

# CEPAL

## Review

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The following symbols are used in tables in the *Review*:

Three dots (...) indicate that data are not available or are not separately reported.

A dash (—) indicates that the amount is nil or negligible.

A blank space in a table means that the item in question is not applicable.

A minus sign (-) indicates a deficit or decrease, unless otherwise specified.

A point (.) is used to indicate decimals.

A slash (/) indicates a crop year or fiscal year, e.g., 1970/1971.

Use of a hyphen (-) between years, e.g., 1971-1973, indicates reference to the complete number of calendar years involved, including the beginning and end years.

References to "tons" mean metric tons, and to "dollars", United States dollars, unless otherwise stated.

Unless otherwise stated, references to annual rates of growth or variation signify compound annual rates.

Individual figures and percentages in tables do not necessarily add up to the corresponding totals, because of rounding.

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# CEPAL

## Review

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## **Education and changing production patterns with social equity**

*Presentation by Fernando Fajnzylber at the Seminar on Education and Knowledge:  
Basic Pillars of Changing Production Patterns with Social Equity, organized  
by ECLAC and OREALC in Santiago, Chile, 5 December 1991.*

The underlying basis for this presentation is the proposal on Changing Production Patterns with Social Equity which ECLAC submitted for the consideration of the Governments of the region in May 1990,<sup>1</sup> and which has since been debated in various national and regional forums. I should therefore like to mention very briefly, by way of introduction, one of the main messages of that proposal, so as to give a clear idea of the role played in it by the topic with which we are concerned at this meeting. This message could be summed up as follows: in order to attain the two central objectives of development in the 1990s –authentic competitiveness and equity– many institutions and many policies are needed. However, we will attain neither competitiveness nor equity if we fail to take care of human resources and their education, training, and incorporation into scientific and technological knowledge. Talking about equity, or about competitiveness, or even more so, talking about both aims at once without making a consubstantial and consistent effort in this direction is nothing more than fine words. No country can be competitive nor equitable unless human resources are given their due importance.

For ECLAC, the questions of education and science and technology occupy an indisputable leading place. Consequently, in conjunction with the UNESCO Regional Education Office for Latin America and the Caribbean (OREALC) and with the support of consultants from various countries, ECLAC set about the task of going more deeply into this issue, taking three main questions as its starting point: What are the strategic guidelines which should inspire the promotion of this activity which is defined as being of the highest priority? What policies and institutions are needed to progress in this process of change which will give priority to human resources? What kind of order of magnitude are we talking about in terms of mobilization of resources, and what are the potential sources of financing for making this project viable? These are obviously outstandingly important questions which cannot be answered once and for all, and much less by each of the countries alone, through regional-level reflection.

Consequently, the new proposal on education and knowledge as the basic pillars of changing production patterns with social equity<sup>2</sup> which we shall deal with in this Seminar is merely a first effort to outline a response to these three questions. It is an initial effort which seeks to help set in motion systematic reflection on strategic objectives, institutions and policies, and resources and possible sources of financing.

In this presentation, I shall refer only to the first of these questions, since the other two will be dealt with later on in the seminar. Before describing the essential content of the proposed strategy, however, I should like to highlight some of the fundamental elements which served as a source of inspiration in its formulation. Basically, there are five of them: i) analysis of past Latin American experience of the relationship between development and education; ii) outside experience and the international debate on this topic; iii) recent theoretical contributions concerning the human resources/development aspect; iv) specific experiences at the level of individual cases, enterprises, regions, countries and policy instruments, which show up the real trends in this decade of painful learning, and v) the perceptions of the leading actors, as collected in the interviews which were carried out during this study and which we wish to supplement with the present encounter. I shall then proceed basically to review the first three aspects (that is to say, what happened in the past, what the debate is about, and recent theoretical contributions), after which I shall conclude with a description of the proposed strategy.

<sup>1</sup> ECLAC, *Changing Production Patterns with Social Equity*, Santiago, Chile, March 1990. United Nations publication, Sales No.: E.90.II.G.6.

<sup>2</sup> See ECLAC/OREALC, *Education and knowledge: basic pillars of changing production patterns with social equity*. LC/G.1702(SES.24/4), Santiago, Chile, 1992.

## A diagnosis of the Latin American situation as regards the relationship between education and development

Between 1960 and the end of the 1980s, there was a great expansion of educational coverage, and the index of illiteracy in the region went down from one-third to one-sixth of the population. The figures in table 1 show the spectacular and truly epoch-making magnitude of the expansion in the educational system of the region over the last four decades: from 27 million students in primary education the coverage rose to 73 million, that is to say, from 58% of the population to 88%. In secondary education, the number of students rose from four million to 23 million, representing progress from an enrolment ratio of 36% to one of 72%, while in higher education, the number of students increased from half a million to seven million, so that the enrolment ratio rose from 6% to 27%. The effort to increase educational coverage made by the region has thus undoubtedly been on a very large scale indeed.

Table 1

### LATIN AMERICA AND THE CARIBBEAN: ESTIMATED SCHOOL ATTENDANCE AND ENROLMENT RATIOS

(Thousands of persons and percentages)

Level	1960	1970	1980	1985	1986	1988	Annual or average growth rate				
							1960-1970	1970-1980	1980-1985	1985-1988	1980-1988
<b>Preschool education</b>											
Population served	983	1 728	4 739	8 264	8 619	9 491	5.8	10.6	11.8	4.7	9.1
Service ratio <sup>a</sup>	2.4	3.3	7.9	12.8	15.0	14.0					
<b>Primary education</b>											
Number of students	26 653	43 983	64 795	69 646	71 419	72 741	5.1	4.0	1.5	1.5	1.5
Net enrolment ratio of population aged 6-11 <sup>b</sup>	57.7	71.0	82.4	85.2	85.0	87.6 <sup>c</sup>					
Gross enrolment ratio <sup>d</sup>	72.7	90.7	104.8	106.4	107.3	109.3 <sup>c</sup>					
<b>Secondary education</b>											
Number of students	4 085	10 662	17 595	21 318	22 054	23 434	10.1	5.1	3.9	3.2	3.6
Net enrolment ratio of population aged 12-17 <sup>b</sup>	36.3	49.8	62.6	66.2	...	71.6 <sup>c</sup>					
Gross enrolment ratio <sup>d</sup>	14.6	25.5	44.9	50.7	51.6	57.6 <sup>c</sup>					
<b>Higher education</b>											
Number of students	573	1 640	4 872	6 363	6 784	6 978	11.1	11.5	5.5	3.1	4.6
Net enrolment ratio of population aged 18-23 <sup>b</sup>	5.7	11.6	23.6	23.8	...	27.2 <sup>c</sup>					
Gross enrolment ratio <sup>d</sup>	3.0	6.3	13.5	15.9	16.8	18.7 <sup>c</sup>					

Source: UNESCO, Regional Education Office for Latin America and the Caribbean, on the basis of data from UNESCO and CELADE.

<sup>a</sup> With respect to the population from 0 to 5 years of age.

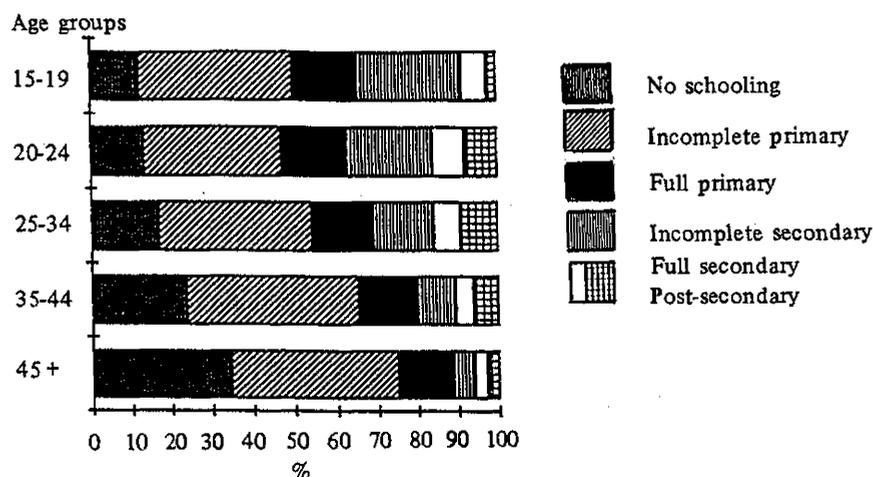
<sup>b</sup> Number of students in an age group (regardless of grade of studies) divided by total population of the same age group.

<sup>c</sup> 1990.

<sup>d</sup> Total enrolment in grade (regardless of age) divided by total population age group corresponding to that grade.

As the growth in demand was even more spectacular, however, the real situation in the 1990s continues to be serious. As may be seen from figure 1, half the young people between 15 and 19 years of age in Latin America and the Caribbean do not have even six years of formal schooling. And what about those who, one supposes, are the source of experience in the region: that is to say, people over 45 years of age? The fact is that 75% of them do not have six years of schooling. This is the real educational situation, in spite of the enormous effort made.

Figure 1  
**LATIN AMERICA AND THE CARIBBEAN: DISTRIBUTION OF POPULATION  
 AGED 15 OR MORE, BY YEARS OF STUDIES COMPLETED**  
*(Percentages, around 1980)*



Source: Joint ECLAC/UNIDO Industry and Technology Division and UNESCO Regional Education Office for Latin America and the Caribbean (OREALC), on the basis of official data.

How does this situation compare with that of other economies which are also of late industrialization? Table 2 shows that in Latin America, impressive rates of coverage were achieved at the primary and higher levels, but a very special feature of the region is that the big advance in university education took place side by side with a serious lag in secondary education. There are countries in Latin America which have rates of coverage in higher education similar to those of the developed countries, but which display serious shortcomings in their secondary education.

Table 2  
**SELECTED COUNTRIES: NET ENROLMENT RATIOS IN PRIMARY,  
 SECONDARY AND TERTIARY EDUCATION, 1975-1987**  
*(Percentages)*

	Primary level		Secondary level		Tertiary level	
	1975	1987	1975	1987	1975 <sup>a</sup>	1987 <sup>a</sup>
Argentina	96	...	42	...	27	41
Brazil	71	84	9	15	11	11
Chile	94	90 <sup>b</sup>	34	56 <sup>b</sup>	16	18
Ecuador	78	...	28	...	27	29
Guatemala	53	58 <sup>c</sup>	10	13 <sup>c</sup>	4	9 <sup>c</sup>
Mexico	98	100	33	44	11	16
Venezuela	81	89	35	44 <sup>d</sup>	18	27
Japan	99	100	...	95	25	30
Korea	99	99	52	...	10	36
Thailand <sup>a</sup>	84	95	25	28	4	16
Italy <sup>a</sup>	105	95	71	75	26	26
Spain	100	100	63	...	20	32
Portugal	91	100 <sup>d</sup>	29	37	11	14 <sup>d</sup>

Source: Joint ECLAC/UNIDO Industry and Technology Division and UNESCO, Regional Education Office for Latin America and the Caribbean, on the basis of official information.

<sup>a</sup> Gross ratio. <sup>b</sup> 1988. <sup>c</sup> 1980. <sup>d</sup> 1986.

The region faces serious problems in the world of production, too. Its biggest contribution to the international economy and to the world in general is made in terms of population. If we look at what this population does, however, the situation is seen to be less encouraging. Latin America has 8.3% of the world's population, but it only generates 6% of the product, produces only 3.2% of capital goods and provides only 1.3% of the scientific authors of this planet (table 3). In other words, a leading feature of Latin America has been its poor capacity to add intellectual value to its people and its natural resources. Consequently, our differences from the developed countries and the Asian countries, or even the Mediterranean countries, are to be seen not so much in terms of educational coverage as in terms of our limited efforts at innovation and the dissemination of technical progress and, above all, in terms of the region's achievements in the sphere of production. Latin America spends less than the developed countries on research and development, and moreover, very little of the knowledge generated in the region is channeled towards the area of production (table 4). As Ricardo Lagos, the Chilean Minister of Education, said only yesterday, this lack of bridges between the world of education and the world of work is a central feature of our continent. Moreover, the fact that the region's educational effort has had motivations and channels different from and independent of the world of production is further compounded by the fact that the world of production has not had much incentive, either, to consider the addition of intellectual value as a basic pillar of its growth.

Table 3

**LATIN AMERICA AND THE CARIBBEAN: ECONOMIC AND  
TECHNOLOGICAL POSITION AROUND 1985**

*(Percentage share of world total)*

Population	8.3
Gross domestic product	6.0
Manufacturing product	6.0
Capital goods	3.2
Engineers and scientists	2.5
Exports of manufactures	1.8
Resources spent on research and development	1.3
Scientific authors	1.3

Source: F. Fajzylber, *Industrialization in Latin America: From the "Black Box" to the "Empty Box"*, "Cuadernos de la CEPAL" series, No. 60, Santiago, Chile, 1990 (United Nations publication, Sales No. E.89.II.G.5), table 11.

This has been changing, however, both with regard to the world of education and that of work. This is why the document we have before us asserts that we are at the end of a cycle. Why have we closed this cycle? Because in both the economic and the educational fields the sources of dynamism have been depleted. Even so, however, this is a favourable moment because we see at least three indications that there is a clear disposition among most of the leading actors to give the transition a constructive character.

What are these three indications? The first one is the fact that in the 1980s, even though public expenditure on education went down, total expenditure on education was not reduced to the same extent. This was because families, enterprises, local and regional authorities, non-governmental organizations and the middle-level institutions of society made a big effort which reflected an implicit decision to give priority to this issue. The scanty information available suggests that this represented a concrete expression of the desire to make up for the shortcomings displayed in the public sphere. The second indication was given at the Fourth Regional Meeting of the Intergovernmental Committee on the Main Educational Project in Latin America and the Caribbean (22 and 25 April 1991), at which the Ministers of Education adopted a declaration expressing their desire to make substantial institutional changes so as to build a bridge between the world of education and that of work. Finally, the third key indication is the reaction which is to be seen among the leaders of the Latin American

Table 4

**SELECTED GROUPS OF COUNTRIES: SCIENCE AND TECHNOLOGY  
INDICATORS FOR VARIOUS YEARS BETWEEN 1988 AND 1990**

Indicator	Latin America <sup>a</sup>	OECD countries <sup>b</sup>	East Asian NICs <sup>c</sup>	Southern Europe <sup>d</sup>
Per capita research and development spending (US\$)	10	448	23	4
Research and development spending (%)	0.5	2.5	1.4	1.0
Research and development spending/engineers and scientists (US\$)	34 858	141 861	50 160	60 647
Engineers and scientists/100 000 economically active persons	99	650	115	185
University graduates/100 000 inhabitants <sup>e</sup>	156	592	478	191
Engineering and technology graduates/university graduates (%)	19.5	15.6	19.6	17.5
Research and development expenditure, by origin (%) <sup>e f</sup>				
i) Public sector	78.8	43.1	35.6	46.4
ii) Business sector	10.5	52.5	61.4	49.5
iii) External funds	3.4	0.4	2.9	3.9
iv) Other	7.3	4.0	0.1	0.2
Research and development expenditure, by activity (%) <sup>e g</sup>				
i) Fundamental research	20.9	14.1	21.1	19.0
ii) Applied research	52.4	28.5	30.4	39.7
iii) Experimental development	26.7	59.5	48.6	41.2

Source: Joint ECLAC/UNIDO Industry and Technology Division, on the basis of official information.

<sup>a</sup> Member countries of the Latin American Integration Association (ALADI), plus Cuba.

<sup>b</sup> Excluding Greece, Portugal, Spain, Turkey and Yugoslavia.

<sup>c</sup> NICs (Newly Industrialized Countries) comprise Hong Kong, Korea, Singapore, Philippines and Thailand.

<sup>d</sup> Including Greece, Portugal, Spain, Turkey and Yugoslavia.

<sup>e</sup> Data for the mid-1980s.

<sup>f</sup> Data do not include Turkey.

<sup>g</sup> Covers only Argentina, Cuba, Mexico and Venezuela; Spain and Portugal; and the Group of Seven (except Canada), in the respective regions.

countries in various fields: those who are responsible for guiding politics or economics or, in general, carry some weight in Latin American society are clearly convinced that we are at the end of a cycle and must make significant changes.

To sum up, the diagnosis we have just made reflects quantitative expansion, serious lags, the end of a cycle, a disposition to make changes, and finally, proposed broad lines of change which are relatively convergent.

### **The international debate on education and the training of human resources**

With regard to the international debate, I should like to highlight what seem to be the main lessons to be drawn from the extensive discussion taking place in the world on the subject of education.

It is worth noting that all the countries acknowledge the truth of the following two assertions: i) competitiveness is increasingly based on knowledge, technology and human resources, so that the place countries occupy in the world depends on what they do in this field; and ii) the State does not have the capacity to provide significantly greater resources than in the past. Although these assertions are accepted by, *inter alia*, Japan, the United States, Korea, France and Germany, the problems involved are very different in

each country. For some countries, the main thing is to make higher education more creative (Japan, Korea). For others (the United States, for example), the main issue is to strengthen a fragile, makeshift and heterogeneous type of basic education. For some countries, such as France, the need is seen for decentralization. For others, such as the United States and, to some extent, England, it is considered necessary to introduce a minimum degree of centralization in order to provide greater rationality. All the countries agree that it is necessary to achieve greater convergence between enterprises and the world of education, but while some countries consider that there is still a great deal to be done in this respect, others are afraid that they may have gone too far. In Germany, which is a paradigm for the relationship between the world of education and that of work, there is perhaps some concern to reduce the degree of specialization and not bring forward so much the moment when young people take separate paths. In all the other countries in general, but especially in the United States, England and France, the aim is to unite the efforts of the world of education with those of the world of work.

In short, although starting from two common initial assertions, the problems that come to the fore are very different. It may be gathered from the international debate, however, that all the countries have arrived at least at the following conclusions:

i) education and human resources represent a priority issue which is not sectoral but national. Assigning due importance to it is not an option, but an imperative for survival.

ii) No country innovates outside the range of its traditions: that is to say, no country does so on the basis of stereotypes stemming from theoretical frameworks. All the countries innovate on the basis of the recognition of their specific institutional characteristics.

iii) Although resource availability is important, the really decisive factor is the institutional aspect. Studies have been made (the most complete investigations have been carried out in the United States) which indicate that the availability of greater resources is not always reflected in better results, the decisive factor being the system of institutions through which the educational issue is processed.

iv) Since the central aspect is that of the institutions, social and political agreements are of decisive importance for education. If the problem were only one of resources, it would not be necessary to establish broad agreements, but if it is a question of making institutional reforms, social and political consensuses and agreements are of decisive importance.

v) In educational matters, it is necessary to take action well in advance, since the efforts made today will only give results in the long term. Consequently, political and social agreements and consensuses must not be of a merely circumstantial nature, but must have solid foundations and broad scope to give them stability.

vi) It is of fundamental importance to evaluate educational achievement. Education is not measured only by the amount spent on it and the number of people working in the sector, but above all by its real results: it is not possible to make judicious changes in institutions without measuring these results.

vii) Since, generally speaking, the issue of coverage has now been overcome, the outstanding issue is that of equity. But in what respect? It is no longer a question of making it possible for everyone to go to school, since virtually all the population already goes to school; what is important is that what young people learn in school should be equitable. In modern knowledge-based societies, the equity of education depends on its quality and content: that is to say, its appropriateness. This, then, is a brief summary of the central elements of the international debate which are described in the document.

### **Recent theoretical contributions**

This reference to recent theoretical contributions does not mean taking an academic approach but instead has a strictly practical purpose, for such contributions exert a great deal of influence on the convictions and behaviour of particular groups of society which, in turn, may have a decisive role in the educational process.

**The contributions of neoclassical economics.** We shall look first of all at the recent theoretical contributions made by the neoclassical school of thought with regard to technical progress. Some may feel that it is not appropriate to incorporate these in a proposal of a general nature. But the fact is that economists as a body and economics as a discipline have a great deal of influence on what happens in the field of education, human resources and science and technology. Moreover, these recent theoretical contributions mark a watershed

in the conception of development held by the neoclassical school (the economic tendency most in vogue at present). Why? Because they give a more endogenous character to technical progress by highlighting the fact that the production of knowledge is an activity just as important as the production of goods and other services.

Furthermore, at least four important concepts derive from these theoretical contributions: firstly, the idea that knowledge and technical change are not aspects foreign to economics, which are manifested through the system of prices or new goods, but on the contrary each economy has the duty and ability to exert influence in this field. Secondly, if we consider that the production of knowledge is a leading economic activity, then policies on knowledge, such as those regarding education and science and technology, become important issues for public policy. Thirdly, as the benefits of knowledge are not necessarily received by those who make the effort in this respect, it is highly probable that there is underinvestment in education, science and technology, and this must be corrected; international experience is perfectly clear in this respect: knowledge is of decisive importance for the growth rate of countries (those which do not make investments in education do not have high growth rates) and their competitiveness. Fourthly, in the process of the production, use and dissemination of knowledge, a crucial role is played by the various agents involved (enterprises, families, local communities, middle-level organizations of society).

The recent theoretical contributions made by neoclassical economics will undoubtedly exert a decisive influence on the way economists approach this issue, concerning which they remained quite distant for a long time past. Indeed, some changes have already been noted. In the last World Bank report, for example, for various reasons, considerable importance is attached for the first time to the question of technical progress and education. Recent theoretical contributions in the field of economics are therefore not just an academic footnote to these reflections, but may result in decisive changes of conception and behaviour by economists with regard to the question of knowledge.

**The contribution made by specialists in business management.** The studies by specialists in business management, which are regularly reported in the press, magazines and even news bulletins, are also important because they exert considerable influence on the business world, the world of professionals, and similar activities. I shall not try to make an exhaustive analysis of these studies but simply try to summarize the main points of the contributions made by some distinguished academics such as Peter Drucker, Omae and Michael Porter, on the subject which concerns us. What have they said in this respect? They have said a great many things, but on this occasion I shall try to summarize the central argument of each of them. Peter Drucker, after highlighting the importance of education and training for business management, emphasizes the decisive civilizing function of education and notes that if the transcendental value-laden function of education is set aside and attention is focused only on its workaday functions directly linked with the interest of the enterprise, there is a risk of giving rise to "educated barbarians". This is how this researcher, who has great influence on the big corporations of the world, has emphasized that the real importance of education goes far beyond its immediate contributions.

Omae, for his part, urges his readers not to cherish any illusions about the possibility of improving business management unless they do the same in the area of education. He argues that Japan has been successful in horizontal, flexible forms of business management, with alliances, work groups, quality control, etc., because these activities are correlative with the values inculcated in the area of education: team work, respect for the values of the group in which one works, exactness, a concrete approach, and honesty: all elements on which the success of business management rests. Consequently, the efficiency of enterprises cannot be substantially improved merely by the introduction of organizational practices similar to those used by the Japanese, if this correlative action in the area of education is missing. Omae thus highlights the bridge between education and work in its purest expression.

In the case of Michael Porter, I shall mention two central concepts: i) the comparative advantages of enterprises are connected, *inter alia*, with their human resources, so that enterprises which do not train their staff are putting themselves at a disadvantage in a competitive world in which all the other enterprises engage in training; ii) the world of education and training is an area of convergence on which the main pillar of the alliance between the public sector and productive sector must be erected. The contributions of these gurus of

advanced business management are of great importance, since there are some indications that the messages they are transmitting have had a great deal of success not only in the world of business but also in the world of professionals and similar activities.

**The contribution of prospective studies.** Finally, we must consider prospective studies, which have far-reaching influence on public opinion in general and create a suitable climate for the penetration and spread of certain *idées-force*. I shall only highlight some of the main ideas emerging from these studies. First of all, they emphasize the fundamental imbalance which exists between the conception of the educational system—established according to nineteenth-century principles—and the demands of the society of the future, and they point the way to imminent changes of the greatest importance. Secondly, they repeatedly stress the idea that the way countries are incorporated in the world is connected basically with what people know rather than with what people have, and the countries whose people know most will be the countries which have most. Thirdly, they emphasize that we are in a world where there is a proliferation of agents, so that the world of education will cease to be the world of educational agents as such. Instead, there will be an interaction between three groups of agents: the educators of the world of education, the educators of the world of work, and the educators of the world of communication. The nature of the links between these three types of actors will be of decisive importance for fixing the new model. Finally, taking a rather apocalyptic view, some prospective studies suggest that technical change will produce profound exclusion, not only between countries, but also within countries and even within enterprises, and that this differentiation will be between those who know and those who do not know. In other words, even those who take this dramatic view see education as the decisive element in the weight people will have in the future, and they consider that raising the level of education is the only way of guaranteeing social inclusion.

To sum up, both the theorists of the world of economics and management and the prospective studies and conclusions arrived at in Latin America on the basis of the diagnosis which has been made take fully convergent views and open up the way for a set of *idées-force* which come from different sources, but regarding which there is growing consensus. This is the basis for the proposed strategy to which I shall now refer.

### **The proposed strategy**

This proposed strategy,<sup>3</sup> whose basic aim is to help set in motion a debate designed to create consensus in Latin America, contains both the *idées-force* which inspire it and the conditions for putting them into practice.

What are the essence and content of the proposal? As indicated in figure 2, we have two guiding objectives: citizenship, and international competitiveness. Let us dwell for a moment on these two goals. What is the real meaning of “citizenship” or, more specifically, “modern citizenship”? It means that every person has the capacity for his full development, not only in the world of work, but also in the family and in the worlds of social relations, political affairs and culture, while at the same time having links that provide social cohesion, access to the codes that permit him to feel that he belongs, and pluralistic, systematic and informed participation in the world of political affairs. Thus, “modern citizenship” is much more than the right to the vote and equality before the law: it is the right to the full development of persons, cohesion and fellowship among persons, solidarity, and also access to a set of common codes. All this makes up modern citizenship: the central objective of the proposed strategy. And there is no doubt that we have made a good deal of progress in Latin America towards this objective, although there are still obvious and sometimes even dramatic lags in the face of the great breadth of the concept.

However, to imagine that we can build societies in which modern citizenship is fully operative without making an effort to attain international competitiveness would be a sheer illusion, because, as already noted on other occasions, the aspirations of the Latin American population run parallel with those of the developed world. Consequently, societies which are hypothetically very well placed with regard to the practical likelihood of modern citizenship will very soon lose their strength and legitimacy if they are not capable of moving in keeping with the aspirations of the population. Moreover, this modern citizenship also involves practical,

<sup>3</sup> See ECLAC/OREALC, *Education and knowledge...*, *op. cit.*, Part Three.

Figure 2  
THE PROPOSED STRATEGY

Objetives	Citizenship	Competitiveness
Policy guidelines	Equity	Performance
Institutional system	Integration	Decentralization

workaday, economic, prosaic requirements. If these are not pursued at the same time, we will find ourselves once again in a situation of speaking fine words about modern citizenship but facing a reality which will not correspond to it at all. There is undoubtedly some degree of tension between the concepts of modern citizenship and competitiveness. Seeking to heighten competitiveness at the expense of modern citizenship is an obviously outdated attitude, however, while giving priority to modern citizenship but ignoring competitiveness is a rather ingenuous approach.

In order to progress towards the objectives in question, two types of policy instruments are needed: on the one hand, instruments designed to tackle cases of lack of equity in terms of coverage, quality and appropriateness of knowledge, and on the other, instruments to measure the performance of the system. Seeking to solve the problem of equity without verifying how far the purposes of the process of education, training or scientific and technological research are being effectively fulfilled would be just as illusory as evaluating the performance of the system without paying any attention to whether or not it fulfills the objectives of promoting greater equity. Once again, there is a certain degree of tension here, but it cannot be avoided.

In order to apply these policies with the purpose of attaining the proposed objectives, the system of institutions requires far-reaching changes which, paradoxically, point in two different directions. On the one hand, they must seek to strengthen national integration, which in many countries of the region is still only in an embryonic state, or at least not yet fully realized. On the other hand, they must promote decentralization, with emphasis on the autonomy of the individual establishments. In order for there to be citizenship and competitiveness at the same time, it is necessary to develop spaces within education, training and science and technology which provide room for identity, projects, initiative and some degree of boldness, so as to be able to face up to the demands of the real world in which the establishments are located. Autonomy can help to generate creative capacity, but the idea that it will solve the problem of integration alone and unaided is not borne out by experience. There must therefore be a parallel integration effort in order to ensure the national integration of autonomous bodies with their own projects and identity.

This, basically, is the essence of the proposed strategy. We now see, however, that there is tension between citizenship, equity and integration, on the one hand, and competitiveness, performance and decentralization on the other (figure 2). The traditional line has always been that education, training and scientific and technological effort will further citizenship, equity and integration. To some extent, this has been the inspiration for the effort we have made in the region. In practice, however, we have lagged behind in some respects: we have not advanced to the full in either citizenship, equity, nor integration. And part of the reason for this is that we have not made a simultaneous effort to ensure that the knowledge attained is fully relevant to competitiveness; we have not evaluated the performance achieved, and we have not given the individual establishments sufficient autonomy to ensure full development of the capacities of those working in this field.

In the 1980s, partly in response to the unsatisfactory nature of previous results, proposals began to be made which put the emphasis basically on competitiveness, performance and decentralization. Thus, some circles give priority to the concepts of citizenship, equity and integration, while others stress competitiveness, performance (efficiency) and decentralization. What we are suggesting here is that it is not possible to advance towards the first-named objectives without making a decided effort to attain the latter ones. Equally, it would be a crass error to pursue the latter objectives while ignoring the fact that important tasks connected with the first-named aims still remain to be accomplished. Obviously, the feedback operates in both directions.

I shall now deal with the criticisms that usually arise with regard to the three terms that appear in the third column of figure 2. The inclusion of the term "competitiveness", for example, does not always bring favourable reactions. The first objection is almost on the aesthetic level. How, it is asked, can one place a transcendental conception such as that of citizenship, which has social, political and cultural connotations, on the same level as competitiveness, which is workaday, economic and financial? The truth is, however, that in real life the transcendental and the commonplace exist side by side, and it is difficult to uphold the legitimacy of transcendental conceptions without also taking account of everyday considerations. Moreover, in this context competitiveness is understood as being based on the addition of intellectual value, that is to say, on the full development of citizens.

Objections have also been made to the use of the term "competitiveness" because it is seen as an extension of the orthodox economic approach and therefore has nothing to do with the world of education. This interpretation limits the concept of competitiveness to its simplest expression, forgetting that it means not only greater exports and openness, but also the intellectual development of the people.

Finally, it has been said that competitiveness is competition, and competition means the market, so that what is proposed is that education, knowledge, science and technology should all pass into the hands of the market. It is true that there are spaces for the operation of the market in the field of education, but there are also areas of values, ethical considerations and a sense of belonging which have nothing to do with the market. Consequently, in the case of the proposed strategy this view is also unfounded.

I have highlighted these objections because there probably will be reactions like these, since our approach so far had more to do with the concepts of citizenship, equity and integration (second column of figure 2) than those of competitiveness, performance and decentralization (third column of that figure). There have also been similar objections to the concepts of performance and decentralization, but I shall not enlarge on them here. Generally speaking, all these objections are connected with the need for change in institutions and a new perception of how to promote the region's growth. We cannot simply fall back on nostalgia, but neither can we base our approach on a sudden change whereby vice is transformed into virtue, and virtue into vice: the situation is much more complex, and involves the tension observed between the two columns referred to in figure 2. This tension exists and appears inevitable in each of the three main fields of action—objectives, policy guidelines, and changes in institutions—so that the task ahead is by no means a trivial one.

We now come to the question of the conditions for the application of the proposed strategy. In this respect, there are basically two things to note. Firstly, the starting point is different in each country. Consequently, there can be no question of a single uniform recipe for the whole region. If the countries are grouped according to the demands of their production system and their educational supply, this gives four basic situations as shown in figure 3. There are countries in the region with a complex and highly developed production base but serious educational lags (for example, Brazil). Others have a highly advanced educational system but substantial lags as regards the level of complexity of their productive system (as in the case of several small countries of the region). Finally, there are others which are backward in the fields of both production and education. So far, however, there is no country in the region which is advanced in the area of production, with a complex productive system, together with competitiveness and a notable educational effort. This is the goal we should aim for, but as the initial

Figure 3

**REQUIREMENTS OF THE PRODUCTIVE SYSTEM AND EDUCATIONAL SUPPLY**

**REQUIREMENTS OF THE PRODUCTIVE SYSTEM**

EDUCATIONAL SUPPLY		-	+
	-	1	2
	+	3	4

Source: Joint ECLAC/UNIDO Science and Technology Division and UNESCO Regional Education Office for Latin America and the Caribbean.

situations are so different, what we say in this article is on the level of general reflection and must be decoded, translated and enhanced in each particular situation.

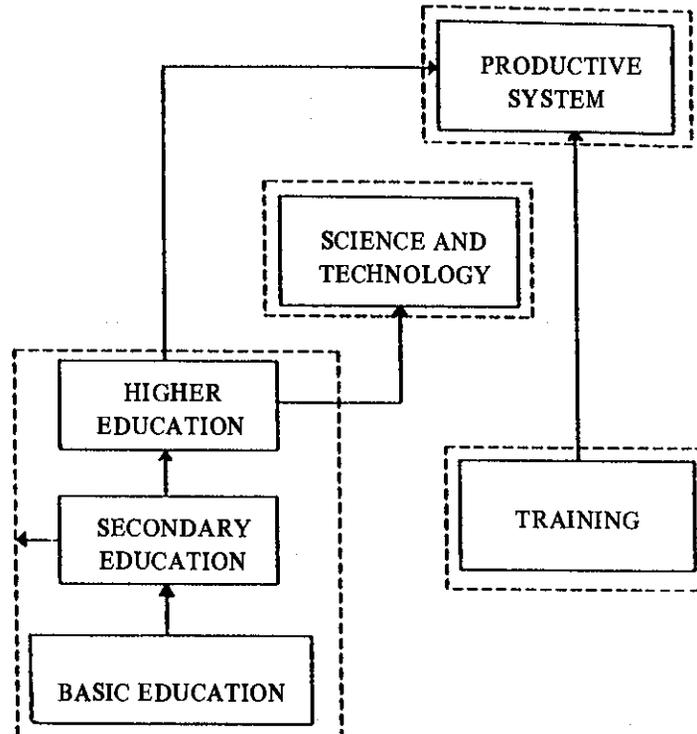
Secondly, the application of the proposed strategy also involves the building of consensus. Why? Because when we look at the present situation we see various sub-systems (figure 4, section A), each of which has its own institutions, leaders, gurus, referents and forums, but very little internal consistency and very little relation with the other sub-systems. In theory, the formal educational system can lead all students to the university, but in practice many casualties fall by the wayside and find themselves without a future. Ultimately, what is proposed here is to move towards another system in which the sub-systems do establish and develop mutual links (figure 4, section B). What this system reflects is not a theoretical aspiration but a real situation towards which progress is being made, more notably of course in the developed countries, but also in Latin America, in spite of the crisis of the 1980s. This is reflected, for example, in the many concrete links of enterprises with basic, secondary and higher education and with technological research centres, as well as middle-level training institutes (ECLAC, 1991, various boxes).

The policies for putting the proposed strategy into practice may be grouped in line with the following objectives:

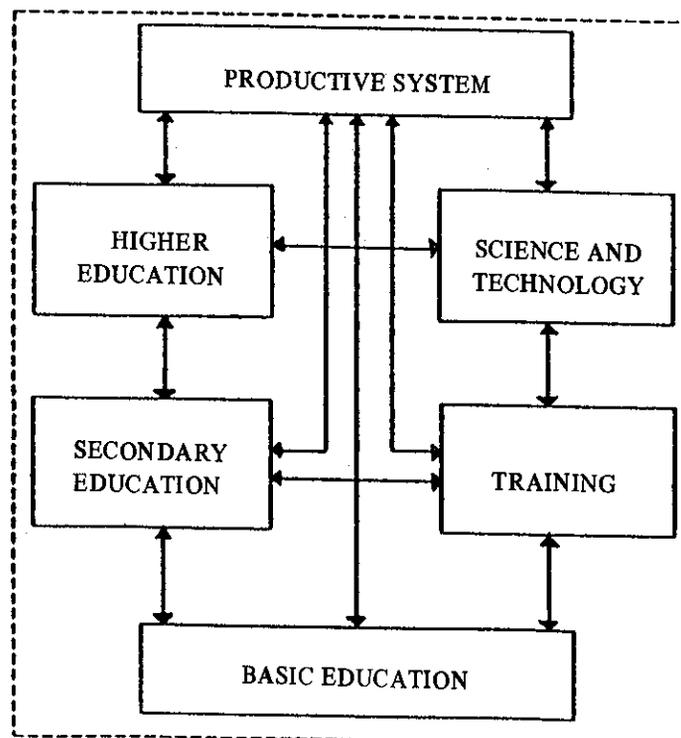
- i) Opening up the educational institutions to the real needs of society: that is to say, establishing suitable institutional conditions to help or at least permit each educational, training or science and technology system to develop horizontal and vertical links with the others.
- ii) Ensuring universal access to the codes of modernity: this is connected with the coverage and quality of both primary and secondary education and training, because thinking that it is possible to train people without having earlier made a corresponding effort at the level of basic education is a mere pipe dream.
- iii) Furthering access to knowledge and taking measures to generate and spread it.
- iv) Promoting responsible management, for it is no longer a question of the traditional educational system, nor traditional training, nor traditional science and technology, but a complex system with a host of actors, perceptions, forms of conduct and aspirations, which make it vitally necessary to have a system of evaluation and information which does not exist at present.

Figure 4  
 RELATIONS BETWEEN EDUCATION, TRAINING, SCIENCE  
 AND TECHNOLOGY AND ENTERPRISES

A. PRESENT SITUATION



B. PROPOSED SITUATION



v) Raising the professional level and status of teaching: a vital requirement without which the proposal will remain merely at the level of good intentions.

vi) Ensuring that support really is provided and that it comes from all the main actors. The educational system will no longer be financed solely by the Ministry of Finance, through a budgetary allocation to the Ministry of Education. This allocation must be increasingly large, but many other contributions will be needed if the question of education and human resources is viewed from this integrated standpoint.

## Conclusions

In conclusion, I should like to highlight three elements in the proposed strategy which seem to me to be most important for the discussion. First of all, this proposal is not the outcome of a beguilingly simple theoretical scheme, but has been constructed on the basis of a learning process taking account of the real situations in Latin America and other regions, the perceptions of the leading actors, and the new visions arising out of the convergent theoretical contributions of the various actors in society. Thus, the first feature of the proposal is its inductive nature.

The second feature of the proposal is its systemic nature. The term "systemic" implies that there is a considerable number of actors, that there must be agreements, and that these agreements must be of a long-term, stable nature. When we speak of a systemic proposal, we are in fact entering a number of fields of great complexity. This proposal is not going to be applied by decree: consensuses must emerge between social actors who have so far not often assumed their parts in the dialogue. The experience pointing in this direction is only of a partial nature, so that while it shows the viability of this approach, it does not guarantee that such viability is general.

The third feature is the existence, at the normative level, of a strong institutional change component, together with a component involving significant additions of resources. In this respect, the proposal diverges from two lines of opinion which currently exist side by side: one of them considers that everything that is being done today in education, training and science and technology is so inefficient that all that is needed is to make institutional changes to solve the problem; the other believes that such institutional change unnecessarily complicates the situation because the real problem is that there are situations of insuperable inertia, and the assignment of more resources would be sufficient to get out of the difficulties.

The proposal which has been formulated recognizes the contribution of each of these components. It takes the view that changes in institutions are inevitable and desirable, but not enough, because when we speak of changes in institutions we are talking about something that affects the culture, history and particular features of the countries, and the proposal does not offer a set institutional formula for all these elements. The specific institutional forms in each country will be the result of the creative effort made on the basis of each country's particular conditions.

In short, the proposed strategy is inductive, systemic, and links institutional change with the provision of extra resources. Ultimately, what it maintains is that education and knowledge are indeed the basic pillars of changing production patterns with social equity.



## The empty box syndrome

*Pitou van Dijck\**

This article examines the thesis –posited in the book entitled “Changing Production Patterns with Social Equity” published by ECLAC– that no country in Latin America was successful in achieving high overall economic growth with a reduction of income inequalities in the 1980s. As compared to the experience of many countries in South East Asia, this was a lost decade for the region. This situation in Latin America has been referred to by Fernando Fajnzylber as the “casillero vacío” or “empty box” syndrome. The examination presented here is based on a comprehensive set of 33 variables related to economic stabilization, structural change, overall economic growth, and the standard of living. It is shown that many Latin American countries did indeed score relatively poorly as compared to Asian countries. However, the study also reveals significant differences among countries within both regions. The relationship between macroeconomic development and human development has been investigated by means of two indexes and is seen to be very complex, as a high pace of overall economic growth does not necessarily result in great progress in terms of human development, but on the other hand, no country has managed to make much progress in human development without being relatively successful in terms of economic development. In the final section of the study, an attempt is made to draw some conclusions from the successful experience of Asian countries that may support the ECLAC proposals for achieving renewed and sustainable development with social equity in the 1990s.

\*With the assistance of Jaap van der Sijs.  
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## Introduction

The 1980s were a turbulent decade for Latin America. In some respects, this was a lost decade, and for all involved in macroeconomic management it was a decade of painful learning. The region was plagued by economic disturbances and suffered from serious internal and external disequilibria. Notwithstanding the painful attempts to adjust and restructure the economies, many of the problems are still unsolved and need to be addressed in the years ahead.

The political constellation in which the economic and social problems need to be tackled has changed dramatically with the establishment of democratic governments in nearly all of the countries of the region. The prime task of the new democracies and, indeed, their main challenge will be to combine in an effective and socially acceptable manner measures to stabilize and restructure the economies, stimulate economic growth and alleviate poverty. The economic performance of most Latin American countries during the 1970s and 1980s was far less successful than that of many other newly industrializing countries in Asia and Europe. Countries in South East Asia, in particular, made impressive economic and technological progress during the 1980s. The economic policies pursued by these countries showed themselves to be more suitable for making economic progress in difficult circumstances, and many countries in that area managed to sustain high economic growth with a reasonable degree of social equity over a long period of years.

In comparison, most countries in Latin America scored poorly with respect to economic growth and social equity. As indicated by ECLAC in its study entitled “Changing Production Patterns with Social Equity” (ECLAC, 1990, p. 61), not a single country in Latin America managed to combine successfully objectives of economic growth and social equity. This phenomenon has been referred to as the “casillero vacío” or “empty box” syndrome of Latin America (Fajnzylber, 1990, p. xiv). In the study in question, ECLAC has made encouraging and far-reaching proposals for fundamental changes in economic policy in the 1990s. The set of proposals aims at replacing regressive adjustment policies of the past by policies that stimulate economic growth with social equity, adopting the strategic criterion of strengthening genuine competitiveness. This requires restructuring and further domestic integration, improved insertion

in the international economy, and a new relationship between government and the private sector (ECLAC, 1990, pp. 98-100). The ECLAC report focuses particularly on long-term strategic objectives of economic policy and institutional problems, and not so much on short-term issues and more specific questions pertaining to the effectiveness of instruments or the timing, sequence and speed of economic reform.

The objective of this paper is to analyse factors that contribute decisively to sustained economic growth with social equity as envisaged by ECLAC. The paper studies in particular the syndrome of economic growth and the relationship between economic development and human development. For that

purpose a statistical analysis has been made of the performance in these respects of countries in Latin America, South East Asia and South Asia during the 1980s. The analysis is based on a large number of variables in the areas of economic stabilization, restructuring and growth, creditworthiness, and human development, and shows the different scores of Latin American and Asian countries with respect to these groups of variables. The research results presented here may contribute to the understanding of the nature of the "empty box" in Latin America and the changes in economic policy required to shift the course of development into the direction envisaged by ECLAC.

## I

### Dimensions of sustainable development

The ECLAC proposals on changing production patterns with social equity cover a wide range of economic policies and will affect many aspects or dimensions of the economic performance of the countries in the region. To take these widely different aspects properly into account and to appreciate fully the differences in economic and social performance between countries, the statistical analysis should include the dimensions presented in table 1, which cover all areas touched upon by the ECLAC strategy for sustained economic growth with social equity.

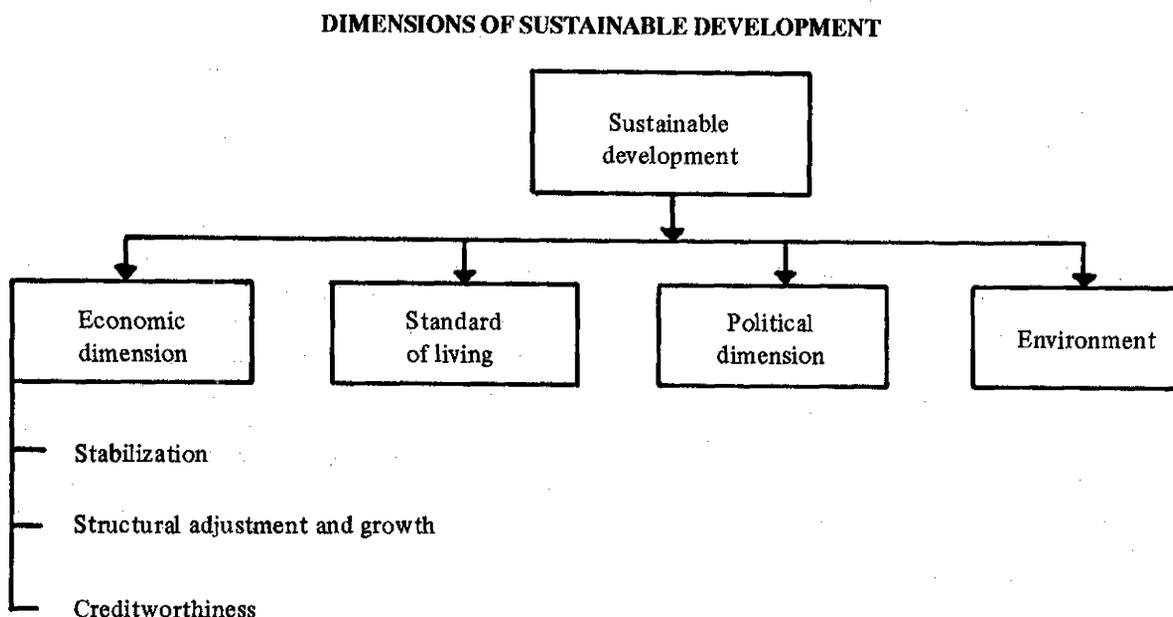
The dimensions have been defined in such a way that they link up with groups of variables traditionally used in studies of the economic and social performance of developing countries, as undertaken by IMF, the World Bank, UNICEF, UNDP and other institutions. However, lack of data in some areas sets limits to the depth and breadth of an analysis of this type. This is particularly true of the non-economic dimensions mentioned above. These dimensions will be briefly discussed below, and in the next section the 33 variables or performance criteria included in the study will be presented.

In the course of the 1970s and particularly during the 1980s, stabilization and adjustment problems dominated economic policy in most developing countries. The monetary approach to the balance of payments, and the policy prescriptions that follow

from it for curing the imbalances, were the subject of an ongoing controversy. IMF analyses traditionally tend to emphasize domestic causes of inflation and unsustainable imbalances in the current account. To monitor the success of orthodox stabilization policies, the Fund has used a limited number of performance criteria such as the rate of growth of domestic credit (particularly growth of credit for the government sector), the government deficit, and the international reserve position.

This rather narrow focus on stabilization measures was complemented in the course of the 1980s by restructuring policies designed to stimulate economic growth, especially by supporting the expenditure and production switching component of stabilization policies. The main components of restructuring policies that have been supported by World Bank sectoral and structural adjustment loans are the liberalization of domestic markets and reduction of protection against imports, timely adjustment of the exchange rate to compensate for domestic inflation that exceeds the international rate of inflation, and direct government support for activities in the tradeables sectors, particularly export promotion. Performance criteria in this area are the current account position, the efficiency of domestic markets, the levels of domestic savings and investment, and the rate of economic growth.

Figure 1



Methodological problems hamper a proper evaluation of stabilization and restructuring policies, and generalizations concerning their effectiveness are hard to make (Khan, 1990). These methodological problems are not always sufficiently appreciated and have often been neglected in the literature. Differences in economic and political conditions set limits to comparisons of economic performance between countries with and without the application of traditional stabilization and restructuring policies. Likewise, comparisons of economic performance before and after the introduction of an adjustment programme do not exclusively reveal the impact of the adjustment programme, but the combined effect of all factors having an impact on the economic situation of the country. For these reasons, the design of adjustment policies, as well as the analysis of their impact, is extraordinarily difficult. This also holds true for alternative plans and proposals to change production patterns.

Notwithstanding these methodological limitations, it is true that many attempts to stabilize and restructure the economies during the 1970s and 1980s were a failure, although some countries were rather successful in this respect, as will be shown in the statistical analysis presented in the next sections. This state of affairs means that stabilization policies must form part of a more comprehensive effort to change production patterns with social equity.

The propensity of domestic and foreign investors to invest depends on a large number of variables at the project as well as macro levels. Private investors such as international banks investigate the investment climate and creditworthiness of economies on the basis of variables related to economic policy, the balance of payments position, the availability of natural resources, and the capacity to export.

Most sovereign risk analyses also include variables related to political stability and cultural factors that in one way or another may have an impact on the profitability of investments and the capacity of governments to service their debts (Heffernan, 1986). The score in terms of creditworthiness determines the position of countries in the international capital market and their rating in the secondary loan market, and determines ultimately the possibilities for supporting economic growth and technological development by foreign loans. Statistical methods such as logit and probit analysis have been applied to assess the risk of foreign lending. However, such analyses include only economic variables and focus predominantly on the very short term.

In addition to these three sets of economic indicators that partly overlap, three groups of non-economic indicators have been introduced in order to permit a comprehensive and truly multi-dimensional analysis of the process of development and structural change. Many studies of the

performance of developing countries during the past few decades have bypassed such non-economic dimensions and have neglected the interaction between economic, political and ecological conditions.

Economic theories still provide only little insight into the relationship between economic growth and social equity. At the same time, data limitations seriously hamper the study of the impact that alternative economic policies have on income distribution and poverty. Although many studies show that poverty increased in Latin America during the 1980s, the relationship between policies actually pursued during the 1980s and changes in living conditions is difficult to establish. Moreover, the meaning of complex concepts such as the standard of living and human development is not entirely clear.

These are not merely theoretical problems but are also relevant in the context of policy formulation, and they deserve serious attention in this context, since improvement of the standard of living is the heart of the strategy that ECLAC envisages. The definition of this concept obviously has important consequences for the type of strategy to be pursued and the type of technological development that should be stimulated. As Sen rightly stresses, the concept of the standard of living should be broad and include a wide range of relevant aspects. At the same time, however, the concept should be quantifiable in order to permit a proper assessment of the actual living conditions in countries (Sen, 1988, p. 20). In one way or another, the concept of the standard of living should express the quality of life rather than the quantity of goods and services that are used or available. Put differently, the criterion should be the opportunity to live in an acceptable manner, and the capability to lead a decent life, rather than the range of products available.

In this context it should be noted that the Basic Needs economic policy approach has contributed significantly to the understanding of the relationship between economic policy and the availability of the shopping baskets of goods needed to satisfy basic human needs. These shopping baskets of goods may be considered as the necessary inputs for an acceptable standard of living. From this line of reasoning it follows that the objective of economic policy is to support the realization of basic human capabilities (Drèze and Sen, 1989, pp. 12, 13 and 42).

The interest in policies focusing on the alleviation of poverty has recently increased significantly,

and new data systems are now being developed by international agencies active in this area. UNICEF has made an attempt to identify the relationship between changes in economic conditions and changes in living conditions and welfare, particularly child welfare. Three types of variables have been distinguished in this complex relationship: input indicators related to the availability of resources, such as household incomes in real terms, real earnings per employee, and employment; process indicators related to the availability and use of key social services, such as per capita consumption, availability of food, calories, vitamins and safe drinking water, availability of health services, and primary and secondary school enrolment; and outcome indicators that show the actual changes in welfare in terms of life expectancy at birth, child mortality, health and skill development (Cornia, Jolly and Stewart (eds.), 1987, pp. 24-58).

To quantify human development and rank countries accordingly, UNDP has constructed an index that includes three variables: per capita income, life expectancy at birth, and literacy rate of the adult population. UNDP has shown that the ranking of countries according to the level of human development may differ significantly from the ranking according to the level of per capita income, although in general there is a strong similarity in the positions of countries with respect to both performance criteria (UNDP, 1990). The present study can only focus on some of the many aspects of the standard of living included in the capability approach outlined above. Data systems that have become available only recently enable the inclusion in this study of 12 performance criteria related to the standard of living.

Political conditions play an important role in the strategy envisaged by ECLAC for two reasons. First, protection of basic human rights can be considered one aspect of an acceptable standard of living. Second, political conditions determine the feasibility of policies and proposals that aim at fundamental changes in the pattern of growth and the distribution of the product. Democratic participation and widespread support are prerequisites for a successful transformation towards greater social equity.

Although most governments have officially recognized individual and collective human rights and have committed themselves to respect and protect them by the ratification of treaties, many of these rights have been violated on a large scale. However,

the introduction of democratic institutions after a long period of military dictatorship has brought about a significant improvement of the human condition in this respect during the last decade.

The human development index initially constructed by UNDP does not include variables related directly to political conditions or human rights. The latest UNDP report, however, includes a much wider range of variables in the area of human development, human rights and freedom, although it is debatable whether all of the selected variables are genuine proxies for universally accepted basic human rights (UNDP, 1991). In the statistical analysis presented here, no variables related to political factors or human rights have been included for lack of data.

The final dimension distinguished here is related to the condition of the environment. The sustainability of development strategies is conditioned by ecological factors. The environmental consequences of economic activities were neglected for a long time, but recent planning takes ecological costs and limitations more explicitly into account. The ECLAC strategy introduces ecological aspects only in general terms and does not explicitly say what the consequences of ecological limitations are for production patterns in the future. However, development strategies for the future should focus in more detail on the relationship between poverty alleviation and ecological decline.

Some indicators are now available with respect to the condition of the environment, but an international comparison of changes in this area during the 1980s could not be made due to data limitations. Put together, these aspects span a substantial part of the development process. Ideally, a fully comprehensive analysis of the development process would include all of these areas. However, the availability of data limits the scope of our study. The 33 variables included in the statistical analysis are related to the three economic dimensions and to some aspects of living conditions. Political and ecological variables could not be included, and several aspects of living conditions have not been covered. In this context, it is particularly unfortunate that data on technological progress are available only for a limited number of countries and therefore could not be included. Also, indicators for the level of competitiveness of industries are not available.

It should be noted that economic dimensions partly overlap and variables can play a role in the analysis of several dimensions of development at the same time. For instance, variables related to the balance-of-payments position can be relevant as performance criteria with respect to economic stabilization and creditworthiness. To put it in statistical terms: the dimensions may not be considered as factors or rotated factors, but are merely different aspects of the economic situation.

## II

### Performance indicators

The performance of Latin American and Asian countries has been measured by means of 33 variables at two moments in time: 1977 and 1987 (see sources in the appendix). Variables 1 - 8 relate to structural transformation and growth; variables 9 - 16 relate to stabilization; variables 17 - 21 relate to foreign debt and creditworthiness; and variables 22 - 33 relate to living conditions and human development.

The following variables have been included in the analysis:

- |            |  |
|------------|--|
| 1. I/GDP   | = gross domestic investment as a percentage share of gross domestic product.                       |
| 2. S/GDP   | = gross domestic savings as a percentage share of gross domestic product.                          |
| 3. dGDP/dI | = contribution of the growth of gross domestic investment to the growth of gross domestic product. |
| 4. RO/L    | = real output per employee.  |
| 5. X/GNP   | = exports of goods and services as a percentage share of gross domestic product.                   |
| 6. Xm/X    | = exports of manufactures as a percentage share of total exports of goods and services.            |

7. HCI = Hirschman Compliance Index in 1972 and 1984.
8. GNP/P = per capita gross national product.
9. (X-M)/M = exports less imports as a percentage share of imports.
10. (T-G)/G = tax income less government spending as a percentage share of government spending.
11. (S-I)/I = savings less investment as a percentage share of investment.
12. G/GNP = government spending as a percentage share of gross national product.
13. INFLATION = rate of inflation, according to changes in the overall price index (GDP deflator).
14. RDR = real deposit rate, i.e., nominal deposit rate less the rate of inflation.
15. RER = real exchange rate, i.e., nominal exchange rate less the rate of inflation.
16. ARI = average annual rate of inflation, 1980-1987.
17. DSR = debt service ratio, i.e., debt service payments as a percentage share of exports.
18. D/GNP = total international debt as a percentage share of gross national product.
19. D/X = total external debt as a percentage share of exports.
20. RES/TDS = international reserves as a percentage share of debt service payments.
21. RES/D = international reserves as a percentage share of international debt.
22. IM = infant mortality rate.
23. LEO = life expectancy at birth.
24. SEp = primary school enrollment
25. SEs = secondary school enrollment.
26. RE/L = real earnings per employee.
27. MIE = employment in manufacturing industry
28. ASW = availability of safe drinking water.
29. CALd/P = per capita daily calory intake.
30. PROTd/P = per capita daily protein intake.
31. IRONd/P = per capita daily iron intake.
32. VITAd/P = per capita daily vitamin intake.
33. HDI\* = UNDP human development index (1987).

It should be noted that all variables have been defined in such a way that an improvement of the economic or social situation between 1977 and 1987 is associated with a positive value of the relevant indicator. In most cases, positive rates of growth are, indeed, associated with an improvement of the situation, but in a number of cases this is not true. For instance, progress in the area of economic stabilization results in a reduced rate of inflation, and an improvement of the balance-of-payments position and greater creditworthiness are associated with reduced debt-service obligations. Also, the reduction of infant mortality indicates social progress and human development. Therefore, the signs of the following variables have been reversed: HCI(7), G/GNP(12), INFLATION (13), RDR(14), RER(15), ARI(16), DSR(17), D/GNP(18), D/X(19), IM(22).

Many economic studies have made a comparison between the economic performance of Latin American countries and the four "Asian tigers": Taiwan, South Korea, Hong Kong and Singapore. Some other countries in South East Asia also experienced high economic growth and impressive change in their production patterns during the 1970s and 1980s, however. To enable a comprehensive international comparison of the economic performance of Latin American countries, this study therefore also includes newly industrializing and other developing countries in South East Asia, countries of the Indian subcontinent, and China. Thus, the following 31 countries have been included: Latin America and the Caribbean (19): Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Haiti, Honduras, Jamaica, Mexico, Paraguay, Peru, Trinidad and Tobago, Uruguay, Venezuela. Asia (12): Bangladesh, China, India, Indonesia, Malaysia, Nepal, Pakistan, Philippines, Singapore, South Korea, Sri Lanka, Thailand.

### III

## Economic and human development

Two statistical steps will be made in order to study the economic growth syndrome and the relationship between economic growth and human development, and to compare the scores registered by countries in their economic and social development indicators. First, we will investigate the relations between the 33 indicators, and next we will construct indexes for economic and social development and rank countries according to their scores on these indexes.

Table 1 shows the coefficients of correlation between the 33 variables. As noted in the previous section, an improvement of the situation between 1977 and 1987 is indicated by a positive value of the variable. Here we shall not discuss all relations in great detail but limit ourselves to some observations pertaining to findings that are particularly relevant in the context of the proposals for structural change with social equity formulated by ECLAC.

On the basis of table 1, the following four observations can be made.

1) With respect to the group of variables related to structural transformation and economic growth (1-8), we note that there are significant relations between changes in the shares of investments (1), domestic savings (2) and exports (5) in GNP. This indicates that improvement of the export performance and strengthening of international competitiveness require stimulation of investment and domestic savings. Domestic savings as a share of GDP are particularly stimulated by high real interest rates (14), and to a lesser extent this also holds good for the share of investment in GDP. Conversely, investment and savings are particularly discouraged in destabilized economies with high rates of inflation (16).

2) There is some interrelation among the variables related to economic stabilization (9-16), but there is no relationship between inflation (16) and economic growth (8). This should not come as a surprise, since economic theories differ substantially in their views of the causes and effects of inflation, and many statistical analyses have failed to reveal a strong relationship between inflation and overall economic growth. However, we do find a significant relationship between a reduction of the rate of inflation (16) and increases in the rates of investment

and savings in GDP, the growth of labour productivity in real terms (4), and the contribution of the manufacturing sector to the country's export performance (6).

3) There is no simple, evident syndrome of overall economic growth that holds good in all countries under all circumstances. The analysis presented here does not show clear relations between economic growth, structural transformation and stabilization. Many international comparisons have shown a simple clear-cut relationship between overall economic growth (8) and openness of the economy (5), but such a relationship does not appear to be significant in this analysis. Apparently, some countries in the sample managed to keep up economic growth during part of the period under consideration in conditions of high inflation and a large trade deficit, thanks to the assistance of foreign savings. High growth rates during the first years of the period were succeeded by years with negative growth in this group of countries. Other countries managed to attain a relatively favourable and more stable pattern of economic growth throughout the greater part of the period without opening their economies in a significant way. Finally, there is a group of countries that were very successful in terms of overall economic growth. Some of the countries in this group made great progress in opening their economies, but other countries were already open at the beginning of the period. These differences in starting positions and in strategies during the period 1977-1987 underlie the limited correlation that we have found between economic growth and other variables.

The table shows, however, that the more open the economy, the better its balance of trade position (9), the larger its saving surplus (11), the more favourable its debt servicing position, and the greater its international creditworthiness (17-21).

4) The group of 12 variables related to living conditions and human development includes three types of indicators briefly described earlier: input, process, and outcome indicators. Not surprisingly, there are strong relations among the process indicators (29, 30 and 31). Our analysis does not show many significant and logical relations between the group of variables related to living conditions and

Table 1  
MATRIX OF CORRELATIONS AMONG 33 PERFORMANCE INDICATORS

	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24	25	26	27	28	29	30	31	32	33	
1. I/GDP	<b>.73</b>	<b>.36</b>	<b>.23</b>	<b>.37</b>	<b>.18</b>	<b>.12</b>	<b>.06</b>	<b>.09</b>	<b>-.06</b>	<b>.21</b>	<b>-.24</b>	<b>.27</b>	<b>-.47</b>	<b>.09</b>	<b>.55</b>	<b>.10</b>	<b>.22</b>	<b>.42</b>	<b>.13</b>	<b>.31</b>	<b>-.06</b>	<b>.04</b>	<b>.21</b>	<b>.00</b>	<b>-.22</b>	<b>.36</b>	<b>.33</b>	<b>.35</b>	<b>.38</b>	<b>.23</b>	<b>.17</b>	<b>-.04</b>	
2. S/GDP		<b>.37</b>	<b>.28</b>	<b>.54</b>	<b>.16</b>	<b>.12</b>	<b>.08</b>	<b>.28</b>	<b>.03</b>	<b>.82</b>	<b>-.14</b>	<b>.35</b>	<b>-.67</b>	<b>.10</b>	<b>.63</b>	<b>.25</b>	<b>.17</b>	<b>.43</b>	<b>.24</b>	<b>.32</b>	<b>.10</b>	<b>-.08</b>	<b>.14</b>	<b>.01</b>	<b>-.05</b>	<b>.25</b>	<b>.29</b>	<b>-.05</b>	<b>-.07</b>	<b>-.16</b>	<b>-.01</b>	<b>.29</b>	
3. dGDP/dI			<b>-.27</b>	<b>.37</b>	<b>-.29</b>	<b>.10</b>	<b>-.16</b>	<b>-.17</b>	<b>.38</b>	<b>-.20</b>	<b>.38</b>	<b>-.14</b>	<b>.07</b>	<b>.35</b>	<b>-.07</b>	<b>.42</b>	<b>.14</b>	<b>.35</b>	<b>.55</b>	<b>.56</b>	<b>.02</b>	<b>.01</b>	<b>.14</b>	<b>-.14</b>	<b>-.38</b>	<b>.19</b>	<b>-.03</b>	<b>.03</b>	<b>-.01</b>	<b>-.14</b>	<b>-.02</b>	<b>-.04</b>	
4. RO/L				<b>.25</b>	<b>.29</b>	<b>.01</b>	<b>.54</b>	<b>.26</b>	<b>-.14</b>	<b>.21</b>	<b>-.20</b>	<b>.47</b>	<b>-.31</b>	<b>-.25</b>	<b>.41</b>	<b>-.03</b>	<b>.14</b>	<b>.21</b>	<b>-.13</b>	<b>-.03</b>	<b>-.12</b>	<b>-.19</b>	<b>.14</b>	<b>.28</b>	<b>.42</b>	<b>.15</b>	<b>.45</b>	<b>.17</b>	<b>.18</b>	<b>-.05</b>	<b>.19</b>	<b>.05</b>	
5. X/GNP					<b>-.12</b>	<b>-.21</b>	<b>.05</b>	<b>.59</b>	<b>.18</b>	<b>.46</b>	<b>.07</b>	<b>-.12</b>	<b>-.24</b>	<b>.12</b>	<b>.24</b>	<b>.39</b>	<b>.02</b>	<b>.51</b>	<b>.49</b>	<b>.51</b>	<b>.03</b>	<b>-.09</b>	<b>-.13</b>	<b>-.31</b>	<b>.01</b>	<b>.30</b>	<b>.16</b>	<b>.13</b>	<b>.09</b>	<b>-.04</b>	<b>.07</b>	<b>.19</b>	
6. Xm/X						<b>-.04</b>	<b>-.10</b>	<b>.03</b>	<b>-.42</b>	<b>.11</b>	<b>-.54</b>	<b>.12</b>	<b>-.37</b>	<b>-.10</b>	<b>.37</b>	<b>-.22</b>	<b>-.13</b>	<b>-.21</b>	<b>-.19</b>	<b>-.22</b>	<b>.15</b>	<b>.06</b>	<b>.40</b>	<b>.27</b>	<b>.03</b>	<b>.23</b>	<b>.39</b>	<b>.13</b>	<b>.09</b>	<b>-.00</b>	<b>.24</b>	<b>-.02</b>	
7. HCI							<b>.09</b>	<b>-.19</b>	<b>.20</b>	<b>.08</b>	<b>.10</b>	<b>.20</b>	<b>.05</b>	<b>-.09</b>	<b>-.10</b>	<b>-.15</b>	<b>-.02</b>	<b>-.05</b>	<b>-.30</b>	<b>-.20</b>	<b>-.01</b>	<b>.22</b>	<b>.12</b>	<b>-.00</b>	<b>.04</b>	<b>-.01</b>	<b>.13</b>	<b>-.21</b>	<b>-.31</b>	<b>-.17</b>	<b>.06</b>	<b>-.12</b>	
8. GNP/P								<b>.23</b>	<b>-.14</b>	<b>.06</b>	<b>-.20</b>	<b>.18</b>	<b>-.05</b>	<b>.10</b>	<b>.10</b>	<b>-.03</b>	<b>.53</b>	<b>.41</b>	<b>-.11</b>	<b>.02</b>	<b>-.52</b>	<b>-.07</b>	<b>-.07</b>	<b>.19</b>	<b>.51</b>	<b>.18</b>	<b>.23</b>	<b>.13</b>	<b>.08</b>	<b>.05</b>	<b>.21</b>	<b>-.07</b>	
9. (X-M)/M									<b>-.08</b>	<b>.47</b>	<b>-.17</b>	<b>-.18</b>	<b>-.22</b>	<b>.03</b>	<b>.13</b>	<b>.29</b>	<b>.22</b>	<b>.41</b>	<b>.24</b>	<b>.25</b>	<b>-.09</b>	<b>.05</b>	<b>-.29</b>	<b>.06</b>	<b>.22</b>	<b>.15</b>	<b>.13</b>	<b>-.29</b>	<b>-.27</b>	<b>-.09</b>	<b>.09</b>	<b>.25</b>	
10. (T-G)/G										<b>.05</b>	<b>.61</b>	<b>-.19</b>	<b>.41</b>	<b>.03</b>	<b>-.40</b>	<b>.21</b>	<b>-.02</b>	<b>.12</b>	<b>.16</b>	<b>.31</b>	<b>.15</b>	<b>-.08</b>	<b>-.23</b>	<b>-.21</b>	<b>.11</b>	<b>-.10</b>	<b>.05</b>	<b>-.36</b>	<b>-.33</b>	<b>-.43</b>	<b>-.18</b>	<b>.07</b>	
11. (S-I)/I											<b>-.03</b>	<b>.29</b>	<b>-.61</b>	<b>.06</b>	<b>.47</b>	<b>.27</b>	<b>.05</b>	<b>.26</b>	<b>.22</b>	<b>.19</b>	<b>.20</b>	<b>-.14</b>	<b>.03</b>	<b>.02</b>	<b>.08</b>	<b>.05</b>	<b>.13</b>	<b>-.37</b>	<b>-.40</b>	<b>-.42</b>	<b>-.14</b>	<b>.45</b>	
12. G/GNP												<b>-.15</b>	<b>.41</b>	<b>-.13</b>	<b>-.32</b>	<b>.21</b>	<b>-.14</b>	<b>-.07</b>	<b>.21</b>	<b>.21</b>	<b>.30</b>	<b>.03</b>	<b>-.06</b>	<b>-.20</b>	<b>.09</b>	<b>-.03</b>	<b>-.07</b>	<b>-.21</b>	<b>-.22</b>	<b>-.41</b>	<b>-.42</b>	<b>-.05</b>	
13. Infl.													<b>-.54</b>	<b>-.41</b>	<b>.63</b>	<b>-.36</b>	<b>-.11</b>	<b>-.09</b>	<b>-.35</b>	<b>-.21</b>	<b>-.09</b>	<b>-.46</b>	<b>-.03</b>	<b>.12</b>	<b>.13</b>	<b>-.24</b>	<b>.01</b>	<b>.02</b>	<b>-.05</b>	<b>-.08</b>	<b>.13</b>	<b>.12</b>	
14. RDR														<b>-.02</b>	<b>-.83</b>	<b>.10</b>	<b>-.00</b>	<b>-.07</b>	<b>.16</b>	<b>.11</b>	<b>-.17</b>	<b>-.44</b>	<b>-.09</b>	<b>.12</b>	<b>.21</b>	<b>-.34</b>	<b>-.04</b>	<b>.03</b>	<b>-.03</b>	<b>-.09</b>	<b>.08</b>	<b>.02</b>	
15. RER															<b>-.23</b>	<b>.48</b>	<b>.39</b>	<b>.25</b>	<b>.40</b>	<b>.26</b>	<b>-.07</b>	<b>.03</b>	<b>-.07</b>	<b>.05</b>	<b>.07</b>	<b>-.13</b>	<b>-.07</b>	<b>-.01</b>	<b>.03</b>	<b>-.02</b>	<b>-.14</b>	<b>-.16</b>	
16. ARI																<b>-.16</b>	<b>.02</b>	<b>.13</b>	<b>-.16</b>	<b>-.04</b>	<b>.01</b>	<b>.08</b>	<b>-.10</b>	<b>.03</b>	<b>-.20</b>	<b>.10</b>	<b>-.10</b>	<b>-.04</b>	<b>-.14</b>	<b>.10</b>	<b>.05</b>	<b>.01</b>	
17. DSR																	<b>.55</b>	<b>.64</b>	<b>.84</b>	<b>.73</b>	<b>.42</b>	<b>.06</b>	<b>-.10</b>	<b>.19</b>	<b>-.18</b>	<b>.19</b>	<b>.05</b>	<b>-.22</b>	<b>-.20</b>	<b>-.24</b>	<b>.06</b>	<b>.10</b>	
18. D/GNP																		<b>.84</b>	<b>.36</b>	<b>.60</b>	<b>-.14</b>	<b>.11</b>	<b>-.17</b>	<b>.39</b>	<b>.10</b>	<b>.27</b>	<b>.01</b>	<b>-.11</b>	<b>-.10</b>	<b>-.13</b>	<b>.40</b>	<b>-.15</b>	
19. D/X																			<b>.53</b>	<b>.77</b>	<b>-.11</b>	<b>.04</b>	<b>-.16</b>	<b>.15</b>	<b>.00</b>	<b>.40</b>	<b>.11</b>	<b>.02</b>	<b>-.01</b>	<b>-.18</b>	<b>.43</b>	<b>-.02</b>	
20. RES/TDS																				<b>.85</b>	<b>.24</b>	<b>-.06</b>	<b>-.14</b>	<b>-.08</b>	<b>-.09</b>	<b>.10</b>	<b>-.07</b>	<b>.01</b>	<b>-.02</b>	<b>-.04</b>	<b>.10</b>	<b>.19</b>	
21. RES/D																					<b>.06</b>	<b>-.01</b>	<b>-.24</b>	<b>-.05</b>	<b>.02</b>	<b>.19</b>	<b>-.03</b>	<b>.01</b>	<b>-.05</b>	<b>-.15</b>	<b>.35</b>	<b>.03</b>	
22. IM																						<b>.24</b>	<b>.09</b>	<b>.05</b>	<b>-.22</b>	<b>-.08</b>	<b>-.19</b>	<b>-.39</b>	<b>-.11</b>	<b>-.23</b>	<b>-.39</b>	<b>.10</b>	
23. LEO																							<b>.29</b>	<b>.11</b>	<b>-.02</b>	<b>.36</b>	<b>.08</b>	<b>-.05</b>	<b>.09</b>	<b>.07</b>	<b>.01</b>	<b>-.38</b>	
24. SEp																								<b>.33</b>	<b>-.19</b>	<b>.42</b>	<b>.56</b>	<b>.17</b>	<b>.31</b>	<b>.09</b>	<b>-.11</b>	<b>-.31</b>	
25. SEs																									<b>.06</b>	<b>.12</b>	<b>.39</b>	<b>-.36</b>	<b>-.06</b>	<b>-.14</b>	<b>-.02</b>	<b>.25</b>	
26. RE/L																										<b>-.01</b>	<b>.21</b>	<b>-.10</b>	<b>-.18</b>	<b>-.17</b>	<b>.04</b>	<b>-.08</b>	
27. MIÉ																											<b>.36</b>	<b>.33</b>	<b>.25</b>	<b>-.04</b>	<b>.25</b>	<b>-.30</b>	
28. ASW																												<b>.05</b>	<b>.13</b>	<b>-.00</b>	<b>-.04</b>	<b>-.32</b>	
29. CALd/P																													<b>.72</b>	<b>.48</b>	<b>.32</b>	<b>-.04</b>	
30. PROTd/P																														<b>.55</b>	<b>.02</b>	<b>-.20</b>	
31. IROND/P																															<b>.15</b>	<b>-.09</b>	
32. VITAd/P																																<b>-.22</b>	
33. HDI*																																	

<sup>a</sup> Correlation coefficients significant at the level of 0.5 are printed in bold type.

<sup>b</sup> For definitions of these indicators, see Section II.

variables related to overall economic growth and development. The change in real earnings per employee (26) is positively related with economic growth (8), and this fits in with the relationship between the investment indicator and the change in real output per worker (4). We also find a positive relationship between the growth of the investment share (1) and the growth of employment (27). The UNICEF study suggests that employment and real income are key input indicators for welfare, but here we do not find such

an evident relationship between these two input indicators and the outcome indicators. Apparently, changes in living conditions and human development are determined by more structural factors that have an impact in the long run, and not so much by short-term changes in economic variables, as has also been suggested by the World Bank (World Bank, 1990a, pp. 26-39). This relationship between economic change and human development will be analysed in more detail in the next section.

## IV

### In search of the empty box

We shall now compare economic and social developments in Latin America, South East and South Asia by means of two indexes for macroeconomic development and human development.

The economic development index has been based on seven variables: I/GDP(1), S/GDP(2), X/GNP(5), GNP/P(8), (T-G)/G(10), INFLATION(13) and, alternatively, ARI(16), and D/X(19).

The human development index has been based on five variables: IM(22), LE(23), SE(25), ASW(28), and CAL<sub>d</sub>/P(29). Contrary to the human development index constructed by UNDP, our index does not include income-related variables.

The way our indexes have been constructed differs somewhat from the approach followed by UNDP (UNDP, 1991, p. 211). The values of all variables were transformed into index values with a maximum value of one and a minimum value of zero. The maximum and minimum values of each range were determined by the best and worst performances of the countries in the sample. Next, the index values of the economic and social variables, respectively, were added and transformed into aggregated economic and human development indexes.

Thus, the calculations were made as follows.

$$I_{ij} = \frac{(X_{ij} - X_{i \min})}{(X_{i \max} - X_{i \min})}$$

$$I_j = \sum_{i=1}^n I_{ij}$$

$$(\text{Index})_j = \frac{(I_j - I_{\min})}{(X_{i \max} - X_{i \min})}$$

where

$I_{ij}$  = score of country j on indicator i (0-1)

$X_{ij}$  = value of variable i in country j

$X_{i \min}$  = minimum value of variable i (0)

$X_{i \max}$  = maximum value of variable i (1)

Indexes on the basis of economic and social indicators were made for 1977, 1987 and for the changes during the period 1977-1987. Table 2 shows the correlations among the indicators included in the human development index, economic growth, the indexes for economic development and human development, and the UNDP human development index.

Before we focus on the performance of individual countries in terms of economic and human development, a number of observations are called for regarding the relations among some of the variables that play a key role in this part of the analysis.

Table 2

**CORRELATIONS AMONG VARIABLES RELATED TO  
ECONOMIC AND HUMAN DEVELOPMENT**

	LE <sub>0</sub>		SE <sub>s</sub>		ASW		CAL/P		GNP/P \ GNP/P			HDI		HDI*		EDI		HDI EDI	
	77	87	77	85	75	85/87	77	84/86	77	87	77-87	77	87	1987	77	87	77-87	77-87	
IM 1977	-.95	-	-.72	-	-.52	-	-.68	-	-.62	-	-	-.93	-	-.90	-.59	-	.47	.18	
IM 1987		-.99	-	-.66	-	-.67	-	-.69	-	-.50	.11	-	-.93	-.93	-	-.51	.37	-.16	
LE <sub>0</sub> 1977			.71	-	.53	-	.69	-	.62	-	-	.93	-	-.90	.50	-	-.48	.14	
LE <sub>0</sub> 1987				.66	-	.68	-	.69	-	.52	-.11	-	.94	.93	-	.51	-.38	.14	
SE <sub>s</sub> 1977					.56	-	.49	-	.39	-	-	.82	-	.71	.33	-	-.51	.20	
SE <sub>s</sub> 1987						.54	-	.59	-	.54	.17	-	.79	.74	-	.39	-.37	.20	
ASW 1975							.51	-	.53	-	-	.73	-	.56	.21	-	-.60	-.11	
ASW 1985/87								.55	-	.42	-.19	-	.81	.70	-	.33	-.39	.13	
CAL/P 1977									.62	-	-	.80	-	.73	.33	-	-.37	.09	
CAL/P 1984/86										.54	.07	-	.82	.72	-	.38	-.32	.15	
GNP/P 1977										.86	-.41	.66	.68	.66	.69	.44	-.46	-.13	
GNP/P 1977-87											-.05	.57	.58	.56	.73	.64	-.43	.07	
GNP/P 1977-87												.07	-.05	-.06	-.19	.03	.21	.27	
Human Development Index (HDI) 1977													.97	.91	.47	.49	-.58	.13	
Human Development Index (HDI) 1987														.94	.47	.50	-.43	.18	
Human Development Index (HDI*) 1987														.45		-.40	.10		
Economic Development Index (EDI) 1977														.72		-.30	-.19		
Economic Development Index (EDI) 1987																-.21	.49		
Human Development Index (HDI) 1977-1987																			.13
Economic Development Index (EDI) 1977-1987																			

In a sample of 31 countries correlation coefficients above .35 are significant at the level of .05.

- The index related to changes in the level of human development during the period 1977-1987, HDI 77-87, is significantly and inversely related to the variables and indexes for 1977 and 1987. Thus, the lower the level of development initially was, the more progress was made in the subsequent period. Nevertheless, this did not alter very much the ranking of countries according to their level of human development, since the correlation between the indexes for human development in 1977 and 1987 is .97. It should be noted that there is no such inverse relationship between the initial level of economic development and the speed of economic development.

- The indicators for human development are strongly related to each other. Note that a low rate of infant mortality is a positive indicator for human

development, hence the negative signs in the correlation matrix.

- The human development index for 1987 has more correlation with the five selected indicators than the UNDP human development index for 1987 has, as was to be expected. This implies that our index gives a more comprehensive indication for the different aspects of human development than the more limited UNDP index. Nevertheless, the correlation between the two human development indexes for 1987 is very high (.94).

- The correlations between the economic and human development indexes in 1977 (.47) and in 1987 (.50) are significant but not outstanding. Thus, the level of economic development, as measured according to the variables in the index, is not a very

good indicator for the overall level of human development in a country. It comes somewhat as a surprise that the similarity between the level of per capita GNP and the level of human development is stronger: .66 in 1977 and .58 in 1987. Moreover, the two human development indexes have almost the same correlations with per capita GNP in 1987 (.58 and .56). Thus, the economic development index that has been introduced here reflects a specific state of the economy, but this economic condition is not necessarily a good indicator for the average living conditions in the country. To a large extent this is also true of the simple per capita GNP indicator. Nevertheless, all correlations between the levels of economic development and human development are positive and significant.

– It should be noted that there is only very little correlation between changes in the levels of human development that were taking place during the period 1977-1987, and changes in the levels of economic development, be it measured by means of the human development index (.13) or per capita GNP (.21). The experiences of individual countries and groups of countries will be described in greater detail below.

Figure 2 shows the pace of economic development and human development in the 31 sample countries during the period 1977-1987. If, indeed, development in Latin America were correctly characterized as generating only limited economic growth and sharp inequality –as suggested by the “empty box” syndrome– countries in this region should be concentrated in an area quite close to the origin of the axes.

The main findings of this analysis (figure 2) are as follows:

– At the origin of the axes in quadrant three there are only Latin American countries, except for the Philippines. The countries that score lowest on both indexes are Argentina, Trinidad and Tobago, El Salvador, Bolivia, Guatemala, Venezuela and Honduras.

– Nearly all Latin American countries have low scores in terms of changes in the level of human development: 16 of the 19 countries of the region are in quadrants three and four at the lower part of the figure. Chile scores relatively well in terms of economic development and human development as compared to most other Latin American countries.

However, the most outstanding position among the countries of the region is occupied by Brazil.

– Asian countries have the best performance in terms of economic and human development. This is particularly true of Indonesia, and to a lesser extent of Nepal, Sri Lanka and India, which are all located in quadrant one at the upper right hand side of the figure. As compared to these countries, the pace of human development in Bangladesh has been strikingly low. South Korea shows the highest pace of economic development of all developing countries, followed by Singapore and Pakistan.

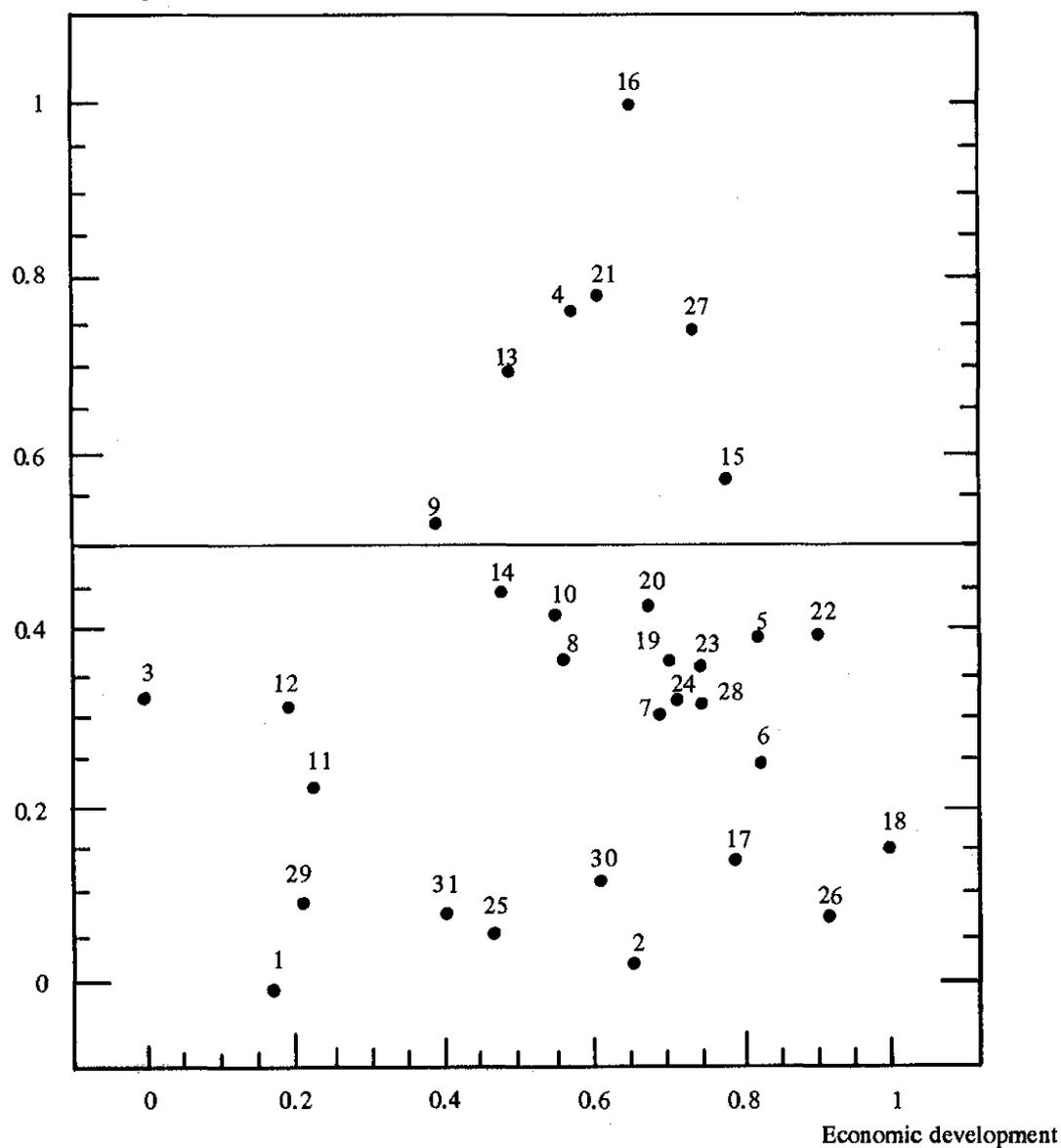
– The positions of the groups of countries indicate that high economic growth and a high pace of economic development, as measured by the variables in the index, do not necessarily result in great progress in terms of human development. However, major progress in human development requires at least some economic growth and development. This follows from quadrant two, at the upper left hand side of the figure, which is almost empty.

The results of this type of statistical analysis should be interpreted with caution. The outcomes of studies that compare the performance of groups of countries depend, of course, very much on the selection of countries and performance indicators, and the period under investigation. For that reason, the classification of countries presented here may differ from classifications in other studies (World Bank, 1990b; UNDP, 1990, p. 99).

Moreover, the pace of development during a period cannot be viewed in isolation from the starting conditions. As shown earlier, the higher the level of human development initially is, the slower progress in this respect tends to be. With respect to some consumption-related indicators that have been included in the study, increases beyond a certain level may even reduce living conditions and life expectancy, and may consequently be considered a negative contribution to human development. Particularly in South Asia, levels of human development are still extremely low as compared to most countries in Latin America. To a much lesser extent this also holds true for many countries in South East and East Asia. Although the 1980s were an extremely difficult period for many countries in Latin America, per capita GNP and living conditions are still much higher than in most Asian countries.

Figure 2  
**SELECTED COUNTRIES OF LATIN AMERICA AND THE CARIBBEAN  
 AND ASIA: ECONOMIC AND HUMAN DEVELOPMENT, 1977-1987**

Human development



*Latin America*

- 1 Argentina
- 3 Bolivia
- 4 Brazil
- 5 Chile
- 7 Colombia
- 8 Costa Rica
- 9 Dominican Republic
- 10 Ecuador
- 11 El Salvador
- 12 Guatemala
- 13 Haiti
- 14 Honduras

- 17 Jamaica
- 20 Mexico
- 23 Paraguay
- 24 Peru
- 29 Trinidad and Tobago
- 30 Uruguay
- 31 Venezuela

*Asia*

- 2 Bangladesh
- 6 China
- 15 India
- 16 Indonesia
- 18 South Korea
- 19 Malaysia
- 21 Nepal
- 22 Pakistan
- 25 Philippines
- 26 Singapore
- 27 Sri Lanka
- 28 Thailand

## V

## New challenges

ECLAC has outlined new policies to bring about a more sustainable and socially acceptable pattern of economic growth in the future. These proposals are a great challenge to the newly elected democratic governments in the region, and make heavy demands on their capacity to manage the economy. The success of these policies will depend critically on the capacity of governments to stabilize and restructure the economy, improve external creditworthiness, and introduce measures that favour particularly income generation in lower income groups. The question is whether these demands are realistic and what should be done to enhance the capacity of governments to stimulate development in the direction outlined earlier.

Many stabilization and restructuring plans have failed, and this is not only true of the policies formulated in conjunction with the IMF and the World Bank, but also of the heterodox shock policies in the 1980s. Understanding the causes of these failures is a precondition for the appropriate specification and implementation of these new proposals.

As indicated earlier, the effects of economic policies are difficult to assess, and consequently the causes of their failure are hard to detect. Methodological problems hamper not only the evaluation of past policies but also the recommendation of new ones. Notwithstanding these problems and limitations, some of the findings of reviews of traditional stabilization and structural adjustment policies can be of particular importance in this context. The reviews show that the cuts made in government spending have resulted in significant reductions of government investments in physical and human capital (World Bank, 1990a, pp. 11-39). The great political risks involved in cuts in many types of current expenditures explain the preference for reductions in investment programmes rather than in current expenditures. However, these cuts in public investment programmes and in education, i.e., human capital formation, can have a negative impact on private investments and economic growth in the future.

In general, structural adjustment programmes in the 1980s had little success in raising the shares

of total investments and exports in GDP. In many countries with structural adjustment programmes, the shares of investment as well as exports in GDP, measured in constant prices, actually went down (World Bank, 1990a, p. 21). These developments are particularly worrying in view of the key role that exports and investment play in the ECLAC strategy for economic recovery in the 1990s (ECLAC, 1990, pp. 48-49).

The limited response to price measures aimed at stimulating exports may be due to several reasons: the inadequacy of the price effect, measured in real terms, for the producer; an unfavourable product range or low product quality; lack of government and private investments to support the expansion of export production; or inadequate facilities and infrastructure to facilitate international trade and foreign market penetration.

The decision to invest and export is based on expectations regarding the profitability of such investments. These expectations and the response of the private sector to new government policies have been shaped by past experience and policy failures. In this respect, policy failure is not only a missed opportunity but also adversely affects the economic climate in the future and reduces the chances of success for new attempts to stabilize and restructure the economy. Rational expectations help to explain the inertial nature of inflation over a very long period, and the failure of monetarist and heterodox policies to bring down the rate of inflation. Policy failures have also led to restraint over investment decisions, particularly in export-oriented industries. This is particularly true of countries with a long history of discrimination against exports and inconsistencies in trade policy and macroeconomic management that have often resulted in debilitating shifts in policies.

The chances of a successful reorientation of economic policy depend to a great extent on the relationship between government and the private sector, and on the capacity of the government to create an atmosphere that is conducive to investment. In view of the negative effects of inconsistent,

destabilizing and unpredictable policies on production and investment in the private sector, much emphasis has recently been given to the need to limit the economic activities of governments and particularly their intervention in markets. Orthodox stabilization and restructuring policies aim at liberalizing markets and reducing the role of government (van Dijck, 1990). There are indeed many good reasons to scrutinize government activities and their impact on the overall functioning of the economy. However, although it is true that governments fail, so do markets. Markets are not only distorted because of government intervention –so-called policy-induced distortions– but also for many other causes, and in such cases corrective measures are required. Sustainable and equitable growth may require frequent and efficient government interventions to reduce barriers to market entry, control monopolies and oligopolies, and limit pollution and the exploitation of nature. Consequently, the less perfectly markets operate, the more corrective government intervention is required.

Moreover, the private sector often falls short of providing the goods and services demanded by society, and this can make necessary stimulating measures by government such as subsidies and tax reductions, or production by the public sector. This is not only true of (semi) collective goods and services but of many other products too.

It is not possible to make generalizations regarding the optimal size of government or the areas of government activity, and there is no obvious relationship between the size of the government sector and the overall rate of economic growth or the rate of investment. The issue is not so much the size of government, but the objectives of its policies and the effectiveness of the instruments used. At this stage of the analysis it is tempting to draw some general conclusions from the experience of the successful South East Asian countries.

As we have indicated earlier, however, one should be extremely careful in making comparisons across countries with respect to government policies and the response of the private sector. Wide differences among countries with respect to their histories and cultures, natural resource endowments and dependence on external factors create different options for development strategies.

Although, in principle, economic laws are universal and economic mechanisms generally applicable, differences in the initial setting result in quite different types of responses of the private sector to policy measures and price incentives. Consequently, the success story of the four “tigers” cannot serve as a simple blueprint for other countries. In the ongoing controversy over this theme, these limitations tend to be somewhat neglected, and strong statements on the causes of successes and failures have often been based on weak foundations.

The approach followed by the successful “tigers” in South East Asia is definitely not typical of the orthodox development policy that advocates a restricted role of government in the economy (Linnemann, van Dijck and Verbruggen, 1987). Governments in these countries have played a very active role, directly as well as through far-reaching interventions in capital markets and markets for products and services. More specifically, they have been particularly active in the areas of export promotion and the support of technological development and investment: two interrelated key areas in these small and natural-resource-poor economies, which are highly dependent on the capacity to exploit comparative advantages and to penetrate foreign markets.

This, however, does not mean that these interventions have always been efficient and successful. On the contrary, costly mistakes have been made, particularly in efforts to stimulate the use of capital-intensive and more advanced technologies and to upgrade the structure of exports. The Heavy and Chemical Industry Plan of the Korean Government in 1972 is a case in point. More generally, it may be said that government policies aiming at the creation of new comparative advantages in capital-intensive and technologically advanced sectors have frequently failed and have created white elephants all over the world.

Traditional indicators of government behaviour may show some important and indeed striking differences between the Asian and Latin American countries, but a more detailed analysis is required to appreciate fully the differences in development strategies. The most striking differences are not so much related to the share of government expenditure in total spending or the contribution of government firms to total production. Much more striking are

the differences in the imbalances of the government budgets and the destabilizing effects of government overspending on the rest of the economy, as shown in the statistical sections. Also, there are important differences in the size and type of distortions caused by government interventions in markets. Although recently many shock-type changes have occurred in a number of Latin American countries, available indicators show that price distortions are smaller in South Korea and Taiwan than in most Latin American countries. Also, average nominal rates of protection are lower and the export incentives are higher in many countries in South East Asia than in Latin America (Erzan *et al.*, n.d., and Agarwala, 1983). It is true that there are wide differences among the incentive rates given to sectors in many countries in both regions. In some cases these differences reflect the power of rent seekers to lobby, and can consequently be regarded as distortions that hamper efficient use of available resources. However, measures to protect and stimulate industry can also reflect strategic choices that are part of a longer-term strategy to develop technology and stimulate diversification of exports. A key element in the industrialization strategies of South Korea and Taiwan has been temporary protection for potential export firms on the domestic market and price discrimination. Preferential credit allocation by the government enables these firms to improve their productivity and international competitiveness.

The characteristics of the so-called developmental State in South East Asia, including Japan, have been discussed elsewhere and need not be reviewed here. Briefly, they are:

- i) a strong State that steers firms by means of price signals, regulations and compulsion;
- ii) co-operation and frequent consultation between the State and the private sector in key areas such as trade, investment and technological development; and
- iii) predictability of policies and risk reduction for the private sector in order to stimulate investment and production.

The intense and strongly focused relationship between government and the private sector in these countries has played an important role in shaping efficient economies that are able to compete successfully in world markets on the basis of genuine competitiveness.

Technological development is the crux of the ECLAC strategy. In this context Fajnzylber made some observations on the critical contribution of government in creating a proper economic climate in which decisions on investment and production are made. The opening of the black box of technological progress, as Fajnzylber puts it, would require the transformation of a rent-seeking society into a society that is oriented towards savings, investment and competition (Fajnzylber, 1990, pp. 182-190). As follows from the experience of South East Asia, such a type of development can indeed be stimulated by an active government that intervenes in markets in many different ways without hampering efficiency and blocking international competition (van Dijck, 1989).

Some final observations are called for on the role of human capital formation in the process of development as envisaged by ECLAC. Absorption of technology requires not only investment in physical capital but also human capital formation. Moreover, skill formation is probably the single most important factor contributing to the alleviation of poverty. Education, therefore, should be the heart of any policy focusing on the twin objectives of technological development and social equity. A well-educated and highly trained labour force is required in order to develop comparative advantages in dynamic markets and generate more value added in manufacturing and the processing of primary products. Training and skill formation have contributed greatly to the dynamism of the densely populated economies of South East Asia, where initially comparative advantage was based on low wages and poor labour conditions.

Austerity –that is to say, savings and investment– and education are the two engines of economic growth with equity, and a fundamental shift in policy is required to reverse the declining investment rates and the cuts in government spending on investment, education and services that are of critical importance for alleviating poverty.

## Appendix

## SOURCES OF VARIABLES

Variables 1-6, 8, 9, 11, 13, 15, 22-27:	The World Bank, <i>World Tables, 1988-89</i> , Washington, D.C.
Variable 7:	UNCTAD, <i>Handbook of International Trade and Development Statistics</i> , several issues, Geneva, United Nations.
Variables 10, 12, 14:	IMF, <i>International Financial Statistics</i> , several issues.
Variables 16, 28, 33:	UNDP, <i>Human Development Report 1990</i> .
Variables 17-21:	World Bank, <i>World Debt Tables</i> , several issues.
Variable 29:	FAO <i>Yearbook: Production</i> , several issues.
Variables 30, 31, 32:	United Nations, <i>Report on the World Social Situation</i> , several issues, Geneva.

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## Consolidating democracy and development in Chile

*Osvaldo Sunkel\**

The transition to democracy in Chile has been achieved in an unusually rapid and successful manner. Its consolidation is only just beginning, however, and is faced with serious challenges which will call for extensive and complex efforts in the years to come.

At the political level, it will be necessary to do away with the institutional anomalies originally agreed to for facilitating the transition, to overcome the anachronisms that built up before and during the long spell of authoritarian rule, and to enhance the social and cultural dimensions of the democratic process. In the economic sphere, it will be necessary to strengthen the process of outward growth by promoting an industrialization-based form of export development—capable of further strengthening future structural dynamics both in terms of the country's place in the international economy and its domestic linkages—through a concerted strategy of "development from within". At the social level, the greater structural heterogeneity generated by the need to attain international competitiveness will call for redoubled economic and social efforts and the highest level of effectiveness of public policies, including profound conceptual and institutional changes in them in order to make significant advances toward basic macrosocial balances. All this, coming as it does on top of the wild swings observed in the past from the excesses of Statism to those of neoliberalism, and the new domestic and external challenges now being faced, calls for a profound reform of the State, which must be transformed into the socially negotiated institutional expression of the above-mentioned interrelated political, economic and social changes. If these changes mutually strengthen each other, this will strengthen in turn the possibility of consolidating development and democracy. If we fail in one of these fields, this could lead to growth without democracy, or democracy without growth, or—if the worst comes to the worst—to a situation where there is neither democracy nor growth.

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This article is an abridged text of the address delivered by the author on 6 April 1992 in the Hall of Honour of the University of Chile, on the occasion of his incorporation as a full member of the Academy of Social Sciences of the Instituto de Chile.

I have been examining many aspects and stages of the development of the region over the last four decades from the standpoint of the Latin American structuralist approach, which uses a historical, multi-disciplinary and transnational method.

The most recent stage has been characterized by an extremely severe economic and social crisis and drastic adjustment and restructuring policies which are generating serious political tensions in our democracies. This has caused me to concentrate on studying the current economic, social and political problems and their future prospects and, in particular, to undertake a critical review of the role of the State. This is why I have considered it appropriate to reflect on some of these questions on this occasion, since they seem to me to be particularly relevant to this moment of transition to democracy in Chile.

In contrast with other countries of the region which have gone through similar processes, two years after recovering our fundamental democratic institutions there is a widespread feeling in the country and among international observers that the *transition* has been a success and that it provides solid ground for the consolidation of democracy in the future. Once the initial priorities have been taken care of, however, concern begins to shift to more fundamental levels related to the economic and social content, and to the nature of civic interrelations and of political institutions. Consequently, there is a growing awareness that the *consolidation* of democracy in Chile displays the shortcomings and problems typical of a process which is only just beginning and still has a long way to go.

In this initial period, priority has been given to efforts to reach agreement on the changes which most Chileans considered indispensable and urgent in the first stage. Because of this, there was express recognition of the need to accept certain restrictions and even distortions of the democratic regime because these were laid down as essential conditions for the transition by powerful sectors linked with the previous regime which felt profound misgivings over what the restoration of democracy could mean for them and for the country.

In these circumstances, the new government has had to foster confidence among key economic and political sectors (such as national and foreign business circles, which are now leading social actors in the market economy), in the vitally important world of international finance, among the

opposition parties, and within the armed forces themselves, which had only just vacated the government.

It has also had to foster the moderation, understanding and support of the majority social and political sectors of the centre and the left. These sectors had long been systematically ignored or persecuted, and their access to and participation in the cultural, social, economic and political life of the country had been seriously restricted by means which included exile and violations of human rights. This was especially so in the case of the leaders and active members of left-wing parties and movements.

Thus, the political spectrum of the country –which had displayed extreme discrepancies and conflicts before the military coup– is now tending to converge towards centrist positions. The main political currents define themselves as centre-right or centre-left, and one current even calls itself “centre-centre”. This is a direct consequence of our stormy history of the last two and a half decades, but it is also due to the far-reaching changes which have taken place in the international geopolitical, ideological and economic context. The prevailing disposition of the most significant political currents and social actors has therefore been to play down, moderate and reduce controversies, often avoiding tackling them head-on and putting them off into the future.

This relatively cosy situation should not and cannot be a reason for passivity and complacency. On the contrary, it provides grounds for carrying out a very necessary and urgent exercise: to shift our attention from immediate and urgent matters and contemplate the medium- and long-term future. This should not be misunderstood or seen as an unjust criticism, for I fully acknowledge that important initiatives are already to be observed in this respect in various spheres of national life.

I am firmly convinced, however, that it has become an urgent and top-priority national task to begin to devote more explicit, systematic and decided attention to building a Chile which can enter the twenty-first century with an institutionally normalized, socially integrated and politically cohesive democracy and a dynamic, flexible and innovative economy capable of eradicating poverty and creating suitable conditions for greater equality of opportunity, while at the same time generating new capabilities for winning fresh positions in the world economy. All this must be accompanied by a process of cultural renewal which can combine the international trends towards greater homogenization with

the maintenance of variety and pluralism in an effort to build a national identity on the basis of the values of an authentically democratic culture which combines our own special features with those of universal scope, reconciles human and spiritual values with the specific demands of science, technology and efficient organization, and unites tradition with innovation and modernity.

In the limited time available to me, I shall briefly examine four subject-areas: one political, another economic, a third one social, and finally a subject-area –based on all the foregoing ones– which deals with the role of the State. I consider it essential to clarify these matters so that, now that we are well into the *transition*, we can advance towards the *consolidation* of democracy and development.

At the *political level*, the process has been complex, with positive aspects predominating over some serious shortcomings. All in all, however, the situation now is that the executive and legislative authorities have been legitimately elected; the fundamental freedoms of opinion, assembly and association have been restored; there are political parties which freely exercise their functions of supporting or opposing the government; the rule of law now prevails to a reasonably satisfactory degree, with due separation of the powers of the State; and human and civil rights have been restored. From this point of view –that of the procedures and forms of political coexistence inherently associated with democracy– it could even be accepted that in many respects the transition has already been accomplished.

It is also obvious, however, that some of these procedures suffer from serious shortcomings. Some of them are the result of the institutions inherited from the previous regime and the conditions negotiated in order to ease the transition. They are well known to all, and for our purposes it is sufficient merely to note that they have the effect of creating situations of political, economic, institutional and legal privilege for those who were leading figures in the military government.

As the transition to democracy progresses in a generally satisfactory manner, there is growing acceptance of it by those who previously mistrusted it. However, concern is beginning to be shown by other sectors of society who, now that they have fulfilled their desire to recover a democratic political regime, want it to be reflected in greater achievements at the economic, social, cultural and legal levels. Thus, for

some the reasons for these safeguard clauses are gradually disappearing, while for others there is a growing perception that they represent increasingly unjustifiable anomalies.

These clauses played a stabilizing role in the early phases of the transition. Now, however, they are beginning to have the opposite effect, since they are introducing a systematic bias in favour of minority political currents and actors which supported the military regime, and they often produce domestic and international friction and tensions in civil-military relations in circumstances which should not give rise to major problems if these anomalies were eliminated. They thus form a constant source of irritation, frustrations, conflict and pressures for the normalization of the political regime and the reform of the Constitution and the legal system.

There are other political problems, of a more general nature, which are connected with the ongoing process of perfecting democracy. These include, for example, the possibility of reforming the Presidential system in order to make it more flexible and improve the balance between the Executive and the legislature; securing greater participation and representation of the masses and of the various social agents at the national, regional and local government levels; agreeing on legislation which is more in keeping with actual conditions and social values in such areas as the status of women and youth and in regard to such issues as abortion and divorce; recognizing the urgent need to review the legislation and institutions concerning the environment; and modernizing the public administration and public action in general, especially with regard to the social sectors. Among these, I think that priority attention is particularly necessary with regard to the deplorable state of the judicial services and their inherent inability to meet the needs of the popular sectors.

These and other similar issues have been increasingly prominent in public debate, and some of them have managed to find a place on the agendas of the political authorities, so that they have been, are, or will be the subject of legislation. Thus, the more permanent institutional features of the State are gradually taking shape, even though the political bias referred to earlier means in practice that the parliamentary process is still not democratically representative. This could have serious consequences: broad sectors of the population which are under-represented could feel that the emerging set of institutions lacks political legitimacy.

In addition to the limitations of the legislature, due to the peculiar electoral system and the institution of the "designated senators" who were not elected by popular vote but appointed by the previous régime, there are the constitutional and legal restrictions which hamstring important powers of the Executive, especially with regard to its relations with the Armed Forces. Even more serious, in my opinion, is the situation with regard to the legal system and especially the Supreme Court. The generally accepted fact of their anachronism gives rise to skepticism among the population with regard to their authority, respectability and effectiveness, and this weakens the perception that the rule of law prevails in Chile, which is of the essence of democracy. I therefore believe that if certain State authorities continue to display these characteristics, this will seriously hinder the consolidation of democracy in the minds of the population.

The main political task of the moment is therefore to overcome this anomalous situation. In order to do this, it is necessary to press on tirelessly with the dialogue- and negotiation-oriented attitudes, dispositions and procedures which were so successful in overcoming the critical initial phase of the transition. It is also necessary to advance in the process of their social extension and enhancement from the political elites to the other social sectors and actors and the population as a whole. The values of a democratic culture must be assumed to the full and the representativeness and efficacy of the institutions which regulate their functioning must be further perfected. The social leaders in general, and the political parties in particular, have a historic responsibility in this task, especially when political controversy is heightened in the periods before electoral processes or debates on fundamental reforms.

In its *economic aspects*, the Chilean transition has been even more highly praised than in its political dimension, since the contrast with most of the other countries of the region is particularly marked. There is no doubt that during the military regime fundamental and vitally urgent corrections were made in key aspects of economic policy. Nevertheless, there are still some decisive tasks to be carried out. Without prejudice to the important initiatives which are already under way, it seems to me to be essential to draw attention also to the need to heighten and generalize concern and reflection over medium- and long-term problems.

Chile is a small country, geographically distant from the great centres, but it is increasingly part of

transnational circuits in the spheres of culture, the environment, technology, economic matters, and politics. This is an inevitable and irreversible feature of the current situation, and it offers both advantages and drawbacks. In order to minimize the latter and take advantage of the former, the country must make a major effort to meet the unavoidable challenge of forming part of a world society which is rapidly becoming more and more globalized. As we are not outstandingly significant in terms of geographical size or population and we do not enjoy a strategic geographical location either, we can only interact advantageously with the rest of the world on the basis of quality, creativity, efficiency, seriousness and competitiveness in all our international forms of expression. This calls for an exceptional degree of social cohesion, discipline and co-operation, and poses demands on which I shall dwell later in this presentation.

With regard to internationalization, I cannot resist mentioning a coincidence which I only noticed when I was writing this address, after the date and place of this ceremony had been decided. The only previous occasion on which I had the honour of speaking here was on 17 November 1966, when I gave one of the inaugural lectures of the Institute of International Studies, whose twenty-fifth anniversary was celebrated only a little while ago in this same hall. My presentation on that occasion was entitled "National development policy and external dependence".<sup>1</sup> In it, I noted that the cycle of the expansion of industrialization through import substitution was becoming exhausted and that a radical change of course towards an export strategy was becoming essential. Indeed, the corresponding section of my presentation was entitled "Export or die". I also drew attention to the emerging phenomenon of the great expansion of transnational corporations and the dangers that this involved, alongside the opportunities it offered. In order to take advantage of the latter in terms of transfer of technology and export promotion, I proposed a form of association which I called "co-production": similar to the current "joint ventures".

<sup>1</sup> Reproduced in *Estudios Internacionales*, Institute of International Studies, Santiago, Chile, April 1967, and in the *Journal of Development Studies*, London, October 1969.

The success achieved in recent years by the Chilean economy on international markets has been based, on the one hand, mainly on recognition of the vital need to progress from an inward-looking development strategy to another one based on the idea of incorporating the economy into a new international setting: something which was already clearly perceived at that time. On the other hand, it is also based on the establishment of a suitable framework of macroeconomic conditions, greater confidence in and expansion of the role of the market and private economic agents, and a great effort of entrepreneurial innovation. In my opinion, making this urgently needed change of course was the most important function fulfilled by the military regime's economic policy.

It is only fair to acknowledge that in achieving this the regime had the advantage of considerable existing production potential inherited from previous decades, in the form of already evaluated natural resources, energy and transport infrastructure, industrial, forestry and agricultural production capacity, experienced entrepreneurs and skilled human resources. Far-reaching structural and institutional changes had also already been effected, which permitted better use to be made of these resources. In technical terms, there was a new and more favourable set of initial conditions for growth.

At the same time, however, this economic reorientation process also meant great social sacrifices: a long period of high unemployment and considerable declines in real wages, with abnormally high rates of profits, resulting in a deterioration in income distribution and heavy concentration of ownership of assets.

The most positive aspect of these changes was the great qualitative and quantitative improvement in the form of incorporation of the Chilean economy in the international setting. Even here, however, there are no grounds for complacency. Nothing guarantees that this dynamism will be of a lasting nature, for it contains contradictory tendencies: on the one hand, an ongoing learning process regarding the winning of external markets and the development of international links, which must be further strengthened in order to make it a cumulative phenomenon, but on the other hand a probable slackening of this dynamism as the momentum of the once-and-for-all changes in initial conditions gradually wears off. After an exceptional first phase, in many cases this

momentum is entering, or may enter, a stage of diminishing returns.

The main institutional and economic policy changes have already been made. The exceptional rates of profits are tending to level off under the pressure of the drop in the real exchange rate and the increase in domestic and foreign competition. Wages are going up again with the reduction in open unemployment and the renewed organization of the working class. The most easily accessible external markets are beginning to show signs of saturation, and new competitors are arising in the form of countries which have adopted or are adopting export strategies of a similar nature. The installed capacity of both the infrastructure and production facilities is reaching its limits. Renewable natural resources are suffering from over-exploitation, while the non-renewable resources are showing signs of exhaustion. Entrepreneurial dynamism and innovation, which are found primarily, though not exclusively, in big firms, now face the challenge of linking up with and spreading to medium-sized and small enterprises, and even micro-enterprises.

New initiatives and greater efforts are needed, both to offset these constraints and to support the new capabilities which have been acquired, for the praiseworthy level attained by exports is not enough: it is necessary to maintain and even increase its growth rate. In a dynamic context, growing as fast as the rest really means standing still: in order to progress it is necessary to advance at a relatively faster rate. It is not enough to continue to follow the established paths: what is needed is to create a recurrent dynamic of structural change with regard to markets, products, processes, organization, technology and resources.

This means moderating consumerism and increasing the investment and saving effort; heightening the process of innovation, incorporation, adaptation and exploitation of scientific and technological knowledge; penetrating new markets and further enhancing the present ones; boosting and modernizing upstream and downstream linkages with domestic production sectors and entrepreneurial circles by connecting them with the export sector; bringing the informal production sector into the trend towards modernity; using the production potential of renewable resources on a sustainable basis through a form of management which preserves the ecosystems on which their survival depends; finding substitutes

for non-renewable resources which are becoming depleted; and advancing towards the export of products with higher added value and technological content.

A particularly important aspect in successful export economies has been the changes made in business organization, both within enterprises and in their relations with each other and with the State and workers. This last aspect includes the provision of greater stability, better status and enhancement of skills of the workers and their active participation and collaboration with a renewed entrepreneurial sector in the management and improvement of production: all crucial factors which raise productivity and decisively aid in achieving flexibility, efficiency, discipline and cooperation.

In the final analysis, what is involved is promoting an "industrializing" form of export development through policies designed to increase the proportion of the fastest growing exports in international trade and to link up other branches of production and domestic entrepreneurial strata with the expansion of the export sector.<sup>2</sup>

This set of structural and institutional policies is particularly important at the present time, when the leeway for traditional economic policies is extremely limited for both domestic and international reasons.

In some of these aspects, important private and public initiatives already exist or have been proposed. A matter of concern, however, is the lack of a generalized national awareness of the need for a renewed collective effort of sufficient scope, persistence and coherence. This effort should involve the various economic and social actors in an informed and systematic process of forward-looking exploration, investigation of possible and probable scenarios, and shared reflection on basic orientations and priority actions aimed at the medium and long term. This means concentrating limited resources in order to identify and make the best possible use of the available production potential and the opportunities offered by an extremely competitive and difficult international setting. It must also be understood that it is impossible to meet all social demands in a satisfactory, simultaneous and immediate manner, so that it

<sup>2</sup> Osvaldo Sunkel (ed.), *El desarrollo desde dentro; un enfoque neoestructuralista para la América Latina*, Fondo de Cultura Económica, Serie Lecturas, Mexico City, 1991; English version: *Development from Within: Toward a Neostructuralist Approach for Latin America*, Lynne Rienner Publishers, Boulder, CO, 1993.

is essential to define priorities and seek concrete trade-offs between what is feasible at the present moment and what can only be achieved gradually. This calls for the preparation of future scenarios in which the various sectors of Chilean society, especially the most underprivileged ones, are able to see that they will have a place for which it is worth striving.

We have learnt that while the market constitutes an indispensable system of signals for ordering economic transactions, it is not sufficient for settling these types of questions, which call for major strategic decisions. These decisions must be arrived at collectively through a prospective and properly socialized planning mechanism which stimulates and helps to generate proposals and initiatives that supplement those emerging from the market itself. No truly modern organization, institution or enterprise can be without this function and its corresponding set of institutions. In the past, Chile invented an exemplary planning institution for carrying out a function of historic importance: namely, the Corporación de Fomento de la Producción (CORFO). It must now invent a new set of institutions in line with the conditions and needs of the present and those anticipated for the future. Here, too, the social actors and the State, together with the political parties, have a fundamental contribution to make from their own respective standpoints.

Let us now move on to the question of *social affairs*, which is undoubtedly the most difficult of all. The unavoidable effort currently being made by the country to find the best possible place in the international economy cannot be successful or sustainable unless it is accompanied by a thorough-going change in forms of domestic organization and cooperation. Little attention has been paid to the fact that the dynamics of transnational integration often generate conditions of social segregation within the country.<sup>3</sup> This may be seen in the various sectors of economic activity, where new enterprises are set up and those of the greatest innovative capacity are restructured to compete in international and domestic markets. This means new and well-paid jobs of high productivity for some employees, but it also means unemployment for the workers displaced from the restructured

enterprises and from those which are not able to stand up to the new competition.

Divergent trends are thus generated between those who enter the modern sector of high productivity which is in the process of internationalization and those who sink to an inferior level of employment in low-productivity jobs, underemployment or self-employment, swelling the ranks of the informal economy and the poor. Unfortunately, when matters are left to the free play of market forces, the former tend to be much fewer than the latter, in view of the growth of the population and of the labour force, the severe demands for restructuring deriving from policies that foster liberalization, privatization and international competition, the massive incorporation of capital-intensive technology, the insufficient investment effort, and the lack of skills, education and suitable work habits on the part of much of the active population.

In this way, a new situation of structural heterogeneity with features different from those of the past is being built up. It discriminates against older persons, the big contingents of young people without work experience, and women, especially if they are heads of households and do not have the necessary skills. In contrast, it favours urban adults with better qualifications and skills, greater initiative, and the ability to gain access to the segmented labour markets.

Thus, in the different productive sectors, in the regions, in urban and rural areas and in the different social strata, we have a situation of coexistence, in very unequal proportions, of modernity and backwardness in production activities, affluence and poverty in terms of income levels, and sharp environmental contrasts which give rise to tremendous cultural, institutional, political and demographic differences which tend to be self-reproducing. Consequently, the new generations living in a state of poverty have few possibilities of escaping from it. Economic growth, although without doubt an indispensable condition for tackling this situation, nevertheless does not represent the solution in itself. Without institutional changes and effective economic and social policies, it may even accentuate inequalities and contribute to discrimination and social conflict, criminal behaviour, political confrontation, and dissatisfaction, instability and social violence in general. Ultimately, it threatens all that has been

<sup>3</sup> Osvaldo Sunkel, *Integración transnacional y desintegración nacional*, *Estudios Internacionales*, Santiago, January-March, 1971. English version: "Transnational Capitalism and National Disintegration in Latin America", *Social and Economic Studies*, vol. 22, No. 1, Jamaica.

achieved in recent years: the incipient democracy, some fundamental points of consensus, and the indispensable economic growth itself.

We know that substantial efforts have been and are being made in these respects. In this connection, special mention may be made of the change of emphasis from basically assistance-oriented policies to productive policies designed to establish suitable conditions for the permanent elimination of marginality. The task is of daunting scale, however. It is not just a question of the enormous deficits already built up: the "old poverty" inherited from the previous economic model, and the "new poverty" generated by the change of model, the crisis, the adjustment and the restructuring process. In addition to this, it is necessary to halt and reverse the effects of the mechanisms tending to reproduce inequality through the differences in conditions of access, quality, efficacy and permanence with regard to both the infrastructures and services aimed at providing assistance and those designed to support productive activities.

New forms of public and private institutions are required. In particular, imaginative additional efforts by the private sector are needed in the field of labour relations and cooperation within the enterprise, which includes the types of relations now recognized as being crucial factors in entrepreneurial superiority and success. A change of priorities and greater efficacy is also required in public expenditure and management, together with additional transfers of assets and income between sectors of production, regions and social strata, through truly progressive approaches to public income and expenditure.

Quite apart from their ethical grounds, the elimination of poverty, the reduction of inequalities, the search for equity and the opening up of an attractive horizon of opportunities are pressing needs for the consolidation of democracy and the firm establishment of a dynamic and modern economy.

I must stress at this point the need for special concern for youth, which forms a large proportion of the population. It is the section which is most seriously affected by unemployment and discouragement, which is most exposed to all kinds of risks, and which has the greatest need for opportunities and above all for encouragement, understanding and hope.

I feel that the great scope of the social task calls for profound conceptual and institutional changes.

Economic policy, for example, has well-defined priority objectives of growth, macroeconomic equilibrium and price stability, and to help establish these objectives there are a number of institutions comprising the Ministry of Finance, the Central Bank, the Department of the Budget and other bodies, with suitable procedures for control of activities, programmes and projects, evaluation of the results, and monitoring of extensive and timely statistical information. There are even international institutions, both public and private, which follow up, supplement and backstop the domestic ones.

In social matters, which should really be the ultimate objective of economic policy, something similar is called for. Thus, just as everyone accepts the need to achieve basic macroeconomic equilibria, it is also necessary to achieve "basic macrosocial equilibria". This notion is implicit in political action at the highest level and should be reflected in an institutional organization which gives greater effectiveness and coherence to the work of the government in these fields. Notwithstanding the praiseworthy efforts and achievements which have been made in the area of coordination, social policies and actions are in fact still organized on a sectoral basis, through multiple programmes carried out by a number of different ministries. Moreover, they are affected indirectly, and more often than not implicitly, by the economic policies adopted. This institutional weakness is the result of having assumed in the past that economic growth and stability would inevitably result in social improvement. As this assumption was not fulfilled in practice, the social services were gradually expanded in the course of time, resulting in a set of sectoral policies supplemented with special programmes and projects. More recently, part of these services (those servicing the higher income groups) have even been privatized.

It is essential to set up an institutional structure of sufficiently high political level and operational capacity to secure the effective integration of social policies both with each other and with economic policy. This presupposes theoretical and conceptual work to define priority objectives, identify and specify their content and determinants, and permit the formulation of the corresponding policies, including the systems of information, management, follow-up and evaluation. I consider this to be an indispensable task for progressing more resolutely towards the elimination of poverty, the reduction of social inequalities and injustices, and the opening up of an horizon of opportunities which will be attractive

above all to young people, for without this it will be very difficult to achieve the social stability and co-operation needed to consolidate democracy and development.

This brings me to the need to make a critical and dispassionate review of the *role of the State*. Firstly, as I hope I have already clearly shown, the action and reform of the State in the political, economic and social fields are essential if those objectives are to be consolidated in conjunction. Secondly, to a considerable extent the State should be the organic institutional expression of the interrelation between those fields. If these conditions mutually strengthen each other, then this will also strengthen in a synergistic manner the possibility of consolidating development and democracy. Failure in one of these tasks could result in a situation where there is growth without democracy, democracy without growth, or, in the worst of all events, neither democracy nor growth. Thirdly, it is essential to dispel the excessive ideologization currently prevailing in these matters, in order to be able to debate in a rational manner the general lines that should guide their reorganization in the future.

For this reason, it is also desirable to shift our attention for a while from the problems and tasks of the present and examine the changing role of the State from a historical perspective.<sup>4</sup>

After the Great Depression of the early 1930s, the State came to play a leading role in the development and structural transformation of the Chilean economy and society. It took on new functions of intervention in the markets for goods and services in order to reorient the economy towards industrialization and modernization; it made itself responsible for the financing of long-term investment projects and programmes, in order to make up for the absence of a financial market which would support the development of private activities in industry and other sectors; it took income redistribution measures, creating and expanding the infrastructure and the public social services for health, education and culture, housing and town planning, and social security and insurance; it made State investments in infrastructure in order to secure the physical integration of the domestic market through the modernization and expansion of the national transport, communications and

energy services; it set up public enterprises in industries where private enterprise was not interested or unable to do this; and it generated employment opportunities in the activities in question, thus contributing to the training of skilled human resources and the formation of a substantial organized wage-earning sector and a substantial middle class made up of entrepreneurs, non-manual workers, technicians and professionals.

In this respect, Chile was doing no more than following world trends. After the golden age of nineteenth century *laissez-faire* there was a profound crisis of capitalism which lasted from the First World War to after the end of the Second World War, including the turbulent 1920s and the great crisis of the 1930s. During this period there were great economic, social and political changes aimed at tackling and reversing that crisis and its consequences.

The first of these great changes was the Socialist Revolution. As is well known, in the economic changes that took place in the Soviet Union and in the countries where that nation imposed its model, the State took total control of the economy, and through a process of centralized planning it carried out far-reaching structural changes and forced ahead rapid processes of economic growth and social improvement.

State action was also resorted to within the capitalist area in order to tackle the difficulties that arose. This was so, for example, in the fascist corporative regimes established in much of Europe in the 1920s and 1930s. The Scandinavian and Anglo-Saxon countries, for their part, developed the Welfare State and the New Deal, which represented unprecedented State intervention in the economy in order to overcome the crisis, redistribute income and cure the cyclical instability of capitalism. The underdeveloped countries of Latin America, Africa and Asia turned to the developmentalist State in order to carry out modernizing changes in those backward peripheral societies.

In contrast with the "black legend" which has been woven in recent years around this period, the empirical evidence shows beyond any doubt that those policies were very successful for several decades. From the late 1940s until the 1970s, the majority of the capitalist countries, whether developed or underdeveloped, registered unprecedented rates of economic growth and of improvement in material well-being. Although this may seem paradoxical in

<sup>4</sup> Osvaldo Sunkei, *Auge, crisis y renovación del Estado: una perspectiva de largo plazo*, in Matías Tagle (ed.), *Los desafíos del Estado en los años noventa*, Foro 90, Santiago, Chile, 1991.

view of their current collapse, the same was true of most of the socialist countries.

As well as making a very necessary reappraisal of the role of the State in this period, however, it is also necessary to make a critical review of it, since that historical cycle entered into a stage of decadence and reached its end in the 1970s, when the mass of new functions that the State was assuming gave rise to contradictory trends which became more and more acute with time.

In the economic field, the State intervened in the market to an ever greater degree, but with less and less justification, hindering and distorting its indispensable complementary function in the allocation of productive resources, with increasingly negative effects on their proper use, efficiency, competitiveness and growth. In the financial field, the State displayed an insatiable hunger for fresh resources in the face of growing resistance to increased taxation, thus heightening inflationary pressures and wage demands and reducing profit margins, thereby discouraging the private sector. In the institutional field, there was excessive bureaucratization, interference and administrative controls in economic and social life, giving rise to growing rigidity and arbitrary actions and leading to the questioning of the political legitimacy of the State. In the economic and social field, there was a heightening of the conflict between the crushing weight of the State apparatus and the strengthening of aspirations for greater participation, decentralization and freedom in both individual terms and with regard to civil organizations. In international relations, there was a worsening of the imbalance between the processes of transnationalization of the economy, finances, society and culture and the efforts of individual States to restrict, limit and control these processes. These and other contradictions ended up by causing the expansionary phase of State interventionism to run out of steam, and they finally caused its terminal crisis.

In Chile, the above-mentioned contradictions gave rise to some important reorientations of a more market-oriented type already in the 1960s. With the arrival of the Unidad Popular government, however, the functions of the State were greatly expanded, even involving the replacement of the market with generalized price controls and the nationalization of the banking system and much of the system of production, leading to economic and financial chaos which was socially and politically unsustainable.

The military government adopted a radically opposite programme, characterized by unrestricted and indiscriminate support for the market mechanisms and private enterprise through liberalization, deregulation, opening up to the exterior, the privatization of public enterprises and services, and reduction of the size and functions of the State. Not only did it reverse the policies of the socialist government in this way, but it also dismantled and replaced even the more moderate forms of State interventionism which had grown up in previous decades.

This set of policies was carried out in a strongly regressive manner, with the whole weight of the drastic process of adjustment and restructuring being placed on the shoulders of the lower and middle classes. There was a considerable increase in unemployment, underemployment and informal sector activities; incomes and wages went down; the tax burden of these sectors was increased; and the public services in the fields of education, health, housing and social security suffered cuts, went down in quality, and became more expensive. All this was in sharp contrast with the succulent benefits received by the minority sectors which enjoyed privileged conditions for gaining access to the processes of privatization, deregulation and greater external openness and participating and obtaining benefits from them.

Fundamentally, the outbreak of the structural crisis of the Chilean State in the 1980s had three main roots in my view. The first –the most widespread and deep-rooted– was the long-term tendency of the rise and fall of the State cycle, which began with the years between the wars and ended in the 1970s. The second was the all-embracing but unsuccessful attempt at State control and socialization promoted by the Unidad Popular government between 1970 and 1973. The third had its origins in the drastic neoliberal policies applied as from 1975 and subsequently further intensified on account of the debt crisis and the adjustment and restructuring policies.

The sharp pendulum-like swings observed in the role of the State in Chile in recent times have had heterogeneous and complex effects on its structural, institutional and functional characteristics. No realistic, balanced and detailed diagnosis is yet available of the true nature of the State apparatus which we have inherited. In the meantime, we are facing new historical conditions and there are novel problems

and challenges for national development and its effective interaction with the world context, including those which I referred to in earlier sections. This brings me finally to posit the urgent need to tackle the question of reform of the State in all its magnitude and scope.

It is necessary to start a broad-ranging, pluralistic and well-informed debate on the nature and characteristics which the State should have in the future in order to overcome its current shortcomings and appropriately meet, *inter alia*, the new objectives, realities, challenges and tasks noted earlier in this presentation. It will be necessary to make the greatest possible collective effort to bring the interests of the pressure groups in line with the common good of society, to identify and overcome as far as possible the ideological skews which characterize the different schools of thought on these matters, and to make use of the greatest possible realism, basing our efforts above all on the critical and dispassionate analysis of our own experience, as well as that of other

countries. Despite its occasional distortions, its vicissitudes and its current detractors, we have the advantage in this of having a respected and fruitful tradition of public service and of a "State in due form", as Alberto Edwards called it some time ago. The path which the State has followed in the course of our history as a Republic deserves the deepest respect, which can and must be recovered. The fact is that even though the State has lost some important functions, it undoubtedly represents –if I may be excused the use of an "economicistic" expression– one of the most important comparative advantages of our country.

In my opinion, the problems of the State, together with those which I referred to in the political, economic and social fields, form the main challenges, and their solution represents the most crucial task, if the successful transition which we have experienced so far is to be converted effectively, as most of us wish, into a process of consolidation of democracy and development in Chile.

## Development pattern and environment in Brazil

Roberto P. Guimarães\*

After describing the present situation of ecological transition, which is one of the factors in the economic, institutional and environmental crisis of present-day society, the author tries to identify the main features of the industrial and agricultural expansion of Brazil, highlighting the socio-environmental impact of the style of development pursued by that country since the war. On the basis of this diagnostic study, and especially of the technical background material prepared for the drafting of the National Report presented by Brazil at the United Nations Conference on Environment and Development (UNCED) (Rio de Janeiro, June 1992), the author describes the main requirements and components of a sustainable industrial and agricultural development strategy which will permit both proper management of the country's natural resource endowment and the maintenance of the environmental quality of the Brazilian ecosystem, while at the same time ensuring satisfaction of the basic needs of present and future generations.

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*The first thing you will see is  
the smoke from our chimneys.  
That smoke means food  
and drink to us. It is the healthiest  
thing in the world in every way,  
especially for the lungs...*

Charles Dickens (*Hard Times*, 1854)

### I

## Styles of development, the ecological transition and the environmental crisis<sup>1</sup>

If this final part of the century had to be summed up in a few words, it could be characterized as the exhaustion of a style of development which proved to be ecologically destructive, socially perverse and politically unjust. In this respect, the clear signs of vulnerability of our planet's whole ecosystem have acted as a great sounding board for the various individual processes of "depletion" which we are witnessing, linked together in an inflexible logic whose inescapable conclusion is the need for far-reaching changes. The debate on the new development model for Brazil is thus only a first step towards defining the significance, the direction and the limits of the transition to sustainable development.

The most obvious manifestation of the current crisis is undoubtedly the fact that we are living in an era of shortage of resources, difficulties in expanding the economic base of our national societies, saturation of the dumps for storing or eliminating the waste products of the industrial society, and above all an era with a feeble capacity of response by local, regional and world institutions to the challenges posed by this crisis. Although the crisis is of course of an environmental nature (progressive depletion of the natural resource base and reduction of the recovery capacity of the ecosystems) it is above all a political and institutional crisis, directly related with the power systems governing the possession, distribution and use of society's resources, which ultimately leads to a situation of either total shortage (complete exhaustion of our resource endowment) or relative depletion (unsustainable consumption patterns or inequitable access to those patterns).

<sup>1</sup>For more comments on this subject see Guimarães (1991b).

The incorporation of an ecological dimension into the public decision-making process—in order to take account in advance of the repercussions of public policies on the network of relationships which affect the ecosystems—is not only a reasonable aspiration but a veritable biological necessity for the proper maintenance of the natural systems which make life possible. This aspect of the present situation means that we must recognize that mankind is passing through a period of authentic ecological transition (Bennett, 1976). Among other dimensions, the present stage of the transition is characterized, in energy terms, by the tendency to use energy more and more extensively for the satisfaction of human needs, but also more and more inefficiently. Even more important, perhaps, is the fact that ecologically there is not only an increasing accumulation of goods for social uses not directly related with biological survival, but also the possibility of attaining this objective through the exploitation of environments increasingly far removed from local society.

It is not surprising, therefore, that the great majority of present-day institutions—established under the sway of the economic dogmas of abundance and material progress—are proving to be incapable of facing up adequately to the challenges of the transition. This situation naturally leads to the questioning of an internationalized style of development which is manifested mainly in the processes of modernization of agriculture, urbanization, appropriation of the natural resource base and use of non-renewable energy sources. The global and interdependent nature of society in these final years of the century does not manage to conceal the persistence of the North-South dimension, even in ecological matters. In the highly industrialized economies, environmental problems can generally be assimilated to pollution, so that their environmental policies are oriented towards avoiding even more serious degradation or even seeking to restore the patterns of water, air and land quality which existed before the crisis, while in the underdeveloped countries, the environmental crisis is clearly associated with the exhaustion of their resource base, and their policies should therefore give priority to rational natural resource management. However, this distinction has lost much of its validity, especially in the countries of the South, which are faced with situations of environmental degradation characteristic of the

impoverishment of their natural resource endowment, as a result of their underdevelopment, at the same time as situations normally associated with an “excess” of development. In this respect, not only has the economic gap between North and South grown still wider in recent decades, but there has also been an increase in the environmental and ecological disparity between the two worlds. It is blatantly obvious that the countries of the South are at the more vulnerable end of this dichotomy and are suffering the consequences of world degradation.

In short, the world is faced with the following alternatives: to continue with the present pattern, in which the more highly developed countries make intensive use of natural resources, allowing their population to enjoy a high level of consumption which contrasts with the shortages in the underdeveloped world, or to review these patterns in search of a model which puts less pressure on the natural resource base and permits more equitable levels of development. This model presupposes a new international division of labour involving far-reaching industrial retrofitting, changes in the consumption habits of the developed countries, and greater international solidarity in the sense of facilitating the access of the less developed countries to scientific and technological advances.

At the same time, the issues before the world pose unprecedented challenges for Latin America as a whole and Brazil in particular. The environmental crisis comes at a time when the region is in an equally unfavourable situation in many other areas. Resuming the road to development involves strengthening democracy, but at the same time stabilizing the economy—which presupposes the solution of the external debt problem—, incorporating it into world technology flows, establishing more austere and socially homogeneous consumption patterns, and improving income distribution. Finally, there are more than a few institutional difficulties standing in the way of the establishment of a new style of sustainable development in Brazil. Since the mid-1980s, Brazil has gone through eight stabilization plans, the national currency has changed its name four times, exchange policy has been changed on 18 occasions, nearly 60 different price policies have been tried, and the number of wage policies is already close to 20. For a country with a background of political and

institutional instability as marked as that of Brazil, the search for a new pattern of industrial and agricultural development which will permit a more harmonious relationship with the functioning of natural

systems is an exercise which calls for daring and creative imagination on the part of the economic elites, political leaders, the working classes and the population in general.

## II

### **The Brazilian style of development since the war: broad elements of a diagnostic study<sup>2</sup>**

Up to the mid-1960s, the mainstay of Brazilian economic growth was import substitution, while protectionism was the basic instrument of the country's industrial policies. The main financing mechanisms were direct contributions by foreign investors and money issue, which generated "involuntary saving" by the non-business sector. The exhaustion of this pattern of financing coincided with the speeding up of inflation and the accumulation of balance of payments deficits, which culminated in the recession and political crisis of the early 1960s.

After 1964, fiscal and financial reforms made it possible to overcome the fiscal crisis and reduce inflation, creating suitable conditions for a second growth phase, in the 1970s, in which import substitution was supplemented with the expansion of industrial exports. The 1973 oil crisis undermined the bases of this model, however. The reaction taken by economic policy was to support growth through greater external indebtedness, avoiding major variations in the basic economic indicators such as the exchange rate, interest rates and real wages. In terms of the economic results obtained, it can be said today that the investment programme begun in 1974 produced undoubted achievements. Industry leapt forward in the metallurgical and chemical sectors and also registered considerable advances in the production of machinery and equipment. Exports grew and were diversified. A boost was given to technological

training. Consequently, the structure of production underwent substantial changes which materialized as the big projects came on line.

At the same time, the adaptation of the territorial structure to the industrialization plans served to consolidate the territorial planning strategies aimed at removing the material, political and ideological obstacles standing in the way of the expansion of modern capitalism. In reality, the aim was to impose a technical and political control network on the national territory through government planning. In this way, a complex territorial dynamic was built up whose focal point was the group of great urban centres of the South-Central region, which absorbed massive proportions of investment by the State and by transnational corporations. The metropolitan expansion axis linked the cities of São Paulo and Rio de Janeiro in a great and almost uninterrupted industrial zone which also incorporated part of the State of Minas Gerais and sent out tentacles towards Brasília (essential an administrative centre) and Espírito Santo (an important port, agroindustrial and steelmaking complex). In addition, another group of big cities was formed –made up of Belo Horizonte, Curitiba and Porto Alegre– which stood out by the rapid growth of their industry. A ranking of functions and power in terms of productive activities, distribution and resource management was thus created.

The maintenance of the extremely highly concentrated structure of land tenure resulted in the migration of large contingents of population to small towns, where they became a labour reserve for seasonal agricultural work, or to the big and medium-sized cities, where they swelled the ranks of the underemployed and unemployed. In some regions they became "prospectors" for deposits of valuable metals scattered over the national territory. It was thus that,

<sup>2</sup> With regard to this and the next section, see the technical background material prepared for the Brazilian National Report to UNCED by A. Barros de Castro; B. K. Becker and C.E. Egler; L. Guimarães Neto, S. Buarque and T.B. de Araújo; G. Martine; M.A. Ribeiro; Ch. C. Müller; A.C. de Souza Raes, and R.C. Aguiar. See also IBGE (1990); Guimarães (1991a).

in the economic and social and agrarian context, dramatic levels of rural and urban poverty continued to exist side by side with privileges with regard to land tenure, markets and participation in public resources. In the Northeast, the use of the admitted fragility of the regional economy due to the periodic droughts as an instrument for seeking differentiated treatment for the region led to a maze of subsidies and State protection impervious to the forces of competition associated with modern capitalism.

The social conditions in which the Brazilian population still lives after decades of rapid economic growth are only too well known. The rapid economic growth since the war, which turned a country whose level of development in the 1940s and 1950s was barely above that of the poorest countries of the region into the eleventh industrial power in the whole world, did not succeed in reducing the levels of economic and social inequality. On the contrary, in the period of fastest growth, between 1960 and 1980, the richest 10% of the labour force managed to increase its share of income from 40% to 50%, while the poorest 50% saw their share sink from a modest 17% to only 12% in 1980. Comparison of the available statistics for urban and rural areas clearly shows the spatial concentration of poverty in urban areas. In rural Brazil, poverty levels registered a downward trend throughout the 1970s and the early 1980s, though this trend levelled off in 1986. In urban areas, poverty went down from 35% to 30% between 1970 and 1980, but rose again to the level of 34% of the population in 1986.

The foregoing analysis makes it necessary to recognize that ecological problems reflect inequalities of a social and political nature (patterns of relations between human beings and the way society is organized) and also derive from structural distortions in the economy (the consumption patterns of society and the way it is organized to satisfy them). In Brazil, because of the size of the country's territory and population, the extent and diversity of its ecosystems, the complexity of the structure of production and the disparities in income distribution, the dilemma of sustainable development is expressed in the challenge of speeding up material development while at the same time improving social justice and securing good environmental quality. However, the homogenizing logic of economies of scale has bulldozed natural and cultural diversities which were seen as obstacles to progress. Considerable

parts of the national heritage, in the form of biodiversity and ways of life, have been sacrificed in the name of modernity, to the detriment of the quality of life of the population as a whole. It is hardly necessary to point out, in this respect, that in situations of extreme poverty, those who are marginalized from society and from the national economy have absolutely no commitment to avoiding environmental degradation, since society does nothing to prevent their own degradation as persons.

### *1. Evolution and impact of manufacturing industry*

After the Second World War and up to the mid-1970s, the capitalist economies registered some of the highest rates of economic growth and the greatest changes in the structure of production in the whole of human history, spearheaded by the industrial sector. This expansion was headed by two great subsectors: metal products and machinery (the motor industry, capital goods and consumer durables) and the chemicals subsector (especially petrochemicals). At an early stage, the United States style of consumption spread to the European countries and Japan, and the energy matrix was changed through the replacement of coal by oil. This style of consumption was accompanied by a technological, organizational and entrepreneurial pattern focused on industrial production and backed up by big corporations, which closely linked together the world economy, especially in the capitalist countries. As is well known, in the case of Brazil the great boost for capitalist expansion was provided by the triad formed by the State, transnational corporations and private national capital. The rapid establishment of the international industrial matrix in Brazil made it possible to internalize the production vectors of the chemicals and petrochemicals sector, metal products and machinery, the transport equipment industry, the timber, paper and pulp industry, and non-metallic minerals, all of which have a strong impact on the environment.

In general, the massive late industrialization of the Brazilian economy brought in technological patterns which were advanced for the national base but were outmoded in terms of the environment, with few technological elements for treatment, recycling and reprocessing. Leaving aside the particular features of each ecosystem, the impact of the industrial sector on the environment depends on three major

factors: the nature of the industrial structure in its different relationships with the environment; the intensity and spatial concentration of the various types and branches of industry; and the technological pattern of the production process – technologies for the filtering and reprocessing of effluents and the economic reutilization of byproducts.

In order to estimate the effective impact of industry on the environment, it is necessary to analyse the way in which the spatial concentration of branches of industry accentuates or disperses their potential impact. The estimates of the value of industrial processing presented by the Brazilian Institute of Geography and Statistics (IBGE) for 1980 make it possible to identify the concentration profile of the various industrial branches on the basis of the proportion of this value accounted for by four industrial centres. According to the IBGE classification, the group considered to be of “extremely high concentration” comprises pharmaceuticals, toiletries, soaps and candles and printing and publishing, which have an average of 50% of the total value of industrial processing concentrated in a single centre, and 80% in three centres. After this come the electrical and communications equipment branch and plastics and rubber manufacturing, whose concentration amounts to 50% in one centre and 70% in three centres, so that they may be classified as “highly concentrated”. At the other extreme there are the “dispersed” and “highly dispersed” groups. The first of these comprises non-metallic minerals, hides and skins, and the foodstuff and beverages sector, whose value of industrial processing concentrated in a single centre varies from 13% for beverages to 20% for non-metallic minerals, with the figures for the value of industrial processing concentrated in three centres rising to 27% for beverages and 37% for hides and skins. The second group comprises the branches engaged in the extraction of minerals and timber, which have 8% of the value of industrial processing concentrated in one centre and between 21% and 27% in three centres.

Taking industrial activity as a whole, it may be seen that from the very beginning concentration was intensified in the Southeast region, reaching a peak in the 1970s, when 79% of the total value of industrial processing was accounted for by that region. From that period onwards, partly thanks to the regional development policies adopted by the Government, partly because of the diseconomies of scale resulting from excessive concentration of economic activities in the region, and also because of the strengthening

of trade union movements, there was a slight tendency towards industrial deconcentration. Thus, since the early 1980s the Southeast region has only accounted for 72% of the total value of Brazilian industrial processing. Obviously, this process basically reflects the situation in two states: São Paulo and Rio de Janeiro. Even as far back as 1950, these States accounted for 20% and 10% of industrial establishments, 39% and 17% of the labour force employed in industry, and 48% and 20% of the total value of industrial processing in the country, respectively.

In 1970, the process of concentration reached its peak: São Paulo accounted for 31% of the country's industrial establishments, 48% of the employed labour, and 57% of the value of industrial processing. In 1980, however, the situation showed a trend towards deconcentration after that peak year of 1970. Thus, in 1980 São Paulo accounted for 29% of the industrial establishments, 45% of the employed labour, and 52% of the value of industrial processing, with Minas Gerais, Rio de Janeiro and Rio Grande do Sul competing for second place as regards concentration of industrial activity. It is also worth noting the intensification of the industrialization process in other states of the federation such as Paraná, Santa Catarina, Pernambuco and Bahia, whose values for the indicators in question ranged from 3% to 7%.

Using a methodology prepared by the State Foundation for Environmental Engineering (FEIMA) of Rio de Janeiro, the IBGE used the data of the 1980 industrial census to identify “potentially polluting” industrial establishments, according to the intensity of air and water pollution and the pollution parameters for the different branches of industrial activity. Thus, it was noted that in 1980 Brazil had a total of 214 156 industrial establishments, of which 106 506 (50%) were potentially polluting. The Southeast region contained the largest number of potentially polluting establishments, with 41% of the total, headed by São Paulo and Minas Gerais (with 23% and 12%, respectively). Next came the Northeast region, with 24% of the total, of which the state of Bahia accounted for 8%. The southern region contained 21% of the potentially polluting establishments, with the states of Paraná, Santa Catarina and Rio Grande do Sul accounting for relatively equal shares.

With regard to the specific problem of air pollution, the regional distribution of the polluting industries is approximately the same. First place is

occupied by the Southeast region, with 36% of the total establishments (São Paulo, 18%; Minas Gerais, 11%), followed by the Northeast states with 25% (Bahía, 8%) and the southern region, with 23%. The problem was more serious in the South (23%) than in the Northeast (17%), although an outstandingly unsatisfactory situation is occupied by the state of Maranhão which –largely because of Carajas– contained 4% of the establishments which are potential polluters of water resources. Moreover, the situation in some regions reached critical levels, as shown by the state of emergency declared in São Paulo in 1974 because of the concentration of pollutants in the atmosphere: a situation which was repeated on innumerable occasions up to the mid-1980s.

Finally, if we look at the situation of each industrial branch, we see that out of the total number of potentially polluting establishments, 40% corresponded to the non-metallic minerals branch. Of these, 15% were concentrated in Minas Gerais and another 15% in the state of São Paulo. With regard to air pollution, the potentially most highly polluting branches are food industries (20%) and the timber industry (17%). The food industries were mostly in the Southeast (30% of the total for the branch) and southern (27% of the total) regions, while the timber enterprises were in the states of the southern (40% of the total) and northern (18%) regions. With regard to water pollution, an outstanding place is occupied by the metropolitan regions of São Paulo and Rio de Janeiro, which have 15% and 5% of the total number of polluting establishments, respectively, concentrated in the metalworking, textiles, electrical and communications equipment, foodstuffs and timber industries.

Without denying the specific aspects connected with the impact of industrial activity on the Brazilian environment, there can be no doubt that the urban ecosystem is the one which has been most degraded by industrial expansion. This point of view, which has an eminently demographic basis, involves two different analytical dimensions from the environmental standpoint, both connected with the use of space. The first of them is the progressive concentration of the Brazilian population in cities, in a process of urban densification which takes place in all the regions of the country and raises environmental problems of a similar nature, with similar results and solutions, in all of them. The second aspect refers to the unequal spatial distribution both of natural

resources and of the economic activities undertaken by human beings. The combination of these two dimensions means that environmental problems have different degrees of intensity in different regions.

In terms of dynamics, the previously high population growth rate began to go down as from the late 1960s. This decline was only slight to begin with, but then speeded up and later became generalized. The abrupt drop in fertility took place in all regions, although this phenomenon was most marked in the urban areas and in sectors of society with higher levels of information and education. Thus, the total fertility rate fell from 5.8% in 1960-1970 to 3.2% in 1980-1990. As a result, the population growth rate likewise went down, from 2.9% per year in the 1960s to 2.1% in the 1980s. With the decline in fertility, it is calculated that at the end of the century Brazil will have a population of some 170 million people, with a growth rate of 1.5% per year in the 1990s. It is also calculated that the population will stop growing when it reaches the level of 265.5 million inhabitants, around the year 2075, when the average growth rate will be 0.58% per year. Analysis of Brazilian population growth patterns thus indicates that Brazil is already in an advanced stage of the demographic transition.

In the past, because of the spatial isolation of their various economic cycles, the occupation of the various regions of Brazil was always characterized by abrupt changes and solutions based on continuity. This is why there are so many dispersed or disconnected population centres in many points of the national territory. During the present century, however, the region polarized by its capital, São Paulo, has had an integrating influence, gradually unifying the national market in spite of explicit regional development policies which have made a systematic effort in recent decades to deconcentrate economic activity, including industrial activity, to more distant regions. The transfer of the national capital to Brasília attracted big migratory flows to the Centre-West region of the country, so that the population shifted to the interior. The process of geographical deconcentration in the 1970s may be explained by the expansion of the road network, the application of regional and urban policy instruments, and industrial promotion, which was reflected in the growing trend towards the installation of subsidiary plants and branches of companies from the metropolitan São Paulo region, especially those producing

intermediate goods. In this sense, the movement does not represent a true reduction of the process of concentration, but rather an expansion of the zone of influence of the dominant pole. In 1940, Brazil had only 51 cities with more than 20 000 inhabitants, whereas in 1990 it is calculated that the total came to 685. The total population living in localities of this size rose from 8.03 million in 1940 to 61.8 million in 1980. At present, 60% of the total urban population lives in nine metropolitan areas (São Paulo, Rio de Janeiro, Belo Horizonte, Porto Alegre, Curitiba, Salvador, Recife, Fortaleza and Belén). If current population growth trends continue, by the year 2000 nearly 80% of the population will be living in cities.

The urban environmental problems of Brazil are basically of two types. On the one hand, urban poverty (particularly in the big cities) affects a large proportion of the Brazilian population and merges with the consequences of environmental degradation. On the other hand, as already noted, there are the problems caused by the concentration of economic activity (especially in the industrial sector) in urban localities. The rapid urbanization resulting from the industrialization process has given rise to a deficit in the urban services infrastructure, the most serious environmental manifestation of which is the lack of basic sanitation. If it is borne in mind that nearly 33 million people now live on the periphery of the big cities, it is obvious that the problem of basic sanitation is and will continue to be one of the biggest urban problems in Brazil in coming decades. According to official data, 35% of urban dwellings (mostly located in the "favelas") are considered to be deficient from the sanitation point of view. The statistics on residential services hardly scratch the surface of the question of urban environmental sanitation.

Generally speaking, there have been big advances in water supply services. Thus, the indexes of service to the urban population rose from 45% in 1970 to 88% at present. With regard to the elimination of sewage, however, the results are much less satisfactory: over the same period, the growth in services was from 22% of the population to 35%, and the services continued to be of an extremely makeshift nature. This situation is aggravated by the fact that only 10% of total effluents receive proper final treatment, which would indicate that nearly 10 billion litres of sewage are discharged in the raw state every day into the earth or into bodies of water. Finally, it may be noted that the lack of sanitation

services mostly affects the low-income population. Of the 5.9 million urban dwellings which were not connected to the drinking water system and did not have flush toilet installations in 1980, 72% (over 21 million people) corresponded to families earning less than three minimum wages.

Another basic problem of urbanization is connected with refuse and urban cleaning. Refuse collection is as shaky a service as that for sewerage. Of the nearly 12 000 tips where municipalities put their solid waste, most are open tips or bodies of water, which involves problems of contamination of the air, water and soil, quite apart from favouring the proliferation of vermin harmful to human health. A sample of the biggest urban/industrial centres selected by the IBGE in 1980 revealed that in 63% of the 192 biggest urban centres in the country, solid refuse ended up in open tips. Few municipalities engage in the selective collection of refuse in order to recycle such materials as paper and cardboard, plastics and metals so as to reincorporate them in the economic cycle.

The situation with regard to workers' health (mostly in urban areas) is equally depressing. In ten years, over 10.5 million insured workers suffered accidents, and of this total over 41 000 died, while nearly 250 000 were permanently incapacitated. Studies indicate that the most frequent ailments are loss of hearing because of excessive noise; occupational dermatitis; metal poisoning, especially due to lead; effects of exposure to solvents, and various forms of pneumoconiosis. A special problem which has affected Amazonia since 1980 is due to the intensive use of mercury in gold mining. The main non-occupational form of exposure to mercury among human beings is the consumption of contaminated fish or fish products. Estimates based on the real production of gold indicate that approximately 900 tons of mercury were dumped in the Amazonian ecosystem during the 1980s.

Finally, ecological disasters are increasingly menacing risks for urban centres. It may be recalled by way of example that the presence of inhabited areas near pipelines transporting dangerous products can lead to serious accidents, as occurred in 1984 in Vila Socó (Cubatão, São Paulo), where the ignition and explosion of 700 000 litres of gasoline killed over 100 people. Both this accident and the radiation accident in Goiania (Goias), in which six people died and a further 244 were contaminated with radiation from a cesium capsule, are eloquent in this respect.

## 2. *The expansion of agriculture and its socio-environmental impact*

The expansion of agriculture has reflected a pattern of industrial development and has been subordinated to it; it has been due mainly to the continual advance of the agricultural frontier and the introduction of more capital-intensive production techniques. The area occupied by agricultural enterprises almost doubled between 1950 and 1980, increasing by 1.67 million square kilometres. The process of modernization has been marked, however, by its uneven distribution –both regionally, by types of crop, and by classes of rural establishments– which reflects the piecemeal nature of this process and its links with the process of internationalization of the economy. Modernization has taken place at an intensive rate in the Southeast and southern regions, especially in São Paulo, Paraná and Rio Grande do Sul, as well as, in general, in areas engaged in the production of export crops such as certain areas in the Centre-West region and the Mata area in the Northeast. In brief, this process has represented the consolidation of the model based on agroindustrial complexes: a combination of science as applied to agriculture and profound changes in the organization of production, which has resulted in the elimination of the gap which previously separated agriculture from industry. The indicators on technification corroborate the great regional disparities in this sector.

Tractor use in agriculture illustrates the marked inequality of the modernization process. Although the number of tractors grew by 7 800% over the period 1950-1985, even in the latter year only 7.2% of farms had tractors. The southern region, where 16.3% of the farms had tractors, accounted for 43.2% of the total number of tractors in use in Brazilian agriculture. In 1980, three-quarters of the rural production units in Brazil only had manual production tools such as hoes, machetes, scythes and axes. Only 22% of these units used animal-drawn ploughs.

The 1980 data reflect the same inequalities in distribution with regard to chemical fertilizer use. Although the number of establishments using chemical fertilizers doubled over the period 1970-1985, in 1980 only 25% of Brazilian farms used them. The states of São Paulo, Paraná, Minas Gerais and Rio Grande do Sul accounted for 70.4% of the establishments using these inputs, although they only represented 18.4% of the total farms in Brazil. In

regional terms, and by types of crops, the available data clearly show that chemical fertilizers are used primarily for export crops. In the northern and Northeast regions taken together, sugar cane (which occupied 6.2% of the cultivated land) consumed 85% of the fertilizers used in those regions, followed by cacao, which, although occupying only 2.9% of the cultivated area, absorbed 10% of the fertilizers used. In the Southeast and Centre-West regions, coffee, sugar cane, soya beans and cotton consumed 75% of the fertilizers used, although they only occupied 27.2% of the cultivated area in those regions. In the south, the predominant crops were soya beans and wheat, which accounted for 90% of the chemical fertilizers used in the region.

The modernization strategy applied in Brazilian agriculture has also promoted a significant increase in the consumption of toxic agricultural inputs: herbicides, insecticides and fungicides. According to data from the IBGE, the consumption of toxic agricultural inputs grew by 300% between 1970 and 1980, from 27 000 to 80 000 tons per year. In corroboration of the subordinate position of agricultural modernization *vis-a-vis* industrial modernization, it may be noted that in 1974, 75% of the toxic agricultural inputs used were imported, but in 1980 national production already satisfied 50% of annual consumption. In 1984, 80% of the total consumption of toxic agricultural inputs was concentrated in the states of São Paulo, Paraná and Rio Grande do Sul, and was used above all for export crops: soya beans and citrus fruit alone accounted for 23% of total national consumption that year.

The social impacts of agricultural activities on the country were numerous and varied. First of all, the development of capital-intensive agriculture proved to be incapable of generating the number of jobs needed to absorb the rural labour supply, and this led to migratory flows to the cities or to areas on the agricultural frontier, especially Cerrado and Amazonia. Secondly, modernization was reflected in marked changes in labour relations, leading to the employment of former smallholders, settlers and sharecroppers on a partly wage-earning casual basis, so that they became seasonal migratory workers because of the expansion of single-crop agriculture and the consequent increase in seasonal work. The single-crop agriculture resulting from modernization led to the disappearance of the subsistence crops of rural workers, who became wage-earners looking for work in rural areas or in the cities.

Thirdly, when the average growth rates of the cultivation of staple foodstuffs and export products are compared with the population growth rates over the last 30 years, a clear picture is obtained of the general tendency over this period. Thus, it is observed that there has been either stagnation or a steady decline in the production of rice, beans, maize and cassava, while production of coffee, soya beans, oranges and sugar cane has remained at high levels. The increase in demand for staple foods which are no longer cultivated in the old subsistence farming units, together with low wages, has been reflected in a sharp drop in food consumption and greater malnutrition of the migrant population. Thus, in 1990 hunger or malnutrition prevailed among two-thirds of the Brazilian population. Fourthly, the modernization of agriculture has favoured to an even greater extent the concentration of rural property and the incorporation of small farms into large and medium-sized establishments. Another effect of the process has been the increase in the number of dwarf holdings, that is to say, the proliferation of very small holdings whose average area has steadily gone down. In 1960 there were 1.5 million rural properties, with an average area of nearly four hectares, whereas in 1980 the number had risen to 2.6 million, with an average area of 3.5 hectares, and in 1985 these tiny holdings amounted to 3.1 million, with an area of 3.1 hectares each. Data for 1980 show that 80% of the total area of agricultural holdings was accounted for by only 10% of the total number of properties.

The rapid growth of modern commercial agriculture, as well as aggravating the social crisis, has raised environmental problems which have not always been properly appreciated in all their seriousness. The growing use of chemical fertilizers and toxic agricultural inputs, the intense and concentrated process of mechanization, and the extension of single-crop agriculture aimed at the external market have led to the erosion and degradation of agricultural land, as well as serious impacts on forest resources, rivers, lakes and the ecological balance as regards pests and diseases. Finally, in some areas which have been the subject of public irrigation programmes, improper use of the technology has led to serious environmental problems, especially the leaching of chemical products and the salinization of agricultural land.

By the mid-1980s, Brazil had become the third biggest world market for toxic agricultural inputs, after the United States and France. As an indication of the problems caused by this growth with regard to the biological balance in agriculture, it may be noted that in 1948 the number of species harmful to cultivated plants amounted to 989, whereas in 1976 such species numbered 3 037. With regard to erosion, it is considered that normal agricultural activity causes an erosion rate of the order of 17 tons per hectare per year. The cultivation of soya beans and wheat in Paraná, however, causes an annual loss of 144 tons per hectare, which corresponds to over one centimetre of soil lost on each hectare each year. In the state of São Paulo, the total soil losses amount to 194 million tons. For Brazil as a whole, the losses averaged 25 tons per hectare per year, which represents an overall loss of one billion tons per year.

A process which is related with that of erosion is desertification, which represents the last stage in soil degradation. In 1977, at the Conference on Desertification organized in Nairobi by the United Nations Environment Programme (UNEP), it was asserted that Brazil is in the process of forming the third biggest desert in the world, only a little smaller than the Sahara and the Arabian Desert. This "Central Brazilian Desert" will extend from the coast of Rio Grande do Norte to the Centre-West region and also include large areas of the Northeast. The problem is not limited to these regions, however. In Paraná, for example, 20% of the territory is unproductive and open to the risk of desertification. In Rio Grande do Sul, at least three important focal points in the formation of deserts have been identified: San Francisco de Assis (2 000 hectares); Alegrete (1 500 hectares) and Itaqui (1 000 hectares), which together make up the "Desert of the Pampas".

The impacts of the horizontal expansion of agriculture which are most difficult to put right are those connected with the felling and elimination of native vegetation which has taken place in vast areas of the national territory. Before the coffee boom, forests covered nearly 82% of the area of the state of São Paulo, but by 1973 this proportion had gone down to only 8.3%. At the end of the 1940s, nearly 90% of the territory of northern Paraná was covered by native forests, but these now cover only a little over 17% of the region. There has been a similar impact in other regions.

### III

## Basic components of a sustainable industrial and agricultural development strategy

### 1. Preliminary considerations

Some words of caution are called for with regard to the interrelation between industrial and agricultural development and between the development of these two sectors and the maintenance –or in many cases, the restoration– of environmental quality patterns which represent an effective improvement in the quality of life of the population, and also with respect to the great diversity of regional situations existing in the country. In the first place, some of the requisites for sustainable development which will be presented below cannot be differentiated between the industrial and agricultural sectors. Secondly, most of these requisites demand, as prior conditions, the correction of the veritable gulfs dividing social groups and strata, separating the big cities from the rural areas, and differentiating the various regions of the country from each other.

In reality, a new development paradigm must permit a thorough review of the present practices with regard to the use of natural resources, through new forms of social organization and new patterns of production and consumption. For a start, it is impossible to conceive of an environmentally sustainable style of development which does not include the solution of the serious imbalances caused by the situations of extreme poverty and economic and social inequality which characterize Brazilian society in these last years of the century. It is not only wealth and natural resource ownership which are concentrated in the country, however. Access to the decision-making centres is still unequally shared among the cities. It is therefore felt to be equally essential to improve Brazilian democracy so as to tackle the problem of the divorce between society and the State and to overcome the situation of political poverty which aggregates and perpetuates economic and social inequality.

The recent pattern of development has left as its great legacy the unresolved problem of social duality. Nearly 40% of Brazilian families live in a situation of poverty, with a monthly income of less than a quarter of a minimum wage per head. Of this

total, 45%, representing 4.7 million families, live in conditions of total indigence. In 1989, the richest 5% of the population received 38.5% of the total income, whereas the poorest sectors received only 7.2%. The high indices of concentration are due to the differences in income between regions and sectors of production, as well as the structural characteristics concerning age groups and the educational base.

The Northeast, which contains 29% of the Brazilian population, has 53% of the country's poor. In 1980, each inhabitant of the Northeast earned on average the equivalent of a little over a quarter of what was earned by a person living in the Centre-South region. In short, a review of the social indicators at the beginning of this decade reveals an increase in the gap between urban areas and rural communities, as well as between regions. The majority of rural areas ended the 1980s in a more unfavourable situation than that registered by the cities 20 or 30 years before. The same is true of the Northeast, in comparison with the Southeast.

Part of the problem is due to a kind of superimposition of history. Whereas the countries which were industrialized a long time ago went through the industrialization process over a period of many decades, with consequent very gradual urbanization and social differentiation of their population, in Brazil these processes frequently occurred at much faster rates, within a single decade or even less. Trotsky's description of events in the Russian Revolution can easily be transferred to Brazil: "The savages are replacing their bows and arrows with rifles from one moment to the next, without first covering the path which separated these two arms in the past" (Deutscher, 1963, p. 230).

The results of this legacy, which acts as a kind of mortgage on Brazil's future development prospects, cause the social structure to exist against a background of dramatic tensions. The first aspect which must be highlighted is therefore that the mere restoration of economic growth is not enough to solve these serious problems. The transformation of the structure of production, which is essential in order to ensure the recovery of economic growth,

must be interlinked with a firm policy aimed at ensuring greater social equity, not only for the people of today, but also for future generations.

At the same time, criteria of economic efficiency guided solely by the market forces do not lead to a reduction of social and regional inequality or to rational natural resource use. The Brazilian experience has proved that the intensive mobilization of the factors of production favours the plundering of environmental resources and tends to spontaneously reproduce the initial social and spatial conditions which formed its basis. It must therefore also be recognized that the economic growth process does not take place in a social vacuum. Whatever the diagnoses underlying economic policy proposals in favour of the socio-environmental sustainability of development, it is necessary to examine with care the various global options proposed for overcoming the present problems and their implications with regard to the objectives of greater social equity and reduction of poverty.

In short, giving priority to macroeconomic policy options which permit the satisfaction of the basic needs of the poorest sectors; developing integrated social policies which have an impact that goes beyond the immediate combating of poverty; devoting a significant part of the product to the social sectors; modifying the distribution of public expenditure at the basic level, and reorienting social programmes for the most vulnerable groups do not seem to represent an economic obstacle. In fact, accumulation, distribution and citizenship are synchronous processes which are the form and substance of a single historical process. This being so, the economic, social and political evolution of the country is clearly pointing to the need to overcome the disparities between material progress, social justice and environmental sustainability. This is an eminently political challenge which must be faced by building alliances among the various social groups so as to obtain the consensual basis for the necessary reform of the public institutions. At the micro level, the institutional challenge of the crisis of the sustainability of Brazilian development amounts in essence to the democratization of society, while at the macro level it amounts to the democratization of the State. The first of these objectives assumes the strengthening of social and community organizations, the redistribution of resources and information to the underprivileged sectors, and an increase in the capacity of analysis of their organizations and their decision-making capacity. The second objective is achieved through the

opening up of the State apparatus to citizen control, the updating of political parties and electoral processes, and the incorporation of the concept of political responsibility into public life.

## *2. The components of a new pattern of industrial and agricultural development*

The transition towards a new style of development presupposes well-defined strategies for transforming sectors of production which are essential for the economy and for the well-being of society. The present economic and environmental crisis may be attributed to the imbalances resulting from a style of development based on production processes making extensive use of natural resources and fossil fuels, which were considered to be extremely abundant. It may be attributed, above all, to the belief that the "free goods" of nature, such as air, water and even the forests, are unlimited and capable of receiving any amount of wastes, refuse, polluting gases, etc. generated by a consumer society which squanders natural and human resources.

Certain general components of the new development strategy are essential prior conditions for giving consistency to industrial and agricultural development policies. Thus, the establishment of a new and sustainable style of development in the country calls for the strengthening of the existing instruments and the creation of new ones. The first action to be taken must undoubtedly be the establishment of a system of resource accounts which makes it possible to incorporate the economic value of the natural resource endowment of the country in macroeconomic planning. To put it briefly, just as government planning only became possible once there was already a solid system of national accounts, without which it would be quite impracticable to indicate to the productive sector the optimum resource distribution which should be applied, likewise, any development strategy which seeks to internalize the environmental costs of economic activity needs instruments for establishing natural resource endowment accounts.

Parallel with the establishment of resource accounts, a thorough review of the economic paradigms is called for, so as to give a strictly operational character to the criterion of the environmental sustainability of development. The contributions made by Herman Daly in this respect have been very valuable (Daly, 1990, pp. 1-6). There are two basic ideas in this new form of economic thinking. Firstly, for the

case of the management of renewable natural resources, there are two fundamental principles that must be taken into account: on the one hand, the rates of utilization must be commensurate with the rates of replacement, and on the other hand, the rates of emission of effluents must not be greater than the capacity of assimilation of the ecosystems into which they are released. This means that the "rates of recovery" and the "rates of regeneration" must be treated as "natural capital". Inability to maintain these rates must therefore be considered as the consumption of capital: that is to say, it is not sustainable. Secondly, for non-renewable resources, which by their very nature cannot be used indefinitely on a sustainable basis, it will be necessary to limit their rate of utilization to the rate of development or discovery of new substitutes. This means, among other aspects, that investments made for the exploitation of non-renewable natural resources must be accompanied by equivalent investments devoted to the search for substitutes.

With regard to the financing of development, the Brazilian economy must recover its saving capacity. For this purpose, it will be necessary to overcome the fiscal crisis which characterized the 1980s and the early 1990s and emerge from the present impasse in which the balance of payments surplus is immediately absorbed by the external debt repayment commitments. In this respect, lengthening the term of the debt merely reduces the frequency of the renegotiation exercises, since the commitments are perpetuated and the international banking system becomes a kind of rentier installed in the country's economy without any risk whatever to itself.

Specifically in respect of environmental matters, it is necessary to redefine the schemes for the application of penalties for damage to the environment in order that the income collected in this way may be used by the environmental bodies themselves. In order to increase this income, it would be important to apply market mechanisms, such as rates and tariffs which incorporate the costs of environmental preservation into private costs, through mechanisms which could be in line with the principle that "the polluter must pay". Among other market mechanisms which deserve to be strengthened, mention may be made of the "waste exchanges" –on which the industries of a given region trade the effluents arising from their activities, which can often become inputs for other industries– and "pollution rights".

It is worth placing special emphasis here on these pollution rights, which, through their transfer within industries, make it possible for the public authorities to give up using tax regulations based on the establishment of emission limits for each industrial unit and apply instead regional effluent emission limits, according to the recovery capacity of each ecosystem. In this way, a substantial part of the maintenance of environmental quality would become the responsibility of the market, since the trading of pollution rights would stimulate the modernization of technology and cease to penalize industries which, in the present state of development of technology, are not in a position to reduce their levels of emission of effluents. The present system of fines, in addition to hindering the internalization of the costs of environmental degradation through the regulations it applies, penalizes industries which, although they use the best technology available, nevertheless exceed the pollution limits, while it favours those which, although admittedly within the established limits, do nothing to improve their production processes.

Quite apart from the potential income offered by many of these arrangements, it is of fundamental importance to secure external resources also. Conversion of the external debt for application in environmental projects and, more broadly, in sustainable development projects, is an important alternative way of obtaining resources for both governmental and non-governmental bodies. Bilateral loans and loans from multilateral credit agencies will continue to be essential for the execution of environmental projects as well as development projects. What may appear to be perfectly valid for certain projects or sectors, however, may tend to lose its validity in an overall setting. Thus, if the level of indebtedness is contained, this means that there will be no new money: the dollars obtained will go to service the debt, and such projects as are "financed" will actually be carried out in national currency with domestic saving. To sum up, as preservation of the environment is an investment whose profitability is difficult to quantify, and frequently it involves world-level responsibilities, then the external resources used for it should not be governed by market conditions. Preference should be given to donations or loans on very soft terms, especially for regional-scope projects.

With regard to industrial development, the scientific and technological progress attained in recent decades makes possible a fuller knowledge of the

ecological processes in the biosphere and offers suitable techniques for monitoring world changes in these processes. There is also the possibility of using new production processes which are less dependent on energy and raw materials, of using new energy sources based on new materials, and above all, of taking advantage of the possibilities of making much better use of biological resources. The common denominator of all these changes could be described as the shift of emphasis from matter and energy to information; from quantity to quality. In other words, the type of economic production now taking shape at the international level makes intensive use of scientific and technological knowledge rather than natural resources as such. This explains how countries with a poor endowment of natural resources, such as Japan, have attained a high level of economic and social development.

Scientific and technological progress is incorporated into the productive sector, with benefits for the environment, in three main ways: high-technology industrial development; use of knowledge in the existing productive structure, and projects designed to promote the recovery of the environment. The proper use of technology makes it possible to establish clean industries, which are the basis for a form of economic growth that is more balanced and integrated with the environment. In respect of the second line of action, it may be noted that even slight under-utilization of technological knowledge causes shortcomings in production management; the present times call for innovations in the management of technology itself. Every effort should therefore be made to promote a management philosophy based on quality and productivity, integrated within an environmental approach. In the third major line of assimilation of new and environmentally acceptable technologies by the productive sector, it may be noted that there is a big market for activities and projects directly linked with the environment. A typical example is the recycling of refuse and the re-use of wastes and effluents.

The use of appropriate technologies offers opportunities for achieving optimum regional solutions, since when these technologies have been developed over many years or decades this means that they have absorbed the cultural tradition of the environment in which they are used, thereby offering an empirical basis for understanding problems and favouring the emergence of appropriate projects. In this respect, biotechnology is a natural option for

Brazilian development. The use of biological systems for converting forms of energy or changing one chemical substance into another (bioconversion) has various advantages: high selectivity, flexibility, low energy input requirements, high catalytic activity, environmental compatibility, ease of application regardless of the place where they are used, and renewability. The impact of biotechnology in such sectors as textiles, fine chemicals, new materials and microelectronics is undoubtedly impressive, as may be seen already in the developed countries.

With regard to renewable sources of energy, leading possible alternatives or supplements to petroleum are natural gas, shales, peat and nuclear energy. All of these, with the possible exception of peat, are centralized forms of energy. In the case of decentralized renewable forms of energy, there is a wide range of possibilities, including wood and charcoal, liquid fuels such as alcohol and vegetable oils, gaseous fuels derived from biomass, and small hydroelectric power stations, as well as forms of technology of more restricted use, such as biogas and direct, thermal or voltaic solar energy. A new industrial development strategy also calls for a thorough change in the transport system of the country, with greater use of the railways and seagoing and river vessels for transporting cargo, as well as support for programmes to expand public transport systems and replace diesel oil with natural gas, biogas or electricity in urban centres. It may be noted that the Brazilian Constitution lays down that cities with 20 000 inhabitants or more must have an urban development plan which provides for the establishment of an integrated transport system. In establishing the infrastructure, a prior requisite is guaranteed control over land use, since road administrations only have power to act in the actual space occupied by the roads.

With regard to sustainable agricultural development, we have seen how the process of institutionalization of agriculture, subsidized by the State and propelled by the logic of industrial expansion, has led to an increase by leaps and bounds in the impoverishment of the population and the squandering of much of the available natural resources. Reversing this situation involves changing the priorities of agricultural policy and applying a new model which includes better distribution of the rural population over the territory, gives priority to food production and proper soil management, as well as the proper distribution of water resources, and presupposes the use of appropriate technologies for each region.

It is vital to adopt a broad programme of reform of the system of land ownership. Side by side with the agrarian reform initiatives, it is also essential to gradually replace single-crop agriculture with diversified cropping. It is also necessary to develop integrated agricultural-forestry-stock breeding production systems, in keeping with the ecological vocation of each region. It goes without saying that a policy of this nature also requires the development of agroecology, with the replacement of toxic agricultural inputs with biological controls for species which are harmful to crops. The use of herbicides, insecticides and fungicides would initially be restricted and subsequently scheduled for virtual elimination. With regard to food security, finally, it is necessary to expand the genetic base contained in the plants traditionally used for food production. It is vitally important for the country to seek alternatives in this respect through agricultural research carried out in systems of *in situ* and *ex situ* conservation based on germ plasm banks, botanical gardens and genetic reserves.

The aim of conserving genetic resources and preserving biodiversity is to concentrate on the species which can have an impact on the modernization of strategic sectors such as human and animal health, food production, agriculture and the environment, and to ensure that this genetic material, as well as information on it, is available for present and future generations. However, the internationalization of the legislation on intellectual property applied to biological products, as proposed by some developed countries, will permit the legalized appropriation of those resources by the most advanced countries, which have an indisputable advantage over the developing countries in terms of techniques for making use of genetic resources. It is well known today that real control over genetic resources lies in access to information on genetic material and the possibility of using it, through the mastery of manipulation techniques. Consequently, any law on intellectual property applied in this area will tend to benefit those countries which are already most advanced in techniques for making use of genetic resources.

## IV

### Final comments

In advanced capitalist countries, the reconciliation of economic and environmental objectives depends on technology capable of turning industry and transport into systems which use fuels and raw materials in an extremely efficient manner and are based on inputs of low environmental cost which generate few residues. To this end, it is necessary to establish closed technological systems, that is to say, systems depending only to a minimal extent on natural resources. For the developing countries, whose trade balance depends mainly on their exports of primary commodities, the prospects presented by a situation where such closed technological systems prevail is gloomy. In most of the countries of the South, little progress has been made in the area of new technologies. These technologies are obtainable—generally from the private sector of the developed countries—only through payment of royalties and acceptance of other financial, trade, and often political commitments.

Consequently, the technological solution proposed for environmental problems by the industrialized countries brings into question the role which the developing countries play in the international economic system. Their traditional role as suppliers of primary commodities, the proceeds from which are already insufficient to take care of their basic development needs, will tend to go down still further in the near future. The evolution of new technologies very clearly shows the need to make a concentrated domestic effort to develop spearhead technologies which are not aggressive for the environment, as well as to arrive at international agreements designed to facilitate access to the technologies developed by the industrialized countries.

In short, while Brazil is beginning to make adjustments in the profile of its industry, the world economy is entering on a new technological cycle and paradigm. In contrast with what happened in post-war industrialization, which was characterized

by intensive consumption of natural resources—raw materials, basic commodities and energy products—the new growth pattern is characterized by high demand for information and knowledge, with a relative reduction in the consumption of environmental resources and the production of polluting effluents.

In spite of the foregoing, it must be acknowledged that there have been substantial changes in the treatment given in Brazil to environmental questions, from the political, legal and institutional point of view. From the economic, financial, scientific and technological point of view, however, there are structural problems which prevent any hope of major progress in the short term. Restrictions on public expenditure, measures to contain inflation and the debt burden are some of the factors which considerably limit the possibilities for large-scale action by the government.

The problems inherent in the fact of being a developing country are further magnified by the special features of Brazil. The great extent of the biggest reserve of tropical forests in the whole world, the heterogeneity of its ecosystems, its biodiversity, the location of extraordinarily large mineral deposits in various points of the subsoil under the forests, and the existence of rivers capable of producing energy and food are all elements that make up a rich endowment of resources but at the same time a challenge that cannot be ignored by politicians, planners and scientists. There are few developing countries which still have territories theoretically available for settlement or economic conditions for promoting such settlement on a large scale, and none of them have such a huge area, with such a biological diversity that must be investigated, studied and ultimately preserved or used, as Brazil. These features impart a world dimension to the country's environmental problems and make it obligatory for Brazil to take part in multilateral efforts to seek solutions for world imbalances. Just as the challenge of reconciling environmental quality and economic growth, in its international expression, calls for the participation of Brazil in the search for solutions for world environmental problems, so, in the domestic dimension, it is essential that society as a whole should participate in building a new style of development for the country. The relationship between the private sector and environmental protection, for its part, must be understood as part of the political, institutional and

historical process of the country, especially with regard to the role that the State has played in mediating between the social forces and guaranteeing democratic rights. Such features, together with the income distribution profile, explain why generally speaking the bias of decisions in society is inclined too far towards income concentration and penalizes the exercise of the basic rights of the citizen, among which is the right to a decent quality of life. Thus, economic power has traditionally meant the power to pollute in spite of the laws. It is not without justification that it is asserted that the country has adequate environmental legislation, but it is not fully complied with.

Recently, however, some reaction has been observed in entrepreneurial circles themselves against the evils of a type of economic development which pays no heed to environmental considerations, even when these represent a risk for the continued existence of certain activities and their acceptance by society. Thus, in recent years environmental management has become a part of industrial planning and operations, just like community relations. The legal requirement to carry out studies on the environmental impact of the entry into operation of industrial units and other forms of resource use, and the holding of public hearings to discuss projects, will lead the productive sector to pay increasing attention to environmental factors. In this transitional process, the adoption of clean technologies which minimize negative environmental impacts has taken place on an uneven scale in the different sectors, although it is recognized that the costs of controlling pollution are less and the efficiency achieved is greater when environmental protection and management measures and measures to control risks are taken into account from the initial stages of an industrial project. In some sectors, such as the aluminium, chemicals, petrochemicals, and paper and pulp industries, the process of incorporating environmental safeguards is at a more advanced stage, since these industries are adopting, *inter alia*, technologies and measures for the control and recycling of wastes. The public sector, generally speaking, already has experience in environmental control of large-scale projects such as those in the electricity and mining sectors. Positive results have been obtained in research on technological solutions for the environmental problems generated in the agricultural sector.

These small seeds of a new growth pattern, more in keeping with the ecological conditions of the

country and aimed at improving the living conditions of the population, seem to have fallen on fertile ground. Nevertheless, the magnitude of the challenges calling for decisive action demands an even more determined attitude by Brazilian society as a whole. When what is involved is something more than the mere maintenance of a certain lifestyle and involves the total reformulation of its material, productive and even ethical bases, more is demanded from human beings than their mere capacity to adapt or their capacity for "fine tuning". What is needed is a firm determination to bring about a veritable revolution in the paradigms and practices which govern life in society. Albert Einstein said, with regard to the beginning of the nuclear age, that "everything has changed" and that "we need a different way of thinking if humanity is to survive". The global crisis in the environment also marks the beginning of a new age and a new style of development. There can be no doubt about this. Charles Birch was completely right

when he said "maybe we could not predict this new era, but we can certainly invent it".<sup>3</sup>

Consequently, ecological arguments also necessarily constitute political arguments. Before examining the technical arguments for the taking of rational decisions, it will be necessary to create alliances between the different social groups capable of furthering the necessary changes. It is to be hoped, in this respect, that Brazil will take advantage of the momentum provided by the Rio Conference to begin a search for compromises—both internally and internationally—which will make possible the emergence of a new pattern of industrial and agricultural development which fulfills the requirements of environmental and social sustainability.

<sup>3</sup> Both quotations are from Guimarães (1990), pp. 59-95.

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## Integration today: bases and options

*Eugenio Lahera P.\**

The idea of regional integration is deeply rooted in Latin America. It has been part of the proposals for the region's development for decades past, and now, through a combination of domestic and external circumstances, it occupies a leading place in the regional economic debate. It was a novel idea which, through being applied only partially in so many cases, gradually became an issue of the past: an empty prospect and a contradiction in its own terms.

Integration is a subject which is full of paradoxes. Much has been written on it, yet its real nature continues to elude us. The results it has given have not been in line with its potential, yet it continues to spark off efforts. It is easy to show how desirable it is for promoting development, but at the same time the conditions limiting it are all too evident. Great efforts of imagination have been devoted to defining objectives and instruments for integration, but many of them have had little chance of being applied. It enjoys enormous popularity, yet at the same time it lacks sufficient political support. Moreover, various economic and social agents of integration, on whose behalf frequent assertions are made, have usually been absent from the design and application of the policies affecting them. The present circumstances seem appropriate for resolving these paradoxes in the interests of regional development.

Section I of the article analyses various interrelations between economic integration and development in Latin America and the Caribbean. In section II, various obstacles which the integration process must face are examined. Finally, section III analyses various policy lines. The overall aim is to identify the present role of economic integration in the process of changing production patterns with equity in the region and to note the main options open in this respect.

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## Introduction

For ECLAC, integration is both a foundational and a constantly renewed topic, since it formed part of the recommendations which the institution made to the Latin American countries from its earliest years. The circumstances then were different, but the main concern, then and now, was the enhancement of the regional economic space.

The *Economic Survey of Latin America, 1949* affirmed the need to increase intra-Latin American regional trade. Subsequent events—those accompanying the Korean War—caused this assertion to seem less urgent, but it became a valid issue once more when the region's exports to the United States fell again.

In a statement made in 1959, Prebisch noted that:

“The idea of a possible common market had been taking shape for a number of years, until in November 1956 the Latin American governments, in the ECLAC Trade Committee, asked our Secretariat to set up two expert groups, one for the gradual establishment of a multilateral payments system, and the other to define the characteristics of the regional market... the common market is not something which can be carried out or not carried out at will in the face of this growth problem... a most intensive effort must be made to technify agriculture and advance resolutely in the industrialization process, not only in the big countries but also in the medium-sized and small ones. A big increase in the capital stock will be needed, and it will be necessary to tackle in all its magnitude the generally neglected problem of technical training at all levels of productive effort.

“Even if all this were carried out effectively, however, we do not believe that it could be achieved and maintained in practice... if the industrialization process continues to operate within the relatively narrow limits of each national market and if each country seeks to achieve full supply of its requirements for agricultural products, no matter how high the cost to the consumer.

“It is not just a problem of productivity, however, although this problem is indeed very important. There is another aspect which I should also like to highlight: that of the economic vulnerability of the Latin American countries... I do not see any fundamental solution to this serious problem and to that

of the high cost of the substitution process, other than breaking out of this outmoded system through the gradual and progressive formation of a common market and the consequent diversification of imports and exports" (United Nations, 1959).

In that same year, the ECLAC Executive Secretariat put forward as a long-term objective the free circulation of "goods and services, labour and capital, without any kind of hindrance, in a vast Latin American Common Market" (United Nations, 1959). The analysis and specific proposals of ECLAC on integration were partly accepted and partly rejected in the proposals that were closer to the GATT approach (Wionczek, 1964).

Attempting to make an evaluation of the whole integration process is beyond the possibilities of this article. It may be noted, however, that this process has had both positive and negative aspects.<sup>1</sup> Between 1960 and 1980, and above all in the first of these two decades, the integration process in Latin America and the Caribbean registered significant progress. At the beginning of the 1960s, trade among the countries of the region was only incipient, and there was practically no complementation in terms of production activities. During subsequent years, however, mutual trade became a dynamic element in the external trade of the region. At the same time, there was an increase in the levels of economic interdependence, especially in the subregional processes involving countries with small and medium-sized economies. Intra-regional cooperation found many other varied expressions in the development of the various sectors of production and of the physical infrastructure, as well as in the emergence of intergovernmental institutions and subregional or regional associations representing various groups and interests. The increase in mutual trade also facilitated the expansion, diversification and modernization of industrial production, as well as some specialization of activities at the subregional level.

At the same time, integration has also suffered shortcomings and setbacks, especially the reluctance of governments and of some groups to open national production to the competition of goods from other countries of the region; unequal distribution of the costs and benefits of integration and, in general, the difficulties in ensuring reciprocity between countries of different economic size and levels of development; and finally, the conflicts between the undertakings entered into under integration agreements and the objectives of national development strategies and policies, especially when national decisions must be subordinated to those of a multi-lateral nature (Rosenthal, 1989).

When all the deadlines for the original undertakings had run out and the situation had become unsustainable from the legal point of view, it was decided to adapt the legal framework formally to the actual situation by extending the deadlines and making the instruments more flexible. Examples of this are the conversion of the Latin American Free Trade Association (LAFTA) into the Latin American Integration Association (ALADI) and the protocols modifying the Cartagena Agreement. Thanks to these adaptations, in the 1980s there was a fresh proliferation of bilateral understandings (ECLAC, 1991). These understandings, which have further increased in the 1990s, are different from the traditional agreements, especially with regard to the scope of the trade covered by them.

The Latin American economy requires right now "second generation" ideas which go beyond adjustment and fiscal discipline. It is not a question of taking the place of these policies, which would be very undesirable and harmful, but rather of turning them into a prerequisite for policies aimed at growth with equity. It is possible that in the 1990s trade, production and financial integration will have more opportunities than they did in previous decades.

<sup>1</sup> This analysis is based on Rosenthal (1989).

## I

**The actuality of integration**

Almost all the countries of Latin America have committed themselves to efforts aimed at mutual free trade; a number of them have done so through guarantees for the investments of the respective countries and the harmonization of their economic policies. By the mid-1990s, the region could be organized into a small number of economic groupings complemented with bilateral free trade areas, and direct investment of regional origin could increase very significantly. It is probable that later on the subregional groups will tend to become unified and that there will also be regional or national progress towards free trade with the United States and Canada. These possibilities represent unprecedented developments.

*1. Is this really integration?*

Is there a common denominator for all these processes? A point which is frequently overlooked is that the concept of integration is quite broad. It may be recalled in this respect that the publications on this subject distinguish various degrees of economic integration (Belassa, 1964; French-Davis, 1979). The lowest level of integration is represented by a free trade area: the members of the area agree on the mutual reduction or elimination of customs tariffs, but each member country retains its own tariffs with regard to third countries. Another option is that of forming a customs union, which differs from a free trade area in that its member countries establish a common tariff with regard to third countries. Still greater integration is that represented by a common market: controls on movements of capital and labour are eliminated, so that not only goods but also factors can move freely. The stage of economic union is reached when the common market is complemented with supranational regional policies and the coordination of all branches of economic policy.

The present integration processes are clearly different from those of the 1950s and 1960s. The objectives have changed and have been reduced to a single aim: that of economic development; the orientation is now also outward-looking and aimed at world markets; the instruments have been changed into a macroeconomic framework with greater exchange and tariff transparency; among the agents involved,

the private sector is now the main source of dynamism of the process; and the international political and economic environment with regard to integration processes has changed.

*2. The reasons for its actuality*

A set of both domestic and external circumstances affecting the countries of Latin America has placed integration in the foreground of the current regional economic debate.

Among the domestic circumstances are the new emphasis on export-oriented activities, within a framework of growing internationalization of the national economies. Integration boosts trade and –even more important in the medium term– favours growing international specialization in production, thus making it an important factor in the modernization of the latter. Its current objective, rather than giving integration an “outward-looking” attitude –as proposed in contrast with the type of integration which accompanied the import substitution process– is to speed up the changes in production patterns in the region.

An export strategy must take account both of primary commodities –which, although registering sluggish growth, are the goods which give the region its static comparative advantages– and products with greater added value. Incorporation into the international economy through dynamic exports of growing complexity seems to be the most promising way of increasing productive employment and the payroll in a rapid and sustained manner, thereby contributing both to growth and equity. This second export phase is closely linked with the internationalization of production and direct investment. Expanded markets make possible optimum levels of production which minimize average costs and make it possible to increase the international competitiveness of the countries’ economies in various ways; this new integration is aimed at strengthening the incorporation into the international economy, favouring production linkages, and bringing about creative interaction between public and private agents (ECLAC, 1992).

Among the external circumstances, the enhancement of various regional trade agreements is to be observed at the world level, and in the case of Latin America, a noteworthy development has been the launching of the Enterprise for the Americas by President Bush. The region cannot fritter away the advantages of liberalizing its economic space and securing economic complementation within it, when other regions are striving to achieve this. At the same time, in order to negotiate better trade agreements with the industrialized countries it is necessary to achieve strengthened bargaining power, and this could be facilitated through the existence of broader associated markets. It is foreseeable that, other things being equal, the industrialized countries will prefer to come to agreements with larger integrated trade areas.

Looking at the situation from another point of view, the orientations of the national economic policies of the countries of the region are tending to converge, and this acts as an endogenous factor favouring the integration process. The great diversity and inconsistency of those policies in the past, which represented a formidable obstacle to integration, are giving way to efforts –albeit with very different starting points and paths– to achieve high and stable real exchange rates, low and even tariffs, interest rates not too far out of line from international ones, and few or no restrictions on foreign investment. In this way, the trade flows provide solid and durable bases for development and for the international specialization of production, including direct investment (Lahera, 1992).

The future of this still incipient process is not yet assured, since although the international economy will continue to be the “great coordinator” of macroeconomic policies (through the costs involved in departing from it), there will undoubtedly be some countermarches. A number of effects have already taken shape, through the expectations which this process has generated, but their consolidation is a matter which remains to be seen.

The various factors referred to above mutually strengthen each other, and it is possible that none of them may be determinant on its own. This explains the diversity of the present integration process, which is one of its most outstanding features. In some cases, the main impulse in favour of integration is the similarity of macroeconomic conditions; in others it is the enormous potential for economic

complementation, in spite of macroeconomic divergences; in other cases, it is the advantage of being able to negotiate collectively with the United States and Europe; and in still others it is the renewal of long-standing commitments. Moreover, with regard to free trade agreements with industrialized countries, it is not so much a question of trying to obtain tariff reductions as of eliminating non-tariff barriers for some products and, in general, achieving better and more stable trade and investment relations with those countries. As a very minimum, efforts must be made to ensure that the present level of protection in those countries does not increase, especially as a reaction to the export successes of developing countries.<sup>2</sup>

This continuity of efforts to promote regional and hemispheric integration, which was unthinkable only a few years ago, is also a result of the factors already noted in this article (Juan Alberto Fuentes, 1991). Henceforth, it would be highly undesirable for the liberalization process to stop at this point and exclude other economic areas of the world on a permanent basis.

### *3. Integration and international trade*

From one point of view, integration may be analysed as a specific aspect of international trade theory. From another viewpoint, such trade may be placed within the framework of integration, with the latter being understood as a dynamic factor for economic development, with all its aspects in terms of specialization of production, both for the region and for the world economy.

In international trade theory, integration was a suspicious expression for a long time, particularly because the integration process, if successful, has an indisputable, although temporary, effect of diverting trade. This would mean leaving aside the optimum free trade scenario, which permits the best possible international specialization in line with the comparative advantages of each country. This optimum scenario would be obtained by integrating all markets, without restrictions such as tariffs, managed exchange rates, prior import licenses, etc. In this way, the theory asserts, goods would be produced where it was cheapest to do so, for the benefit of all.

<sup>2</sup> This idea was suggested to me by Joseph Ramos.

In principle, a correct manner of judging the general economic effects of a free trade area would be to compare the real income that would be obtained if it existed with that which would be obtained if no such changes were made. This totalizing approach is difficult to apply, however, so that in evaluating the effect of integration on international trade it is usual to distinguish, in line with Jacob Viner's studies, between the trade creation and trade diversion effects (Viner, 1950).

In general terms, international trade provides benefits by making goods available to users at lower cost. When a free trade area is formed, however, two different movements are generated: one member purchases from another goods which it previously produced domestically, thus improving efficiency by reducing costs. Trade also suffers some diversion, however, since one member may purchase from another goods which it previously imported from third countries.

Creation of trade normally brings benefits for all the countries involved, thanks to the increase in exports and the acquisition of imports at lower costs, thus promoting more efficient resource allocation. At the same time, however, the distribution of the benefits between the countries cannot be determined in advance. Diversion of trade involves a loss of well-being because of the importation of products which are more expensive than those produced outside the integration area; at all events, its net impact on consumption will depend on the variation in tariffs. By increasing the product, however, the diversion may benefit third countries whose exports thereby increase. The general theoretical conclusion is that if creation of trade predominates, then efficiency will improve; if trade diversion predominates, then the efficiency will go down. This issue arises differently in a free trade area compared with a customs union. The conditions needed for the phenomenon of diversion to take place are more restrictive, and their application almost always differs from one country to another.

However, there are reasons why integration may be an appropriate course even in the second case (Wonnacott and Lutz, 1989). Three different situations may arise in this respect: in the first case, the diversion of trade is the result of a selective reduction of tariffs and the new prices may be lower, even when the production costs of the exporting country are higher than those of the previous suppliers.

In the second situation, the economies of scale achieved through integration may allow the costs of the third producers to become competitive. In the final analysis, the undesirability of trade diversion is based on the assumption that tariffs form the main trade barrier. To the extent that other protectionist measures proliferate, however, it is no longer so clear that trade diversion will necessarily reduce efficiency.

In the third situation, the lack of transparency of exchange rate regimes and balance of payments disequilibria may mean that the imports which have the lowest monetary costs may not precisely measure the economic costs. They are not always the imports with the lowest opportunity costs.

From another point of view, the success of an integration programme in the region may not only create new exports, but also increase the global import capacity of the group. Thus, the dilemma between creation and diversion of trade may be rather artificial in the case of countries with imbalances and scarce resources.

If the protectionism against third countries is not increased, integration is an approach which will bring closer relations than free trade, rather than divergence: this possibility is recognized in article XXIV of the General Agreement on Tariffs and Trade (GATT).<sup>3</sup> This point of view is also gaining ground in the literature on this subject.<sup>4</sup> The countries forming part of such agreements can gradually attain a situation where they can conduct their external trade and their investments abroad with fewer restrictions. The process of convergence of economic conditions facilitates investment flows to and from other countries and allows discussion to be focused on the other economic, legal and administrative conditions which are of decisive importance for such productive investment.

<sup>3</sup>This article states that for the purposes of GATT, free trade agreements must fulfil four requirements: they must be of broad scope, that is to say, they must cover a substantial part of the trade between countries; they must be applied over a reasonable transitional period; they must not raise barriers to the trade of other contracting parties, and they must contain rules to identify the origin of the goods covered by the Treaty.

<sup>4</sup>See the arguments in this sense in Lawrence (1991).

It is for these reasons that integration is seen less and less as an option which is in contradiction to international free trade. The truth is that it would not be realistic to assume that both are equally viable, or that economies of the size of the Latin American ones can freely choose in this respect. In practice, integration may be considered as an effective way of coming closer to freer trade, in view of the existence of distortions and imbalances whose total elimination is outside the reach of the member countries alone.

From another point of view, to the extent that the effects of trade liberalization are greater than those of geographical discrimination, integration will contribute to the formation of a less discriminatory international economy.

#### *4. Integration and changing production patterns with equity*

Integration and intra-regional cooperation are functional to the achievement of broader development objectives. Outstanding among these is the transformation of production patterns, as proposed by ECLAC (1990a).

Integration commitments may facilitate the application of the systemic approach which is characteristic of this strategy; increase the efficiency of the production process and help to incorporate technology in it; give rise to economies of scale in both production processes and in the infrastructure; reduce monopoly and oligopolistic rents, and give rise to new investments. Integration is compatible with

the objective of increasing international competitiveness, and it can help to attain it.

Enhanced trade would help to lay the basis for systems of specialization and competition which would facilitate changes in the production patterns of each country. This would make it possible to take more advantage of intra-regional comparative advantages and of the opportunities for sectoral and intra-sectoral complementation.

Mutual cooperation would help to strengthen exports to countries outside the region, thus enabling many medium-sized or small countries to achieve advances that would be almost impossible for them in other circumstances.

From another point of view, by causing the participating economies to be more closely related with each other, expansion of mutual trade would make them more similar in their cyclical fluctuations, thereby requiring similar monetary and fiscal policies. Consequently, speculation on short-term interest rates and exchange rates would be reduced, and there would be more freedom in the balance of payments for long-term investments seeking greater marginal productivity of capital.

Integration can expand the effects of innovation by reducing the average costs of technological research and development, increasing the efficiency and use of specialized inputs or support services, and generating technological externalities. Thus, an expanded market would make it possible to derive greater advantage from investment in research and development by exploiting economies of scale and reducing the cost/sales ratio.

## II

### Obstacles to integration

#### *1. Macroeconomic policy*

A prior condition for furthering a broad integration process in the medium or long term is that there should be a minimum degree of macroeconomic stability. Moreover, it has traditionally been recognized that growing harmonization of economic policies must be sought in order to progress in the integration process. This is a difficult objective to attain,

however, since it is conditioned by the existence of various imbalances, for some of which integration itself is proposed as a remedy. Thus, the argument takes on a circular form and may give rise to structuralist pessimism or technocratic voluntarism.

Exchange rate instability gives rise to uncertainty about the evolution of relative prices, and this in turn causes higher risks for investments, creates maladjustments in the allocation of resources

between tradeable and non-tradeable goods, and gives rise to financial instability, with its well-known effects on the monetary sector. At the same time, imbalances lead to the failure to fulfil commitments that have been entered into, thus undermining the very idea of integration. Finally, financial imbalances may cause variations in the real exchange rate and obscure the transparency of policies, hindering reciprocal flows of trade and capital; moreover, they can also heighten the differences already existing between countries by leading to concentration of foreign investment in the most stable countries (Alfredo Fuentes, 1991).

### *2. Trade and investment policies*

The possibility of selecting only a certain set of products in some integration agreements favours the granting of preferences in sectors where there is little trade potential, in order to obtain greater openness than that normally granted. It also gives rise to a permanent review of the preference lists with a view to their possible expansion or rebalancing, which brings a constant element of uncertainty into the agreements and complicates the negotiations, as well as discouraging the participation of the private sectors. Furthermore, in those cases where the opening-up is not of a general nature, it leads to inter-sectoral distortions which favour unjustified privileges and make better resource assignment impossible (Noyola, 1991).

As in the case of tariff preferences, non-tariff barriers have traditionally been eliminated in respect of a limited number of products which are normally not those offering the greatest opportunities for trade.

Moreover, the current agreements have generally not defined machinery for settling trade disputes, which has facilitated failure to fulfil commitments entered into, trade reprisals, and general uncertainty about the application of the concessions negotiated.

Nor is there currently a full system of statistical information on the exports and imports of Latin America and the Caribbean. The external trade statistics come from customs registers, and this decisively affects the quality and nature of the information in them: it affects the quality because this depends on the degree of reliability of the registers; and it affects the nature of the information, because these registers are used for the ongoing adaptation of customs

duties, that is to say, they are designed to fit in with the characteristics of tariff systems and are not suitable for economic analysis. Moreover, some external trade practices, such as the operational and marketing systems for carrying out external trade transactions, have certain special features which make it difficult to keep proper registers and affect the type of statistics thus compiled.

### *3. Sectoral policies*

There is a great variety of special regimes for specific economic activities, industrial branches and geographical locations of enterprises in the region, and these regimes also differ from one country to another. This complex system of regulations, as well as not being very efficient as a means of promotion in the present circumstances, makes it difficult to build up common economic spaces and favours the consolidation of anti-integration interests.

### *4. Consistency and convergence*

The simultaneous –or even consecutive– negotiation of various different agreements entails considerable difficulties of coordination and adaptation. Moreover, there are serious difficulties in managing an excessive number of bilateral or subregional agreements, and if these also include special conditions, they will present serious problems of transparency for exporters, importers and investors.

A particularly complex matter is the joint administration of new agreements and “inherited” commitments already negotiated. Article 68 of the Cartagena Agreement –the Treaty which gave rise to the Andean Group– lays down that trade agreements established outside the Cartagena Agreement must have the approval of all its members. In 1991, however, the Guayaquil Commitment confirmed the possibilities of bilateral or community negotiations with other countries and referred to the desirability of regulating the application of article 68. In the case of ALADI, agreements can be made at various levels –regional, bilateral and sectoral. Each one includes different lists of products with levels of preferences varying from 2% to 100%. This makes it a very complex matter to administer, understand and make use of the agreements, thus making it difficult to take full advantage of them and consequently limiting their impact on trade flows (ALADI, 1991).

The possibility is now being proposed of a free trade agreement with the United States under the Enterprise for the Americas Initiative launched by President Bush. The question of integration between economies of different levels of development is such a novel matter that it has not yet been covered by the specialized literature. A central issue in this type of agreement is that the developing countries cannot obtain unilaterally discriminatory treatment, except in a few expressly agreed cases. For example, they cannot take advantage of the rights laid down in GATT without also accepting its obligations. Moreover, it is also necessary to include such matters as services, which are of great interest to the developed countries. Another matter is the extension, extent and speed of application of the agreements.

Various countries and groups of countries of the region have special trade relations with some developed country or group of countries. Examples of this are the relations of the Caribbean countries and territories with the United States under the Caribbean Basin Initiative; the tariff preferences granted by the United States to the Andean countries, and the participation of some countries in the Lomé IV Treaty with the European Community. These are unilateral trade systems, different from the dynamics of an integration process. A similar case is that of the Generalized System of Preferences. Conversely, there are countries which are affected by United States trade sanctions: Nicaragua, until recently, and Cuba.

The countries of the region encounter a very low tariff structure in the United States which is almost without exception lower than their own. Thus, generally speaking quantitative and non-tariff restrictions may be of greater sectoral importance, and they will also be the most difficult ones to dismantle. In some economic sectors and subsectors, a free trade agreement with the United States will be particularly complex to negotiate, or will require longer transitional periods (in the case of agriculture, for example).

Although it is unlikely that the region's exports to the rest of the world will be affected by a free trade agreement with the United States, it is possible that part of its imports from the rest of the world will be reduced in favour of imports from the latter country. The United States and Canada currently provide only one-third of Latin America's imports, so that there is big potential for diversion of trade;

consequently, under no circumstances should the agreements arrived at involve the application of common barriers to imports from other areas.

#### *5. Aspects concerning financial matters and clearance of payments*

In the last two years, ALADI, the Central American countries and the Andean Group have considerably improved the operation of their respective systems of payments and financing of trade. Basic problems still persist, however, with regard to the nature of mutual trade, and these demand further advances in this financing. The current difficulties with regard to intra-regional financial cooperation are due both to the influence of exogenous elements which affect the economies of the region and to the macroeconomic instability of the countries themselves (ECLAC, 1990b).

#### *6. Physical integration*

Most of the transport infrastructure of the Latin American countries has been constructed in order to export to the rest of the world the basic commodities produced by the region. This characteristic means that, in spite of the advances in integration achieved in recent decades, nearly all the countries of the region have higher transport costs in their intra-regional trade than in their trade with countries outside the region. This is so in spite of the shorter distances involved in intra-regional transport and is due largely to the lower density of transport within the region, since this is strictly subject to the principle of economies of scale and decreasing costs.

Progress in border integration is hindered by the lack of suitable institutional support. There are 16 South American and Central American countries with a total of 27 various kinds of projects for border integration, affecting most of these countries' borders. In a further 19 cases there are suitable conditions for such integration or efforts are being made by governments to reach formal agreement on border integration. Of the 27 projects backed up by formal agreements, however, only 12 have specific, permanent institutional organization, and of these 12, only four are actually structured as programmes (Bolognesi-Drosdoff, 1990).

### III

## Policy guidelines

### 1. *Macroeconomic policy*

The harmonization of economic policies is not usually exclusively the result of increased and closer trade relations. Indeed, on the contrary, in conditions of imbalance policy coordination measures precede those for trade liberalization. In these conditions, it is hard to see how there can be any considerable expansion of trade simply as a result of the removal of tariff obstacles. Moreover, the elimination of tariff and non-tariff barriers makes mutual trade still more sensitive to exchange rate fluctuations.

In the short term, it is unlikely that the bigger trade and investment deriving from integration will be sufficient on their own to lessen economic policy divergences to any marked extent, since both the external trade and mutual trade coefficients of the countries of the region and the flows of direct investment are still only at a low level. The key to progressive harmonization of economic policies seems to lie rather in the achievement of relative macroeconomic balance in the countries making up the group; consequently, its main factors would be the elimination of fiscal imbalances and the application of a more prudent monetary policy. At the same time, more realistic exchange rates and reduction of what Fernando Fajnzylber called "frivolous" protection would also aid the convergence of regional costs. These conditions would facilitate fuller application of the present mutual payments systems.

Some forms of partial harmonization of policies in economic preference areas have been suggested, including self-restrictive clauses for preferential treatment in favour of particular economic activities (industrial and regional promotion, for example) and the establishment of consultation and coordination machinery with regard to certain national economic policy decisions, especially on exchange rate matters (Halperin, 1990).

### 2. *Integration for changing production patterns*

The integration agenda could be reviewed and expanded so that its various items would tend to strengthen the process of changing production patterns rather than foster import substitution.

With regard to the interaction of the public and private sectors, experience shows that governments can create various conditions which are favourable to increased trade and investments, but it is up to the private sector to turn them into reality. Integration will not progress without the active participation of the private entrepreneurs of the respective countries, and this should take place from the earliest stages of formulation of the integration options, rather than merely being the result of the perception of new trade or investment opportunities by these agents. In view of the need for active links between the private and public sectors, at both the national and regional levels, which will frequently call for the coordination of entrepreneurial organizations representing the interests involved, it would seem advisable to set up bilateral entrepreneurial councils. The labour sector should also be informed and consulted, and the effects that various aspects of integration may have on the workers must be taken into account.

Integration must go beyond the mere reciprocal sale of surpluses: it must raise the international competitiveness of the economy by transforming the production sector itself and exposing it to greater competition in an expanded market, and it can lead to growing international specialization in production (Lahera, 1984). International competitiveness will improve to the extent that external trade goes beyond marginal levels and helps to modify national systems of production both in terms of the investments which have already been made and new investments. This is a process which must be strengthened if integration is to lead to growing international specialization in production.

The internationalization of production may take the form of horizontal expansion, in order to produce the same goods in the recipient country, or vertical integration –involving inputs or greater added value of products– which brings establishments in the recipient country into the global production process.

The prototype of horizontal integration corresponds to full local production, including local production of inputs, of a final good for the same market. The opposite extreme is internationally integrated production, with mostly imported inputs, of a product which in turn complements the production of

a final good to be marketed in various national markets. Obviously, there are also various intermediate types of specialization in production, as well as combinations of the two types already referred to (Lahera, 1988).

It would be unrealistic to try to remove from the influence of the market the distribution of production activities among the countries involved. Consequently, efforts to promote modernization of production and raise competitiveness must be directed more towards the generation of positive externalities than towards special treatment for particular products or sectors. There are extensive possibilities for cooperation in this field, especially with a view to technical change and environmental protection.

Agreements on double taxation and protection of investments are necessary complements to free trade agreements. There are still only a few of them, and this not only represents a barrier to specialization of production but also discriminates against local firms compared with transnational corporations from developed countries, which are increasingly protected by such agreements.

The elimination of subsidies on Latin American and Caribbean exports to member countries of subregional groups, which in fact already occurs in the case of the Central American countries, would avoid conflicts between exporters and domestic producers and obviate a struggle over incentives in the region. It is necessary to reach agreements on the subjects of services, investment and intellectual property, the clear definition and gradual liberalization of which will be of fundamental importance for promoting the interaction of some spearhead sectors of the economies of the area. The question of mobility of factors should also include that of the mobility of labour and should take account of various aspects of the labour market. At the same time, negotiations on subsidies and countervailing duties should continue within GATT, where the advantages of a multilateral forum for the weakest countries are evident. Moreover, it will be necessary to keep watch in order to ensure that industrial technical standards, and regulations on security and public health applied by the members of the agreement, do not artificially hinder mutual trade (Juan Alberto Fuentes, 1991).

### 3. Trade policies

Economies which are in a relatively balanced situation have more leeway for developing a broad range of integration policies, while at the same time

increasing their international economic liberalization. In these conditions, external trade policy could combine unilateral tariff reductions with multilateral free trade negotiations and with subregional or bilateral free trade agreements, as long as these do not involve raising barriers against third countries (Lahera, 1991). The same is true in the area of direct investment, the positive effects of which are further strengthened by similarities between local and international conditions, by non-discrimination between national and foreign investment, and by the elimination of export subsidies and discriminatory fiscal charges.

The debate on integration instruments should be broadened. The application of various instruments which could be considered as being of a strictly trade nature depends on other more general policies, while international production specialization depends on variables which go beyond the field of trade, and sometimes even on specific or sectoral policies.

Except for a few very sensitive products, the fixing of a maximum tariff and the elimination of non-tariff barriers will guarantee a certain level of openness and give greater confidence to importers and exporters. Starting from the maximum tariff, which does not necessarily need to be common to all the countries, a tariff reduction process with precise deadlines can be established which will eventually lead to total trade liberalization among the parties. The negotiations must concentrate on lists of exceptions to liberalization rather than on the lists of products to be liberalized. With regard to direct investment, it is desirable to guarantee non-discrimination on the grounds of origin of the capital and to simplify the conditions for its repatriation.

Likewise, the rules on origin must be clear and flexible, in order to be better adapted to the characteristics of some sectors. They must permit the compatibilization of two objectives –that of high regional content, and that of growing internationalization of production– in order not to hinder the latter process. The safeguard clauses must be of a general and temporary nature, and they must be gradually reduced with the passage of time. Moreover, it is essential to create legal instruments for the solution of trade disputes, with flexible and transparent procedures and the ability to compel the fulfilment of agreements, thus guaranteeing exporters access to the market. A suitable mechanism for these purposes is that of arbitration with decisions against which there can be no appeal.

Administratively, the handling of non-tariff barriers is more complex than that of tariffs, and it is more open to arbitrary action, distortions and pressure by interest groups. Consequently, from the first moment when subregional markets are set up, it would be necessary to promote the total elimination of non-tariff barriers, even if this were accompanied by some increase in tariffs in order to facilitate the transition process. On these issues, it is not possible to accept proportionality, but instead the need for total elimination must be spelt out in an unmistakable manner.

The negotiation of a free trade agreement with the United States and Canada must be complemented with simultaneous negotiations with other areas. Latin America should begin free trade negotiations with the European Community and with Japan as soon as possible, as a way avoiding the trade and production distortions that could arise from the successful conclusion of the negotiations with the United States and Canada.

In this process, it is necessary to avoid the consolidation of trade blocs which are inwardly open but outwardly protectionist. The trade diversion effect can take place both through the fixing of a common external tariff for the subregional or bilateral agreement which is higher than that previously prevailing in some of the countries, and through the elimination of tariffs within the respective grouping, while maintaining them with respect to third countries.

#### 4. *Consistency and convergence*

The task of combining various forms of integration calls for careful handling in order to avoid possible inconsistencies. In order to coordinate external trade policy, there should be a centralized technical body, probably in the area of economic policy management. It would seem necessary to progress towards the establishment of an international trade office, like those which exist in some developed countries, as has recently been proposed in some countries of the region.

The new regional spaces could be formed on the basis of an integration process simultaneously advancing in a number of directions at different rates, but with a single consistent overall orientation (CLEPI, 1991). It is also foreseeable, however, that options of high complexity may arise, including situations in which the "prisoner dilemma" occurs, especially with regard to countries which have few tariffs

to eliminate and few tariff barriers to dismantle. It might even seem a bad deal not to have tariffs to lower; this is an economic mirage, of course, but it is a political reality. Consequently, greater imagination is required in the negotiations, with broader definition of the objectives, instruments, deadlines and forms of integration.

The attempt to establish free trade with developing countries has specific elements which no general argument can remove, and it differs from the same process involving industrialized countries, but one process must not be subordinated to the other.

Integration with the countries of the North American Free Trade Area may take place through the formation of subregional groups, but there are also various possible combinations, including intermediate or simultaneous stages in this process. These stages could cover integration between existing subgroups and also the integration of subgroups with the North American Free Trade Area, with various Latin American and Caribbean countries, and with various countries of the North American area. If progress towards hemispheric integration were more rapid than regional integration, this could lead to massive diversion of trade from Latin American to North American products, especially because most of the countries of the region compete with the United States in markets in the area in a wide range of products (Lrzan and Yeats, 1992). Looking at the matter from another point of view, a country which is in a position to sign a free trade agreement with the United States could normally also do so with the other countries of the region.

The pre-existing agreements between countries of the region and some industrialized countries, in which special conditions are granted on a unilateral basis, must be gradually incorporated into a general framework which takes account of the different situations and compensates for them.

#### 5. *Trade facilitation*

In addition to conditions of a macroeconomic type, other factors which facilitate integration are the elimination of administrative hindrances and improvement of the physical, transport and telecommunications infrastructure.

The effective integration of the region makes it necessary to link together the transport systems more closely, thus advancing towards the creation of a land, sea and air transport market which is

increasingly integrated and open and in which there is equality of conditions.

In land transport, it is necessary to promote the liberalization and facilitation of passenger and cargo transport in order to make the available supply of these services broader and more flexible. In air transport, it is necessary to expand freedom of traffic in order that all the airlines of the region may have the possibility of operating and competing in line with the conditions of each country.

In sea transport, it is necessary to take measures to give South American shipping companies freedom of access and facilities for improving their capacity to compete, while respecting the principle of reciprocity. The geographical characteristics of the region make sea transport the most appropriate form for international trade, over 90% of which is carried by this means. Without a coordinated policy on ports and sea and land transport, the countries of Latin America and the Caribbean would run the risk of being limited to only minority participation in the sea transport consortia from outside the region or to the mere provision of linking services with ports where the cargo would be transferred to bigger ships, or to the provision of land transport services in the region (ECLAC, 1989).

The participation of the private sector is of key importance for the development and maintenance of the physical infrastructure, but the public sector must make available its technical and financial resources if these objectives are to be reached.

#### *6. The relatively less developed countries*

As experience shows, reciprocity in the benefits of integration is both an objective and a condition for the success of the process, since a country cannot be expected to participate in it if, in the long term, its costs exceed its benefits. It is improbable

that integration will have completely even-handed effects, however, since the initial differences may tend to increase rather than diminish. It must not be forgotten that changes in trade policies and in the form of insertion in the international economy normally cannot automatically eliminate differences in the specific situations of each country, including its resource endowment—especially of human resources—and its level of development.

There are no technical recommendations which can alter this basic economic fact, although it is possible to suggest compensatory or balancing measures which do not represent any impediment to the integration process. Moreover, the dynamism deriving from the integration process affects each participant's view of the medium-term effects of this process on the various economic sectors. The very concept of reciprocity must be defined more broadly and must incorporate a bigger time dimension.

It will therefore be necessary to adopt compensatory or balancing measures. Some degree of flexibility in fulfilment of the integration objectives and support for increasing the exportable supply of countries of relatively less development could be considered for this purpose.

Small economies are characterized by their higher degree of openness and are therefore more vulnerable to fluctuations in the economies of their trading partners. Their export sectors are relatively weak and encounter serious structural obstacles on the supply side when they try to increase their exports (Salazar and Lizana, in the press).

Moreover, the application of very strict rules of origin would adversely affect the weakest economies, which generally have less capacity to export products with a higher proportion of added value or of domestically produced materials. The application of rules which are not excessively strict would therefore be justified.

## Conclusions

Economic integration cannot give short-term responses to the problems of adjustment, stabilization and growth of the Latin American countries. Indeed, it could hardly be expected to do so. The integration process has its own particular type of complexity, and its results are not automatic. To

begin with, its effects will necessarily be limited, in view of the low global coefficient of external openness of the countries of the region (around 25%) and the limited share of intra-regional trade in the product (between 10% and 15%). As changes in production patterns become more pronounced and

the structure of production of the countries making up integration groups becomes more diversified, however, integration will be more viable, since it will expand the base for trade and specialization in production.

Moreover, taking another point of view, integration is not a linear process. In some cases, it might be possible to make very rapid progress. In contrast, however, severe setbacks could be suffered in the event of a major economic crisis: in this case, intra-regional trade would be affected, but not so severely as intra-regional direct investment, which

perforce follows the ups and downs of the recipient economies.

To sum up, integration is a winning idea, and its management is a complex but perfectly possible matter. It will be necessary to move very carefully, respecting the specific features of bilateral or regional economic relations and the need to avoid inhibiting the global trend towards free trade. By following this strait and narrow path, with the difficulties that have always marked the development process, integration will become a factor in the economic modernization of Latin America.

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## Globalization and convergence: Latin America in a changing world

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A new international order which is the result of the recent changes in international political and economic relations is in the process of formation. The initial characteristics of this order point to a world setting in which the centripetal forces seem to be more marked than in the past and are leading to a more convergent world favourable to greater consensus, in which the actions of each country have repercussions on those of the others, so that concertation and harmonization become necessary. Together with these forces, however, there are others of a centrifugal nature, such as the awakening nationalisms in eastern and southern Europe and the pressures for greater protectionism by those who are having to bear the burden of the adjustment to a more convergent world. These pressures have caused some analysts to fear that the world will be divided up into opposing trade blocs. Furthermore, the multipolarity emerging in economic relations makes it more difficult to coordinate policies, which is an important feature of the necessary harmonization. Consequently, the new international order opens up an era fraught with possibilities, but also with uncertainties and hence risks for the world in general and Latin America in particular.

Section I of this article indicates the main changes which have favoured the emergence of the new order, while section II describes the main features of that order, especially with regard to convergence in North-South relations, interdependence and the need for harmonization in the world economy, the possibilities offered by the new international context for obtaining resources for development, and the new multipolarity of economic relations.

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## I The main political and economic changes

Since the late 1980s and during the first years of the 1990s, profound changes have taken place in the world scene (a chronological list of the main changes which have taken place since mid-1989 is given in the annex). Of these changes, possibly the most important are the great transformations in the Eastern European countries, which found their symbolic expression *par excellence* in the fall of the Berlin Wall in November 1989. In addition to the process of reform underway in the former Soviet Union, there are the political changes in the Eastern European countries, the main landmarks of which took place between October 1989 and January 1990, opening up the way for the transition of the centrally planned economies of those countries to market economies, as well as the reunification of Germany in October 1990. Outstanding among the ramifications of these events is the end of the Cold War and of the bipolarity which characterized much of the twentieth century. The virtual disappearance of the socialist option as historically represented in Eastern Europe and the end of the ideological struggle of previous decades have completely overturned previous views on world political and economic relations.

The effects of these sudden changes have come on top of a phenomenon which has characterized the world economy in recent years: the process of globalization. This process has been taking place for some time, but only recently, as it gathered force, has there begun to be a generalized awareness of the phenomenon and its implications, especially for the developing world.<sup>1</sup> Globalization is yet another manifestation of the growing interdependence which exists between nations, and it forms part of a historical trajectory which began with the increase in international trade and continued with the internationalization of finance in the 1970s, when the size of international capital flows exceeded for the first time that of trade flows.<sup>2</sup>

<sup>1</sup> For an early analysis of the consequences of the growing integration of the world economy, see Sunkel (1971).

<sup>2</sup> The presentation made below in this article is based in part on the analysis of the concept of globalization and its consequences made at an expert meeting on *International Governance: Trade in a Globalizing Economy*, organized by UNCTAD in Jakarta, Indonesia, on 19 and 20 June 1991.

The globalization of the world economy is one aspect of a broader phenomenon which affects all dimensions of human life: population growth, poverty, employment, endemic diseases, the narcotics trade, the environment, etc. In its economic variety, globalization is a result of the speeding up of technological progress in general, which affects competitiveness in all sectors, and advances in information and transport technologies in particular, which cause changes in the way companies and countries trade with each other. These phenomena, together with liberalization and deregulation of markets in the more developed countries, have led to the establishment of transnational production systems or networks. This has taken place as a result of the expansion of the sphere of influence of transnational corporations, the organization of strategic alliances between firms, including firms from different sectors, and the generalized use of world information and communication systems. An important and growing part of world trade takes place under these systems.

These new forms of organization of production result in the redefinition of comparative advantages, in which ongoing innovation and the global nature of business organization and strategies have a decisive influence. Some concrete manifestations of this are the rapid internationalization of production and the fact that trade grows faster than the product; the increase in the intra-sectoral component in world trade;<sup>3</sup> greater mobility of the factors of production and the crucial function played by foreign investment in the growth of production and trade; integration among the various sectors of the economy at both the national and the international level; the growing importance of services in international trade, and the reduction of the differences between economic policies with different objectives (for example, industrial policies and trade policies or policies designed to increase competitiveness), with emphasis on the need for the systemic integration of these policies.

<sup>3</sup> Intra-sectoral trade means the simultaneous export and import of manufactures forming part of the same product line. De Castro (1989, p. 2) notes that intra-sectoral specialization and the resulting trade are affected, *inter alia*, by the internationalization of production and structural convergence among the trading countries, as well as technological factors.

Globalization is an unavoidable fact of life for the Latin American countries, just as it is for other nations, and it means both opportunities and challenges.

It means opportunities, because it forms the frame of reference within which the countries can incorporate themselves into the international flows of investment, trade and technology on which their economic growth prospects so vitally depend. Globalization does not necessarily extend to all countries, however; indeed, it shows strong tendencies towards concentration and inequality in the geographical distribution of its benefits, and many developing countries are still on the sidelines of the process because of certain structural shortcomings. Among the latter are their low level of technological and human resource development, along with insufficient technology transfer; small markets; a faulty infrastructure; restrictive foreign investment regimes; poorly developed financial systems, and limitations on the access of their exports to outside markets.

It represents a challenge, because it is essential to put these shortcomings right in order to take advantage of the opportunities offered by globalization, through positive participation in a way which makes it possible to avoid the risks inherent in a process which takes place mainly beyond the control of the Latin American countries. The elimination of such obstacles is necessary, for example, in order to stimulate foreign investment, which occupies a leading place in the globalization process. This must be achieved, however, without overlooking the risks connected with possible restrictive trade practices – such as inter-company agreements to limit competition, market sharing arrangements, the use of transfer prices, prohibitions on exports to certain markets, etc.– and the effects of the exclusion of third countries which the new organizational practices can bring with them. The awareness which exists of the importance of these issues is clearly seen in the negotiations and discussions taking place in international forums such as the General Agreement on Tariffs and Trade (GATT).

The recent developments in the area of relations between East and West combine with the above-mentioned tendency to the globalization of the world economy to make up a new emerging international order, and this order defines the international setting in which the Latin American and Caribbean countries must operate.

## II

## The structural characteristics of the new international order

## 1. North-South relations and the process of convergence

## a) The new multilateralism

The new international order which is taking shape is quite different from the New International Economic Order (NIEO) whose pursuit by the developing countries has characterized North-South relations since the 1970s.

The demands for the NIEO were the result of the situation then created on the international scene by the appearance of a number of sovereign developing countries as a result of decolonization. These countries, organized politically in the Movement of Non-Aligned Countries and economically in the Group of 77, proposed changes which would make the international economic system more favourable to the achievement of economic development. As a result of these demands, in May 1974 the United Nations General Assembly adopted a Declaration and Programme of Action on the Establishment of a New International Economic Order.<sup>4</sup> This Declaration and Programme of Action, together with the Charter of Economic Rights and Duties of States and the resolution on development and international economic cooperation (adopted by the General Assembly in that same year and in September 1975, respectively), formed the programmatic base of the NIEO.<sup>5</sup>

The Programme of Action for the NIEO provided for the changes needed in the main areas of North-South relations in order to achieve: i) effective control by the countries over their natural resources; ii) regulation of the activities of transnational corporations; iii) fair and equitable prices for basic commodities and other exports of the developing countries; iv) reforms in the world monetary and financial systems; v) market access for the products of the developing countries, and vi) strengthening of the scientific and technological capacity of the developing nations.

<sup>4</sup> See resolutions 3201 (S-VI) and 3202 (S-VI) adopted by the General Assembly at its sixth special session.

<sup>5</sup> For a detailed description of the NIEO, see Sauvant (1981).

In the first few years after the adoption of the Programme of Action, some progress was made towards the application of its provisions. Among other things, the establishment of the Generalized System of Preferences was accompanied by the establishment of new institutions to deal with the problems of the developing countries, such as a Common Fund for Commodities, which was set up later, and the United Nations Commission on Transnational Corporations. In GATT, the Tokyo Round negotiations led to the adoption of the so-called *enabling clause*, whereby it was made permissible to give special and different treatment to developing countries. A set of rules and principles to control restrictive trade practices, a convention on international multimodal transport, and a code of conduct for shipping conferences were adopted, and negotiations were started on, *inter alia*, a code of conduct for technology transfer, a code of conduct for transnational corporations, and a review of the system of industrial property.<sup>6</sup>

However, the reforms achieved were of very limited scope and did not affect the structural foundations of the established order. In the 1980s, the negotiations stagnated, so that many aspirations of the developing countries were never realized. This was the decade of the "adjustment". The negotiating climate took on some characteristics of a confrontation between the supporters and opponents of the NIEO, against the background of the rivalry between the two opposing development models for the Third World: the western capitalist model and the socialist model. In an atmosphere like this, reminiscent of the East-West confrontation, the position of the developing countries, which was now markedly weaker than in the golden years of the Organization of Petroleum Exporting Countries (OPEC), was not strong enough to secure the desired agreements with the developed countries.

<sup>6</sup> For a fairly exhaustive list of the advances made, see United Nations (1983).

The lessons learnt in that period have now been assumed as part of the consensual basis of the new world order. The developing countries must be more self-reliant in solving their problems, and only the poorest of them can expect unilateral concessions from the developed countries to represent a substantial contribution to an improvement which is largely beyond their own unaided capacity. As a result, the domestic economic policies of the countries have been the subject of greater attention in world forums.

Nevertheless, the end of the ideological conflict between East and West in a context of globalization of the world economy opens up new prospects for multilateral cooperation for development. Now that some of the main factors of confrontation of the past have been eliminated and interdependence has been accepted by all countries as a reality, it is possible to revitalize the arguments for a NIEO on the grounds that a more equitable world is in the interest of all countries, including the richest ones. Consequently, a new kind of language is now being used in North-South relations. The OECD countries explicitly recognize the links between suitable domestic policies and a positive international economic environment, accept their particular responsibilities within the context of growing interdependence, and also recognize the importance of acting in partnership with the developing countries on the whole range of major world economic questions (OECD, 1991, paragraph 4). Many developing countries, for their part, have now declared that they have resolved to leave behind the tactics of confrontation in order to embark instead on "more pragmatic policies".<sup>7</sup> This new climate is reflected in the Declaration adopted by the member countries of the United Nations Conference on Trade and Development (UNCTAD) at its eighth session (held at Cartagena de Indias, Colombia, in February 1992), which embodies what is described in the same Declaration as the "Spirit of Cartagena". Naturally, this spirit of consensus remains to be translated into concrete measures, and this is the challenge that will be facing multilateral cooperation in the years to come.

<sup>7</sup> Address delivered by the Deputy Minister of Foreign Trade of Iran, in his capacity as Secretary-General of the Ministerial Meeting of the Group of 77 in Teheran on 18 November 1991. See also United Nations (1991).

#### b) *Convergence on economic policy matters*

The new spirit of multilateralism referred to above is based on a growing consensus on the priorities and instrumental mechanisms of development. This consensus takes many forms and has been expressed, for example, in the results of deliberations in multilateral forums such as the Declaration on International Economic Cooperation and the International Development Strategy for the Fourth United Nations Development Decade, recently adopted by the United Nations General Assembly, and the documents prepared at the eighth session of UNCTAD. Greater consensus facilitates the acceptance and application of the new development policies in the Latin American and Caribbean countries.

With regard to priority objectives, there has been increasing recognition all over the world that development cannot be reflected only in the evolution of the macroeconomic variables, but must be manifested above all in an improvement in the living conditions of the major part of the population—especially the most underprivileged sectors—with the specific objective of reducing poverty.<sup>8</sup>

Furthermore, the world community is now keenly aware that development must be compatible with the preservation of the environment and must not contribute to its destruction. The environment is seen as the patrimony of all mankind, and the actions of the various countries in this field have repercussions which go far beyond their national frontiers. International concern for the environment has been manifested in the efforts made now and in the recent past to arrive at operational agreements in various intergovernmental forums and meetings, especially the United Nations Conference on Environment and Development (the "Earth Summit"), held in Rio de Janeiro in June 1992. The relation between the environment, trade and development is expressed in the programmes of UNCTAD and of GATT itself, which agreed in October 1991 to reactivate its working group on trade and environment to discuss these issues.

<sup>8</sup> See, for example, Pronk (1991), pp. 21-22.

The greater consensus on major development strategies extends, *inter alia*, to the indispensable function of the market and of private enterprise, together with the recognition that private enterprise and public policies are complementary and equally necessary, and the desirability of greater openness of the economies. In this respect, there has been a rapprochement between liberal and structuralist attitudes. The latter, in response to changes in the international situation, have recognized that import substitution policies are now exhausted and outmoded and are incapable of generating the foreign exchange needed for development. In place of them, they see trade openness and exports as the natural following stage for taking advantage of the industrial platform set up in the previous stage (Sunkel and Zuleta, 1990, p. 44). The supporters of liberalism, for their part, now accept that the State has an indispensable function to carry out in correcting the shortcomings of the market.<sup>9</sup> This greater agreement is undoubtedly based on the consensus which exists on the priority objectives of development, since the market alone has proved to be a very imperfect instrument for achieving social equity and protection of the environment. This consensus must not cause us to forget, however, that there are still important differences of opinion, deriving from the different diagnoses of the problems, with regard to the actual policies that should be applied.

## 2. *The trend towards harmonization in the world economy*

The growing globalization and integration of the world economy has been reflected in constant pressures for the elimination of the barriers to such integration presented by obstacles to the movement across national frontiers of goods, services, capital and technology, to say nothing of people.

The first obstacles which it was sought to eliminate were those encountered at the national frontiers. After successive negotiating rounds in GATT, tariff barriers to trade were spectacularly reduced in the main developed countries: in 1987, the weighted average tariff for imports was only 4.3% in the United States, 6% in the nine member countries of the European Community (EC) and 2.9% in Japan. Some efforts were also made to reduce non-tariff barriers, as witnessed by six of the codes negotiated at the Tokyo Round.

<sup>9</sup>See, for example, World Bank (1991).

With such a considerable reduction of frontier barriers, it became clear that this reduction alone was not enough to make possible full mobility across borders, and it became more obviously necessary to harmonize the measures whereby governments regulate conditions of competition, so that the scope of the negotiations was expanded in consequence. As a result, the dividing line between trade and other policies became increasingly vague (Tussie, 1991). The tendency to harmonize a set of measures and public policies which go beyond the strictly trade area has been observed both at the multilateral level (especially in the trade negotiations in the Uruguay Round of GATT) and at the level of groups of countries (particularly with the development of economic spaces which are advancing towards integration).

### a) *The Uruguay Round*

The Uruguay Round of GATT, which had begun in September 1986, was scheduled to end in December 1990. This did not take place, however, and the breakdown of the negotiations at that date, together with their subsequent long and arduous continuation, highlight the serious difficulties facing attempts to secure international management of the interdependence of the countries involved.

The Uruguay Round agenda was much more ambitious than that of preceding rounds. In spite of the substantial tariff reductions achieved in the past, there were still major tariff barriers in respect of some sectors and products, and during the 1980s there was a certain proliferation of protectionist measures in sectors and countries (especially in the developed nations) which were suffering the consequences of the adjustment to the new conditions of competition in the world economy. These measures were above all of a para-tariff rather than a tariff nature: anti-dumping investigations and duties, countervailing duties and voluntary restrictions on exports were all used as discriminatory instruments which evaded the GATT rules. The idea was that the Uruguay Round should serve to negotiate measures to make these practices subject to stricter rules and disciplines, as well as achieving greater tariff liberalization.

The mandate of the Round went further than that, however. For the first time, a round of trade negotiations included such matters as rules on intellectual property, external investment regimes, and the services sector. Consequently, the Uruguay

Round negotiations have run into the problems and forms of resistance that naturally arise in the course of the harmonization of an ever-broader set of national policies. For example, the discussions have included such issues as the subsidies used by countries to keep up the standard of living of their rural population, attain food self-sufficiency, or promote the investments needed for economic development; measures designed to ensure that foreign investments make an effective contribution to development and to check the restrictive trade practices of transnational corporations; and measures on the protection of the intellectual property that the technologically less advanced countries need to use in order to relieve poverty, promote public health, and satisfy the food requirements of their population.

Carried to its extreme, the final result of the harmonization process would be to turn national markets into sub-areas of a global market and to subordinate national policies to a uniform global policy, with all the limitations that that implies for independent national policy.

In this context of interdependence of nations and strengthening of mutual relations between national policies, internationally accepted rules and disciplines, and the functioning of the market, the Latin American countries have shown their interest in the negotiations by participating actively in them. After having made a big effort to open up their economies on a unilateral basis,<sup>10</sup> their legitimate objective in the Round has been to secure the reversal of the protectionism which affects their exports, the establishment of clear and strengthened rules of the game in international trade which protect all the parties involved, especially the weaker ones, and recognition of the disparity in the levels of development of the parties and the application to them of treatment in line with those disparities when it is necessary to enter into new commitments, especially in the new areas of services, foreign investments and intellectual property rights (ECLAC, 1991a, section II).

#### b) *The development of economic spaces*

The evolution of the Uruguay Round has highlighted the difficulty of harmonizing policies and rules in the heterogeneous group formed by the more

than 100 member countries of GATT, with different levels of development and in many cases reluctant to give up part of their national sovereignty insofar as it affects the adoption of their own policies. The process is more viable when carried out in a limited number of countries with greater affinity with each other. In this respect, during the last two years there has been an accentuation of the trend towards the consolidation of regional economic spaces and the signing of bilateral agreements between countries. The creation of such spaces, in the form of free trade areas, preferential agreements and customs unions, is recognized and accepted, subject to certain conditions, in GATT itself, even though it represents a departure from the principle of non-discrimination which is the cornerstone of that Agreement.

i) *Consolidation in Europe.* The most advanced example of this process of harmonization and integration is the European Community. In 1990, the Community completed the preparation of legislative proposals for the definitive establishment of the Single European Market on 1 January 1993, which means that on that date all national barriers to the free movement of goods, services, people and capital will have been eliminated.

To this end, the Community programme provides for the adoption of 282 common regulations and guidelines, most of which have already been approved by the EC Council. The final result will be the harmonization of rules covering such different areas as the production, packing and labelling of goods; sanitation; State purchases; services; capital movements; consumer protection; fiscal taxation; activities of private firms; human and plant health controls; trade and transit documentation and procedures; free movement of workers and recognition of professional qualifications; and rules and procedures for industrial inspection and certification. In December 1991, a treaty on European Union was signed in Maastricht which provides for the progressive introduction of economic and monetary union, with the establishment of a European Bank and a common currency by 1999 at the latest.

The process of consolidation of the Community, which now also includes programmes aimed at political union, has a decisive gravitational effect on the countries around it. At the beginning of the present decade, there were two other economic groupings in Europe in addition to the Community: the European

<sup>10</sup> For a summary of the process of trade liberalization in Latin America in recent years, see Benavente, Schwidrowski and West (1991).

Free Trade Association (EFTA) and the Council of Mutual Economic Assistance (CMEA). In October 1990, the 13 million East Germans, who had up to then formed part of the CMEA, entered the EC as a result of German reunification. A year later, in October 1991, the EC and the EFTA countries brought two years of negotiations to their culmination by agreeing on the extension of the Single Market to the latter countries. The way was thus opened for the establishment of a European economic space extending from the Arctic to the shores of the Mediterranean. This space will include 19 countries and over 380 million people, and its current share in world exports is over 47%. Moreover, it represents a first step towards the possible entry of member countries of EFTA into the EC. As for the CMEA, the political and economic evolution of the Eastern European countries led to its dissolution in June 1991. Its former member countries are now gravitating around the Community, which has reduced its restrictions on imports from some of those countries. Three of them have expressed a desire to sign association agreements with the EC which could result one day in full membership of the Community.

Since the process of European integration takes place at two levels—the incorporation of new members and the intensification of integration among the existing members—the Community of the future has been described in terms of “concentric circles”. In addition to these circles, there are the Mediterranean countries with which the Community has signed preferential agreements, and the African, Caribbean and Pacific countries linked with the Community through the Lomé Convention. These two groups of countries thus form a broader economic space around the EC.

ii) *The new integration in America.* Largely in response to the European process, a similar process is taking place on the American continent, although of course it is less advanced. In January 1989, the agreement between the United States and Canada to set up a free trade area between the two countries within 10 years came into force, and since June 1991 negotiations have also been underway to extend this area to include Mexico.

The expansion of this economic space to the entire hemisphere, so that it extends “from Alaska to Tierra del Fuego”, is a long-term objective of the Enterprise for the Americas which was announced by

the President of the United States in June 1990. To this end, the United States has already reached framework agreements with almost all the Latin American and Caribbean countries, either individually, or in groups in the cases of MERCOSUR and the Caribbean Community (CARICOM).

These framework agreements lay down, in line with the Declaration whereby the Enterprise was announced, the principles on which future formal agreements should be based, and they establish a joint body, generally called the Trade and Investment Council, which forms the axis for the relationship between the parties. These principles refer largely to the same issues that were the subject of negotiation in the Uruguay Round. Among them, as stated in successive declarations, are the liberalization of trade—including trade in services—between the parties; the coordination of action in the multilateral trade negotiations, especially with a view to achieving the successful conclusion of the Uruguay Round; recognition that investors of each party will be given the same treatment as nationals in the territory of the other party; an undertaking to refrain from imposing requirements on investments by the other party which would cause trade distortions; and protection of the intellectual property rights of the citizens and companies of the other party.<sup>11</sup>

Since the Enterprise for the Americas was announced, the Latin American and Caribbean countries have stepped up their efforts to promote integration among themselves. This process has undoubtedly been favoured by the new policies of uniform trade openness applied in the continent and by the greater consensus on those policies mentioned earlier. This also explains the characteristics of the new form of integration, which is no longer seen so much as a way of substituting imports at the supranational level as a means for increasing the competitiveness of exports on external markets. This accounts for the similarity of goals and objectives of the new integration initiatives, which are generally aimed at forming common markets or free trade areas within unusually short spaces of time.

<sup>11</sup> See the text of the address delivered by George Bush, President of the United States, in Washington on 27 June 1990, and the statement by Myles Frechette, Assistant Representative for Latin America and the Caribbean and Africa of the United States Department of Commerce, in the seminar on *The United States and Argentina in relation to the Enterprise for the Americas Initiative*, The American University, 12 June 1991.

The formation of a common market by 1995 is the objective both of MERCOSUR, set up under the Treaty of Asunción between Argentina, Brazil, Paraguay and Uruguay in March 1991, and of the member countries of the Andean Pact (Bolivia, Colombia, Ecuador, Peru and Venezuela), as stipulated in the Act of La Paz signed in November 1990. At the end of 1991, the latter countries set up a free trade area and decided to bring forward to 1992 the entry into operation of the agreement for establishing the common market, although this was finally held up by some problems that arose over the definition of the common external tariff. In August 1990, it was decided to set up a common market in CARICOM. The Central American Common Market (CACM) is preparing to establish an "economic community" among its members, as provided for in its Economic Action Plan for Central America. For its part, in January 1991 Mexico signed an agreement with the CACM member countries with a view to the establishment of a free trade area. The same objective is pursued by the Group of Three (Colombia, Venezuela and Mexico). In addition to these subregional initiatives, there is a growing number of bilateral agreements aimed at eliminating trade barriers between Latin American countries (ECLAC, 1991b), outstanding among which is the establishment of a free trade area between Chile and Mexico, which was agreed on in September 1991 and is to be carried out gradually from 1992 to 1996.

iii) *Reticence over regionalization in Asia.* In Asia, efforts to set up regional economic links have been led by developing countries. After the selective liberalization of tariff barriers among the signatories of the Bangkok Agreement, the member States of the Association of Southeast Asian Nations (ASEAN)<sup>12</sup> agreed at the end of January 1992 to set up an ASEAN free trade area within the space of 15 years. Within this area, an effective common preferential tariff will be established, applicable to manufactures, capital goods and agricultural products, but excluding agricultural raw materials. The formal creation of an exclusive economic space for the whole region, where Japan has the dominating economic weight, has not materialized, however. In contrast, at the ministerial meeting of the Asia Pacific Economic Cooperation Group (APEC) held in Seoul in November 1991, there

<sup>12</sup> ASEAN comprises Brunei and Darussalam, the Philippines, Indonesia, Malaysia, Thailand and Singapore.

was a further assertion of the desirability of strengthening regional initiatives to further the multilateral liberalization –within GATT, for example– of trade and investment. This decision involves the countries on both sides of the Pacific, since the members of the APEC Group are Australia, Canada, Japan, New Zealand, South Korea, the United States, the six ASEAN nations and the new members: the Chinese People's Republic, Hong Kong and Taiwan.

### c) *Regionalization and multilateralism*

Consequently, only in Europe is there a formally constituted economic bloc, while one is beginning to be formed in the Americas. Developments in Asia, above all, indicate that the forces of multilateralism exist side by side with those of regionalism and, depending on the circumstances, may even predominate over the latter. There is nothing surprising about this, since, as already noted, both tendencies are in line with the same logic of the supranational harmonization of the global system. The harmonization efforts which took concrete form in the Structural Impediments Initiative signed between the United States and Japan in the summer of 1990 also fit in with this logic. As currently conceived, and in the light of their past record, the economic spaces which are in the process of consolidation (in Europe) or formation (in the Americas) represent a potential for opening up to the exterior which will favour the trend towards universal integration produced by globalization. In the field of trade, for example, the process of European integration has been reflected in an increase in United States exports to that market, which have grown spectacularly since 1986, having almost doubled between that year and 1990. The Single Market due to come into operation in Europe by 1993 will make it even easier for other countries to sell their goods inside this great economic area, where, furthermore, the demand by enterprises will increase in line with their investments (Duesterberg, 1991). It is expected that fixed investment by enterprises in Europe will more than treble between 1985 and 1995.

These tendencies could relieve the fears, shared by some experts, that a resurgence of protectionism could turn what were supposed to be open economic spaces into closed spaces; that is to say, that the possible regional blocs would become obstacles that would lead to the division of the world economy instead of serving as the basis for its integration

(Tussie, 1991; Lawrence, 1991; UNCTAD, 1991a). In actual fact, the blocs could serve to relieve the harmful effects of increased protectionism for their member countries. Only if the existence of the blocs themselves represented an incentive for the establishment of barriers against third countries could they be considered as a danger to multilateralism. The main potential risk is connected with the diversion of trade that the blocs could cause. Although this diversion would probably be more than offset by the trade creation effects at the world level, countries which remained outside the blocs could be adversely affected (Krugman, 1991; Bergsten, 1991).

From the Latin American point of view, if all the countries of the region were integrated into a single American economic area, the real risk could be of another nature: namely, that the increase in trade and integration between the various regional spaces might take place above all between the economies with the greatest weight within those spaces (the EC, the United States and Japan), with the other countries mainly being linked to the dominant country in their own space. In the case of the Latin America countries, this would mean greater dependence on the United States.<sup>13</sup>

For the Latin American countries, the challenge lies in avoiding a possible tendency to concentrate relations in a single market, especially in view of the fact that the European and Asian markets may possibly register higher growth rates than the United States market in the medium term. This does not mean scorning the possibilities offered by the Enterprise for the Americas, but it does mean that this should not be the only possible option. It is a question of keeping alive the spirit of multilateralism, to which end the countries of the region must persist in their efforts to achieve liberalization of world trade, make sure that the establishment of a possible free trade area with the United States does not bring

<sup>13</sup> This could happen, in view of the possible features of trade within and between the spaces. Trade between the "poles" seems to include a high and growing content of horizontal intra-sectoral trade, that is to say, trade in different varieties of the same products. Trade in manufactures between each pole and the other countries in its economic space could include a big component of vertical intra-sectoral trade: the export of parts and components from the former to the latter, for assembly and reexport to the country of origin (ECLAC, 1991c, pp. 3-4). The application of strict rules of origin – a thorny question in the negotiations on integration with the United States and within the EC – would mean that this type of trade would only take place within the economic space, to the exclusion of parts and components from third countries.

with it an increase in protection against third countries, and promote economic relations with the other regions.

At the same time, it would not be desirable for the possible American economic space to take the form of a system of free trade agreements between the United States and each of the Latin American countries or groups of countries. The liberalization must extend to the mutual relations of the countries of the region, so that a true hemispheric free trade area is set up. For this purpose, it is necessary to advance resolutely towards Latin American integration, which demands among other things, as a prior condition, the success of the macroeconomic stabilization efforts of the individual national economies.

By the mid-1990s, the Latin American and Caribbean region could be structured around four solid economic groups: the Central American Common Market, CARICOM, the Andean Pact and MERCOSUR. In addition, there could be a complex network of bilateral free trade areas between various countries. This network could bring with it, however, the risk of causing multiple trade diversion effects and distortions in comparative advantages. The next challenge will be to extend this bilateral system to take in the subregional groups themselves, so that by the end of the decade there is a single Latin American free trade area or customs union, as a minimum, which can form a space of the same type with the North American countries. In this respect, the Presidents of the 13 Latin American countries making up the Rio Group announced in December 1991 their decision to continue to promote the subregional integration processes already underway, so that they would reach their culmination in the course of the decade and by the year 2000 the American free trade hemisphere would be fully established.<sup>14</sup>

### *3. The international context and resources for development*

One of the essential tasks for recovering economic growth in Latin America is to secure a considerable increase in the rate of investment, which fell from almost 23% of the gross domestic product in 1980 to only 16.2% in 1989. In order to do this, a substantial

<sup>14</sup> Joint Declaration of the Fifth Presidential Summit of the Permanent Mechanism for Consultation and Policy Coordination, held in Cartagena de Indias, Colombia, from 1 to 3 December 1991.

increase in external or internal saving is needed. International conditions influence both of these types of saving, and the current conditions have a special influence, different from that of the past decade.

To begin with, recent events give grounds for expecting greater competition for external resources. It is estimated that the reunification of Germany, the financing of the transition in Eastern Europe, and the reconstruction programmes in the Middle East will involve a bigger demand for external saving of the order of 100 billion dollars per year between 1991 and 1996. This bigger demand alone would cause an increase of approximately half a percentage point in real long-term interest rates in the industrialized countries, as well as a slight slackening in the growth rate and a moderate rise in inflation (IMF, 1991a). There is thus a need to raise the rate of saving throughout the world, but especially in Latin America, where, in view of the possible greater competition for external resources and their higher cost, it would be advisable to intensify the efforts already being made to increase domestic saving and improve the productivity of capital.

On the other hand, however, certain features of the international setting favour increased external and domestic saving in Latin America. In the 1980s, the heavy external debt burden prevented the use of a large proportion of domestic saving for investment purposes and represented an insuperable obstacle to the procurement of new loans on international capital markets. The result was the heavy net transfer of resources abroad registered by the region in the 1980s. Lately, however, there has been some progress in reducing the debt burden, and this reduction, together with the growing integration of the international capital markets, has opened up new possibilities for securing financial resources on those markets. These two circumstances have made it possible to reverse the net resource transfer to the exterior. In 1989, the net outflow still represented 21% of the total value of exports of goods and services, but by 1990 this figure had gone down to 11%. In 1991, thanks also to the considerable reduction in interest rates in the United States, the net transfer became positive for the first time since 1981, when the debt crisis began. According to provisional data, in 1991 the net inflow of resources was equivalent to 4% of the total exports of the region, although it should be noted that most of the capital inflow was

concentrated in a few countries, especially Mexico and, to a lesser extent, Argentina and Venezuela (ECLAC, 1991d). At the same time, the new climate of reduced tensions between East and West makes possible an increase in public domestic savings through the reduction of military expenditure.

a) *The international climate for solution of the debt problem*

After a long delay in recognizing the seriousness of the external debt problem of the developing countries and the need to reduce it substantially, since the late 1980s a somewhat more flexible official position has been observed in the creditor countries.

One manifestation of this greater flexibility has been the consolidation of various agreements for reducing the amounts owed to the commercial banking system under the Brady Plan, which was announced early in 1989. So far, six countries, including four from Latin America (Costa Rica, Mexico, Uruguay and Venezuela) have concluded agreements of this type, and it is expected that other important debtors such as Argentina and Brazil will achieve similar arrangements. According to calculations by the International Monetary Fund (IMF), the net effective reduction in indebtedness secured by those four Latin American countries comes to US\$11 billion, representing 15% of the total value of their commitments before the application of the respective programmes (IMF, 1991b, table 15, p. 76). Moreover, greater tolerance has been displayed by creditors in respect of the unofficial accumulation of debt servicing arrears. This has been a temporary safety valve for the problem of overindebtedness and the slowness of the negotiations for achieving permanent reductions in the debt.

Another sign of the new attitude is the fact that the official bilateral debt has also been reduced in line with criteria which vary according to the income level of the debtors. After the adoption in 1988 of the "Toronto Terms" for the granting of special terms to low-income debtors, in 1990 the creditor governments grouped together in the Paris Club agreed to offer new payment facilities (the "Houston Terms"), including conversion of the debt into local currency, to medium-low income countries. The first-named terms were applied in 1990 to Bolivia and Guyana, while the latter terms were applied to El Salvador, Honduras, Jamaica and Peru.

Various creditor countries have put forward proposals for a much greater reduction of the bilateral debt of low-income nations; for example, the "Trinidad Terms" proposed by the United Kingdom provide for the condonation of two-thirds of the outstanding balance. The principle of condoning the debt of middle-income countries was introduced with the decision to reduce the bilateral official commitments of Poland and Egypt by at least half: a decision strongly influenced by some particular political factors. Finally, the Enterprise for the Americas proposes debt reduction mechanisms which would be applied to the commitments of Latin American and Caribbean countries with the United States, totalling US\$12 billion. Up to the end of September 1991, the United States had condoned debts totalling US\$1.5 billion of seven countries of the region. Since most of the countries involved had relatively small economies, the reductions granted were quite significant: in the case of Honduras, Nicaragua and Guyana, the amount condoned represented 90% of the total owed to the United States Government, while in the cases of Bolivia and Haiti it amounted to 70%.

With regard to the debt owed to multilateral agencies, a noteworthy development is the so-called SDR accumulation approach introduced in 1990 in order to regularize the position of countries with a long history of arrears in their payments to the IMF. Under this mechanism, the debtor country accumulates refinancing rights as it complies with the goals of an adjustment programme. Once the programme has been successfully applied, the country pays off its arrears to the Fund through the organization of a bridging loan granted by a group of "support" governments, and it subsequently converts the accumulated rights into a disbursement of Fund resources, as part of a normal programme with that agency. In Latin America, this scheme is being used as the central element in normalizing Peru's situation *vis-à-vis* its external creditors.

As a result of the application of these measures, as well as the significant reduction in bank debt achieved through various national mechanisms—mechanisms which have been of great importance in the cases of Chile and Bolivia—the question of the external debt has tended latterly to become less prominent in some Latin American countries. Nevertheless, the problem of overindebtedness persists in many countries of the region, and its structural consequences continue to constrain the leeway for economic policy decisions and growth possibilities.

#### b) *The international capital markets*

The external financing situation of Latin America has undergone substantial changes in recent years. During most of the 1980s, the voluntary credit market (except for short-term external trade financing) was completely closed to the countries of the region, crushed as they were by the debt burden. Recently, however, some countries have been able to take advantage of the positive trends registered in those markets in order to begin a process of return to voluntary loans.

The international financial markets have been characterized in recent years by growing integration between countries, between market segments, between institutions, and between financial instruments. This process has been based on various factors, especially the technological advances which have taken place in telecommunications and computation systems; the application of policies of exchange and financial deregulation, and the increasingly important position occupied in the capital market by institutional investors (pension funds, insurance companies, mutual funds and investment management firms), which have more capacity than individual investors for operating on foreign markets. This integration has had positive results in that it has promoted greater competition between financial institutions and greater effectiveness of the financial intermediation process at the world level. It has also accentuated the volatility of financial asset prices, however, and has raised serious problems with regard to banking supervision and the handling of monetary and exchange policy.

The volume of resources handled on the world financial market is now enormous; it may be noted, for example, that the total value of loans contracted on international capital markets almost trebled between 1982 and 1991, reaching US\$517.6 billion in the latter year (OECD, 1992). At the same time, everything seems to indicate that the integration process will be further intensified in the future. These two circumstances offer important opportunities and challenges to the Latin American countries, since the increasingly global view taken by institutional investors and their interest in diversifying their portfolios by incorporating high-yield instruments mean that there is a considerable potential supply of resources.

Some countries of the region have already begun to take advantage of these possibilities. Mexico, above all, but also Chile and Venezuela, have

re-entered the world capital market, and in 1991, Argentina and Brazil also joined the countries which have managed to obtain resources on that market. Unlike the 1970s and the early 1980s, when the predominant loans were from the commercial banking system, this new access to voluntary financing is taking place through the issue of international bonds, on the one hand, and foreign portfolio investments in stocks and shares on the other.<sup>15</sup>

The reopening of the international bond market for Latin American borrowers began in the period 1987-1989, but it speeded up spectacularly in 1990 and 1991. The total value of the issues made rose from US\$600 million in 1989 to US\$3 billion in 1990, and according to initial estimates it reached US\$5 billion in 1991. So far, Mexico is the country which has managed to procure the biggest flow of resources through the issue of external bonds, while other countries which have carried out operations of this type are Venezuela, Argentina and Brazil. The cost of the financing obtained in this way has been relatively high, although there has been a clear trend towards lower risk premiums on Mexican and Venezuelan issues. Another feature of this type of financing is that it has been of a relatively short-term nature: the maturities have usually been between two and five years, although there have also been operations with terms of seven or even ten years. Consequently, it would be necessary to keep up a continuous flow of new loans in the future if it is desired to avoid a situation where the net transfers through this form of financing become negative after a short time.

The other way in which resources have been obtained from private international capital markets is foreign portfolio investment in stocks and shares. The available information indicates that considerable external resources have recently entered some Latin American countries in this way. Thus, for example, stock issues by Latin American companies on the stock exchanges of the industrialized countries through American Depositary Receipts (ADRS) amounted to over US\$4 billion between 1989 and the early months of 1992. Another index is provided by the balance of payments statistics of Mexico, which indicate that in that country income from foreign portfolio investments, which had amounted to US\$490 million in 1989, rose to US\$2 billion in 1990 and to over US\$6 billion in the first half of 1991.

<sup>15</sup> For more details on the characteristics of these sources of financing, see West (1991).

The new private capital flows are helping to relieve the external financing restrictions which the Latin American and Caribbean region suffered during the 1980s. It is not yet certain, however, that these flows will become a lasting form of financing which can serve as a basis for development, nor that further countries in the region will also be able to enter this market. In this respect, the question arises as to the extent to which the recent availability of funds for the region may be due merely to a short-term drop in interest rates in the United States, which has made the yields offered by Latin American instruments very attractive. It must not be forgotten that the unstable and procyclical nature of private international capital movements means that access to this type of financing involves certain risks and possible costs. On the one hand, there is the danger that, in particular circumstances, the capital inflow may be suddenly reversed. On the other hand, a diametrically opposite problem may arise: an excessive inflow of resources at periods of economic boom and great confidence among foreign investors could complicate macroeconomic management, especially as regards the handling of monetary and exchange policies.

#### c) *Disarmament and resources for development*

The end of the military tensions which characterized the Cold War has recently given rise to a debate on levels of military spending and the real possibility of reducing such spending and using the resources thus made available for development. What has been called the "dividend of peace" is potentially of considerable size. World military spending has been estimated at over a million million dollars per year (which may be compared with the US\$1.3 million million represented by the debt of all the developing countries together), of which US\$800 billion corresponds to the developed countries and the rest to the developing nations (McNamara, 1991). Reduction of this spending would make it possible to increase global saving in order to cope with new investment needs, and it would even facilitate better budgetary balance in the main developed economies, with positive effects on real interest rates and the world economy. Moreover, if the industrialized countries agreed to devote part of these resources to activities that would aid

development, the developing countries could benefit directly from this. In October 1991, the Group of 77 made an appeal for part of this expenditure to be devoted to settling the debt problem, and multilateral agencies such as UNICEF have made similar appeals for the reallocation of the resources currently devoted to military expenditure.

Latin America and the Caribbean, too, now have an opportunity to increase domestic public saving and investment for development by reducing their own military budgets. In 1988, these budgets were estimated to absorb some US\$13 billion, representing 3.3% of the GNP of those countries as a whole, and even more in some of them. This percentage was higher than that corresponding to expenditure on health (2.3%). In many countries, the percentage of GNP represented by military expenditure even exceeded that corresponding to spending on education (McNamara, 1991). It would be sufficient to reduce military spending by an average of less than half in order for governments to be able to devote an extra 1.5% of their gross national product to investment expenditure (for example, construction of highways and hospitals, repairs to ports, opening of new schools, etc.). And if each country were to fix a maximum of 2% of GDP for military expenditure, at least 12 countries of Latin America and the Caribbean could achieve substantial increases in their domestic saving.

This reallocation of resources is now possible, thanks to the climate resulting from the new relations between East and West. This new climate is not only reflected in the successive disarmament agreements between the United States and the Soviet Union, but also has a moderating influence on regional conflicts. The causes of these conflicts do not disappear as a result of the understanding between East and West, but it is possible that the external support which in many cases made these conflicts possible and even fomented them could disappear. A clear example is the recent process of pacification in Central America, which fits in perfectly with the new climate of détente and pacification in other regions of the world (including the Middle East, after the lamentable episode of the Gulf War).

Furthermore, in Latin America nearly 90% of the armed conflicts which have taken place since the Second World War, and which have caused over 864 000 deaths among civilians and military

personnel, have been internal conflicts of the countries.<sup>16</sup> That is to say, the armies have not been used to fight the armies of other countries, but to act against citizens of their own country. Consequently, a redefinition of the concept of national security which has traditionally been used to justify the allocation of scarce economic resources to military expenditure is called for. The idea of national security should not be limited to the capacity to deal with conflicts: it should also cover the capacity to prevent them. In this respect, it should include the guaranteeing of both political and economic human rights, including the reduction of unemployment and poverty. The resources devoted to these latter purposes would represent an effective contribution to the prevention of conflicts, so that they should be considered as part of the national security effort.<sup>17</sup>

The reduction of military spending in the various countries is also favoured and facilitated by the strengthening of the function of the United Nations in the solution and prevention of conflicts and the more favourable international climate for such reduction. The generalized consensus on the central role that should be played by the United Nations has been manifested explicitly in three summit meetings recently held in London, Abuja and Guadalajara. The organization is now in a better position to help to guarantee the territorial integrity of countries, so that governments now feel greater confidence in reducing their military budgets. The favourable international climate for this latter objective has been manifested on many occasions. For example, the IMF is considering the possibility of including reduction of military spending and ceilings on military debts among the conditions for its loans. Various developed countries have stated that they are in favour of linking their

<sup>16</sup> Of 23 conflicts registered in Latin America during this period, on only three occasions were there confrontations between the armies of different countries: the interventions by the United States in the Caribbean, the "football war" between Honduras and El Salvador, and the Falklands War between Argentina and the United Kingdom. See the statistics collected by Nicole Ball in McNamara (1991).

<sup>17</sup> Moreover, these measures would not only free resources for development but could also check the danger of a possible tendency towards militarization in other areas of social coexistence. As the South Commission says in its recent report, "equally harmful is the development of a military culture which scorns democracy, popular participation, human rights and the principle of government responsibility and which encourages corruption, abuse of authority and the constant alienation of the population from the political system" (South Commission, 1991, p. 63).

development aid to reductions in military expenditure, and they have also made appeals to take the reduction of military spending by debtor countries into account in initiatives aimed at solving the debt problem.

#### 4. *Towards a multipolar economic order*

At the level of international economic relations, economic centres such as the EC and Japan have been playing a more prominent role, thus offsetting the predominant role of the United States and pointing the way to a more multipolar economic order.

Although the United States continues to be the biggest economic power, its position has steadily weakened compared with that of the other major developed countries. This situation has been reflected in such indicators as the United States share in world product and trade, its loss of competitiveness in spearhead industries and, during the 1980s, its growing trade deficit, which has turned it into the biggest net debtor in the world (Krasner, 1991).

This latter phenomenon is connected with the evolution of international financial markets described earlier. The liberal availability of capital on those markets in the 1980s permitted the United States to maintain a prolonged heavy budgetary deficit together with a deficit on its balance of payments current account. This budgetary deficit has to some extent limited the country's ability to use fiscal policy to reactivate its economy. The need to attract capital to finance the current account deficit, in a world where the increase in demand for investments has intensified competition for external resources, comes into conflict with the use of monetary policy, and especially the lowering of interest rates which may be needed to stimulate demand.

In these circumstances, the evolution of the United States economy has become more dependent on external conditions and particularly on the policies adopted in the other economic centres. In these centres, the will and policies of the United States government have less influence now than in the past, when the dominating position of that country facilitated the compatibility of the policies of countries such as the Federal Republic of Germany and Japan. The planned formation of a European economic and monetary union will erode the influence of the United States still further by reducing the importance of the dollar in world trade. The key

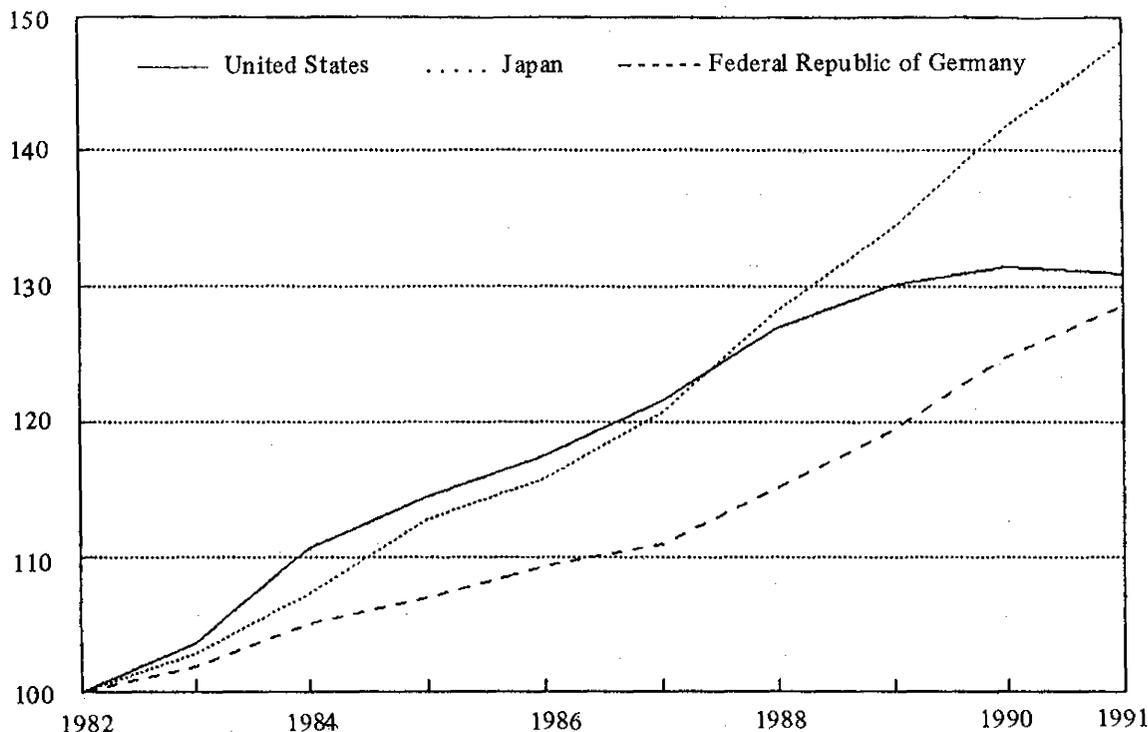
variable in this situation is interest rates: the greater difficulty in keeping interest rates in line with each other is a disturbing element, especially for the United States.

The recession which began in 1990 in that country was thus preceded by a gradual loss of influence in recent years. The evolution of the United States economy in comparison with those of the Federal Republic of Germany and Japan seems to have followed the same pattern. As may be seen from figure 1, after the 1982 crisis the United States economy registered solid growth at a higher rate than the other two countries. This dominant position began to weaken, however, and by 1988 the economic growth rate of the United States had already fallen below that of Japan. In 1990, for the first time a situation of completely divergent growth trends arose: whereas the United States economy was entering into a recession, the German and Japanese economies continued to grow, so that United States growth seems doomed to fall below that of the German economy also. With the passage of time, the recession in the United States also dragged down the economies of the other two countries.

This evolution highlights certain elements of vulnerability in the new world order and the risks that these may imply for the future. On the one hand, coordination and harmonization of public policies is increasingly necessary,<sup>18</sup> but the emergence of a multipolar order makes this increasingly difficult. During the 1980s, important steps were taken towards coordinating the monetary and fiscal policies of the main industrialized countries grouped together in the Group of Seven. This coordination was needed in order to cope with the integration of financial markets and to try to limit the severe balance of payments disequilibria caused by massive capital movements in response to changes in interest rates and exchange parities (Webb, 1991). The Plaza (1985) and Louvre (1987) agreements are examples of these attempts at coordination. However, such coordination has been lacking in recent years, as witness the fall of the dollar when abandoned to the market forces in 1990.

<sup>18</sup> The need to strengthen efforts to secure more effective economic cooperation between the United States, Japan and Europe in order to guarantee favourable evolution of the world economy in the 1990s is emphasized in Bergsten (1990).

Figure 1  
**GDP INDEX FOR FEDERAL REPUBLIC OF GERMANY,  
 UNITED STATES AND JAPAN**  
 (1982 = 100)



Source: International Monetary Fund.

At the same time, the economic growth prospects in a multipolar and globalized world in which technical progress plays a crucial role have become more dependent on the expansion of international trade. For a long time past, the growth of trade has exceeded the growth of the world product (except in 1985), and since 1988 it has been twice as great. This is why the multilateral efforts at liberalization and harmonization carried out in the Uruguay Round of GATT and in the regional groupings are so important.

If these conditions of greater coordination and harmonization are fulfilled, and the multilateral efforts at trade liberalization are successful, the IMF forecasts of a reasonable medium-term growth rate of over 3% per year on average for the world economy between 1993 and 1996 could come true. The new world order would then be in a position to contribute to an international setting relatively favourable to the domestic development efforts of the Latin American countries.

## Annex

### OUTSTANDING EVENTS SINCE MID-1989

23 July 1989

Mexico reaches an agreement for debt reduction under the Brady Plan (the first country to do so).

18-19 October 1989

In Hungary, after a process of growing political openness, the National Assembly approves extensive reforms to the Constitution, including the suppression of any reference to the guiding role of the Communist Party and the legalization of political parties.

- 9 November 1989 Fall of the Berlin Wall.
- 17-29 November 1989 Mass demonstrations in Czechoslovakia culminate with the suppression of any reference to the guiding role of the Communist Party in the Constitution.
- 1 December 1989 The changes in East Germany culminate in the suppression by Parliament of the constitutional guarantee of the guiding role of the Communist Party, followed by prosecution of many of its leaders.
- 10 December 1989 Summit meeting between Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua for the establishment of peace in Central America.
- 19 December 1989 The Parliament of Czechoslovakia approves a programme of free elections and liberalization of the economy.
- 16-26 December 1989 Violent demonstrations in Romania culminate with the prosecution of President Ceausescu, his subsequent execution, and a change of government until the holding of elections.
- 1 January 1990 Poland adopts a radical programme of economic reforms.
- 15 January 1990 In Bulgaria, after several weeks of opposition demonstrations, the National Assembly suppresses the constitutional guarantee of the guiding role of the Communist Party.
- 20 January 1990 In Yugoslavia, in a climate of dissension between Serbs and Slovenes, the Communist League suppresses the constitutional guarantee of the guiding role of the Communist Party.
- 22-23 January 1990 The Communist Party of Albania approves the holding of elections with multiple candidates and some reforms aimed at a market economy.
- 13 March 1990 In the Soviet Union, the Congress of Deputies of the People approves a political system with multiple parties and suppresses the guiding role of the Communist Party.
- 20 May 1990 First free elections held in Romania.
- 29 May 1990 It is agreed to set up the European Bank for Reconstruction and Development in London in order to help finance the Eastern European countries.
- 31 May 1990 The Soviet Union and the United States sign a framework agreement in Washington on the reduction of strategic nuclear weapons and an agreement to abandon the production of chemical weapons.
- 8-9 June 1990 In Czechoslovakia, the Communist Party loses the parliamentary elections.
- 17 June 1990 The Central American Presidents approve the Economic Action Plan for Central America, providing for the establishment of an economic community.
- 27 June 1990 The President of the United States announces the Enterprise for the Americas, aimed at establishing a free trade area in the western hemisphere.
- 28 June 1990 Structural Impediments Initiative between the United States and Japan.
- 6 July 1990 At a summit meeting in London, NATO drafts the London Declaration in which it is proposed to the Warsaw Pact that both organizations should jointly declare that they are no longer adversaries, thus putting an end to the Cold War.
- 2 August 1990 The CARICOM countries lay down a deadline for the establishment of a common market.
- 3 October 1990 Reunification of Germany.
- 19 October 1990 The Supreme Soviet of the Soviet Union approves an economic plan providing for transition to a market economy.

- 28 October 1990 The EC member countries (except for Great Britain) announce in Rome their support for the establishment of a Community Central Bank by 1994.
- 19 November 1990 NATO and the Warsaw Pact sign the treaty for the reduction of conventional forces in Europe.
- 21 November 1990 The Paris Charter, putting an end to the division of Europe into two antagonistic blocs, is signed by 34 Heads of State of the member countries of the Conference on Security and Cooperation in Europe.
- 30 November 1990 Signing of the La Paz Act, providing for the establishment of a common market in the Andean Group.
- 6 December 1990 Suspension of negotiations at what should have been the closing meeting of the Uruguay Round in Brussels.
- 15 December 1990 The EC countries, meeting in Rome, officially begin negotiations to establish a political federation with a common currency and shared security and external relations policies.
- 22 December 1990 In a plebiscite, the Republic of Slovenia approves its independence from Yugoslavia.
- 11 January 1991 Signing of the Declaration of Tuxtla Gutiérrez for the establishment of a free trade area between Mexico and the countries of the Central American Common Market.
- 27 March 1991 Signing of the Treaty of Asunción, setting up MERCOSUR.
- 12 June 1991 Negotiations are begun for the establishment of a free trade area between the United States, Canada and Mexico.
- 28 June 1991 Council of Mutual Economic Assistance (CMEA) dissolved.
- 2 July 1991 Warsaw Pact ceases to exist.
- 19-21 August 1991 Frustrated coup d'état in the Soviet Union, which considerably speeds up the process of change in that country.
- 26 October 1991 Draft agreement between the EC and the EFTA countries for the formation of a European economic space.
- 31 October 1991 Middle East Peace Conference opened in Madrid.
- 12-15 November 1991 Ministerial meeting of the Asia Pacific Economic Cooperation Group held in Seoul.
- 10 December 1991 Signing in Maastricht of the Treaty on European Union, which is to form the basis for the progressive application of economic and monetary union by 1999 at the latest.
- 21 December 1991 Establishment of the Community of Independent States by the Republics (except for Georgia) which had made up the former Soviet Union, whose official disappearance had been declared two weeks before.
- 28 January 1992 Summit meeting of the ASEAN countries, at which it is decided to establish a free trade area within the space of 15 years.
- 8-25 February 1992 Eighth session of the United Nations Conference on Trade and Development (UNCTAD), the main forum for the North-South dialogue.
- 3-14 June 1992 United Nations Conference on Environment and Development ("Earth Summit") held in Rio de Janeiro.

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## The world agricultural outlook in the 1990s

*Giovanni Di Girolamo\**

This article analyses various international trends in the agricultural sector which have a bearing on the external trade of the Latin American countries. The balance in recent years has been rather negative for the agricultural sector of the developing countries, both from the point of view of the terms of trade and with regard to the weakness of the markets for their commodity exports.

The coming years will be marked by intensive competition in world agricultural markets. A leading problem in world agricultural trade will continue to be the lack of resources to permit the potential demand for the products of this sector to be converted into effective demand.

Various projections bring into question the idea that processes of greater openness based mainly on incorporation into world trade by means of agricultural or agroindustrial products can be a reliable way to development. The exporting countries must diversify their primary production and progress towards a form of agroindustrial development which will make possible better internal linkages in the economy, the modernization of rural areas, and the satisfaction of domestic demands.

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## Introduction

The second half of the 1980s was marked by the consolidation of a number of unfavourable trends for the agricultural sector of the developing countries. In international agricultural markets, competition between exporting countries grew considerably, and there was a heightening of protectionist tendencies in the developed countries. The terms of trade between agricultural products on the one hand and manufactures and crude petroleum on the other deteriorated to the detriment of the former throughout the period 1980-1988 (figure 1). On average, in 1988 the terms of trade between agricultural and industrial products were 25% below those of 1980. At the same time, the agricultural balance proper of the developing countries, taken as a whole, deteriorated under the simultaneous pressure of the drop in the relative value of their agricultural exports and the increase in imports of foodstuffs from the developed countries. In Africa, for example, the lower income obtained from agricultural exports in 1989 meant that that region was only able to buy 28% less manufactures and crude petroleum than in 1979-1981. In Latin America and the Caribbean too, over the same period, the total value of exports went down in spite of a considerable increase in their volume.

The deterioration of the agricultural balance of the developing countries may be explained principally by the adverse evolution of export prices, especially for food products (figure 2). Moreover, in many developing countries which are net importers of foodstuffs there was a clear divergence between the tendency towards rapid population growth and the relatively slower increase in production. In some cases, this phenomenon is due to climatic factors (partly of a previously unprecedented nature), over-exploitation of the soil, and situations of local political instability. The main cause, however, seems to be the profound crisis in peasant agriculture caused by the internationalization of agricultural markets, the growing instability of prices, and the lack of capital and training. The crisis in peasant agriculture gives rise to a vicious circle: larger contingents of the rural population move to the cities; the consequent increase in the urban population causes governments to adopt agricultural policies which tend to fix low prices for

food, for social security reasons,<sup>1</sup> and this, in turn, generates further subsequent backwardness in the peasant economy and fresh migrations. At the same time, the country registers a food deficit and its balance of payments deteriorates.

In most of the non-oil-exporting developing countries, the agricultural sector provides between 20% and 40% of GDP, between 60% and 80% of employment, and between 50% and 70% of total export income. Although there are a number of cases of successful and promising agricultural export-based development, at both the country and enterprise levels, recent years have not been particularly favourable for agricultural exports from the southern part of the world. The FAO (1990c) has calculated that in the 40 developing countries whose exports consist mainly of agricultural products, the macroeconomic indicators suggest a generally rather disappointing situation in recent years. Thus, for example:

a) The per capita gross domestic product went down by 1.1% in 1989, and it is estimated that in 1990 it fell by a further 0.8%. In contrast, in the developing countries with a more diversified export base the product grew by 1.1% in 1989 and is estimated to have risen by a further 0.2% in 1990.

b) In the developing countries which mainly export agricultural products, gross capital formation went down from around 17% of GDP in the early years of the 1980s to less than 14% in 1989 and 1990, whereas in the developing countries with more diversified exports the level remained relatively constant at 20%.

c) In the 1980s, inflation was considerably higher in the group of countries which are essentially exporters of agricultural products than in the developing countries with more diversified exports.

d) During the greater part of the 1980s, export volumes grew considerably less in the developing countries which primarily export agricultural products than in the countries which export manufactures, and the terms of trade of the former fell by almost one-third between 1985 and 1990.

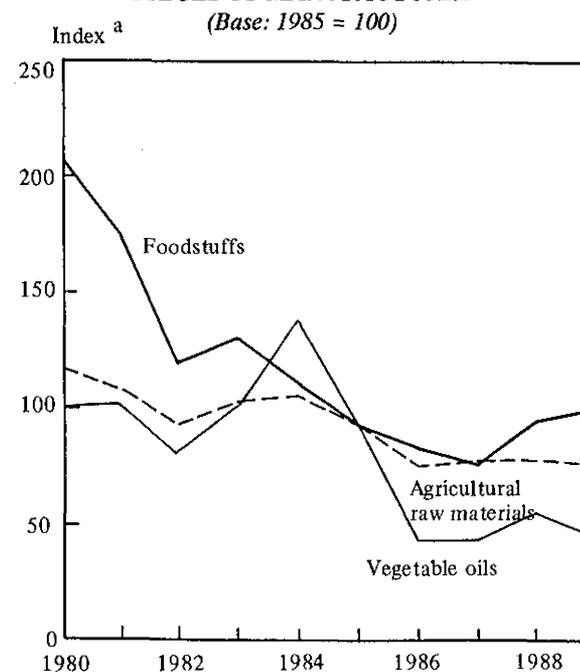
e) Import volumes went down in the countries which are essentially exporters of agricultural

products by a total of 11% between 1982 and 1990 (FAO, 1990c).

It should be noted that these disappointing results were registered at a time (the second half of the 1980s) when the world economy was recovering. It does not seem likely that better results will be obtained in the immediate future, since the growth rates of the economies of the industrialized countries are expected to be less satisfactory than in previous years.

Moreover, the most successful and frequently cited cases of agricultural export-based development have been in countries with an export base which is quite diversified rather than mainly agricultural. Thailand, Malaysia, Brazil and Chile, for example, have important non-agricultural export sectors in the fields of mining, manufacturing, etc., and they also have a dynamic agroindustrial sector which has taken advantage of the opportunities presented by agricultural export development and is at the same time stimulating domestic demand for agricultural products.

Figure 1  
RATIO OF PRICES OF SELECTED  
AGRICULTURAL PRODUCTS TO  
PRICES OF MANUFACTURES

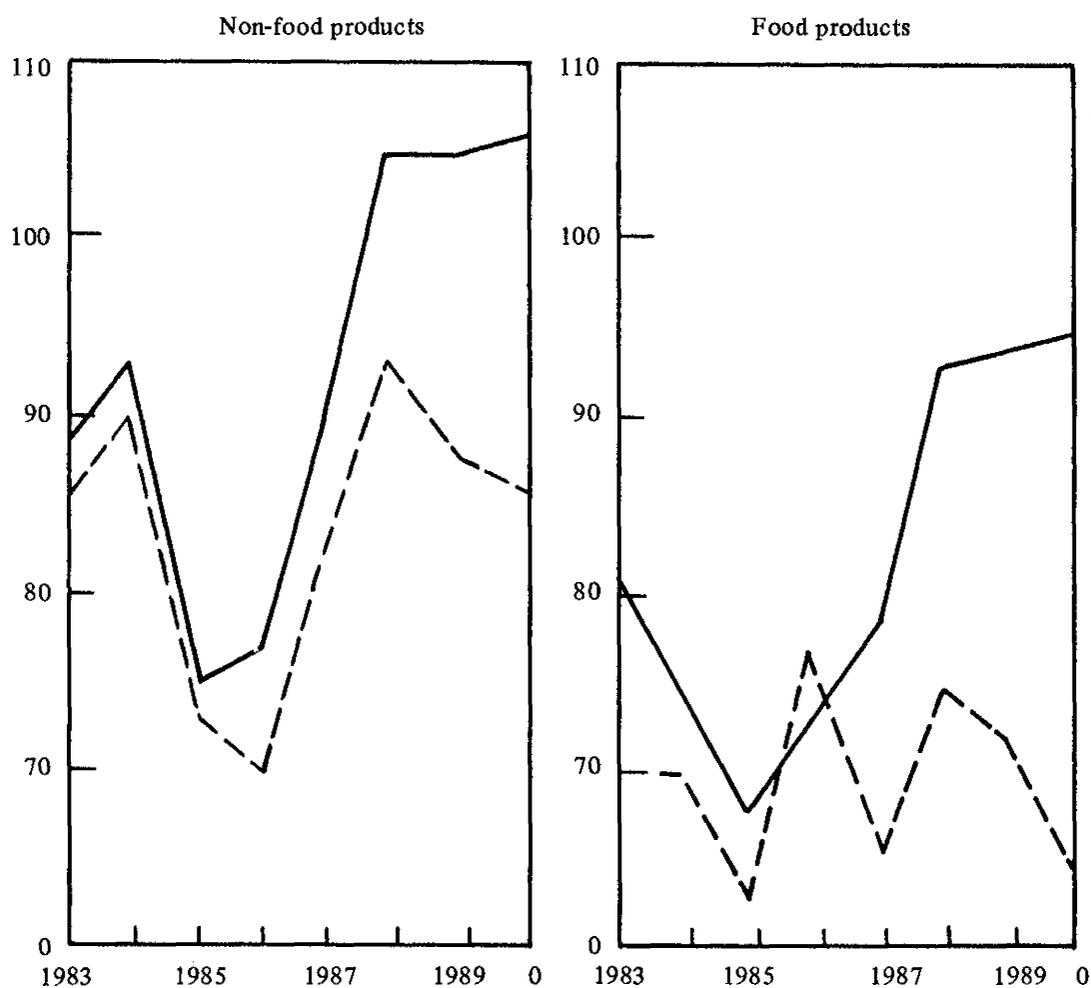


Source: United Nations, *World Economic Survey, 1990*, New York, 1990.

<sup>a</sup> Index of prices of agricultural products, divided by index of prices of manufactures.

<sup>1</sup> At present, there are around 100 developing countries where one person in five is suffering from malnutrition. Serious food crises are expected in 1992 in Algeria, Ethiopia, Liberia, Mozambique and Somalia.

Figure 2  
VARIATION IN EXPORT PRICES OF AGRICULTURAL PRODUCTS  
(1980 = 100)



Source: United Nations, *World Economic Survey, 1990*, New York, 1990.

— Developed countries.  
- - - - - Developing countries.

## I

### The case of Latin America and the Caribbean

#### 1. Production

In Latin America and the Caribbean as a whole, agricultural production grew between 1981 and 1988 at an average annual rate of 2.4%, that is to say, a little faster than the population. In 1989, however, the growth rate of agricultural production in the region dropped to 1.9%, which was less than the increase in the region's population in that year.

At the same time, the long-standing downward trend in the percentage contribution of agriculture to GDP in the region ceased because of the economic crisis of the early 1980s, and it was even reversed in following years (the same thing occurred in Africa, but not in the Far East and the Middle East, where the ratio of agricultural GDP to total GDP levelled off as from 1981-1983). The reversal of this trend in Latin America and the Caribbean confirms the

agricultural sector's capacity to act as a buffer against general macroeconomic upsets in periods of depression, but if this situation persists for long it could mark the beginning of a process of de-industrialization of the region as a whole.

## 2. Agricultural exports

Between 1984 and 1989, the value of world exports of all types of goods grew by 60%, but over the same period the value of Latin American exports rose by only 8%. The Latin American and Caribbean region as a whole registered lower growth rates than the world average, and its share in the total value of world exports dropped from 5.8% in 1984 to 3.9% in 1989. In that year the region's share in world exports was less, in terms of value, than those of countries such as France (5.9% of world exports) or the United Kingdom (4.9%). This relative redimensioning of the region's exports is due, on the one hand, to the low level of dynamism of commodities all over the world,<sup>2</sup> and on the other, to the difficulties encountered by the region in trying to improve its relative position in the most dynamic export sectors. Thus, over the last ten years Latin America has not been able to increase its relative share in world exports in any of the six main categories of goods and services (agricultural products, mining sector products, manufactures, transport, travel and other services).

In the second half of the 1980s, world exports of agricultural products reflected the deterioration in the terms of trade already referred to, and their growth rate was less than that of world GDP and also lower than that of world trade in all categories of products (figure 3).<sup>3</sup>

<sup>2</sup>The main causes of the decline in the relative share of primary commodities in international trade have been: i) stagnation of global demand because of slackening world economic growth; ii) the growing generalization of replacement processes; iii) technical advances which make possible greater savings in industrial processes; and iv) the generally protectionist inclinations of the importing countries. It is also important to note that although primary commodities had a declining share in relative terms in international trade, the proportion of commodity exports from developed countries grew throughout the 1980s. See ECLAC, Santiago, 1991.

<sup>3</sup>Between 1984 and 1989, the value of world exports of agricultural products rose by 35.7%, while –as already noted– that of world exports of all goods rose by 60%.

For some products such as coffee or cocoa, the second half of the 1980s was a very negative period: it is calculated that in 1989 the drop in coffee prices caused loss of income of over US\$1.5 billion worldwide. Between 1989 and 1990, however, the market for this product settled down, and although the equilibrium which exists today is rather precarious, the evolution of production in coming years will probably influence export income more than in previous periods (FAO, 1990b).

Furthermore, in 1989 and 1990 there was a reversal of the upward trend in the prices of some products such as wheat, sugar and beef, which had been rising quite briskly in previous years.

At the general level, the fact that global agricultural exports have grown more slowly than world GDP has naturally meant an increase in the proportion of consumption of domestic production by the countries: that is to say, a reduction in the global import/consumption index.

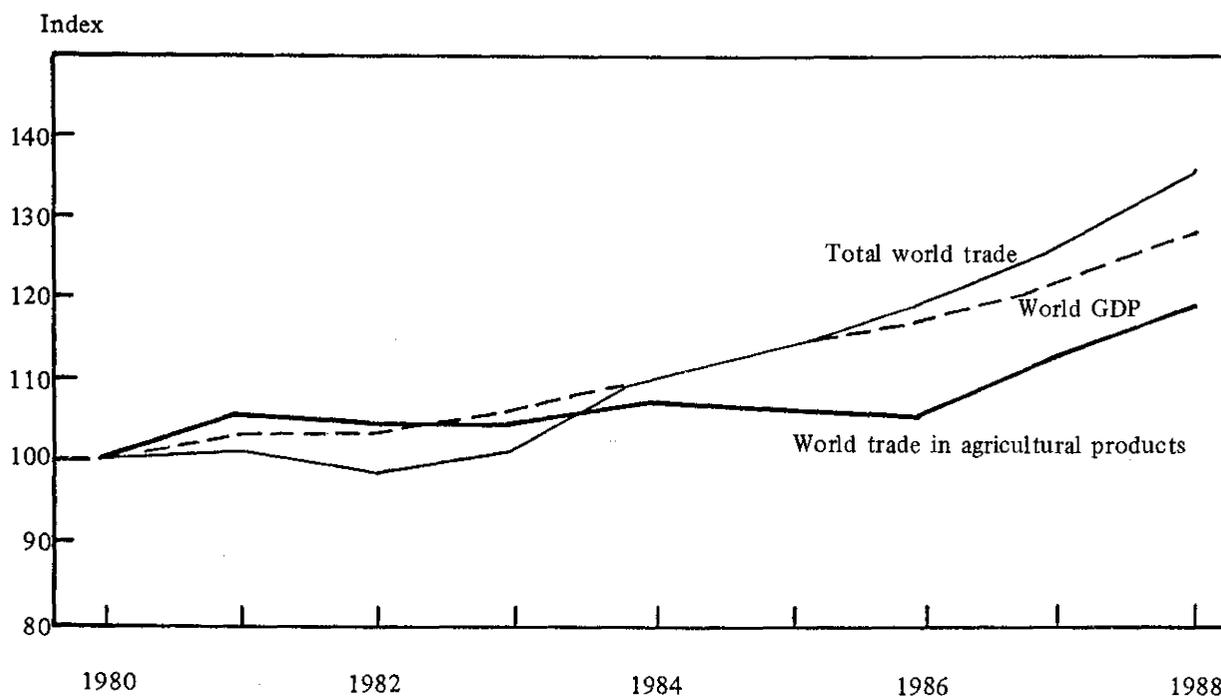
The slow growth of global agricultural exports, together with the deterioration in relative prices, has resulted at the world level in a smaller percentage share of agricultural exports in total exports. Thus, the value of world agricultural exports, which represented 11.4% of world exports of all types of goods in 1984, went down to only 9.6% in 1989. Within this already lower total, the percentage contribution of Latin America and the Caribbean contracted even more sharply, going down from 14.4% in 1984 to 10.5% in 1989. As may be seen from table 1, between 1984 and 1989 Latin America's total agricultural exports did not increase in value (on the contrary, they went down by 0.7%), whereas world agricultural exports increased, mainly because of the increase in European and Asian exports. Much of the sluggishness of the figures for the region's agricultural exports is explained by monetary factors (decline in the value of the dollar) and prices (declines in the prices of coffee, etc.). Other factors were the protectionist attitude of importing countries and, possibly, some cases of inefficiency in marketing.

The stagnation of the value of the region's agricultural exports compared with total regional exports, which grew by 8% between 1984 and 1989, has meant a decline in the relative importance of the agricultural sector in the region's external trade. Thus, agricultural exports formed 28.2% of total regional exports in 1984, but by 1989 the figure had gone down to 25.9%.

Figure 3

**TRENDS IN WORLD TRADE IN AGRICULTURAL PRODUCTS  
AND IN TOTAL WORLD TRADE**

(1980 = 100)



Source: GATT, *International Trade 1988-1989*, Vol. II, Geneva, 1989.

By way of comparison, it may be noted that over the same period forestry and fishery exports grew by 52.1%, so that in 1989 they represented 4.7% of total regional exports, compared with 3.7% in 1984.

At all events, it should be noted that the relative stagnation which took place in the second half of the 1980s came after an important period of expansion in the first half of the decade. In the period 1978-1984, Latin American agricultural exports grew more rapidly than the world average in terms of both volume and value (table 1).

Furthermore, it should be borne in mind that even in a situation of slow growth of global exports, as was the case in the region in the second half of

the 1980s, there were nevertheless products and countries which turned in a good performance. Thus, if we look at it in detail, the situation with regard to Latin American and Caribbean agricultural exports is seen to be fairly balanced, with sectors and countries which continued with quite well advanced processes of change in production patterns. Exports of non-traditional products were particularly dynamic. Moreover, not all the traditional export products went through stages of crisis or stagnation. On the contrary, the performance of the exporting countries of the region was quite good in the case of some products, especially cotton and bananas.

Table 1

**LATIN AMERICA AND WORLD TOTAL: EVOLUTION OF EXPORTS  
OF AGRICULTURAL PRODUCTS, 1978-1989**

(Indexes 1979-1981 = 100)

	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989
	<b>Volumes</b>											
Latin America	95	98	92	111	104	121	116	127	109	106	114	113
World total	89	92	101	106	105	105	109	108	107	114	117	120
	<b>Unit values</b>											
Latin America	89	95	113	92	87	79	90	79	92	85	91	90
World total	86	98	103	98	90	88	90	85	93	95	104	107
	<b>Global values</b>											
Latin America	84	93	104	102	91	97	105	101	102	91	104	102
World total	77	91	105	105	95	93	98	92	99	108	122	128

Source: FAO, *Trade Yearbook 1989*, Rome, 1990.

### 3. Non-traditional products

At the present time, one of the most interesting features of Latin American and Caribbean international trade in agricultural products is the promising performance of non-traditional exports.<sup>4</sup> In some countries, the bigger earnings from increased non-traditional exports made it possible to compensate for or even more than offset the impact of the drop in traditional export lines. In Brazil, for example, the increased income from exports of products based on soya beans and orange juice (US\$1 908 million more in 1989 than in 1986) more than made up for the lower value of exports of coffee and sugar (US\$581 million less in 1989 than in 1986).<sup>5</sup>

In spite of the satisfactory performance of non-traditional exports in many countries of the region, however,<sup>6</sup> it is difficult to forecast the degree of stability and the real prospects for the long-term expansion of international trade in these products. At any moment there may be unexpected upsets in the markets for particular vegetables, flowers or fruit. Often the high profitability of some products—especially temperate-zone products for the out-of-season market—has led a growing number of countries to embark upon or increase the cultivation and export of such products, resulting after a while in saturation of the market and a drop in prices and profitability. Something like this happened in the case of the markets for asparagus and fresh raspberries, causing a crisis which has affected several Latin American countries in recent years.

<sup>4</sup> The definition of non-traditional export products is not very strict and often varies from one country to another. Generally, however, a non-traditional product is considered to be any agricultural product which was not exported at all or only on a very limited scale before the period 1975-1980.

<sup>5</sup> Data provided by the Banco do Brasil, External Trade Department. See also ECLAC (1990).

<sup>6</sup> In addition to Brazil, there are other cases of development of agricultural exports based on non-traditional lines of products which have been closely studied by specialists in the sector and are often cited by the media. Examples of this are Colombia (cut flowers, tropical fruit), Chile (fruit, vegetables), Guatemala (vegetables), Mexico (vegetables), Paraguay (soya beans) and Peru (tropical fruit and vegetables). This very incomplete list shows, however, how most of the countries have concentrated on similar product lines.

The problem with some non-traditional products is their intrinsic vulnerability,<sup>7</sup> frequently connected with the fact that they are luxury products aimed at a relatively small percentage of consumers in the industrialized countries. These products are extremely sensitive to the economic cycles of the importing countries, especially because their prices are relatively high and also because –unlike traditional products such as bananas– their consumption has not become a regular habit in the importing countries. Consumers there consider that these products are attractive but not essential, and they can give them up very easily. It is therefore important that there should be good communication between exporters in the developing countries and importers in the recipient countries, particularly with regard to demand trends. As a general rule, countries exporting non-traditional products must pay close attention to information on markets and on competing supplies.

The trading characteristics of a non-traditional product may change with advances in storage and transport techniques. In the case of fresh fruit, for example, regardless of whether this is tropical or out-of-season temperate fruit, the possibility of changing from air transport to sea transport, thereby

substantially reducing prices, opens up new markets in the importing countries and is a factor in facilitating the incorporation of the product into the regular consumption habits of those countries.

For other products, especially those for agroindustrial use such as soya beans and cake, regardless of whether or not they are exported in semi-processed form, the markets may display price curves tending to go down in the medium and long term, because of the existence of production potential which is greater than demand possibilities. In other words, with the passage of time some non-traditional products may become subject to the mechanisms which are already tending to depress the markets for traditional commodities.

In view of the foregoing, and in the light of the experience of recent years, it may be stated that countries which wish to expand their trade successfully in non-traditional agricultural export lines must make an effort to ensure that their supply is as diversified as possible and they must also strive to attain a level of production and trading flexibility which will enable them to adjust to markets whose essential features change with considerable rapidity.

## II

### International markets in the 1990s

According to the mean “most probable” projection by the United Nations, by the year 2025 the world population will amount to 8 504 million people: a net increase of 3 104 million over the level assumed to have been reached in 1991 (UNFPA, 1991). With this growth, potential world demand for agricultural products should also increase considerably in the coming years, both in respect of foodstuffs and raw materials of vegetable and animal origin.

<sup>7</sup> Some specific studies which have taken due account of the oligopsonic nature of many markets for non-traditional products have come to the conclusion that the exporting countries tend to accept rather than fix the prices paid. This phenomenon is also observed in the case of countries which control a substantial share of the market for a particular non-traditional product. Thus, for example, in the United States market for out-of-season grapes, an exporting country such as Chile does not manage to exert any decisive influence on prices, even though it controls some 25% of the market.

At the same time, however, it is difficult to forecast to what extent this potential demand will be transformed into effective demand, for 95% of the population increase foreseen will correspond to the developing countries, especially South Asia, Africa, Latin America and the Caribbean and the Middle East. In contrast, it is expected that in most of the countries of Europe, North America and Oceania natural population growth will be very low (below 1%) or even zero. In East Asia, too, population growth is beginning to stagnate. Japan has already reached fertility rates below the replacement level, with an average of less than two children per family, and China will possibly reach this level towards the end of the century, while similar situations exist in the Republic of Korea and Thailand.

Thus, in the regions with the greatest economic growth prospects, the population –and hence the

potential demand for agricultural products— will grow very slowly. In contrast, in regions such as Africa or Latin America, which are more dependent on exports of agricultural products, the agricultural sector will have to increase its output sufficiently to feed the new population contingents, while at the same time it will have to generate a trade surplus sufficient to finance the necessary imports of industrial products.

It might be useful to sketch quite briefly a table indicating the real net position of the major areas of the world in the international agricultural product markets. For this purpose, we shall use the concept of the agricultural balance (Boulard, 1990). Over the last 25 years, there have been four deficit areas: i) Western Europe; ii) Japan; iii) Eastern Europe and the Soviet Union, and iv) the Persian Gulf countries. Japan has kept its deficit more or less constant, but the deficit of the Gulf countries has grown during the 1980s. The most interesting features are the increase in the deficit of Eastern Europe and the big reduction in the deficit position of Western Europe, which is now both the biggest exporter and the biggest importer of agricultural products in the world. Both the imports and exports of Western Europe grew rapidly during the 1980s, but the growth rate of that region's exports was markedly greater. In the period 1984-1989, for example, the cumulative increase in imports was around 55.6%, whereas the growth of exports was 70.3%. In many product lines, Western Europe is now a net exporter. Underlying this expansion of its exports are the big surpluses that have been generated in many member countries of the European Community as a result of the Community's Common Agricultural Policy (CAP) and its production support mechanisms.

Among the areas with a surplus, the United States has the highest positive balances, but these are characterized by big fluctuations, which cause their value to vary between 5% and 15% or 16% of world agricultural exports. The United States surplus comes mainly from its grain exports.

Latin America, which is the other main area with a surplus, is the principal supplier of the United States in most agricultural products other than cereals (60% in 1988). The balances for Latin America also fluctuate markedly as a result of the interaction of the variations in exports of tropical products, agricultural raw materials, cereals and beef on the one hand, with those of imports of food products on the other.

Other areas with surpluses, such as Canada, Australia, New Zealand and some Asian countries, register more stable positive balances. In the case of Africa, however, which registered a substantial positive agricultural surplus equal to almost 10% of the value of world agricultural exports in the late 1960s, its surplus has gone down steadily under the pressure of growing imports of food products and the decline in the prices of its main export products.

All this forms a picture whose essential features are unlikely to be changed much in the medium term. Let us now see what opportunities could arise on the markets as a result of the great processes of economic and social change which are taking place in some regions (Eastern Europe and the Far East) and world trends with regard to trade liberalization.

It is thus possible that big changes may take place in the structures of the world agricultural food supply system, which will bring with them increases in the demand for agricultural products originating in the developing countries. These changes could result from three parallel processes currently underway in the world, whose final outcome is not yet completely predictable. These processes are: i) the social, economic and political changes taking place in the Eastern European countries and the Republics which made up the former Soviet Union; ii) the process of industrialization and rapid expansion of GDP in many countries of the Far East, and iii) the negotiations within the Uruguay Round on the liberalization of international trade in agricultural products.

We shall now briefly analyse the effects that these processes could have on world trade in agricultural products, and the possible implications of this for the developing countries.

### *1. The effects of the changes East of the Elbe*

The intensive processes of social, political and economic change which are taking place in the Eastern European countries and the former Soviet Republics will affect the structure of the world agricultural food supply system in two different ways: on the one hand, there will be an increase in the global demand of those countries; on the other, there will be an increase in their own supply of agricultural products. These two phenomena must naturally be of particular interest to the developing countries, which, in the medium term, must organize themselves to take advantage of the opportunities and reduce the risks involved in the entry of important new actors on the world agricultural market.

There can be no doubt that an increase in the growth rate of GDP in the Eastern European countries and the Republics which made up the former Soviet Union would raise demand for some products from the developing countries, especially Latin America and the Caribbean. A higher standard of living in the former communist world would be reflected in bigger imports of tropical beverages (tea, coffee and cocoa), tropical fruit, cotton, sugar and other products. Although most analysts assert that in the medium or long term these countries should register a substantial process of economic growth, however, it is not possible to forecast with any certainty the magnitude or rate of this process, or the length of time that would be needed for GDP and demand to begin to grow significantly. Consequently, it is as yet too early to quantify these variables.

A more probable development in the medium term could be an increase in the exports of agricultural products from some of these countries—especially those closest to the EEC—to the OECD countries. The radical changes already made in countries like Hungary and Poland are giving rise to substantial increases in their agricultural productivity. In 1988, these two countries came to an agreement with the EEC whereby they can export their agricultural products to the Community free of duties. At the same time, under the powerful stimulus of the liberalization of domestic markets, Hungarian and Polish farmers have considerably increased their output, while domestic consumption has continued to stagnate or even go down as a result of the elimination of price controls. This situation has been reflected in the rapid generation of substantial exportable surpluses.

According to some estimates (Fottorino, 1991), Poland—a country which has traditionally been an importer of butter—now has exportable surpluses of this product estimated at 70 000 tons. Czechoslovakia already has the capacity to export nearly 40 000 tons of dried milk, while various Eastern European countries also have export capacity for beef and live animals (it is estimated that in 1990 these countries sold some 80 000 head of cattle at low prices).

While the potential of the Eastern European countries to export agricultural products is by no means negligible, that of the Republics which made up the former Soviet Union could be much greater in the long run. Although, as it stands at present, Soviet agriculture on the whole registers deficits, this does not mean that it will continue to do so indefinitely. Various analysts consider that between now and the

year 2000 at least some of the former Soviet Republics, such as the Ukraine, could recover the position as grain exporters which they occupied before 1917. Others consider that this could hardly take place before the period 2005-2010, but at all events, considering the present size of the cereals sector of the former Soviet Republics,<sup>8</sup> the hypothesis of the development of agricultural export capacity in the medium term must be taken very seriously (table 2).

## 2. *The potential of the Asian markets*

In the medium term, opportunities may also arise for exporting countries in the markets of the Asian countries. In recent years these countries have registered and continue to register growth rates which are among the highest in the world.<sup>9</sup>

With regard to growth in international trade in agricultural products of the Asian countries in recent years, between 1984 and 1989 the agricultural imports of the nine countries in question grew by 58.4%. The highest growth rates of agricultural imports corresponded to China, South Korea, Thailand and Hong Kong, whose imports rose in percentage

<sup>8</sup> In 1989, Soviet cereals production represented 10.9% of the world total. In the same year, United States production represented 15.2% of the total and that of Argentina 0.9% (1.2% in 1988).

<sup>9</sup> Although economic growth rates in Asia and the Pacific slackened in 1989, they continued to be among the highest in the world. Thus, the real rate of increase of the aggregate GDP of the region went down to 5.3% in 1989, after the unprecedented figure of 9.4% registered in 1988. China and India—the two biggest Asian economies after Japan—registered quite a sharp drop in their GDP growth rate. In China, this went down from 11.2% in 1988 to 3.9% in 1989, while that of India fell from the record level of 9.5% in 1988 to 4.5% in 1989. In the latter year, the agricultural GDP grew by 4.5% in China and 2.0% in India. In the region in question, only Nepal, Papua, New Guinea and Samoa registered GDP growth rates in 1989 that were below 2%. No negative rates were registered at all. On the contrary, the Republic of Korea, Singapore, Thailand, Indonesia, Malaysia, the Philippines, Pakistan, Fiji, the Maldives and Taiwan all had GDP growth rates over 5%. Thailand, with a growth rate of 10.8%, was the fastest-growing economy in the whole world in 1989. Likewise, a number of countries obtained excellent results in the agricultural sector in 1989. In Nepal, Pakistan, Burma, Fiji and Vietnam, the agricultural GDP grew by 6% or more in that year. Indonesia, Laos, Malaysia, Thailand and the Philippines, for their part, registered agricultural growth rates between 3.5% and 4%. In 1989, the Asian region generated almost 90% of world rice production and 42% of world cereals production. China, India, Bangladesh and Thailand had record rice harvests thanks to a combination of good weather, greater use of high-yielding varieties, and an increase in the area planted with the cereal.

Table 2  
**SOVIET UNION: TOTAL CEREALS PRODUCTION, 1986-1990**

(Thousands of metric tons)

	1986	1987	1988	1989	1990	Average 1986-1990	Percentage of total
Russia (RSFSR) <sup>a</sup>	117 968	109 084	102 807	112 360	127 000	113 844	53.5
Ukraine	43 063	50 184	47 388	54 900	53 200	49 747	23.4
Moldavia	2 044	2 011	3 052	3 538	2 600	2 649	1.2
Byelorussia	7 041	9 281	6 922	7 900	8 200	7 869	3.7
Kazakhstan	28 306	27 444	22 560	20 200	31 200	25 942	12.2
Transcaucasian Republics	2 035	2 057	2 504	1 607	2 400	2 121	1.0
Central Asia	3 447	4 443	4 775	4 071	4 400	4 227	2.0
Baltic Republics	6 164	6 897	5 050	6 324	6 800	6 247	2.9
<b>Total</b>	<b>210 068</b>	<b>211 401</b>	<b>195 058</b>	<b>210 900</b>	<b>235 800</b>	<b>212 645</b>	<b>100.0</b>

Source: U.S. Department of Agriculture, Foreign Agricultural Service.

<sup>a</sup> Russian Soviet Federated Socialist Republic.

terms more than those of Japan. At the same time, the total agricultural exports of these countries also increased at a rapid rate—around 45%—between 1984 and 1989. In this period, the fastest growth of agricultural exports was registered by China (81%) and Thailand (57.2%). Thus, China has almost ceased to be a deficit country, and Thailand, Malaysia, Indonesia and India are net exporters (table 3).

It is interesting to note that in a number of countries agricultural export development has been accompanied by substantial growth of agroindustry. During the 1980s, another two nations—Thailand and Malaysia—joined the group of newly industrialized Asian countries.<sup>10</sup> Unlike what happened so far in other countries of the region which are included in this category, however, Thailand and Malaysia are developing, within a rapidly expanding industrial sector,<sup>11</sup> a substantial agroindustrial subsector closely linked with export agriculture (FAO, 1990c, p. 55). In Thailand, for example, the average annual growth rate of exports of frozen poultry in 1984-1989 was 26%, and that of canned pineapple

was 14%. During the same period, exports of processed goods by Malaysia grew at an average annual rate of 10%.<sup>12</sup>

The success of Thailand and Malaysia in increasing their production and trade in traditional and non-traditional agricultural products, together with their capacity to create a dynamic and aggressive agroindustrial complex in order to export high-quality products, explain why they are considered newly agro-industrialized countries (FAO, 1990c, p. 55).

The dynamic development of the Asian region—one of the most striking economic and social phenomena of these final years of the century—opens up opportunities but also represents threats for the Latin American agricultural exporting countries. On the one hand, the economic growth and growing consumption capacity of their inhabitants are creating new markets for the products of the Latin American and Caribbean countries. On the other hand, however, the great dynamism of the Asian agricultural exporters may in time reduce the market shares currently won by Latin American enterprises, not only in the Asian region itself but also in Europe or North America.

<sup>10</sup> This definition had already been applied in previous years to Hong Kong, the Republic of Korea, Taiwan and Singapore.

<sup>11</sup> In the 1980s, the average annual growth rate of the industrial sector was 30% in Thailand and 20% in Malaysia.

<sup>12</sup> This growth of the agroindustrial sector has formed part of the general growth of industries processing renewable natural resources. In the 1980s, for example, Thailand's exports of canned fish and shrimps grew at an average annual rate of 29% and exports of wood products grew at a rate of 21%. Malaysia's exports of rubber-based manufactures and wood products grew at average annual rates of 33% and 10% respectively.

Table 3

**SELECTED FAR EASTERN COUNTRIES: IMPORTS AND EXPORTS OF  
AGRICULTURAL PRODUCTS, 1984-1989**

*(Millions of dollars)*

	Imports						Exports					
	1984	1985	1986	1987	1988	1989	1984	1985	1986	1987	1988	1989
Japan	18 446.4	16 865.9	18 129.8	20 934.3	26 805.4	29 059.5	853.7	755.3	834.6	947.5	1 016.3	1 073.6
China <sup>a</sup>	5 736.7	4 785.1	5 386.4	7 439.9	9 740.2	11 074.8	5 589.6	6 248.0	7 886.9	9 056.7	10 058.8	10 168.5
Republic of												
Korea	3 431.4	3 074.7	3 267.1	4 055.6	5 282.5	6 308.5	562.1	502.4	590.0	747.1	1 006.2	1 106.4
Hong Kong	3 569.6	3 542.0	3 707.3	4 758.9	5 738.1	6 293.3	1 279.9	1 467.8	1 644.9	2 173.4	3 020.3	3 272.3
Singapore	2 801.1	2 436.2	2 292.3	2 451.1	3 058.0	3 196.5	2 205.5	1 832.1	1 742.6	1 828.4	2 306.6	2 434.7
Malaysia	1 634.0	1 465.9	1 300.2	1 488.1	1 852.9	2 067.2	4 641.9	3 717.9	3 305.0	4 082.7	5 181.9	4 620.5
Thailand	651.1	547.9	571.1	771.9	1 056.6	1 248.8	3 821.3	3 202.7	3 596.0	3 949.0	5 045.5	6 010.2
Indonesia	1 117.1	903.5	934.7	1 124.0	1 319.3	1 625.2	2 462.0	2 475.2	2 528.3	2 769.9	3 323.0	3 184.4
India	1 941.6	1 650.5	1 311.3	1 582.7	2 319.8	1 426.7	2 259.2	2 264.6	2 376.1	2 373.4	2 207.4	2 469.0
<b>Total</b>	<b>39 329.0</b>	<b>35 271.7</b>	<b>36 900.2</b>	<b>44 606.5</b>	<b>57 172.7</b>	<b>62 299.7</b>	<b>23 678.2</b>	<b>22 466.0</b>	<b>24 504.4</b>	<b>27 928.1</b>	<b>33 166.0</b>	<b>34 339.6</b>

Source: FAO, *Trade Yearbook 1989*, Rome, 1990.

<sup>a</sup>Including Taiwan.

Indeed, in the main Asian market –Japan– the presence of Latin American products is not very great (5.9% in 1988) in spite of the great possibilities for

complementation between the economy of that country and those of the Latin American and Caribbean agricultural exporting countries.

### III

## The Uruguay Round

#### *1. The past extent of agricultural protectionism*

The direction taken by the processes of change in the Eastern European countries, as well as the processes of rapid development observed in the Far East, will decisively influence the evolution of world trade in agricultural products in coming decades. In the short term, however, the most important developments could emerge from the multilateral trade negotiations being carried out in the eighth round of GATT: the Uruguay Round. Their outcome will be of the greatest importance for world trade in general and agricultural products in particular. Indeed, the most important new feature of the Uruguay Round compared with previous GATT negotiating rounds has

been the extensive space reserved for agricultural issues on the agenda.<sup>13</sup> As the debates have progressed, it seems evident that the success of the

<sup>13</sup> Within GATT, agricultural issues had already been discussed in the Dillon Round (1960-1962), and more extensively in the Kennedy Round, where the opposing positions of the European Economic Community and the United States took shape quite clearly. In the Tokyo Round (1976-1979), agriculture was one of the main points of tension, and the discussions were also complicated through the lack of agreement between the United States and the EEC on procedural matters. The experiences of the Tokyo Round led to the formation in 1982 of an Agricultural Trade Committee made up of representatives of 57 nations, with significant presence of the developing countries. The work of this Committee made it possible to identify more precisely the issues and procedures for negotiation in the Uruguay Round. For a detailed analysis of the role of agriculture in GATT, see Basile (1991), Hathaway (1987) and Mine, Ingersent and Rayner (1989).

Round as a whole will depend on the possibility of reaching agreement on the liberalization of trade in agricultural products.

Another important feature of the Uruguay Round is the broad scope of the negotiations, which cover not only protective measures such as tariffs and import quotas, but also policies on subsidies for agricultural exports and the fundamental issue of subsidies and other support measures for domestic agricultural production.

The possible successful outcome of this Round could lead to a fundamental reversal of the tendency which has existed for over a century towards agricultural protectionism.<sup>14</sup> With the depression registered in the last twenty years of the nineteenth century, the European countries began, one after another, to use tariffs to protect their agricultural production which was threatened by competition from Russia and from the new producers of those days, that is to say, the United States, Canada, Australia, New Zealand and Argentina.

The main reasons put forward in justification of protection were: i) the need to maintain a certain level of food self-sufficiency; ii) considerations connected with the "special nature of the sector";<sup>15</sup> and iii) the need to protect the standard of living of the inhabitants of rural areas.<sup>16</sup>

With the crisis of the 1930s, the protectionist logic spread to the United States, which since that decade has displayed an attitude of openness with regard to trade in manufactures and protectionism with regard to agricultural trade.

After the Second World War, the United States progressed from defending its agriculture to active promotion of its agricultural exports. In its view, this involved the protection of a natural comparative advantage. Between the early 1950s and the beginning of the 1970s, United States agricultural exports grew fourfold and began to play a more important role in offsetting the trade deficits which grew more and more as from that period.

<sup>14</sup> For more details of the past evolution of agricultural protectionism see: K. Anderson and Y. Hayami (1986), Basile (1990) and Jones (1989).

<sup>15</sup> The concept of the "special nature" of the agricultural sector refers to the fact that agricultural activities run bigger risks than other sectors of production, because in addition to the risks inherent in any economic activity there are also those due to the weather and pests and diseases.

<sup>16</sup> With the passage of time, the supporters of protectionism have also emphasized the "special social importance" of the agricultural sector in terms of both employment and political and territorial equilibria.

As long as the United States saw itself as an exporting country and the EEC as an importing area, the conflict between the United States agricultural export thrust and European agricultural protectionism remained latent. When the Community began to develop big export potential in direct competition with the United States, however, the trade conflict was manifested in increasingly open forms.

As well as stepping up the conflict, the protectionist instruments were refined and diversified.<sup>17</sup> Tariffs were increasingly accompanied by quantitative restrictions, non-tariff duties, technical and customs barriers, and various forms of direct State intervention in agricultural markets (through subsidies for production and exports, acquisition of products by government agencies for price defence purposes, and political and diplomatic intervention in order to achieve voluntary self-restraint agreements with other countries).

Over the last hundred years of protectionism, the evolution of these instruments has also been accompanied by an evolution of the objectives pursued. There has been a gradual progression from policies involving closing markets or strengthening natural comparative advantages to policies designed to create artificial conditions of competitiveness for national agricultural producers.

It is important to note that the problems of international trade in agricultural products are of political importance, not only in the sense of the implications of these matters for the domestic policy of the various countries (electoral weight of farmers, food prices, regional policies, etc.), but also the growing international political dimension of agricultural trade. It might seem a paradox that in the last decade of the twentieth century, the most controversial aspect of trade relations between the two greatest economic areas in the world, the United States and the EEC, is agriculture. This international political dimension of agricultural issues is bound to last for many years to come, whatever the outcome of the Uruguay Round, because of the increasing importance that food and agricultural balances will have for the stability of various regions of Africa, South Asia, and, looking forward into the future, Latin America too.

<sup>17</sup> Reference has been made to the "escalation" of protectionist instruments. See Basile (1991).

## 2. The positions of the various actors

The GATT rules on agriculture are relatively few in number, rather generic in nature, and moreover drafted in slightly ambiguous terms. In one way or another, they are strongly conditioned by the priorities which the contracting parties had at the time when the agreement was ratified. Thus, in keeping with the objective of permitting the consolidation of a world trade system which is as free as possible, some pains were taken to avoid introducing into the text any reference or declaration of principle on the "special nature" of the agricultural sector. In order to permit the reconstruction of European agriculture, however, some rules were incorporated which, in fact, were to give various degrees of protection to national agricultural production.<sup>18</sup>

What the Uruguay Round has aimed to modify in depth is therefore a complex of rules and established forms of behaviour which have governed international agricultural trade over the last 40 years. Furthermore, there has been an explicit desire to measure the effective obstacles impeding trade in agricultural products and to establish a clear conceptual connection between national agricultural policies and distortion of markets.

The main participants in the debates in this Round have been the United States; the EEC; the

Cairns Group;<sup>19</sup> Japan, Korea, the Scandinavian countries and Switzerland, which share a marked sensitivity to domestic food security issues; and the developing countries which are importers of food.<sup>20</sup>

These debates have highlighted above all the discrepancies between the two main negotiators—the EEC and the United States—over three points:

i) *The conversion of non-tariff obstacles to imports into customs tariffs which provide equivalent protection to begin with and could be gradually reduced to zero in the course of time.* So far, it has not been possible to reach agreement on this point for various technical reasons connected with the criteria for the determination of reference prices and years and the opposition of the European Community to a form of conversion into tariffs which does not provide for suitable "correction coefficients" for protecting the income of farmers from abrupt variations in international prices or fluctuations in exchange rates.

ii) *Reduction of domestic assistance and criteria for measuring it.* The European Community offered a 30% reduction of the global aid which it has been applying to products where it is known that there are serious structural imbalances: rice, cereals, sugar, meat, protein-rich foods, olive oil and oilseeds.<sup>21</sup> This proposal has been considered unsatisfactory by other negotiators and by the United States in particular. An even more paralyzing element has been the discrepancy between the United States and the European Community on the criteria for measuring effective domestic aid. The United States negotiators proposed the use of producer subsidy equivalents, whereas the European Community advocated the use of a support measurement unit, because this essentially identifies aid affecting international markets.

<sup>18</sup> These rules consist, primarily, of articles XI, XII and XIII, which permit the adoption of quantitative restrictions on imports and exports for various reasons (food crises, need to control international production, balance of payments problems). These articles are very important because in principle GATT does not permit the adoption of such instruments, since it considers them a form of "non-transparent" protection, in contrast with tariffs, which are the only form of "transparent" protection. In addition, article XVI, which is drafted in complex and rather vague terms, actually permits the adoption of subsidies. It is worth noting that the generic nature of the criteria and of the frame of reference selected in this article for imposing discipline on the adoption of subsidies lie at the root of the great majority of the controversies in GATT between the United States and the EEC in the period 1976-1986. Finally, article XXV.5 permits temporary exemption from the obligations of GATT in "exceptional circumstances". This rule has been repeatedly used by the United States since 1951 (in respect of dairy products).

<sup>19</sup> The Cairns Group, named after the Australian city, is made up of 13 countries which are major exporters of agricultural products: five Latin American countries (Argentina, Brazil, Chile, Colombia and Uruguay), four Asian countries (the Philippines, Indonesia, Malaysia and Thailand), three countries from Oceania (Australia, New Zealand and Fiji), and one Eastern European country (Hungary). As may be seen, this is a group of countries which are quite different in their general economic structures but share the common feature of being efficient exporters of temperate-zone agricultural products.

<sup>20</sup> Among these countries, a particularly active role has been played by Egypt, Jamaica, Mexico, Morocco, Nigeria and Peru.

<sup>21</sup> Some of these products are of great importance for the Latin American and Caribbean region.

iii) *Export subsidies*. The United States proposes the total elimination of these subsidies over a period of five years, whereas the European Community proposes a system of gradual reduction, combined with "correction coefficients".

Both the question of domestic aid and that of export subsidies form part of the same fundamental issue for the long-term interests of the developing countries: that of the net transfers of resources which the industrialized countries regularly make to their farmers in order to create artificial competitiveness, evading the cost differences with producers in developing countries. In order to appreciate the real dimension of these transfers, it may be recalled, for example, that in 1988 the global transfers by the OECD countries to their agricultural sectors totalled US\$266.7 billion, that is to say, a value comparable to that of the entire world agricultural exports in that year (US\$287.2 billion). In 1989, these transfers grew still further to US\$299 billion while world exports of agricultural products came to US\$299.9 billion in the same year (table 4).

It may be seen from table 4 that, with the notable exception of Australia and New Zealand, which are big exporters of agricultural products, all the OECD countries heavily subsidize their agriculture.

It is obvious that a reduction of subsidies and, in general, a successful outcome of the Uruguay Round, would considerably increase the relative competitiveness of the developing countries which export agricultural products. At the present time, however, the great processes of openness which are taking place in many areas of the developing world, especially Latin America and the Caribbean, are creating an unbalanced situation between a South which is opening up its economy and a North which is engaging in protectionism.

After the resumption of the Uruguay Round negotiations, the prospects of reaching agreement on agriculture could improve as a result of the debate on the reform of the Common Agricultural Policy which is taking place within the EC. The agricultural budget, which absorbs two-thirds of the entire Community budget, grew by 20% in 1991 compared with 1990, and initial calculations on the 1992 budget indicate a possible increase of 12.6% compared with 1991. In view of these spectacular increases, together with the growing imbalances which exist in the markets for cereals, beef and mutton, milk and wine, the

Commission of the European Community has prepared new guidelines for a fundamental reform of the Common Agricultural Policy. If this reform is finally approved by the member countries, it could open up the way for an agreement within the Uruguay Round (ECLAC, 1991).

At the same time, it is important to bear in mind that not all the individual countries within the Community take the same positions. The main concern of Germany is to defend the income levels of its agricultural producers, while other countries, such as France, also want to defend the export capacity of their agriculture. These internal differences markedly reduce the freedom of action of the Community negotiators.

For the North American negotiators, on the other hand, the main objective is to defend their agricultural trade surplus. The United States, in particular, regularly turns in a positive balance on its external agricultural trade. In the last two years, however, that positive balance has begun to be threatened by the reduction in the volumes exported and in the prices obtained. In other words, United States agricultural exports have suffered the effects of the same phenomena which are affecting some developing countries. In the light of these circumstances, and in view of the importance that the agricultural surplus has for a trade balance like that of the United States, which registers an overall deficit, it is easy to understand the efforts which that country is making to gain greater access to the markets of Europe and Japan. These United States efforts are clear proof of its declared will to increase the volume of its agricultural exports to all markets. In the coming years, the United States will probably further intensify its promotional activities in two geographical areas in particular: firstly, in Latin America and the Caribbean, within the trade openness initiatives which are underway throughout the region; and secondly, in the Republics of the former Soviet Union, and especially Russia itself. Indeed, of the US\$4.5 billion which the United States has so far promised to the members of the Community of Independent States (CIS) as a whole (Crisafulli, 1991; Marti, 1992), US\$3.75 billion correspond to guaranteed agricultural credits. At the same time, other credits will be given to the group of former communist countries through a specialized agency (the Commodity Credit Corporation), in order to enable them to purchase agricultural

Table 4

**ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT (OECD):  
TOTAL TRANSFERS TO AGRICULTURAL SECTOR**  
(Billions of dollars)

	Fiscal transfers <sup>a</sup>				Transfers paid by consumers <sup>b</sup>				Fiscal income <sup>c</sup>				Total transfers (1)+(2)-(3)			
	(1)	(1)	(1)	(1)	(2)	(2)	(2)	(2)	(3)	(3)	(3)	(3)	(1)+(2)-(3)	(1)+(2)-(3)	(1)+(2)-(3)	(1)+(2)-(3)
	1987	1988	1989	1990	1987	1988	1989	1990	1987	1988	1989	1990	1987	1988	1989	1990
Australia	0.3	0.2	0.3	0.3	0.4	0.4	0.4	0.4	-	-	-	-	0.7	0.6	0.7	0.7
Austria	1.0	1.0	0.8	1.1	2.8	2.6	2.0	2.7	-	-	-	-	3.8	3.5	2.8	3.8
Canada	5.6	5.7	4.3	4.7	3.6	3.6	3.5	3.6	0.1	0.1	0.1	0.1	9.1	9.3	7.8	8.3
EC (12 countries)	38.2	45.6	41.3	49.3	82.7	75.0	61.9	85.1	0.9	1.0	0.8	1.0	120.0	119.6	102.4	133.4
Finland	1.6	1.8	1.7	2.2	3.1	3.3	3.2	3.8	0.3	0.1	-	0.1	4.4	5.0	4.9	5.9
Japan	17.9	19.6	18.0	14.9	60.0	65.6	59.0	54.7	11.5	15.0	11.7	10.6	66.4	70.1	65.3	59.0
New Zealand	0.1	0.1	-	-	0.1	0.1	0.1	0.1	-	-	-	-	0.1	0.2	0.1	0.1
Norway	1.8	1.9	1.8	2.1	1.8	1.7	1.6	2.2	0.2	0.1	0.1	0.1	3.3	3.5	3.3	4.2
Sweden	0.6	0.6	0.5	0.5	2.7	2.6	2.7	3.0	0.2	0.2	0.1	0.1	3.1	3.0	3.1	3.4
Switzerland	1.7	1.8	1.8	2.1	4.5	4.7	3.9	4.9	0.8	0.8	0.6	0.7	5.4	5.7	5.0	6.2
United States	51.6	44.2	47.8	47.1	31.4	26.0	24.2	27.9	1.4	1.0	0.7	0.9	81.5	69.1	71.3	74.1
<b>Total</b>	<b>120.3</b>	<b>122.3</b>	<b>118.4</b>	<b>124.3</b>	<b>192.9</b>	<b>185.6</b>	<b>162.6</b>	<b>188.3</b>	<b>15.3</b>	<b>18.4</b>	<b>14.2</b>	<b>13.6</b>	<b>297.8</b>	<b>289.6</b>	<b>266.7</b>	<b>299.0</b>

Source: OECD estimates.

<sup>a</sup> Fiscal transfers include State, federal and Community taxes.

<sup>b</sup> Transfers paid by consumers represent additional outlays which consumers in the various OECD countries must make as a result of national price support policies and protectionist measures.

<sup>c</sup> Fiscal income generated as a result of price policies occurs only in the case of products in which the countries are not self-sufficient.

products from the United States. Some US\$2.5 billion were granted through the Commodity Credit Corporation in 1991, and a third credit of US\$1.25 billion was agreed in November 1991. The CIS currently absorbs between 25% and 30% of the agricultural

exports of the United States, and in the short and medium term, until the agricultural sector of the former Soviet Republics is fully reorganized, the percentage of United States agricultural exports that goes to these markets is bound to increase further.

## IV

### Trade liberalization prospects and the developing countries

A successful outcome of the Uruguay Round would lead to at least the partial liberalization of international trade in agricultural products. At present the leeway open to the negotiators is not very great, especially in view of the pre-electoral period in the United States and the debate on the reform of the Common Agricultural Policy in the member countries of the European Community. As the months go by, however, the prospects of a compromise

agreement could become more likely. Open failure of the Uruguay Round would have very strong adverse psychological effects on the economic agents, precisely at a moment when the signs of world recession are already very serious.<sup>22</sup>

<sup>22</sup> According to an updated version of the United Nations *World Economic Survey 1991*, total world production and income went down in 1991 for the first time since the Second World War.

If the negotiations have a satisfactory outcome, this would strengthen general confidence and have a substantial anti-recessionary effect.<sup>23</sup> Moreover, the Uruguay Round already involves too many vital sectors of the world economy to be allowed to fail merely because of the impasse over agricultural trade.<sup>24</sup>

It therefore seems important to try to guess in advance what effects international agricultural trade liberalization is likely to have on the economies of the developing countries.

In recent years, a number of analytical models have been prepared, some of them of high formal sophistication, which are expressly designed to cover the problem of the effects such liberalization would have on the various markets (Goldin and Knudsen, eds., 1990). The set of models presents multiple scenarios for different degrees of liberalization and different analytical approaches (partial equilibrium models, general equilibrium models; cases of a single product or several products; partial or specific markets, etc.). In general, they have been criticized, *inter alia*, for not taking account of the existence of preferential trade agreements (the Lomé Agreement, the Caribbean Basin Initiative, etc.); for not having paid sufficient attention to the question of food security; for not having taken account of the reactions of the countries concerned when presenting hypotheses on price variations, and not having highlighted the differences of basic interests between the various groups of developing countries (Ananía, 1990). Nevertheless, it is interesting to make a rapid review of the results of these models, which are the only analytical instruments available so far for gaining some indications of the trends that might be followed in terms of the possible effects of liberalization on agricultural markets.

<sup>23</sup> As the Director-General of the International Monetary Fund expressly stated in his address before the Economic Commission for Latin America and the Caribbean on 29 November 1991: "Nothing could do more to strengthen the medium-term growth prospects of the developing countries, and the industrial countries too, than the successful completion of the Uruguay Round. This would boost confidence precisely at the moment when it is most needed".

<sup>24</sup> There are 14 issues under negotiation in the Uruguay Round: 1) tariffs, 2) non-tariff measures, 3) natural resource-based products, 4) textiles, 5) agriculture, 6) tropical products, 7) the articles of GATT, 8) multilateral agreements, 9) safeguard measures, 10) subsidies, 11) intellectual property rights, 12) investments, 13) settlement of disputes, and 14) functioning of the GATT system.

In general, the analysis of these results indicates that the developing countries will be the most affected –positively or negatively, depending on the particular cases– by the liberalization of agricultural trade. In a way, this is obvious, since the agricultural sector is relatively much more important to the developing countries than to the developed nations.

In the short and medium term, efficient exporting countries, such as the Cairns Group countries, will considerably increase their exports and earnings.

The food importing countries, on the other hand, will be adversely affected in the short and medium term by the increase which is expected in the prices of many products. All the models foresee an increase in the short and medium term in the prices of meat, dairy products and sugar. Moreover, all of them except the MTM model of the OECD (Moreddu, Parris and Huff, 1990) also foresee increases in the prices of cereals for human consumption. In the case of basic grains for animal feed, the results are more open to controversy. Thus, both the MTM model and the model prepared by Zietz and Valdés (1990) foresee a decline in prices as a result of the crisis in the stock-raising sector of the OECD countries caused by the liberalization of markets. The other models, however, foresee an increase in prices in the basic feed grains sector also.

Examination of the models also clearly reveals that if there were liberalization of the export markets of the developing countries together with liberalization of the OECD import markets, the rise in prices would be significantly less in the medium term.

In other words, if the policies of the developing countries adopted an export bias and if they abandoned, at least partially, the tax, exchange rate (overvaluation of the exchange rate) and tariff (duties on inputs) measures which make it less attractive to produce for export, this would considerably increase the possibility that farmers in the developing countries could respond rapidly to the new opportunities created in international markets as a result of liberalization in the OECD countries.

Thus, simultaneous liberalization in North and South would cause a gradual change in the geography of trade flows, together with a general increase in efficiency instead of a mere generalized rise in prices (Krissoff, Sullivan and Wainio, 1990). This makes clear the fundamental strategic importance of the transmission mechanisms between international and domestic prices in developing countries which are exporters of such goods.

Consequently, the rise in international prices would be a strong stimulus for the agricultural supply of the developing countries. In the medium and long term, it would also stimulate technological change, with consequent increases in yields. With time, the increase in international prices could be reabsorbed. It is important that the whole process should be of a gradual nature: rapid increases in food costs could have very severe political and social consequences for the importing countries, while the gradual nature of the process could facilitate the adjustment of both the importing and exporting countries.

At all events, it is necessary to highlight two unknown quantities which the models do not help to solve because of their inherent methodological approach. Firstly, it is not clear what aggregate effect the big changes in the structure of international prices will have in the medium term on the aggregate supply of China, the Eastern European countries, and the members of the CIS. Because of the size of their total agricultural production, even modest percentage increases in the supply of countries such as China or India could have big effects on prices.

Secondly, it is not clear either what impact the strategies of the big transnational firms are likely to have on the agricultural food market. In view of the market shares controlled by these enterprises,<sup>25</sup> the hypothesis of perfect competition which is at the basis of the great majority of the models seems unrealistic, at least for some products. The intermediation of the big transnational corporations means that agricultural producers in the exporting countries are faced in many markets with an oligopsony, while consumers in the importing countries are supplied through an oligopoly.

For many developing countries, the negotiations specifically devoted to tropical products have been of special importance. The position of the developed countries with regard to these products has generally been more flexible than in the case of other products.

<sup>25</sup> In the early 1980s, for example, five big firms controlled around 90% of the wheat and maize exports from the European Community, almost 90% of the exports of Argentine wheat, and 90% of exports of Australian sorghum. At the same time, four enterprises controlled between 60% and 65% of the world sugar market and three enterprises controlled 60% of the cocoa market. For more details on these points, see Davies (1986) and Cramer and Heid (1983).

The specific objective of the negotiating group within the Uruguay Round has been to secure the fullest possible liberalization of trade in these products, including their trade in processed and semi-processed form, extending to all the tariff and non-tariff measures affecting this trade. According to the Punta del Este Declaration, this sector should receive special attention, in view of the importance of the trade in tropical products for many developing countries.<sup>26</sup>

The main achievement of these negotiations has been the unilateral granting of tariff reductions by a number of developed countries, which began to be applied in January 1989. Subsequently, other more far-reaching proposals have been put forward, but the developed countries have linked the results of the negotiations in this field with those attained in other groups. Furthermore, their markets have tended to become less and less open as the degree of processing of products increases (Ananfa, 1990). This has been reflected in the phenomenon of tariff scaling already referred to.

Since it is very important for the developing countries to progress from the phase of developing agricultural exports to that of developing agroindustry, the problem of tariff scaling must be given due consideration by all the interested parties.

A final point that should be highlighted is that of the possible effects of the liberalization of agricultural markets on food aid flows. So far, the existence of big surpluses in the North has been an important prior condition for the food aid plans designed to help many developing countries. If trade liberalization not only puts an end to the tendencies of agriculture in the developed countries to produce surpluses but also leads to the cessation of food aid, this could result in famine in a number of areas of the world. It is therefore important to strengthen and suitably modify the bilateral and multilateral food aid mechanisms, in order to avoid emergencies that will be difficult or impossible to cope with when the effects of the liberalization begin to felt.

<sup>26</sup> Although there is no agreed definition of tropical products, the negotiations of this group have covered the following product groups: tropical beverages (coffee and coffee products, cocoa and cocoa products, tea and instant tea); spices and essential oils, cut flowers, plants, vegetable materials, lacs, etc., and products thereof; certain vegetable oils, oilseeds and oilcake; tobacco and tobacco products; rice, cassava and other roots of tropical plants, and products thereof; bananas and banana products, and other tropical fruits and nuts and products thereof, including fruit juices; tropical timber and products thereof; natural rubber and rubber products; and jute and hard fibres.

## V

## Conclusions

The second half of the 1980s was a difficult period for agriculture in the developing countries. The deterioration of the terms of trade, the weakness of the markets for their commodity exports, the external debt burden and inflationary tensions all combined in a number of regions of the world to depress income and wages and bring down the standard of living of broad sectors of the population. These were years in which many countries asked too much of agriculture. On the one hand, it was asked to feed a growing population, and on the other it was asked to provide the resources needed for financing the debt and imports.

Although the growth rate of the value of the agricultural exports of many developing countries has been going down and, in any case, has been below the growth rate of the agricultural exports of the OECD countries and some Asian countries, in a number of cases—particularly in developing countries which do not have mineral resources—agriculture has become the main source of foreign exchange.

Whatever the outcome of the Uruguay Round, the 1990s will be a period of intensive competition on international agricultural markets. If the OECD import markets are liberalized, it may be expected that initially there will be a rise in the prices of many temperate zone products, including basic grains for human consumption. It is foreseeable, however, that in the long term prices will go down once again unless there are profound structural changes in the composition of world agricultural demand.

There is a key point which is of fundamental importance in all this: the basic problem of world agricultural trade, and the factor which severely limits its development possibilities, lies in the gulf between potential demand and the resources needed to turn that potential demand into effective demand. As long as the markets of the developing countries are not in a position to purchase the agricultural products they need to feed their growing populations, the development possibilities of world agricultural trade will always be limited.

The new markets which are opening up for renewable natural resources undoubtedly offer big opportunities for innovative countries or enter-

prises which—through new products, new transport technologies or new trade strategies—are able to incorporate themselves successfully into this trade and take advantage of unexploited market segments or niches. Regional and world experience shows, however, that with the passage of time other competing countries enter international markets, giving rise to crises of over-supply and falling prices. The industrialized countries have limited markets for new renewable primary commodities, and the cycles of expansion and saturation are currently quite short. It may therefore be very important to study these spaces and cycles when preparing national development strategies.

It would be desirable to initiate, expand or consolidate some agricultural export chains, promoting their efficiency and competitiveness by various means, provided that these options are not at variance with the essence of a growth and development strategy. Except in some very special situations, diversifying primary production for the purpose of domestic or export supply does not seem to be a sufficient basis for a long-term development strategy, no matter how promising some agricultural export chains may seem.

It is obvious that the various agricultural exporting countries must pursue agroindustrial development in order to progress to a more complex level of production and increase the diversification of their exports. Agroindustrial development also favours the internal linkages of the economy, speeds up the process of social and production modernization in rural areas, and leads to the production of goods which can readily be sold on domestic markets. Even when conceived in the broadest terms and oriented to both the domestic and the international market, however, agroindustrial development alone cannot radically change the situation of the agricultural exporting developing countries.

Latin America and the Caribbean must follow up with the greatest attention the changes which are taking shape in the world markets for agricultural products, including the evolution of the agricultural sector of the Eastern European countries and the Republics which made up the former Soviet Union; the changes in the Asian economies, which are

making decided progress towards greater food self-sufficiency and even towards the conversion of their agricultural sector into an important source of exports; the evolution of the tensions between the leading countries which export temperate-zone agricultural products, as reflected in the Uruguay Round; and the relatively rapid saturation which is taking place in the markets for new products, especially tropical and subtropical products, into which various African and Asian countries are trying to penetrate.

Consequently, processes of economic openness based mainly on incorporation into international trade through agricultural or agroindustrial products call for close and cautious attention.

In conclusion, it may be noted that, within the economic trends predominating today, greater economic openness, together with the simultaneous reduction of the regulatory capacity of the State, may be leading in some countries to the creation of new forces tending to concentrate renewable natural resources. The trend towards greater concentration could be channeled through the exchange of external debt for resources and through the transnationalization of the ownership or use of renewable resources. This phenomenon would be strengthened by the tendency to rediscover comparative advantages with regard to the enhancement of such resources by processing.

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## Evolution of the rural dimension in Latin America and the Caribbean

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This article addresses rural issues from a double perspective. First, analysis is focussed on the rural environment and its particular ways of life and sociability known as the rural dimension of a society or, generically, as *rurality*. Second, issues are addressed from an agrarian point of view, given that agriculture, in a broad sense, is the main productive and economic base of the rural sector and is, for that reason, its most essential component.

This double perspective corresponds to the objective of evaluating the leading aspects of rural society and the challenges to be faced in pursuit of greater equity, both with respect to the socio-economic situation of the various agricultural agents and the rural population as such. The essence of rurality is perceived as the active and dynamic link established between the population and natural resources.

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## I Rurality in industrial societies

Given the frequent reference made to the trajectory followed by the industrial countries, and especially the recently industrialized economies, it seems worthwhile to analyse the rural dimension of those processes, although, in view of the breadth of the topic, we will only present a brief synthesis. In addressing this issue, we are far from suggesting that the trajectory which led to the development of those countries ought to be that followed by our countries. Our only purpose is to show that their processes of economic change involved substantial participation of the rural sector, with more or less radical transformations of the traditional, pre-industrial system.

### 1. *Parallel and complementary dynamic change*

A constant element in the historical experience of old and new industrial societies continues to be parallel and complementary dynamic change in both the cities and the countryside. Although agrarian revolution preceded industrial change in some cases, close interaction between both spheres of transformation came to be the norm over time. Given that the pre-industrial scene was predominantly rural, changes in the rural-agrarian sector took place in different ways as a function of urban-industrial evolution and the conflicts occurring in that sector. The fewer the options that rural societies had for dealing with their tensions, the greater such changes were. In some cases, there were massive migrations to new lands, pushing forward the agricultural frontier; in others, new foreign lands were colonized or there were massive migrations to other continents or countries.

Among the causes of the social processes which were to affect both the urban and rural, or the industrial and agricultural dimensions, of industrial societies, special mention may be made of the following: a) the pursuit of social and political stability through the solution of the agrarian problem in broad terms, by creating improved survival options for major segments of the population through the cultivation and use of renewable resources; b) the increase of the saving capacity of rural communities and the possibility of transferring resources to promote the industrialization of urban development;

c) the simultaneous, or nearly simultaneous, increase of savings, investment and productivity in the urban-industrial and rural-agricultural sectors; d) the recognition of the future importance of natural resources (especially renewable resources) and of the urban-industrial contribution, given that the foundational bases and growth profiles of industrial growth have had as their implicit or explicit points of reference the basic supply of primary resources; e) the recognition that there is a functional correlation between advances in urbanization and industrialization and gradual de-ruralization; f) the channelling of population movements towards a more functional distribution of the population in line with the progressive demand for labour generated by urban-industrial growth, the possibility of cultivating new rural lands, and the options provided by migration to other countries or continents.

The social processes involved offered a broad spectrum of alternatives, from strong social mobilization combined with changes in the political system to planned interventions in very particular conditions, as in the cases of Japan, Korea and Taiwan.

## 2. Definitions with respect to rurality

The transition from rural to industrial society called for a number of definitions with respect to rurality, that is, with respect to the ratio of population to renewable resources. Before and during the formation of industrial society, there was a thorough reshaping of the traditional agrarian order with the aim of resettling the rural population within its own environment. Seen *ex post*, the rural environment became, to a large extent, the ante-chamber of industrialization in the countries which undertook that task, and this explains why they made their agrarian systems more equitable, as a means of achieving more stable and less conflictive occupation of the land and, in addition, as a means of freeing resources to make industrialization itself more viable. This does not mean that agrarian change has obviated population pressures in the industrializing cities, nor significant migratory movements. However, these phenomena tended to improve the situation of the rural population, as migrations made room for the emergence of new land owners and slightly larger land holdings.

In the initial stage of the industrialization process, the countries which are now industrialized went through certain common experiences, such as the

tendency to do away with feudal forms of land and labour exploitation and to secure more uniform resource distribution on the basis of the direct ownership and cultivation of such resources. If modernity is understood as the cultural and social change accompanying industrialization, it may be asserted that one of its first consequences in the rural areas of countries which are now industrialized was greater equality in the agrarian systems. Modernity and the often contradictory tendency toward equality and equity were seen to be related. Generally, in those countries the process of agrarian change took place when society was still predominantly rural. The weight of the rural population within the economic and social order and in the contribution to the industrialization process was noteworthy, as was its participation in the overall socio-political process, in which agricultural change was closely involved, since it formed part of a larger process of change.

To summarize all this in extremely simplified terms, it may be said that a first wave of change swept through the countries of Western Europe toward the end of the eighteenth century and continued in the nineteenth century, becoming more intense and definitive in its later stages. Early in the present century, those processes extended to Eastern Europe, including Russia (1905). In Japan, agrarian change began before the Second World War and was consolidated after that war. In Taiwan, the creation of egalitarian ownership structures took place in the 1940s. In Korea, it began with the withdrawal of the Japanese and was consolidated in the 1950s. In the southern parts of some European countries (Spain, Italy, Yugoslavia), the last vestiges of the traditional ownership structures were swept away by the agrarian reforms or processes of land parcelling implemented after the Second World War.

In the smaller and more densely populated European countries, agrarian structures were in line with very small-scale patterns, as for example in Belgium, where, in 1860, 84% of all holdings had an area of less than three hectares, and 65% were less than one hectare. In the Netherlands, around 1880, the area of agricultural holdings averaged less than 1.2 hectares. After the 1949 reforms in Korea, the amount of cultivated land per family was around 1.2 hectares, with a maximum limit of three hectares per family. In 1955, in Japan, the average size of agricultural holdings was one hectare, and they were all directly

operated by the families that owned them. After the 1952 reforms in Taiwan, peasant families held an average of 1.1 hectares, likewise farmed directly. A noteworthy feature of the history of the development of these Asian countries is the radical agricultural changes which they carried out and which allowed them to increase agricultural production and reduce dependence on foreign suppliers, in order to embark on their industrialization.

### 3. *Effects of agrarian change on rural trajectories*

The most noteworthy of the various effects of agrarian change was the maintenance of rural populations on the land and in their traditional localities thanks to private ownership of the resources. Secondly, there was the expansion and consolidation of a stratum of independent farmers who owned their land and, for the most part, worked it directly. Thirdly, these farmers retained more of their income, with increased savings, investment and productivity. Finally, urbanization and industrialization, by broadening the markets for agricultural products, tended to give rise to increasing commercialism and monetization of the rural economy, as this became a growing market for urban-industrial products and services. From the point of view of social stratification, industrialization led to the formation of independent producers, associated on a basis of solidarity for various purposes, who were both owners of land and co-owners of capital and equipment. Cooperation was essential for agricultural and rural progress, as well as for social articulation with industry. Parallel to these processes, the number of landless farm workers or rural proletariat gradually declined. In addition to their economic objectives, the rural and agrarian adjustments which accompanied the industrialization process gave rise to greater social stability, by making withdrawal from rural areas more gradual, while they fostered greater political stability, by satisfying the basic demands of the rural population.<sup>1</sup>

The emergence of independent socio-economic actors (merchants, artisans, farmers, etc.) following the collapse of the feudal system created a climate of

strong independence in the social sphere and, sometimes, in political matters too, compared with the traditional systems, which were very closed and rather decentralized. The result was vigorous development of the basic political units at the territorial level, such as communes with their corresponding municipalities and local organizations and institutions. In many cases, participation was greater at the local level than in other spheres, and democratizing processes arose, or were allowed to arise, more at that level than at other, broader levels.<sup>2</sup>

National processes of adjustment in the agrarian structure gave rise to land units of relatively similar scale, the size of which depended both on the availability of arable land, pasturage and forests, and on population pressures. Territorial dimensions such as the abundance and fertility of renewable resources conditioned not only the achievement of a relatively steady urban-rural dynamic balance, but also the definition of options in the areas of industrialization, foreign trade and development in general.<sup>3</sup> In the course of their economic and social evolution, the industrialized countries also established various mechanisms, regulations and policies for inducing adjustments, either automatic or guided by public institutions, aimed at generating a rural dynamic more or less functional for urban-industrial growth.<sup>4</sup> The magnitude of the results of these agrarian adjustments has led, in turn, to the creation of endogenous

<sup>2</sup> In the European countries, the early "municipalization" of society, with the municipality as the basic nucleus of local government during a period of high rurality, was maintained until recently, when the urbanization process made restructuring necessary. In Federal Germany, there were 24 513 municipalities in 1950, reduced to 8 594 by 1970. In France, there were 37 000 municipalities in 1970 (of which 24 000 had less than 500 inhabitants), but these had gone down to 36 500 by 1985, in a process which has continued since that time.

<sup>3</sup> This relationship is seen most clearly in the cases of Korea, Japan, Taiwan, etc.

<sup>4</sup> Laws have been adopted giving heirs or immediate neighbours preferential rights to purchase land; rental contracts have been regulated, giving preference to tenants in the event of land sales; maximum limits have been set for the accumulation of renewable resources; lines of credit for land purchase have been created; policies for retaining population in upland agricultural areas have been established; and subsidies have been provided for land improvement, irrigation or reforestation. In other cases, tax policy has promoted relatively homogeneous agrarian structures, through the application of progressive land taxes. In this way, certain automatic adjustments have been achieved, accompanied by slow increases in the scale of production and the abandonment of marginal land.

<sup>1</sup> In the countries which now make up the European Economic Community, around 36% of their population lived in rural areas in 1970.

technology, with a variable capital structure, as well as the development of the agricultural inputs industry. This has resulted in significant differences between the technological and productive systems of the countries which are now industrialized. The most marked contrasts have been between the United States and Canada and Japan and South East Asia. In those countries which were successful in their industrialization, the agrarian structure has made possible endogenous technological models adapted to the demographic processes and the availability of renewable resources, as well as solid linkages between agriculture and industry.

These new agrarian systems, which allowed for greater autonomy, initiative and equality among the productive agents, were fertile ground for various forms of associative processes (associations for savings, credit, technification, construction of infrastructure, trade and industrialization), thus providing favourable conditions for the formation of strong cooperative and guild (trade union) systems. Through those intermediate-level organizations, more coherent economic linkages were achieved between agriculture and the rural, industrial and urban economies in general. These associative processes were possible because there was a horizontal relation among peers which made it possible to achieve economies of scale, while sharing costs and benefits.<sup>5</sup>

Agricultural expansion and increased production were achieved through the economic agents which were already present in rural areas, with their resources, experience and culture, organizations, institutions, initiative and capacity for innovation. In Europe, it was difficult, and still is to a degree, for a non-farmer to gain access to arable land, because everything has been oriented toward the consolidation of the farmers themselves, through regulations giving them preferential treatment with regard to

<sup>5</sup> In European countries, a high percentage of the harvest is sold through cooperatives (in Ireland, 97%; in the Netherlands, 86%; in Federal Germany, 65%; in France, 50%; in Belgium, 65%; in Italy, 32%; and in Spain, 10%). In the case of fruit, 90% is sold through cooperatives in Denmark; 70% in Belgium; 65% in Federal Germany; 82% in the Netherlands; 45% in France and Greece; 31% in Italy; 26% in Spain, and 25.8% in the United Kingdom. Many more examples could be given for other products and other countries, such as Japan and Korea. The relatively low levels of cooperation in Spain and other Southern European countries have given rise to some interesting reflections, applicable in some aspects to Latin America.

land, credit and markets. This agrarian base was complemented with scientific and technological facilities providing ever-increasing potential for increasing productivity and efficiency. Something similar occurred in the financial, commercial and industrial fields.

The most notably dynamic processes of industrialization have occurred in societies where the agricultural sector has made major advances in productivity. Historically, there has been a certain correlation between the per capita agricultural product and the corresponding manufacturing product. This is particularly evident in four countries which were colonized relatively recently (from an historical point of view): i.e., the United States, Canada, Australia and New Zealand. However, the same correlation also applies in societies with fewer resources and older cultures, which have followed parallel paths in the improvement of agricultural productivity and industrialization. In contrast, the experience of the Soviet Union or the Balkan countries suggests that agricultural lags have made their industrialization more difficult. This correlation derives from the macroeconomic function of agriculture in the initial stage of industrialization and the ever-increasing contribution of industry to increased agricultural productivity. In many countries, the size of the industrial sector depends directly on agricultural productivity, as do the type and nature of the industrialization process (the Scandinavian countries).

If agriculture manages to produce sufficient food for a growing urban-industrial population and raw materials for industry as well, the latter sector can grow and rural areas can become markets for consumer goods produced by industry and for farm inputs (Fonquín *et al*, 1991). The more efficient agriculture becomes, the greater its potential for correlation with industry will be and the greater the opportunities for creating dynamic intra-industry linkages (Senghaas, 1985).

In the formation and progressive expansion of agricultural product markets, producer organizations, the creation of agro-industries, the establishment of "certified origin" of products, and the enhancement of local quality have contributed to stable linkages offering improved investment prospects and greater market security for a substantial proportion of products, many of which are sold under futures contracts.

Diversity of innovative capacity has been a general phenomenon, but nevertheless innovations spread rapidly in the agricultural sector, without prolonged periods of unequal production levels, either because technological change was socialized through economic and social organizations, or because technological supply was ample and well adapted to the existing scales of production.

The functionality between the rural and the urban-industrial sectors has had more or less common foundations in currently industrialized countries: ownership of natural resources; relatively egalitarian resource distribution; assignment of priority to family-based agricultural units; technological development and its deliberate adaptation to the structural evolution process; strong promotion of organization through educational and financial stimuli; promotion of associative trade and industrialization (at least in the early stages); professional and technical training; training in business management; construction of local infrastructure; broad powers of local administration; municipal responsibility for control of renewable resource use (forests, water supplies, fauna, hunting, etc.) and, in many cases, municipal ownership of shared resources (forests, pasture land, etc.).

The linking-up of the rural economy, and especially of the agricultural economy, with other sectors such as services and the agricultural inputs industry or with industries which process agricultural produce was close-knit and progressive. Moreover, it took place through associated and simultaneous processes, with their own profiles in each country according to the availability of renewable resources, the agrarian structure, the availability of labour, and the advance of technology. Greater uniformity in agricultural scales of production also means more homogeneous technologies, which in turn results in homogeneous demand for capital goods. This makes it possible to link up the production of consumer and capital goods—one of the most important linkages for development—which is also one of the bases of industrial competitive capacity.

In the search for rural-urban equilibrium, the industrial economies have, in differing circumstances, tended to protect their farmers and their agricultural

sectors in order to keep a significant percentage of the population on the land.<sup>6</sup>

In order to maintain a rural stratum compatible with the settled areas of the territory, with the conservation of the environment, the defence of the cultural heritage, and a degree of social equilibrium, there has been a tendency to guarantee the average rural income at levels similar to urban incomes, while the quality of life has also been made similar to that of the urban population, at least in basic aspects. These protective measures reflect the social recognition of the positive externalities arising from the stability of rural societies, which they are unable to secure by themselves. In 1988, according to the Secretariat of the Organization for Economic Co-operation and Development (OECD), agricultural subsidies cost its 18 member countries around US\$270 billion (OECD, 1989): a figure very similar to the total value of world agro-foodstuffs trade for that same year. In the process of industrialization, together with the initial cost of freeing farm labourers from serfdom in order to form free and dynamic economic agents in the rural sector, industrial societies were obliged to pay a later, additional cost in order to compensate the rural population for remaining on the land. To that end, the agricultural economy has been protected or resources have been transferred to improve the quality of life in that sector. These societies have paid high costs for the creation of living conditions and incomes capable of keeping a certain proportion of the population on the land for cultural, environmental, geographic and economic reasons.

<sup>6</sup> Europe passed through this phase at the end of the last century, as new agricultural exporters emerged (Argentina, New Zealand, Uruguay); and it repeated the process after the Second World War in respect of the United States and the countries already mentioned. The exception was Imperial Great Britain. The processes of proletarianization and accelerated migration in Europe at the end of the last century gave rise to protectionism. In recently industrialized economies, protectionism is even greater than in Europe.

## II

### Rurality in the region

Historically, in Latin America and the Caribbean, the patronal system –noted by Tannembaum as the most important structure of those societies– has been of enormous social, economic and cultural significance. Except in two or three cases, neither social revolutions nor agrarian reforms have weakened its dynamism. The transition from that system has been more a continuance than a break with the past, since the system has strengthened its productive structures through technological progress. If rurality is understood as the active and dynamic link between the population and renewable resources, as defined above, both ethnic groups and indigenous peoples, as well as the rural population in general, have historically faced difficulties in retaining or gaining access to land. In Latin America and the Caribbean, the rural population either has no land or possesses very little. We have named this phenomenon precarious rurality, since the precarious link between the rural population and the land is one of the principal characteristics of the agrarian trajectory of the region.

The lack of appreciation for that population's productive functions, its capacity to generate employment, its rootedness in the land, and its importance as a producer of basic foodstuffs and reproducer of rural culture and the work ethic proper to peasants, have hindered the progress of peasant agriculture. The leading role played by landowners and entrepreneurs has overshadowed the economic, social and cultural potential of the peasant sector, while public strategies have failed to keep open lasting and serious options for the universe of peasant economies.

The new entrepreneurial structures being established in the rural medium have introduced salaried farm labour. The better qualified workers have managed to gain an organic and stable place in those business structures, as has occurred in other social sectors. However, the vast majority of wage workers obtain only very sporadic and unstable jobs, with long periods of unemployment in between. The creation of rural labour markets for seasonal tasks which require abundant labour attracts the urban unemployed population, making rural worker organizations even more vulnerable and collective

negotiation practically impossible. The rural proletariat or owners of dwarf holdings who participate in those markets face serious difficulties when they attempt to achieve more organic insertion in the world of work.

#### 1. Rurality from the demographic standpoint

If a demographic criterion is used in estimating the rural dimension of Latin America and the Caribbean as a whole, the region is seen as one of low rurality, since only 27.9% of its population currently lives on the land (1990). In comparative terms, Asia and Africa have very high levels of rurality (69.7% and 64.5%, respectively). From this standpoint, the region has reached a preeminently urban state, with 72.1% of its population living in cities. In this sense, its level of urbanization is nearer to that of the European countries (82.8%), although qualitatively there can be no comparison.

Considering overall rural population trends at the regional level, it may be said that a relatively stable situation is being achieved, since average annual growth of that population has been only 0.4% over the last ten years. However, as many regional indicators obscure the concrete reality of each country, it must be noted that there are countries with very different levels of rurality in the region. For analytical purposes, four categories have been identified: high (more than 50% of the population is rural); middle-level (between 30% and 50% rural); low (between 15% and 30%); and very low (less than 15%). Application of these categories to the data for 1990 reveals that there are: a) ten countries with high rurality, accounting for 10% of the total population of Latin America and the Caribbean; b) four countries with middle-level rurality, with only 5.2% of the total population; c) five countries with low rurality, representing 69.3% of the total population of the region; and d) four countries with very low rurality, with 15.5% of the total (table 1).

Among the countries with the most rapid rates of de-ruralization in relative terms is Brazil, which was 65.5% rural in 1950, but only 23.1% rural in 1990. In 1950, no Latin American country qualified for the category of very low rurality, but in

1990 four countries already had rural populations lower than 15%. In that same year, five countries accounting for 69.3% of the total Latin American and Caribbean population were in the category of low rurality (less than 30% rural).

To sum up, in 1990 nine countries (85% of the Latin American population) were in a situation of low or very low rurality, and the rural population fell in absolute terms. The countries with low rurality

(Brazil, Colombia, Mexico and Peru) experienced processes of absolute de-ruralization, at an average annual rate of -0.5%, in the 1980s; in the countries with very low rurality, the average annual rate was -0.7% for the same period (tables 2 and 3).

Although the rural population still registers small increments in absolute terms, it has dropped in relative terms, given that it has fallen from 58.9% of the regional total in 1950 to 27.9% in 1990.

Table 1

**LATIN AMERICA AND THE CARIBBEAN: RELATIVE WEIGHT OF DIFFERENT CATEGORIES OF COUNTRIES, BY DEGREE OF RURALITY, IN TOTAL REGIONAL POPULATION, 1950-1990**

(Percentages)

Categories of countries:	1950	1960	1970	1980	1990
<b>Total population</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>
High rurality <sup>a</sup>	9.9	9.7	9.6	9.6	10.0
Middle-level rurality <sup>b</sup>	4.9	4.9	5.0	5.1	5.2
Low rurality or rapid urbanization <sup>c</sup>	66.3	67.4	68.7	69.2	69.3
Very low rurality or traditionally urban <sup>d</sup>	18.9	18.0	16.7	16.1	15.5

Source: Prepared by the ECLAC Agriculture Division, on the basis of data from CELADE (Latin American Demographic Centre).

<sup>a</sup> (More than 50% rural population): Barbados, Bolivia, Costa Rica, El Salvador, Guatemala, Haiti, Honduras, Paraguay, Suriname and Trinidad and Tobago.

<sup>b</sup> (Between 30% and 50% rural): Dominican Republic, Ecuador, Jamaica, Panama.

<sup>c</sup> (Between 15% and 30% rural): Brazil, Colombia, Cuba, Mexico, Peru.

<sup>d</sup> (Less than 15% rural): Argentina, Chile, Uruguay, Venezuela.

Table 2

**LATIN AMERICA AND THE CARIBBEAN: EVOLUTION OF RURALITY BY CATEGORIES OF COUNTRIES, 1950-1990**

(Percentages of total population)

Countries with:	1950	1960	1970	1980	1990
High rurality <sup>a</sup>	72.0	69.3	66.5	63.2	57.8
Middle-level rurality <sup>a</sup>	72.5	66.3	59.1	52.3	45.0
Low rurality or rapid urbanization <sup>a</sup>	62.2	52.6	42.6	33.3	25.6
Very low rurality or traditionally urban <sup>a</sup>	37.1	28.5	22.5	17.4	13.6
Total Latin American and Caribbean rurality	58.9	50.5	42.5	34.5	27.9
<b>Total Latin American and Caribbean population</b>	<b>161 256 000</b>	<b>212 733 000</b>	<b>279 148 000</b>	<b>355 054 000</b>	<b>438 924 000</b>

Source: Prepared by the ECLAC Agriculture Division, on the basis of CELADE data.

<sup>a</sup> See notes of table 1.

It is well known that the processes of growth and industrialization are accompanied by the de-ruralization of societies. As agricultural and overall productivity rises, fewer and fewer people are needed for primary agricultural activities (table 4). Countries with very low rurality, including those of Latin America, have higher per capita income levels. However, a special feature of the Latin American and Caribbean rural trajectory is the early de-ruralization of the societies, without adequate corresponding economic growth, nor levels of productivity which would justify rapid urbanization, nor an extreme scarcity of renewable resources.

Table 3

**LATIN AMERICA AND THE CARIBBEAN:  
RURAL POPULATION GROWTH BY  
CATEGORIES OF COUNTRIES,  
1950-1960 TO 1980-1990**

(Average annual growth rates)

Countries with:	1950-1960	1960-1970	1970-1980	1980-1990
High rurality <sup>a</sup>	2.2	2.2	2.0	1.6
Middle-level rurality <sup>a</sup>	1.8	1.7	1.4	0.8
Low rurality or rapid urbanization <sup>a</sup>	1.3	0.9	-0.1	-0.5
Very low rurality or traditionally urban <sup>a</sup>	-0.4	-0.3	-0.6	-0.7
<b>Total</b>	<b>0.8</b>	<b>0.6</b>	<b>0.4</b>	<b>0.4</b>

Source: Prepared by the ECLAC Agriculture Division, on the basis of CELADE data.

<sup>a</sup> See notes of table 1.

Table 4

**RURALITY AND PER CAPITA INCOME BY  
CATEGORIES OF COUNTRIES, 1990**

(Percentages and 1980 dollars)

Countries with:	Rural population	Per capita income
High rurality <sup>a</sup>	57.8	820
Middle-level rurality <sup>a</sup>	45.0	1 273
Low rurality <sup>a</sup>	25.6	1 889
Very low rurality <sup>a</sup>	13.6	2 625

Source: Prepared by the ECLAC Agriculture Division, on the basis of CELADE data.

<sup>a</sup> See notes of table 1.

**2. Rurality and renewable resources**

Latin America and the Caribbean are in a relatively advantageous position in comparison with other continents, in terms of the availability of arable land, pasture land and forests (table 5).

With regard to the area occupied by renewable resources, the region is in a better position than Asia and Africa, and even Europe. It is only surpassed by the vast areas of the Community of Independent States (ex USSR), Oceania, and North America (Canada and the United States). Analysis of resource endowment in terms of the categories of rurality defined above reveals the region's great potential for very diverse agricultural activities (table 6).

Table 5

**AVAILABILITY OF LAND IN MAJOR  
GEOGRAPHICAL AREAS, 1989-1990**

(Hectares per person)

Geographical areas	Arable land	Pasture land	Forests
Asia	0.14	0.22	0.17
Africa	0.29	1.26	1.08
Europe	0.28	0.16	0.31
Latin America	0.41	1.30	2.18
Community of Independent States (ex USSR)	0.80	1.28	3.27
North America	0.86	1.00	2.26
Oceania	1.86	16.85	5.99

Source: Prepared by the ECLAC Agriculture Division, on the basis of FAO, *Production Yearbook*, Rome, 1989 and 1990.

Table 6

**LATIN AMERICA AND THE CARIBBEAN:  
AVAILABILITY OF LAND BY LEVELS  
OF RURALITY, 1989-1990**

(Percentages and hectares per person)

Countries with:	Rural-ity	Arable land	Pasture land	Forests
High rurality <sup>a</sup>	57.8	0.28	1.31	2.61
Middle-level rurality <sup>a</sup>	45.0	0.23	0.39	0.73
Low rurality <sup>a</sup>	25.6	0.39	1.05	2.43
Very low rurality <sup>a</sup>	13.6	0.67	2.78	1.48
<b>Latin America, total</b>	<b>27.9</b>	<b>0.41</b>	<b>1.30</b>	<b>2.18</b>

Source: Prepared by the ECLAC Agriculture Division, on the basis of CELADE data.

<sup>a</sup> See notes of table 1.

Generally speaking, countries with high rurality have little available per capita arable land and pasturage, in contrast to the situation in countries with low and very low rurality, where those lands are considerably more abundant. Hypothetically, it could be asserted that the latter countries have achieved higher levels of urbanization and industrialization thanks to their more adequate agricultural foundations. Moreover, countries with high and middle-level rurality, because of their greater difficulties in promoting development of their agriculture, have remained more rural because of their initial difficulties in attempting to diversify production.

Latin America and the Caribbean have displayed little ability to integrate their renewable natural resources into industrialization strategies in a balanced manner: that is to say, by inculcating into society as a whole an attitude toward the rural sector which would tend to create the necessary conditions for the introduction of technologies and the broad linking-up of that sector with the other economic, social and political sectors. The relative abundance of renewable natural resources was not converted effectively into that retention of rural population on the land which could have been expected. The preservation of land ownership has been weak in comparison with that achieved in industrial societies at a similar level of development. The relative abundance of the region's renewable natural resources, in comparison with those of the industrial countries, taking into account the populations of the respective countries (table 5), was sufficiently greater and more appropriate to have served to bring about greater intra-rural equilibrium, if structural adjustments had been undertaken to make resource distribution more equitable.

A particular feature of the region is the *progressive expansion of the agricultural frontier*. In four decades (1950-1990), more than 200 million hectares have been incorporated into agriculture: an area approximately the same as the arable land of Western Europe. This phenomenon is perhaps the best indicator for appreciating the demand for land which still exists in rural areas of the region. Up to the 1970s, the weight of that expansion in the increase of agricultural production (60% of growth is explained in this way) was greater than that of technological change and increased productivity—a situation which was reversed only in the 1980s.

Such expansion provoked serious deterioration of renewable resources, together with the expulsion or deterioration of indigenous communities, and it

has given peasants and other social categories only limited access to land resources. The new agrarian structures have reproduced in the new areas the profound heterogeneity characterizing traditional agriculture.

### 3. Intra-rural disequilibria

One of the most serious difficulties faced by Latin American and Caribbean society is that of intra-rural disequilibria and, as a direct or indirect consequence, imbalance between urban and rural growth rates. This is a long-standing phenomenon noted repeatedly in analyses of agrarian conditions in the countries of the region. The rural trajectory of Latin America and the Caribbean displays serious imbalances in the relation of the population to renewable natural resources.

The basic parameter of every agrarian structure is land allocation and, in the region, this is marked by sharp inequities. If indexes of the concentration of land ownership in Latin America and the Caribbean are compared with those found in Asia and the Pacific, a strong bias toward concentration, typical of the ownership structures of the region, is noted (table 7).

The persistent tendency to reproduce inequitable patterns of land distribution and of access to that resource has led to the proliferation of dwarf holdings. In Brazil, for example, over the last 45 years the number of agricultural units of less than one hectare has grown 16 times; those of from one to ten hectares, four times; while those of more than 50 hectares have doubled. The dwarf holding is an endemic characteristic of Latin American agriculture. For the foregoing reasons, the rural population is mainly made up of landless peasants or those with very little land (table 8).

A special feature of Latin America, even more than its urban-rural duality, is its unshakable intra-rural duality, which was not corrected at the proper time and now marks the whole of society. Duality in the economy—a modern sector and another traditional sector—is part of the process of social change to industrialization. In Latin America and the Caribbean, however, agrarian heterogeneity tends to become more pronounced with industrialization, contrary to what has occurred in the industrialized countries, where technological progress and economic and social demands led to the creation of more equitable agro-rural structures.

Table 7

**INDEXES OF LAND OWNERSHIP  
CONCENTRATION, 1970-1971**

Range of Gini coefficient	Developed countries <sup>a</sup>	Asia and the Pacific	Latin America
0.80 or more	1	1	10
0.70-0.79	5	-	5
0.60-0.69	2	3	1
0.50-0.59	4	4	1
0.40-0.49	6	-	0
Less than 0.40	2	1	0
<b>Total</b>	<b>20</b>	<b>9</b>	<b>17</b>

Source: Estimates of the FAO Statistics Division, based on agricultural censuses.

<sup>a</sup> Excluding the centrally planned economies.

Table 8

**LATIN AMERICA AND THE CARIBBEAN:  
ESTIMATE OF LANDLESS OR NEARLY  
LANDLESS PEASANT FAMILIES  
IN SELECTED COUNTRIES**

Countries	Percentage of all rural families
Bolivia	85
Brazil	70
Colombia	66
Costa Rica	55
Ecuador	75
El Salvador	80
Guatemala	85
Mexico	60
Peru	75
Dominican Republic	68

Source: E. J. Easman, *Landlessness and Near-landlessness in Developing Countries*, Cornell Rural Development Committee, Ithaca, 1978, cited in R. Sinha, *La condición del campesino sin tierras: un problema que se agrava*, FAO, Rome, 1984.

The large scale of the agricultural units of the region hindered the more extensive and prolonged settlement of the population on the land, leaving the majority crowded onto small plots of low fertility. The distribution of renewable natural resources has not changed significantly, even in those countries in which there has been an enormous expansion of the agricultural frontier, such as Brazil (table 9).

The region has not addressed the issue of intra-rural disequilibria in depth. Efforts made since the 1950s, that is, once the process of import substitution

industrialization was under way, were tardy and limited in scope. That delay has had serious consequences for both economic and social development and for political stability in Latin America and the Caribbean.

Public interventions, such as agrarian reform or the settling of new lands, have not managed to alter the agrarian heterogeneity of the region (Sinha, 1984). There are several reasons for this. Perhaps it was not appreciated that agrarian change could make a decisive contribution to the process of industrialization, if the inactive resources of the landowners were used to form industrial companies. In this sense, the low indemnities established by agrarian reform legislation were more like a penalty than an incentive to relocate resources in industry. Moreover, reforms were undertaken when processes of capitalization, technological innovation and agricultural modernization were already under way in patronal economies and there were already many instances of increased efficiency and high levels of productivity. This sparked off a long controversy over the agrarian and rural options available to the region in the future. One of the results of this controversy was the complicated juridical system of the agrarian reform processes, which, because of its complexity, often made it possible to circumvent reform efforts by exploiting loopholes in the laws and regulations.

Table 9

**BRAZIL: EVOLUTION OF LAND  
CONCENTRATION MEASURED  
BY THE GINI COEFFICIENT  
FOR MAJOR REGIONS,  
1960-1985**

Regions	1960	1970	1975	1980	1985
North	0.944	0.839	0.868	0.835	0.800
Northeast	0.846	0.855	0.863	0.862	0.870
Southeast	0.771	0.761	0.762	0.771	0.774
South	0.727	0.727	0.735	0.745	0.753
Centre-West	0.845	0.856	0.856	0.845	0.841
Whole of Brazil	0.842	0.844	0.855	0.857	0.858

Source: R. Hoffman, "Evolução da desigualdade na distribuição da Posse da terra no Brasil no período 1960/1980", *Reforma Agraria*, Nº 12, 1987.

Comparative analysis of the stages at which industrialized countries undertook agrarian change in function of industrialization reveals that, in Latin America and the Caribbean, the few attempts made

were tardy and the role of the rural population in macro-social equilibrium was not taken into account. Because of this, the agrarian experience of the region is very different from that of the industrialized countries in its basic socio-economic elements. Agrarian policies (settlement of new land, agrarian reform, rental and sharecropping regulations, sale of public land, protection of land controlled by indigenous peoples) managed to shake the large-scale patronal agrarian structures only in a few cases and, indirectly, accelerated their productive change, but they never managed to create a mature and socially important peasant-farmer. Reform processes had wider-ranging effects than the direct redistribution of land ownership, because the patronal system tended to change more quickly, while public strategies stimulated that change. Peasants, in general, did not have access to land ownership and did not become independent farmers on a large scale, as occurred on other continents. Nor was the formation of a landed peasant class energetically promoted through administrative channels, such as the sale of public land or other public policy mechanisms, such as public investment in irrigation. Indeed, some public subsidies for forestry activities directly or indirectly encouraged the massive concentration of resource ownership.

Rural families have had only limited access to land through the natural resource market, due to its imperfections. Since they have had to finance land purchases themselves, in the absence of special credit mechanisms for that purpose, it has been very difficult for them to become landowners. In the experience of the region, when renewable resource market restrictions have been lifted and all limitations on land purchases have been eliminated, not only has land become even more inaccessible for rural families but the market has led to the concentration of resource ownership, to the detriment of the continued presence of peasant families on the land. The large-scale land purchases observed in recent years are creating pressures on land availability which limit peasant access to that resource even more seriously and provoke a massive exodus to mid-sized and large cities or the formation of extremely precarious human settlements.

In frontier agricultural areas, after rural families clear the land and prepare it for cultivation, local land markets are created and many of the colonizing families are displaced from the land. Even so, however, the opening of new lands for agriculture has

given peasants much greater access to land than the agrarian reform processes (Ortega, 1986).

Something unheard of in other continents is occurring in rural Latin America. The land is increasingly coming into the possession of persons who live in the cities or domestic or foreign companies, while, even more uniquely, agricultural workers also tend to live in the cities in ever increasing numbers. As the urban-based landowners close off access to land, making it impossible for peasants to work and live on their own land, and as moreover rural dwellers do not have access to the basic elements of modernity, such as electricity and other services, they opt for moving to the cities.

The regional agrarian model has forced peasants to emigrate to the cities (something incomprehensible to Europeans and Asians), and when they do not find employment there, some of them return to look for casual or part-time work in rural areas.

#### 4. *The evolution of agrarian strategies*

According to some analysts, the marked inequality in economic and social stratification has been sustained by primary commodity export economies which hindered or blocked not only agrarian change but also the desire and will to undertake the process of industrialization. This situation was, in large part, a consequence of the fact that certain social strata were allowed to attain both high levels of consumption, similar to those of developed countries, and also a position where they financed fiscal expenditures to some degree, thus becoming in one way or another one of the mainstays of the State apparatus.

One of the decisive factors in the persistence and rigidity of the rural trajectory seems to have been the historical insertion of the regional economies in markets centered on the exportation of renewable resources (and also non-renewable resources, such as energy and mineral resources).

The best option for entering the market and obtaining high profits, for the *plantation* and the *ranch* and, to a certain degree, the *hacienda*, lay in the production of exportable goods. For this reason, each expansionary cycle of the economy based on renewable resources such as sugar, tobacco, coffee, cotton, cocoa, bananas, wheat, meat, soy beans, and other crops, strengthened the large-scale patronal system of production. That type of international insertion seems to have been a strong contributory factor to the very rigid control of renewable resources

exercised by a few minority social groups, for those who were coffee, cocoa, sugar, banana, grape, fruit, or lumber producers belonged not only to a productive category but also to a social group.

When the economy remains undiversified and progress in industrialization is not achieved, not only are agriculture and rural areas impregnated with the special features of the predominant agrarian structures, but society as a whole reflects those traits in the economic, social and political spheres. Given the region's long and persistent insertion into the international market through the exportation of agricultural products, the control of land and farm labour became the basis not only for private and public income but also for economic, social and political organization. This is why the agrarian order has been so important in society as a whole, and so untouchable as well.

As Latin America embarked upon the process of industrialization and technological progress, it had to confront the patronal agrarian order to which the "patina of the centuries had given special rights and legitimacy". The power of the patronal system came not only from ownership of the land, from the type of markets available, or from its prestige, but also from the "weight of the past", that is to say, the leading role it had played in the past. At the same time, however, in contrast with the feudal system, the patronal system has been more flexible due to its more extensive connections with its markets, especially the export markets, which have made it more sensitive and permeable to commercial and technological trends. This characteristic is clearly observable in the *plantation*, but also in the cases of the *ranch* and certain types of *hacienda* too. In many areas of agriculture, this connection with foreign and sometimes domestic markets has made necessary elementary vertical integration or some degree of articulation with industrial or packing activities, sometimes of a traditional nature, but always requiring certain levels of capital and equipment. This has been the case in the production of sugar cane, cotton, cocoa, coffee, yerba mate, grapes, and cattle and sheep-rearing, among others.

A key element in the Latin American rural trajectory has been the fact that the landowners were also producers. Under the feudal system, for centuries the overlords gave much of their land to the peasants for them to cultivate, obtaining in return income and services. In the region, however, the vast majority of landowners were also producers who ran their own agricultural activities, although because of

scarcity of labour or for other reasons they gave part of their land under rental or sharecropping agreements.

This relative flexibility of the landowners in their relations with the markets, together with their close links with the State, made possible this transition—so typical of the rural trajectory of Latin America—consisting of the conversion of the patronal system into much more economically efficient forms of behaviour, increasingly similar to entrepreneurial production structures, that is to say, organized as a function of production and profits. That kind of large-scale change in production patterns, accompanied by the incorporation of technology and capital and the use of wage labour, has become a very particular feature of the trajectory under analysis here.

Over time, a new order has been gaining legitimacy, based on economic efficiency and corporative and associative action by landowners, directed by the landowners themselves and enabling them to face up to both the reform efforts to redistribute land among peasants and the various social movements, sometimes accompanied by violence. For decades past, the traditional social agrarian order has been going through its own process of adjustment, maintaining control of the land, with significant public support, in the form of trade strategies which, while not always guaranteeing product prices, nevertheless compensated landowners through commitments to low wages, relatively low taxes, mortgages often not adjusted for inflation, or soft loans, and various forms of direct or indirect public transfers granted to the landowning class. In difficult times, the State intervened in order to safeguard patronal agrarian structures. Thus, veritable ideologies have arisen with respect to agriculture, its strategic importance, its weight in the balance of trade and generation of foreign exchange, and even its role in maintaining employment and the social order. "Agriculture" came to be equated, in some contexts, to "farmers and stockbreeders", on the clear understanding that they formed, and continue to form, a particular social group.

##### 5. Changing production patterns and rurality

This historical and ideological basis of the Latin American rural trajectory left little room for the conservation of the resources or land occupied by gathering or farming ethnic groups or independent family farmers cultivating their own land. A central

question, beyond the recognition of this social fact, is the identification of the causes or factors which impeded or hindered the formation of a peasant stratum which, over time, would have been made up of direct cultivators of the land, as occurred in practically all of the countries now industrialized. One of the most decisive factors in this respect is the fact that the large-scale patronal units were not broken up but instead became agro-businesses and achieved a modern form of consolidation.

In this transition towards modern agricultural businesses, sometimes smaller in size but of greater economic weight, a demand for qualified labour has arisen. From the higher management levels, the main function of which was to oversee labour (a key factor in that productive system), there was progress towards the formation of a technical and administrative class, capable of operating with new capital in its diverse technological forms. This new class has a sphere of action that goes beyond the physical limits of the productive unit, since it involves relations with the technical, commercial, financial, industrial and service centres related to agricultural activities and is responsible for the interchanges with those centres. This new, emergent agrarian order, based on new technological structures, has also required the collaboration of a new class of agricultural worker whose function is to execute specialized tasks requiring training in the use of machinery and equipment, biological and chemical products, and feed concentrates and which must have the necessary knowledge to operate specific technological packages. These specialized agricultural workers are the social counterpart of modern production systems, and this gives them a certain amount of negotiating power. According to some of the available data, these workers constitute only a relatively small proportion of farm workers. Both technical and administrative personnel and specialized workers have relatively high income levels, compared to the low average wages paid in rural areas.

It is worth asking if the patronal structure has been so decisive in Latin American society that it has been able, firstly, to withstand the changes which normally accompany industrialization and, subsequently, to generate self-modernization strategies. The answer is undoubtedly affirmative, so that there are grounds for returning to the idea—put forward by several social scientists (Dahrendorf, 1979)—that in certain historical circumstances, some social strata can acquire a real capacity to exercise a kind of veto within their society.

However, it is also worth asking if there may have been certain elements within the prevailing circumstances which may have interfered with or hindered the formation of an independent peasant class within the existing rural strata, thereby rendering them unable to act to take the place of the patronal regime. It might be considered that peasants lacked tradition or rank, the myth of legitimacy, or “ancestral prestige”. However, the indigenous communities or ethnic groups with a tradition of agriculture do constitute nuclei for the emergence of a peasant society devoted to direct cultivation of the land, and the demand for land for crops and pasturage continues. Sugar, cotton and other plantations had recourse to slave or wage labour, and this did not stimulate the emergence of small farmers among rural families, who confined themselves rather to the cultivation of small plots for subsistence farming.<sup>7</sup> The granting of land to settlers or sharecroppers, which has been a characteristic feature of the patronal system, especially in the case of the haciendas, allowed for the formation of a peasant culture which acquired considerable weight in various countries. In certain social and political circumstances, this identification with the land activated aspirations to land ownership and contributed to the generation of reform proposals.

The opening up of new agricultural frontiers is living testimony to the rural population's capacity to become small peasant farmers. That population continues to make superhuman efforts to bring new lands under cultivation, but they are then often unable to retain them because of lack of financing, of markets for their produce and of competent authorities who could orient those projects socially so as to avoid the sale of the land thus settled.

#### 6. *Labour markets and work*

As well as being farmers, landowners were above all patrons: that is to say, they presided directly or indirectly over social and cultural organization, labour and other economic relations in their haciendas, ranches, or plantations and the local surroundings and over the broader political order as well. The patronal

<sup>7</sup> Something similar occurred in the rural trajectory of several areas of the United States, where large units were modernized through intensive use of capital and technology and little use of permanent labour. In that case, as in Latin America and the Caribbean, migrant workers (be they “wetbacks” or ex-slaves) have been an important element.

tradition has taken different forms in the conduct of the agricultural entrepreneurs who have been emerging in the region and, especially, in the treatment and payment of labour, due, among other factors, to the abundance of labour available in the rural areas and cities. Thus, the economic changes in the patronal system have not meant that the benefits of increased productivity have been shared with workers through higher pay, which explains the co-existence of modernized areas alongside situations of poverty and misery.

In the industrialized economies, great importance has generally been assigned to keeping the rural population on the land, and in some countries there has even been public intervention to form very small units which nevertheless made it possible to provide minimum subsistence units or the basis for part-time agricultural activities, in which the agricultural income is supplemented with income from industrial or service activities in nearby cities. In Latin America, on the contrary, given the abundance of urban labour, trends are being observed in which purely agricultural tasks are performed by persons who live in cities. Thus, for example, in São Paulo, Brazil, in 1970, 26% of the economically active agricultural population was of urban origin, and this percentage had risen to 38% by 1980. For Brazil as a whole, that percentage rose from 12.3% to 17.7% over the same period (FAO, 1988) and in Mexico, from 23.8% to 26%.

In several countries, because of fear of agrarian reforms or due to the effects of the capitalization, mechanization and technification of production, it was decided to uproot the peasant families who lived and worked on the large holdings, while sharecropping and similar arrangements (settlement, renting) under which, for centuries, part of the patron's lands had been granted to the families settled on them were drastically reduced. Thus, the modernization of the patronal system has been accompanied by the uprooting of the rural population, contrary to what occurred in the industrialized countries, where it was explicitly sought to keep peasants on the land as part of the modernization process.<sup>8</sup> As modernization allowed landowners to expand their scales of production, it also limited peasant access to patrons' land which they had previously rented or sharecropped.

<sup>8</sup> In some regions of some industrialized countries, such as the United States, for example, this process of keeping peasants on the land occurred only to a limited extent.

This combination of processes, which the Interamerican Committee for Agricultural Development has called the latifundio-minifundio complex, has tended to disappear, and relations between agricultural entrepreneurs and peasants or farm workers have been reactivated through the labour market.

The rural population of the region is divided between wage workers and peasants owning some land. The peasant economy is very important in the supply of agricultural products. The social category which seems to be expanding is that of the rural proletariat who live by wage work. In this regard, the rural trajectory is different from that followed in the industrialized countries, because in those nations the number of owner-farmers tended to increase. The demographic trends involved in the trajectory of the region are therefore different, because the rootedness arising from land ownership is different from that generated within the labour market, especially if work in agriculture is only casual. The characteristics which the rural or agricultural workers have been acquiring arise from situations of anomy and the instability caused by interruptions in work in terms of time or geographical location, which make it difficult to regulate labour relations both as they affect labour directly and in relation to social welfare and insurance. This situation also affects the family and group orders of relations, especially with regard to the possibility of articulating workers' interests and achieving social representation.

As already noted, more and more urban workers are entering the agricultural labour markets, especially for seasonal work (table 10). At the same time, however, more and more peasants are working in non-agricultural activities in rural or non-rural areas. In Mexico, for example, in 1980, 42.4% of the economically active rural population was performing non-agricultural tasks: a phenomenon which becomes even more significant when it is considered that in 1970 the figure was only 23.1%. Something similar is occurring in Costa Rica, Nicaragua and Ecuador (table 10).

The dynamics of the rural labour market have been changing in various ways. Firstly, in the process of change from patronal systems to entrepreneurial agriculture, there has been a reduction in the degree of rootedness of the populations permanently living and working on the large agricultural units, as the resident work force of those units has diminished and increasingly frequent recourse has been had to the markets for independent labour based in nearby

Table 10

**LATIN AMERICA AND THE CARIBBEAN: EMPLOYMENT STRUCTURE  
IN AGRICULTURE AND THE RURAL SECTOR**

Countries	Years	Proportion of agricultural EAP living in urban areas	Proportion of rural EAP employed in non-agricultural activities
Brazil	1970	12.3	15.2
	1980	17.7	
Pernambuco	1970	13.1	
	1980	16.3	
São Paulo	1970	26.6	
	1980	38.0	
Costa Rica	1963	5.4	29.1
	1973	6.2	41.2
Ecuador	1962	6.5	19.3
	1974	6.8	26.4
Mexico	1970	23.8	23.1
	1980	26.0	42.4
Nicaragua	1963	11.0	12.8
	1971	11.7	20.0
Peru	1961	18.3	20.1
	1972	23.7	18.8

Source: For Mexico, General Population and Housing Censuses of 1970 and 1980. For Brazil, Population Censuses of 1970 and 1980. For other countries: United Nations, *Patterns of Urban and Rural Population Growth*, Population Studies, Nº 68, New York, Department of International Economic and Social Affairs, 1980. United Nations publication, Sales Nº E.79.XIII.9.

towns and even in the cities. As already noted, the sharp increase in demand for some types of seasonal labour (for harvesting and other tasks) has led to the hiring of gangs of labourers from the small towns and cities where job opportunities are very scarce. The seasonal nature of the demand for labour means that temporary, rather than permanent, work is more readily available and has made it possible for the urban proletariat to carry out these tasks in competition with rural workers. Thus, in some areas or zones, there is an over-supply of labour on the rural labour markets where both the owners of dwarf holdings and landless peasants look for work. These markets are also increasingly open and fluid, and their radius or scope of operation is increasingly wide because of the possibilities now available to the urban and rural population to travel to ever more distant places. There are also certain modernized areas of production, growing crops that require an abundant supply of labour, in which some scarcity of this factor is beginning to be felt.

In areas where labour is used more intensively and where families can find work for sufficiently long periods to permit them to work out survival strategies, there is a tendency for population settlements to

be formed whose inhabitants come from other areas where there is less demand for labour or where poverty is greater, thus leading, over time, to migrations to areas which offer more job opportunities.

Changes in life styles, the demographic transition towards smaller families, and greater acceptance of women workers have created a climate of greater labour mobility as a function of the available job opportunities, even though these may be seasonal.

The transition from patronal-type agrarian systems to entrepreneurial agriculture, together with productive and technological change, has created the necessary conditions for the creation of increasingly uniform labour markets in rural areas, with wage levels established in the light of those prevailing in the towns and cities. The patterns of settlement and control of the work force which prevailed in the patronal system have been replaced by wage criteria. Labour markets have become increasingly important since the reform processes of the 1960s and the technological innovation registered in agriculture in recent decades, and they have also come to play a more significant role in determining the rural population's income.

### 7. *The peasantry*

Among the issues which have emerged with great force, first in the social sciences (in the 1970s) and later in the public and private (non-governmental organizations) spheres is that related to the peasant economy or peasant agriculture, which had been traditionally overshadowed by the patronal system and the agrarian ideology of the 1950s and 1960s. The chronic scarcity of land which affects a large portion of families is a leading feature of the Latin American peasant experience. The proliferation of dwarf holdings had, as its counterpart, a process of semi-proletarianization, as it obliged families to adopt survival strategies which include, as a decisive element, the sale of the family labour. As a result of the process of the proliferation of dwarf holdings experienced by families which possessed some land and the limited access to land available under the patronal system, since there has been a downward trend in sharecropping, rental and payment in the form of land granted for cultivation, peasant families have tended to have increasingly frequent recourse to the labour market. In some cases, however, the wages thus obtained have not been sufficient to make up for the impoverishment produced by the spread of dwarf holdings. As noted by Figueroa (Figueroa, 1990), in some circumstances there has been a tendency to pauperization in the peasant economy.

In the region, the social importance of the peasantry is still very considerable, both with respect to the rural population and to the total population. For this reason, all efforts to solve its problems deserve high priority. Moreover, the resources controlled by the peasantry are relatively important, taking into account the total area of the millions of small units which, together, represent a by no means inconsiderable part of the agricultural resources of the region. They do not, however, control the most productive land, and must therefore make more intensive and more arduous efforts to earn benefits from it.

Increasing the productivity and incomes of these rural family economies, in an environmentally reasonable manner, is to create greater equity. This means that more energetic efforts than those undertaken to date must be made to modernize those economies. It also means accepting their cultural originality by improving the quality and presentation of traditional products to raise their value in domestic and foreign markets. Technological, technical

assistance, financial and insurance services do not reach the low-income sectors, nor are they designed for them. Because of the traditional abandonment of the rural family economy by the scientific, technological, financial and other systems, agro-industry and agro-industrial complexes have taken on a role which may be of great importance for opening-up the traditional rural economies and integrating them into markets and knowledge. This type of linkage represents an interesting option for rural development, as the experience in a fair number of cases indicates, as long as the economic and social relations are suitably balanced.

In short, both wage labourers and landed peasants—the two main segments of the Latin American and Caribbean rural population—face serious restrictions in terms of their insertion into the economy, social organization and the representation of their interests, all of which complicates the solution of the inequitable situation affecting them.

### 8. *Sources of income of the most important rural strata*

Detailed analysis of the sources of income of the most important segments of the rural population reveals the relative importance of wages, income from own-account activities, and transfers. The most striking fact is the growing importance of the labour market and transfers.

The importance of the labour market may be seen from the fact that in Brazil in 1979, for instance, 39% of rural family income came from wages and salaries, but this percentage had risen to 43% by 1987. At the same time, income from own-account activities fell from 47% in 1979 to 42% in 1987. Remaining income came from transfers (table 11). In Costa Rica, in contrast, the weight of wages and salaries has remained fairly constant at around 57% of total income. This percentage is very high in comparison with that of other countries, but this is because of the high proportion of permanent crops in that country. In Chile, wages and salaries account for 30% of rural family income, but this should not be interpreted as indicating a scarcity of labour markets because, in fact, they are large and growing. The explanation is that 25% of the agricultural labour force lives in cities, from which it may be deduced that a substantial segment of the urban population receives income from agricultural work.

Table 11

## LATIN AMERICAN COUNTRIES: INCOME STRUCTURE OF RURAL HOUSEHOLDS

(Percentages)

Countries	Year	Wages and salaries	Income from own-account activities	Transfers
Brazil	1979	39	47	12
	1987	43	42	13
Costa Rica	1981	57	23	12
	1988	57	28	6
Chile	1987	30	58	12
Venezuela	1981	44	47	9
	1986	41	48	10

Source: ECLAC, Statistics and Projections Division.

## 9. The "empty slot" and the rural situation

One of the explanations for the "empty slot", that is, the absence of growth with equity which characterizes the region, lies in the rural trajectory followed by the countries of Latin America and the Caribbean for many years past.

The notable growth of the agricultural and rural economy in the last forty years<sup>9</sup> does not seem to have done much to alleviate the poverty and indigence which have affected rural areas of the region for centuries past. According to statistical data, the number of rural poor rose from 75.2 million in 1970 to 79.5 million in 1989: that is to say, the proportion of poor in the total rural population only went down from 65% to 61% in those 19 years. At the same time, between the 1970s and the 1980s the level of indigence remained constant, affecting around 30% of rural homes. In some countries, such as Chile, indigence worsened (from 11% to 16%) between 1970 and 1987, while in other countries, such as Mexico, it stayed constant at around 19% of rural households.

In spite of increased, more technified and more diversified production, a greatly expanded agricultural frontier and the various economic and social changes effected, a high degree of inequity persists in the rural sector. Only in a few cases can this be

explained by growth of the population in absolute terms. In practice, enormous contingents of population have sought to escape from that situation by emigrating to the cities or to new lands, in that order of preference. It is therefore hard to sustain the argument that rural poverty is due to the excessive increase in population density with respect to the available renewable resources. Moreover, as already noted, in the last three decades the population of Latin America and the Caribbean has become essentially urban.

This poverty seems to be linked rather to the lack of distributive and redistributive equity. Latin American society has not opened sufficient physical, cultural, economic and institutional spaces for its rural society. Experience demonstrates that the most critical situations in terms of income, work opportunities, and poverty and indigence in general are to be found: a) in peasant settlements in semi-arid zones, where the shortage of water is crucial; b) among indigenous peoples, because ethnic and indigenous groups continue to be marginated throughout the region, so that neither their lands and resources nor their social and cultural values are respected; c) among peasant families which attempt to settle new land on the agricultural frontier but are subsequently deprived of it, so that those areas become nuclei of conflict and extreme poverty; d) in peasant settlements, which are often those of indigenous communities, on severely eroded and densely populated mountain slopes; and e) among the rural masses who can obtain only very occasional

<sup>9</sup>The value of agricultural production trebled over the period 1950-1990.

employment (4 to 6 months a year) and who lack basic infrastructure (space, housing, public services, proper authorities). Among these groups, one which is a source of particular concern because of its high levels of indigence is that connected with the forest economy and the exploitation of woods and forests.

#### 10. *The rural trajectory and public institutions.*

The fact that the political and social functions of the patronal system were not replaced with another form of institutionality when that system lost its traditional power and role has created a vacuum in the rural sector which neither the State nor other bodies of society have filled. Moreover, the long reign of the patronal agrarian system hindered the creation of a more decentralized set of institutions. During that reign, social activities were circumscribed within the institutionality and traditions of the hacienda, plantation and ranch. In that sense, rural life depended heavily on the dominant agrarian structures, whose organization and rules were projected into the local and regional surroundings, so that the patronal system was the real expression of power (Ortega, 1987, pp. 217 - 220).

In the past, rural society remained under the control of the patronal system: a situation which led to the almost complete absence of local public powers. It is for this reason that in Latin America and the Caribbean, with only a few exceptions, there has been a situation which we may call under-municipalization: that is to say, very sparse local public powers, with serious limitations on their functions. Generally speaking, rural populations have only limited institutions, and it is difficult for them to gain access to the decision-making centres, public services and even social benefits. The clearest evidence of political and administrative centralism is the weakness of the institutions at the level of the commune and the municipality, which have not gained the importance they have long had in the industrialized countries. Municipal affairs are alien to the rural sector, yet their presence is essential for the integral development of that sector.

Our rural society therefore lacks public authorities to express the will and aspirations of the population and to guide social progress. Because of this lack, it is not possible to channel any initiatives,

contributions of resources or labour or projects which may arise, as would be possible when suitable conditions for participation exist. The lack of authorities that seek to promote public welfare and progress is manifest. Local government does not extend to rural areas, and it is therefore ineffective. The weakness or total absence of authorities in rural communities undermines, perhaps more than any other factor, the possibilities of development of that society. This situation also leads to immobility, passive attitudes and caudillismo or caciquismo, which may be reflected in arbitrary actions in extreme situations. At the same time, it is entirely possible that there is a positive correlation between the lack of participation and protagonism channelled through proper institutions, and extra-political forms of social action. Violence in rural areas may be linked with the weakness of the institutions there.

#### 11. *The weakness of existing forms of association*

The area of organized interest groups or cooperative action in the rural or agricultural societies of the region, is, once again, notably different from the situation in the industrialized countries. There, trade associations and organizations are very long-standing and fulfill a broad variety of functions which permit them to secure a high degree of economic decentralization and linkages between agriculture, industry and the services sector. In our experience, the lack of representative organizations which are functional to the development process is very notable. Cooperative enterprises have very little weight in the areas of technical assistance, distribution of inputs or sales of produce. As for credit, in 1987 crop-farming cooperatives received only 6% of total credit, while livestock cooperatives received only 6.9%.

According to available information, the existing cooperatives did not result from social processes of association among poor producers, peasants or rural families, but rather from cooperative associations of mid- or large-scale producers. The experience of Brazil illustrates this point (table 12). In many cases, cooperative associations were formed in order to take advantage of certain benefits or opportunities offered by governments (tax exemptions, subsidies, provision of services, public investment in agro-industry, and other forms of infrastructure). In the

Table 12

**BRAZIL: PRODUCERS GROUPED  
TOGETHER IN COOPERATIVES,  
BY SIZE LEVEL, 1980**

Size level (hectares)	Establishments grouped in cooperatives
Less than 1	1.2
1 - 2	1.7
2 - 5	4.2
5 - 10	9.4
10 - 100	19.9
100 - 1 000	26.0
1 000 - 10 000	30.1
Over 10 000	20.5
Not specified	2.7
<b>Total</b>	<b>12.8</b>

Source: Prepared by the ECLAC/FAO Joint Agriculture Division on the basis of Brazilian Institute of Geography and Statistics (IBGE), *Censo Agropecuario IX Recensamento Geral do Brasil*, vol. 2, part 3, Nº 1, Rio de Janeiro.

agricultural sector of the region only a few associative processes have arisen as the social expression of changing production patterns and technological progress.

In industrial societies, where rural families and, in particular, peasant farmers were specially trained to exercise a leading role in the development process, association for economic purposes was a common social phenomenon.

The structural weakness of rural society in Latin America and the Caribbean produces distortions in the allocation of functions between the public and private sectors. The lack of a leading role for the rural population and the repression of attempts at rural mobilization have led to imbalances in the representation of rural and agricultural interests, which have been left in the hands of minority strata. The rural population have not only not had sufficient access to the renewable resources which they sought, but they have also not been given adequate levels of participation and, for that reason, have been deprived of the minimum benefits of modernity they need in order to be able to conserve their position as rural dwellers. In terms of access to basic public services, their situation is still quite shaky. For example, in most countries of the region, less than a third of rural homes have electricity, and in some countries that service is available to less than 10% of the rural population.

## 12. Reflections on rurality

Within this context of imbalances between the rural population and resources and between the rural population and markets, a sharp rural-urban imbalance is created which tends to produce a type of urbanization dysfunctional to industrialization and to satisfactory levels of productivity and income in the economy. Moreover, the population growth rates of most of the countries of the region, comparatively higher than those of the industrialized countries, and the sweeping influence of the mass media, which homogenize aspirations and demands, join together to strengthen rural-urban migratory processes.

In several societies in the region, the rural population is entering upon a stage of evolution which adds new factors tending to speed up migration. When a process of demographic deterioration occurs in which the rural population drops in absolute terms, this leads to the decomposition of certain population pyramids, giving rise to population ageing, the migration of young women, which affects the formation of new families, and a series of phenomena that further accentuate the trend toward exodus. Moreover, due to the cultural transition underway within the rural population, towards values, habits, aspirations and demands which are increasingly similar to those of an urban-industrial nature, distances no longer involve only economic considerations (productivity-income) but also have a physical dimension because of the lack of communications infrastructure, which means that even the notions of time and opportunity (for example, access to health services in case of illness) are different. Living in a consumer culture without having access to industrial consumer goods or basic services is a destabilizing factor for those who live in rural areas. The rural population of Latin America and the Caribbean continues to suffer situations of poverty and discrimination and, above all, lack of opportunities and social protagonism, at a time when the mass media and educational systems, either directly or indirectly, are offering rural dwellers an urban-industrial culture with which they are now perfectly familiar but from which they are as far removed as ever.

The failure to define coherent strategies which include both the urban-industrial and the rural-agricultural sectors is generating a vigorous migratory process and producing heavy urban concentrations in which people turn to degrading forms of

social conduct in order to obtain income and survive. The externalities of the lack of equity in the agricultural sector can be perceived far beyond the limits of the rural sector and represent costs that must in many respects be paid by urban inhabitants. When peasants and rural dwellers in general lack opportunities to work, produce, and obtain income in their own environment, they put pressure on urban labour markets with consequent effects on wages.

Latin America and the Caribbean as a whole are entering on a stage of stabilization of their rural population, without any clear indications that rural areas will be able to fulfill the function of retaining a greater proportion of the population in the future. On the contrary, in some countries there is a veritable exodus from the countryside. The last three decades have transformed the region into an essentially urban space. Between 1960 and 1990, 94% of total population growth (230 million persons) took place in the cities. Villa (ECLAC/CELADE, 1991) states that, on the basis of the successive proportions of total population increase attributable to the urban segment, the net total transfer of rural dwellers between 1930 and 1990 may be calculated at some 106 million persons, equivalent to 38% of the urban increase for that period; while on the basis of assumptions on differences of natural growth rates between urban and rural areas, he calculated a magnitude of around 100 million persons for that same period.

The resurgence of poverty and indigence in Latin American and Caribbean cities may be considered to be an externality of the situation of inequity affecting the agricultural and rural population. In 1990, 72% of the population of the region lived in urban areas. Urban growth has been rapid, due largely to migrations from the countryside. Of the total urban population registered in 1970, 41.8 million persons (i.e., 37%) were poor, and for 1989 the corresponding figure has been estimated at around 104 million, or 57% of that population.

The externalities of more equitable and less heterogeneous agrarian patterns have not been adequately appreciated in the region, perhaps because there has not been a proper appreciation of the effects of the broader and more equitable distribution of property, knowledge and capital on demographic processes and the use and management of resources. More balanced and egalitarian agrarian systems tend to give rise to association and participation; to

stimulate settlement on the land and offer greater prospects for progress; to encourage initiatives designed to link together agriculture, industry and services; to make the collective adoption of technological innovations aimed at improving rural housing, health and educational services more viable; and to promote improvements in the energy, transport and communications infrastructure.

As noted below, the strategies for changing production patterns with equity proposed for Latin America and the Caribbean do not include the minimum conditions necessary to ensure that rural areas can play the role they fulfilled in the development strategies of the currently industrialized countries. This is the Gordian knot in the formulation of proposals for development with equity in the regional agricultural sector. Perhaps the capacity of the peasant economy for work, saving, technification and initiative has been overlooked, together with the fact that broader land ownership leads to integrated management of the factors of production and, in particular, of initiative and labour. For different reasons, from the early days of its economic and social evolution Latin American rural society has tended more to generate a proletariat than to give rise to independent farmers. In our region, there has been a tendency to avoid the issue of the role which natural resources could play in a strategy providing options for living which would constitute alternatives to those offered by industrialization and urbanization.

Historically, advanced societies have made marked progress in their efforts to achieve structural or basic equity, that is to say, "ex ante equity", because they have seen it as a requisite for stability, technological progress and industrialization. These changes in the direction of greater equality in the distribution of renewable resources have, it is true, involved significant economic and social costs, but, over time, they have mitigated poverty or made it less painful and prolonged, and they may well have reduced the social expenditure needed to alleviate it.

In the region—at least in certain periods—policies have been designed and attempts have been made to implement them with a view to achieving equity through *ex post* efforts subsequent to the development of essentially inequitable societies in which no serious concessions had been made. In other words, in a sense equity represents the social cost involved in mitigating the effects of those initial inequalities which continue to show up in society, to

and sometimes even get worse. It is in this context that ways of changing production patterns with equity must be sought, through efforts to correct basic inequalities through strong growth stimuli, more effective social policies, and serious reconsideration of the public and private institutional order.

In addressing this issue, it must be recognized—without allowing this to become an obstacle to reflection on the ways which have been pursued or should be pursued in the search for equity—that the challenges the region faces today are, perhaps, greater than those of other moments in its history, since in a sense the questions raised are how to make something work in an equitable manner which has essentially been operating inequitably; and how to balance something which is congenitally unbalanced.

The slow but steady introduction of technology which has traditionally taken place in the rural economies has become much faster in the last four decades. At the same time, technological change, which has made possible the development of entrepreneurial agriculture, has also had an impact on peasant agriculture through some of its biological, chemical or mechanical components, although more selectively and slowly. In general, the capacity for technological innovation displayed by the rural economy has been relatively high when the essential prerequisites for changing production patterns have prevailed, such as flexible and efficient incorporation into technological trends, the inputs market, the financial system, produce markets and, in particular, agro-industry.

The transition from the patronal system to entrepreneurial agriculture has revealed a large institutional void, since the arrogation of public functions by the patrons prevented the establishment of open and efficient local administrations, as well as other forms of public institutions, leaving a legacy of limited State presence in the countryside. Because of this fact and its limited possibilities for participation, the rural population has had little incentive to undertake associative and cooperative activities and achieve efficient representation of its interests, thus further strengthening situations of clientage and caciquism. Rural society is weak because it lacks both

adequate institutions and forms of representation, its disorganization being a traditional feature.<sup>10</sup>

Several factors have helped to bring about gradual changes in the ways of thinking, behaviour and aspirations of the rural population. Among these are the intensification of urban-rural relations, the multiplication of forms of interchange between these two areas, the development of information and communications systems, and the broadening of education. In many respects, however, the process of transition under way has not had a counterpart at the economic, social and institutional levels. Rural areas, considered as the place of residence of rural families or peasant communities, have not progressed sufficiently in the areas of basic infrastructure and essential public services. Housing programmes are practically unknown, as are rural telephone services or other communications systems which are essential in order to break the isolation and lack of timely attention to the needs of the community. That situation, which further aggravates the problems deriving from institutional shortcomings and the lack of social participation, is in turn a real reflection of these latter two voids. Nevertheless, a good deal of progress has undoubtedly been made in education, especially primary education, and in the area of primary health services.

The figures and details of rural poverty and indigence are all too well known. In spite of the big expansion of the rural economy, the significant increases in productivity and the incorporation of new land into production, there are still situations of great structural rigidity which give rise to poverty and indigence. Those most affected are the ethnic groups and indigenous peoples, peasants on the agricultural frontiers, those working semi-arid lands and uplands, and also peasants suffering from the prevalence of dwarf holdings and the lack of job opportunities. The peasant proletariat also suffer from the shortage of job opportunities.

Beyond any doubt, the rural trajectory of Latin America and the Caribbean does possess its own very special character.

<sup>10</sup> In comparative terms, Latin America and the Caribbean today have fewer municipalities than Federal Germany did in 1950, and less than half the communes and municipalities which France possessed in 1970.

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## The potential of Mexican agriculture and options for the future

*Julio López G.\**

Mexican agriculture, which had deteriorated as a result of the global adjustment process, only began to recover as from 1989. If the recovery of the national economy which began in 1987 becomes even more marked, it is possible that agriculture may not be able to respond with increased production.

In this article, it is suggested that the potential of Mexican agriculture is enormous. In order to evaluate the short-term potential of Mexican agricultural activity, the author calculates the volume of production which could be achieved if the maximum area cultivated and the peak yields of the recent past were achieved simultaneously. In order to estimate the indirect contribution of agricultural recovery to the national economy, he also calculates the level of imports that could be attained if the country's agricultural potential were fully exploited. On the assumption that insufficient import capacity limits economic activity and on the basis of the import coefficients of the past, the indirect contribution of agriculture is accordingly evaluated. According to a relatively optimistic hypothesis, the direct and indirect contribution of the increase in the sector's gross domestic product is estimated at the equivalent of 6% of total GDP. According to a less optimistic hypothesis, it is estimated that that contribution would raise total GDP by 3.2%.

That potential could be realized if the supply conditions of the sector were increased through recapitalization and other institutional measures. In addition, in order to stimulate supply it would be necessary to provide suitable incentives for producers, such as selective subsidies. These should be short-term subsidies and should be differentiated by product, type of producer and, possibly, by region.

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## Introduction

During the period of adjustment of the Mexican economy, the growth of the agricultural sector was even more limited than that of the rest of the economy. Thus, while overall economic activity began to recover in 1987, agriculture only began to make up for its past deterioration as from 1989, thanks to favourable weather conditions.

Clearly, limitations in the supply of agricultural goods may threaten national economic recovery. On the one hand, stagnation of agricultural production would directly weaken the overall economic growth rate. On the other hand, a significant part of the increased demand for food and agricultural goods due to the recovery would have to be covered by imports. In a situation of external constraints, this would restrict the possibilities of increasing demand and, hence, production. It is therefore necessary to see whether the recent recovery in agricultural sector production is based on solid foundations or not.

In this article, it is argued that Mexican agriculture does in fact have enormous potential and that realizing that potential would not only allow that sector to go along with the overall recovery but even stimulate it. Several general sectoral policy lines which could help take advantage of that potential are also explored.

## I

### The potential of Mexican agriculture and its impact on the national economy

Analysis of the main crops grown in 1988—the latest year for which the data needed for the following exercises are available—makes it possible to identify the immediate causes of the agricultural stagnation which prevailed up to that year and to evaluate the agricultural potential. If the production of rice, beans, maize, wheat, sesame, soy beans, cotton, barley and sorghum (which account for 35.4% of the total value of agricultural production in that year) is considered, it may be seen that during the 1980-1988

period, both the area under cultivation and the yields per hectare declined for all those crops.<sup>1</sup>

This suggests that, in agriculture as in the national economy, productive resources were not adequately exploited. If both the (maximum) yields and areas under cultivation achieved previously had been maintained, the production of the sector could have been greater than that actually achieved.

It is interesting to try to quantify the foregoing statement. To that end, table 1 seeks to measure the loss of potential production (that is, the difference between the actual production and that which would have been achieved if the area cultivated and the yields had been at their maximum levels) due to the lower yields and smaller areas under cultivation.<sup>2</sup> In the table, a calculation is made of the volume and value of production that each of the crops in question would have registered in 1988 if the potential yields and areas under cultivation had been maintained. Subtracting the values actually achieved in that year from the amounts calculated in this exercise gives the potential production and its potential value.

The table shows that all the crops analysed could have reached higher production levels. Although the orders of magnitude must be viewed with great caution, the data clearly show losses caused by under-exploitation of resources. Thus, the loss in potential production in 1988 was of the order of 3 924.7 billion pesos: equivalent to 45% of the actual value of production of those crops.<sup>3</sup>

Moreover, further conclusions can be drawn from the fact that in that year gross agricultural production was worth 24 741 823 million pesos, whereas the sectoral GDP was 18 953 547 million pesos. If the potential yields and areas under cultivation had been achieved for the nine crops in question, and if those crops had registered the average ratios of GDP to gross production (0.766) obtaining for the whole

of agriculture, then the agricultural GDP would have been 21 959 320 million pesos, or nearly 16% higher than that actually achieved. Furthermore, the total national GDP, which came to 392 791 754 million pesos, would have been 395 798 074 million pesos: that is to say, 0.8% higher than it actually was.

In other words, if the historical yields and areas under cultivation had been achieved in the case of only nine products, the sectoral and total products would have been 16% and 0.8% higher than they actually were. This would have been the direct contribution of agriculture, if its potential production had been realized. Below, it is demonstrated that its indirect contribution could have been even greater.

So, what would it mean for the national economy if agriculture could realize its potential production in those nine crops? Above and beyond the higher agricultural GDP already analysed, the most significant contribution would be indirect, connected with its effects on foreign trade and, in particular, its effect in helping to alleviate external constraints

Table 2 examines the contribution that could have been made by agriculture to foreign trade, if the potential production of these nine crops had been realized. For this exercise, it is assumed that the potential production would be used exclusively for export or for import substitution, and that it could be sold on foreign markets at the prevailing prices. Naturally, these are simplifications. A more realistic analysis would have to address the situation crop by crop.

The table makes it possible to arrive at some interesting conclusions. Firstly, if it is assumed that the potential production can be achieved without affecting previous levels of imports and exports,<sup>4</sup> it is seen that Mexico could have been not only self-sufficient, but even a net exporter, in the case of seven of the crops under consideration. Thus, it could have eliminated imports and achieved exportable surpluses in the case of beans, maize, wheat, sesame and barley, and it would only have been necessary to keep on importing soy beans and sorghum.

<sup>1</sup> This statement is not based on trends in these variables, which were rather erratic, but rather on the fact that in 1988 both the area under cultivation and the yields were below the maximum levels achieved during the 1980-1988 period.

<sup>2</sup> It may be noted, for example, that in 1988 the total area under cultivation was 18 597 000 hectares, in contrast with the 23 964 000 hectares cultivated in 1983. Macroeconomic and trade policies which would help to restore the area under cultivation and yields to their maximum levels are considered below.

<sup>3</sup> It does not seem that the lower yields of 1988 were caused by the use of marginal land, since in that year the total area cultivated was less than in 1983, for example.

<sup>4</sup> This is a simplification: increased agricultural production would increase the demand and need for imports of inputs for the sector and would somewhat reduce its balance for exportation. This matter is considered below.

Table 1

## MEXICO: POTENTIAL AGRICULTURAL PRODUCTION, 1988

	Rice	Beans	Maize	Wheat	Sesame	Soy beans	Cotton	Barley	Sorghum	Total
Real area planted (Si) (thousands of hectares)	171	2 344	8 029	965	103	155	298	246	1 941	14 252
Real yield (Ri) (tons per hectare)	1.75	0.37	1.32	3.80	0.33	1.46	1.65	1.42	3.04	
Production (thousands of tons)	300	857	10 600	3 665	34	226	491	350	5 895	
Production (millions of pesos)	200 494	835 184	4 143 155	1 148 007	37 559	175 620	166 317	122 719	1 948 976	8 778 031
Price per ton (Pi) (thousands of pesos)	668.31	974.54	390.86	313.24	1 104.68	777.08	338.73	350.63	330.62	
Potential yield (Rip) <sup>a</sup>	2.23	0.58	1.69	4.24	0.50	2.01	1.83	1.99	3.26	
Potential area (Sip) <sup>a</sup>	216	2 462	8 551	1 274	358	505	333	361	2 060	16 120
Rip*Sip*Pi	321 621	1 386 566	5 634 244	1 692 466	199 427	789 756	206 629	251 931	2 220 126	12 702 765
Ri*Si*Pi	200 494	835 184	4 143 155	1 148 007	37 559	175 620	166 317	122 719	1 948 976	8 778 031
$\Sigma Rip*Sip*Pi - \Sigma Ri*Si*Pi$										3 924 734
Rip*Sip	481	1 423	14 415	5 403	181	1 016	610	719	6 715	
Ri*Si	300	857	10 600	3 665	34	226	491	350	5 895	
Rip*Sip - Ri*Si	181	566	3 815	1 738	147	790	119	369	820	

Source: Prepared by the author on the basis of figures from the Annex to the First Presidential Report, 1989.

<sup>a</sup> Based on the maximum yields and areas cultivated in the period 1980-1988.

Moreover, if that production is valued at current international prices,<sup>5</sup> the realization of the potential production would have meant foreign exchange earnings (amount saved by import substitution, plus the earnings from increased exports), equivalent to US\$1 581.5 million (table 2). That figure is slightly higher than the total agricultural exports registered in 1988, when agricultural exports and imports amounted to US\$1 401 million and US\$1 397 million, respectively.

It is now possible to estimate the total contribution of agriculture to the national economy, if the potential production of those crops had been realized. The direct contribution, as already noted, would have amounted to a 16% increase in the agricultural GDP and a 0.8% increase in the total GDP in 1988. However, the indirect contribution would have been much greater.

<sup>5</sup> These represent the average price of Mexican exports and imports in 1988. Estimates were based on data provided by the Bank of Mexico.

The reason for this is as follows. Even though Mexico has regained access to international credit and the inflow of capital has been rising, the external situation of the country is still delicate. Moreover, after the debt crisis and the implementation of the new economic policy, all the new conditions for expansion have involved strong surges in imports.

The fact that the external situation is still difficult reduces the capacity of the State to apply policies which will increase demand, since it does not seem prudent to continue financing current account deficits with foreign capital much longer. This explains why, after several years of recovery, there is still a large amount of idle production capacity, along with unemployed labour.<sup>6</sup> In this sense, it is not too much to argue that, for Mexico, foreign exchange availability is a critical limiting factor on production.

<sup>6</sup> According to one estimate, the utilization of production capacity in 1990 was still 20% below the 1981 level (López, 1991a). Moreover, in various surveys made in 1991, manufacturing sector representatives indicated that 30% of their capacity was idle (see various recent issues of the Mexico City business magazine *Expansión*).

Table 2

**MEXICO: REAL AND POTENTIAL FOREIGN TRADE  
IN NINE AGRICULTURAL PRODUCTS, 1988**

	Rice	Beans	Maize	Wheat	Sesame	Soy beans	Cotton	Barley	Sorghum	Total
Real imports <sup>a</sup>	1.0	31.0	3 125.0	1 189.0	-	989.0	44.0	7.0	1 523.0	
Real exports <sup>a</sup>	3.0	8.0	-	104.0	-	-	108.0	-	415.0	
Real net exports <sup>a</sup>	2.0	-23.0	-3 125.0	-1 085.0	-	-989.0	64.0	-7.0	-1 108.0	
Potential exports <sup>a</sup>	181.2	565.8	3 814.9	1 738.2	146.5	790.3	119.0	368.5	820.1	
Potential net exports <sup>a</sup>	183.2	542.8	689.9	653.2	146.5	-198.7	183.0	361.5	-287.9	
Average foreign price <sup>b</sup>	300	381	130	125	740	306	772	163	120	
Potential foreign exchange earnings <sup>c</sup>	54.4	215.3	494.0	217.3	108.4	241.8	91.8	60.1	98.4	1 581.5

Source: Prepared by the author. The average foreign price was obtained from Foreign Trade Statistics of Mexico.

<sup>a</sup> Thousands of tons.

<sup>b</sup> Dollars.

<sup>c</sup> Millions of dollars.

Now, agriculture produces goods which are tradeable in foreign markets, which means that the potential production could be exported and serve to substitute imports.<sup>7</sup> Greater availability of foreign exchange would make it possible to raise aggregate demand, and this would permit increased production, employment, wages and private profits in sectors limited by low demand. This is exactly what the indirect contribution of agriculture to the national economy would be, if its potential were realized: it would allow demand and production to expand in the other sectors, without causing inflation or unmanageable balance of payments problems.

Table 3, which was prepared on the basis of the same assumptions as the preceding table, together with those indicated below, seeks to measure the indirect contribution of agriculture, if the potential production of the nine crops had been realized in 1988.

In order to measure this contribution, it is necessary first of all to deduct the sector's foreign exchange requirements—which can be obtained for each crop by multiplying potential production by the corresponding coefficient for imported inputs—from the foreign exchange which would be saved or obtained thanks to this potential production. This

<sup>7</sup> It should be noted that, from this point of view, the benefits accruing from the generation of exports and the substitution of imports are identical.

*agricultural surplus* can be expressed in physical units, as in the table.<sup>8</sup>

Secondly, it is necessary to estimate the *exportable surplus of agricultural goods*, which is calculated by subtracting from the agricultural surplus the domestic demand for agricultural goods. This latter demand is equal to the increased domestic consumption (or apparent consumption) of those goods which would arise from the expansion of GDP and personal income. In the table, it is assumed that the income-elasticity of apparent consumption is 0.8, or 80%; this is a pessimistic assumption, because the income-elasticity of demand for agricultural goods is actually quite low and, historically, has been below 0.4 (López, 1991a). The exportable surplus, multiplied by the average external price of each product, gives the *potential foreign exchange surplus*, both for each crop and for the economy as a whole. This latter factor would amount to US\$1 363 million, which is only slightly less than total agricultural exports in 1988 (table 3).

<sup>8</sup> The import coefficients for each crop were obtained from the "Input-output matrix for Mexico. Breakdown for the agricultural and forestry sector, 1980" prepared by the National Geographic, Statistical and Informatics Institute (INEGI) and the Ministry of Agriculture and Water Resources (SARH). It should be noted, as may be clearly seen in the table, that the agricultural sector is peculiar in an important and beneficial way: its inputs are mainly produced domestically, so that its coefficient of imported inputs is very low. Thus, few imported inputs would be needed to realize the potential production, with the result that the amount of foreign exchange freed for other sectors would be substantial.

Table 3

**MEXICO: INDIRECT CONTRIBUTION OF AGRICULTURE TO  
THE REST OF THE ECONOMY**

	Rice	Beans	Maize	Wheat	Sesame	Soy beans	Cotton	Barley	Sorghum	Total
Production <sup>a</sup>	300	857	10 600	3 665	34	226	491	350	5 895	
Potential production <sup>a</sup>	181.2	565.8	3 814.5	1 738.2	146.5	790.3	119.0	368.5	820.1	
Real imports (volume) <sup>a</sup>	1.0	31.0	3 125.0	1 189.0	-	989.0	44.0	7.0	1 523.0	
Real exports (volume) <sup>a</sup>	3.0	8.0	-	104.0	-	-	108.0	-	415.0	
Real net exports (volume) <sup>a</sup>	2.0	-23.0	-3 125.0	-1 085.0	-	-989.0	64.0	-7.0	-1 108.0	
Import coefficient	0.0186	0.0138	0.0118	0.0162	0.0112	0.0175	0.0085	0.0221	0.0330	
External inputs required <sup>a</sup>	3.4	7.8	45.1	28.1	1.6	13.8	1.0	8.1	27.1	
Agricultural surplus <sup>a</sup>	177.9	558.0	3 769.8	1 710.1	144.9	776.5	118.0	360.4	793.1	
Domestic demand for agricultural goods <sup>a</sup>	13.0	38.5	600.3	207.8	1.5	53.1	18.7	15.6	306.3	
Exportable surplus <sup>a</sup>	164.8	519.5	3 169.5	1 502.3	143.4	723.3	99.3	344.8	486.8	
Average external price <sup>b</sup>	300	381	130	125	740	306	772	163	120	
Potential foreign exchange earnings <sup>c</sup>	49	198	410	188	106	221	77	56	58	1 363
Potential contribution to GDP <sup>d</sup>	778 587	3 111 947	6 462 061	2 956 509	1 670 682	3 484 817	1 206 331	884 760	919 607	21 475 301

Source: Prepared by the author.

<sup>a</sup> Thousands of tons.

<sup>b</sup> Dollars.

<sup>c</sup> Millions of dollars.

<sup>d</sup> Millions of pesos.

On the basis of these potential foreign exchange surpluses, it was possible to measure the potential indirect contribution of agriculture.

In making this estimate, it was taken into account that in 1988 total GDP came to 392 791 754 million pesos and that, in order to generate that GDP, US\$24 948 million of imported goods and services were needed. This means that, for each million dollars spent on imports, 15 744 million pesos of GDP was generated.

If it is assumed that the import coefficients for the agricultural and non-agricultural sectors are identical (which is of course a simplification), the foreign exchange which agriculture could transfer to

the rest of the economy in 1988, a total of US\$1 363 million, would make it possible to generate an increase of GDP of the order of 21 475 301 million pesos. This would be equal to 5.5% of total GDP and 13.3% higher than the agricultural GDP for that year.

This would be the exact indirect contribution of agriculture to an increase in the GDP. Since, as estimated earlier, the direct contribution due to an increase in sectoral GDP would have been 3 006 320 million pesos (equal to 0.8% of GDP), it may be concluded that the total contribution from the realization of the potential of agriculture would be 24 481 621 million pesos: equal to more than 6% of the 1988 GDP.

## II

### Future prospects and options

Once potential resources and the insufficient current yields have been verified, the question arises of what can be done to avoid such inefficiency and realize the potential production: that is to say, what would be the most appropriate set of instruments to achieve those objectives.

In the recent debates about Mexican agricultural and agrarian policy, the main emphasis has been placed on organizational and institutional change. With the reform of Article 127 of the Constitution—which establishes the conditions for the functioning of the *ejidos*—and with the free trade treaty with United States and Canada, Mexico is seeking to reform its institutional and organizational frameworks in order to strengthen entrepreneurial activity in rural areas and make it more dynamic.

These reforms will probably help stimulate Mexican agriculture by attracting fresh investments and giving agricultural exports easier access to the North American market. However, the modernization of the agricultural sector will also depend on the macro-economic and trade policies applied, since they will establish the conditions for the relative profitability of that sector. In the following pages, emphasis will be placed on those types of policies, without however ignoring the importance of organizational and institutional measures or of sectoral and microeconomic policies.

In an earlier study by the present author it was argued, on the basis of various econometric estimates, that agricultural production is partially determined by demand and, above all, by domestic demand (López, 1991b). For example, the drop in domestic demand which followed the debt crisis had an almost direct impact on agriculture, since there was no short-term possibility of selling part of that sector's production on international markets.

In this sense, the continuation and enhancement of the recovery begun in 1987 seems to be a first condition for realizing the potential of agriculture. Indeed, during the two years 1990-1991 there was a degree of recovery in that sector, with an average

annual growth rate of 4.5% in its GDP. To a large extent, this has been due more to the buoyant domestic market than to increased demand for exports, and it has not been accompanied by significant investments in agriculture, nor the channeling of substantial resources to that sector.

This latter aspect represents a further necessary condition if the record areas under cultivation and yields of the recent past are to be recovered. Because of the adjustment process, investment in rural areas virtually collapsed, and the ratio between federal public investment and the agricultural GDP, which had been 11.5% on average between 1980 and 1985, fell to 4.5% during the 1985-1988 period, while the participation of federal public investment in the agricultural sector, as a percentage of total public investment, fell from 11.6% to 8.4% over the same period. At the same time, credit for agriculture fell sharply: the share of farm credit in total credit granted by the consolidated banking system fell from 5.7% to 3.6% during those years, while farm credit as a percentage of the GDP of that sector went down from 35.3% to 28.4%. It seems doubtful, to say the least, that agricultural production can continue to grow without investment efforts in the sector.

Another condition—also necessary, although not sufficient in itself—for the realization of potential production is related to the recapitalization of agriculture. In other words, a significant part of the increase in overall demand should be converted into investment designed to modernize and capitalize the sector. This would make it possible to improve the material conditions of production and increase future soil yields and the productivity of agricultural labour.<sup>9</sup>

<sup>9</sup> It is very probable that what are needed are not so much large projects as smaller complementary investments to rehabilitate the infrastructure, which seriously deteriorated during the adjustment process.

However, increased demand may not lead to increased production, even if agriculture is recapitalized; the sector faces growing marginal costs,<sup>10</sup> so that greater demand may simply lead to more imports. Consequently, a third condition seems to be higher relative prices for agricultural products.<sup>11</sup>

Would this latter measure be sufficient? In the past, higher relative farm prices have not always stimulated production.<sup>12</sup> It may therefore be affirmed that, although it is a necessary condition, raising these prices is not a sufficient condition in itself either.

In this context, and in view of the proximity of the free trade treaty with the United States and Canada, it is worthwhile considering what would happen if domestic producer prices were to come into line with international prices. In fact, the ratio between domestic and foreign prices has not remained constant: in some years, the former were higher than the latter, while in others the opposite has been the case. For the purposes of analysis, it may be useful to take as a reference the situation in 1990. In that year, the domestic prices of at least five basic products were higher than the

corresponding foreign prices.<sup>13</sup> Price alignment would therefore mean lowering prices and profitability for most crops. In the short term, at least, this would probably mean lower overall sector supply.

It could be argued that this phenomenon would not occur if, together with price alignment, the national currency were devalued, because in that case relative farm prices would improve. In fact, several analysts have asserted (with powerful arguments) that over-valuation of the national currency is particularly harmful to agriculture, because nearly all of the production of that sector is tradeable or potentially tradeable in international markets (Valdés, 1986).

Obviously, the advantages inherent in a devaluation would depend on general economic conditions and not only those of the agricultural sector.<sup>14</sup> However, if the decision to devalue is made, it must be borne in mind that this would give rise to another problem: the devaluation would stimulate inflation and also reduce domestic demand. It has been confirmed (López, 1991b) that there is a negative association between the real exchange rate index, on the one hand, and domestic demand and the GDP on the other. In this sense, it cannot be affirmed *a priori* that such a measure would benefit agriculture.

<sup>10</sup> Agriculture, unlike manufacturing, faces increasing direct marginal costs.

<sup>11</sup> As an alternative –or together with these measures– the profitability of agriculture could be improved by lowering costs. However, there seems to be only limited leeway for this, especially if openness to foreign markets is continued and broadened. In fact, studies of effective protection show that at the end of 1987 –the last year for which figures are available– agriculture had a positive rate of effective protection of 4%, compared with an average negative effective protection rate of 28% for the other sectors of the economy. This, in a context of domestic prices for crops which seem to be higher than international prices, suggests that Mexican farmers do not pay higher prices for their inputs than world market prices.

<sup>12</sup> The past experience of Mexico –and of other countries– shows that, generally, higher relative farm prices tend to generate inflationary pressures, to depress the purchasing power of the lower-income groups, or both phenomena simultaneously. Because of this, and of the efforts of the State to control inflation by lowering its expenditures, domestic demand contracts, and this reduces the market for agricultural products. Thus, the supply stimulus associated with improved relative prices is cancelled out.

<sup>13</sup> In May 1990, the ratios of the international price to the domestic price for selected products were: yellow maize, 0.6; rice, 1.20; soy beans, 0.58, and sorghum, 0.88.

<sup>14</sup> The Mexican peso reached its lowest real value in 1987, when the real exchange rate index was 170 (on a base 1970 = 100), and it has since been gradually revalued. In October 1991 the index was 120, although this was still higher than its 1977-1979 level, when it is generally accepted that it was in equilibrium.

### III

#### A suggested policy for the agricultural sector

The foregoing section demonstrates the complexities involved in designing a policy to stimulate agricultural production. No single measure, by itself, is sufficient. This, however, also leads to the general conclusion that agricultural production could be increased if several conditions linked to macroeconomic and trade policy are satisfied simultaneously:

- i) That the upward trend and growth of demand continues and increases;
- ii) That the sector is recapitalized;
- iii) That producer prices are improved;
- iv) That these increases are not offset by reduced demand for farm products.

This conclusion makes it possible to suggest a way of satisfying the necessary conditions: a policy of producer subsidies<sup>15</sup> which would increase profitability but would at the same time avoid acceleration of inflation and reduction of the purchasing power of the lower-income groups.

If that policy were complemented with improvements in the infrastructure and trade channels, the elimination of bureaucratic obstacles and similar measures, the expansion of supply would be stimulated and the potential production could be realized. Thus, measures for organizational and institutional modernization, especially reform of the *ejido* system and the entry into operation of the free trade treaty, would also be supported.

How much would such a policy cost in terms of public expenditure? That figure would depend on the amount of the subsidies and their relation to prices. Table 4 seeks to make a first approximation to this question. In it, it is assumed that domestic producer prices would rise for the basic crops considered above. In the case of rice, prices would be fixed according to external prices. With respect to the other products, the 1988 prices would be raised by

<sup>15</sup> Another option would be a devaluation, accompanied by consumer subsidies (so that farm product price increases would not lower the buying power of the lower income groups and reduce domestic demand). The term subsidy is used here in a broad sense: it includes preferential credit rates, sale of inputs or products at reduced prices, etc.

15%.<sup>16</sup> In order to raise producer prices, a subsidy equivalent to the difference between the new domestic price and the international price would be granted. At the same time, consumer prices would be brought in line with international prices, which would mean that (except for rice) those prices would fall. This would eliminate the implicit transfer which consumers had been paying to agricultural producers because domestic prices were higher than those on the world market.

How could such a subsidy be financed? One option would be for the State to collect in one way or another the implicit transfer which consumers are now paying, but which they would cease to pay if prices were lowered. However, a different proposal will be considered here.

In principle, higher producer prices generate extraordinary earnings, that is, earnings over and above those generated by previous production.<sup>17</sup> In this analysis, it will be assumed that those earnings are taxed at 100%. It will also be assumed that this measure is accompanied by other forms of support (for marketing, infrastructure, etc.) which will stimulate an increase in production to a level equal to the potential production of each crop.

Table 4 shows that, first of all, this measure would eliminate the implicit transfer which Mexican consumers are paying today and which amounts to 2 404 652 million pesos, equivalent to 0.6% of the 1988 GDP. Secondly, this measure would be accompanied by a net subsidy (that is, net of taxes on the extraordinary earnings) for producers, equivalent to 4 050 445 pesos. That subsidy would amount to only 16.5% of the total increase (direct and indirect) in GDP generated by the potential production [4 050 445 divided by 24 481 621]; (3 006 320) (direct contribution) + (21 475 301) (indirect contribution).

<sup>16</sup> These domestic prices were obtained by dividing the value of production by the total production (according to the figures contained in the Statistical Annex of the First Presidential Report, 1989). The ratios between domestic and foreign prices for maize, wheat, sorghum, rice and soy beans were obtained from direct information provided by SARH. For the other products, it was assumed that the ratio was equal to the average (simple) ratio of the five products already mentioned.

<sup>17</sup> These extraordinary earnings are equal to the product of the volume of original production, multiplied by the difference between the necessary price and the original domestic price.

This is not all, however: in reality it would not even be necessary to make such large outlays, because the subsidy would partially pay for itself for the following reason. Given that the subsidy would increase the product, other taxes collected would also increase. Assuming a tax rate of 12.27% (non-oil domestic taxes), which was the rate in 1988, the total increase in the product would generate greater tax income of the order of 3 008 895 million pesos. That figure is only 1 041 550 million pesos less than the net subsidy required, which represents the deficit that the State would have to absorb.

What problems would that deficit cause? Clearly, that amount is much less than the implicit transfer which Mexican consumers are paying today. From that point of view, there would be a net improvement in the general well-being of the

community. Moreover, for each peso of the final deficit, 23.5 pesos of gross national product would be obtained (24 481 621 million pesos, divided by 1 041 550 million pesos), which is undoubtedly highly advantageous.

However, that deficit could generate inflationary pressures and/or put pressure on the balance of payments. Given the characteristics of agricultural production, there would be a lag between the moment of the expenditure (subsidy) and the time when the benefits of that expenditure would be felt. For that reason, it might be necessary to obtain foreign credit to cover that public deficit. However, those loans would pay for themselves, thanks to increased exports and the lower import coefficient which the subsidy would make possible.

Table 4

**MEXICO: ESTIMATED COST OF AN AGRICULTURAL  
SUBSIDIES POLICY, 1988**

	Rice	Beans	Maize	Wheat	Sesame	Soy beans	Cotton	Barley	Sorghum	Total
Domestic price per ton (PI) (thousands of pesos)	668.5	974.5	390.9	313.2	1 104.7	777.1	338.7	350.6	330.6	
Ratio PI/external price	0.9	1.2	1.8	11.1	1.2	1.5	1.2	1.2	1.2	
Equivalent domestic price	735.1	803.0	222.8	294.4	910.3	520.6	279.1	288.9	277.7	
"Necessary" price	735.1	1 120.7	449.5	360.2	1 270.4	893.6	389.5	403.2	380.2	
Subsidy (per ton)		317.7	226.7	65.8	360.1	373.0	110.4	114.3	102.5	
Gross subsidy per crop <sup>a</sup>		452 021	3 267 861	355 418	65 013	379 083	67 361	82 129	688 239	5 357 125
Implicit transfer <sup>a</sup>	-20 049	146 992	1 781 557	68 880	6 610	57 955	29 272	21 599	311 836	2 404 652
Extraordinary earnings	20 049	125 278	621 473	172 201	5 634	26 343	24 948	18 408	292 346	1 306 680
Net subsidy per crop <sup>a</sup>		326 743	2 646 388	183 217	59 379	352 740	42 413	63 722	395 893	4 050 445
Total net subsidy <sup>a</sup>										4 050 445
Gross production of sector <sup>a</sup>										24 741 823
GDP of sector										18 953 547
GDP of the economy										392 791 754

Source: Prepared by the author.

<sup>a</sup> Millions of pesos.

## IV

### Final considerations and conclusions

All the foregoing arguments could be questioned on the grounds of the assumptions made or the concepts or principles adopted. It could be said, for example, that the estimate of potential production is too high. It could also be argued that it is over-optimistic to assume that there will be export demand for surplus production.

Moreover, it could be argued that subsidies for producers or consumers –just like protection against external competition, for example– distort the market signs and therefore lead to sub-optimum resource allocation. If this were so, the benefits of the subsidies would be illusory or short-lived.

With respect to possible criticism of the assumptions made, it should be noted for a start that those used in the exercise do not pretend to be exact. In-depth research would be needed to achieve such exactness. Consequently, perhaps the best course for the present, until such research has been performed, would be to subject the results of the exercise to a sensitivity analysis: in other words, to see how far the results would be affected if other assumptions were used.

To this end, the same type of exercise was performed with the following different assumptions:

i) It will not be possible to increase the area under cultivation for the crops under consideration, although the potential yields could be attained for each of them. Thus, the potential production for 1988 would be obtained by multiplying the area actually cultivated that year by the potential yield for each crop.

ii) Because of lower farm prices, the income-elasticity of agricultural demand will be greater than in the previous exercise. A value of 0.9 is therefore assigned to that variable (instead of 0.8, which was itself high in comparison with historical values).

It is not necessary to go into detail about the specific aspects of this exercise, but its main results may be summarized as follows:

i) Potential production would amount to 2 117 204 million pesos. Sectoral GDP could have been 1 621 778 million pesos (8.6%) greater. The direct contribution to total GDP would be an increase of 0.4%

ii) Mexico could be self-sufficient and generate exportable surpluses, not only in rice and cotton –as in 1988– but also in beans, wheat, sesame and barley, while imports of maize, wheat, soy beans and sorghum would remain constant. The trade deficit for these nine products, which was US\$935.8 million in 1988, would be only US\$144 million in this case. The foreign exchange saving would thus amount to US\$791.6 million.

iii) The indirect contribution of the sector would be to raise GDP by 10 729 053 million pesos, i.e., by 2.7%.

iv) Consequently, the total contribution would be to raise GDP by 12 350 831 million pesos (1 621 778 million plus 10 729 053 million). This is equivalent to 3.1% of the 1988 GDP.

v) The gross subsidy would be 4 667 729 million pesos, and the net subsidy, 3 381 098 million pesos. The net subsidy would represent 27.4% of the total GDP increase obtainable from the potential production.

vi) Taxes collected would amount to 1 539 192 million pesos, so that the deficit would be 1 841 906 million pesos. For each peso of deficit, 6.7 pesos of GDP would be generated.

Thus, it may be seen that even with less optimistic assumptions than those used in the original exercise, the balance would be very favourable, if measures to realize the potential production were implemented.

What should be done, however, if the international market does not absorb the exportable surplus?

First of all, it should be noted that a substantial part of the foreign exchange benefits would come from the substitution of domestic products for imports, so that, at first, the domestic market should not be a problem for this production increase.

In the exercise performed earlier, for example, import substitution alone would produce foreign exchange benefits of US\$464 million, equal to 50% of the original deficit of those crops in 1988 and to 59% of the foreign exchange benefits obtained from the potential production. Those foreign exchange

savings alone would raise GDP by 7 305 216 million pesos, or 1.9% of the total 1988 GDP. Thus, even in these less favourable circumstances, taking advantage of the potential production would raise total GDP by 2.3% (0.4% directly and 1.9% indirectly).

If this were not enough, however, and if it were really impossible to sell the additional potential exports, another option could be considered. This would involve encouraging a change in crops, favouring those which would replace the remaining food imports. This would not be easy, because resources are not perfectly flexible. However, with adequate incentives –such as more favourable relative prices and credit and tax support– a good deal of progress could be made in this direction.

This reasoning shows that intervention above and beyond the signs given by the market may be preferable to doing nothing and leaving everything to market forces. In certain circumstances, intervention would make it possible to realize the potential production and utilize resources which would otherwise remain idle.

Such a proposal is usually associated with structural thinking. How different is it from conventional theory?

Although a detailed analysis of this question is not possible here, it can be stated that, when factor mobility is limited and wages cannot be lowered, neoclassical theory also recognizes that governmental intervention may be preferable to leaving the situation to market forces.<sup>18</sup> In fact, the main difference between neoclassical theory and the protectionist concept, for example, does not derive from the rejection of government intervention. The difference is rather that neoclassical theory recommends the application of subsidies or taxes up to the specific point at which domestic distortions are produced.

As already noted, this seems to be a reasonable conclusion. Be that as it may, however, it applies only at the theoretical level. Nothing has been said of the practical difficulties which may be involved in the proper implementation of subsidies, and this is where the main inconveniences and problems could arise. After all, agriculture has been heavily subsidized in Mexico in the past and the results have been far from satisfactory.<sup>19</sup> However, practical examination of this point goes beyond the limits of this paper.

To sum up the arguments and conclusions of this paper, it may be affirmed that Mexican agriculture definitely has unexploited potential. Realizing the potential production of basic crops would allow agriculture to increase both its production and its added value.

According to a relatively optimistic hypothesis, the *direct* contribution arising from an increase in the sector's GDP could be as much as 0.8% of total GDP. Even a less optimistic hypothesis gives an estimated 0.4% increase.

Moreover, and more importantly, that potential production would make it possible to save and generate foreign exchange, a large part of which could be transferred to other sectors of the economy, where it could finance additional imports and increase production. According to an optimistic hypothesis, such an *indirect* contribution from agriculture could raise total GDP by 5.5% with respect to the 1988 level, so that the total contribution accruing from the realization of potential production would be over 6% of the total 1988 GDP. According to a less optimistic hypothesis, the indirect contribution of that sector would raise GDP by 2.8%, so that the total contribution would be a 3.2% increase in the 1988 GDP.

<sup>18</sup> In the current debate on the economic policy that should be pursued in the light of the forthcoming free trade treaty with the United States and Canada, agricultural subsidies have been defended on the grounds that those countries also have such subsidies. This is an important argument, but it is different from that developed here. The article which may best express the position of the neoclassical school on this point is that by H. G. Johnson (1981). See also M. Chacholiades (1985) on this topic.

<sup>19</sup> Naturally, it must be noted that those subsidies have been granted in order to compensate for sectoral losses caused by the maintenance of low prices, while –due to protectionism– the prices of inputs have often been higher than international prices: in this case, the intervention was designed to correct a distortion in economic policy, which it perhaps did not fully offset.

That potential could be realized if the sector's supply conditions were improved through recapitalization and other types of institutional measures. In addition, in order to stimulate supply it would be necessary to grant producers adequate incentives, such as subsidies, which would guarantee them prices higher than those on the international market and which could be complemented by taxes on extraordinary earnings. Such subsidies should be short-term and

differentiated by crop, type of producer and, perhaps, by region.

With such policies, the total contribution of agriculture to the national economy could be enormous and could produce increased tax revenues which would finance a substantial part of the subsidies that it would be necessary to grant to the sector, either directly or indirectly, while at the same time eliminating the implicit transfer which consumers are currently paying to agricultural producers.

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## The privatization of the Argentine telephone system

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This article presents a detailed analysis of the situation of the Argentine telephone system prior to 1990 and evaluates the process of its subsequent privatization. Its main conclusion is that the previous situation of a State quasi-monopoly will probably end in a private oligopoly.

The main objective of the privatization was to do away with State subsidies for that sector and make services cheaper; however, it is possible that the forms taken by the process will generate a regressive transfer of resources, with respect both to customer tariffs, which have gradually been diverging from the cost structure, and to the equipment supply industry, which will no longer enjoy a preferential relationship with the National Telecommunications Company (ENTel).

Another objective was to modernize telephone services by introducing competition into the sector. However, competition will depend basically on the modification of the conditions laid down in the current transfer contracts.

In the light of these considerations, the article concludes that the regulatory framework may be unstable.

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## Introduction

From the mid-1940s up to the end of 1990, the telecommunications industry of the Argentine Republic was similar in structure to that of most other countries: a big State company – in this case the National Telecommunications Company (ENTel) – with monopoly powers over 95% of all telephone communications<sup>1</sup> and over telex, fax, data transmission, transport of radio and television signals, etc. At the same time, as was also the case in the rest of the world, since ENTel was a quasi-monopolistic purchaser of telecommunications equipment, it decisively contributed to the establishment of an oligopolistic structure in the domestic supply of communications switching and transmission equipment, within which the relative shares of each company remained more or less stable until the late 1980s.

Today, in the early 1990s, little remains of that situation: the State monopoly over services is dead and has given way to a private oligopolistic structure; the regulatory framework has been completely changed, and the relative shares of the various suppliers within the domestic equipment market have changed significantly.

The pressure to privatize came from two different sources. Firstly, there was a political decision to favour the creditors of Argentina's foreign debt and, at the same time, alleviate the short-term fiscal deficit. As will be seen below, the transfer of ENTel to the private sector was effected mainly through the acceptance of debt paper in exchange for State assets and monopoly rights over a number of services. This involved advance payment of both interest and capital and constituted an extremely significant event for the Peronist government: the use of debt capitalization mechanisms in the sale of the telephone company would prove to foreign creditors not only the authorities' will to honour their commitments, but also their capacity to do so.

<sup>1</sup> The remaining 5% belonged to two private companies: CAT (established in 1916) and CET (established in 1927), both subsidiaries of the Swedish firm Ericson. In the late 1980s, CET was acquired by CAT.

Secondly, all over the world telecommunications equipment and services suppliers and their major customers were pushing for a change in the regulatory framework and for a type of privatization which would allow them to explore the new possibilities opened up by the evolution of the sector at the international level (Herrera, 1990). On the one hand, the spread of microelectronics in the industry had relativized (in some subsectors) the importance of economies of scale and created opportunities for investment both in the production of new equipment and the supply of new kinds of services; this—in the eyes of certain companies and major customers—called into question the functionality of the current regulations, which had been designed to control a monopolistic market offering almost exclusively “traditional” voice transmission services. On the other hand, in the headquarters of the most important equipment suppliers, it was perceived that the investments made in the light of the “technology race” had created large amounts of idle capacity (in some cases due to overestimation of the growth potential of the respective markets), and it was sought to reduce this

idle capacity by expanding exports of the latest generation of products. The success of such a competitive strategy based on exports depended largely, in turn, on the possibility of changing the purchasing policy of the companies engaged in the provision of services, which still maintained protectionist attitudes with respect to a small number of suppliers. Finally, it is worth noting that in some developed countries the companies engaged in the provision of services opted for the transnationalization of their activities, which led them to support the privatization movement in those markets to which they sought to gain access.<sup>2</sup>

Thus, the fact that the transfer of ENTEL to the private sector was undertaken for the purpose of paying part of the foreign public debt and alleviating the short-term fiscal crisis, rather than solving the serious problems of the domestic telecommunications system, imparted some special features to the regulatory framework which emerged from the process, with important consequences both for consumers and for the structure of the domestic equipment supply industry.

## I

### The period prior to privatization

In the early 1980s, Argentina had less than 8.5 telephone lines per 100 inhabitants. In 1985, that figure rose to 10, thanks to a network expansion plan called Megatel.

Even though this level of “telephone density” was slightly higher than the average in countries with per capita incomes similar to that of Argentina, a large part of the population continued to be outside the network (which is unequally distributed both in terms of social sectors and regions) and the quality of service continued to be deplorable.<sup>3</sup>

At the same time, ENTEL—like most of the world’s telecommunications companies—maintained a positive operating balance, although it faced growing financial difficulties in expanding and modernizing its network. This situation led to high foreign indebtedness, since the prohibition of use of the local financial market by State companies made each new loan more expensive. The difficulty of financing expansion was, in turn, related to three factors. Firstly,

the ENTEL planning and work control systems suffered from policy discontinuity,<sup>4</sup> the absence of multi-year

<sup>2</sup> The most important case is that of the Baby Bell companies in the United States, not only because of their weight within the structure of the telecommunications industry at the international level (the North American market is equivalent to approximately half of the world telecommunications market), but also because of their ability to influence the United States Government in their favour.

<sup>3</sup> By way of example, according to data provided by the General Supervisor of Public Companies, in the late 1980s the percentage of faulty calls was double that considered normal by international standards and the annual average number of complaints was four times greater. Both local and interurban transmission services were deficient in this respect.

<sup>4</sup> For example, between March 1984 and October 1987 there were four Ministers of Public Works, four Communications Secretaries and three General Managers of ENTEL.

expansion plans<sup>5</sup> and work control systems, and the lack of coordination between the planning of customer hook-up<sup>6</sup> activities and equipment acquisition policy (Herrera, 1989). In this chaotic situation, ENTel could not even evaluate the price actually paid for each exchange,<sup>7</sup> and the connection of the thousands of lines acquired took years, weighing heavily on the company in the form of higher fixed costs. Secondly, ENTel's purchasing policy meant that it had to pay very high prices for equipment and construction work. Finally, the tariff structure for the services provided did not allow the State company to make up for costs due –among other things– to the perverse combination of policy discontinuity, administrative and management chaos,<sup>8</sup> and overpayment of subcontractors<sup>9</sup> and equipment suppliers.<sup>10</sup>

<sup>5</sup> The public network was not expanded gradually but rather in abrupt increments, because of the concentration of huge investments in brief periods (as extreme examples, in 1975 only 6 000 lines were installed, while in 1979 the figure was 200 000). Normally, the decision to undertake such investments and the selection of expansion objectives (in quantitative and qualitative terms) was in the hands of a very small group of political functionaries named by the current Executive, while the participation of engineers, technicians and other qualified personnel of the ENTel permanent staff was extremely sketchy, to such a point that sometimes their technical opinion was not even sought.

<sup>6</sup> This refers to the system of connections between customers and their respective telephone exchanges.

<sup>7</sup> For a number of reasons (lack of precise specifications for the goods and services to be acquired, indexing mechanisms, partial payment on reception of materials, etc.), the prices really paid by ENTel could be very different from those specified in contracts for equipment supply or construction works. See Herrera, 1989, pp. 121 – 123.

<sup>8</sup> Over a period of more than twenty years, the Supervisor of Public Companies only accepted ENTel's financial statements twice, and even then with reservations.

<sup>9</sup> In particular, the Union of Telephone Workers (FOETRA) has made numerous accusations of over-billing in respect of the subcontracting of work to install lines between the exchanges and subscribers.

<sup>10</sup> During the second half of the 1980s, under the Radical Party government, it was proposed that the issue of financing investments could be resolved by asking applicants for new telephone lines to pay for the new equipment in advance (up to that time ENTel had only charged connection costs). Under this system of payment, the Megatel Plan was launched (1985) with the aim of installing one million new lines in five years. The anticipated results, in terms of financing expansion of the system, were not attained, however, basically because the prices eventually paid for the equipment were very much higher than those foreseen when the Plan was launched.

From the industrial point of view, it is important to note the stability both of the duopolic structure of the domestic supply of telephone exchange equipment (with the domestic affiliates of the American company, ITT, and the German company, Siemens) up to the end of the 1980s, and the predominance of another group of transnational company affiliates in the production of public transmission equipment. In that situation, domestic capital had little opportunity to sell products directly to ENTel.

During the era in which electromechanical technologies prevailed, the State company's purchasing policy obliged supplier firms to maintain productive capacity within the country, although no specific conditions were imposed with regard to technology transfer and there were no particularly stringent requirements for the incorporation of domestic components in the products sold. Even so, the degree of domestic integration of the Argentine affiliates of telecommunications equipment producers reached a level of around 90% in 1973 (Argentina, 1986). A number of factors contributed to this situation: a competition strategy based on the reduction of costs; the adaptation of products and production processes to local conditions; the barriers raised against the entry of new competitors, exploiting the advantages of being first in the market; the financial capacity to maintain large margins of idle capacity over long periods;<sup>11</sup> and the possibility of persuading ENTel and other State companies to pay higher prices than those obtaining for the same equipment in developed countries.

In the early 1980s, ENTel's decision to incorporate semi-electronic and electronic exchanges in the system meant new criteria in the selection of suppliers. The most notable results of this change –in terms of the structure of domestic industry– were a radical setback in the levels of domestic content of production and the entry of Japanese firms into the Argentine telecommunications market. Moreover, for the first time price competition played an important role in the strategies of firms competing for the domestic market, even though ENTel still paid very much higher prices for digital equipment than those prevailing on the international market. In the

<sup>11</sup> The absence of multi-year equipment acquisition plans in ENTel made the ability to maintain high levels of idle capacity for long periods a key element in suppliers' competition strategies.

mid-1980s, however, after the Siemens affiliate acquired most of the shares of the ITT affiliate, the telephone exchange equipment market resumed its traditional duopolic structure, this time with the firms involved being the affiliate of the German company and an affiliate of the Japanese firm NEC, in association with a big domestic capital group.

In the late 1980s and early 1990s, the companies with plants in the country experienced a double threat to their relative position in the Argentine market. On the one hand, the Executive signed economic cooperation agreements with, among others, the Government of Italy, which meant that telecommunications equipment produced in that country would

now be imported into Argentina. On the other hand, in October 1987 the Radical Party government announced its decision to privatize ENTEL. I will not go into detail here on the ways in which each of the firms involved reacted to these changes in the environment in which they had been operating, but I do feel that it is interesting to note that they resorted to strategies of lobbying and the formation of cartels, seeking political support on the grounds that their continuance as ENTEL suppliers would guarantee not only the maintenance of domestic levels of production, investment and employment, but also further progress in the process of improving domestic technological capacity.

## II

### The privatization process

The origins of the privatization process lie in the measures taken by the military government in the 1979-1983 period, when several secondary or peripheral activities previously carried out by ENTEL were transferred to the private sector.<sup>12</sup> Later, the Radical Party government continued that policy of peripheral privatization—especially with respect to the contracting-out of the installation of lines between the exchange and the subscribers—and sold several value-added services, although it was frustrated in its intention to sell 40% of the ENTEL shares

to Telefónica Española.<sup>13</sup> At that time, privatization of the network was openly opposed by some parties of the Left and State workers, who even expelled from the telephone workers' union some members who supported privatization; equipment suppliers associated with the financial sector sabotaged the government's initiative by presenting themselves as candidates to be the future operators of the system, while in 1985 the Peronist legislators blocked the legislation needed to implement the project.

Subsequently, however, under the Peronist government, the effective transfer of ENTEL to the private sector was effected on 8 November 1990, only three months after the Decree regulating the privatization process was signed. To achieve his goals, the President of Argentina legislated by means of Decrees, making use of the extraordinary powers which

<sup>12</sup> Among the most important of these privatization measures were those involving work on the installation of lines between the exchanges and subscribers and others involving systems of financial collaboration whereby—in certain localities of the country—the private sector could be responsible for the purchase of land, construction of the telephone exchange building, the installation of telephone exchange equipment and long-distance links, and the construction of the networks of lines to the subscribers.

<sup>13</sup> The proposal of the Radical Party government, which was paralyzed in the National Congress by Peronist legislators, provided for the sale of 40% of the ENTEL shares to Telefónica Española, which would pay US\$750 million for them (with a margin of variation of 20%). Of the US\$750 million, two-thirds was to be paid in cash (US\$200 million within the first year and the rest in 30 months) and the remaining third was to be paid through debt capitalization mechanisms. The proposal of the Spanish firm required that the mixed company thus formed would retain monopoly control over all services, but would not be obliged to provide public telegraph services nor to attend the population of remote localities.

the Peronist and Radical legislators had given him (Petrazzini, 1991) and invoking the Economic Emergency and State Reform laws, which had opened up the possibility of privatizing public service companies.

The basic mechanism for privatization consisted in dividing the company into two regions (North and South) and auctioning 60% of its total stock package,<sup>14</sup> with a fixed minimum price.<sup>15</sup> The auction would be won by those who offered the most Argentine foreign debt paper in payment, over the minimum price (the minimum amount acceptable was 3.5 billion dollars for each zone).<sup>16</sup>

The sale of ENTEL led to the formal creation of four new telecommunications companies. Telecom Argentina (Telecom) and Telefónica Argentina (Telefónica) offer basic telecommunications services throughout the country, while they also own equal shares of the other two companies: TELINTAR, which provides international services, and STARTEL, which offers the so-called "services under a competitive regime" (mobile radio-telephony, mobile maritime radio services, telex, and data transmission within the national territory).<sup>17</sup>

With regard to the sectoral regulatory framework for this change, three aspects should be noted: firstly, although a majority of Deputies and Senators

say that they agree on the need for a new telecommunications law, the National Congress has yet to approve one.

Secondly, in the first half of 1990, the Communications Secretariat—responsible until then for the drafting and execution of national policy for the sector and for control of the companies operating in it—became a Sub-Secretariat,<sup>18</sup> but on 31 January 1991 that Sub-Secretariat was dissolved and its approximately 400 employees were dismissed. Thus, the State was left with virtually no technicians with experience in the field of telecommunications. The re-establishment of a Communications Sub-Secretariat, many months later, did not change that situation.

Thirdly, a few months before the sale of ENTEL, but several months after the conditions for private sector acquisition of that company were established, the National Telecommunications Commission (CNT) was set up (June 1990) to serve as a regulatory and control body.<sup>19</sup> However, more than a year after the State monopoly disappeared, that Commission, which lacks human and financial resources, is conspicuous by its absence in the definition of the main aspects of present and future domestic telecommunications policy. On the one hand, none of the significant disagreements which have arisen between the State and private firms in the past year have been settled in the CNT. On the other hand, the users of the public network find themselves totally defenceless (for example, the CNT has been unable to force the companies to give way in some clear cases of over-billing for services).

In this context, in order to make some prospective conjectures with respect to this sector it will be necessary to analyse in greater detail the characteristics of the consortia which acquired parts of the ENTEL package and to study the fine print of the transfer contracts which they signed with the Argentine State.

<sup>18</sup>The Ministries of Economy and of Public Works and Services were merged to form the Ministry of the Economy and Public Works; the Public Works and Communications Secretariat came under this new Ministry and, in turn, was responsible for the Communications Sub-Secretariat.

<sup>19</sup>According to its terms of reference, the CNT is to regulate, control and oversee all telecommunications services, administering the radio frequency spectrum (except for radio broadcasting) and ensuring compliance with the conditions established by the State for the companies which purchased ENTEL stock (tariffs, mechanisms for selecting equipment suppliers, quality and network expansion goals, etc.). It is also responsible for protecting the public interest, defending customers, and certifying equipment.

<sup>14</sup>The remaining 40% was sold later to company personnel (10%), telephone cooperatives (4.8%) and the public (25%).

<sup>15</sup>This minimum was US\$100 million for the Northern region and US\$114 million for the Southern region, to be paid in cash on taking possession, plus a somewhat higher sum (US\$228 million for both regions) in six-year promissory notes, with a three-year grace period.

<sup>16</sup>The consortium which bought the Northern region offered US\$2.308 billion in debt paper, while that which bought the Southern region offered US\$2.72 billion (reference is always to the nominal values of the debt, including the corresponding interest). In the secondary market, this paper was valued at around 12% of its face value, and payment of the principal was scheduled for the twenty-first century. In this regard, it is interesting to note that: i) for the 30% of shares of the Southern region sold later, more than US\$800 million in cash was received, and for the 30% corresponding to the Northern region, US\$1.2 billion; ii) this later sale changed the composition of the consortia (for example, in the case of Telecom, the participation of the domestic group Pérez Companc increased by around 5 percentage points).

<sup>17</sup>For its part, Telecom Argentina acquired 160 000 lines from CAT (see note 1) for US\$67 million (*Ambito Financiero*, 25 February 1992).

### III

#### Features of the purchaser consortia and the transfer contracts

The participants in Telecom Argentina are STET, *France Cables et Radio*, the Pérez Companc group, and the Morgan bank, while the participants in Telefónica Argentina are Telefónica de España, the Techint group and Citibank. Thus, each of the consortia which dominate the domestic telecommunications market are made up of at least: i) a large European State company, linked in turn to several equipment suppliers; ii) one of the main creditor banks of the Argentine foreign debt; and iii) a large domestic economic group.<sup>20</sup>

The domestic economic groups forming part of these consortia<sup>21</sup> grew up as State suppliers (mainly in the construction sector, but also in telecommunications) and are among the principal beneficiaries of State subsidies to domestic industry. Moreover, being among the private companies with the highest absolute levels of foreign debt, they supported the proposal in the early 1980s to make private foreign debt a State responsibility, so that they played a significant part in the State indebtedness which it was proposed to pay off through the sale of ENTel.

By purchasing 60% of the shares of ENTel, the consortia acquired the company's assets (f.c.c. of nearly all of the US\$1.5 billion debt, which was taken over almost entirely by the State); licenses to provide services for an indeterminate period; and monopoly rights for seven years (extendable to 10) over basic domestic services in the corresponding regions (Southern for Telefónica and Northern for Telecom) and all international services (telephone, data transmission, Telex, and value added services, etc.). Moreover, through STARTEL, which inherited the ARPAC network from ENTel (for data transmission through package processing), they can operate in

the second band of mobile cellular telephones and offer domestic data transmission, telex, etc. services, since in this latter area there is no prohibition against the entry of new firms.

The acquisition of the mobile cellular telephone services<sup>22</sup> warrants special comment, since in February 1992 conversations about that service between the private consortia and the Ministry of the Economy were publicly revealed. That Ministry, against the opinion of Telecom and Telefónica, maintained that the second band of mobile telephone services (the MOVICOM firm already operated in the first band, prior to privatization) should be awarded on the basis of bidding.<sup>23</sup> Agreement was reached at the end of February: the consortia could offer that type of service without having to take part in a bidding contest, but in return they must agree to make an average 3% reduction in their charges for mid-range and long-distance communications, and they must also accelerate the previously agreed timetable for price reductions in respect of new telephone lines (*Página 12*, 1992).

With respect to this latter point, it should be noted that: i) the 3% reduction is insignificant in view of the fact that long-distance and international tariffs in Argentina are generally very much higher than the average rates in developed countries for the same services, which, in turn, bear no relation to service costs and reflect extremely high surcharges; and ii) the reduction in respect of the installation of new lines—the price of which is also extremely high—would probably have occurred in any case because, at those high prices, the demand for new lines would not have been in line with Telefónica's and Telecom's plans for network expansion.

<sup>20</sup> For more details on the relation between the big domestic economic groups and the privatization processes, see Verbinsky, 1990.

<sup>21</sup> In some cases, they associated themselves, either directly or indirectly, with the private service company which is now a member of the consortium (Acevedo, Basualdo and Khavisse, 1991).

<sup>22</sup> At the international level, this sector is changing the whole shape of the industry, and many specialists believe that it is the spearhead for the introduction of competition in the network.

<sup>23</sup> The position of the Argentine Minister of the Economy was publicly and emphatically supported by the United States Ambassador in Argentina, who stated that it was his duty to defend the interests of United States companies, such as Motorola, which wished to enter the Argentine mobile telephone market.

## IV

## Concrete results and potential instability

In addition to acquiring assets, licenses and monopoly rights to provide basic domestic and, especially, international services, the consortia have also taken on a number of commitments. These are not expressed in terms of obligatory investments, but rather as the obligation to achieve certain levels of service quality and physical network expansion goals. If the contract conditions are fulfilled, by the end of the century the Argentine network will have a million or a million and a half more telephones,<sup>24</sup> together with substantial improvements in the quality of services (measured, for example, by the number of calls actually completed, repair time delays, etc.), even though it will still be operating far below the average efficiency of European or North American networks.

With respect to the expansion goals proposed, it is necessary to take into account: i) the feasibility of attaining those goals; ii) the possible sources of the financing needed to reach them; and iii) the likelihood that the State really will ensure that the original contractual conditions are respected after the transfer to the private sector.

With respect to the first point, internationally there is a very high correlation between teledensity (the number of lines per 100 inhabitants) and the per capita gross domestic product.<sup>25</sup> As noted above, after the Megatel Plan was launched, Argentina reached a teledensity of approximately ten lines, a figure slightly higher than the average for countries with similar per capita GDP. On the other hand, the number of applications to join Megatel has been somewhat below government expectations. It may be assumed that putting another million lines on the market would be a resounding failure for lack of

demand, unless there were a significant increase in real wages, a considerable reduction in hook-up prices, or a real boom in economic activity. In view of these facts, everything seems to indicate that the consortia will find it hard to attain the expansion goals to which they are committed unless they are willing to lower the hook-up prices laid down in the transfer contracts.<sup>26</sup> At all events, to the extent that the expansion strategy adopted by the consortia is centered on the digitalization of the existing installations in order to be able to offer the higher-income sectors improved access to the network—and particularly to special and international services—the rate of expansion of the network will be partially conditioned by the extent and speed with which the business community changes the role of telecommunications within the production process, by moving towards new ways of organizing production, marketing and distribution which make greater use of informatics (Herrera, 1992).

With regard to the investments which the firms must make in fulfillment of their contracts, five aspects may be mentioned. Firstly, during the first three years the companies can charge applicants for new lines between 50% and 100% of the direct costs in advance.<sup>27</sup> Secondly, the authorized scales of charges are sufficiently high to allow for a reasonable level of self-financing of investments. Thirdly, the consortia received 295 000 lines which had been bought by ENTel before the transfer but had not been connected (debts to equipment suppliers for

<sup>26</sup> In fact, hook-up prices for new lines were recently renegotiated. This may benefit the consortia, because for a certain length of time—sufficient to cover the demand from the higher-income sectors—the old and very high rates will be in effect, while later the reductions will make it possible to capture an intermediate segment of the market which, although unwilling to pay very high hook-up prices, may be able to pay the current high charges for telephone calls.

<sup>27</sup> Up to 50% can be charged in respect of home service, while for other types of service the maximum is 100%. The concept “direct cost of a line” includes, in addition to the cost of telephone exchange equipment and access to the interurban and international networks, such items as a proportion of the cost of land and buildings, energy, etc. After the third year, instead of cash payment they must take out a debt instrument in dollars, due in five years from the date of issue, with an interest rate of 7% per annum.

<sup>24</sup> When ENTel was transferred to the private sector, it had 3 500 000 telephone lines and two ground stations (Balcarce and Bosque Alegre) for satellite communications. Only 3 100 000 of those lines were functioning, however.

<sup>25</sup> Obviously, the teledensity/GDP ratio is only one indicator of network development, and it is insufficient because it reveals nothing about the possibility of access to the network by the various social sectors, nor about its geographical distribution, nor about maintenance of the infrastructure which ensures effective access to services (Noguera, 1991).

that purchase were assumed by the State). Of that total, Telecom and Telefónica can sell 205 000 lines<sup>28</sup> to the public at prices of between US\$1 000 and US\$3 000, and the corresponding connections will be taken into account in the State evaluation of the fulfillment of network expansion goals. Fourthly, connection of the lines acquired through the use of the nearly US\$200 million in credits granted by the governments of France and Italy in negotiations with the Argentine government prior to the transfer<sup>29</sup> will be accounted for in the same way. Finally –an issue to which I will return below–, the companies can finance the expansion of the basic network with income from international services, over which they exercise monopoly rights.

Before referring to the possibility that the conditions for the provision of services stipulated in the contracts which transferred ENTEL to the private sector can be maintained, I will make some observations on the structure and level of tariffs in order to make it easier to understand why I believe that those agreements are intrinsically unstable.

According to the terms of the transfer contracts, during the first two years the private firms can adjust the tariffs for basic local, national and international services monthly in accordance with the consumer price index (CPI), and they can also vary them in dollars when substantial changes occur in the real exchange rate (the initial tariff was 4.2 US cents per unit in November 1990).<sup>30</sup> During the following five years, tariffs are to be reduced by 2% per annum in

<sup>28</sup> The other 95,000 lines had already been paid for by customers to ENTEL before the transfer. There are another 105,000 unconnected lines which it would be reasonable to maintain in reserve for technical reasons.

<sup>29</sup> To a large extent, the conditions for the use of those credits oblige the consortia to buy equipment from companies connected with firms which are members of the consortia. For example, the suppliers which are beneficiaries of the Italian credit include Techint and Italtel.

<sup>30</sup> Between 8:00 a.m. and 8:00 p.m. from Monday to Friday, and between 8:00 a.m. and 1:00 p.m. on Saturdays, the length of a unit for local calls is two minutes; at other times, it is six minutes. For long distance calls, the length of a unit varies with the distance and the time the call is made. Moreover, residential customers pay a fee of 274 units in advance every two months, while commercial customers pay 2 460 units. This fee gives them the right to make additional calls equivalent to 200 and 330 units, respectively, at no additional charge during the following two-month period (this applies to customers in areas of high telephone density), so that the tariff system penalizes those who use their telephone less. The original set of tariff rates may be adjusted when the devaluation rate of the dollar is more than 25% greater than monthly inflation, either in a single month or in three months, cumulatively.

real terms. After the period of exclusivity, there will be no price controls as long as there is real competition.<sup>31</sup> The private companies may transfer to their prices all taxes, rates and national contributions that they must pay, with the exception of the profits tax.<sup>32</sup> In order to gain an idea of the size of the tariff increase with which the private consortia began their operations (4.2 US cents per unit), it may be recalled that from the beginning of 1985 up to a couple of months prior to the privatization, the average quarterly price per unit was never more than 220 Australs (at March 1990 values) and was always less than 1.5 US cents. In March 1991, however, the average rate was 380 Australs or nearly 4 US cents (at March 1990 values). As for the prices for interconnections and use of the public network by other telecommunications service suppliers, the contracts stipulate that Telefónica, Telecom and TELINTAR must charge normal and non-discriminatory prices, though they do not spell out the criteria for determining normality and non-discrimination.

These two problems in respect of tariffs (customers who must pay very high rates and potential competitors of STARTEL who could be paying discriminatory connection charges, to the detriment of effective competition)<sup>33</sup> are a very important source of potential conflict. The situation could have a negative impact on both private users and on firms in general, especially transnational companies, which make heavy use of the services or which plan to expand their activities as suppliers of telecommunications services in the domestic market.

<sup>31</sup> The reference point is the consumer price index. If the rights to exclusivity are extended for three years, tariffs are to be reduced by 4% per annum in real terms during that period.

<sup>32</sup> It is important to note that because of the privatization the State will cease to receive revenue from a tax equivalent to 30.4% of the value of a call unit which ENTEL charged its customers and which was intended to help pay pensions. Moreover, the government guaranteed the companies that the tariff scheme would be maintained and, in the last instance, it promised to pay them compensation if it found itself obliged to intervene for any reason by lowering the price of telecommunications service. As a final safeguard, if the authorities were to decide not to pay that compensation, the companies would acquire the right to adjust rates every six months for the first two years, so as to ensure a profit margin of at least 16% over the fixed assets in use.

<sup>33</sup> See Noan (1989) and Heim and Yarrow (1988).

Maintaining this regulatory scheme, which made business communications so expensive and kept powerful oligopolistic international companies out of the Argentine market was not viable, and finally the facts spoke for themselves: hardly anything remains of the original contracts as far as tariffs are concerned. The new agreement—signed on 28 November 1991, nearly eight months after the privatization—reduced the price of business telecommunications, at the expense of residential users, so that Telecom and Telefónica would not suffer.

This new tariff agreement<sup>34</sup> was ratified by Decree and was basically reflected in the following changes:<sup>35</sup> i) tariffs were dollarized and raised by 1.3% over the rates in effect at the time of signing the new agreement, and it was agreed that they would be adjusted in the future twice yearly—on April 1 and October 1—according to the United States consumer price index;<sup>36</sup> a system of gradual reduction of hook-up prices, beginning in November 1992, was established, to culminate in 1997 with the equalization of residential and business prices at a level not exceeding the average current price in countries with mature networks;<sup>37</sup> iii) an increase in basic fees was introduced which favoured business users to the detriment of residential customers, with a probably neutral impact on Telecom and Telefónica income from monthly fees (for residential customers, the number of call

units made available at no additional charge over the monthly fee was reduced<sup>38</sup> and the monthly fee itself was raised, while the minimum monthly cost of commercial lines was lowered),<sup>39</sup> and iv) renegotiation of the entire tariff structure was promised, with a view to lowering the cost of telecommunications for the business sector and at the same time increasing residential prices in such a way that overall Telecom and Telefónica will not suffer from those tariff modifications.

There is an peculiar feature of the privatization of telephone services in Argentina which is not unrelated to the subsequent renegotiation of the tariff structure. Thus, the transfer contracts do not propose the separation of international from domestic services, which would create the possibility of allowing the entry into the market of companies previously excluded and avoid a situation in which users of international services would subsidize the rest; on the contrary, the contracts allow Telecom and Telefónica to dominate local, national and international telecommunications simultaneously and authorize them to finance expansion of the network through crossed subsidies for ten years, using TELEINTAR income for that purpose. The results have also been rather unusual: as noted above, privatization began with sharp price increases in real terms for all services, instead of the anticipated reductions in the price of international services and increases in local services (as in other countries). This policy, which sparked angry protests, especially on the part of some big users of the system, has placed the telephone consortia in an excellent position for the subsequent renegotiation of relative prices.

In order for the Argentine State to be able to closely monitor the evolution of the cost structure of the consortia and thus be able to know what kind of tariffs could prevent cross-subsidies or discrimination against potential competitors of STARTEL, firm political will (which the government has not yet shown) and a team of qualified technicians devoted

<sup>34</sup> Tariff levels have been a bone of contention between the government and the consortia ever since 1 April 1991, when the Law on the Convertibility of the Austral was promulgated, prohibiting price indexing throughout the country and requiring that tariffs—calculated in dollars—be returned to the August 1990 level. The government was not able to achieve full compliance with this law on the part of the telephone companies, and in the end the price per call unit was lower than that which would have resulted from the application of the formula established in the contracts, but was 21.5% higher than that prescribed by the Law on Convertibility. For their part, the companies declared that, if they considered it opportune, they could, in the future, demand the tariff increases (even retroactively) which they were now giving up, but to which they would have been entitled under the transfer contracts if the Law on Convertibility had not intervened. At that same time, moreover, the value added tax collected through telephone tariffs was lowered from 16% to 11%.

<sup>35</sup> See, in this respect, Telefónica Argentina (1991).

<sup>36</sup> The price per call unit was raised by 1% on 1 April 1992.

<sup>37</sup> That average is estimated at US\$250. For the coming fiscal year, hook-up charges will be US\$1 800 for business and US\$900 for residential customers.

<sup>38</sup> By 39.4% for those in areas with more than 200 000 telephones, for example.

<sup>39</sup> The monthly fee for residential customers in areas with more than 200 000 telephones was raised by 46%, while it was lowered for business customers in similar areas.

to the attainment of this objective are needed.<sup>40</sup> It is worth recalling that dismantling the technical capacity of the State in the area of telecommunications was

a preparatory step for the sale of ENTel shares (dissolution of SECOM, dismissal of its technicians, creation of a spurious CNT).

## V

### Effects of the privatization of ENTel

Finally, I will address the effects which the privatization of ENTel has had and will continue to have on the telephone equipment supply industry. Inasmuch as the bulk of the demand for telephone equipment comes from the companies operating the networks, the transfer of the networks' assets to the private sector could lead to a veritable earthquake among the suppliers already established in the country, which could suffer severe damage to their relative positions in the domestic market.

The consortia which acquired ENTel are under no obligation to purchase equipment from any particular firm,<sup>41</sup> although they are obliged to make acquisitions by public tender when their purchases amount to more than US\$500 000 per year, giving preference to companies with plants in Argentina, if their prices are not more than 10% higher than those of other companies (the 10% clause). Moreover, they are obliged to respect several purchase commitments

made by the State during the months prior to the privatization (including those deriving from the credits granted by the governments of Italy and France). With regard to future purchases, Telefónica and Telecom are not allowed to supply their own equipment to end-users, although they may supply, install and maintain equipment made by others, in competition with other firms. Such equipment must have been approved by the regulatory authorities, and all producers of approved equipment have the right not to be subjected to discrimination in their dealings with Telefónica and Telecom.

In fact, the 10% clause alone could cause more political problems than a policy of real protection of those industries installed in the country. If anything was proved by the decades of implementation of the "Buy National" regime, it was that it is perfectly feasible to arrange public tender contests in such a way as to exclude certain suppliers. Although at this time it is difficult to predict the future composition of the domestic public equipment supply market, it may be expected that the combined effects of the technological revolution, underdevelopment and privatization will probably lead to a considerable structural (rather than merely transitory) decline in the levels of domestic content in the production of telephone exchange equipment.

At all events, if the experience of the past year is generalized and projected into the future, a trend may be observed towards the introduction of at least a third supplier, while purchases will continue to be made from those companies which were the principal suppliers of the State company,<sup>42</sup> even though they are not linked to one or another of the members of the consortia. The maintenance of such purchases,

<sup>40</sup> This task is particularly complicated because the combination of rapid technological progress with the privatization process has generated marked informational asymmetries, to the detriment of the State's power to control developments. The government itself recently stated that the sale of 30% of the shares of Telecom (which only took place in March 1992, although it had been announced for December 1991) was delayed because it had not been able to secure from the Board of Directors of Telecom Argentina the data on the economic and financial evolution of the company needed for the preparation of a prospective balance-sheet for future shareholders. For its part, the company denied the government's statements, maintaining that its reluctance to collaborate in the sale of the remaining ENTel shares was related to difficulties in reaching agreement on the tariff issue. (*Ambito Financiero*, 1991 and *Clarín*, 1991).

<sup>41</sup> ENTel's traditional suppliers pressured that company, in the final months prior to privatization, to accept advance deliveries of material and equipment, with no regard to previously established schedules, but rather so that the State would assume the commitments arising from those deliveries. In some cases, this benefited the consortia in two ways: on the one hand, because ENTel bought equipment from firms related to them, and on the other, because this increased the stock of assets which they received.

<sup>42</sup> Although they may be given a relatively smaller share, at notably lower prices.

even apart from the formal commitments made with the government, is probably related to two types of considerations. On the one hand, it may be politically expedient to avoid confrontations with companies which have considerable lobbying capacity with the government authorities, thus avoiding "making waves" until the private operators are firmly established and they have completed their negotiations on the sectoral regulatory framework. At the same time, importance will probably be attached –at least temporarily–to the economies deriving from the need to ensure compatibility of equipment and to acquire detailed knowledge of the characteristics of the domestic network, as well as the possibly greater capacity of firms already established in the country to respond without delay to a substantial increase in demand.<sup>43</sup>

Within this context, the most likely outcome is that the transnational equipment suppliers will decide, quite apart from the strict logic linked to the evolution of their cost structures, to maintain their plants in the country as an element of political pressure in the hope of gaining purchase decisions from Telecom and Telefónica,<sup>44</sup> even though they may be obliged to completely restructure their domestic production. Moreover, it must not be forgotten that

the transnational companies which operate within Argentina also do so in Brazil and, in some cases, in Mexico and other Latin American countries. Consequently, if those companies believe that, in the long term, the present government initiatives aimed at the creation of subregional trading blocs (Mercosur, for example) will be consolidated, they may seek to restructure their operations in order to apply schemes for complementary production by their affiliates in the different countries and/or the elimination of redundant plants.<sup>45</sup>

Moreover, it is probable that in the coming years, even though tariff barriers will tend to fall, there will continue to be a place for small and mid-size local firms producing mechanical parts or components for equipment used in customer service networks and for end-user equipment, especially telephones, private branch exchanges, etc. Those companies will have the advantages of geographic proximity, the persistence of certain levels of tariff protection,<sup>46</sup> and lower costs in comparison with other companies which would be obliged to adapt their programmes and products to the conditions of the local network and the characteristics of the end-users (Herrera, 1992).

## VI

### Final comments

Perhaps the most noteworthy aspect of the Argentine privatization process is that, although it formed part of a strategy aimed, among other objectives, at ending State subsidies of economic activity and lowering the price of services through increased efficiency on the part of the companies offering them, it has

ended up generating a new mechanism of regressive resource transfer.

In fact, privatization was preceded by a generalized increase in charges, and moreover, since the guidelines laid down for the adjustment of such charges separated the prices charged from the cost

<sup>43</sup> Especially in view of the high levels of idle capacity which most of them still have. For an analysis of a similar situation in North American industry, see Herrera (1992).

<sup>44</sup> Similar strategies are being applied by the main equipment suppliers even in the Eastern European countries. For example, the German firm Siemens –one of the most important suppliers of the Argentine market– has set up mixed companies for the manufacture of equipment in Poland, Czechoslovakia, Romania, Hungary and the Ukraine, so as to put itself in a favourable position when it comes to competing for public telephone supply contracts. On 27 January 1992, that company announced an agreement to provide 12 new telephone exchanges in Poland, worth a total of US\$36 million (*The Economist*, 1992).

<sup>45</sup> It must not be forgotten that, in general, the decision to make direct investments in the production of public telephone equipment in Latin America was taken only in those cases in which that option was perceived to be a condition for access to the market imposed by national governments, since the small size of the markets in question meant that those investments were not economically justified even when electromechanical technology predominated (Herrera, 1992).

<sup>46</sup> Currently –in spite of reductions in the average level of duties for industrial products in general– tariff protection for the production of all types of end-user telephone equipment is very high, since end-users who wish to import them must pay tariffs of 50%.

structure, it is not even likely that increased private efficiency in the future will mean the lowering of prices for services to an extent that truly reflects those lower costs, given that the corresponding service licenses have given the consortia monopoly rights. In this sense, it is interesting to compare the recent agreement for the assignment of the second band of mobile cellular telephone service to STARTEL. It may be recalled that in return for this agreement, Telecom and Telefónica granted a discount of only 3% on the high international rates charged by TELEINTAR. Meanwhile, the international press had been giving permanent coverage to the complaints by North American, Japanese and European companies that in spite of the recent reductions and the fact that they are much lower than the Argentine rates, international telephone charges in most developed countries are 50% to 100% higher than the actual costs.

The private telephone companies, for their part, are not willing to pay the excessively high prices with which ENTel favoured its equipment suppliers. This means that, quite apart from the transfer of resources from customers to the consortia through higher prices, there is another transfer from the equipment producers to Telecom and Telefónica, TELEINTAR and STARTEL, through the lower prices that the latter pay for their equipment.

Consequently, privatization has not eliminated the old mechanisms of the regressive transfer of resources, but only given them a new form.

Another central objective announced by the government authorities which is far from being achieved is the transformation of the sector through the beneficial mechanisms of competition. If some of the conditions established in the ENTel transfer contracts are maintained, it is probable that in ten years' time (when the monopoly rights of Telefónica, Telecom and TELEINTAR are supposed to end), far from the entry of new capital, there will simply have been consolidation of the dominant position of the present consortia in the provision of basic national services and all international services, with very few new firms having emerged in the area of domestic value-added services.

With regard to the possibilities of the appearance of effective competition now or within ten years, the following should be noted: i) the presence of two firms providing basic services (Telecom and Telefónica) does not of itself create a situation of competition, since each company exercises monopoly

control over different areas of the country; moreover, their rates are established on the same basis and are adjusted by the same indexes so that, at least in terms of prices, there probably could not even be "competition by comparison"; ii) economies of precedence are very important in the telecommunications industry; this means that the first company to enter a market has competitive advantages over others, both because of its knowledge of the characteristics of demand and of the installed network and because it can impose its own technical standards, with which others entering the market later must conform; iii) the fact that the firms can operate simultaneously in subsectors which are still natural monopolies or oligopolies and in others which may be potentially competitive, opens up the possibility of using cross-subsidies as a way of impeding competition; and iv) the private consortia can impose discriminatory conditions of access to the basic network on independent operators who wish to compete with them in important areas.

All this reveals the potential instability of the regulatory framework created in the privatization process. At the present time, the losers have been not only residential users, who do not currently seem to have much chance of changing the situation in their favour, but also the big users of international services (affiliates of transnational corporations, news agencies, the financial system, etc.); potential suppliers of all kinds of international services whose expectations that privatization would allow them to enter the market have been frustrated; domestic value-added service suppliers, who have been forced to accept the conditions for connection to the network imposed by the dominant consortia, and equipment suppliers who have lost ground in the Argentine market. It is reasonable to suppose that the mobilization of this set of interests against the monopoly powers of Telecom and Telefónica (which has already begun) will not be content with the relatively marginal modifications made after ENTel was transferred to the private sector and will, in the mid- or short term, achieve a redefinition of the current regulatory framework, at least with respect to conditions of access to the international telecommunications market.<sup>47</sup>

<sup>47</sup> In this regard, it is worth recalling that the United States Government aims to reduce the income received by Latin American operators for processing calls from abroad. If these pressures by the United States are successful, this would be a serious reverse for TELEINTAR.

To sum up, it can be stated that the continuation of the current regulatory framework would mean the consolidation of the duopoly beyond the time limits established for exclusive rights, and some of the most powerful sectors most severely affected by the Telecom and Telefónica monopoly in the market have already begun to react. The potential for conflict implicit in the current legislation is somewhat attenu-

ated, however, by the sluggishness of the national economy, which helps to keep the demand for telecommunications services relatively low. If the economy began to register sustained growth, however, this would be incompatible with the maintenance of the current legislation and the stability of the relative position occupied by the consortia which dominate the market today.

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## Rationalizing social policy: evaluation and viability

*Ernesto Cohen and  
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In this article, it is argued that only a small fraction of social expenditures actually reaches the poor. Diverse social policy weaknesses which account for leaks and ineffective use of resources are reviewed, and the authors maintain that it will only be possible to overcome those deficiencies if serious *ex ante* and *ex post* evaluations of social programmes and projects are made.

Three different analytical procedures are then discussed: cost-benefits; cost-effectiveness; and impact evaluation. A methodology is proposed which seeks to take advantage of all three approaches: cost-impact analysis, which takes into account the special features, especially those connected with public investment, which make social projects different from other types of projects. The establishment of information systems (also called social project data banks) for the evaluation of social projects is proposed, and the differences between these and other similar systems are noted.

Finally, the possibility of using the proposed instruments to rationalize social policy is analysed.

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## I Social policy weaknesses

Social policy in Latin America today faces a crucial problem: the low proportion of resources allocated to aid the poorest sectors. A few examples will suffice to illustrate this problem. In 1987, only one dollar of every 7.83 dollars spent on social programmes reached the poorest 20% of the population in Chile, a country which for several years had made significant efforts to focus expenditure on that sector (Haindl, Buvinic and Irrázaval, 1989). Likewise, in a confidential report it was asserted in respect of another country of the region that the suppression of all the current social programmes would not give rise to any change in the living conditions of the poorest 50% of the population.

What is the reason for this? There are two basic reasons. On the one hand, social policy has concentrated mainly on dealing with other groups: as argued in another paper, social policy is not only for the poor. On the other hand, the ineffectiveness observed is due to the prevailing social institutions, the way in which programmes are designed and implemented, and leakages which occur in those programmes.

The Latin American State provides social services through a fragmented network in which functions and services are often duplicated. This means that resources are wasted and that only a small portion of them reaches those who should be beneficiaries. It has been calculated that, in some programmes, the effective transfer to the poorest groups does not exceed 5% of the overall budget, with the rest being absorbed by bureaucratic expenses or leakages to other groups.

The common and reassuring conviction that social programmes and projects always generate at least some benefits also creates problems. It assumes that, if there is supply, there must also be impact, which will grow with increased supply. However, that correlation is not always linear. Sometimes there is only an impact when a certain threshold is passed in the provision of goods or services. The evaluation of a school nutrition programme revealed that it began to have an effect only when the daily ration exceeded 770 calories per child, which only occurred in 17% of the schools involved in the programme. When the rations provided were smaller, those resources were simply being wasted.

The investment-impact ratio is conditioned by many decisions. Results depend not only on proper selection of the beneficiary group (focussing), but also on that group's economic, social and cultural capacity to participate in the programme, and on whether or not the quantity and quality of the goods and services provided are appropriate.

A very common error which hinders the achievement of positive investment-impact ratios in practice can be observed in school lunch programmes with nutritional objectives. Universalism is commonly applied as the allocation criterion. Similar rations are given to all the students in a class, when it would be more appropriate to take actions designed to solve a specific problem –malnutrition– which does not affect all the students to the same extent. If the beneficiaries of the programme are not initially suffering from nutritional problems, then in the best of cases the effect of the rations consumed will be nil, while in the worst cases the children will become overweight. As the resources are poorly allocated, they may not have any positive effects, or if they do, these will surely be less than those which could have been obtained had the same resources been concentrated on truly malnourished children.

Errors of programme design also occur when family survival strategies are not taken into account. Thus, it has been demonstrated that beneficiaries from families with unsatisfied basic needs suffer a worsening of their nutritional situation when they begin to receive nutritional programme rations. The reason is that those programmes provide a calorie-protein supplement which is not intended to replace the nourishment supplied at home. Since no steps have been taken to communicate information on the nature and aim of the services offered, however, the poorest families exclude those of their members who eat outside the home, when sharing out the available food.

Social programmes usually also pursue secondary objectives which lower the possibilities of achieving the main objectives. The resources of some social development funds are designed to cover the outlays necessary for "social investment", without considering recurrent costs, or else by stipulating that those costs are to be met by beneficiaries; in this

way, programme designers pursue something which appears to be reasonable, i.e., to promote commitment to the endeavour. However, the poorer the community is, the more remote is the probability that beneficiaries will be able to meet those expenses. Moreover, the decision to release such funds only in response to initiatives by the beneficiaries may lead to a situation in which they only benefit those who are aware of the availability of public funds and know how to negotiate administrative channels, which effectively excludes the poorest sectors. The same thing occurs when it is stipulated that the preparation of projects is the responsibility of the beneficiaries themselves, who in most cases are unable to perform that task. Likewise, bureaucratic inertia tends to allocate resources to the most easily reached areas, whose inhabitants are not usually those who are in the greatest need.

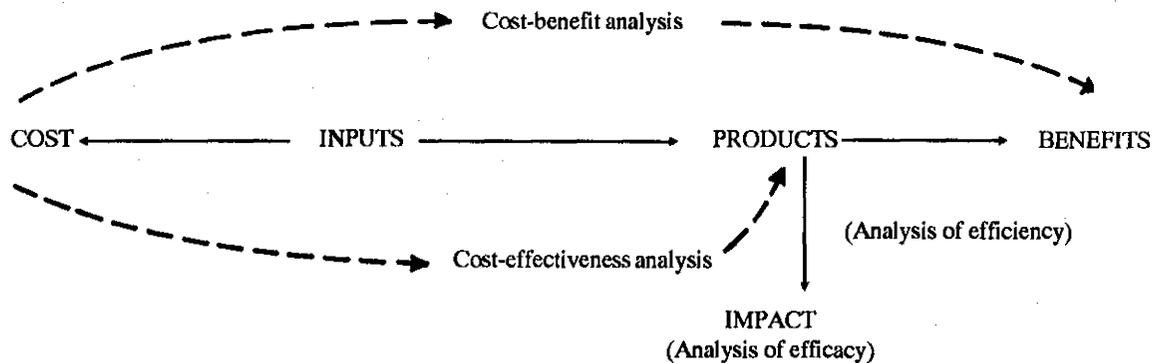
Programme and project execution decisively influences their impact. In that stage, situations often occur which lead to perverse results, even in well-designed programmes. This happens, for example, when those responsible for executing a programme designed to alleviate some crisis distribute the available food to a larger number of persons than those originally foreseen. As a result, everyone receives smaller rations which do not satisfy minimum needs, and if there are leakages to groups other than those originally designated, the impact of the programme is still further reduced.

It may be concluded from the foregoing that usually there is little or no knowledge of the real performance of programmes and projects embodying social policy objectives, and above all there is no knowledge of the impact of those activities on the population. Generally speaking, it is not known if those programmes are worthwhile or not; and if they are worthwhile, it is not known to what extent they help or to what degree they are justified. Moreover, it is not known who really benefits from them, or who is adversely affected.

It seems essential, therefore, to rationalize present-day social policy by increasing the efficiency of resource use and the effectiveness of programmes and projects. Only in this way will it be possible to satisfy the most pressing needs of the most vulnerable groups.

Figure 1

**PROJECT FLOW AND THE APPLICATION OF COST-BENEFIT  
OR COST-EFFECTIVENESS ANALYSIS**



Source: Adapted from D. Piachaud, *Cost-benefit techniques and social planning*, J. Midgley and D. Piachaud, *The fields and methods of social planning*, New York, St. Martin's Press, 1984.

## II

### The need to rationalize

In the field of social programmes and projects, rationalization is based on evaluation. Rationalizing means achieving optimum allocation of available resources—which are scarce, by definition—in order to achieve the proposed objectives. This is possible only if projects are evaluated in order to know both their costs and the impact they produce.

First of all, it is necessary to clarify a very frequent semantic confusion deriving from the different meanings of the term “social” as employed in connection with two different methodologies: the social evaluation of projects and the evaluation of social projects. In the former, the term concerns the spatial (national) area which defines the framework within which the evaluation will be performed. In the latter, on the other hand, the term is used to define the specific condition (social) of the object of the analysis (project).

Social projects can be evaluated using various methodologies, each of which has its own advantages and limitations. Figure 1 illustrates the differences among them.

#### 1. Cost-benefit analysis

Cost-benefit analysis makes it possible to determine and compare project profitability by comparing the updated benefits and costs to be derived from execution of the project.<sup>1</sup> In order to perform this analysis, it is necessary to define an initial situation (without the project) and another one with the project.

<sup>1</sup>“Since resources are limited, it is necessary to choose between competing uses; project analysis is a suitable and comprehensive way of evaluating options. In essence, it weighs project benefits and costs and reduces them to a common scale of measurement. If benefits exceed costs according to that scale, then the project is acceptable; if not, the project should be rejected. In weighing the merits of different projects, the objectives of each society should be kept clearly in mind. In other words, project costs and benefits should be measured comparatively in terms of how far they help or hinder the achievement of the objectives of that society” (Squire and van der Tak, 1980).

The evaluation can be at the private level, if it concerns a specific economic unit whose costs and benefits are valued at market prices, or it can be social, if what is sought is a comparison of the relative contributions made to society by various projects involving investment in some economic sector. In this case, the benefits and costs must be valued in terms of accounting units, efficiency or social value. For cost-benefit analysis, it is essential that both costs and benefits be expressed in monetary terms.

It may happen that the private evaluation of a given project indicates a loss, whereas its social evaluation indicates that it enhances the well-being of the community.

There are two methodologies for social evaluation. The first, known as economic or efficiency evaluation, determines the profitability of a project through the correction of current prices in imperfect markets by transforming them into those which would obtain in conditions of perfect competition (Fontaine, 1984). In this case, income distribution is an aspect on which the evaluator does not give an opinion. The comparison of costs and benefits is performed without considering who bears the former, nor who receives the latter.

The second methodology, which represents social evaluation proper, explicitly incorporates the issue of distribution, assigning a central role to the target population of the project and to those who will receive benefits from it. This type of evaluation must be linked to planning, in order to reflect the current policies in the form of concrete criteria for the analysis of public investment. The integration of efficiency and equity means that it is a valuation at "social prices" (Squire and van der Tak, 1980).

In economic projects, evaluation is usually *ex ante*, since what is sought are findings which will guide the decision to implement the project or not. *Ex post* evaluations based on cost-benefit analysis may also be carried out, however. This type of evaluation, which is particularly useful for social projects, seeks to determine the usefulness of continuing projects or the appropriateness of undertaking other projects of the same type. Even when evaluating projects where political considerations prevail, "cost-benefit analysis clarifies the question of value, that is to say, what those responsible for establishing policy are willing to pay (or to give up) in order to

achieve a certain type and level of benefits" (Weiss, 1982, p. 110).

Sometimes, monetary value is assigned to the extra-economic objectives of social projects, on the assumption that they are means for achieving an economic goal. The underlying reasoning is that the results obtained by these educational, nutritional, health and other projects will increase the beneficiaries' future income by a certain amount. Another way of assigning monetary value to the goods and services of a social project is to value them at market prices, as is usually done in the case of self-build or environmental sanitation projects.

However, there are social projects where it is difficult to subsume the value of their benefits in terms of economic efficiency. "In these cases, it is methodologically simpler and logically more correct to give up any attempts at monetization and use (other) indicators" (Musto, 1975, p. 116).

It should be noted that cost-benefit analysis cannot be used to evaluate programmes in which investment is nil or very small, although current expenditures may be significant, as occurs very often in the social area. Moreover, this type of analysis is not centered on the degree to which projects and programmes achieve their objectives, so that it is of little use for overcoming the weaknesses of social policy already mentioned.

## 2. Cost-effectiveness analysis

This type of analysis involves comparison of the (monetary) costs of a programme or project with the possibility of efficiently attaining goals which cannot be expressed in monetary terms (*ex ante* evaluation), or determination of the real differences in efficiency between various execution options having the same objectives (*ex post* evaluation).

Although cost-effectiveness analysis does not allow for the comparison of projects with different objectives, such comparison is possible if the projects are made compatible through the use of a common denominator, such as their likelihood of achieving the same results. Thus, a programme designed to combat malnutrition could be compared with one aimed at reducing malaria, the common element being the possibility of reducing

the number of handicapped persons and deaths in the target population.

The choice between a nutritional programme and a self-build programme for low-income groups is more difficult. In this case, the only rational criterion which can be used (independently of cost-effectiveness analysis) is that of giving priority to the most basic needs.

Cost-effectiveness analysis leaves aside the examination of objectives. It accepts that they derive from political decisions and merely seeks to ensure that they are achieved at minimum expense. In other words, it seeks to discover the way to allocate resources so as to obtain the greatest number of units of results.

To that end, it compares the degree of relative efficiency of either different projects with the same objectives, or of alternative options for the same project. A basic requisite is therefore that those options must be comparable with each other, i.e., that they have the same target population and that the goods and services generated are comparable in quantity and quality.

Traditionally, cost-effectiveness analysis examines the operational efficiency of project execution, with a view to revealing difficulties in programming, administration and control so as to correct them and thus reduce the costs due to inefficiency. It is difficult to generalize the results of this type of analysis, since in order to do so it would be necessary to address the problem of the economies and diseconomies of scale which derive from the expansion of projects.

When the product unit of the project is the same as the latter's final objective (for instance, an additional life saved), the criterion of choosing the option which will minimize unit costs is sufficient. If the products of the project are only a means to an ulterior end—for instance, the distribution of nutritional rations (the products) in order to eliminate or reduce malnutrition in a target group (the objective)—conventional cost-effectiveness analysis only guarantees efficiency through the pursuit of minimum costs, but it sheds no light on the efficacy of the project.

### 3. Analysis of the impact of projects

There are factors other than operational efficiency which may hinder or even completely prevent many social projects from achieving their goals. The purpose of impact analysis is to identify these factors. Impact is understood as the degree to which a project transforms some aspect of reality as a function of its objectives. This calls for explicit consideration of the net effects of the project, in order to eliminate changes deriving from the context in which it is executed.

Impact analysis determines the extent to which the project has achieved its objectives, the changes brought about in the target population, and the secondary effects produced (both foreseen and unforeseen).

On the whole, it may be concluded that impact analysis is a necessary, though not sufficient, condition for the evaluation of social projects. Since it seeks to measure the degree of efficacy of a project, it does not explicitly consider the costs incurred, which implies that the resources available are presumed to be unlimited. This is the result of the classical division of disciplines in evaluation activities. Economic analysis is mainly concerned with efficiency, whereas efficacy has traditionally been the main concern of specialists in the substantive areas of social projects (nutrition, health, education).

The evaluation of processes and appraisal of their impact are therefore distinguished from each other by the type of questions they answer, the decisions they affect, and the potential users of their results. The evaluation of processes looks ahead in order to suggest corrections or adjustments; impact analysis looks back to see if the project worked and to what degree it was successful. The first-named type of evaluation seeks to affect daily, operational decisions; the second type provides information for deciding on the possible continuation of the project or the design of similar ones, so that ultimately it permits the taking of policy decisions. This means that the users of one and the other type of evaluation are also different: some of them are responsible for managing projects, while others are authorities with the capacity to lay down more general guidelines on the basis of the results.

### III

## A comprehensive methodology: cost-impact analysis

### 1. Efficiency and efficacy

A methodology designed to overcome the current limitations of social policy must incorporate analysis of both project efficiency and efficacy (Cohen and Franco, 1992).

*Efficiency* is the relation between the cost of inputs and the cost of the products (services or goods) obtained. When the quantity of products to be generated is defined, the aim is to minimize the cost per product unit. When the total expenditure to be made is fixed, however, the aim is to maximize the product. Thus, both definitions mean basically the same thing.

Analysis of efficiency is undertaken both *ex ante* and during project implementation. It should not be confused with follow-up or monitoring, which is limited to comparing the actual results with the goals established in the programme.

The *efficacy* of a project is the degree to which it achieves its goals within a certain period of time, without taking the costs into account. When contextual effects are eliminated and the net effects of the project are considered, the term *impact* is used.

Impact analysis is carried out independently of the evaluation of operational efficiency (process evaluation). These two types of analysis are performed separately because some of them require more extensive collection of data than others. Reprogramming a project requires only one data collection step, in order to determine the "base line", which is a cross-section on the basis of which a diagnosis is made which permits the proposal of solutions. For impact evaluation, however, both a diagnostic "base line" and an "end line" of results are needed. Comparison of the two makes it possible to determine the magnitude of the changes which can be attributed to the project.

The base line, usually associated with the diagnosis, can be drawn at any time during project implementation. On the other hand, in order to determine the "end line" it is not always necessary for the project to have ended; in reality, it is merely another cross-section which provides information equivalent to that obtained from the base line. The time which must elapse between the collection of the

initial information and that required for the end line depends on the nature of the changes pursued (nutritional, health, educational, etc.) and the degree of sensitivity of the indicators used to measure them. Those indicators should be selected by experts in the substantive areas of the project.

Impact evaluation may be carried out during execution of the project, at its conclusion, or even after it has ended, once the necessary time has elapsed for all its effects to become apparent. *Ex post* impact evaluations can be used as the basis for *ex ante* estimates for analogous projects.

### 2. Central elements of the methodology

Efficiency analysis seeks to determine which project or project option will minimize the cost per unit of product (CUP). For this purpose, it is necessary to annualize capital, operational and maintenance costs to obtain the total annual costs (TAC). At the same time, it is necessary to establish the annual services provided (ASP) by the project (in the case of new projects), or the additional annual services provided (AASP), in the event of the extension of pre-existing projects. The relation between these services and the total annual costs gives the cost per unit of product (CUP).

$$\text{CUP} = \frac{\text{TAC}}{\text{ASP}} \quad \text{or} \quad \text{CUP}^* = \frac{\text{TAC}}{\text{AASP}}$$

CUPs are indicators of operational efficiency. They are a product of the investment made. Cost-effectiveness analysis usually goes this far, that is, it tries to minimize the cost of the products of the project and assumes that the actual impact, which is more difficult to measure because it requires more time and effort, will be achieved through proper focussing on the target population. Those considerations are undoubtedly valid, especially when the alternative is the situation which usually obtains in social projects, which tend to have a loose form of programming that does not include evaluation. In such cases, the performance of cost-effectiveness analysis is obviously a significant step towards more

rational resource allocation in the social area. However, efficiency in the generation of products in a social project does not necessarily mean efficacy in the achievement of its objectives (impact).

To sum up, if the objective of the evaluation were only to analyse efficiency, it would be sufficient to determine only the minimum CUP. What is sought, however, is also to maximize the efficacy of projects, that is, their impact. Optimizing both the efficiency and efficacy of a project means making it achieve its objectives with the best possible allocation of available resources, or, in other words, maximizing its impact at the lowest possible cost. In order to determine the degree to which that purpose has been achieved, it is necessary to consider jointly, in each project or project option, the total annual costs, the impact achieved in respect of each objective, and the relative importance assigned to each of these.

The backbone of cost-impact analysis is the determination of the cost per unit of impact (CUI) ratio (see appendix). This is defined as follows:

$$\text{CUI} = \frac{\text{TAC}}{\text{OB} \cdot 100}$$

where CUI is the cost per unit of impact achieved in respect of each project objective, or the cost of achieving 1% of the impact in each objective; the numerator is the total annual cost (TAC), and the denominator is the magnitude of the impact achieved or estimated (OB), multiplied by 100.

The consideration of various technically viable options for implementing a project, by establishing their respective cost-impact ratios, will make it possible to select the alternative which minimizes the cost per unit of impact.

In *ex ante* evaluation, this procedure makes it possible to choose the best project option or to select one project from among several with the same objectives. Not only the costs, but also the products and impact are estimated. Within the margin of uncertainty inherent in every estimate, the levels of knowledge and standardization are much greater in the case of costs than in that of impact. The latter must therefore be estimated on the basis of *ex post* evaluations of analogous projects and expert judgment.

*Ex ante* evaluation attempts to anticipate the future, which is, by definition, uncertain. Moreover, there are always practical limitations on gathering

the data needed for the analysis. Since the essence of *ex ante* evaluation is the prediction of probabilities, some degree of possible error or risk is inherent to this methodology. It is therefore necessary to determine the ranges of possible variation of the basic parameters of the project in order to define the evaluation's degree of reliability (or uncertainty). Sensitivity analysis makes it possible to determine the basic assumptions which will have significant effects on the acceptability of projects.

*Ex post* evaluation seeks to determine the option with the best cost-impact ratio, together with its causes, by learning from operational experience. The cost, products and net effect are revealed by the analysis of what really happened in the project. Costs are extracted from existing records, while the annual services provided, additional annual services provided, and impact emerge from measurements performed for that purpose.

The evaluation of social projects on the basis of cost-impact analysis does not calculate the rate of profitability or the contribution made by the project or programme to society as a whole. These two dimensions are subsumed in the political decision about the goals to be given priority. After that decision has been made, it remains to determine the most efficient and effective option for achieving those goals. In that respect, cost-impact analysis makes possible a rational choice.

### 3. Generalizing evaluations: social project data banks

Isolated experiences of evaluation are important because they make it possible to reprogramme the project in question and to learn from that experience for the design and implementation of future actions. However, in order to truly rationalize social policy it is necessary to evaluate every project, which can be done through the creation of information systems for evaluation or social project data banks.

The main objectives of the idea of establishing project data banks are "to facilitate, standardize and coordinate the follow-up and control tasks involved in investment projects, as well as to support pre-investment execution and planning, investment programming and the performance of *ex post* project evaluations" (ILPES, 1991). This has been done in a number of countries. In Chile, for example, this

system has been operating for years, and it is also used in Belize, Bolivia, Colombia, Guatemala and the Dominican Republic.

The methodological design of these banks permits the registration of information in each stage of the project (pre-investment, investment and implementation). In this way, the system can provide essential information for decision-making related to the programming and control of investments, thus making it possible to improve the efficiency of the latter.

Social programme and project data banks pursue similar goals. Naturally, their structure and methodology must be adapted to the particular nature of the social actions involved.

The main differences between investment project banks and social project banks are the following:

i) *Evaluation methodology.* In social project banks, cost-impact analysis rather than cost-benefit analysis is used, the impact being understood, not as

the project's effect on society, but as the set of changes produced by the project in the target population, as a function of its objectives.

ii) *Predominant type of evaluation.* In public investment projects the emphasis is on *ex ante* evaluation and on physical-financial follow-up during implementation. In social projects, however, *ex ante* and *ex post* evaluations are both equally important. The latter type of evaluation serves both for reprogramming and for improving the *ex ante* evaluation of future projects.

iii) *Investment versus current expenditures.* Public investment project banks seek to help rationalize such investment. They do not include social programmes and "projects" which require little or no investment, even though the current expenditures involved may be considerable. In contrast, social project banks include both projects in the strict sense (i.e., those involving investment) and programmes which do not call for investment.

## IV

### How can the practice of evaluation be made viable?

As we have already seen, the problem faced by social policy is not only the scarcity of resources, although excessive emphasis is usually placed on that factor. There is also the problem of low efficiency in the use of resources and ignorance regarding the efficacy of the actions financed with those resources.

In order for social policy to be able to contribute to the achievement of the objectives of equity and economic development, it must be made more rational by changing the way it is executed and ensuring that its effects are truly positive. In order to achieve this, it is essential to evaluate what is being done and to establish permanent mechanisms for the follow-up and evaluation of programmes and projects.

There is no point in insisting on the provision of more resources if all that is intended is to repeat what

has been done in the past, because as we have already seen, that will not help to overcome poverty or improve the quality of human capital. It is therefore necessary to modify institutions and financing mechanisms so as to incorporate evaluation activities.

Currently, there are a large number of important programmes under way in Latin America, many of them financed by international cooperation, where the logic of projects has been adopted. This logic differs considerably from the traditional way of implementing social policy. These experiences provide fertile ground for the institutionalization of the idea of incorporating evaluation activities and, in that way, generating a "virtuous circle" of demonstration and dissemination which will cause this logic of resource allocation and management to spread to the rest of the social area.

Appendix

MATRIX OPERATIONS INVOLVED IN COST-IMPACT EVALUATION

A. DEFINITIONS

TAC<sub>i</sub> = Vector of the total annual costs of each of the systems i.

$$TAC_i = (TAC_1, TAC_2 \dots TAC_n)$$

OB<sub>ij</sub> = Matrix representing the impact or degree of achievement of each of the objectives j of the systems i.

$$OB_{ij} = \begin{bmatrix} OB_{11} & OB_{12} & \dots & OB_{1m} \\ OB_{21} & OB_{22} & \dots & OB_{2m} \\ \vdots & \vdots & \ddots & \vdots \\ OB_{n1} & OB_{n2} & \dots & OB_{nm} \end{bmatrix}$$

W<sub>j</sub> = Vector of the weightings assigned to each of the objectives j.

$$W_j = (W_1, W_2 \dots W_m)$$

B. OPERATIONS

1. *Cost/unit of impact ratios (CUI)*

These are obtained by dividing the total annual costs vector (TAC) by the achievement of objectives matrix (OB).

$$CUI_{ij} = \begin{bmatrix} CUI_{11} & \dots & CUI_{1m} \\ CUI_{21} & \dots & CUI_{2m} \\ \vdots & \ddots & \vdots \\ CUI_{n1} & \dots & CUI_{nm} \end{bmatrix} = 1/100 \begin{bmatrix} TAC_1 \\ TAC_2 \\ \vdots \\ TAC_n \end{bmatrix} \begin{bmatrix} OB_{11} & \dots & OB_{1m} \\ OB_{21} & \dots & OB_{2m} \\ \vdots & \ddots & \vdots \\ OB_{n1} & \dots & OB_{nm} \end{bmatrix}^{-1}$$

2. *Minimum cost/unit of impact ratios CUI (m)*

For each objective (column) the minimum value of the CUIs must be selected

$$CUI_{ij}^{(m)} = \text{Min}_i CUI_{ij}$$

A matrix is then completed with the values thus obtained. This matrix has identical values in each column.

$$CUI_{ij}^{(m)} = \begin{bmatrix} CUI_{11}^{(m)} & \dots & CUI_{1m}^{(m)} \\ CUI_{21}^{(m)} & \dots & CUI_{2m}^{(m)} \\ \vdots & \ddots & \vdots \\ CUI_{n1}^{(m)} & \dots & CUI_{nm}^{(m)} \end{bmatrix}$$

3. *Differences in absolute values (DA)*

These are obtained by subtracting from the matrix of the cost/unit of impact ratios (CUI) the minimum value obtained for each objective.

$$CUI_{ij}^{(DA)} = \begin{bmatrix} CUI_{11}^{(DA)} & \dots & CUI_{1m}^{(DA)} \\ CUI_{21}^{(DA)} & \dots & CUI_{2m}^{(DA)} \\ \vdots & \ddots & \vdots \\ CUI_{n1}^{(DA)} & \dots & CUI_{nm}^{(DA)} \end{bmatrix} = \begin{bmatrix} CUI_{11} & \dots & CUI_{1m} \\ CUI_{21} & \dots & CUI_{2m} \\ \vdots & \ddots & \vdots \\ CUI_{n1} & \dots & CUI_{nm} \end{bmatrix} + (-1) \begin{bmatrix} CUI_{11}^{(m)} & \dots & CUI_{1m}^{(m)} \\ CUI_{21}^{(m)} & \dots & CUI_{2m}^{(m)} \\ \vdots & \ddots & \vdots \\ CUI_{n1}^{(m)} & \dots & CUI_{nm}^{(m)} \end{bmatrix}$$

#### 4. Differences in relative values (DR)

These are obtained by dividing the matrix of the differences in cost per unit of impact in absolute values ( $CUI_{ij}^{(DA)}$ ) by the matrix of minimum values of those ratios ( $CUI_{ij}^{(m)}$ ).

$$CUI_{ij}^{(DR)} = \begin{bmatrix} CUI_{11}^{(DR)} & \dots & CUI_{1m}^{(DR)} \\ CUI_{21}^{(DR)} & \dots & CUI_{2m}^{(DR)} \\ \vdots & & \vdots \\ CUI_{n1}^{(DR)} & \dots & CUI_{nm}^{(DR)} \end{bmatrix} = 100 \begin{bmatrix} CUI_{11}^{(DA)} & \dots & CUI_{1m}^{(DA)} \\ CUI_{21}^{(DA)} & \dots & CUI_{2m}^{(DA)} \\ \vdots & & \vdots \\ CUI_{n1}^{(DA)} & \dots & CUI_{nm}^{(DA)} \end{bmatrix} \begin{bmatrix} CUI_{11}^{(m)} & \dots & CUI_{1m}^{(m)} \\ CUI_{21}^{(m)} & \dots & CUI_{2m}^{(m)} \\ \vdots & & \vdots \\ CUI_{n1}^{(m)} & \dots & CUI_{nm}^{(m)} \end{bmatrix}^{-1}$$

#### 5. Differences in weighted relative values (DRW)

These are obtained by multiplying the matrix of differences in relative values of the cost/unit of impact ratios ( $CUI_{ij}^{(DR)}$ ) by the vector of the weightings of each of the objectives in question ( $W_j$ )

$$CUI_{ij}^{(DRW)} = \begin{bmatrix} CUI_{11}^{(DRW)} & \dots & CUI_{1m}^{(DRW)} \\ CUI_{21}^{(DRW)} & \dots & CUI_{2m}^{(DRW)} \\ \vdots & & \vdots \\ CUI_{n1}^{(DRW)} & \dots & CUI_{nm}^{(DRW)} \end{bmatrix} = \begin{bmatrix} CUI_{11}^{(DR)} & \dots & CUI_{1m}^{(DR)} \\ CUI_{21}^{(DR)} & \dots & CUI_{2m}^{(DR)} \\ \vdots & & \vdots \\ CUI_{n1}^{(DR)} & \dots & CUI_{nm}^{(DR)} \end{bmatrix} (W_1 \dots W_m)$$

#### 6. Vector of final results (RECES)

This is obtained by multiplying the matrix of differences in weighted relative values  $CUI_{ij}^{(DRW)}$  by a vector of value 1.

$$RECES_1^{(W)} = \begin{bmatrix} RECES_1^{(W)} \\ RECES_2^{(W)} \\ \vdots \\ RECES_n^{(W)} \end{bmatrix} = \begin{bmatrix} CUI_{11}^{(DRW)} & \dots & CUI_{1m}^{(DRW)} \\ CUI_{21}^{(DRW)} & \dots & CUI_{2m}^{(DRW)} \\ \vdots & & \vdots \\ CUI_{n1}^{(DRW)} & \dots & CUI_{nm}^{(DRW)} \end{bmatrix} \begin{bmatrix} 1 \\ 1 \\ \vdots \\ 1 \end{bmatrix}$$

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## The political economy of the developmentalist State in Brazil

*José Luis Fiori\**

The study of the political economy of the crisis of the State and its role in the trajectory of Latin American development is an urgent political task which could also contribute to the historical and theoretical debate about industrial development in late evolving capitalist economies.

The central thesis of this article is that the Brazilian developmentalist State was predominantly authoritarian. As it was not sufficiently strong, however, it ended up in reality as a prisoner of the interests embodied in the sociopolitical pact which that same State attempted to form throughout its history. For this reason, it could not rid itself of its protectionist rigidity or its exclusive character, nor could it avoid the failure of its key element: the public sector. That failure was caused by a passive strategy of financing through indebtedness and markedly inflationary attempts to harmonize social interests.

The article analyses the various dimensions of the developmentalist pact, including the relations of the State with private capital, workers, regional oligarchies and the urban citizenry. It then examines the various crises and cycles through which the developmentalist State passed and concludes with a reflection on some queries that arise in connection with the present situation.

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*If two individuals observe a figure from afar and one says that it is a man and the other, a horse, then before concluding that they are incapable of distinguishing a man from a horse, it may reasonably be considered that they may be observing a centaur (in which case it could be said that they are both wrong, because centaurs do not exist).*

NORBERTO BOBBIO, *O futuro da democracia*

### Introduction

Efforts to defend the role of the State in the development of late-evolving capitalist economies are not new, but neither are the ideological arguments which form part of the neo-liberal debate today about the "depoliticization of the market" in the central and peripheral countries. In the final analysis, mercantilism and advocacy of free trade, together with nationalist and liberal theses, oppose and succeed each other throughout the history of capitalism with a regularity which, at times, recalls the ancient Greek idea of stationary circularity.

In the 1950s, both in Latin America and in advanced capitalist countries, developmentalism overcame liberal resistance and gained a consensus analogous in its thrust and scope to Keynesianism in Europe. In these circumstances, the proposal to create independent national industrialized economies, promoted by judicious State activity, won the support of extremely diverse sectors of the political spectrum: from conservative nationalism to the anti-imperialist Left, including the timid -though active- support of liberals. As occurred in other places, the latter remained on the defensive from the theoretical point of view during the entire period, even though they participated in most of the "developmentalist" governments, both democratic and authoritarian.

In this sense, it may be said that the supremacy of the "developmentalist State" in Latin America was the counterpart of the "Keynesian" hegemony in Europe. And that supremacy was constructed almost exclusively on the analytic and conceptual basis provided by the economic thinking and project of ECLAC, so that its central ideas played a decisive part in the political struggles which accompanied the economic and social changes that took place in Latin America in the last four decades.

Very soon, however, in the 1950s and 1960s, the more lucid and impartial observers of the Latin American situation realized that the developmentalist strategy for industrialization was viable in only a few countries. Thus, when the international crisis hit Latin America in the mid-1970s, the ECLAC-inspired industrialization project could only be said to be in force in Brazil and Mexico. By the end of the 1980s, only Brazil had still not entirely abandoned the developmentalist model, in spite of being completely paralyzed by external indebtedness and the economic and political failure of the State: a failure which took the form of a long period of ungovernability, accompanied by a slow and complex transition to democracy.

It is against this background that, in the early 1990s, the ideas which had dominated the economic and political thinking of the central countries since the 1970s have gained rapid acceptance among Brazil's political and intellectual elites. With a decade of delay, neoliberalism is today mounting an unprecedented ideological offensive against the Brazilian State, which is seen as the main culprit of the stagflation and economic losses of the 1980s.

As sometimes happens, a new ideological hegemony succeeds in temporarily sweeping away the knowledge accumulated in the past, replacing history and theory with pure and simple ideology capable of suddenly convincing intellectuals and politicians that only the market holds the secret of economic success and universal happiness. As always, in such a moment of ideological euphoria it is difficult to think objectively and analyse in a critical spirit. Thus, developmentalist theses have very quickly been put on the theoretical and ideological defensive, and their survival now depends much more on the silent power of resistance of the interests which grew up under their aegis than on the force of their arguments. Their sudden fragility surprises even the least observant, although it is more an inevitable consequence of developmentalist incoherences and contradictions than of the virtues or originality of the new liberal arguments.

In reality, the problem is not so simple, and there are no unilateral causes or responsibilities for it, because by definition it is difficult for the classical separation between the State and the economy or society to fit in with the conditions prevailing in countries of

late and peripheral development. In fact, the crux of the issue lies precisely in understanding those relations and perceiving how they explain the simultaneous success and failure of the Brazilian State.

Accepting the short cuts involved in ideological generalities means ignoring the fact that the developmentalist project in Brazil was backed by a solid, politically conservative coalition which always enjoyed the support of the advocates of economic liberalism. It also means ignoring the fact that, before the crisis of the 1980s, developmentalism achieved extraordinary success in its industrialization goals. In this way, theoretical and political attention is diverted away from the fact that the final crisis not only basically followed the same course of success, but also paradoxically ended up by affecting its own ruling force, in a movement so inherently complex as to make it difficult to distinguish between causes and effects.

Our central thesis in this regard is that the Brazilian developmentalist State was predominantly authoritarian. As it was not sufficiently strong, however, it ended up in fact as a prisoner of the interests gathered together in the sociopolitical pact which it attempted to form during those decades. For this reason, it could not rid itself of its rigid protectionist attitude or of its socially exclusive character, nor could it avoid the failure of its key element—the public sector—due to the use of a passive strategy of financing expenditures through indebtedness and the tendency towards the inflationary harmonization of interests.

Thus, after forty years of State-developmental consensus, all the lessons of history about underdevelopment, the periphery and even the strategic role of the State were forgotten in the heat of the political struggle sparked off by the severity of the economic crisis, although the most recent example of the potential role of the State is to be found in the experiences of the East Asian countries in adjusting to the new international political and economic order.

For this reason, analysing the political economy of the crisis of the State and of its role in the trajectory of Latin American developmentalism is not only a politically urgent task but may also contribute to the larger historical and theoretical debate about industrial development in late-evolving peripheral capitalist economies.

## I

**The main dimensions of the developmentalist pact**

There seems to be consensus with respect to the role played by the State as an agglutinating agent in the process of industrial accumulation in Brazil.

It was always the State which determined the level of integration and the possibilities of expansion of international capital, as well as the areas of expansion for domestic capital, so that the opening of new frontiers for accumulation always depended on its agency. (Coutinho and Belluzzo, 1982, p. 22-23).

However, neither the size nor the functions of the public sector give a clear idea of the specific nature of the role of the State in Brazilian industrialization. Nor does the authoritarianism of its political system during the "developmentalist cycle" explain, by itself, the organizational structure and the simultaneous strength and fragility of the public bureaucracies *vis-à-vis* private interests. In this sense, the crisis of the 1980s is instructive insofar as it brings out the real aspects and dimensions that go to make up the special nature of the Brazilian "style of development". In fact, these were the aspects and dimensions of an economic, social and political pact which, in our judgment, prevailed during the entire developmentalist trajectory, simultaneously and contradictorily stimulating the motive forces of economic growth but also simultaneously its dysfunctions, which were responsible for the financial and political disorder which, in the 1980s, eventually paralyzed its own *condotiero*, the State.

Of course, when we affirm that that crisis reveals the critical features which were always present in that pact, we are not ignoring the profound structural changes brought about by industrialization and their obvious social consequences. It would be absurd not to see that the material changes in the productive base were responsible, especially as from the 1950s, for radical demographic, sociological, cultural and political changes which gave rise, among other phenomena, to new patterns of behaviour and new interest groups.

During that period, the agricultural frontier expanded and was closed, powerful new agro-export and agro-industrial complexes were created, while at the same time small traditional land holdings were broken up, freeing or expelling populations which

were forced into uncontrolled internal migrations, thus changing the whole economic, social and cultural panorama of our labour force. New productive sectors became oligopolistic and were internationalized, and metalworking and petrochemical complexes which were to stimulate the emergence of a "modern" working class were set up or expanded. Together with the growth of the public sector of the economy, there was corresponding expansion of the cities, the marginated masses, and the middle classes, regardless of whether the latter were linked or not to the expanding State bureaucracy.

In this same period, the institutional apparatus of the State expanded and became more complex, but there were also three changes of political regime, two changes of systems of government, as well as two sweeping administrative reforms and a similar number of reforms of the public financial system, several modifications of the tax system, and at least three changes in the institutional structure of the public social security system.

However, it would be analytical blindness not to perceive also that certain phenomena persisted or reappeared repeatedly over time: in the economic field, for example, the issue of the structure of land ownership, together with fiscal and exchange rate crises aggravated by chronic difficulties of a financial nature; in the sociological sphere, the various manifestations of authoritarianism in the social relations of production; and finally, in politics, the permanent tensions between local powers and authoritarian centralized bodies and between civil populism and military interventionism.

This heterodox and explosive combination of change and continuation seems to indicate that Brazil unquestionably experienced a form of late industrialization different from those of the second half of the nineteenth century studied by Gershenkron, or those which Johnson (1983) and Amsden (1989), among others, identified in Asian experiences after the Second World War.

In metaphoric language, it could be said that this developmentalist pact of a conservative nature was organized around several fundamental issues, especially that of the political and economic relations of

the State with private capital and with labour and that of the power relations of the State with the regional oligarchies and with the "urban citizenry".

### 1. *The State and private capital*

The first point to note here is that there was the reaffirmation of a very old rule, which remains unchanged: the structure of land ownership is untouchable. This was part of the tacit agreement in Brazil which vetoed every attempt at agrarian reform and sanctified the protection of agro-mercantile capital interests as an essential condition of the industrialization pact.

From the hierarchical point of view, only later was it possible to define the norms governing the relations between the State and domestic and foreign industrial capital, in accordance with what some have called "associate capitalism" (Cardoso, 1975), but at all events this was very much prior to the industrial acceleration of the 1950s, and it coincided, in the 1920s, with the arrival of the first wave of foreign affiliates linked to the industrial sector (Lessa and Dain, 1982). It was at this time that the pact really setting up the Brazilian industrial "triad" was established (Evans, 1981). This pact was based on two fundamental clauses, with the State as its great guarantor and moving spirit.

The first clause reserved for domestic capital the areas of greatest interest to the State, as fields of development. The second laid down rules for the horizontal distribution of profits, according to which the profitability of the areas controlled by domestic capital would never be less than that of the industrial area, which was then under foreign control (Lessa and Dain, 1982, pp. 221 and 222).

With the advance of industrialization, this agreement described by Lessa and Dain was broadened as domestic capital also entered the industrial field. In essence, however, it maintained its validity until the 1980s and had some permanent structural and institutional effects which were reflected basically in the way in which industrial production was financed and expanded and the way in which State protection and mediation were organized.

Thus, and primarily, the fragility and dispersion of domestic capital, together with the protection given to an atrophied private banking system, transferred the task of financing the big investment projects needed for industrialization to public credit. At

the same time, however, the anti-State attitude and the heterogeneity of business interests systematically impeded every effort by the public sector to bring about more dynamic financial centralization. Consequently, it may be said that in Brazil the public institutions only played a passive financial role, i.e., that of providing capital in various forms, including subsidized credit. They did not participate as an agent in the process of the monopolization of capital (Tavares, 1978, p. 42).

Consequently, industrialization was ultimately financed by resorting to inflation and internal and external public indebtedness: both equally precarious ways of sustaining a process of growth which some eventually came to believe should be self-sustaining. This occurred because in Brazil, unlike France, Japan and South Korea, the State was never able to resolve the financial aspects of industrialization. The political and ideological veto exercised by its conservative supporters placed it in a passive position, based on extremely fragile foundations, as would be seen later, when international resources became scarce and it was no longer possible to resort to inflation or domestic indebtedness in order to support the process of industrial accumulation.

Secondly, as a direct result of what has been called the "Holy Alliance", international capital assumed and maintained a leading position in industry, but domestic capital always managed to obtain profits which systematically exceeded the true potential values of its operations (Lessa and Dain, p. 225). Meanwhile, this coexistence within the same market of types of capital with different levels of productivity and competitiveness was only possible through a kind of ongoing State protection which blocked the inevitable process of centralization and preserved by political means the "perverted" patterns of profitability of certain segments of capital.

Thirdly, the inevitable political freezing of this protectionism, which Fajnzylber (1983) termed "frivolous", inhibited the emergence of more aggressive business sector strategies for technological development aimed at increasing the productivity and competitiveness of domestic capital, which naturally affected the overall productivity and competitiveness of the Brazilian economy over time.

Fourthly, these strategic options or vetos eventually led to a kind of imperfect centralization, something like a politico-structural blockage of the centralization of capital (Lessa and Dain, p. 223).

That blockage gave rise to a process of sectoral monopolization which was not accompanied by the centralization of capital or business conglomeration, both of which are indispensable factors for multiplying private sector energies in late-evolving capitalist economies. Thus, while the Brazilian State was unable to use its power to articulate the industrialization process organically, neither was there any private articulation of any kind of "financial capital".

Another effect which was produced directly by the political rules of the foundational pact of Brazilian developmentalism was the maintenance and further reproduction of structural heterogeneity (Pinto, 1965) which constantly reconstituted itself at levels ever more complex and distant from those of the old "dualism" of which so much was said in the 1950s. This was "modern", politically protected heterogeneity, which arose and grew in all regions and segments of the economy.

Another important effect was felt in the area of the institutional organization of State protection and arbitration. The veto power of the various regional or sectoral interest groups, recognized in the original pact and confirmed because of its financial or electoral contribution to the political reproduction of the dominant order, eventually came to be concentrated in certain groups which literally appropriated the centres of State decision-making responsible for protecting their captive markets. This phenomenon seriously restricted the autonomy of the economic bureaucracies: an autonomy which was an essential element in the success of East Asian industrialization, as it was also for the reconstruction of France after the Second World War. Thus, there was little bureaucratic autonomy *vis-à-vis* domestic capital and still less with respect to foreign capital, the financial and commercial independence of which was undoubtedly a key element in Brazilian associate capitalism.

In this way, the State was obliged to accommodate each of its projects to the specific and changing interests of each segment of capital. However, since none of those interests or groups of interests managed to gain ascendancy and make the State's objective viable, the State was constantly harassed by innumerable contradictory demands which it was unable to reconcile and satisfy (Cardoso de Mello and Belluzzo, 1982, p. 157).

This permanent instability and tension not only reduced the leeway for autonomous strategic initiatives by the State but also repeatedly impeded the

reconsideration of positions in respect of the withdrawal of protective measures or stabilization of the currency. On the contrary, in all the cyclical crises which accompanied Brazilian industrial expansion, the members of the original grand pact absolutely vetoed orthodox stabilization policies, leaving the State with no option but to "flee ahead" (Fiori, 1984) in search of new forms of indebtedness which could boost short-term growth, at the expense of the State's own ever-increasing fiscal fragility.

In each new crisis, this process only served to increase and aggravate the battle among the various segments of capital for control of the State's monetary and juridical capacity to arbitrate, giving rise to an interminable struggle accompanied, as a corollary, by chronic financial, juridical and political instability (Fiori, 1984, p. 207-208). This struggle was undoubtedly the main factor responsible for the dissolution of the "stable future prospects" indispensable for the more modern sectors of the economy.

In this sense, inflation always had a highly political dimension, inasmuch as it was an essential element in the harmonization of the various confederated interests, which were the real culprits of the unstable and volatile course being run by developmentalist macroeconomic policy. Thus, although the fact that Brazil was a closed economy with an internationally isolated currency (despite its great dependence on the international capital circuits) allowed the Brazilian State to direct its monetary and exchange rate policies in a relatively elastic manner, subordinating them simultaneously to the associated interests and to its aim of promoting industrialization, that greater freedom also impeded the implementation of reforms which could have led to more stable macroeconomic scenarios.

This last option was always eluded, in order to avoid collisions among the various economic interests which formed part of the pact and were involved in the industrialization strategy. In this case, too, it was decided to flee ahead by simply passing on costs and responsibilities, until, with the crisis of the 1980s, that strategy became impossible, as did recourse to stabilization measures.

## 2. *The State and the workers*

With regard to this chapter of the developmentalist pact, it is worth recalling that slavery, as the dominant form of the organization of productive labour,

was endorsed by the monarchy (1822-1889) and was only abolished in Brazil in 1888. Moreover, the migratory flows from Europe, which came to replace slave labour, were decisively encouraged by the State, thus making the labour market a pioneering area of State intervention and regulation. It would be beyond the scope of this paper to recall also the police measures with which the governments of the Old Republic (1889-1930) faced the labour issue. Although the first legislative initiatives in the area of social security appeared as early as 1923, the basic rule in the organization of the relations between the State, private capital and labour was repression, intermittently replaced or complemented with various forms of populist co-optation, especially of urban workers. This system of a triangular relationship between the State, private capital and wage-earners remained practically unchanged, in spite of the profound changes produced by the industrialization process. Consequently, in this case as well, the basic rules for the organization of labour relations during the "developmentalist cycle" were defined, tried out, and given the seal of approval long before industry became the leading light of Brazilian capitalist development.

We have already commented on the corporative and authoritarian nature of the labour, trade union and wage legislation adopted by the Brazilian State as from the New State (1937-1945). That same legislation was to remain nearly intact during the democratic period (1945-1964) and even during the military regime, which lasted until 1985. Throughout that time, the State managed wages in a coercive manner, during the democratic phase through definition of the preferential value of the "minimum wage" or through the fixing of public sector wages, and during most of the military regime, through an official formula for calculating the readjustment of all private sector wages. It can thus be said that a basic rule of the conservative pact was that conflicts in respect of income distribution were made political and State concerns.

However, this was only the foundational formula –imposed by circumstances but also necessary– for the rules which governed worker participation in the developmentalist pact. Not only was it decided that the State would play a permanent leading role in labour relations –not just as an arbiter– by restricting or repressing union activity, but it was also decided to base industrialization on "low wages" (Medeiros,

1992), involving the widespread use in rotation of a labour force whose levels of skills were never considered an important element in the development of microeconomic competitiveness. It represented the choice of a kind of Taylorism, without Fordism.

Brazilian business associations openly took it upon themselves to defend this wage strategy. Taking as their starting point the great productive and regional heterogeneity of the Brazilian economy (assumed, once again, to be an immutable fact), the business sector proposed that the real average wage should remain constant or grow less than the per capita product. Within this strategy, rationalized on the grounds of the need for growth with low wages, it was supposed that expansion of the overall wage bill should only occur as a result of displacement of the active population from the countryside to the big cities (Medeiros, 1992, p. 228). This was an objective enthusiastically assumed by the military regime which began in 1964 and which, together with the adoption of this wage policy, also did away with job stability.

It is very interesting, in this respect, to look at the economic and social dynamics which led to the political crises of the 1960s and 1980s, because although it cannot be categorically stated that they were preceded by a phenomenon of lower profit margins, it is nevertheless significant that they erupted after substantial wage increases. These increases were followed by inflationary spurts linked to the immediate fiscal and financial crises of the State, during which there was a hard struggle over income distribution, with the aim of preserving the purchasing power already gained. In fact, on both occasions this defensive action by the labour unions was used by the ruling classes as a pretext, from the economic point of view, for speeding up price increases and making this appear as a decisive political factor responsible for upsetting the institutional political order.

Thus, it can hardly come as a surprise that the progress of the Brazilian economy towards a style of growth propelled by mass consumption should have become a mirage, always overtaken by the economic movement of "fleeing ahead", led by Brazil's political, military and technocratic elites. On the one hand, there was a crisis which ended in a military coup, while on the other there was a crisis which ended in a democratic transition, accompanied by a chronic process of contained hyper-inflation. In spite of the

new political freedom and the trade union movement, the result was a new wage squeeze which was even worse than that of the 1960s.

The structural consequence of this political option adopted in the conservative pact for sustaining the developmentalist State was not only enormous wage dispersion and segmentation of labour markets, but also the formation of a whole set of social, individual and regional inequalities which have now reached levels without precedent in the capitalist world. Thus, in 1980 the share of total income received by the highest quintile of the population was 27.7 times greater than that of the lowest quintile. This inequality increased because of the powerlessness of the State to face the interests linked with the land ownership structure and the monopolization of urban spaces, in which the degree of capital accumulation, within the framework of unchecked metropolitan expansion, eventually relegated a significant part of the population to a state of almost complete marginality in terms of access to basic social services.

Social inequalities became so extreme that during the economic crisis of the 1980s, in spite of the return to democracy, it was impossible to appeal to a policy of solidarity with respect to adjustments and stabilization, based on social concertation. In the early 1990s, and in extremely perverse ways, wages are once again seen as the factor responsible for the hyperinflationary process, and workers are called upon to support a policy of adjustment and stabilization, which –ironically, if it were not so tragic– punishes them as the culprits of the inflation which has been part of the entire history of Brazilian industrialization, consistently based on a policy of low wages.

### 3. *The State and the regional oligarchies*

In Brazil, as in several other Latin American countries, the relations between the central power and local bosses have been a key element in the organization and stabilization of the State ever since independence (1822). Unlike the other countries of the region, however, in Brazil the vastness of the territory, the lack of communications, and the segmentation of productive activity, oriented predominantly towards foreign markets, made it possible for land owners to build up extremely solid oligarchies of regional power. Those oligarchies were so strong and autonomous that it can be said that only the common

interest in the face of foreign pressures to end slavery explain the ties of mutual dependence and “solidarity” which have sustained the unity of the national political institutions, in spite of the distances and differences. This is why the abolition of slavery in 1888 led to the immediate proclamation of the republic in 1889, reframing in a new and challenging way the problem of the geopolitical balance of power among the various regional oligarchies.

During the Old Republic, also called the oligarchical republic (1889-1930), which was governed by a rigorously liberal Constitution approved in 1891, this question of balance was resolved through an informal agreement known as “the governors’ policy”. This recognized the juridical and fiscal autonomy of the subnational states and did not question the power of the oligarchical fractions arising from electoral victories at the local level. At the same time –or in return– the regional oligarchies supported a non-interventionist central State and recognized its implicit leading position in the hierarchy of the various states, the order of which was determined by their relative economic power or, in other words, by their agro-business exporting complexes. In the place of slavery, the basic implicit common interest of this new agreement lay in the inviolability of the structure of land ownership, on which the power of the joint oligarchies rested.

The revolution of 1930 represented, above all, the armed questioning of the political and electoral rules which served as the basis for the “governors’ policy”; however, the dictatorship of the New State went even further and explicitly proposed to reduce the power of the regional oligarchies, as a condition for modernity.

In this sense, the developmentalist State was created in opposition to the joint power of the oligarchies, and it favoured a centralization of power which was considered to be indispensable for the unification and organization of Brazilian society and its economy. However, since this proposal could never have been accompanied by the power, conditions or even the real desire to modify the forms of land ownership, the developmentalist State’s aim of furthering centralization was eventually weakened, worn down or even completely perverted, due to the relations of permanent tension –and co-optation– between the wishes of the central authorities and the political power of the innumerable and heterogeneous regional interests.

This phenomenon was already apparent in the New State, but it became much more marked during the democratic regime (1945-1964) and –paradoxically– even continued to be vigorous during the military regime, in spite of that regime’s policy of favouring fiscal concentration and the reduction of the political power of state governors. During the whole of this period, successive modifications of the electoral system of proportional representation meant that the more politically “backward” districts of the country were always over-represented in the National Congress. This made it possible to neutralize the weight of the predominantly urban “modern” vote and led to the conflict which Furtado (1979) saw as a basic cause of the crisis which ended in the military coup of 1964: i.e., the conflict between the innovative will of the Presidential figures elected by universal suffrage and the conservative resistance of the Congress, controlled by the over-numerous representatives of the pockets of political backwardness and strong oligarchical control.

With the advance of the industrialization and urbanization process, the power of the agrarian oligarchies of the Centre-South (more industrialized) region rapidly declined, but such power remained intact in the North and Northeast of the country, where there were still huge population and electoral contingents linked, in general, to the most backward productive sectors of the Brazilian economy.

With industrialization, the relations between backwardness and modernity became more complex and no longer corresponded to a simple dualist model. The notion of “structural heterogeneity” seeks in fact to reflect that new configuration, in which pockets of political and economic backwardness are found throughout all regions and sectors of activity. Undoubtedly, however, from a strictly political and electoral point of view, there exists, even today, a certain superimposition which permits the continued existence of regions of the country in which the old oligarchies, based on political relations which are personal in nature and involve favours or economic dependence, still predominate: during the entire developmentalist cycle, these oligarchies, which controlled the economies and political power in these more backward regions, obtained positions and favours from the State precisely because of their enormous capacity for electoral mobilization, which was indispensable for the political reproduction of the conservative order.

Even during the military regime it was impossible to dispense with these forms of support and the consequent presence of oligarchical interests in the structures and the decision-making centres favouring industrial modernity. Thus, this rule of accommodation and mutual dependence between “modernity” and “backwardness” was a basic dimension of the developmentalist pact, becoming the true essence of what Weffort (1978) called “the compromise State”: a compromise which weakened the modernizing zeal of the technocratic elites and military men involved in the central administration of the State.

#### 4. *The State and the “urban citizenry”*

Mention has already been made of the speed and intensity attained by the urbanization process in Brazil as from the 1950s. That process gave rise to the expansion and rapid renewal of the wage-earning population and the emergence of large metropolises in which there was a concentration of populations totally marginated from the labour markets most directly linked to industrial growth (Quijano, 1974). This process also disrupted the geo-electoral balance which had existed prior to the 1950s.

During the Old Republic, the legal impediments to political citizenship had been so strict that they never permitted the participation of more than 3% of the population in Presidential elections, but during the New State such restrictions became absolute, due to the dictatorial nature of the political regime. The promulgation of the Constitution of 1946, however, although restricting the electoral participation of illiterates, opened up a space for new and broader political citizenship which was progressively occupied by the masses migrating to the urban centres, who thus joined the working and middle classes in this respect, and such enfranchisement even extended to the pockets of marginality.

Since then, the electoral weight of this new citizenry has grown by leaps and bounds, rapidly threatening the electoral strength of the more backward and still predominantly agricultural regions. In the face of this new challenge, the old originally oligarchical structures of participation proved inadequate as channels of incorporation, but even so they remained sufficiently strong to dominate the political system created in 1945, and they systematically

impeded the development of national, ideologically oriented political parties.

Thus, there rapidly emerged, in the words of R. Dahl (1971), a situation of incompatibility between the number and rapid growth of the new urban citizenry and the scanty institutionalization and competence permitted by the old rules of the intra-oligarchical pact, which had been incorporated into the political structures of the developmentalist State.

The conservative response to this new challenge had various nuances, but it maintained a constant common denominator: authoritarianism, either explicit, as in the 1930s or after the mid-1960s, or in the form of co-optation and populism, which impeded the consolidation of solid and effective representative institutions during the period of democracy.

In reality, the conservative pact which sustained the Brazilian developmentalist State never included democratic participation in any of its forms, and consequently never sponsored the institutionalization of structures which could respond to pressures by expanding political and social citizenship.

Thus, when it found itself obliged to coexist with democracy, the State could neither impede the appearance of populism, nor control its spread as the only possible means of electoral mobilization of the urban populations. And it was only able to respond to this challenge by having recourse to the State apparatus itself, as an instrument of mobilization and co-optation of support on the basis of clientage, which involved as its counterpart, among other things, the erosion of existing hierarchies and of the efficiency of the public bureaucracies, especially those responsible for the social promotion and protection of the population.

The conservative pact's rejection of the idea of political participation was so radical that, even during the long periods of authoritarian rule, the political elites and even the State itself never proposed any type of popular mobilization as a means of sustaining and strengthening its project of conservative modernization.

This attitude had significant consequences. Firstly, it affected the way in which the different governments and regimes identified with developmentalism sought legitimacy, i.e., through performance and efficiency.

Secondly, it affected the form of discourse of the State and the political elites. To the contrary of what was observed by Gershenkron, in Brazil eclecticism

was the keynote and ideas became entangled in an unfailingly inconsistent and demobilizing way. In the final analysis, the nationalist component of Brazilian development never enjoyed massive popular support, nor even that of the business sector, and it eventually became the banner of "national security", with exclusively military support, while its Statist component had an almost exclusively technocratic base. However, both components coexisted on almost always friendly terms with a rabidly "liberalist" discourse maintained by the vast majority of the business sector, which had the "competence" to know how to take advantage of the State, while attacking it ideologically.

This succinct analysis of the four chapters or basic issues of the conservative commitment which sustained the industrialization strategy in Brazil makes it possible to draw several conclusions with respect to the nature of the most successful developmentalist State in Latin America.

Although the most visible manifestations of its weaknesses were in the fiscal and financial areas, its deepest roots were political and, in the final analysis, were the result of the limits imposed by the confederated interests on the decision-making autonomy of the State. The State expanded its organization and extended its presence in terms of production or regulation to nearly all fields of economic activity and social interaction, almost always in authoritarian fashion. But although the State was "strong" when it came to disciplining the workers and the urban citizenry, it was extremely weak and submissive in the face of the economic and political demands of the oligarchies linked to backward areas and of the big corporations, which obtained monopoly conditions and advantages without ever committing themselves, as occurred in the Asian countries, to clear goals in terms of productivity and competitiveness, and still less in the areas of the protection and training of their own labour force.

There were very few moments during the "developmentalist cycle" when the economic bureaucracy of the State managed to resist external pressures and its own internal "Balkanization". Its links with the business sector never took the form of organic, strategic coordination, while the interests of private capital tended to take an individualized rather than a cooperative form, through linkages which, during the military regime, took the form of what F. H. Cardoso has called "bureaucratic rings".

This political weakness of the State always obliged it to flee ahead and take the line of least resistance, creating an industrial structure which was highly developed but was not self-sustaining financially or technologically. It was a form of industrialization which moved towards and became acclimatized to an extremely volatile and permanently inflationary macroeconomic environment.

It may be asserted, then, that while the Brazilian State did not repeat the performance of the Asian developmentalist States, it was not Keynesian, either, and at no time was it ever social-democratic. Nor, from the point of view of the social organization of labour, did it ever promote anything which could be called Fordism, nor did it ever allocate resources or even create adequate institutions for the functioning of a Welfare State. With respect to Keynesian-

ism, the State's liberal recourse to public deficits was never intended to seek full employment or to support consumption, but was rather the result of its own weakness and inability to sustain the growth of the modern sector of the economy without at the same time being "overwhelmed" by the most backward sectors. The same problem appeared again in the cyclical crises when the State did not have the necessary leeway for applying corrective policies. Thus, when it was overwhelmed by inflation and lost control of the monetary variables, it was obliged to give up all attempts to apply orthodox stabilization policies. In search of a way out of those crises, it promoted new fronts of expansion financed with fresh forms of indebtedness which only succeeded in temporarily putting off the final catastrophe, as we shall see below.

## II

### Cycles and crises

The history of Brazilian industrialization is marked by vigorous but short-lived cycles of expansion interrupted by very profound crises, nearly always of an economic and political nature.

Furthermore, this is not the first time that it has been noted that one of the most noteworthy characteristics of industrialization based on import substitution is the specific design of its economic cycle: the production curves of those industries tended to be uneven, shooting up rapidly when engaged in the substitution of imports, but slackening when growth of the market is based on an increase in domestic demand. Profits followed that same uneven pattern. Thus, industries moved rapidly from a situation of high growth and profitability to one of precocious maturity, with monopoly practices and low profitability, low levels of investment, and ageing plants and equipment (Félix, 1964, quoted in Hirschmann, 1968, p. 11).

Consequently, maintaining profits in that type of economy depended to an excessive degree on the existence of new fronts for investment in substitution, which, in turn, depended on the behaviour of two decisive factors: the structure of financing and the degree of weakness of the exchange rate.

Cyclic expansions began with these substitutive investments, but the success of those measures did not depend only on the type of financing but also on the political conditions imposed, in the sense that at the same time spaces for growth and profitability must also be opened for productive sectors which were not direct beneficiaries of the industrial policy. That imposition led to the politically conditioned expansion of credit and liquidity, not linked to the direct requirements of the substitutive wave. The adoption of policies to contain imports, together with this increase in public expenditure, created a climate of generalized euphoria in times of expansion, with high profit margins.

However, the persistence of exchange rate and financial problems rapidly and repeatedly eroded the macroeconomic scenario. The expansion of the public deficit—without a corresponding broad market for public securities—, the overvalued exchange rate and the worsening of inflationary tensions were the main causal factors, and they were also indicators of the beginning of instability in each of these cycles. At the first sign of any change in economic policy in the direction of restabilization, however, discord always arose again among the various segments of capital capable of taking political action to defend the rights

they had been guaranteed in the original pact. This capacity for reprisal is not taken into account in the models used by economists, and they therefore found it difficult to understand why the State authorities had so little control over the expansion of liquidity and macroeconomic imbalances.

On the one hand, the low level of openness of the economy had a dual effect: it guaranteed high profitability for recently installed sectors and permitted considerable autonomy in domestic monetary and exchange rate management. That autonomy only existed, however, when it was desired to apply expansive policies: it was useless or nonexistent when attempts were made to take the reverse course. On the other hand, paradoxically, the small size of the new sectors and the rapidity of the expansive cycles made them extremely dependent on public expenditure, thus making inflation an essential element for sustaining their extraordinary profits when growth slackened.

Thus, in the phases of deceleration, increased inflation converged with the unequal sharing of its redistributive effects, exchange rate and financial crises, and the fiscal contraction of the State. These "economic" phenomena coincided with the intensification of the conflict over income distribution on the part of wage-earners and the parallel increase in pressures on public expenditure by all the private interests dependent on it. It was at these times that the developmentalist State always showed its weak side *vis-à-vis* the business sector and political pressures responsible for worsening those fiscal crises.

In these circumstances, since the conservative pact vetoed every effort to permanently increase tax revenue and the level of the fiscal burden on the product, at such moments of pressure the State had no choice but to resort to indebtedness, with its obvious circular effects on inflation and other macroeconomic imbalances, which were further intensified in periods of slackening of import substitution.

In this way, the inflationary process associated with intersectoral imbalances and disproportionate increases in public expenditure in periods of economic expansion continued during periods of recession also, as a means of preserving profits in the face of the growing struggles over income distribution. The exchange rate problems, for their part, seemed to be associated with tensions in the balance of trade, during expansive phases, and with tensions in the capital account during recessions.

Generally, these periodic "fiscal" crises were overcome by emergency fiscal and/or monetary reforms, which never constituted a definitive solution to the fundamental problem linked to low tax income and the lack of an active capital market or of a private banking system in solidarity with the industrialization process. Nor were those reforms able to prevent each crisis from invariably affecting not only the conventional expenditures determining the quality of public services, but also the very investments which were indispensable for furthering the industrialization project.

During those crises, when it was necessary to make do with scarce credit and administer a currency in crisis, the government nearly always sought a solution in the same way: by imposing new "credibility" of the currency through the centralization of political power, generally in an authoritarian manner, and by "fleeing ahead" by opening new frontiers of expansion with the support of foreign resources. For this reason, the cyclic crises of this system of economic growth were always deeper and more severe when the domestic fiscal problem coincided with international financial problems capable of blocking the chances of "fleeing ahead". In these cases, there was unchecked financial speculation which coincided with political crises that led to radical reforms of the State in terms of political and administrative organization and pacts of domination.

In all of these crises, pressures for the "socialization of losses" were accompanied by violent and paradoxical attacks by the business sector on the economic intervention of the public sector, previously so well received and even considered indispensable in times of euphoria and growth. Nevertheless, the solutions adopted by different governments ended up by strengthening, in a very similar way, the "undesirable" State intervention and its association with foreign capital.

This was because, although the business sector always resisted State interventionism ideologically, it invariably yielded to it in exchange for "protection" which had the effect, at the institutional level, of what some have called "pigeon-holing" or others the "privatization" of the State and of "order". The result of this state of affairs was a system of labour relations which was extremely authoritarian, as well as being concentrative and exclusive from the point of view of wages and income distribution.

Something different, however, began to occur during the 1970s, when the government of General Geisel (1974-1979) responded to renewed exchange rate and financial difficulties, arising from the first oil crisis, with a government plan (the Second National Development Plan) which sought to complete the process of substitution of imports of basic inputs and take a definitive step forward in the development of heavy industry. To finance the plan, the government resorted once again to foreign indebtedness, with well known economic consequences: the increases in international interest rates, followed by the State's assumption of the private foreign debt, led to increases in the domestic public debt and the financial and resource erosion responsible for the new "fiscal" crisis of the 1980s. That crisis, however, as in the 1930s, coincided with an international financial crisis which, especially after the Mexican moratorium of 1982, made the recovery of growth impossible. The facts and economic consequences of that crisis are well known, but the political reasons which caused us to describe this episode as marking the end of the pact and of the developmentalist State are less familiar (Fiori, 1984).

In this sense, the term "democratic transition", in the case of Brazil, conceals various aspects of a political crisis which evolved from the exhaustion of the authoritarian regime into a situation of chronic ungovernability. History has highlighted two decisive events in this political decomposition of "bureaucratic authoritarianism" (O'Donnell, 1977; O'Donnell and Schmitter, 1988):

i) The "lack of electoral discipline" of the urban middle classes, which, beginning with the 1974 elections for the National Congress, inflicted a series of defeats on the government, obliging the military regime to adopt a strategy of "controlled openness" and successive hurried electoral and political party reforms;

ii) the "lack of trade union discipline", which, beginning with the success of the 1978 and 1979 strikes in the São Paulo automobile industry, marked the emergence of a new form of trade unionism, independent of the State, and of a new working class no longer willing to accept union and wage tutelage. At that time, workers began to question, in a manner which was at once radical and "modern", the continuation of a system of industrialization governed by a policy of "low wages".

In our judgment, however, the death-blow to the authoritarian regime came from the "lack of discipline of capital". This blow was delivered by the business sector when, beginning in 1977-1978, it definitively ceased to display solidarity with General Geisel's "Prussian" proposal to save the developmentalist project through what the business sector considered to be a firm option for "State capitalism". Contrary to what had happened in the past, this time there was an outright veto of the global strategy itself which had been followed (though not in a planned fashion) since the 1930s.

From that time onwards, the Brazilian business sector was converted to the cause of "democratization" and came to be ever more radically opposed to the old developmentalist objectives. The rules of the old conservative agreement were called into question, thus destroying the triple economic and political support for Brazilian industrialization. Although the State and foreign capital began to "desert" for economic reasons as from 1982, the first group to abandon the pact was the national business sector, which did so for eminently ideological reasons. This is a decisive element for understanding the ungovernability of the 1980s, and it is even more important for understanding the roots of this new organic and terminal crisis of the developmentalist State.

### III

#### Unknown quantities in the present situation

The facts speak for themselves. During the 1980s, there were eight monetary stabilization plans in Brazil, four different currencies, 11 different indexes for calculating inflation, five price and wage freezes,

14 wage policies, 18 changes in the exchange regulations, 54 modifications in the price control rules, 21 proposals for external debt negotiations, and 19 government decrees on fiscal austerity. And it is

symptomatic that this political and economic calamity began precisely in 1979, when the Finance Minister of the Figueiredo government (1979-1985), Delfim Netto, changed the value of the currency and of wages through pre-established monetary correction, a devaluation of the exchange rate, control of interest rates and an increase in the levels of wage indexing.

All this occurred simultaneously with a change in United States monetary policy which set off a general depression which was to last until the mid-1980s, thus causing a sharp increase in the external debt of debtor countries and closing the door to a new Brazilian attempt to "flee ahead" on the basis of fresh foreign indebtedness. It also occurred at the same time that the Brazilian business sector and working class were questioning the basic rules which had governed their political relations with the developmentalist State. Since then, the critical manifestations of this state of affairs have increased ever more rapidly and the loss of power on the part of the State has been reflected still more clearly in the vacillation and impotence of its economic policy in the face of rapid inflation and the persistence of economic stagnation.

It was in this context, and especially in the second half of the 1980s, that the conservative political elites and the main leaders of the Brazilian business sector enthusiastically adhered to what John Williamson (1990) called the "Washington consensus": an orthodox programme of monetary stabilization, accompanied by a "structural" reform package designed to deregulate economic activity, privatize the State-owned productive sector and open up domestic economies to international competition. These were ideas which had adorned business sector rhetoric during the recessive cycles, but which it had never been possible to put into practice because of the political veto of the factions which could have been most directly affected by such stabilization.

Today, however, this new liberal consensus is much more vigorous than in the past. The problem lies in the fact that these old-new ideas are no longer able to solve, either analytically or prophylactically, the difficulties and impasses faced by the Brazilian economy and society, due precisely to the contradictory success of the industrialization policy which the national business sector criticizes today.

These matters indicate that the current paralysis of the Brazilian State is not due to the weakness and

fragility of its economy, but rather to the fact of having completed a heavy industrialization programme on a scale no longer readily adaptable – except at enormous economic and social cost – to the changes which have taken place in the international context.

From a strictly economic point of view, this is the great problem: the Brazilian economy, unlike smaller economies, does not admit of viable solutions through the export sector, and since it does not have really meaningful forms of complementarity with any regional trade bloc, the only way out is for the country to pursue a complex course of thoroughgoing productive and technological restructuring.

However, for such restructuring to be viable, the strategy to be adopted would have to be the opposite to that which the Brazilian intellectual, political and business sector elites are proclaiming so enthusiastically, because what is needed is a national State capable of assuming strategic command of an effort to construct growth scenarios and trajectories.

The State can no longer keep on using the old formula of "fleeing ahead" and "low wages". Overcoming the current crisis requires the preparation of an appropriate strategy and presupposes a complete realignment of the old commitments between the State, private capital and the workers. This is the true essence of the reform of the State which is needed today: a reform much more profound than that undertaken in the 1930s, and which has actually already begun with the re-democratization of political and labour union institutions, but which will still have to face many obstacles in the future, especially because, in contrast with neo-liberal thinking, this State must be "strong", without being over-large and authoritarian, as was the developmentalist State.

Consequently, in contrast with neo-liberal convictions, the transformations called for today must seek a new and decisive role for the State, which should be made the central pillar of business sector strategies for the conquest of new markets, as well as being an active promoter of policies designed to further social welfare and retraining of the work force. This would be a State which is at once strong, flexible, autonomous and democratic, with the responsibility of formulating and strategically articulating a new style of development compatible with the promotion of social and political citizenship for the sectors of the population which have been marginalized to date.

Quite a problem! This project presupposes the adoption of a new pact or commitment radically different from that which arose in the 1930s, and in

these first years of the 1990s this still seems a challenge comparable with squaring the circle.

(Translated from Portuguese)

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## Guidelines for contributors to *CEPAL Review*

The editorial board of the *Review* are always interested in encouraging the publication of articles which analyse the economic and social development of Latin America and the Caribbean. With this in mind, and in order to facilitate the presentation, consideration and publication of papers, they have prepared the following information and suggestions to serve as a guide to future contributors.

—The submission of an article assumes an undertaking by the author not to submit it simultaneously to other periodical publications.

—Papers should be submitted in Spanish, Portuguese or English. They will be translated into the appropriate language by ECLAC.

—Papers should not be longer than 33 double-spaced letter-size pages (US quarto), but shorter articles will also be considered. The original and one copy should be submitted, as should the diskettes, if any (in IBM or compatible Word-Perfect format).

—All contributions should be accompanied by a note clearly indicating the title of the paper, the name of the author, the institution he belongs to, and his address. Authors are also requested to send in a short summary of the article (no more than 250 words) giving a brief description of its subject matter and main conclusions.

—Footnotes should be kept to the minimum, while bibliographical references and direct quotations should be carefully checked, since they are the responsibility of the author. It is also recommended that the number of tables and figures should be reduced to the minimum and that they should not duplicate information given in the text.

—Special attention should be paid to the bibliography. All the necessary information must be correctly stated in each case (name of the author or authors, complete title (including any subtitle), publisher, city, month and year of publication and, in the case of a series, the title and corresponding volume number or part, etc.).

—The editorial board of the *Review* reserve the right to make any necessary revision or editorial changes required by the articles.

—Authors will receive a courtesy copy of the *Review* in which their article appears, plus 30 offprints of the article, both in Spanish and in English, at the time of publication in each language.



## **Recent ECLAC publications**

**A collection of documents on economic relations between the United States and Central America 1906-1956.** (LC/G. 1629-P), Santiago, Chile, May 1991, 398 pages (English only).

The documents included in this collection provide direct information on the most important external linkages of Central America during the twentieth century. They reveal that the pervasive presence of the United States is one of the keys for understanding the current economic and social evolution of the Central American countries. It is clear that, for Central America, the twentieth century has been the century of the United States.

The documents included contain few references to current conditions in the Central American countries or to the positions they assumed in negotiations with the United States Government and the companies of that country. With few exceptions, what they reveal is the point of view of that government, as reflected in the dispatches sent by its diplomats stationed in Central America. Those interested in the Central American points of view must consult the national archives of each country.

This fairly limited sample –representative, but not exhaustive– shows the richness of the store of original documents kept in the National Archives of the United States. Nevertheless, several important events of the period were not documented in those archives (for example, the economic consequences of the United States military intervention in Nicaragua between 1911 and 1933), and they are therefore absent from this collection.

The period studied was chosen for pragmatic reasons: the documentation in the National Archives of the United States has been classified by topics since 1910, while 1956 is the latest year available to the public.

This collection, which includes some virtually unknown documents, makes it possible to identify the profound economic and social changes which occurred in the region during those years. It may also lead historians to examine the special relationship between the United States and Central America during this century, together with the characteristics of Central American development, and may serve to discourage rough generalizations which misinterpret and fail to reflect the ongoing dynamics of that intense and varied relationship.

The documents included, classified by topics, are presented in chronological order in five chapters. The first chapter contains documentation on the general economic conditions prevailing in Central America in three different

periods: early in the century, during the crisis of the 1930s, and after the Second World War.

The second chapter contains documents on trade relations between the United States and the Central American countries, covering negotiations on trade agreements, evaluations of their implementation, and the termination of those special trade relations.

The third chapter contains documents on development financing, as undertaken in the 1920s, and illustrates the difficulties some countries had in servicing their foreign debt during the crisis of the 1930s.

The fourth chapter refers to foreign investment, covering investments in telecommunications, railroads and the banana industry, and brings out some important differences between the negotiations on those investment flows in the 1930s and in the 1950s. The chapter ends with an examination of the prospects for foreign investment, which a team of international consultants considered to be favourable in the early 1950s.

The fifth and final chapter is a collection of brief but very illustrative documents about the process of economic integration which the Central American governments began to promote in the 1950s.

**Economic Survey of Latin America and the Caribbean, 1990** (LC/G.1676-P and Add. 1). Santiago, Chile, June 1991, 249 pp. (vol. I) and 590 pp. (vol. II).

This publication is the complete and definitive version of the *Economic Survey of Latin America and the Caribbean* for 1990, which initially appeared in sections in the course of 1991, and is divided into two volumes. The first part of volume I gives an overview of the main economic trends in the region, analysing in greater detail the international context, levels of activity, overall supply and demand, inflation, employment and wages, the external sector and external indebtedness, and, finally, the evolution of the economies of the Caribbean. The second part of this first volume analyses the international economic situation and the evolution of public finances in the region.

Volume II reviews the economic evolution of each country of the region during 1990.

**Statistical Yearbook for Latin America and the Caribbean, 1991.** (LC/G.1798-P), Spanish/English bilingual edition, Santiago, Chile, March 1992, 779 pp.

This publication is divided into two parts. The first part contains updated statistical series on social development and welfare, economic growth, capital formation and financing, external trade and external financing. The second part includes statistical series on population, national accounts, domestic prices, the balance of

payments, external financing, external indebtedness, external trade, natural resources and production of goods, infrastructural services, employment and social conditions. An appendix gives various estimates for 1991.

**Equity and changing production patterns: an integrated approach** (LC/G.1701 (SES. 24/3), Santiago, Chile, February 1992, 252 pp.

In this document, which the ECLAC Secretariat presented at the twenty-fourth session of the Commission, it is asserted that although most of the countries of the region have made significant progress in the stabilization and restructuring of their economies, this does not mean that future success is ensured. Indeed, in some cases democracy itself is in danger, because the benefits of the economic reforms which have been effected have been achieved at the expense of the most impoverished sectors of the population. This need not necessarily be the case, however: economic advances and social progress not only should, but indeed can, go hand in hand. This is possible when—as has occurred in a number of developing countries, although less frequently in Latin America—the policies applied take advantage of the important complementarities which exist between growth and equity: productive employment, investment in human resources, and modernization in order to achieve international competitiveness.

The trickledown theory is rejected as illusory, since economic growth has rarely achieved a broad distribution of its benefits within a reasonable period of time. The narrow view that growth and equity are always in conflict, which imposes on social policy the nearly impossible task of compensating for the regressive effects of various economic reforms, is also rejected. Instead, it is held that economic and social policies must maximize the complementarities and minimize the conflicts between those two objectives, so that considerations regarding distribution are incorporated into economic policy and those relating to efficiency are taken into account in social policy.

Together with highlighting these desirable complementarities, with which many would be in agreement, the document translates them into operational proposals. It recognizes the importance of establishing correct prices, of applying an outward-oriented growth strategy, and of leaving production basically to the private sector. It notes, however, that because many markets and essential institutions in developing countries tend to be very incomplete and segmented, the fruits of growth tend to be biased and highly concentrated. In order to overcome these failings and critical constraints caused by unnecessarily slow and regressive growth, the State must assume an active, though selective, role.

By way of example, it is considered that the outward reorientation of the industrial platform of the region and

the achievement of international competitiveness are extremely urgent and pressing tasks. To that end, it is proposed that not only are low tariffs and a high and stable exchange rate necessary, but also a transitory pro-export orientation in economic policy rather than a merely neutral approach, because currently the promotion of “emergent industry” is no longer so much a question of production as of penetration into international markets. Thus, companies which find new markets for their exports or new products to sell on foreign markets are true “Schumpeterian” innovators and, as such, warrant transitory incentives for their efforts.

It is also noted that competitiveness is not just a matter of correct prices and exchange rates, but depends ultimately on productivity and technological modernization, both inside and outside the enterprise. Raising productivity requires the strengthening of the technological infrastructure, especially in the areas of telecommunications and informatics, together with national research and development activities more closely linked with the productive system and the modernization of those elements of the business environment which are determinants of competitiveness, such as transport systems, ports and marketing facilities.

It is emphasized that, in order to achieve sustained growth, increased public sector saving is necessary. However, the efforts made in this direction so far have been very one-sided, since they have concentrated on reducing expenditures much more than increasing revenue, without which the indispensable and too long delayed investments in human capital, infrastructure and communications will not be possible. It is noted that there is ample scope for increasing such revenue, as the average private sector tax burden in the region is around 16% of GNP: i.e., 10 percentage points less than in a typical member country of the Organization for Economic Cooperation and Development (OECD). Moreover, the whole of this difference is explained by the very low level of direct taxes (3% of GNP, compared with 7% in the recently industrialized Asian countries and 13% in the OECD countries). Consequently, in order to give the fiscal system a more progressive nature, it will be necessary not only to focus expenditures on the poor, but also to increase the proportion of progressive taxes in overall revenue.

In particular, private savings must increase, if adequate levels of investment (20% of GNP) are to be achieved and productive employment is to be expanded. Emphasis is placed on the need to ensure positive real interest rates, although it is doubted that the mere freeing of those rates will lead to significant increases in private saving. The compression of wages is flatly rejected as a mechanism for increasing savings, and instead increased institutional savings are suggested, especially those related to social security, for even those pension systems which have positive cash balances usually register deficits from an actuarial point of view, since the current decreases in

fertility rates and the continued increase in life expectancy will raise the number of retired persons per active worker by 30% by the year 2020. It is therefore necessary to begin to reserve funds now, by increasing social security contributions and adjusting benefits as a function of longer life expectancies.

In order to increase productive employment, it is likewise necessary to improve the allocation and efficiency of investment and credit. Financial liberalization, although important in some ways, will not fill the virtual void of private credit for post-secondary training and education, nor will it give medium-sized and small companies access to capital markets. In order to correct the current under-investment in those very profitable areas, the use of pension funds to guarantee bank loans for family investment in human capital is proposed, together with the promotion of new financial instruments (for example, leasing for long-term capital and factoring for working capital), as a means of overcoming the problems of guarantees and high costs associated with loans to small and medium-sized companies.

No one doubts the need for greater public investment in human capital (training, education, nutrition, family planning). However, there is an urgent need to raise the quality (rather than the coverage) of education. To this end, it is proposed that the educational system (especially secondary education) should be more directly linked to the labour market, rather than to the University, and that greater autonomy should be given to the teachers and authorities of each establishment, with the efforts of the national authorities being concentrated on "quality control" and programmes of distributive compensation, while financial incentives for teachers and establishments should be linked to student achievement (adjusted to take initial conditions into account) rather than teacher seniority.

Finally, in order to encourage increased productivity and employment, a significant part of wages could be determined by company performance (profits, sales, production, etc.), as is done very successfully in Japan, Korea and other countries, rather than simply on the basis of the number of hours worked, as is the general rule in Latin America. Such participative wage formulas could also serve to reduce tensions between labour and management and achieve the vitally necessary cooperation between those two sectors, which would be more in keeping with the present situation, in which the real "adversary", both for labour and management, is the competition on foreign markets.

The proposals made in this document highlight the complementarities –rather than the conflicts– between growth and equity, institutions and correct prices, and the quality rather than the mere size of the State, to which a selectively active role is assigned. Thus, the report fulfills its objective of proposing an integral approach for growth with social equity, and in the final analysis, inasmuch as it enriches and, in many ways, surpasses the Washington

Consensus, it actually broadens the range of strategic options available to developing countries.

**Education and knowledge: Basic pillars of changing production patterns with social equity (LC/G.1702 (SES.24/4)/Rev. 1), Santiago, Chile, 18 March 1992, 257 pp.**

A preliminary note to this study indicates that, as an exception to the practice of maintaining the authors of United Nations documents in institutional anonymity, it is only fair on this occasion to recognize that the leading inspirer of this study was Fernando Fajnzylber, Director of the Joint ECLAC/UNIDO Industry and Technology Division until his untimely death at the end of 1991: "His own direct contributions, the encouragement he gave to colleagues and collaborators, the critical review he made of the various preliminary versions of this study, and the numerous consultations he undertook with a view to enriching the text left an indelible imprint on the whole project. On the very day he finished the final review of the text, his life was prematurely cut short by a sudden heart attack".

The first part of this study briefly describes the pattern of development of Latin America and the Caribbean after the Second World War, the "painful learning experience" of the 1980s, and the challenges of democratization in the 1990s. Reference is then made to the ECLAC proposal for changing production patterns with equity, to current trends in the area of international production, and finally to the nature of the strategy proposed in this document, which seeks both changes in production patterns and greater equity.

In the second part, which is of a diagnostic nature, an analysis is made both of various national-level initiatives designed to bring about changes in education, training and scientific and technological studies, and of recent theoretical contributions regarding the linkages between education and economic development. The current debate about these issues in some developed and recently industrialized countries is summarized in an appendix.

The third part presents the broad outlines, expressed as *idées-force*, of the proposed educational strategy, with emphasis on primary and secondary education, secondary-level vocational training, and the strengthening of technological development.

In the fourth part, on the basis of the background information analysed and within the framework of the orientations already presented, a set of policies for putting the proposed strategy into practice is suggested. The actions and measures proposed are accompanied by boxes illustrating experiences, designs, methodologies and applications of those policies in various contexts, both inside and outside the region.

In the fifth and final part of the document, the order of magnitude of the resources needed to implement the proposed policies is estimated, purely for purposes of illustration.

In recent decades, educational, training and scientific and technological development systems have undergone significant, although incomplete, expansion in quantitative terms in most countries of the region. Nevertheless, they display obvious deficiencies in terms of the quality of their results, their relevance to the demands of the economic and social environment, and the degree of equity with regard to the access of the different social strata to them, while their institutions tend towards rigidity, bureaucracy and scant linkage with their surroundings. The 1980s, which was characterized by restrictions on public resources, growing openness to the international economy and democratization, marked the end of a cycle and made it a matter of urgency to progress to a new stage in which growth and performance will be determined by the degree of importance that societies assign to education and the production of knowledge.

The proposed strategy revolves around certain objectives (citizenship and competitiveness), guiding criteria for policy formulation (equity and performance), and guidelines for institutional reform (national integration and decentralization). The strategy has three main features. It is *inductive*, which sustains its viability and is reflected in its design, based on recognition of the changes observed in regional and international conditions, on proper appreciation of the emergent *idées-force* which influence the postures, aspirations and perceptions of the different protagonists in the process of generation and communication of knowledge, and on careful analysis of the experiences in the region and elsewhere which point to trends that could become generalized. At the same time, it is *systemic*: that is to say, it takes into account both the linkages that exist between education, training, science and technology and the productive system and the multiple nexuses binding together the economy and society at the individual and collective levels. Finally, it assigns great importance to *institutional change*. Although the need for additional financial resources is fully recognized and is even quantified, an effort is made to show that those resources –although indispensable for reform– will not be sufficient for correcting the shortcomings unless they are accompanied by profound changes that will give rise to a set of institutions open to the demands of society.

The changes proposed here are oriented in the following main directions: i) from the political point of view, the aim is to give the activities of production and communication of knowledge the status of long-term strategic tasks requiring the broadest possible consensus among the social actors and a stable financial commitment for their execution; ii) from the point of view of content, action is to be focussed on the results of education,

training and science and technology and on their linking-up with the demands for improvement of the performance of persons; iii) from the institutional standpoint, the aim is to break the isolation of educational establishments and of those engaged in the production and communication of knowledge, and to introduce forms of action which will offer the actors in this field a greater degree of autonomy in decision-making and greater responsibility for results.

The policy proposals for the implementation of the strategy are grouped around seven objectives. The first is to overcome the relative isolation of the system of education, training and acquisition of scientific and technological knowledge, opening it up to the real needs of society. Overcoming that isolation is considered to be the richest potential source of dynamism and change for each sub-system and for the relationships among all of them. The next two objectives refer to the results sought by such greater openness, namely, to ensure universal access to the codes of modernity and to promote creative advances in access, dissemination and innovation in the field of science and technology. The remaining four objectives are of an instrumental nature: responsible management of institutions; professionalization and enhanced roles for educators; financial commitment on the part of society to education, training and scientific and technological efforts; and regional and international cooperation. For each of these objectives, guidelines are presented for the various components of formal education, training and scientific and technological activities, and, very specially, for improving their linkages with each other and with the productive sector.

Regional and international cooperation can play an important role in the application of the strategy and the proposed policy measures, especially in the following four areas: human resources training in the countries of Latin America and the Caribbean with a view to more efficient use of the installed capacity of the Universities and academic centres of the region; establishment of closer links between the system of education and generation of knowledge, on the one hand, and the productive and social development sectors on the other; research into education and the process of the generation, communication and use of knowledge; and research on the process of the application of the proposals in operational and institutional terms, at the level of individual countries.

The performance of the proposed tasks presupposes financial support for implementation of the changes suggested in each sub-system and strengthening of the ties between them. In the past, development banks played a decisive role in the expansion of productive capacity and the emergence of new sectors, mainly through large public and private companies. During the 1980s, however, those banks lowered their capacity for action, both in terms of resources and with regard to the profile of their activities. For the 1990s, a new space is being opened for them: that

of the tasks directly related to education and the production of knowledge, seen as the heart of the process of changing production patterns with equity. In concrete terms, the development banks, in collaboration with the private financial sector, could promote institutional mechanisms for supporting investment in human resources, scientific and technological development and the expansion of small and mid-sized companies, and for establishing linkages among the different sub-systems.

The proposed strategy places education and knowledge at the heart of the process of changing production patterns with equity, as necessary elements for

promoting the development of the region and as objectives which can be achieved through the application of a coherent set of policies. The partial experiences already underway today, together with the perceptions of those involved in the process of education and the production and communication of knowledge, tend to converge in the same direction as the guidelines proposed in this study. This is a massive, complex, inevitable task, which is already underway; its results will condition both the domestic economic and social evolution of the countries of the region and the weight they will have within the world context.





## ECLAC publications

ECONOMIC COMMISSION FOR LATIN AMERICA AND THE  
CARIBBEAN  
Casilla 179-D Santiago de Chile

### PERIODIC PUBLICATIONS

#### CEPAL Review

*CEPAL Review* first appeared in 1976 as part of the Publications Programme of the Economic Commission for Latin America and the Caribbean, its aim being to make a contribution to the study of the economic and social development problems of the region. The views expressed in signed articles, including those by Secretariat staff members, are those of the authors and therefore do not necessarily reflect the point of view of the Organization.

*CEPAL Review* is published in Spanish and English versions three times a year.

Annual subscription costs for 1993 are US\$16 for the Spanish version and US\$18 for the English version. The price of single issues is US\$10 in both cases.

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#### Anuario Estadístico de América Latina y el Caribe / Statistical Yearbook for Latin America and the Caribbean (bilingual)

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#### Libros de la CEPAL

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