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Instituto Latinoamericano y del Caribe de Planificación Económica y Social  
NACIONES UNIDAS-CEPAL-PNUD GOBIERNOS DE AMERICA LATINA Y EL CARIBE

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ILPES: "EXTERNAL INSERTION,  
COMPETITIVENESS AND FISCAL CRISIS"

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## PRESENTATION

This document lays the foundations for and details the first five parts of the Central Report prepared by ILPES for the VII Conference of Ministers and Heads of Planning (Montevideo, May 1989), according to the mandate of the governments of Latin America and the Caribbean, ratified in the XI Board Meeting of the Regional Planning Council (San Jose, November 1988). In compliance with this mandate, the document is organised into three major topics: External Insertion and Development (Chapters I to III), Entrepreneurial Capacity and Competitiveness (Chapter IV), and Fiscal Problems in Public Management (Chapter V). Each chapter corresponds to one of the first five parts of the Central Report (document NTI/G.VII.3).

Its main source of enrichment will be the debate of the VII Conference, although, due to its norms, this document is not subject to formal approval. Criticisms and comments will be incorporated in a subsequent review; the new version will then be sent to the Internal Editorial Service.

When Carlos Salinas de Gortari presided over SCCOPALC and CRP, he insisted that the technical documents prepared by ILPES for these forums help to focus and stimulate the debate. At this time, with the complexity of the central theme and the plurality of the viewpoints that it brings together, the component of stimulus seems to be assured.

Nonetheless, it is not an exhaustive document, since many aspects demand greater elaboration. In any case, it is sought here to delve into the most integrated view of contemporary development and the relative position of the region; also a balance of some certainly relevant regional concerns is offered. The report incorporates some certainties, sows several concerns, and contains an implicit agenda for later lectures and works. Applied research oriented toward policymaking; this was the spirit with which it was produced.

(I/TWRZY)

Santiago, Chile, March 1989  
General Administration of ILPES

## Chapter I

### INTRODUCTION

1. Finally, the "Crisis of the Eighties" is being definitively left behind. Thus, its end already has a deadline: December 31, within 270 days. The post-crisis has a name also: it will be called the "Crisis of the Nineties." On the Gregorian calendar, two phases; in true history, continuity.
2. Part of this continuity is a remnant from the seventies. The analysts who aim their searchlights back in time illuminate different roots and points of departure. From 1979, when sustaining the parity of the dollar meant abruptly raising the interest rate, first in its crib and then in the world. From 1978 or 1973, for those who believe that the breath of life for the crisis issued from OPEC. From some year in the middle, when the region grew and was delirious with the easy catch of external savings. From 1971, on the day that the exchange rates began to fluctuate, fomenting the erratic mobility of international capital. And, with this we would be nearly regressing another decade. Other analysts, with flashlights of a shorter reach, tend to guide them in the direction of 1982, a year marked by the sharpening of the recessive cycle and the imbalance in the balance of payments of the region. Afterwards, the most recent years would be analysed under diverse focuses.
3. This document is not directed at the "crisis of the eighties," but it cannot omit it either, and, sometimes, it will be necessary to touch upon it. Its roots receive even less attention; however, some of the phenomena mentioned here are based on them also. The document starts with the international insertion of Latin America and the Caribbean; passes through the role that private and governmental sectors can play in different reinsertion policies; and

concludes with some functions that national planning agencies can perform in its support. Of course, "insertion" or "reinsertion" are used here in a very broad sense (see Document NTI/G.VII.3). To limit, "insertion" refers to the globality of the situations of region's "interdependence" with the rest of the world. In this particular case, "reinsertion" suggests changes in the foreign policies that seek--within the framework of interdependence--a less perverse distribution of vulnerability.

4. The region entered the eighties euphoric and vulnerable; it will end them sad and more vulnerable. Undoubtedly, euphoria, sadness, or vulnerability--just as nearly all other attributes--are not distributed very homogeneously, both among countries and within each of them. Deliberate policies to reorganise foreign relations can help to mitigate the current vulnerability, but will hardly be enough to eliminate it. In fact, the type of external integration of the region explains part of its problems--including some serious ones--and conditions others, but it would be a simplification to explain the vicissitudes of the region only on the basis of its external insertion.
5. The region will surface from the eighties with a population of nearly 450 million inhabitants, slightly less than 8% of the world total, with geography being one of the main elements of unity. Two accumulated rates sum up the decade: the product rose by 11.6%, while the population grew by 16.1%.<sup>1/</sup> However, spread measurements must replace nearly all the averages.

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<sup>1/</sup> See ECLAC, La Evolución Económica Reciente de América Latina y el Caribe, Santiago, Chile, January 1989.

6. The demographic heterogeneity increased in the region: today 97% of the population is concentrated in practically one half of the countries (20), the other (14 countries and four associated states) hold the rest. The population in the age group of the economically active (15 to 60 years of age) varies from country to country, from less than one half to nearly two thirds of the total population. The life expectancy fluctuates between 52 and 72 years of age. In one of its countries, of every 100 inhabitants, 85 live in cities; on the extreme, only 27 are urban residents. In the latter case, of every 100 inhabitants, there are more than 60 illiterates, both men and women. In the following four cases, between 41 and 48 of every 100 women are illiterate, while this number varies from 5 to 9 in the four best cases. Of every 100 inhabitants, between 32 and 42 are illiterates in four national cases; figures that go from 5 to 8 in the four best situated cases.
  
7. In addition, the economic and social differences in the region have been increasing. The largest per capita income (1986) was 16 times the smallest, while the highest GDP was 96 times the lowest. Only three countries generated 77% of the value added by the regional manufacturing industry (1985). As for income distribution, the top 10% of the population absorbed from less to one third the national revenue to more than one half, in the two extreme cases. The lowest 20% received between 2% and 3% of the national revenue of their countries and, in the best situation, slightly less than 4%. In the situation of the most concentrated national revenue, one citizen from the highest 10% received US\$ 7,620 in 1986, higher than the per capita income of Saudi Arabia or New Zealand and equivalent to 60% of the per capita income of Japan in the same year. In one of the four poorest Latin American countries, a citizen from the income class defined as the lowest 20% received US\$150,



the same as an average citizen from Butan, Burkina Faso, or Nepal, and only higher than Ethiopia, the poorest country in the world (US\$ 120 per capita income in 1986).<sup>2/</sup> These few spread indicators provide an idea of how much the averages can falsify the economic and social analyses of Latin America and the Caribbean at the end of this decade.

8. In the beginning, the hope for progress--fed by some indicators from the seventies--would rapidly dissipate. "The outset of the eighties was a decisive moment. The change in the industrialised countries toward anti-inflationary macroeconomic policies caused a prompt hike in nominal interest rates. The developing countries, with high foreign debts, were harshly punished. The combination of the highest interest rates with the lowest prices of exported basic products (barring petroleum) produced a staggering rise in the real costs in all kinds of debt, new or old."<sup>3/</sup> Since that time, the region would show signs of an enormous instrumental creativity, alternating policies with different degrees of orthodoxy and oriented predominantly at controlling monetary aggregates and key prices. A moderate reactivation thrust was followed by greater imbalances; then, enthusiastic austerity would end up aggravating unemployment and accentuating social tensions. Back to the same...
9. In the area of macrovariables, two terminated with irreparable damages: investment (physical and social) and expenditures for science and technology (S&T), both having the attribute of being embryos of the future. In a

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<sup>2/</sup> The basic demographic data is from CELADE: América Latina en el Año de los 5.000.000.000, Santiago, Chile, 1987; the other data (especially those on the product and value added) are from the World Bank, Informe sobre el Desarrollo Mundial, 1988, Washington, June 1988.

<sup>3/</sup> World Bank, op.cit., Part I.

globalised world, the opportunities for the reinsertion of Latin America and the Caribbean are already restricted today--and will continue to be restricted in coming years-- as a consequence of this basic fact: **the short-term decisions forgot that, in each yesterday, there were definitive factors that influenced the future.** In the recent past, certain slowdowns in the capital formation of developed countries were frequently accompanied by increases in research spending, giving birth to decisive innovations in S&T. Latin America and the Caribbean, on the contrary, reduced both: investment and research spending.<sup>4/</sup>

10. Reducing the analysis of the external insertion to the examination of trade and financial data is a relatively frequent occurrence. The perspective of this document is broader. In the contact among nations--while the trade of goods and services and capital movement are on the frontline--in reality, in logistics, on the rear they are confronted by all their economic, social, political, and cultural structures. As seen, the internal image of the region is disparity and lack of unity. Also, the balance of internal successes, in general, has been poor, when aiming at both reactivation and stability. Finally, the negligence with investment and S&T spending reduced the opportunities for productive restructuring and technological progress. **All these phenomena must be considered when examining the subject, "External Insertion, Development,**

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<sup>4/</sup> However, in the same period domestic savings as a percentage of GDP has remained relatively stable, almost the same 23% as in the seventies. In round numbers, 4% has been lost due to the deterioration in the terms of trade and another 4% as payment of the debt service. The savings available for investment would be limited to nearly 15% of the regional GDP. During the seventies, the average growth of investment slightly exceeded 7% per year, later (1981-1987) it was negative, with the exception of five countries. Simultaneously, research and development spending was curtailed in the region to less than 0.7% of the GDP.

**and Planning.**" On this basis, the rest of the report is subdivided into five chapters.

11. In Chapter II, certain dynamic aspects of the relationship of Latin America and the Caribbean with the rest of the world are reviewed. As a frame of reference, the change in the relative standing in the most conventional indicators of trade and financial movements is shown; this part ends with a reference to the reduced weight in decision-making of the region in the multipolarised world of today. Next (Chapter III), a relationship is established between external insertion and five major phenomena that, in the opinion of ILPES, enable a better understanding of contemporary development. Although it starts with the cultural aspect, this is a trilogy of an essentially economic nature: first, the weight of the "input of knowledge" per product unit grows; second, the innovations in processes, products, organisation, and market are accelerated; third, a proliferation of new specialisations of labour, formal and informal, is being witnessed. The fourth refers to the growth in the complexity in modern society, largely as a result of the three previous phenomena. This leads to the fifth and last: the crisis of governability, where the "internal" and the "external" also intermingle.
  
12. Later (Chapter V), emphasis is placed on the vitality of the productive enterprise as a strategic resource for external reinsertion policies. At the outset, some facts on world trade are re-examined, pointing out the need for an authentically competitive productive structure. Based on this, the real boost in productivity as the key mainstay for external competitiveness is considered. The growing disparity between the region and the developed world is evident.

13. Potential policies for external reinsertion will contain a broad variety of instruments. They will have to affect integrally different areas: capital formation, scientific and technological research, the infrastructure of communications and services, restructuring of the productive apparatus, the understanding of current markets and their trends, new modes of productive organisation, health, and education. It will also be necessary to have a keen coordination among monetary, fiscal, and credit measures, in order to finance development projects that are necessarily medium and long-term. Finally, it will be necessary to make the expected external success compatible with internal results that favour greater social integration and improved conditions of living and political coexistence. The premise here (Chapter V) is that **a renewed public sector will be irreplaceable for the organisation of so many means and such difficult objectives.** This renovation will imply both fiscal and management aspects. The last year of the decade is an especially opportune moment for these challenging reflections.

## Chapter II

**DYNAMIC OF LATIN AMERICA AND THE CARIBBEAN IN THE WORLD CONTEXT**

14. A full knowledge of the integration of Latin America and the Caribbean with the rest of the world should consider the **main phenomena that altered the world economy in the period following the Second World War**. Doing this would go beyond the limits of this work. In any case, several of them are hidden behind the numerical series registered by international economic transactions, influencing the international insertion of developing countries. It should be repeated, however, that the relevance of the distinct factors varies from country to country.
  
15. The evolution of the rhetoric--in different phases and organisms of international dialogue--was producing signs that probably would have given a hint as to the background of some structural transformations. Reconstruction, development, mutuality of interests, cooperation were all concepts progressively replaced by protectionism, interdependence, bilateralism, market. In the world of facts...**a process of internationalisation of production and markets intensified**. Some of its current peculiarities should be noted. One, the concentration of capital in the enterprises that sustain that process is magnified, allowing them a growing influence in the orientation of future development. Two, its specific business policies--of productivity, wages, reinvestment, for example--are designed also with an international scope and do not always coincide with the respective policies of the countries where they act. Three, consequently, an appreciable part of what is conventionally known as the "international division of labour" exists today within some enterprises. Four, a new, and yet little studied, articulation of the three

conventional spheres of capital (productive, trade, and financial) has occurred, as well as between them and a new sphere that is beginning to be called "intellectual capital."

16. Likewise, in the productive sphere there is a: fifth, a change of strategic procedure that puts an end to a secular paradigm of industrialisation based on, until recently, stable models of manufactures and mass production; sixth, this change opens up new perspectives for the geographic deconcentration of production and the main offices of companies go on to retain only key segments of overall organisational control (finances, quality guidelines, decisions on technologies, market distribution, among others); seventh, in mutual fertilisation with the above phenomenon, there is an overwhelming development of communications technologies pushed as high priority; eighth, a significant change takes place in the industrial scenery of developed countries; ninth, production and trading have almost equivalent strategic importance and, therefore, real productivity and competitiveness must be associated as a sine qua non condition for penetrating and consolidating markets in this new context (see Chapter IV).
  
17. Parallely, there is another restructuring process of the international scenario--not completely independent from the previous one--which is shaping new blocs of association among countries. As is known, the United States-Canada agreement, the unification of the EEC, the rise of Japan, and, more recently, of other countries of Southeast Asia are new nodes in this restructuring. This could be complemented by China, the USSR, and other CMEA countries, apparently on the verge of important changes in their type of foreign relations. To a certain point, these new nuclei would appear to be moving, little by little, the center of gravity

of the world economy from the Atlantic Basin to the Pacific Basin.<sup>5/</sup>

18. The first changes are more related to the international private sphere: the latter, with their public sphere. Either of them affect the region's opportunities in the establishment of its foreign relations. Both reflect, moreover, a restructuring of world economic power: in production, trade, finances, and technological development. In the business realm of the region, the increase in productivity and the creation of competitive capacity are two instrumental objectives for improved external practices; in the governmental realm, it would be necessary to develop a new negotiating capacity. Just as in industrialised countries, both realms should be complementary. The synergy between private and public sectors has been generally poor in the region; both were posed as being little compatible. Thus, another factor takes shape that thwarts the opportunities for a dynamic reinsertion of the region. In comparison, the polynuclear nature of the world of the future should favour those opportunities: herein lies another demand for fine harmony between diplomacy and development policies.

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<sup>5/</sup> A similar viewpoint can be seen in SELA: El Proceso de Industrialización de América Latina, XIV Latin American Council, Caracas, September 1988. An up-to-date analysis of the relations among developed countries from the perspective of the region is presented in SELA, Relaciones Económicas Externas de América Latina y el Caribe, Caracas, September 1988.

## II.1 LOSS OF TRADE POSITION

19. This first section,<sup>6/</sup> of an introductory nature, briefly analyses some global trade relations. In the first place, it should be noted that the share of the region in world production remains relatively stable when the comparison is limited to the recent past, for example 1970/1988, in relation to both the rest of the world and all developing countries.<sup>7/</sup>
20. However, for a relative appreciation of the degree of external insertion, the rates of participation in exports are more eloquent than those of production. In this case, the optimism of the conclusions varies with the base year chosen for the analysis. By regressing in time, the loss of global presence is more evident. In 1948, the Latin American share in world exports was practically 11%, dropping slightly two years later. In 1960, it had slid to 6.7%; in 1970, to 4.8%, rallied in 1980 to 5.7%, and fell

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<sup>6/</sup> ILPES limits itself, in this part, to pointing out the most relevant aspects for its specific mandate, that is, the coordination of long-term policies or development planning, especially in mixed economies. The subjects of trade and development belong to other fields of specialisation, particularly ECLAC. This commission and other regional organisms--OAS, SELA, IDB, among others--systematically produce ample documentation in this regard: it would be worth consulting these sources for details that are not included here: see in particular, ECLAC, La Evolución Reciente de las Relaciones Comerciales Internacionales, International Trade Division, Santiago, Chile, August 1988.

<sup>7/</sup> Of the extremes of the period, agricultural production increased its share from 12% to 14.2% of the world total, while the industrial share went from 7.2% to 7.5%. With respect to all developing countries, the changes in relative position have an analogous direction and intensity; in agriculture, it went from 22.3% in 1970 to slightly less than 25% at the middle of this decade; in industry, the share rose from 34.4% to somewhat less than 40%. In both comparisons--with the world and with developing countries--the share averages are far from the values corresponding to specific products. In some manufactures the relative share of the region grew between 1970 and 1985 from 2% to less than 8%. See CLEPI data, El Desafío de la Incertidumbre: Informe sobre la Economía Mundial - Perspectiva Latinoamericana (Santiago, Chile: Nueva Sociedad, 1988).



again in 1986 to 4.2%, a little less than the share of fifteen years before. Latin America and the Caribbean occupy today less than 40% of the space that they had in exports 40 years ago.<sup>8/</sup>

21. In this part of the document, the references to imports or the deterioration in the terms of trade will be omitted. Undoubtedly, the export and import coefficients in relation to demand <sup>9/</sup> reveal significant changes in the relations of the region with the rest of the world. During the eighties, the import restraint of the region has permitted, in several countries, the generation of expressive balances in their trade balances (see Chapter IV). However, the external trade surplus earned, through heroic reductions in imports, has not necessarily been favourable from the standpoint of long-term development. The fact that imports are less--to the point of weakening the productive structure--, along with the cutback in investment and insufficient spending on science and technology, led to a greater separation from the developed world.

## II.2 NET TRANSFER OF RESOURCES

22. For at least three decades, the different flows that make up the balance of external resources have been undergoing significant changes. Due to both simplicity and reasons of recent history, these brief comments will be divided into two periods, with a different approach: in the first, stress

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<sup>8/</sup> The data up to 1960 are from R. Ffrench-Davis, Intercambio y Desarrollo, (Mexico:FCE, 1981); later data came from INTAL/ECLAC, América Latina en la Economía Mundial (Santiago, Chile: ECLAC, 1988).

<sup>9/</sup> "Proxis" variables of external opening and external dependence, according to some specialists. F. Fajnzylber, Industrialización en América Latina: de la Caja Negra al Casillero Vacío, Cuadernos de Cepal, No. 60, Santiago, Chile, January 1989.

will be placed on the changes in structure; in the second, on the change in the sign of the net transfers.<sup>10/</sup>

23. It would be convenient to make an additional distinction. As is known, the Net Transfer of Resources results from a combination of two flows: Net Capital Revenue (one) from which are deducted year to year, the Net Payment of Earnings and Interest (two). This paragraph deals with **the changes in structure in the series of Net Capital Flows**, precisely at a time when they have been very pronounced: that is, 1960-1975. As is also known, two inflows meet in these flows: the Net Revenue from Public Resources and those from private resources. In the period, both change their relative weight: in 1960-1965, the receipts "via governments" corresponded to 60% of the total Net Capital Revenue and the private to the rest; these percentages were inverted in 1966-1970. In the following five-year period, the receipts "via governments" dropped to 25% (always in annual averages). In 1977, the trend was accentuated: only 12% were of public origin and 88% private.
24. **The currents of resources within each inflow also have changed.** For the sake of simplicity, let us compare the annual average of the 1960-65 period to the year 1977.
- a) In the current of the external resources "via governments," the multilaterals dropped their share from nearly 20% to around 7% ("funds for development" were cut back simultaneously to one half). In the meantime, the resources of a bilateral origin retransferred to the region "via

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<sup>10/</sup> As will be seen, the region received from abroad until the end of the seventies around 2% of the GDP from the Net Transfer of Resources. During the eighties, as already mentioned, it reached the point of remitting an amount approaching 4% of the GDP. The rest of "less 6%" is doubly significant; it explains the fall in investment, which will affect the near future, as well as the systematic reduction in per capita income that in 1988 equalled that of ten years before. See ECLAC, Balance Preliminar de la Economía Latinoamericana-1988, Santiago, Chile, December 1988.

governments" fell from 41% of the total to slightly less than 5%.

- b) In the resources of private origin, the differences in composition are also pronounced. The banks raised their share from an average close to 2% in 1960-1965 to more than 48% in 1977.<sup>11/</sup> The credits from suppliers fell slightly (from almost 8% to nearly 6%); a similar situation occurred with receipts from direct investments (which descended from 25% to 20% during the period).<sup>12/</sup>

25. In fact, the Net Capital Revenue more than doubled between the 1971-1975 period and 1976-1977; nevertheless, these figures already referred to resources of a highly diverse origin, subject to varied types of conditionality, of differing uses, and with future effects that were also distinct. On the other hand, in the change in structure occurring at the start of the seventies, commitments with the remittance of earnings and interest payments that, later, would end up voiding the developmentalist effect of the Net Capital Revenue were already partially incubated. Finally, there are clear indicators that this revenue--since that period--had different destinations within the region and a greater concentration.<sup>13/</sup>

26. As mentioned, the analysis of the 1976-1988 period will be made with another approach and centered on the series of data on the Net Transfer of Resources. The 1976-1977 period can be considered as transition.

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<sup>11/</sup> The region had already imported--at this point--some embryos of the crisis of the eighties. Remember that all the percentages are in relation to the yearly average of the Net Capital Revenue.

<sup>12/</sup> The data from the 1960-1977 period are from by O. Sunkel, América Latina y la Crisis Económica Internacional: Ocho Tesis y una Propuesta, (Buenos Aires: RIAL/GEL, 1985). On the subject, see especially the "Cuarta Tesis," starting on p. 22.

<sup>13/</sup> Source: ILPES, La AOD en América Latina y el Caribe, Santiago, Chile, 1985 (reserved). The Caribbean comes to absorb 34% of the Official Aid for Development and Central America an almost analogous percentage.

- a) the **Net Capital Revenue** rose by 36% as compared to the previous two-year period, reaching somewhat less than US\$ 17.2 billion in 1977 and began a cycle of expansion that would last until 1982;
  - b) the **Net Payment of Earnings and Interest** went up by 41% as compared to the previous two-year period, reaching US\$ 8.2 billion in 1977 and began an expansion that will easily continue into the nineties.
27. In 1978, the Net Transfer of Resources reached a historical record.<sup>14/</sup> Since 1982, it shows negative annual values (less US\$ 28,990 million in 1988). In seven years, from 1981 to 1988, the region transferred overseas domestic savings totalling US\$ 178.7 billion; which was mainly only for the partial payment of interest. The total transferred was 12% higher than all Net Capital Revenue received from abroad during the last ten years.

### II.3 CHANGE IN WEIGHT IN MULTILATERAL DECISIONS

28. In closing this background on the structural changes in the relative position of Latin America and the Caribbean, it is necessary to add, although briefly, some considerations on their progressive loss of influence in multilateral development policy matters. The comments on production and trade and especially on resource transfers already back this perception of less relative power. The following considerations are based on positions of entities more directly related to this subject, contrasting 1969, 1979, and a recent year.

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<sup>14/</sup> A maximum of US\$ 16 billion, result of US\$ 26.2 billion in Net Capital Revenue and US\$ 10.2 billion in Payment of Earnings and Interest. Since then, it has declined until reaching US\$ 10.4 billion in 1981, that is, less than five years before. The data on the period that begins in 1976-1977 corresponds to ECLAC, La Evolución Reciente de América Latina y el Caribe, Santiago, Chile, January 1989.

29. Once again, the problem has remote roots. Exactly twenty years ago, the "Latin American Consensus of Viña del Mar" stated in its final resolution: "The process of development of the region and the transformations that have been operating in each of its countries, along with the changes that occur in the world, impose important modifications in the relations of Latin America with the other members of the international community." Further on, it added that it is "...recognised at the same time that the solution to development problems has become a dominant concern in the international community, whose cooperation has not been sufficient. The success of those efforts 15/ largely depends on the international community, and particularly the countries having larger weight in world decisions, recognising and assuming the responsibilities that befall them."16/ Five years later, multilateral aid for development directed at the governments of the region had reduced its participation by two thirds and the bilateral aid of the "country that had the greatest weight in decisions" by nine tenths. The regional voice no longer carried so much weight...
30. Ten years later, in a meeting on North-South relations, a specialist of the region stated with a certain sense of premonition, "As the resources available for international cooperation programmes become increasingly more scarce and as--correctly or incorrectly--the international community perceives the new "status" of Latin America within the Third World as a privileged situation, it would be almost certain that our region would no longer be a recipient of official

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15/ The original text refers to national "efforts" for overcoming underdevelopment.

16/ Quoted by H. Santa Cruz, Cooperar o Perecer: El dilema de la Comunidad Mundial, Vol. II (Buenos Aires: GEL, 1988), p. 428. (The boldface type is from the transcription.)

aid."<sup>17/</sup> Afterwards, other analysts would condemn a proposal to reorient international cooperation, which would have, on the long run, the effect anticipated above: a declining presence of Latin America and the Caribbean in the list of aid to the Third World. The new orientation--it was said--would end up implying an additional loss of weight for the region in the dispute over long-term financing for development. The reference presented next is on one of the few proposals of the Brandt Report,<sup>18/</sup> accepted by developed countries and later by some international organisms: the emphasis on the poorest countries. It was affirmed then,<sup>19/</sup> "In practice, the emphasis on the world of absolute poverty tends (i) to reduce the resources for the world of those that are a little less poor; (ii) to permit the North to adopt relatively cheap measures in relation to the South, of undeniable impact on the public but that, basically, do not alter at all the current international economic order, and (iii) to constitute consequently a mere analgesic to relieve consciences without modifying substantially the structure of the dependence that perpetuates poverty." Since 1980, Latin America and the Caribbean would undergo "graduation," which reduced their priority in the distribution of official development aid. This would erode the availability of external resources that, in prior years, were being provided through commercial bank operations.

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<sup>17/</sup> See the presentation of R. Botero at the CPU/RIAL seminar held in Chile, January 1979 in L. Tomassini, et.al., El Diálogo Norte Sur: Una Perspectiva Latinoamericana (Buenos Aires: EB, 1982), p. 93.

<sup>18/</sup> As is known, in 1979 the report presented a far-reaching summary of North-South relations. A substantial part of its proposals referred to the real and urgent needs of the Third World; however, the future would continue an opposite course (see the ILPES proposal: Cooperación e Integración Regional en la Reactivación y en el Desarrollo: El Papel de la Planificación, ILPES/SCCOPALC, Santiago, Chile, March 1987).

<sup>19/</sup> The quote corresponds to the presentation by R. Abdenur and R. Sardenberg at the ILPES/RIAL Meeting, Canela, Brazil, August 1980; see in Tomassini, et.al., op.cit., p. 263.

31. As a final example, it is convenient to remember what was expressed in the recent OAS report. It is recognised there that, "The profound interdependence among industrial countries that make up the bloc of advanced market economies involves production, investments, technological currents, and trade. There is a system of ongoing negotiations that has impeded the prevention of the collapse of the multilateral system of trade and payments of the North." Next, the same document concludes: "In the case of Latin America and the Caribbean, the situation is very different. The region is a passive agent of international events and its weight in decision-making in the international system is practically null. This helps to explain the depth of the economic depression in which the region is immersed."<sup>20/</sup>
32. In conclusion, it is necessary to add that the little relative influence of the region in the world is not limited to global trade, capital movements, and the feebleness of multilateral dialogue, the three aspects considered so far. In matters such as energy,<sup>21/</sup> services,<sup>22/</sup> intraregional integration,<sup>23/</sup> among others, its current situation could be

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<sup>20/</sup> Apud OAS, Desarrollo Integral y Democracia en América Latina y el Caribe - Ideas y Agenda para la Acción, XVIII Regular Period of Sessions, Washington, October 1987, p. 17. (The boldface type is from the transcription.) See also Eloy Mestre, Cambios en la Marco Internacional y la Estructura Cooperación Interamericana: El Desafío, OAS, Statistical Bulletin, Washington, December 1987; also SELA, *op.cit.*

<sup>21/</sup> See IDEE, Energía y Desarrollo: Desafíos y Métodos, Bariloche Foundation/EEC, Editorial Patagonia, Fuerte G. Roca, Argentina, 1984; and, for a more recent view, see C. Risopatron, Cambios en la Inserción de América Latina en el Mercado Mundial de Energéticos, 1960-1985, Natural Resources Division/ECLAC, Santiago, Chile, November 1988.

<sup>22/</sup> See ECLAC, Integración Regional: Desafíos y Opciones, International Trade Division/ECLAC, Santiago, Chile, February 1988 (especially Section II.C.). In addition, R. Beca, El Comercio Internacional de Servicios en el Area de la Informática, la Información Electrónica y las Telecomunicaciones, UNDP/UNCTAD/ECLAC, Project RLA/87/019, Santiago, Chile, November 1988.

<sup>23/</sup> As more recent works in this regard, see ECLAC, *op.cit.*, and J. Marcovitch, O Novo Contexto Mundial. Deafio Tecnológico e a Integracao Latinoamericana, CINDA/UNDP/SECAB, Sao Paulo, October 1988; C. Massad,

characterised as below the needs of its population, the virtual potential of its human and natural resources, and its right of historical realisation. The region's insufficient weight in decisions in key issues of contemporary development has helped to magnify the effect of the double compression to which it was subject since the beginning of the decade: on the one hand, its "graduation," that practically voided its access to development aid funds<sup>24/</sup> and that was reflected in the cutback in the transfers of its governments; on the other hand, its subordination to new conditionalities established by bilateral cooperation or credit operations contracted at inadequate maturities and floating interest rates.

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Integración: Una Nueva Estrategia, INTAL/ECLAC, Santiago, Chile, November 1988; F. Peña, ¿Sólo un Sueño del Futuro? La Integración Económica y los Desafíos Actuales de América Latina, IDB/ALIDE, Buenos Aires, May 1988.

<sup>24/</sup> It should be kept in mind that, during the eighties, only one country in the region maintained the right to apply as a beneficiary of certain lines of multilateral technical cooperation. Likewise, UNDP regional projects for Latin America and the Caribbean were considerably reduced in comparison to other regions.



## Chapter III

**III. THE REGION IN RESPONSE TO KEY PHENOMENA OF  
CONTEMPORARY DEVELOPMENT**

33. The possibility that Latin America and the Caribbean achieve fulfillment in the world of tomorrow will depend on their adaptation to the patterns of business and governmental behaviour that prevail then. This premise implies a shift in the perspective of the past. In fact, the availabilities of the productive factors of the region have changed in potential with respect to the world of the future. Therefore, the mere recent history of the economic presence of the region in the world is only one of the elements that will shape its possibilities starting in the next decade.
34. ILPES has been articulating its understanding of contemporary development around five phenomena, which can be differentiated but closely linked among themselves.<sup>25/</sup> Next, the chapter is organised according to a sequence that can be summed up in the following:

- knowledge accumulates, dominated by a technological purpose; then
- it permits the acceleration of productive and organisational innovations; for this reason the present is witnessing

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<sup>25/</sup> In its effort to renew planning conceptually, methodologically, and technically, it is necessary for ILPES to have a minimally articulated view of those aspects that make the actual development peculiar. The task of coordinating medium- and long-term policies is not indifferent to the development strategies themselves; orientations and alternatives with respect to the future are inseparable from possible proposals on the management of policies and concrete instruments. See the bibliography produced by ILPES from 1984 to present. Chapter III reproduces parts of A. Costa-Filho, A Imersao Internacional de América Latina, ILPES, Santiago, Chile, April 1989.

- a proliferation of specialisations of formal and informal labour; which contributes to generating
- a great complexity of structure and social interaction; which, in turn, creates
- new tensions as regards governability and the capacity to govern.

### III.1 TECHNOLOGICAL KNOWLEDGE:

#### THE NEW CRITICAL INPUT

35. Some time ago enterprises and governments of advanced industrial economies have modified the pattern of their spending on Science and Technology (S&T), expanding them and reorienting them with a more pragmatic sense. Both the knowledge destined to being technology and the technology destined to being a product and expanding markets increased their relative rates of growth with respect to other types of knowledge and technology. Thus, the "touchstone" of a new productive paradigm was being prepared: knowledge and technology converted into "information" would penetrate and dominate modern production relations. It seems difficult to study contemporary development without understanding this basic phenomenon.
36. That "ownership," although mentioned figuratively, must be understood very concretely: the inputs of knowledge are today on the "critical road" of any search for better alternatives for combining productive factors. "Better" is a vague concept and warrants definition: "better" is the technological road that permits a drop in costs, which is bolstered by inputs of renewable and controllable supply

and has potential for mass diffusion.<sup>26/</sup> All this is logical and functional within the framework of the market paradigm of advanced economies, where ongoing, accelerated technical progress performs a strategic function. "Information" as input makes the synthesis among R&D, accumulation of knowledge oriented toward production, technological change, productive reorganisation, and in addition, broadens the conditions for the strategic control of production and marketing.

37. As critical input, knowledge converted into "units of information" changes the ratio in the use of other inputs (natural resources, labour, energy) and, little by little, introduces a factor of obsolescence into previous business management techniques. That knowledge is not abstract; it can refer to the ownership of a new productive process, modernised design of a product, a solid prognosis of the market, or a different management procedure. However, production itself "dematerialises" since there will be less raw materials, labour, or energy per product unit.<sup>27/</sup> Productive capital is partially freed from its physical and financial roots and takes the form of "intellectual capital."<sup>28/</sup>

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<sup>26/</sup> With a similar approach, FLACSO refers to "key input"; see Nochteff, et.al., Revolución Tecnológica, Autonomía Nacional y Democracia, FLACSO, Buenos Aires, August 1987.

<sup>27/</sup> The well-known opinion of UNCTAD states that the ratio "raw material/industrial product unit" fell annually by between 1% and 1.5% since the beginning of the century. A more recent IMF study shows that this ratio has been declining more rapidly. The chip is a symbolic example of "dematerialised product": raw materials correspond to 2% to 3% of its cost (quoted by R. Arocena and J. Sutz, Los Desafíos del Cambio Tecnológico, (Montevideo:FESUR/F.F. Ebert, January 1989).

<sup>28/</sup> See especially I. Minian, "Cambio Estructural en la Economías Avanzadas: Temas para el Debate sobre Estrategias de Desarrollo" en I. Minian, et.al., Cambio Estructural y Producción de Ventajas Comparativas, CIDE, Mexico, August 1988.

38. The accumulation of intellectual capital displaces the boundaries of technological power forever; this is concentrated in political geography. The electronic complex,<sup>29/</sup> biotechnology, development of new materials, and new energy resources are some branches in which the efforts are concentrated. Thus, high technologies are oriented from birth: first they inaugurate, then they spread the new technological and productive pattern. Conquering it has a cost in foreign exchange; resisting it, a cost of historical isolation; and being submerged in it, a cost of sovereignty. It is necessary to assimilate it selectively, but this assumes prior spending on R&D; the most difficult intermediate slope for those countries that did not previously accumulate some intellectual capital.<sup>30/</sup> This sums up some of the concrete challenges of the end of this decade.

39. There are other more intangible challenges. In economic theory, for example, it is necessary to consider how many cracks there are already in its foundations in both directions of the theoretical spectrum.<sup>31/</sup> There are other more complex challenges, such as the formation of a new

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<sup>29/</sup> In this meaning, the electronic complex includes the entire information technology sector. See the series of UNIDO/ECLAC publications, Industrialización y Desarrollo Tecnológico (Nos. 1 to 4), Santiago, Chile.

<sup>30/</sup> The objective of R&D in developing countries can only have, on a limited basis, the creation of high technology. However, it plays an indispensable role in creating their own capacity of selection, adaptation, and management of those technologies. With respect to the idea of "filtering" of new technologies, see the summary by GRADE, Ciencia y Tecnología Hacia el Año 2.000, in Report of the Consulting Meeting, UNESCO, Caracas, June 1988.

<sup>31/</sup> Three examples: the greater weight of the inputs of knowledge in the modern relations of production could affect the bases of distinct theories of value (ILPES, 1986); the "third wave" of transformation "demands rethinking the very nature of ownership." (See article by H. Toffler and A. Toffler, El Concept de Propiedad empieza a ser Repensado, F.S.P., Sao Paulo, January 1981); and three, magnetic payment cards are altering the conventional concept of the speed of currency circulation.

society, with yet little known changing relations of regulation and control. The challenges--one or another--are not to be chosen, they simply "are." The contemporary economic dynamic is impregnated with them. Whatever the development strategy adopted may be, it means assuming a stand on the type of integration desired in the international context, from where many of these challenges surface. In the region, this is even more crucial because--justifiably or not--these challenges have been relatively ignored in the past and especially during the eighties.

### III.2 ACCELERATION OF INNOVATIONS: SLOGAN OF LEADING ENTERPRISES

40. This negligence with regard to the future has reduced the region's possibilities of implementing reinsertion policies whose effects are felt rapidly and are longlasting. Recognising the increased presence of the inputs of knowledge in modern production relations--with the downgrading of the other inputs to positions of lesser relevance--means admitting that the comparative advantages of the region have been altered. This is clearer when distinguishing the accelerated introduction of innovations in the entire spectrum of economic activities from the previous phenomenon. Indeed, this distinction is quite valid when involving innovation at the level of products or marketing and organisation procedures; but it is nearly impossible when referring to changes in productive processes. In fact, innovating in processes implies increasing the relative weight of the information inputs per product unit.
41. The control of technological innovations is concentrated at an international scale. When the goal of dynamic external reinsertion undergoes productive modernisation or technology

transfer, a delicate negotiating problem immediately arises. Internally, it is necessary to be aware of and know how to select options; outside, the transfer agreement will be impeded as long as it implies a potential risk of competition against the vendor. Therefore, there will be transfers that will be closed, and others whose conditionalities will reinforce asymmetrical interdependence among the advanced countries that supply it and developing countries that receive it. Also, here the subjects of external insertion and development connect.

42. New reinsertion policies acquire greater urgency as innovations accelerate in world production and trade. The longer that the restructuring of the productive apparatus of the region is delayed, the more difficult it will be to gain access to a dynamic position with more weight in the world economy, since it would be initiated from a more isolated situation. Once again in history, possible modernisation will be heterogeneous both among the countries of Latin America and the Caribbean and within each of them. Various indicators could be used to demonstrate the acceleration of the innovative process.<sup>32/</sup>

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<sup>32/</sup> In the United States, the high tech sector has grown, between the late seventies and early eighties, at an annual rate of around 14% (five or six times higher than the average growth of the domestic product). In that sector information technologies have a special relevance, as is known; thus, it is felt that between 1947-1983, while the "production sector" tripled, the "information sector" multiplied 5.5 times and its segment of communication technologies, information equipment and office material, nearly seven times. If base 100 is attributed to the number of patents requested during 1975-1977 in some advanced technologies, that indicator in the 1980-1982 period reached 131 in telecommunications, 157 in integrated circuits, 227 in robotics, and 544 in microbiology and enzymology, for all the most advanced economies. ILPES estimates on the basis of OECD original data, *Economics Studies*, No. 11, Paris, Autumn 1989, and C. Jonscher, quoted by I. Minian, et.al., *op.cit.*, pp. 15 and 16. The indicators presented on patents requested correspond to West Germany, the United States, France, Japan, Italy, and the United Kingdom.

43. That acceleration has been possible only due to the previous growth in R&D spending. West Germany, Japan, and the United States dedicate, on the average, more than 6% of their manufacturing value added exclusively to R&D.<sup>33/</sup> In terms of percentages of GDP, the advanced market countries would be dedicating between 3% and 3.5% to R&D, while Latin America and the Caribbean, no more than 0.7%.<sup>34/</sup> Two years ago, the region disbursed on S&T less than 1% of the spending of developed countries.<sup>35/</sup> As already mentioned, in this aspect the region as a whole is unequipped to assume an immediate restructuring of its productive apparatus, independently of the specific problems in financing it. In the framework of the concepts expressed, **two capital deficits are added here: financial and intellectual.**
44. During the eighties, the total of these insufficiencies acquired greater importance when the pressure doubled due to modernisation. Up front, as suction, a psycho-social factor: the enchantment of something new, the fascination for something novel; particularly induced and globalised by the increased scope of mass communications. From the rear, a subtle "technicism": in the calculation of private and public cost-benefits, the hike in interest rates at the beginning of the decade displaced to the right, in the axis of the abscissas of the domestic rate of return, the break-

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<sup>33/</sup> OECD, Economics Studies, *op.cit.*

<sup>34/</sup> Data quoted by J. Marcovich, El Nuevo Contexto Mundial, *op.cit.*, p. 96. The spending of the region on S&T corresponds to an expectation of maximum; the author states that, in the region, "no country spends more than 0.7%" of its GDP on S&T.

<sup>35/</sup> ILPES estimates on the basis of data from the World Bank, IDB, ECLAC, OAS, *op.cit.*, and Marcovich, *op.cit.* There are indications that the region's expenditures on S&T fell, as compared to the world, by more than half since 1979, according to 1986 estimates of the National Science Foundation. It should be reiterated that the general observation may not have a similar validity in all countries; in several cases, there are public and private enterprises that maintain an active stance on R&D and participate significantly in foreign trade.

off point for the approval of "profitable projects." Only highly profitable productive projects could absorb the high cost of financing <sup>36/</sup>...in general, those incorporating modern and more efficient technologies. **Four spheres of capital grinding together the opportunities for restructuring and dynamising the economy of the region:** rise in the international interest rate (financial); acceleration of innovations through new and expensive technologies (productive); protectionism and deterioration of the terms of trade (trade); and internal lag in the ownership of the knowledge and in R&D (intellectual capital).

45. The most recent innovations--as already noted--change the international patterns of business competition. The change in comparative advantages pushes toward the production of goods and services "intensive in innovation."<sup>37/</sup> The streamlining of processes, business flexibility, tactical rapprochement between production and market, induction of changes in preferences through communication, and increase in management efficiency are some elements of the new pattern of business leadership. **Innovations undoubtedly open a fan of new opportunities for developing countries, but they also have a more accelerated obsolescence.** In the design of external reinsertion policies, it would be necessary to have special antennas for catching those opportunities, with a sense of urgency. For this purpose, old-fashioned business intuition is not enough; in a world

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<sup>36/</sup> It should be remembered that the nominal rate of interest (LIBOR) grew without interruption since 1975, accelerating from 1978 to 1981; later declined with fluctuations until 1986, when it reached a level similar to ten years before. Very recently, it has been growing discreetly. The real rates, after being negative between 1974-1977, show an evolution approximately similar to nominal rates (except 1984, where it almost matched the maximum of 1982). See ECLAC, La Evolución Económica Reciente..., *op.cit.*

<sup>37/</sup> On the subject it is convenient to see R. Ffrench-Davis, Generación de Ventajas Comparativas y Dinamismo Industrial, UNIDO/ECLAC/The Netherlands, Santiago, Chile, 1987.



of accelerated economic change, this attribute also demands specialised training.

46. At an overall level, the acceleration of technological innovations demands a reformulation of prediction techniques.<sup>38/</sup> The agile innovation of processes, products, organisation, communications, or marketing escalates the degree of indetermination of the future. Uncertainty changes form; the economic processes that permit a prospective calculation based on estocastic regularities lose relative importance; perhaps those processes whose upcoming stages are known may beat it, but not its probabilities of occurrence; undoubtedly, the other phenomena gain weight, those whose possible future states are not even known.<sup>39/</sup> In contemporary development, the space open to human creativity finds a complement in the real world: flexible productive structures, with great innovative potential. This complementarity is not entirely casual: the financing of the production of knowledge was concentrated in those creativities whose sparks could jump more rapidly to production and from there to the market. Parallel to new material goods geared to answering needs and demands, services grow and multiply.

### III.3 LABOUR AND THE INFORMAL SECTOR: TWO CASES OF MEGADIVERSITY

47. The expansion of services in modern society is a subject that moves the discussion from the two previous phenomena--

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<sup>38/</sup> See the different presentations at the First High-Level Colloquium on Planning in Market Economies, organised by ILPES/UNDP, Santiago, Chile, August 1986 (published in Revista de la CEPAL, No. 31, Santiago, Chile, 1987).

<sup>39/</sup> A broad, up-to-date proposal on uncertainty can be found in C. Matus, Política, Planificación y Gobierno, ILPES/PAHO, Washington, D.C., September 1987 (see in particular the chapter, "Teoría Social y Teoría de la Planificación").

more knowledge per product unit and acceleration of innovations--to the third: an "explosion in variety" in the specialisation of labour and informal activities. In fact, although they are two different aspects, the expansion of services is related to both, but in a different way. It is not convenient, however, to force a theorisation that links them. Their joint treatment is based on three reasons: the dynamic of both leads to a broad diversification; the two are essential for understanding contemporary development; and both economic and social aspects are articulated in them.

48. The "increase in services" was understood, until two decades ago, as an increase in the participation in employment or in the domestic product of sectors of construction, transportation, trade, autonomous liberal professions, financial sector, domestic service, attention to social needs, or public administration. Around ten years later, when the first concepts and analyses of the informal sector were coming to the end of their first five-year period, the expression was also applied to the increase in "self-employed" activities, a fact that was explained by the surplus of migration from the countryside without the chance of insertion in the urban labour market.<sup>40/</sup> Today, the same expression includes the impact of the eruption of new technologies on tertiary activity, polarised by the so-called electronic complex <sup>41/</sup> and in whose center is the

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<sup>40/</sup> On an approach of that period, see, for example, PREALC, Sector Informal: Funcionamiento y Políticas, Santiago, Chile, 1981. For a recent view, PREALC, El Sector Informal Quince Años Después, Santiago, Chile, December 1987.

<sup>41/</sup> The well-known conclusion of OECD is that the electronic complex will perform a central role in the industrial development of the next quarter century. For a recent analysis, see ECLAC: La Reestructuración Mundial del Sector de Bienes de Capital y su Proyección en el Decenio de los 90: Políticas Industriales en los Países Desarrollados y en los Países en Desarrollo, March 1989.

process of diffusion of information processing. In Latin America and the Caribbean, tertiarisation must not be reduced to one of these approaches or another; services of a different nature and with rates of expansion that are also distinct coexist, some interlace and together they expand.<sup>42/</sup>

49. Tertiarisation, therefore, affects the megadiversities considered here, but with different qualifications and causalities. Its concept entails broad heterogeneity, since the taxonomy of economic activities includes in services both the scientist who is designing a biochip and the street vendor who sells bubble gum.<sup>43/</sup> Consequently, any globalising theory in this respect is a candidate for the cemetery of megastories.<sup>44/</sup> The reflections branch off from this point.

**a) Proliferation of Labour Specialisations**

50. Cybernetic language helps to define the following aspect: the technological and productive pattern that revolutionises the contemporary economy produces a "multivariation" in the division of labour. The movement is projected in several directions: in manufacturing, in modern primary activities, and, obviously, in the widespread range of services. Just one example on "services to enterprises": at an overall

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<sup>42/</sup> The "increase in services" (measured by their share in total employment) can mean very different processes. Between 1965-1981, in 94 countries with low and low middle income levels, this indicator grew by 23%, the same as in the following 22 countries (of high middle income); in the 27 most developed market countries, it rose by 17%. See A. Uthof and E. Pernia, Una Introducción a la Planificación de los Recursos Humanos en Países en Desarrollo, ILO, Geneva, 1986.

<sup>43/</sup> The biochip (Molecular Electronic Device) will seek to assemble integrated circuits on the basis of organic material; in other words, proteins or enzymes that replace minerals.

<sup>44/</sup> With the permission of J.F. Lyotard, La Condición Premoderna (Madrid: Ed. Categra, 1986).

level, it is warned that the new labour specialisations are spread in the functions of administration, accounting, finances, publicity, marketing, transportation, labour organisation, engineering of installations, R&D, training of human resources, and information systems.<sup>45/</sup> The diffusion of information processing, in turn, generates innumerable new specialisations within each of these functions. The advances in telecommunications, semi-conductors, industrial and office automation, besides the data processing industry, play a triple role in the creation of new specialisations: directly in each of the branches, as well as having an impact on the entire industry of capital goods or, more indirectly, through their diffusion in other industries and services.

51. In the sequence of reasoning being developed, it is interesting to point out some characteristics of the actual multivariation of labour, which are relevant for the phenomenon of social "complexisation" or for business competitiveness. Before, it would be useful to mention that the recent "explosion of specialisations" is not necessarily limited to the productive apparatus of each country, whether developed or not. The flexibility that the new technological and productive pattern propitiates on an international scale opens up new possibilities in developing countries. Although their experiences are not automatically transferible, it is true that the countries of Southeast Asia have taken advantage of those opportunities with greater historical meaning. Latin America and the Caribbean also have some potential advantages. Their active external insertion--based on those opportunities--

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<sup>45/</sup> In this vein, see, for example, P. Escorsa, Servicios a las Empresas y la Promoción de la Competividad: una Perspectiva en el Camino hacia el Mercado Europeo Unico, Círculo de Empresarios, Bulletin 44, Madrid, Fourth Quarter, 1988.

critically depends on the innovative and negotiating capacity of the region's business community, backed by an efficient promotion of the State.

52. From a social viewpoint, it would be convenient to recognise that the generation of industrial labour and service specialisations in high technology spheres broadens the spectrum of heterogeneity.<sup>46/</sup> Increased productivity allows (and demands) high earnings, but also higher wages and salaries and, therefore, the segments of the population linked to the most dynamic sectors tend to push up the profile of the social distribution of income. It seems little realistic to think that competent and active policies of external reinsertion are sufficient for a rapid restructuring of the regional productive base. It is also difficult for the growth of some modern segments to be sufficient for altering expressively the current patterns of inequality.<sup>47/</sup> The countries of this part of the world benefited in a differentiated manner from the previous stages of the world process of industrialisation; it is probable that their differentiation increase again as they modernise. This poses another crucial problem for harmonising public policies among those who advocate a more dynamic external insertion and those who promote social development.

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<sup>46/</sup> As is known, the term refers to the concentration of technological progress in some branches, where the highest productivities are registered. The correlation productivity-wage-family income articulates, in this concept, the technological heterogeneity with disparities in income distribution. There are indications that more than 40% of the increase in productivity is due, in the United States, to the recent advances in high technology (UNIDO, 1986).

<sup>47/</sup> The ECLAC/UNIDO Joint Unit has been analysing exhaustively the relations between industrialisation and equality. See in particular F. Fajnzylber, Industrialización en..., op.cit.

53. On the other hand, the dissemination of the new technological and productive pattern will eventually demand a reorganisation of all public policies related to the labour issue: employment, wages, social security, training of human resources, and right to work. It would be futile to attempt to anticipate the final sign of the changes required. In the asset column, it would be possible to include some beneficial effects of modernisation on social development, among them being: the increased value of specialised labour, the improvement of working conditions, the promotion of human resources, and, of course, wage hikes and the advance toward more participatory schemes in production organisation;<sup>48/</sup> for these reasons, modern business can be transformed into the strategic knot for greater social cohesion.
54. In the liabilities column, the modernisation of industries and services can present a negative balance in terms of the generation of job opportunities,<sup>49/</sup> with the probable displacement of less qualified workers. In addition, the indispensable flexibility of the modern enterprise can result in greater labour instability. Consequently, modernisation introduces factors that hinder even more the formulation of employment policies in the region. Particularly, for those countries with chronic employment problems, since along with the modernisation that Toffler calls the "Third Wave," there are currents of all hues pushing for "deregulation." Labour-related public policies

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<sup>48/</sup> On participation and microenterprise, see V. Cartaya Febres, Nuevas Tecnologías. Microempresas y Capacitación, ILDIS, Work Document, Caracas, 1989. See also E. Conen, et.al., Microempresas y Economía Popular, ILPES/Grupo Esquel/PNM-Guatemala, San Jose, 1989.

<sup>49/</sup> There are convincing indicators that the industrialisation of services is capital-intensive. The heterogeneity of the sector is a stumbling block to reaching clear conclusions on the impact of its expansion in the generation of formal employment.

are also a key ingredient to consider in the global formulation of reinsertion policies; perhaps the most delicate subject on the agenda of the necessary dialogue among enterprises, labour unions, and governments.

**b) Multiplication of the Informal Sector**

55. The other side of this third phenomenon is the multiplication of the informal sector, in a mixture of expansion and greater diversity. Behind it is a situation that dates back three decades: pronounced underutilisation of labour, where underemployment predominates over open unemployment. During the eighties, unemployment grew more than underemployment (more than 8% as compared to a little less than 7% yearly).<sup>50/</sup> Underlying causes of that persistent imbalance, as is known, are some peculiarities of the demographic dynamic (growth rate, structure of age and sex, migrations, and others), which perform different roles in each country. Wage and employment policies are another cause.<sup>51/</sup> Finally, there is a causality that comes directly from investment behaviour, both in its rate of expansion and in the implicit decisions on technology. In this regard, it is worth remembering that technology "is like genetic material--it is codified with the characteristics of the society that developed it--and tries to reproduce it."<sup>52/</sup> One of the old consensus of the analysis of development is that the relative availability of factors has been different among today's advanced countries, generators of

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<sup>50/</sup> E. Klein, El Sector Informal en América Latina, PREALC/ILO, Quito, April 1987. On the other hand, PREALC estimates that from 1980 to 1985 non-agricultural employment grew by 17%, while the informal sector, by 39% (see PREALC, El Sector Informal Quince Años...op.cit.).

<sup>51/</sup> In this case, as long as the concept of wage as a "production cost" is favoured over its concept as a "component of aggregate demand."

<sup>52/</sup> B. Wambi, Una Visión sobre la Transferencia de Tecnología y la Información, CIID, Brazaville, Congo, January 1988.

technological novelties, and those countries with a greater relative lag.

56. On the other hand, the bulk of informality is explained by the accelerated process of urbanisation. According to recent projections, between 1980 and the year 2000, the work force located in cities will double, from 74 to 148 million inhabitants. "Under the current conditions, it would be virtually impossible for the majority of the countries to be able to maintain the rate of growth and levels of income and employment that are needed to absorb this high number of workers in the formal sector. The activities of the informal sector will continue to be the only source of income for many inhabitants of these growing cities."<sup>53/</sup>
57. The policy toward the informal sector fluctuates from preventing urban violence (to offer greater attention to destimulating delinquency) to fostering microproducer initiatives.<sup>54/</sup> Informal labour as a percentage of the economically active population varies in the region from nearly 30% to slightly less than 60%, according to the different national situations. In the face of this magnitude, it is difficult to fall back on only one type of corrective policy; it is more probable that it be necessary to combine, in each case, very diverse proposals. The specific subject of the policies of the informal sector goes beyond this document, but it is convenient to stress the perception that there will be no exclusive successes. The

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<sup>53/</sup> Se IDB, La Problemática de la Informalidad, Washington, August 1988, p. 2. On the experiences with enterprises of the social sector, see SPP, Desarrollo Equitativo y Fortalecimiento del Sector Social de la Economía, SPP/STM/ILO, Mexico, May 1988.

<sup>54/</sup> A successful experience with microenterprises is presented in F. Barca, The Developments of Italian Microproducers Theory and Empirical Evidence, Seminar on Assistance to Microproducers in Latin America, IDB, Washington, February 1989.



intensive adoption of assistance policies is impossible, as the situation of the public sector will continue to be feeble in the near future (see Chapter V); and it is unlikely that programmes based on the development of business capacity have massive success. In fact, if the Schumpeterian talent is already concentrated among all those who possess capital, it will hardly be homogeneous among those who only have their labour force as a unit of production.

58. Up to this point, the references favoured the subject of the growth of the informal sector. There is clear evidence that this is also diversified. Growth and diversification introduce greater heterogeneity in the labour market, of which the informal markets also are a part. This diversification takes place within the informal sector and, in addition, in its direct and indirect relations with the formal economy. For the purposes of this document, two final comments could be added. First, that conscious policies of external reinsercion tend to change the internal structure of relative prices in favour of "tradable goods and services," for which, in the rear, the prices that dominate the consumption pattern of the informal sector are prejudiced. This could seem to be a detail for creating a compatibility between external and domestic policies, but this is not so when considering the relative weight of the informal population. Second, and finally, that the new productive pattern, native of the advanced world, will necessarily push developing countries toward adopting their own "blend" of technologies, with different degrees of progress. The result aims at growth without employment, even for the experience of the developed nations

themselves.<sup>55/</sup> As observed, today knowledge dominates production and innovations head up the markets. In this framework, there is an additional risk for Latin America and the Caribbean: on the basis of their social pyramid, growth without employment is accumulating the less trained citizens as if they were superfluous.

III.4 CONTEMPORARY SOCIETY:  
A DIFFERENT COMPLEXITY

59. Up to this point, three accelerations that interact in the contemporary economic dynamic have been stressed: more inputs of information per product unit; more innovations in processes, products, organisation, and market, and more dispersion in the modalities of labour. All of this alters the "useful" combinations of available production factors; today the labour factor (particularly the less qualified) loses relative standing in this framework of new technologies. This way--but not just this way--, considerable numbers of the population are displaced toward the informal sector; in the last analysis, the area of work for individuals who do not have a job.
60. Everything fits within this process of fractioning; upwards and downwards, the heterogeneity of labour is expanded and, consequently, that of wages and family income. The modern social structure is broken up and scattered in the most diverse articulations with the distinct activities of the classic economic cycle: production, distribution,

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<sup>55/</sup> For a view of the most current employment trends in developed countries, see OECD, *Economic Outlook*, Paris, December 1988. With respect to economic projections in those countries, see A. Guardia, *Orientaciones Metodológicas sobre el Análisis de las Previsiones de la Economía Internacional*, ILPES, Santiago, Chile, May 1988.

consumption, and appropriation of benefits.<sup>56/</sup> This is one of the ingredients of complexity, an unmistakable earmark of today's society. Nevertheless, so that it is really unmistakable, it would be useful to briefly digress in order to standardise the understanding of this key word: complexity.

61. In fact, the proposal can be reduced to six blocs of considerations:<sup>57/</sup>

One, "complexity is a typographical expression that describes a series of new perceptions and scientific representations of reality; it is considered to be an "open entity" and constant mutation, characterised by instability, disorder, and creativity;

Two, dynamic systems--even the social ones--are more unstable than previously recognised; their trajectories have a basic property of "divergence"; or rather there is statistical uncertainty at the very heart of any dynamic system;

Three, an increasingly more complex society and the computerisation of information and decisions has been produced, it is the last link in this process; it adds a memory and logic of its own, which, little by little, will expand its power over our situations; therefore, a new understanding of this "factory of trajectories" which is current reality is necessary and it implies a major cultural transformation;

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<sup>56/</sup> In this fractioning everything fits, from the most redeeming scientific or technological novelty to the most pernicious production and trade. What is registered and not registered also is scattered, upwards and downwards, generating employment and income.

<sup>57/</sup> Each of the first five considerations sums up, almost literally, the stands of world authorities on the subject of complexity. In the same order mentioned: Edward Ploman, Ilya Prigogine, Torsten Hagerstrand, Orio Giarini, and Crawford Holling (see UNU, The Science and Praxis of Complexity, Tokyo, 1985). Since 1986, ILPES has produced more than a dozen applied research works, establishing a relationship among complexity, planning, coordination of public policies, and management. See the annual reports of CRP and, particularly, the publications produced between 1987 and 1988.

Four, the specialisation and expansion of markets stimulate the development of the most complex social system, both vertically and horizontally: vertically, when complexity refers to the multiplication of the stages of transforming raw materials into a finished product; and horizontally, with respect to all service activities that accompany and support production activity;

Five, at the same time, the complexity of every system depends on the view of those observing it; however, detailed explanation is not equivalent to the understanding of the complex phenomenon; besides, this is incompatible with reductionism (which seeks to understand about the basis of analysing the parts of each whole);

Six, "while real economic activity has gone from simple to complex during the last two centuries, economic thinking has followed an inverse process."<sup>58/</sup>

62. In Latin America and the Caribbean, there is no national society free of the attributes of complexity, along the lines of the ideas outlined above. Its nature as an "open entity" can be interpreted in different ways. Of course, the breaking up of the occupational structure is accompanied by a broader spectrum in income distribution, values, and social expectations, which enhances unpredictability in the behaviour of the different actors. In the external space, an intensification in interdependence is being witnessed, a core phenomenon in the conception and design of new

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<sup>58/</sup> Words of Orio Giarini of the International Association for the Study of the Economy of Insurance, Geneva (UNU, The Science and..., *op.cit.*). Steindl agrees with it: "Typically modern economics unfurls great subtlety in the conclusion of the formal apparatus, along with the shocking neglect of our society and its problems," and further on, "General economists have shown little interest in economic realities; this is less true of specialists (currency, trade, etc.) who are dedicated extensively to the problems of today's economic policy. The problem is only that their specialisation tends to narrow their horizons..." (J. Steindl, "Reflexiones sobre el Estado Actual de la Economía," BNL, Quarterly Review, No. 148, Rome, March 1984.

reinsertion policies.<sup>59/</sup> In terms of time, the nature of "open entity" is intelligible as a greater indetermination of the future. In several senses, the societal complexity of the region combines different elements: coexistence of multiorganisations (of their own actors); growing interdependence (with external actors); and an essential vulnerability. The latter is true in both the actual dynamic of the region and, especially, its projection to the future.

63. Vulnerability and uncertainty, those two unseparable attributes of a complex developing society, demand the vigilance and protection of some internal balances.<sup>60/</sup> At the level of inequality existing in Latin America and the Caribbean, those imbalances cannot depend exclusively on the market;<sup>61/</sup> nor are they able to come from rigid exercises of intertemporal planning.<sup>62/</sup> Complexity decreases the effectiveness of all partial balances; on the other hand, uncertainty terminates nearly any normative effort to discipline the future. From the standpoint of development, the need for new planning is weakening among these facts. The recent history of adjustment policies was a succession of tentative partial balances; largely produced through the trial-and-error method. Social pacts, normally

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<sup>59/</sup> See J. Villamil, El Rol Creciente del Sector Privado en el Desarrollo Actual de América Latina y las Implicaciones para la Planificación, Universidad de Puerto Rico, August 1988.

<sup>60/</sup> The usual emphasis is placed on the external imbalances; however, the internal imbalances magnify their weight in the agenda of concerns of some governments of the region. See C. Massad and R. Zahler, Deuda Interna y Estabilidad Financiera, RIAL, Santiago, Chile, 1989 (especially the chapter, "Es la Deuda Interna un Problema?").

<sup>61/</sup> It is recommended to see "Precios Sociales y Precios de Mercado," in R. Ffrench-Davis, Generación de Ventajas..., *op.cit.*; above all, due to the interest in the subject of external reinsertion.

<sup>62/</sup> See the section, "Decidir y Actuar en una Sociedad Postmoderna," in C. de Mattos, Desarrollos Recientes sobre el Concepto y la Práctica de la Planificación en América Latina, ILPES, Santiago, Chile, August 1988.

indispensable, are another type of partial balance. The transitory state of one or another is explained by the accelerated economic change and the progressive intensification of complexity. In this aspect, the major challenge is that there is no room for a general balance either; the real facts dissipate it...63/

64. Another nutrient of complexity--of the greatest importance for the central topics of this document--is, undoubtedly, interdependence; there is a consensus among specialists that it generates or enhances complexity and vulnerability. "In the process of interdependence we have all been vulnerable. Our societies are sensitive to the decisions that are made in any other part of the world. The dynamic of interdependence could be understood better if we thought of earth not as a map of nations, but as a meteorological map..."64/ **Vulnerability emerges as a sort of fingerprint of the complex phenomenon, all similar but each being very specific.** In the concept used here, external insertion is almost an equivalent of interdependence; from this perspective, reinsertion policies are a special case in the management of modern complexity.

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63/ See again the first consideration on complexity, owed to Edward Ploman (see paragraph 61, item one).

64/ See Soedjatmoko, former rector of the United Nations University, Tokyo, in J. Lesourne, Gobernabilidad de un Mundo en Transición, Rome Club, Santander/Spain, 1985. The comparison with the meteorological map is justified... "where the systems act independently of national borders and high and low fronts create new climatic conditions very much ahead of them," concludes Soedjatmoko.

## III.5 INSTITUTIONS AND CRISIS OF GOVERNABILITY

65. New productive function of knowledge, innovation as a nucleus of production and trade strategies, the proliferation of formal and informal labour, increase in the structural and interactive complexity of modern society are the four issues covered up to this point for a more integrated understanding of contemporary development. The road reaches its end: two economic phenomena generated the third, this one articulates economy and society, whose complexity simultaneously challenges its own regulatory institutions. In this respect, a premise summed up in three propositions is clearly posed:

First the vulnerability of the current situation reduces its goverability,<sup>65/</sup>

Second accelerated economic and social change reduce the ability of government,<sup>66/</sup>

Corollary the gap grows--in this very moment--between need for government and ability to govern.

66. This gap is observed not only in modern States, but also in any major social organisation that becomes a complex system. Likewise, the gap grows when the problems of the system are handled without full consideration for their complexity, for example:

- address each symptom separately, aggravating others;
- seek solutions that are short-term and at points where intervention is not effective on the medium and long run; or

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<sup>65/</sup> Accompanying the argument of J. Saint-Geours; this term is used as a "state or quality of being governable." See in J. Lesourne, Gobernabilidad y.... op.cit.

<sup>66/</sup> On the ability to govern, see the many works of I. Dror; especially his presentation at ILPES, Coloquio Internacional sobre Nuevas Orientaciones para la Planificación en Economías de Mercado, op.cit., and the comment by A. Gurrieri (internal document), ILPES, Santiago, Chile, August 1986.

- invent solutions based on the static analysis of the problems (see note 70).

67. The reduction of governability of a developing society is explained by innumerable elements, among which can be mentioned:

- the fractioning of the social structure, which means an extreme differentiation of aspirations;67/
- disparities in "timing" in social expectations;
- innovations concentrate power and, therefore, social heterogeneity is expanded also from this point of view;
- the segments with the greatest intention of ownership multiply, without one or the other emerging in condition to exercise it hegemonically;
- possible options lose transparency with the increase in uncertainty;68/
- the necessary "control" can thus lose social legitimacy;
- communication shortens the transmission time of messages and can detonate inopportune social reactions;
- differences in culture and interests among social strata of distinct age groups deepen;
- the innovative posture collides with the inertia throughout each society; and
- teletransmitted information flows transcend national borders.

68. The reduction in the ability to govern could be engraved in the very complexity of today's world: the loss of

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67/ "In a system where one of the main traits is a strong differentiation between privileged and neglected, the social conflict--always present in a society--acquires special characteristics." A. Touraine, quoted in ECLAC, Equidad, Transformación Social y Democracia en América Latina, ECLAC Social Division, Santiago, Chile, December 1988.

68/ See the speech at the Opening Session of the XVI Interamerican Congress on Planning of F. Agrait, President of the Graduate School, Universidad de Puerto Rico, San Juan, August 1988.



effectiveness is a potential risk for the management of major complex social organisations, including the State.<sup>69/</sup> Thus, there are serious difficulties beyond those already mentioned:

- the information available on the society is increasingly more insufficient--in quantity and quality--with respect to the need to make adequate decisions;
- intuition--an essential attribute of the politician--also staggers in a world of accelerated changes;
- production factors have changed their potential;
- among them, financial capital has acquired a barely containable mobility in a framework of national economies;
- moreover, inside and outside of national borders, the financial aspect has acquired greater relative autonomy vis-a-vis trade and productive aspects;
- externally, the heterogeneity among the countries makes its specific areas of interest in the international space more incongruent;
- this is all coupled with the new strategic role of intellectual capital, whose production is undergoing a subtle articulation of scientific communities, universities, armed forces, private enterprises, governments, and other non-governmental entities.

69. "People see themselves as being more distant from their government, which they distrust due to its size, complexity, and technocratic nature. This lack of satisfaction is partially rooted in the perception of less effectiveness in government management...The vicious circle may be

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<sup>69/</sup> "...the many Nation-States have succeeded in prevailing owing to the ability to develop their original aspects with regard to each culture. The field of human experience has been growing as a consequence and adaptable political systems have arisen, which have made it possible to govern increasingly more complex societies, although with minimal effectiveness. But, perhaps the moment has come in which the challenges with which the international system is confronted are such that the problem of governability has become profoundly altered," in J. Lesourne, *Governabilidad y...op.cit.*, p. 31.

broken...freedom is lost, which is exchanged for the attempt to manage the system, characterised by inevitability, vulnerability, and lack of certainty and ability to make predictions...(then) freedom is sacrificed for the sake of effectiveness."<sup>70/</sup> However, "Complexity cannot be managed either intellectually or practically with greater control."<sup>71/</sup>

70. The conclusion is that the insidious circulation of ineffectiveness expands. Perhaps, one of the few products whose modern mobility can compete with that of financial capital... Also, it is a product whose internal circuit has some interdependencies with the external circuit; with the difference that, in the international setting, there are various focal points of effectiveness that grasp the new technological pattern, push modernity, and accelerate history. Reinsertion policies cannot ignore the true availability in matters of ability to govern. There are strong indications that this is decreasing because ingovernability consumes it from beneath and management inefficiencies erode it from above.

71. However, increased ability to govern is not achieved solely with more power. The multiplication of social agents also generates greater interdependence among their conflicts. The current trend toward the consolidation of political regimes that opens up space to social participation is accompanied by a greater struggle among diverse social actors; consequently, pressure from many sides for "margins

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<sup>70/</sup> Transcription of the words of Canadian mathematician and senator, Michael Kirbi, taken from his work, "Complexity, Democracy, and Governance" in *UNU, The Science and...*, *op.cit.* Kirbi refers here to a general evaluation of governmental activity during the contemporary period: his concepts do not refer to any government of this region in particular.

<sup>71/</sup> See Soedjatmoko, quoted in *UNU, "El Hilo del Laberinto: La Gerencia de la Complejidad," UNU Newsletter, Tokyo, Vol. 8, No. 3, June 1985.*

of preference" in the allocation of public resources and the implementation of domestic policies converge on governments. Another challenge is to promote growing levels of consensus and cooperation in order to push a new development, in the face of a greater expanse of social tensions.

72. As a corollary to the complexity of today's society and the growing difficulties in the government conditions already mentioned, there is a task that ILPES designated before as "...change the energies freed from pressures of demands into forces of social cohesion."<sup>72/</sup> Governments find themselves faced with the challenge of assuming a creative role, conceiving new instruments for action that consider social needs not only because of their aspect of "deficiency," but also due to their positive side; to permit a channeling of new social energies with a significant self-management potential. Freed from the exclusion caused by the type of development and encouraged by the advent of more open political regimes, it is natural that those energies--aggravated by the sacrifices imposed by the current crisis--explode into a sequence of reclamatory actions. In general, governments lack the necessary resources for adequately handling this avalanche of claims, within the framework of traditional social policy mechanisms. Thus, the need arises to conciliate cooperation and social participation with public instrumental creativity for the broader pursuit of satisfying social needs.
73. This requires the promotion of new concepts of organisation and means assigning the direct beneficiaries a leading role in meeting their own needs, minimising direct government assistance. The fiscal austerity that will prevail in

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<sup>72/</sup> See ILPES, Cooperación e Integración Regional en la Reactivación y en el Desarrollo: El Papel de la Planificación, *op.cit.*

coming years acquires greater meaning. Moreover, that approach may be essential for offsetting the increased concentration and exclusion, probably resulting from the economic dynamic generated by the new external reinsertion projects.

## Chapter IV

**DETERMINANTS OF BETTER REINSERTION:  
COMPETITIVENESS AND PRODUCTIVITY**

74. It is time to resume the theme of the document. The heterogeneity of the region has been mentioned (Chapter I), that the eighties have been problematic and, from the standpoint of preparation for the future, almost lost. It has been shown (Chapter II) that the region relinquished trade positions, had to make net transfers of resources abroad, and lost decision-making ability in multilateral settings. Finally (Chapter III), an examination was made of situations, trends, and challenges related to five characteristics of the new world development (knowledge-intensive technologies, acceleration of innovations, diversification of formal and informal labour structures, "complexisation" of the society, and crisis of governability). At this point, eyes will continue to look to the future, but will cross over two very concrete processes of more immediate perception: to generate external competitiveness and to sustain it on the basis of a real boost in productivity.
75. Innovative impetus, creativity, ability to assume risks, awareness of trends in their sphere of activity, flexibility and decision-making agility, trade aggressiveness, and organisational efficiency are some of the vital attributes for propitiating leaps in competitiveness in the future. In general lines, the type of ownership of productive assets (public or private) cannot be considered "per se" an impediment so that those leaps take place. Economic history teaches--leaving aside the doctrines--that many public enterprises have performed this role completely, attaining outstanding positions in the international market. Some of the enterprises of the region that are public jeopardize--

due to their external presence--the hegemony of industrialised countries in the world market, understood by some as their "hunting ground." However, in the real situation of today, the private enterprise is the most generalised asset capable of being mobilised and promoted within the framework of deliberate external reinsertion policies.

76. This certainly does not resolve the most serious social problems that affect Latin America and the Caribbean. But there are two facts, which are hardly of the same liking to everyone's taste: one, it cannot be expected that the private initiative of the region deservedly win over markets under the current conditions of international competition and that, at the same time, it contributes significantly to correcting the accumulated problems of employment and social distribution of income.<sup>73/</sup> Two, it is a lack of realism--with a high degree of purity--to imagine that the region will attain a dynamic and sustainable position in the world economy of the future on the basis of governmental Schumpeterianism or a massive reproduction of efficient public enterprises. The present chapter will stress this fundamental condition for deliberate reinsertion policies: improved competitiveness and greater productivity.

#### IV.A. COMPETITIVENESS AND EXTERNAL INSERTION

77. As is known, an effective productive insertion in the international economy means, from a theoretical and general viewpoint, the need to generate export surpluses, especially

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<sup>73/</sup> The magnitude of these problems and the possible dynamic of the increase in productivity and its distribution restrict the possibility that private enterprise make decisive contributions in both senses. However, the lack of long-term viability of modalities of external insertion based on the intensification of those social problems should be noted.

in response to the problem posed by the payment of the foreign debt. This need will continue, even if a final agreement is reached between debtor countries and the banks and creditor countries to transform the actual liabilities into long-term obligations with real interest rates lower than the present ones. It also demands the introduction of more rationality in the use of resources and, particularly, the promotion and diversification of exports and greater efficiency and effectiveness in import substitution.<sup>74/</sup> These proposals demand changes in domestic macroeconomic and sectoral policies and, obviously, are benefited by decided actions by the region in international forums, when they are able to reduce the protectionist measures of the major importing countries.

#### IV.A.1 SPECIALISATION AND COMPETITIVENESS

78. The debate on the development of the region in the eighties has been largely centered on the export orientation of the policies and the quality of international specialisation. This debate tends to take in the critical balance of the experiences of import substitution in the region, the export success of the economies of Southeast Asia, and their active promotion by multilateral financing agencies. Nevertheless, the foreign debt has caused exports to be favoured due to the critical demand for the foreign exchange needed to service it. Those years, the exporter had a special power to influence policymaking: he sold a scarce good, foreign currency.

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<sup>74/</sup> ILPES has a work on dynamic comparative advantages criteria and public policy coordination underway (see Project UNDP/ILPES RLA/86/029). In addition, the institute has an extensive bibliographic registry on comparative advantages that includes thousands of titles, from books, articles, and dissertations (the latter being post-1982). Public or private organisms of member countries can use these registries. Programmed with Soft Ask-Sam, the access is by author or key words related to the subject.

79. This was clear at the beginning of the decade. At mid-decade, the need for a selective and progressive increase in the level of the region's competitiveness in the world market was being suggested, recommending several measures in this regard: enhance the capacity of the private businessman and the government in the productive and commercial management of the export sector, strengthen the trade among developing countries, and also take advantage of the potential of the regional market. On the other hand, the conviction was growing that the basic products export-manufactures export dichotomy does not entirely reflect available options. Thus, the concern for designing new export strategies that combined activities of two or more productive sectors (mining, agriculture, industry, and services) was gradually expanding. While the need to save foreign exchange stimulated measures to substitute imports, the need not to pit those measures against ones fostering exports was also gaining a consensus.<sup>75/</sup> However, the external constraint was the dominating element: in late 1988, after seven years of adjustment and debt restructurings, imports reached only three-fourths of the level recorded in 1981. In the same period, the region has transferred resources overseas in an amount equivalent to nearly one third its total imports.<sup>76/</sup>

80. The recent trade trend shows a heterogeneous behaviour of tradable products on international markets. Manufactures

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<sup>75/</sup> See ILPES, Summary: Planificación y Políticas Públicas en 1982-1984 y Perspectivas para la Segunda Mitad de la Década. ILPES, Santiago, Chile, March 1985. Next, this chapter is supported in O. Rosales, Competitividad, Productividad y Posibilidades de Reinserción, ILPES, Santiago, Chile, 1989.

<sup>76/</sup> See ECLAC-SELA, Bases para una Respuesta de América Latina a la Crisis Económica Internacional, 1983; in addition, Group of Eight, Compromiso de Acapulco para la Paz, el Desarrollo y la Democracia, Mexico, 1987.



stand out as the motor of world trade, doubling and, at times, tripling crop-farming and mining trade, thus accentuating the trend that began in the sixties.<sup>77/</sup> This differentiated dynamism is also reflected in prices.<sup>78/</sup> Between 1982 and 1987, the value of world exports grew at an yearly average of 6.1%; no economy in the region surpassed that average. In the region, the value of exports rose at an annual average of 1.7%, equivalent to less than one third of the corresponding world value.

81. In the 1984-1988 period, during which foreign trade rallied slightly, the region exported 100 in volume in order to receive 74 in value, while industrial countries exported 100 and received 124.<sup>79/</sup> It seems clear that there is a need to incorporate greater value added into exports and intensify the linkage among industry, technology, and exports. Despite some outstanding breakthroughs, the challenge continues to be to improve the quality of international specialisation, seeking a better insertion in the most dynamic areas of international trade.
82. Moving toward specialisation is one of the necessary directions for increasing competitiveness. This tends to be

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<sup>77/</sup> In 1987, the volume of trade of manufactures was 37% higher than in 1980, crop-farming products increased by 12%, and mining dropped by 7%. Among manufactures, electronic products were the most dynamic, since they nearly doubled their share between 1980 and 1987; in contrast, other products backslid or stagnated; thus, for example, in 1973-1986, international trade of crop-farming raw materials decreased by 4.8%, food products by 4.6%, and iron and steel by 3%. See GATT, International Trade 1986-1987, Geneva, Switzerland, 1987.

<sup>78/</sup> While in 1987 the unit value indicator of manufactures grew by 14.1% as compared to 1980, that of crop-farming products remained stagnant, and that of mineral products fell by 31%. See GATT, International Trade 1977-1978, op.cit.

<sup>79/</sup> See ECLAC, Preliminary Overview of the Latin American Economy 1988, op.cit.

defined as the ability of a country to balance its trade and improve its share in international markets, but simultaneously raising the standard of living of its population.<sup>80/</sup> In this regard, the decade of the eighties is lavish in different types of examples: Japan and the NICs have shown that it is possible to obtain a significant trade surplus and, simultaneously, improve the well-being of the population; the United States has succeeded in increasing well-being through a high trade deficit. Latin America and the Caribbean, on the contrary, drove up the trade surplus at the cost of a greater deterioration in the standard of living of their inhabitants.

#### IV.A.2 THE NEED FOR AUTHENTIC COMPETITIVENESS

83. This decade has been marked by the trade and financial imbalances of the industrialised world, with its aftermath of impacts on interest rates and exchange rates.<sup>81/</sup> In this sense, a relative dissociation between competitiveness and comparative advantages has taken place, since exchange rate movements have affected competitiveness exogenously, depending on the sale markets of the products. The very instability of the exchange rate impedes the identification of relative advantages; in several cases, the system of incentives was biased against non-traditional exports and local companies with fewer resources and ability to manage exchange rate risks. As a response to those fluctuations, the region has concentrated a good part of its exports on

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<sup>80/</sup> See USA, "President's Commission on Industrial Competitiveness," Global Competition: The New Reality (Washington, D.C.: U.S. Government Printing Office, 1985).

<sup>81/</sup> On developed countries, see SELA, op.cit.

only one developed zone, increasing the potential risk of protectionist measures.<sup>82/</sup>

84. As is known, it is possible to differentiate a competitiveness/price--which relates the elements quality and prices on the short run--from long-term competitiveness with a structural base. The latter, without neglecting those elements, directs more attention to the expected development of world demand, the ownership of information and research on applied technology, and technological development. Undoubtedly, competitiveness/price is relevant on competitive markets and markets with little product differentiation; nonetheless, in an international context characterised by technological and product innovation, a country can impose prices only if the quality, technological level, and demand for its products so justifies; in other words, if it has structural competitiveness. In the latter case, competitiveness implies economic organisation and articulation of the productive base, elements of marketing, industrial policies with support of productive chains, and long-term business strategies. At the public level, it requires making credit, labour, tariff, and exchange rate policies compatible.

85. "The initial expansion of the domestic market into an increasingly wider range of goods and services associated with growth is the irreplaceable basis of industrial-technological learning, a necessary condition for growing competitive insertion. This "virtuous circle" of growth and competitiveness--in which the requirements of equity, austerity, and technological learning are frequently

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<sup>82/</sup> Practically two thirds of the value exported by the region in 1986 was destined to developed countries; of this subtotal, the EEC absorbed 29%, Japan, 6.5%, while a little more than 60% was exported to North America (United States and Canada). See CLEPI, *El Desafío...*, *op.cit.*

omitted--is one of the central axis of the successful experiences of industrialisation."<sup>83/</sup> External trade insertion arises, then, as a selective instance that provides an opportune signal of the new technoeconomic paradigm, with greater intensity of information and knowledge, more flexible production forms, smaller-sized plants, interweaving of industry and services, shortening of the product cycle, and awards for innovation. The challenge of public policies in this area is to design a framework that, considering the country's specific advantages in resources and technology, promotes the expansion of national companies in production and marketing, accompanying the process with an active role of technological development and international negotiations.

86. On the short run, it is possible to obtain transitory trade advantages, appealing to protection and export subsidy policies, as well as the discretionary management of wages and relative prices that stimulate exports. However, in the absence of productivity boosts and an effective reallocation of investment to tradable production and the consumption of non-tradable goods, their greatest effects can be limited to a transfer of profits to export sectors.<sup>84/</sup> Appealing excessively to protection and subsidy systems is limited in time and imposes a cost of the growing opportunity on

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<sup>83/</sup> See ECLAC, Restricciones al Desarrollo sostenido en América Latina y el Caribe y Requisitos para su Superación, Santiago, Chile, February 1988.

<sup>84/</sup> An approach favouring basic goods production in combination with an external insertion policy is provided by A. Nuñez del Prado, Economías de Viabilidad Dificil: Una Opción por Examinar, ILPES, Santiago, 1988.

consumers and also on real wages <sup>85/</sup> and fiscal capacity. On the other hand, in an increasingly more globalised and interdependent world economy, those instruments tend to erode the capacity to penetrate and consolidate markets.

87. Furthermore, the advantages of wage costs and natural resources have a declining influence on the strategic capacity of international specialisation.<sup>86/</sup> The key resides in a larger hike in productivity, a variable that is coupled with technology, innovation in designs and products, and the quality of production combined with active marketing management. In modern products with greater commercial dynamism, wage costs tend not to exceed 15% of total cost.<sup>87/</sup>

88. The current trade struggle favours competitiveness through innovation, economies of distance, and quality of business management. For this reason, the consensus on the existence of solid ties between productivity and authentic competitiveness is expanded. In this perspective, the technological lag of the region is grave. The export effort

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<sup>85/</sup> Remember the changes in relative advantages in current development already mentioned. Pronounced changes in productivity even exist among industrialised countries. In the 1970-1986 period, Japan's growth in manufacturing wages measured in dollars doubled that of the United States, the same occurred, although in a smaller proportion, with France and Germany. See USA, Department of Labor, Output per Hour, Hourly Compensation and Unit Labor Costs in Manufacturing, Twelve Countries, 1950-1986, Bureau of Labor Statistics, Office of Productivity and Technology, Washington, D.C., December 1987. Parallel to this, Japan and West Germany have improved their competitive standing in manufactures as compared to the United States. See GATT, International Trade - 1987-1988, Vol. 2, Geneva, 1988.

<sup>86/</sup> Especially due to present trends in the use of neo-protectionist mechanisms: countervailing duties, anti-dumping laws, norms of quality, seasonal restrictions, market disruption clauses, deformation of criteria on reciprocity, and increase in the guideline of graduation. See O. Rosales, op.cit.

<sup>87/</sup> See P. Drucker, The Frontiers of Management, Truman Talley Books/Times Books, 1986.

should not consider exclusively the actual supply of resources and existing productive capacity. Taking advantage of new export opportunities requires a simultaneous concern for industrial policy, investment, financing, and technological development. Above all, because, as is known, true competitiveness is linked to the growth of productivity on the medium run and, therefore, policies that promote savings, investment, and its improved allocation.

89. A strategic approach of specialisation is facilitated by the competent selection of products or integrated production complexes on the basis of criteria of adaptation to world demand. Also, due to the adoption of explicit supply-side policies that generate dynamic comparative advantages, detecting productive chains ranging from primary exploitation to services and bolstering them with social and regional decentralisation policies and labour education and training. Basically, the idea is to **enhance the leverage by means of the potential specificities of national economies and their adaptation to a changing world demand.**

#### IV.A.3 ENGINEERING OF NEGOTIATIONS AND MARKETS

90. The possibility of competitive reinsertion can be strengthened if an active process of internal articulation and international negotiation intervenes that generates economies of complementarity between public and private practice. The public sector--besides eliminating selectively anti-export obstacles and adequately managing the basic balances--can support through the use of its external negotiating capacity both exports and the efficient substitution of imports.

91. The **successful lessons of some developing countries** show relevant results from the articulation between enterprises and the State:<sup>88/</sup>

- a) **Conquest of external markets:** through the evaluation of export capacity, studies of exportable supply, identification of potential markets and export promotionservices, including technical and financial assistance. In these areas, the trade missions and a reorientation of diplomacy have produced good results.
- b) **Internal coordination:** in reference to the integration of public and private investment programmes, coordination of small and medium producers and their incorporation into the export endeavour, coordination of the productive apparatus with the national technological system and the financial system, particularly based on development banking.
- c) **Development and coordination of information and applied technology:** through market studies, new product development, international market trends, adaptation of technologies and examination of main trade and technological trends.
- d) **Basic support infrastructure:** in transportation, ports, communications, and export services.
- e) **Negotiation and treatment with foreign investment:** technological agreements and performance criteria for foreign capital.
- f) **Active international diplomacy:** which articulates national and regional negotiating power through a technification of functionary activities linked to the subjects of trade and international negotiations.

92. In any event, this series of measures escapes a short-term view. It provides interesting clues for an institutional coordination that closens the ties among industry, technology, and foreign trade and that gives content to the cooperation of social actors with regard to productive specialisation. Likewise, these national agreements will

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<sup>88/</sup> See UNCTAD/GATT, Los sistemas institucionales de promoción de exportaciones en América Latina, Document No. 3, International Trade Center, Geneva, Switzerland, 1984.

specialisation. Likewise, these national agreements will make more promissory the possibility of conceiving regional integration as a process that facilitates the penetration of international markets, pushing joint and complementary projects of specialisation and productive modernisation.

93. In the framework of active reinsertion policies, a **collaborating role--potentially significant--of intraregional cooperation** can be expected. The weakening of the multilateral trade system (even GATT, its regulatory organ) has affected the region in a differentiated manner. Conversely, the rally of bilateralism and protectionism, managed trade, the deterioration of the terms of trade and the threats and actions for forcing concessions have affected different countries of the region, stimulating important convergences in the intraregional dialogue. However, those consensus were not sufficient to significantly recuperate the power lost in international forums. On the other hand, a similar occurrence has taken place in the area of the foreign debt: true heterogeneous advances have only been achieved on a basis of "case-by-case" negotiations. Realism imposes prudence, when trying to suggest greater intraregional cooperation in a field, whose perception is even less immediate and more complex than the crude realities of trade and the debt: that of coordination in order to collectively gain more external competitiveness.<sup>89/</sup>

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<sup>89/</sup> In that direction, there are new conceptual developments that warrant attention. See, for example, C. Massad, Integración: Una Nueva Estrategia, *op.cit.*, and F. Peña, Concertación Latinoamericana: Arquitectura de Integración e Ingeniería de Negocios, IDB, Washington, August 1988.



#### IV. B. INCREASE IN PRODUCTIVITY: KEY TO REINSERTION

94. Compared to world trends, productivity in the region seems melancholic. For the 1950-1980 period, annual average labour productivity grew by more than 4% only in one country; it was higher than 3% in the following three; fell between 3% and 2% in seven cases; and finally was lower than 2% in eight countries. Likewise, in eleven of nineteen countries, this indicator is the sign of a regression with respect to the seventies.<sup>90/</sup> As for OECD countries, there are long periods (over a decade) where the annual growth of productivity in manufacturing exceeded 10% (Japan), 7% (Italy and Holland), or 6% (Belgium and France).<sup>91/</sup> Comparable figures for some economies of Southeast Asia indicate annual increases in manufacturing productivity of over 7%.<sup>92/</sup> These productivity differentials sustain the overall diagnosis of the productive apparatus of the region: listless and ailing.

##### IV. B. 1. BROADENED RANGE OF TECHNOLOGICAL HETEROGENEITY

95. The evolution of the trade balance of the balance of payments in nearly three decades reveals a manufacturing sector with a deficit in foreign exchange, financed by the surplus generated in basic exports. At the same time, it shows the progressive drop in the basic export surplus and a cutback in the net demand for foreign exchange by

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<sup>90/</sup> Prepared on the basis of data from the Economic Projections Center, ECLAC (Internal Work Report), Santiago, Chile, 1989.

<sup>91/</sup> See L. Klein, "Components of Competitiveness," *Science*, Washington, July 1988.

<sup>92/</sup> The figures for the 1975-1979 period are: South Korea, 7.9%; Hong Kong, 9.6%; and Taiwan, 7.1%. See U.N., Statistical Yearbook for Asia and the Pacific, New York, 1985.

manufactures.<sup>93/</sup> More recent data even indicates a reversal of the manufacturing deficit for the region as a whole; however, the average data hides a marked heterogeneity. In 1985, the region showed a net surplus in manufactures trade, but many cases of deficit persisted, sometimes in an amount similar to the surplus of their main basic export resource.<sup>94/</sup> The structure of exports exhibits a similar heterogeneity: on the average, the weight of manufactures exceeds 50% of total regional exports; however, in the large majority of the countries, still more than two thirds of the total exported is concentrated in basic exports.

96. In several dimensions of regional economic activity, the concentration by country has been heightening, since the early eighties: almost two thirds of the domestic product, the industrial product, and gross fixed capital formation of the region are concentrated in two countries. A similar situation occurs with exports; the same two countries generated more than half of the exports in 1988; in the meanwhile, some countries that had been salient during the seventies, curtailed their share.<sup>95/</sup> From the perspective of technological complexity incorporated into manufactures

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<sup>93/</sup> The trade surplus of basic goods in relation to the GDP decreases without variation from an annual average of 10.4% in the 1953-1955 period to 4.2% in the 1976-1981 period; the manufacturing deficit, on the other hand, also falls uniformly from -9.3% to -5.7% between the same periods. See PREALC, *Empleo en América Latina: Una Búsqueda de Opciones*, Santiago, Chile, 1987.

<sup>94/</sup> See the comparison between the net trade balances by productive sector of the regional average and its composition per country. ECLAC/UNIDO Joint Industry and Technological Development Division, Internal Work Document, Santiago, March 1989.

<sup>95/</sup> While Brazil and Mexico exported 30% of the regional total in 1970, their share in 1988 reached 53.5%. Colombia-Venezuela reduced their weight from 25.0 to 15.8; the Southern Cone, from 22.8 to 16.4; the Andean Area of less relative development, from 10.7 to 5.3; and Central America, from 8.2 to 4.0 (source: ILPES, on the basis of data from ECLAC, Economic Projections Center).

export, the contrast is yet more pronounced: while the region exports around 18% of its manufactures in different types of new industries, this component in seven of its countries does not exceed 3% of the respective national total of exported manufactures.<sup>96/</sup>

#### IV.B.2 THE PRODUCTIVITY OF THE REGION

97. Some international experiences reveal that the increase in real productivity facilitates a conciliation of the growth of production with greater levels of employment and higher real wages.<sup>97/</sup> That boost in productivity is closely associated with endogenous technological innovation, as shown by contemporary economic development experiences. Similarly, the growth in productivity is associated with the investment that permits the expansion of the productive base and its restructuring, altering the sectoral proportions on the basis of productive specialisation criteria. In this sense, during the decade Latin America and the Caribbean have experienced a considerable drop in the investment level, public and private (see Chapter V). This situation occurs exactly when the world economy challenges the survival of static comparative advantages and favours the flow of new goods and services with a high content of knowledge, as motors of world trade.

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<sup>96/</sup> On the basis of data from the ECLAC/UNIDO Joint Industry and Technological Development Division, Internal Work Document, *op.cit.* The classification of "new industries" is from ECLAC/UNIDO and distinguishes three types: labour-intensive, capital-intensive, and technology-intensive.

<sup>97/</sup> The growth in average wage and value added per worker between 1975 and 1985 was respectively: 13% and 12.2% in South Korea; 8.9% and 10.2% in Hong Kong; and finally, 10.1% and 8.6% in Singapur. See UNIDO, Industry and Development: Global Report-1987, Vienna, 1987. In the case of South Korea, besides, between 1962 and 1981, manufacturing employment grew at an annual rate of 9%. See UNCTAD/GATT, Logros de la República de Corea en Materia de Exportación, 1961-1982, International Trade Center, Geneva, 1984.

98. Moreover, as already known, in a context of low investment, the indicators of utilised capacity fall and the efficiency of investment is curbed, negatively affecting the growth of productivity. This is reflected in the estimates on regional productivity for the recent period. In fact, the group of countries that exceeds 85% of the regional product shows a drop in labour productivity between 1980 and 1987, which varies from 1% to 2%.<sup>98/</sup> Although they are not strictly comparable, some figures illustrate what is happening in other geographic areas: a recovery in productivity as a reflection of accelerated technological innovation, in several cases higher than the post-war trend.<sup>99/</sup> In sum, the eighties incorporate a decisive component into the external vulnerability of the region: the deterioration of investment and productivity, which reduces the possibility of a more solid trade insertion in future decades.

99. The close relationship between productivity and research and development spending is unanimously recognised.<sup>100/</sup> However, the linkage is a necessary condition, but not sufficient. Technological innovation depends on research and development spending, but other factors can have greater

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<sup>98/</sup> Source: ILPES, on the basis of data from the Economic Projections Center of ECLAC, Santiago, Chile, 1989.

<sup>99/</sup> The average annual rates for some OECD countries between 1979 and 1986 are: the United States, 3.5%; Japan, 5.6%; and West Germany, 2.7%. See ILO, Yearbook of Labor Statistics, Geneva, 1986. The figures corresponding to the countries of Southeast Asia are: South Korea, 5.5%; Hong Kong, 5.8%; and Taiwan, 6.1%. See United Nations, Statistical Yearbook for Asia and the Pacific, New York, 1985.

<sup>100/</sup> It should be remembered that the share of the region in total world resources allocated to R&D is infimal: 1.8% as compared to 30.1% (United States), 10.2% (Japan), and 6.7% (West Germany) in percentages of GDP. The share in the number of engineers and scientists is also low: 2.4% for Latin America, 17.4%, United States; and 12.8%, Japan. See National Science Foundation, International Science and Technology Data, Washington, 1986.

**influence:** among them, quality of labour, degree of productive linkage, diffusion of knowledge, capacity to absorb and adapt new technologies, as well as an economic policy that provides stable signs on the medium run, favouring earnings and the expansion of those branches with greater capacity of innovation.

100. In any case, there is a growing consensus that endogenous technical progress largely depends on the ability of the productive units to assimilate and use the innovations; this demands selective R&D spending. The development of these capacities requires an aggregate demand in growth, to benefit from the advantages of specialisation and world trade; an active role of technological institutions and close ties with production; and furthermore, stimulation of competition on domestic markets. Under the current conditions of the region, productivity acquires, besides its technical and economic meanings, social relevance. Aspects such as that of organisation of productive processes, informed participation of intervening actors, and social cooperation for coming to an agreement on priority subjects are decisive for exploring complementarities among public and private efforts, as well as to provide a new setting for action to the regional attempts at cooperation and integration. This concern over productivity is also a topic of social policy: the new external reinsertion and productive transformation demand a work effort with a growing capacity adapted to the demands of a globalised, highly dynamic world economy.

## Chapter V

## TYPE OF INSERTION AND FISCAL CRISIS

101. As a consequence of the external crisis afflicting the countries of the region, the experience of recent years has evidenced a reduction in the degree of autonomy of governments in the design and execution of public policies.<sup>101/</sup> The adoption of macroeconomic programmes whose rationale was based on external adjustment and internal stabilisation, whether through processes that were either simultaneous or based on time intervals, severely affected the performance level of governments beyond what a bulky fiscal deficit indicates. Consequently, the topic of budget and financial imbalances of the public sector, their interaction with other short-term imbalances and, moreover, their implications for the development process on the short and long run have become focal points of the present debate in the region.

## V.A THE TENSE OBSESSION FOR THE SHORT TERM

102. The impact of the crisis and short-term urgencies distracted the attention to the future. For the reasons already mentioned, it is crucial to recover the traditional levels of investment (physical and social) and spending on intellectual capital. In this last aspect, the State performs a strategic role in both the promotion of R&D in enterprises and direct support for S&T activities. It is time, therefore, to briefly describe the causes and implications of the budgetary and financial imbalance of the

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<sup>101/</sup> This appraisal was stressed by ILPES in 1986; see ILPES, La Planificación en un Marco de Interdependencia, Inaugural Speech of the general director of ILPES at the International Colloquium on New Orientations for Planning in Market Economies, op.cit. Next, this chapter is supported in J. Martin, Inserción Externa y la Crisis Fiscal en América Latina y el Caribe, ILPES, Santiago, Chile, March 1989.

public sector, above all, in its relationship with the external situation of the region.

V.A.1 COMMUNICATING VESSEL OF TWO IMBALANCES

103. As was seen, the debt service in the face of a paralysation of voluntary external financing has required a high net transfer of financial resources to external creditors. Consequently, the debt is no longer merely a problem of the financing of international payments; its service becomes a dilemma for the use of the internal resources of debtor countries. In other words, a problem of the allocation of their own resources between the payment of the debt and domestic consumption and investment.

104. The countries of the region have had to generate considerable balances in the trade balance with the exterior in order to materialise that transfer, affecting some of its basic macroeconomic balances. The recessive effects of the external adjustment policies, as well as their transmission mechanisms, are well-known; it suffices to remember their main characteristics during the eighties. On the one hand, the reduction in imports was imposed despite the regional effort to raise exports and also the contention of spending was predominant vis-a-vis the alternative of a growth of the product.<sup>102/</sup> On the other hand, although domestic savings stayed at its pre-crisis levels, investment fell by an amount equivalent to the transfer of resources overseas--as

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<sup>102/</sup> In the 1980-1987 period, the region as a whole increased the volume of its exports by 32%, while their value was decreased by 1%. The per capita Gross Domestic Product was reduced by 6.6% between 1981 and 1988 (ECLAC: Preliminary Overview of the Latin American Economy 1988, op.cit.).

a consequence of the payment of interest, the deterioration of the terms of trade, and capital flight.<sup>103/</sup>

105. Less attention, though, has been placed on the interaction among external adjustment, fiscal crisis, and the level of inflation. The central point is that nearly all of the foreign debt was absorbed by the State. For this reason, its own indebtedness--considerable in several cases--was accompanied by a high level of private indebtedness, including obligations without initial backing by the State.<sup>104/</sup> In some countries, this process began in the late seventies with the use of public enterprises to receive external savings on deposit with the goal, in some cases, of insuring the global financing of the economy. Parallely, the private sector was reluctant to refinance its loans with the exterior due to the increase in exchange risk; for that reason, in some situations the State granted exchange risk insurance to the private sector; in other cases, the process culminated directly with the statisation of most of the remaining private debt.

106. The cumulative result of this process was the virtual statisation of the foreign debt: more than 80% of the total

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<sup>103/</sup> The simultaneity between the increase in external payments and the severe drop in the terms of trade must be underscored. During the 1981-1988 period, the terms of the price of trade of goods FOB/FOB fell by 22.2%, reaching one of its lowest levels since after the war. See ECLAC, Preinary Overview of the Latin American Economy 1988, op.cit. Capital flight for high indebted countries, in turn, averaged 30%; this means that for every dollar of debt, thirty cents fled. See M. Khan and N. Ul Haque, La Fuga de Capitales de los Paises en Desarrollo, IMF/World Bank, No. 1, Vol. 24, March 1987.

<sup>104/</sup> The short-term debt, public and private, also was becoming a long-term public debt. Between 1979 and 1981, a yearly net average of short-term loans of US\$ 17 billion came in, amounting to 28.5% of the total debt in 1981. Since 1983, its share decreased, reaching 7.7% in 1986. See IDB, Progreso Económico y Social en América Latina, Washington, 1988.



debt became public or had public backing.<sup>105/</sup> In other words, the obligations accumulated by previous flows of external financing to the central government, public enterprises, the private sector (productive and financial) were converging toward one single foreign debt "stock": the public debt. Consequently, since the early years of the eighties, the task of mobilising the internal resources necessary for meeting external obligations became centered in the public sector. Thus, the weight of the payment of debt interest in its overall spending rose significantly. For this reason, the problem of the net transfer of resources abroad presents--besides the already mentioned need to expand the external surplus--a budgetary difficulty for the public sector, in charge of materialising it. This generated more acute problems in those countries where the surplus with the exterior mainly belonged to the private sector.

107. The three non-inflationary roads for the government to be able to raise the needed resources in national currency required by the net transfer overseas are well-known: increase its internal indebtedness, sell public assets, or generate a primary surplus. All of them have been traveled down in the region during the recent past. In some cases, the net domestic indebtedness of the government was limited by the restrictions and fragilities of the local capital markets. In the larger countries, with relatively more developed capital markets, a considerable substitution of the external debt by the domestic debt took place. During the eighties, each new citizen was born with a high

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<sup>105/</sup> In this respect, it is necessary to stress the growth in the share of the public debt in the total debt; it went from 53.7% in 1982 to 80.6% in 1987; while the long-term private debt dropped from 18.7% to 10.3% and the short-term debt, public and private, from 27.6% to 9.1% in the same period. See the World Bank, World Debt Tables, Washington, 1988-1989.

congenital debt in foreign exchange; little by little, they also began to be born with debts in national currency.

108. The second possibility, the disposition of public assets, has been used more slowly and controversially. In particular, the budgetary impact of privatisation operations needs to be evaluated within a multi-annual framework; the immediate reduction in the fiscal deficit may be insufficient to offset the drop in the "permanent income" of the public sector, even in the case of enterprises in deficit. In fact, as observed by the IMF, only if the transfer of assets is accompanied by productivity earnings and they can be partially grabbed by the public sector will the budgetary impact be frankly favourable.<sup>106/</sup>

109. With the first two possibilities restricted, the governments of the region tried to reduce their net need for financing. Considering that expenditure, and public revenue even more, is a small fraction of the product, the reductions involved were considerable. Thus, for example, for a level of government expenditure equalling 20% of the product, an overseas transfer of around 6% of the GDP means 30% reductions in spending. The payment of interest of the public debt (external and domestic) as a percentage of total government revenue was, in several cases and years, over 30%.

110. In several cases, real reductions in public revenue during the period of the crisis were witnessed and its regressive nature also sharpened. Despite the polemics in this regard,

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<sup>106/</sup> See IMF, Privatization and Public Enterprises, Occasional Paper No. 56, Washington, 1988, and also A.M. Mansoor, The Budgetary Impact of Privatization, IMF, Working Paper, WP/87/88, Washington, 1987. Privatisation has been used for achieving financial stabilisation. However, the disposition of public assets, as well as other modalities of destatisation, are being debated as possible instruments of a restructuring policy.

the gross tax burden in the countries of the region is not high in comparison to other areas with a similar level of development.<sup>107/</sup> Moreover, during the crisis, there has been a severe deterioration in the gross revenue due to both business cycle and structural reasons. The recession and acceleration of inflation resulted in a fall in direct taxation. There is differing evidence of a waiver of implicit tax revenue in several of the incentives granted to the private sector (both exemptions and tax cutbacks); insufficient coverage of income tax; little use of some tax bases (such as patrimony and rendering of services). The deficiencies of the tax administration system stimulated, at the same time, high rates of evasion. Indeed, the loss of credibility in the government policy negatively affected several components of tax revenue.

111. In relation to the policy of prices and public taxes, two facts should be mentioned: one, in several countries of the region, they were used as an instrument to contain inflation or cut back export costs, resulting in significant delays in relation to other prices of the economy and the increase in the deficit of the public enterprise sector; two, several public prices include a considerable fiscal component, which poses a contradiction between the macroeconomic objectives of the government (reduction of the deficit and contention of inflation) and the microeconomic objective of the enterprises of covering their long-run marginal costs. The efforts at limiting the need for net financing of the public sector have been concentrated, thus, on cutting back programmable expenditures.

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<sup>107/</sup> See V. Tanzi, "Quantitative Characteristics of the Tax Systems of Developing Countries," in World Bank, The Theory of Taxation for Developing Countries, Washington, D.C., 1987.

112. Current expenditures contracted mainly through a strong reduction in wages, employment (in some cases), and cuts in other components (expendable equipment, for example); the latter particularly affected social benefits. However, the bulk of the decrease in spending was concentrated on investment, especially on the maintenance of infrastructure. The information available for a group of fifteen countries indicates that in the first years of the decade, government expenditure went down by 18.3% in real terms.<sup>108/</sup> The fall in investment is explained not only by the inflexibility in reducing current expenditures, but also by the simultaneous need to curb imports, that, in the case of the public sector, were concentrated in materials and equipment for fixed capital formation.

113. With the flow of traffic over non-inflationary roads limited in order to cover their need for financing, several governments had to resort to flotation as an ultimate alternative for closing the budgetary gap. Three of its consequences should be stressed: one, the inflationary dynamic was accentuated at levels unprecedented in the

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<sup>108/</sup> The composition of the spending cutbacks is the following: capital expenditures, -35.1%; wages, -9.8%; other current expenditures, -13.7%; subsidies and transfers, -9.0%. Conversely, the interest item increased by 43.7%. In the expenditure by sector the greatest drop corresponds to infrastructure, -24.9%, and the smallest to security and defense, -4.4%. The group includes Argentina, Bolivia, Brazil, Costa Rica, Mexico, Paraguay, Dominican Republic, Uruguay, and Venezuela (see World Bank: Informe Económico Mundial, 1988).

region;<sup>109/</sup> two, induced the mobilisation of the monetary balances of the private sector to goods and other financial assets, thus feeding the speculative trends already present in the economy;<sup>110/</sup> and three, reduced the space for the monetary policy that, with the same instruments, had to control the money stock and also maintain the global financing of the economy.

#### V.A.2 AN UNPRECEDENTED PRACTICE: EX-POST PROGRAMMING

114. Despite the differences from country to country, over and above those that need not be repeated, it is clear that the region found itself obligated to make audacious efforts to contain--within tolerable limits--the budgetary imbalance. In a general way, some concurrent factors should be stressed that sum up several of the difficulties encountered, as a consequence of the irregular relationship between public accounts and the external sector.

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<sup>109/</sup> Until 1981, the growth of the average CPI in the region was located at around 50% yearly. Since 1982, this level accelerated, reaching 275% in 1985. After a pronounced fall in this index in 1986, as a consequence of the adoption of energetic stabilisation programmes in the countries of greatest relative inflation, the CPI rose again in 1987 and reached a new record in 1988. In addition, it should be noted that the monetary base is small in most of the countries of the region, varying between 5% and 10% of the product; consequently, a flotation equivalent to a few points of it accelerates inflationary pressure. See ECLAC, Restricciones al Desarrollo Sostenido en América Latina y el Caribe y Requisitos para su Superación, Rio de Janeiro, Brazil, April 1988.

<sup>110/</sup> In particular, the external assets became an important fraction of the financial wealth of the private sector; therefore, the ratios of substitution among the assets relevant for the functioning of the economy were modified. In the actual context of globalisation of international financial markets, the ongoing threat of a greater capital flight reduced the degrees of relative freedom between fiscal policy and other macroeconomic policies. This aspect was already indicated as one of the problems negatively affecting the ability to govern (see Chapter III).

a) Volatility of expectations due to uncertainties of an external and internal origin

The negotiations with external creditors and international financial organisms have forced frequent changes or adjustments in the direction of domestic policies, maintaining national economies in a state of permanent uncertainty.

Likewise, the credibility of public policies has been affected by the fatigue of adjustment, due to its meagre results and the difficulties of the government in sustaining them.

So many uncertainties ended up imposing an inflationary disagreement over any possibility of fiscal consensus.

b) Interlacing of spheres of financing

The loss of degrees of relative freedom for the production of public policies imposed noticeable demands for internal consistency; by not satisfying them, the adjustment processes were, on several occasions, disorganised or chaotic.

The public decision-making process was oriented too much toward the need to provide responses to sectoral or partial crises.

Likewise, the urgency to offer them, the insufficient strength of the instruments and their conflictive effects resulted in some breakdowns in government management.

These were reflected in the dislocation of the different accounts of the government: fiscal, consolidated of public enterprises, monetary, and exchange rate.

c) Differences in time horizon in the management of the public imbalance

A primary difference was presented between the pace of external negotiation, which determines the amount of resources to transfer abroad, and the timing of government measures to control the public deficit, one of the focal variables of the negotiation itself.

The increased rapidity in acting on some expenditures or on the generation of certain extraordinary income contributed to the accumulation of important

distortions in the structure of the main flows and stocks of public resources.

The redefinition of worn out fiscal models--which demands political and sectoral agreements, legal or administrative reforms, and renegotiation of acquired rights, processes that develop in the most diverse time horizons--was impeded by the additional distortions induced by the external crisis.

115. The three groups of factors mentioned ultimately produced--in some cases--an investment in the history of budgetary technique: this instrument, designed for being produced "ex-ante," ended up being determined "ex-post." This, in turn, has led to some upsets in institutional relations, both in the public sector (economic authorities and monetary authority, for example) and between the executive and legislative powers.

#### V.B LAX ATTENTION TO THE FUTURE

116. During the eighties, the management of the tie between the external restriction and the fiscal situation exhausted the best of the regional reserves of public energy. In the cabinets in which the main ordinances of public policies were responsibly produced, all the instrumental leverages were taken advantage of and frequently handled with great skill. Outside of them, those leverages were not always linked to concrete phenomena: the competence of the effort did not succeed in preventing it from being lost. In more than one case, governmental credibility itself dissipated. In its two roles, the State weakened. In the role of management, supported by a schlerotic apparatus, it absorbed scarce resources with little efficient results. As the political representative of the nation, it lost external presence and deferred the integration and consolidation of national societies. In general, the management of

complexity and interdependence was unable to reach height and transcendence.

V.B.1 INVESTMENT AS RESIDUE...DEVELOPMENT AS A DETAIL

117. Regional investment fell without interruption during the eighties. Expressed as a percentage of the GDP, gross domestic investment was cut back from 24.3%, average for the 1973-1980 period, to 16.8% in 1985. This occurred despite the fact that gross domestic savings, in the same time span, rose by slightly less than 1%.<sup>111/</sup> This was caused by the decline in public investment that, as already mentioned, was the main adjustment variable for reducing the programmable expenditure of the government and nearing it to the availability of domestic financing. For its part, private investment also decreased; although it is not a variable of government decision-making, there are several reasons that explain its persistent low level. They involve the complementarity between public and private investment, the distortions in long-term financing, and the difficulties in carrying out an economic-business calculation in an international context with erratically fluctuating exchange rates and high real interest rates and in the presence of major internal imbalances--real and financial--unleashed by the external adjustment process.

118. In particular, the functioning of domestic financial markets was dominated by a short-term rationale, which led to a virtual extinction of the sources of medium- and long-term financing in the economy. The loss of the time horizon in the functioning of financial markets is explained not only by the management of external and internal imbalances, but

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<sup>111/</sup> On the basis of data from the World Bank, Informe sobre el Desarrollo Mundial, Years 1987 and 1988, Washington, D.C., 1987 and 1988.



also by the difficulties in introducing structural modifications in at least three institutional settings: in the financial sector, aiming at greater effectiveness in the system and a reduction in intermediation costs; in the tax system, seeking to recuperate the net tax burden and greater tax equity; and in the regime of incentives for the private sector, based on the fact that competitiveness is not domestic but international.

119. The fall in investment was also accompanied by a deterioration in its quality. The availability of external financing during the seventies and its later restriction in the eighties undermined--due to excess or defect--the efficiency in the investment process in the region. In the first case, the affluence of external resources helped to close little viable or high risk investments, which were, in some countries, also of doubtful priority. On the other hand, during the eighties, the quality of the public investment process deteriorated due to the generalised adoption of controls on financial spending, with little consideration for execution time tables of the works and their economic merit; particularly, there has been a considerable erosion in basic capital stock due to the simultaneous reduction in operating expenses and, above all, expenditures for the maintenance of the existing capacity that will require broad programmes of selective rehabilitation of infrastructure.<sup>112/</sup>

120. More recent trends in the magnitude and composition of public spending on investment and S&T are impeded due to the

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<sup>112/</sup> See in the respect, W.C. Baum and S.M. Tolbert, Investing in Development. Lessons of World Bank Experiences, Washington, D.C., 1985.

lack of data of general coverage.<sup>113/</sup> However, the available information for different countries allows a qualitative evaluation of what happened. The following points sum up--not in order--the most visible consequences of the fall in public investment.

- . Deferment or indefinición of the bids on new essential projects, above all in matters of basic inputs and productive infrastructure.
- . Suspension of projects in both these sectors and the area of social infrastructure, even of those in an advanced stage of execution.
- . Interruption or disappearance of the lines of financing for social investment (housing and urban development, for example).
- . Frequent discontinuities in the rate of execution, "sine die" interruptions or delays in the execution of works and projects, with the corresponding increase in real costs and the reduction in the expected cost-benefit ratio.
- . Deterioration in fixed capital in physical infrastructure (transportation, energy, urban equipment) and also infrastructure for social services, due to the erratic--and often mistaken--reduction of maintenance expenditures.
- . In some cases, downgrading of existing projects for telecommunications infrastructure or omission of other new ones, with strategic importance for the productive restructuring of the region.
- . Demobilisation of technical and scientific equipment in potentially vital areas for research, especially in university nuclei--research and teaching--centered in key aspects of S&T development.

121. As investment spending was a residual variable in the process of allocation of public resources and, conversely,

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<sup>113/</sup> As is known, the 1988 World Bank Report was dedicated to economic management and public financing; the lack of data for the analysis of government expenditure is clearly outlined there. See Table 5.10 in World Bank, Informe Económico Mundial - 1988, *op.cit.*

the option that was the least lucrative and riskiest for the private sector, aggregate investment (public and private) in the region fell consecutively between 1980 and 1986 at an annual average rate of 8.5%.<sup>114/</sup> The growth in this indicator by country reveals the following conclusions.<sup>115/</sup>

Of the twenty countries considered, the variation has been positive in only four.

In these cases, the increase was modest: between 0.1% and 0.8%.

Conversely, the negative rates define a much broader interval; from -0.7% to -16.3%.

In the countries with negative rates, investment expenditure fell by around 10% in six countries and by approximately 15% in another three.

During the eighties, a similarity in the behaviour of private enterprises and of the public sector was undeniable: in both there was negligence with regard to the future.

122. "Residual Investment...Development as a Detail" is not a mere expression. Although repeating previously expressed concepts, it is worth remembering that the accumulated variation of the per capita Gross Domestic Product in the region, between 1981 and 1988, was -6.6%. Once again the average hides a very wide range of variation. In only one case, the per capita product grew more than 10% and, in another four, between 1% and 4.3%. In all the others the

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<sup>114/</sup> It should be noted that the period includes two relatively normal years (1980 and 1981) previous to the crisis of 1982. Since that date, investment behaviour has deteriorated more than what this average of the period shows. The base data corresponds to the World Bank, Informe sobre el Desarrollo Mundial - 1988, op.cit.

<sup>115/</sup> The countries included are: Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, Trinidad and Tobago, Uruguay, and Venezuela.

reduction varied from -2.8% to -38.6%; two countries lost one fifth; three, one fourth; and one of them more than one third as regards their respective per capita product at the beginning of the decade. External reinsertion will help to dynamise important segments of the economy of the region; however, this will be insufficient for surmounting--in the immediate future--the problems that the decade accumulated in terms of a relative lag in the economic and social areas.

#### V.B.2 MANAGEMENT EFFICIENCY, A COST REDUCER

123. A detailed analysis of public management problems in the region goes beyond the limits of this work.<sup>116/</sup> When this subject is projected to the future both in the perspective of supporting new external reinsertion policies and in its status as a mainstay for broader development strategies, the insufficiency of its actual treatment is more evident. The mode (in the statistical sense of the most frequent) is located today in the accusation of the excessive size of the public sector and the consequent remedy: reduce its presence in the economy and in society. In this document, reference will not be made to this debate.<sup>117/</sup> However, it is

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<sup>116/</sup> The work undertaken in the region by the Centro Latinoamericano de Administración para el Desarrollo with the technical cooperation of the UNDP Project, "Development of the Management Ability of the Public Sector" should be emphasized in this aspect. Both, in conjunction with ILPES, have implemented various activities (technical meetings, research, for example) for a better articulation between planning and public management. See, in particular, ILPES/CLAD, Democracia frente al Reto del Estado Eficiente (Buenos Aires: GEL, 1988).

<sup>117/</sup> See in this respect R. Franco et.al., Las cuestiones clave sobre la estructura y funcionamiento del Estado en América Latina a fines de los Ochenta, ILPES, Santiago, presented at the High-Level Seminar on State Management and De-bureaucratisation, Montevideo, July 1988, and also, E. Palma, et.al., Lineamientos para una Política Social orientada a la Consolidación Democrática en una Epoca de Crisis, ILPES, Santiago, presented at the High-Level Seminar on New Social Policy Orientations in Latin America and the Caribbean, Quito, August 1988.

convenient to call attention to the need for a more qualitative approach. Public management in the region is undoubtedly ailing; to concentrate only on the need for reducing its sphere of action is equivalent to believing that the same illness in a child is less severe than in an adult...because his organism is smaller. Administrative inefficiency has dimensions of stock and dimensions of flow. Correcting it in one sense or another is one of the most subtle tasks for cutting back costs and controlling imbalances in the main public accounts. Today, although there are important exceptions, the public administrative apparatus lacks the preparation necessary for supporting development policies based on new external reinsertion strategies.

124. Acquiring it, in its diverse dimensions, requires an adequate approach to the management of complex systems. Thus, "the turbulent and uncertain context leads to the need for a management of complexity. In relation to it, there are two possibilities: a traditional one is to try to repress uncertainty, without greatly admitting its existence, and to repeat decisions based on the past. The other is to attempt to confront it by preparing the public manager on how to handle that situation. Adding, "in reality, management begins where technique leaves off."<sup>118/</sup> Five areas of relationship of the government should be stressed in this sense.

**Government and Public Apparatus:** in practically all the countries of the region, the direct and indirect impact of the foreign debt gave strength to divisions existing in the institutional functioning and financial imbalances of the public sector. The magnitude of the maladjustments at both levels voids attempts to find

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<sup>118/</sup> See B. Kliksberg, "La Gerencia Pública Necesaria, Hacia un Replanteo Integral," in OCP/CLAD, La Gerencia Pública Necesaria, Caracas, 1985.

partial solutions or solutions that can be implemented quickly. The interdependence of institutional and financial aspects demands a joint treatment, restricting the effects of actions centered on only some of them.

**Government and Political System:** two observations should be made: one, it is necessary to continue and sustain the process of change for a period that exceeds the normal duration of a government, and two, any process of change entails inevitable political costs. At the same time, these characteristics impose two conditions on the functioning of the institutional system: establish the vital consensus on needed transformations among political forces and also negotiate the changes with social organisations instead of simply trying to impose them.

**Government and Private Sector:** the goal is to define new modalities of interaction between both sectors. The delimitation of its respective areas of activity is today a reason of debate in the region, frequently clouded by the reductionism of matching the strength of the economy with the relative size of its public and private sectors. It is probable that now is the time for a new border treaty between the two, but it is doubtful that urgent border integration agreements are necessary. The reason is simple, but powerful: the mixed nature of an economy is not only given by the coexistence of different forms of ownership, but mainly due to the virtue of its interactions and linkages.

**Government and the Creation of External Relations:** the conquest of larger space in the international scenario will also demand a careful renovation of diplomacy. It would then be desirable for, in each national society, the formation of consensus to be able to provide legitimacy--on the rear--to the overall work of the government. In the face of the region's effort to expand its presence, it is possible that the defensive reactions motivated by preestablished interests increase also. In fact, neither the international economic space is infinite, nor can the necessary rhythm of reinsertion be less than that of its slow expansion. The contrary would mean that the region would remain relatively more isolated.

**Government and Social Organisations:** the fiscal austerity that will prevail during the coming years will necessarily limit the traditional compensatory role of the State. The imbalance between traditional resources and needs demands an in-depth revision of the

modalities of production and social benefits; thus, it is necessary to make progress in the exploration of "organisation-intensive" modalities that unite social participation and public instrumental innovation in order to, as stated, dedicate greater attention to social needs.

125. The eighties would only be a lost decade if the meaning of this expression were limited to the development of the economic indicators of the region in comparison to its own past situation. They represent much more than a lost decade, if the expression is extended in any of these two directions: one, in relation to what happened in the industrialised world and some other developing countries as seen in preceding chapters; and two, if dimensions are added in the internal analysis, such as the deterioration in social indicators (nutrition and health, for example) and in the intellectual capital of the region; in the devaluation of its institutions; and in the loss of trust in the very forces themselves, which the national societies have in order to achieve their historical realisation.