERAL
GOVERNMENT AS A PERCENTAGE OF GNP

| Country | Percentage | Year |
|--------------------|------------|------|
| Brazil | 54.9 | 1987 |
| Suriname | 52.7 | 1986 |
| Nicaragua | 47.7 | 1988 |
| Barbados | 44.6 | 1987 |
| Panama | 33.7 | 1987 |
| Argentina | 33.4 | 1987 |
| Chile | 30.1 | 1987 |
| Mexico | 26.9 | 1984 |
| Uruguay | 26.0 | 1984 |
| Venezuela | 22.7 | 1979 |
| Costa Rica | 22.5 | 1985 |
| Colombia | 18.2 | 1983 |
| Peru | 17.8 | 1987 |
| Dominican Republic | 14.3 | 1983 |
| Guatemala | 13.8 | 1983 |
| Paraguay | 11.8 | 1984 |
| Bolivia | 11.3 | 1986 |

Source: International Monetary Fund, *Government Finance Statistical Yearbook 1989*, vol. 13, Washington, D.C., 1989, p. 113.

The World Bank has estimated price distortion indices for different countries which may indicate the relative scope of the regulations imposed by the State (World Bank, 1983). However, this approach is debatable, in its methodology as well as in its substance. Even so, it provides evidence of the dispersion prevailing in the degree of incentives and restrictions of the different countries of the region.

In addition, public participation in financial affairs shows considerable heterogeneity. Undoubtedly, the public sector has played a decisive role in capital accumulation, going beyond the problems of financing, destination and the results of such investment.¹ The participation of the public sector in regional investment is 41%, with important fluctuations according to country and period (ECLAC, several numbers).

The public sector's role in foreign trade varies greatly from one country to another. In some cases it is the main exporter while in others it has no direct participation at all in sales abroad. The same dissimilarity prevails for the public sector's role in administering national imports.

A similar situation is found for the participation of the public sector in various economic activities. At the beginning of the decade, the largest public firms were concentrated in the energy sector (38 to 78%), whereas communications represented 3 to 13%; transport, from 1 to 8%, trade, 1 to 7%, mining, 1 to 4%; and manufacturing industries, 1 to 14% (table 2). In the industrial area proper, its presence has, in general, been less, given that the transnational firms predominate here, this being one of the discrepancies between experience in the region and that of the recently industrialized Asian countries (Gereffi, 1989). The share of the public sector in sales of the 50 largest firms of the industrial sector reached an average of 15% in 1983 (ECLAC/UNIDO, 1985).

¹ On the other hand, it has been observed that the classification of government expenditures is frequently debatable or inconsistent. For the case of Colombia, see López, 1989.

Table 2

SIX LATIN AMERICAN COUNTRIES: CLASSIFICATION BY ECONOMIC ACTIVITY OF THE 50 PUBLIC ENTERPRISES WITH THE HIGHEST SALES VOLUME, 1983
(Percentages)

| Branch of economic activity | Argentina ^a | Brazil | Colombia | Chile | Mexico | Venezuela |
|-----------------------------|------------------------|--------------|--------------|--------------|--------------|--------------|
| Agriculture | - | - | - | - | - | - |
| Mining | - | 4.7 | - | 48.8 | 1.6 | 2.3 |
| Manufacturing industries | (13.1) | (14.2) | - | (7.8) | (12.0) | (9.4) |
| Non-durable consumer goods | 4.8 | 2.8 | - | 7.3 | - | - |
| Intermediate goods | 8.3 | 11.3 | - | 6.5 | 4.7 | 9.4 |
| Automotive industry | - | - | - | - | - | - |
| Capital goods | - | - | 1.3 | - | - | - |
| Household appliances | - | - | - | - | - | - |
| Energy | 48.6 | 70.3 | 72.7 | 38.1 | 77.5 | 63.9 |
| Petroleum | 32.7 | 62.6 | 65.7 | 26.5 | 77.5 | 58.9 |
| Electricity | 15.9 | 7.7 | 7.0 | 11.6 | - | 5.0 |
| Coal | - | - | - | - | - | - |
| Other fuels | 9.2 | - | - | - | - | - |
| Construction | - | - | - | - | - | - |
| Trade | - | 2.9 | 6.9 | - | 0.8 | 1.7 |
| Transport | - | - | - | - | - | - |
| Railway (or land) | 3.0 | 2.6 | - | - | 1.8 | - |
| Air | 7.0 | - | - | 2.0 | 1.9 | 1.1 |
| Maritime | 3.7 | - | 7.7 | - | 0.8 | 0.6 |
| Communications | 13.0 | 5.3 | 12.7 | 3.2 | 3.6 | 2.5 |
| Finances | - | - | - | - | - | - |
| Health | - | - | - | - | - | - |
| Education | - | - | - | - | - | - |
| Others | 2.4 | - | - | - | - | 18.4 |
| Total: 50 firms | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 |

Source: Joint ECLAC/UNIDO Industry and Technology Division, "Empresas estatales y privadas, nacionales y extranjeras, en la estructura industrial de América Latina", *Industrialización y desarrollo tecnológico, Informe No. 1*, Santiago, Chile, September 1985, table 6.

^a1982.

As noted elsewhere, in Latin America and the Caribbean the public sector is handicapped by fiscal fragility of a structural nature. The considerable investment activity of the State and the constant expansion of social services, public employment and subsidies have had their counterpart in considerable increases of the tax burden. However, this tended to grow less than the share of public expenditures in the product, owing to the insufficient broadening of the tax bases and, in many cases, to the erosion of tax payments. In some countries and periods, fiscal deficits allowed the State to carry out its development-promotion and redistributive functions without major macroeconomic disturbances, receiving resources from abroad or from the domestic private sector. In most cases, however, it was necessary to have recourse to inflationary financing. The accelerated indebtedness of the 1970s and the

internal financial crisis added an intolerable burden to fiscal expenditures, with the result that in most of the countries the underlying fiscal fragility was converted, at the beginning of the 1980s, into an outright fiscal crisis (Altimir, 1990).

The establishment of public enterprises resulted from different motivations: the provision of certain public goods and services based on a natural monopoly or corresponding to services it was desired to subsidize; the correction or patching up of the market flaw in sectors or activities where the private sector showed no interest or no capacity for investing; the nationalization of firms for strategic reasons or to save them from imminent bankruptcy that would have serious social repercussions.

The heterogeneous universe of these public enterprises shares diverse problems, mainly financial and administrative. The first of these can originate in

price-subsidy policies, the absence of adequate control over operative and investment costs, overlapping economic and social goals of difficult joint evaluation, or in the practice of systematic transfers to the government, including credit resources secured through borrowing abroad. With respect to administrative problems, the executive function is commonly unstable and subject to an aggregate of restrictions that hamper or distort the development of the main activities. In other cases, the enterprises operate with great independence and follow their own bureaucratic goals, showing very little coordination with the rest of the public sector.

Table 3

STATE-OWNED ENTERPRISES: VALUE ADDED AS A PERCENTAGE OF NON-AGRICULTURAL GNP AND FIXED INVESTMENT AS A PERCENTAGE OF GROSS INVESTMENT, 1981-1985

(Current prices)

| Country | 1981 | 1982 | 1983 | 1984 | 1985 |
|---------------------------|------|------|------|------|------|
| Brazil | | | | | |
| Value added | 4.7 | 3.5 | 3.4 | 3.7 | 3.5 |
| Fixed investment | 25.8 | 30.0 | 26.9 | 24.4 | 17.5 |
| Costa Rica | | | | | |
| Value added | -0.1 | 0.2 | 6.5 | 7.9 | 5.3 |
| Fixed investment | 31.3 | 23.2 | 17.9 | 17.1 | 13.2 |
| Chile | | | | | |
| Value added | 10.3 | 13.0 | 16.1 | ... | ... |
| Fixed investment | 13.9 | 17.5 | 22.8 | 29.3 | 27.5 |
| Jamaica | | | | | |
| Value added | ... | ... | ... | 23.3 | ... |
| Fixed investment | ... | ... | ... | 11.0 | ... |
| Mexico | | | | | |
| Value added | 6.9 | 11.6 | 14.8 | 14.4 | 12.7 |
| Fixed investment | 25.3 | 24.3 | 21.8 | 19.1 | ... |
| Dominican Republic | | | | | |
| Value added | 2.1 | 2.7 | 3.0 | 3.3 | 0.6 |
| Fixed investment | 6.1 | 7.4 | 5.3 | 7.0 | ... |
| Venezuela | | | | | |
| Value added | 31.0 | 26.8 | 26.4 | 32.1 | ... |
| Fixed investment | 41.9 | 52.2 | 51.3 | 52.2 | ... |

Source: Govindan Nair and Anastasios Filippides, *How much Do State-Owned Enterprises Contribute to Public Sector Deficits in Developing Countries - and Why?*, Policy, Planning, and Research Working Papers series, No. 45, World Bank, 1988, table 2.1 (background paper for *World Development Report 1988*).

Apart from the recurrence of some of the characteristics already mentioned, until the beginning of the 1980s, the public enterprises of the region made up a very heterogeneous group. Some operate very efficiently in competitive markets, whereas only the massive transfer of public resources allows the survival of others, which are highly inefficient and have little or no ability to capitalize. There are public enterprises with satisfactory standards of technical and financial administration, repressed by restrictive sectoral policies; enterprises that maintain a vested-interest relationship with private suppliers; and enterprises that have been nationalized in order to prevent their bankruptcy, although they are not economically viable. As is apparent, the impact of public enterprises on global efficiency can differ substantially from one case to another.

In some countries State-owned firms have a large share of gross investment and, in general, quite a smaller one in total value added (table 3). In this subsector, as in the public sector as a whole, investment displays special characteristics and there are problems of overinvestment and bad administration.

The incidence of public enterprises in the financial situation of the sector varies from one country to another and, likewise, within each one. In some cases relatively important transfers from the central government to the enterprises may be observed, while in others it is the enterprises that are contributing to the financial balance of the public sector as a whole (table 4). In general, in those countries where there was a deferment of tariff adjustment, public enterprises tended to contribute to raising the public sector's deficit.

In the period prior to the crisis, quite dissimilar policies were suggested for public enterprises: in some cases they were rationalized, bringing their tariffs up to date and improving their administration; in others they were used to obtain foreign loans (Werneck, 1989; Larranaga, 1989).

The public sector is an important employer in most countries of the region; on average one out of each five urban employees is public, a share that fluctuates between 6 and 36% (table 5). From another point of view, public sector personnel are distributed in an unequal way between the central government, the decentralized administrations, the public enterprises, and State and municipal administrations. In most countries the first category is the most significant (Sulbrant, 1989).

Table 4
NET FINANCIAL FLOW FROM THE
GOVERNMENT TO PUBLIC ENTERPRISES
(Percentages of GNP)

| Country | Averages | |
|--------------------|-----------|-----------|
| | 1977-1982 | 1983-1985 |
| Bolivia | -3.9 | -2.3 |
| Brazil | 3.3 | 2.0 |
| Colombia | 1.0 | ... |
| Costa Rica | ... | 0.2 |
| Chile | -6.5 | -5.2 |
| Ecuador | 1.0 | 0.7 |
| El Salvador | 0.5 | -0.2 |
| Guatemala | 2.3 | 0.8 |
| Honduras | 1.9 | 3.3 |
| Jamaica | ... | ... |
| Mexico | 1.5 | 2.1 |
| Peru | 0.5 | 0.3 |
| Dominican Republic | 0.8 | 1.1 |
| Uruguay | -1.7 | -2.1 |
| Venezuela | -0.2 | 0.2 |

Source: Govindan Nair and Anastasios Filippides, *How much Do State-Owned Enterprises Contribute in Developing Countries - and Why?*, Policy, Planning and Research Working Papers series, No. 45, World Bank (background paper for *World Development Report 1988*).

Table 5
IMPORTANCE OF PUBLIC EMPLOYMENT
TOWARD THE END OF THE 1980s
(Percentages)

| Country | Total population PSP | PSP Total population | PSP | |
|------------|----------------------|----------------------|------|---------------|
| | | | EAP | PSB EAP Urban |
| Venezuela | 16.8 | 6.0 | 17.0 | 21.0 |
| Argentina | 16.0 | 6.3 | 17.7 | 20.3 |
| Mexico | 21.6 | 4.6 | 14.7 | 20.7 |
| Uruguay | 10.8 | 9.2 | 21.7 | 24.7 |
| Costa Rica | 16.2 | 6.1 | 16.4 | 36.1 |
| Chile | 58.9 | 1.7 | 5.0 | 5.9 |
| Panama | 14.2 | 7.0 | 20.4 | 34.7 |
| Peru | 24.0 | 4.1 | 12.3 | 17.8 |
| Guatemala | 47.8 | 2.1 | 6.8 | 15.9 |
| Honduras | 60.4 | 1.7 | 5.0 | 11.7 |
| Bolivia | 31.7 | 3.2 | 10.0 | 20.2 |

Source: José Sulbrant, "El tamaño del sector público en América Latina. Un estudio de once países", *Draft Report*, Caracas, Latin American Centre for Development Administration (CLAD), November 1989.

PSP: Public sector personnel.

EAP: Economically active population.

From still another angle, there are in Latin America about 12 650 local governments, whose joint share in the public expenditures of their respective countries is less than 10%, except in the case of Ecuador. The shares of other levels of public administration in such expenditures shows enormous dispersion, fluctuating between 2.4 and 73.3% of the total (IMF, 1987).

2. Some international comparisons

The role of the public sector in Latin America differs quantitatively and qualitatively from that observed in the industrialized economies. In the region, the State intervenes more directly in the production of goods and services and is an investor or great importance; it serves as a balance between a multiplicity of global and sectoral policies and fulfills the important role of political and social structuring.

The share of the public sector in the region's GNP is much lower than the corresponding figure for the main industrialized countries, where the average was close to 45% between 1982 and 1985. On the other hand, it is higher than that of the Asian developing countries. As will be seen later, these differences are explained in part by the different breakdown of public expenditures by region.

In general terms, the region's public sector places greater emphasis on development through public social expenditure than do some of the Asian countries, and it pays less attention to defence. Its regulation is more generalized, frequently not very selective and incoherent; but its presence in the technology-led industrial sectors (In-Joung, 1987) and in investment is less than that observed in Asia (Kagami, 1989).

On the other hand, in 1986 and 1987 the public sector of the majority of the region's countries allocated for interest payments a percentage much higher than that of the industrialized countries (table 6), in circumstances where, at the beginning of the 1980s, the difference was insignificant. The allocations likewise increased in the Asian developing countries over the same period, but with less intensity.

Table 6

COMPARISON OF SOME ITEMS OF CENTRAL GOVERNMENT EXPENDITURE IN LATIN AMERICA AND THE CARIBBEAN AND ASIA WITH THOSE OF DEVELOPED COUNTRIES

(Percentages in relation to total expenditures)

| Type of expenditure | Subsidies and other current transfers | Interest payments | Capital expenditures | Wages and salaries |
|---------------------------------|---------------------------------------|-------------------|----------------------|--------------------|
| 1982 | | | | |
| Latin America and the Caribbean | 35.4 | 12.8 | 15.4 | 16.6 |
| Developed countries | 49.0 | 9.7 | 5.6 | 13.5 |
| Asia ^a | 23.6 | 8.5 | 19.6 | 14.2 |
| 1983 | | | | |
| Latin America and the Caribbean | 32.5 | 17.0 | 12.2 | 16.3 |
| Developed countries | 49.0 | 10.2 | 5.0 | 13.3 |
| Asia ^a | 23.2 | 10.0 | 18.8 | 14.9 |
| 1984 | | | | |
| Latin America and the Caribbean | 32.9 | 20.5 | 11.0 | 16.0 |
| Developed countries | 48.5 | 11.2 | 4.7 | 12.9 |
| Asia ^a | 23.9 | 11.3 | 17.7 | 15.1 |
| 1985 | | | | |
| Latin America and the Caribbean | 28.9 | 23.6 | 10.7 | 15.8 |
| Developed countries | 47.1 | 12.4 | 5.0 | 12.6 |
| Asia ^a | 24.3 | 11.3 | 17.6 | 14.6 |
| 1986 | | | | |
| Latin America and the Caribbean | 29.5 | 28.0 | 11.0 | 14.7 |
| Developed countries | 47.8 | 12.4 | 5.2 | 12.7 |
| Asia ^a | 23.1 | 12.1 | 18.3 | 14.8 |
| 1987 | | | | |
| Latin America and the Caribbean | 24.3 | 25.3 | 9.6 | 12.5 |
| Developed countries | 48.0 | 12.2 | 4.3 | 13.2 |
| Asia ^a | 25.9 | 14.5 | 16.6 | 15.5 |

Source: International Monetary Fund, *Government Finance Statistics Yearbook 1989*, vol. 13, Washington, D.C., 1989, pp. 70-77.

^a Includes Bangladesh, Burma, India, Indonesia, South Korea, Malaysia, Pakistan, Singapore, Sri Lanka and Thailand.

Public sector capital expenditures in both Latin America and Asia had a higher incidence than those of the industrialized countries, despite their decline since the beginning of the crisis. The sharpest decline, however, occurred in Latin America and the Caribbean, owing to the type of adjustment applied.

The share of wages and salaries in the region's public expenditures declined steadily, so that the area dropped from being the highest to the lowest of the three groups of countries considered in 1987. Subsidies and other current transfers have less incidence than in the industrialized countries and in 1987 fell below that corresponding to Asia. Behind these averages, of course, are hidden significant national differences.

The breakdown of public income in the three groups of countries also reveals marked

discrepancies. The share of taxes on capital is lower in Latin America and the Caribbean, but in this region social security is much more important than in Asia, while at the same time being low in comparison with the industrialized countries. (Moreover, some Asian countries do not include the social security account in the central government.) The share of taxes on foreign trade transactions is substantially less in the region than in Asia, but much higher than in the industrialized countries (table 7).

For Latin America and the Caribbean the ratio of tax revenue to GNP is significantly lower than that prevailing for the industrialized countries, although it is higher than that for the Asian countries. The burden of taxes on profits and capital is noticeably lower in the region, which means that the weight of public expenditure there is distributed less fairly.

Table 7
**BREAKDOWN OF CENTRAL GOVERNMENT INCOME IN LATIN AMERICA AND THE CARIBBEAN, ASIA
 AND THE DEVELOPED COUNTRIES, 1982-1987**
(Percentages with respect to total income)

| | 1982 | 1983 | 1984 | 1985 | 1986 | 1987 |
|---|------|------|------|------|------|------|
| Income and profits | | | | | | |
| Latin America and the Caribbean | 22.0 | 19.3 | 21.0 | 21.5 | 21.9 | 18.3 |
| Developed countries | 41.2 | 39.7 | 39.6 | 40.0 | 40.2 | ... |
| Asia ^a | 28.6 | 27.4 | 25.9 | 26.2 | 22.2 | 22.9 |
| Social security | | | | | | |
| Latin America and the Caribbean | 18.2 | 16.3 | 17.0 | 16.4 | 18.9 | 13.5 |
| Developed countries | 31.4 | 32.3 | 32.8 | 32.7 | 33.6 | ... |
| Asia ^a | 0.2 | 0.2 | 0.3 | 0.3 | 0.3 | 0.3 |
| National goods and services | | | | | | |
| Latin America and the Caribbean | 27.6 | 35.3 | 35.3 | 34.0 | 33.6 | 31.6 |
| Developed countries | 15.1 | 15.1 | 15.3 | 14.8 | 14.6 | ... |
| Asia ^a | 33.1 | 34.9 | 33.4 | 33.3 | 34.2 | 32.7 |
| Trade and international transactions | | | | | | |
| Latin America and the Caribbean | 14.0 | 9.8 | 8.5 | 8.2 | 9.4 | 9.1 |
| Developed countries | 1.4 | 1.3 | 1.5 | 1.4 | 1.4 | ... |
| Asia ^a | 19.1 | 19.3 | 19.8 | 20.1 | 20.1 | 21.0 |
| Non-tax income | | | | | | |
| Latin America and the Caribbean | 17.8 | 18.6 | 19.5 | 20.9 | 16.6 | 28.2 |
| Developed countries | 9.2 | 10.0 | 9.5 | 9.7 | 9.1 | 8.3 |
| Asia ^a | 16.1 | 15.1 | 17.8 | 16.6 | 19.9 | 19.3 |

Source: International Monetary Fund, *Government Finance Statistics Yearbook 1988*, vol. 13, Washington, D.C., pp. 52-57.

^a Includes Bangladesh, Burma, India, Indonesia, South Korea, Malaysia, Pakistan, Singapore, Sri Lanka and Thailand.

The magnitude of the public deficit had been more or less similar in the three regions until the recent crisis; from then on, that of the region increased more rapidly (IMF, 1989).

3. The crisis of the economy and the crisis of the public sector

The immediate origin of the fiscal crisis is to be found in the collapse of the financial pattern of the regional economy which had prevailed during the second half of the 1970s and until 1981. The phenomenon affected the public sector disproportionately, since, in degrees varying from one country to another, it had to take over responsibility for a fraction of the private debt. Two thirds of the swing in the transfer of resources abroad, equivalent to about 4% of GNP, correspond to the public sector.

Both exogenous and endogenous factors were involved in the external financing crisis. Among the first, those that stand out are the change in the sign of interest rates from negative to positive; the deterioration of the terms of trade; and the excessive amount of risk loans (overlending) granted by

international banks (Mortimore, 1989). Among the endogenous factors, the most important are inadequate project evaluation and indebtedness in excess of the capacity to repay generated by external savings.

The public sector assumes a role of protagonist in adjustment efforts, given its diversified economic and social participation and its natural condition as regulator of the national economy. Almost all the components of the adjustment programmes, especially exchange and foreign trade policies, as well as financial and price liberalization, have repercussions in the fiscal sphere. The management of public sector adjustment efforts is a subject of the utmost importance. Often the role assigned to this sector in the adjustment has consisted, exclusively, in its own reduction (IDB, 1984, Marshall and Schmidt-Hebbel, 1989).

The crisis had a generally adverse effect on the public budget, but the intensity varied from one country to another. The interruption of capital flow limited the public sector's capacity to borrow abroad, while the rise in international interest rates increased the burden of foreign public debt service. In many

Table 8
**LATIN AMERICA AND THE CARIBBEAN: EXPENDITURES FOR CENTRAL GOVERNMENT
 FUNCTIONS, 1982-1987**
(Percentages of total expenditures)

| | 1982 | 1983 | 1984 | 1985 | 1986 | 1987 |
|---|------|------|------|------|------|------|
| Defence | 5.6 | 5.5 | 5.5 | 4.5 | 4.6 | 5.0 |
| Social security and welfare | 23.4 | 23.5 | 22.7 | 19.0 | 18.5 | 18.2 |
| Education | 9.9 | 9.4 | 9.8 | 9.2 | 8.8 | 9.3 |
| Health | 4.9 | 5.0 | 5.2 | 4.8 | 4.8 | 6.7 |
| Housing | 1.2 | 2.2 | 1.7 | 1.4 | 1.5 | 1.7 |
| Economic affairs and services | 20.8 | 22.1 | 18.9 | 17.3 | 15.7 | 13.1 |
| Mining, manufacturing and construction | 3.7 | 3.9 | 2.4 | 2.3 | 1.7 | 1.0 |
| Agriculture and others | 5.0 | 6.0 | 4.0 | 3.6 | 3.9 | 2.9 |
| Fuel and energy | 2.1 | 3.1 | 2.5 | 2.5 | 2.6 | 2.0 |
| Roads | 2.2 | 2.7 | 2.4 | 2.3 | 2.2 | 2.8 |
| Other transport and communications | 2.6 | 3.1 | 3.1 | 2.8 | 2.2 | 2.4 |
| Others | 5.1 | 3.6 | 4.7 | 3.8 | 3.3 | 2.5 |
| Other functions | 32.7 | 30.7 | 32.7 | 42.7 | 46.1 | 46.0 |

Source: International Monetary Fund, *Government Finance Statistics Yearbook 1989*, vol. 13, Washington, D.C., pp. 56-69.

countries of the region the Governments guaranteed a fraction of the commitments undertaken abroad by individuals, thus reaching high levels of public-debt responsibility. Frequently the cost of the difference between the interest rate paid and the rate of return received (especially in foreign exchange) was covered in the end by the public sector, even though it had not generated it. On some occasions the corresponding internal debt of the private sector with the public sector was watered down, on others, and with consequent pressure on public finances, the State subsidized private debtors and the domestic financial system, in order to avoid breakdown of the latter (Bresser, 1988; Eyzaguirre, 1989; Lerda, 1989).

Following the interruption of net external financing, countries had to use domestic capital, which led, among other measures, to the creation of money in circulation; the introduction of changes in reserve requirements; the requirement for banks to maintain public bonds at controlled rates; the imposition of government controls over interest rates, accompanied by credit rationing; the concession of bank loans at market rates, and the direct sale of public bonds to the non-financial public sector, at market rates (Chhiber and Khalilzadeh-Shirazi, 1988; Easterly, 1989).

Definitely, the fiscal crisis of the public sector is not the result of an increase in economic development expenditures; rather, the severe cutback of public investment has provided an easy expedient for

contracting the absorption.² Attention to traditional functions of the public sector has been altered by the increase in interest payments charged to the State. This effect is particularly disquieting with respect to social expenditure (table 8).

In different countries and through different mechanisms (including privatization and reprivatization, partial sale, the closing down and the merger of firms) efforts have been made to modify the asset endowment under State control.

From another viewpoint, in recent years there have been profound changes in the region's incentive regime. Outstanding among these are changes in foreign exchange and trade policies, which have been aimed at the generation of trade surpluses, and in fiscal policy. Likewise, there have been important variations in price, credit, and financial policies. Similar developments occurred at the sectoral level with agricultural and industrial policies. The debate over subsidies and transfers has become heated, although frequently there is a lack of adequate information for delving more deeply into the subject. The incentives regime of the public sector has undergone several changes in different countries; in some it has substantially improved the ability of the sector to evaluate projects. Deregulation and the granting of concessions have been infrequent and

² In the opinion of Easterly, an investment-led contraction of absorption was attempted (Easterly, 1989).

their results negligible. On the other hand, some unsuccessful liberalizations, especially in the financial sphere, have provided useful lessons (Dornbusch and Reynoso, 1989).

In short, the diversity of initial situations has been followed by the diversity of the adjustment schemes which have been utilized. The results have also been different, as proved by the trends in interest rates and inflation, in the primary and fiscal deficit, in the balance on current account, as well as in the levels of the product, exports and imports.

4. *A provisional evaluation: subadjustment and recessive adjustment*

Conventional wisdom has insisted on a difficult agenda for achieving the region's recovery from the crisis: recessive adjustment with changing production patterns and simultaneous and high transfers abroad.

The public sector appears as the "financier of last resort" for all accounts, which, in the light of the characteristics it was displaying even before the crisis, is not realistic. The aggregate of tasks that have been imposed on it in most of the countries is very much in excess of its financial, productive, regulatory

and economic-administrative capacity. The public sector now has fewer resources and its capacity to handle them properly has deteriorated, while at the same time its responsibilities and the problems it must deal with are increasing. It is requested, simultaneously, to service the debt, reduce expenditures, invest less, pay lower wages and be more efficient, all this in the context of reduction of its aggregate participation in the economy and of a greater contribution to regional changes in productive patterns. It is clear that the "quantitative" and short-term approach entails destructive components. The private sector, for its part, has had to take refuge in the public sector, diminish its investment and hold large amounts of capital outside the national economy.

The pursuance of these contradictory, and sometimes incompatible, goals has resulted in the deterioration of public sector performance. In practice, the public type of adjustment has become perverse; in some cases through partial and limited measures, comparable to an underadjustment; in others, through policies that have exceeded the needs of a positive adjustment. The results tend to resemble each other but the causes differ in each case.

III

The State and development in the 1990s

1. *Present logic of public intervention*

Conditions favouring private development already exist in various countries of the region and consequently the degree of public intervention that was customary in the past is no longer required. There are instances where it is feasible to increase the relative importance of the private sector in the provision of public goods and services, whether through the deregulation of activities, the granting of concessions or the privatization of firms.

On the other hand, although in the present regional dilemma the public sector forms part of the problem, it should likewise form part of the solution. It cannot be expected that market signals alone will solve the crisis. The public sector is the negotiator of first instance with the multilateral financial organizations and the lending banks. The relevant negotiations will have strong repercussions on external financing and global domestic policies.

Going beyond the debate over the role of the State, it seems evident that in coming years the degree of public intervention in the regional economy will continue to be important, although it will undergo qualitative and quantitative changes. The five main aspects of such intervention may be grouped, for analytical purposes, as follows: i) the achievement of an agreement on the governability of the society; ii) the maintenance of a macroeconomic framework that is relatively stable and has fiscal equilibrium and transparency; iii) the redefinition of direct participation and the regulatory role of the public sector in the economy; iv) the execution of sectoral development policies aimed at creating or developing dynamic comparative advantages.

The dual concurrence of the public sector—in the problem and, at the same time, in the solution—complicates the debate on its future role and the adaptations that this will require. The answers have been diverse and are still in the process of

preparation, which leads to the assumption that the debate will still be open in the medium term. The main options for changes proposed until now are privatization, deregulation, bids for concessions and the closing down of firms.

Less progress has been realized in proposals for new roles for the State, or for "expansive" modifications of existing ones. With respect to the possibility of achieving a *positive adjustment* of the State's role, i.e., contracting some functions and expanding others, this has been until now a carefully-kept secret. However, it is an unavoidable task, to the extent that the dual concurrence of the public sector is a reality. A sequential movement—first shrinking and later expanding the public sector selectively—entails various dangers. The public sector requires reform and reconversion simultaneously.

To sum up, it seems necessary to substitute a purely quantitative approach to the public sector's participation in the economy for another which analyses the public sector in the light of the characteristics of the economic system as a whole. In this way, the debate is transferred from the ideological or philosophical plane to a more practical one, which takes into account such aspects as organization, human resources, political interaction, public administration, etc. In the final analysis, decisions relating to public/private delimitation belong, by their nature, to the political sphere.

2. Governability and coordination

The State is the area where diverse national programmes and options crystallize. It is likewise the entity that is able initially to foster the social coordination required for political stability (Cortázar, 1990). The coordination itself can be based on long-term objectives referring to changing production patterns.

State reform assumes the existence of the social will to achieve it, which must be expressed in the political system. The diverse aspects of the reform can meet with varying degrees of political support, but it is also probable that certain groups will be in favour of some changes and opposed to others. The engineering capacity required for achieving a successful reformist coalition is to be found not in the technical area but inevitably in the political area.

Governability, which is a result and not an independent variable whose evolution can be controlled directly, has both economic and political

antecedents. Among the first is the necessary coincidence between the type and the level of activities that are entrusted to the State and the adequate financing of such activities by society. Among the second is the need to achieve agreement among the different political and social groups, at least in matters concerning the rules for the political functioning of society, including alternation in power and respect for both majorities and minorities.

These antecedents, in turn, involve assumptions which are not realistic or, at best, are difficult to apply. In some cases, the high income strata have achieved a privileged position in the international economy, which isolates them from the rest of the country; these groups are concerned with exports, legal or illegal, whose financial flows circulate through the national economy only as speculative capital and whose consumption patterns differ radically from those of the average sectors of society. In other cases, an oligarchical political system or very traditional systems of land-holding generate conditions of endemic violence that assume their own logic of division and extermination. Moreover, it is probable that there are no politicians capable of achieving agreement on a pact of governability that would overcome traditional rivalries or atavistic prejudices.

The degree of governability constitutes an essential characteristic of any political system. It can be defined as the changing relationship between political and institutional control and the evolution of the principal political, economic and social variables (Tula, 1990). A State that is impotent, overwhelmed by internal conflicts, is typical of a society with problems of governability. On the contrary, a well-run State, which concentrates on the administration of a discreet aggregate of strategic variables, is a precondition of governability.

3. The macroeconomics of changing production patterns

Macroeconomic management must be clear and stable and seek the preservation of the economy's basic equilibria.

Changing production patterns requires that the deterioration of regional investment be reversed and that financial resources be concentrated in the tradeable goods sector. Both processes cover numerous requisites and suppositions, many of which involve the public sector.

It is indispensable that the fiscal deficit be reduced drastically, since it increases inflationary pressures and erodes investment potential. To this end, the net transfer of resources abroad to service the foreign debt must be halted, current public expenditures must be reduced, and fiscal revenue increased. The latter, in turn, requires tax reform that would broaden the tax base, simplify the system and improve the collection process.

In spite of the fact that regional defence expenditures are lower than those of other developing regions, there is room for some compression, since they are already equivalent to 54% of the amount spent on education (table 8). With some exceptions, Latin America's expenditures on military equipment have a smaller multiplier effect, which makes the region suitable as a recipient of the "dividends of peace".

An improvement of fiscal sincerity is likewise required. Society must assume the integral financing of the initiatives it is prepared to approve; otherwise accounts will not balance (Schumpeter, 1954). The "Tax State" implies a contractuality in which means and ends are democratically clarified and decided. Under present conditions, an improvement in the tax yield is indispensable, since, as a general rule, this is low. Tax reform should contemplate the abolition of low-yield taxes, the unification of charges on identical taxable materials, the rationalization of exemptions and, in particular, the modernization of the collection system (LMF, 1989).

Public and private investment must be increased and its yield should be improved. Several roads are open for achieving this result, including concentration of effort and control, and evaluation of the different programmes. Public investment will have to be diversified and recognition given to the decisive role of various intangible assets. It is absolutely essential, likewise, to maintain and improve capital flow, avoiding exclusive concentration in new investments.

A determining factor of present disequilibrium is the foreign debt service; this requires a concerted and adequately-financed solution. However, in all cases there will be an imperative need to carry out internal economic reforms simultaneously with efforts to improve the external financing structure (Selowsky, 1989). Where private foreign exchange income is concerned, it is particularly urgent that the subject of internal transfers receive adequate attention.

Regarding private investment, it is of fundamental importance that economic uncertainty be

reduced and that assurance be given that the policies instituted will be maintained, thus avoiding the capital flight that would severely restrict the financing of economic reform programmes.³ The repatriation of this capital, which is an important objective, is sometimes impeded by legal rather than economic considerations. It has to be encouraged wherever its net result will be positive: if a real devaluation is insufficient, the resultant income transfers can increase the flight that it is sought to reverse (Dornbusch, 1989). Several alternatives may be suggested: exchange amnesty, tax advantages, investment in stocks or bonds without justification of origin, and non-reimbursable import licenses for capital goods, among others.

The orientation of investment toward the production of tradeable goods will be conditioned by exchange and foreign trade policies, which must be realistic and stable.

4. *Direct participation and State regulation of the economy*

a) *Public firms*

The excessive emphasis placed lately on the reduction of the size of the State sector has made people forget that public enterprises will continue, in general, to play an important role, since privatization will not be able to reach the aggregate of the public sector. To concentrate on changing the ownership of assets without modifying the operating conditions of State enterprises would mean leaving them at a dead end. The most serious cases involve enterprises that cannot be privatized; on the other hand, many of the reprivatized firms do not form an important part of the problem or do not alleviate it to any great extent. Obviously, in the case of enterprises for which privatization is not practicable another type of solution is required.

The restoration to good health of the nucleus of enterprises with problems—a few tend to be responsible for the major part of the fiscal deficit—requires the adoption of approaches and specific solutions which include their reorganization, the underwriting of agreements with national and foreign investors and the subcontracting of operations.

³ At the end of 1988 the stock of such capital was 166% of Venezuela's foreign debt; almost 90% of Uruguay's; close to 80% of Mexico's and Argentina's; 64% of Ecuador's; 41% of Colombia's; 35% of Bolivia's and 26% of Brazil's. (*The Journal of Commerce*, 1989.) It is probable that the value of this capital exceeds the value of the region's debt in the secondary market.

The large productive public enterprises of the region constitute an asset of the greatest importance in cases where their economic base is solid and their administration efficient. There are cases where the resource endowment exceeds the requirements of immediate objectives and generates over-capitalization or excessive employment or engineering capacity or even underutilization of installations and equipment. In such circumstances, changes must be made either in goals or resource endowment, or both at the same time.

It is desirable to put greater emphasis on transforming the large governmental enterprises into pivots of technological change, applied research and the development of activities which would integrate the interindustrial chain and pave the way for regional complementarity agreements.

Regarding the fixing of tariffs, it is necessary to satisfy the economic efficiency principle, according to which the price of the additional physical unit must equal the cost of resources to provide it. On the other hand, the tariffs charged must generate sufficient income to cover at least the operating and maintenance costs. In order to favour the added efficiency of the economic system, the tariff structures must be intelligible, so that they provide unequivocal signs for the adoption of investment decisions. In order to apply the criteria of economic efficiency to the case of public resources in natural monopolies, it must be established whether the relevant marginal cost is a short or a long-term one, in order to optimize efficiency and, simultaneously, consider an adequate level of financing for the respective enterprise. As already mentioned, it definitely will be necessary to set the rates at marginal cost, introducing the necessary adjustments to allow the self-financing of an efficient enterprise, as a way of simulating its operation in a competitive market (Alé, 1990).

The distortions in the costs for labour, materials and financing should be eliminated, as well as the price subsidies for various categories of final consumers. Where social goals proper are concerned, it will be necessary to specify and explain them, quantifying their magnitude and evaluating efficiency in achieving the aggregate of the enterprise's objectives. Various criteria may be employed for this purpose, apart from profitability. In addition, it is recommended that the transparency of the various flows between the enterprises and the public sector be increased, which could lead to substantial changes in

salary and working conditions in the public sector. Where economies of scale are not a determining condition of their size, it probably will be found desirable to divide public enterprises into smaller units.

To the extent that it is viable, public enterprises should compete not only among themselves but also with the private sector. Greater financial autonomy and transparency should be promoted; advances should be made in the elimination of subsidies; or, when they are necessary, quantitative deadlines and ceilings should be applied. The accounts of public administrations should be audited externally and the results published promptly.

Personnel policies of public enterprises must correspond to their importance: a reasonable degree of stability and autonomy, as well as a competitive level of remuneration, would seem to be indispensable requisites.

Transparency in the relations of public enterprises with their suppliers, whatever their origin, will contribute to the promotion of healthy competition among the latter, thus avoiding the consolidation of vested interests.

The practice of "saviour nationalizations" should be restricted to truly exceptional situations. For public enterprises in this situation, various alternatives should be analysed: rationalization and sale, final closure or transfer.

The situation of public enterprises conceived in order to overcome a market flaw or void has to be evaluated in a realistic way. In those cases where preconditions for market development exist, the activity can be transferred to the private sector; in cases where these preconditions have not been achieved probably the effort will lead either to the reorganization or elimination of the enterprises.

To sum up, the reconversion of the sector is absolutely essential, if public enterprises are to optimize their contribution to the achievement of development with changing production patterns and social equity. This requires applying policies that grant greater financial capacity and autonomy in a context of gradual elimination of subsidies and specific treatment, according to the individual situation of each enterprise.

b) Privatization

There are various situations where the alternative of privatization appears to be advisable. This may actually form part of an aggregate of measures taken

with respect to public enterprises affected by chronic deficits; or it could be suggested for those that operate in markets where it is possible to replace them with private firms; or privatization could be the logical solution for firms that were originally private and the rationalization of which has made them viable (Lahera, 1989; Vernon, 1989).

Privatization, understood as the mere transfer of public assets to the private sector, appears to be a solution which is simplistic in conception and difficult to carry out. This is because it is based on an approach which emphasizes unilaterally the view of the agents concerned, without giving adequate consideration to the incentives and regulations regime, or to the structure of the respective market.

In some approaches it is assumed, openly or implicitly, that the mere change of ownership of the assets will automatically bring with it a change in the mode of operation and the results of the privatized enterprise. However, privatization in itself does not modify the economic incentives and regulations regime. If this action, when advisable, is to be successful, it is first essential to correct various imbalances; this will likewise permit more accurate judgement concerning the advisability of privatizing. The debate concerning the differential effects of asset ownership by various types of agents becomes more specific and relevant in a context in which other operating conditions have already been discerned. The confusion in these matters favours the introduction of a strong ideological component in the discussions.

Privatization and increasing competitiveness are not necessarily synonymous. The impact of the former on efficiency of resource assignment will depend, in part at least, on the structure of the market, more than on the type of ownership. If, originally, competition did not exist in the sector in question, privatization will have a positive impact on efficiency only if it is accompanied by liberalizing policies which remove market restrictions and intensify external competition. In a context of competition or of correction of the incentives regime, privatization can effectively promote greater competition and productive and economic efficiency. On the other hand, the extreme case of conversion of a public monopoly to a private one, with the same lack of regulation, proves that the transfer to the private sector does not offer, in itself alone, any guarantees in this respect. Thus it is evident that privatization is not an end in itself, but rather an instrument of public

sector reconversion in accordance with the new needs of each country.

The way in which privatization is carried out will be a determinant of its results. In fact, the diversity of situations that can arise from its initiation and even after its conclusion—with respect to regulation, for example—makes very different formulas foreseeable. It is of special importance that, in the sequence of operations, the change of agents should not precede, but rather follow, the deregulation, stabilization and liberalization efforts.

Undoubtedly there are objective limits for the depth and speed of privatization programmes; if the advance is too forced, it can cause excessive pressure on local financing and the interest-rate level. On the other hand, it is indispensable that clear rules of procedure be established; that the relevant assessment be entrusted to an autonomous entity; that some degree of competition be introduced; and that excessive concentration of ownership be avoided. Finally, the transfers resulting from the privatization process must not involve undue privileges or subsidies that could weaken the overall effect or simply alter the cost-benefit ratio. Likewise to be avoided is the constitution or reinforcement of inadequate ties between the financial and industrial sectors. In monopoly situations that are difficult to deregulate, privatization does not constitute the best alternative, and the competitive granting of operational contracts might be explored.

c) Regulation of the economy

A clearer dividing line is required for the activities assigned to the public sector, as well as for progress in dismantling unjustified obstacles to private-sector activity. The regime of incentives and regulations must be as transparent as possible, since this is the starting point from which public and private agents formulate their expectations.

The private sector has the right to demand, as a counterpart of entrepreneurial risk, some stability in the rules of the game relating to ownership and the macroeconomic framework. In turn, the concession of subsidies for private operations, on the part of the State, should be governed by the most rigorously objective criteria and should prevail for clearly-defined periods of time.

Excessive controls, redundancies, and delays in procedures may be the subject of drastic, well-focused reform, the results of which may be

perceptible in the short run. In some cases, the very existence of regulations is a source of income for agents located outside the public sector while in close contact with it, i.e., contractors for the State. The standardization of procedures, publicity given to operations and the competitive nature of acquisitions are steps in the direction of modifying these vested interests.

It has been stressed that it is not enough to have "correct prices" in order to establish firm bases for development. Undoubtedly, this condition is not sufficient but it should not be forgotten that it is absolutely essential that there should be a relation between the different prices of the economy and the marginal costs of the respective production.

Various financial liberalization episodes have ended abruptly, in the face of reversals in international financial and trade circumstances, or because of serious errors in the way the corresponding processes have been carried out. Nevertheless, the aims of ensuring that the market determines the rates of interest and of allowing a sensible balance between savings and investment remain valid. Important lessons must be learned from the errors of the past (Villanueva and Mirakhor, 1990).

The regulation of the labour market should not prejudice the free enterprise of the firm, avoiding excessive rigidity in labour relations. At the same time, it is advisable to promote the establishment of an unemployment insurance system or some similar formula and to strengthen training activities which can permit displaced workers to find other jobs.

Auctioning of concessions and provision of private services is infrequent in the region. However, this represents an important potential for increasing productivity. The fruits of such an increase should also benefit the user of the service auctioned, not only in price but also in quality of the service.

The concession is the act by virtue of which the State grants to a private firm the right to provide a public service, in exchange for the rigorous fulfilment of clear and stable requirements. The concessionary firms are obliged to deliver the service to anyone who solicits it, in accordance with established requisites (Alé, 1990). In the case of non-fulfilment of some of the conditions required, the State can fine the firm and even put an end to the concession.

Incentives must be proportionate and efficient with respect to the specific ends sought, avoiding excesses and remaining in effect for prudent and

precise periods. The implementation requisites should be few and susceptible to objective evaluation.

5. Social equity policies

The State has an irreplaceable role in the satisfaction of the population's basic needs, which is, in turn, a requisite of structural change. The existence of increasing degrees of social equity constitutes likewise a moral imperative and responds to the right of the citizens of a country to participate in the fruits of progress. The viability and the dynamism of a development strategy is founded on full employment of existing resources, especially human resources, on the attainment of basic welfare standards which confer meaning on belonging to a political system, and on growing access to goods the added value of which is steadily increasing.

On the subject of income distribution we must distinguish between aspects which are actually distributive and those which are redistributive. Whereas the former depend mainly on income generation and have important institutional connotations, the latter are related to income already generated. The traditional problems in social relations impede the advance of modernity, often making it spasmodic. From another viewpoint, the extreme inequality of income distribution severely limits changes in production patterns, since it impedes symmetry between the costs and the benefits of such changes (Sarmiento, 1990).

The institutional reforms pave the way for greater participation through the opening up of opportunities for social negotiation and coordination. Outstanding in this sense are labour reforms aimed at promoting the organization and authentic representation of the workers. The institutional sphere includes reforms designed to combat such outdated social customs as the *latifundio* and servile work relationships.

In the short term, we must devise a social policy which responds to the population's most critical needs. In this respect, we must adopt a concentrated approach, which attempts to reduce action in favour of groups that do not require the specific assistance being offered. There has frequently been a tendency to counterbalance the use of the concentration technique with the principle of universality of benefits, which is indispensable with regard to the most pressing needs, those which do not manage to generate economic demand. The truth is that such

criteria correspond to different planes: concentration is, in fact, a way of making social expenditure more efficient, not one of diminishing its positive impact. General policies in the fields of education, social security, housing, nutrition and health are irreplaceable. What is more, most countries of the region are in dire need not only of restructuring but also of an increase in expenditures on basic social services.

6. *Special policies favouring structural change*

The public sector has no advantage over the private sector in terms of ability to predict the degree of success of different projects. However, it is better prepared to identify those projects that are more likely to generate beneficial externalities (Fritsch and Franco, 1989). Other things being equal, what should be subsidized is the potential for generating these externalities. Obviously, the public sector is irreplaceable in the creation of general conditions for the development of these capacities.

State action should give way to market orientations where this exist; and where this is not the case, it must help to develop them through an aggregate of measures that range from the establishment of basic conditions for advancing in the direction desired, to selective programmes in which the public sector assumes a catalytic role in economic activity.

As indicated earlier, strategic designs traditionally started with a sharp differentiation between the various productive sectors, with most of the credits going to industry. Now, however, the drastic separation between branches and sectors has lost a good part of its significance. Technological development has confused frontiers, to the extent that increasing overlapping is observed; this is a basic element to be taken into account in policy formulation. Productive activities tend to form a chain through the multiplication of links between agricultural, mining, industrial or service activities. It is imperative, particularly in the smaller countries, to apply a large dose of selectivity in identifying the link which it is desired to favour. The key criterion in this sense is the possession of comparative advantages susceptible of being dynamized (Ominami and Madrid, 1988).

The success of this policy assumes action in different areas: entrepreneurial development and worker training, which includes stimulating

medium-sized firms and supporting the small ones; the formation of service networks for producers and support of foreign trade; tax, credit and insurance incentives for exports; measures for counteracting the effects of unfair competition (anti-dumping), financial aid and international cooperation; regulations on national engineering; technological transfer programmes for public and private development institutes; special tax treatment of advisory services, training and reorganization of firms (Castillo, 1989).

Policy instruments are also varied: publication of information on markets and technology; creation of subcontracting exchanges and regional markets; tax exemptions, soft loans, direct subsidies, technical assistance; guarantee funds, commercial endorsements, risk capital and joint ventures; industrial promotion; economic regulation; protection of the consumer and anti-monopoly legislation; intellectual property and industrial security (Castillo, 1989).

The public sector can promote technological change by various means. Apart from trying to strengthen its own ability in this field, it could appropriately take the following action with respect to the private sectors: i) stimulate the creation of risk-sharing mechanisms, private, public or mixed, that would be both transparent and impartial; ii) protect innovations with adequate legislation and compensate innovating entrepreneurs who cannot otherwise profit from their efforts; iii) complement research and development activities of the private sector that may be necessary for advancing technology where it is either stagnating or close to stagnation; iv) request the opinion of the entrepreneurial sector concerning the allocation of public resources to activities leading to the creation of technological innovation; and v) prepare and provide to the public sector information of general usefulness which is trustworthy, clear and timely (Wylie, 1990).

When a vigorous effort to improve human resources is lacking, the dissemination of technology is slower or more difficult. Education and the levels of skill in the labour force are factors determining the competitiveness and productivity of an economic system. Technical education is a variable of the utmost importance (UNIDO, 1989).

It is recommended that, in the case of the small and medium-sized firms, cooperation and coordination strategies be initiated so that they can compensate for the restrictions imposed by their size (table 9).

Table 9

ASSOCIATIVE SCHEMES FOR SMALL AND MEDIUM-SIZED FIRMS

| | |
|--|--|
| <i>Marketing:</i> | They centralize the technical and financial resources of a certain number of small and medium-sized industries for the purpose of joint marketing, whether for the internal or external market. |
| <i>Purchasing centres:</i> | A group of entrepreneurs purchase their inputs jointly, thus obtaining better prices. |
| <i>Subcontracting exchanges:</i> | They articulate supply with demand. A large industry subcontracts various small ones for the manufacture of parts, components or semi-assembled products that will be subsequently integrated in a final product. |
| <i>Guarantee and endorsement associations:</i> | Entrepreneurs form an association in order to provide loan endorsements and guarantees before the banks. |
| <i>Savings and credit cooperatives:</i> | A group of entrepreneurs saves and extends credit with its own funds. |
| <i>Microfirm incubators:</i> | A group of new or growing firms is concentrated in one place, which permits them to share services and equipment and receive technical assistance, administrative support for accounting, training, etc. The aim is to strengthen new firms. |
| <i>Industrial parks:</i> | Firms are installed in the same area and share common services, which facilitate technological transfer, training and integration among them. |
| <i>Design centres:</i> | Firms form an association in order to share the design function, a formula that is particularly useful for exporters not competing in the same market. |

Source: Lysette Henriquez, manager of Technical Cooperation Service (SERCOTEC) in *El Diario Financiero*, Santiago, Chile, 9 July 1990, p. 18.

7. Institutions and public administration

In almost all countries of the region the public administration has undergone a long process of deterioration, accentuated by adjustment efforts. This retrocession illustrates one of the main contradictions affecting the State today: while its present situation is deplorable, it is not possible to ignore it, if the next stage of regional development is to be a success. Tasks as important as the design, supervision and the application of a consistent combination of macroeconomic and sectoral policies depend critically on an aggregate of institutional and technical factors and a relatively small group of persons (Israel, 1989). The public sector must be technically and politically capacitated to carry on a fruitful dialogue with economic and social personnel, in such a way that it may be possible to reach agreements which clarify, or establish, the rules of the game.

Personnel selection, the ability to retain good public administrators, and to cast aside the inefficient ones, as well as the training of existing personnel, are

all timely and important subjects, even in a period of adjustment (United Nations, 1983; Grossman, 1983). Experience has demonstrated, however, that it is not very realistic to add administrative reform to the already multiple tasks demanded by the adjustment and the restructuring of production, although this need not be an obstacle to studies of such reform that could be carried out by high-level commissions and that would lead to proposals for organic administrative changes, including transition plans.

At some levels of management, reform of administrative practices cannot be delayed. Adequate understanding and effective management of these situations depends critically on the focus with which they are analysed. Without prejudice to the importance of bureaucratic aspects proper, which in addition to hampering public administration, affect the economy's productivity, priority should be given to the consideration of institutional dimensions and the examination of public policies, viewing these as a flow of specific content.

The public administration is facing endogenous problems which, in some countries are causing its

paralysis. The manager, then is rather like a doctor for his own illness, which is not functional for achieving other objectives and becomes a problem in itself.

Public management takes place almost always at the periphery. What can be changed is never much, owing to restrictions of a financial, legal, administrative, or political nature, or a combination of these.

The central organization has to follow closely the flow of information and decisions, avoiding the temptation to create hypothetical situations. Intraministerial or interministerial coordination in megaministries is of great utility, which justifies considering it as a substantive function in itself.

The concept of public policies is sufficiently generic. It can be assimilated into those courses of action that the authority adopts in relation to a certain goal and which contribute to creating or transforming conditions, ends, or means in which economic agents carry out their activities. The existence of public policies may derive from written provisions or from bureaucratic practice, whether these are general or specific, direct or indirect, universal or individual.

In addition to public policies with a specific object, there are those of "second degree". The latter are characterized by their complexity and result from the simultaneous application of a combination of specific policies. In practice, it can be observed that

the more general the object of public policies the greater the number of these that will be affected. Inversely, the more general the public policies, the larger the number of sectors, in reality, that will be affected by the object (Lahera, 1980).

The various public policies affect the situation constituting their object in very diverse ways, in some cases neither obvious nor direct. Hence the imperative of making an effort to determine the relations between policies and reality, rather than describing in an exhaustive and formally explicit manner the different categories of policies. It is necessary to explore the fields of force created by public policies that are superimposed on pre-existing reality and to discern the intensity of each one.

The management and evaluation of specific public policies makes it possible to diagnose their efficiency with accuracy and facilitates their marginal correction, starting from the detection of deficiencies. The consequent search for alternative solutions is designed to generate and present information on results and on the most efficient manner of realizing the objectives.

Finally, it should be pointed out that the coordination and evaluation of policies constitutes a prerequisite for their efficacy. In the public administration field, the successes are accumulated marginally; the errors, on the contrary, are amplified.

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