

CEPAL

REVIEW



UNITED NATIONS

20

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Review

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Technical Secretary
ADOLFO GURRIERI

Deputy Secretary
GREGORIO WEINBERG



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August, 1983

Notes and explanation of symbols

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 may not necessarily add up to the corresponding totals, because of rounding.

NOTE BY THE DIRECTOR

When, on 11 February of this year, His Excellency Dr. Osvaldo Hurtado, Constitutional President of the Republic of Ecuador, wrote to Enrique Iglesias, Executive Secretary of ECLA, and Carlos Alzamora, Permanent Secretary of SELA, asking them to prepare as soon as possible "a set of proposals designed to develop the response capacity of Latin America and to consolidate its systems of cooperation", he underlined both the seriousness of the crisis affecting the region and the responsibility of the international organizations in helping to tackle it.

At the same time, President Hurtado invited all the Heads of State of the Latin American countries to support his initiative and participate in its formulation, in the deep conviction that "the ideological, political, economic and territorial differences which separate our nations must not be allowed to constitute obstacles". He had earlier emphasized that the collaboration of the governments of these countries could considerably enhance the contributions of ECLA and SELA aimed at formulating a programme of action which will make it possible to create the conceptual instruments needed to overcome the present difficulties and also help to ensure achievement of "the permanent objectives of justice, peace and freedom".

On 16 May, in response to President Hurtado's inspiring initiative, the two Secretaries sent him a covering letter accompanying the document "Bases for a Latin American response to the international economic crisis". In view of the importance of these documents, we consider it useful and appropriate to reproduce them in this issue of *CEPAL Review* in order to give them still wider circulation.

Following the same line of action, and with the object of analysing the international economic crisis and the response capacity of Latin America, ECLA convened in Bogotá from 19 to 21 May a group of some 30 leading figures representing the economic and political life of the region, under the chairmanship of the President of Colombia, Dr. Belisario Betancur. After an intensive exchange of opinions, this group drafted a declaration which is also presented in this issue under the title "The world crisis and Latin America".

**Letter from the Constitutional President
of the Republic of Ecuador,
H.E. Dr. Osvaldo Hurtado**

**TO MESSRS. ENRIQUE V. IGLESIAS, EXECUTIVE SECRETARY, ECLA,
AND CARLOS ALZAMORA, PERMANENT SECRETARY, SELA**

Quito, Ecuador, 11 February 1983

Dear Friend:

Now, as 1983 begins, there are few remaining doubts about the gravity of the international economic situation. Not since the Great Depression of the 1930s has the world known such a serious and prolonged crisis. Almost no society has managed to escape its pernicious effects, for the problems suffered by the countries of the developed North and the developing South, those of the socialist East and the West are all similar. The fact that this crisis affects all societies, whatever their ideological orientation, political system or economic model, is the best demonstration that we are in the presence of a universal phenomenon involving all nations.

Although there is no country today which is free from economic difficulties, it is the peoples of the Third World, and among them those of Latin America and the Caribbean, who are suffering the most political and social problems, for in 1982 both the gross domestic product and the per capita income decreased in terms not witnessed in the past forty years, while the average inflation rate was by far the highest yet recorded in the region. If the high growth indexes of the past decades—which today can be appreciated in all their significance—did not eliminate this deep wound of misery, injustice and underemployment or unemployment which divides our societies, imagine what will happen in the future if the economic depression is prolonged beyond 1985, as is feared. What is at stake, then, as never before, is the social peace of the nations and the stability of the democratic system—in brief, the fate of vast human communities which are seeing their unresolved social problems grow worse day by day, and are fearfully becoming aware of the possibility of total disaster.

It was always thought that the shortage of financial resources was the main obstacle to the development of our continent. But if we look back at the past decade and analyse the current situation, we reach the inevitable conclusion that the overabundance and misuse of the credit provided by the private international banking system, together with its short term and high interest rates, are an essential factor in the crisis. When, in the second half of last year, the external debt was nearing the astounding figure of US\$ 300 000 million, and the Latin American economies required foreign exchange as never before in order to import and pay interest and capital, there was a sudden change from an unlimited supply of credit to an absolute shortage. To these trends should be added the decline in the exports of basic commodities because of the falling growth rate of the industrialized countries, the restrictions they have established, the technological changes introduced in production processes and the dominance of the transnationals in world trade.

The special features of the current economic crisis and the obvious limitations of the measures recommended by orthodox economics, whatever their ideological source, are sufficient grounds for concluding that we find ourselves facing a completely new phenomenon which probably demands the formulation of a new kind of economic thinking. If we add to this the fact that the policies practised by the industrialized countries affect all our nations alike and that we are also witnessing a redefinition of the international economic system which has prevailed since the war, it becomes clear that

Latin America's presence in such a decisive historical process, on which the overcoming of the crisis and our future economic and social development will depend, is absolutely essential.

The crisis is certainly of such magnitude that at times it seems to overwhelm us, but it is also true that the peoples of Latin America and the Caribbean have the necessary qualities for overcoming it. In their long history they have shown stubborn determination to dominate a generous but difficult geography; energy and perseverance to consolidate the States they have set up for themselves; broad-mindedness and creativity to enrich their ancestral culture; imagination to assimilate and renew technology; business skills to carry out new economic activities; and a spirit of hard work and sacrifice. Moreover the region has an abundance of resources, it has progressed in its economic and social development and there has been an improvement in the technical teams responsible for State administration.

The difficult circumstances affecting our countries make it urgently necessary to formulate a Latin American response to the crisis, and this will involve a concerted effort to make full use of all our capacities, resources and institutions.

ECLA, first, and later SELA, have rendered invaluable services to each of the countries of Latin America and the Caribbean and to the region as a whole. The studies by the first-named body have made it possible to form our own economic thinking and have offered concrete solutions to many problems. SELA, for its part, was precisely conceived as a regional forum where the member countries could seek joint answers to their common difficulties. Today, when our continent is living through a dramatic situation, it seems essential that such highly reputed technical bodies should once again make their contribution.

Consequently, on behalf of the Government of Ecuador, I request you, Gentlemen, as Executive Secretaries of ECLA and SELA, to prepare as soon as possible a set of proposals designed to develop the response capacity of Latin America and to consolidate its systems of co-operation.

The contributions of ECLA and SELA, enhanced by those which the Governments of the region may feel it appropriate to make, should give rise to a Programme of Action covering the next few years which will make it possible to face the serious immediate problems, always bearing in mind the permanent objectives of justice, peace and freedom.

This proposal and the request made in this letter are being communicated to the Heads of State of the Latin American countries, with an invitation to support such a plan and participate in its formulation, in the deep conviction that the ideological, political, economic and territorial differences which separate our nations must not be allowed to constitute obstacles. I believe that it will also be necessary to have the help of other Latin American organizations which could offer their valued collaboration in their specific fields of competence.

May I express my appreciation for your kind consideration of my request, and my warmest personal regards.

Sincerely,

OSVALDO HURTADO,
Constitutional President of the
Republic of Ecuador

Letter from Messrs. Enrique V. Iglesias,
Executive Secretary, ECLA, and Carlos Alzamora,
Permanent Secretary, SELA

TO H.E. DR. OSVALDO HURTADO,
CONSTITUTIONAL PRESIDENT OF ECUADOR

Quito, 16 May 1983

Mr. President,

The joint proposal which we are submitting at your request constitutes an urgent appeal for concerted action by Latin America. It proposes that, in the spirit of your important initiative, immediate decisions should be taken to enable the region, through development of its capacity for response and the strengthening of its co-operation systems, to stand up to the serious situation which it is currently experiencing.

*The structural crisis and external vulnerability of Latin America
and a new approach to Latin American development*

Latin America is experiencing what is probably its most serious economic crisis in the last half-century. Economic growth has stopped and the standard of living has gone down in all the countries of the region, with serious social and political consequences.

This crisis is affecting every aspect of economic life. It is reflected in an unprecedented level of indebtedness, equivalent to three times the value of the total annual exports of the region; in the growing cost of servicing this debt, which is already consuming an extremely high percentage of export income; in the sharp drop in that income, affected by a decrease in commodity prices which has brought the real value of many of them down to levels lower than those of 1930, and in the abrupt decrease in the net inflow of capital. All these factors and the policies adopted to correct them have forced a substantial reduction in the imports vitally needed for maintaining the rhythm of operation of the economic apparatus and have produced inflation which is increasingly affecting all the countries of the region.

The nature of this crisis, which originated in the industrialized countries and was transferred, with all its consequences, to Latin America, has highlighted in all its aspects Latin America's structural vulnerability, dangerous dependence on external factors, and insufficient utilization of the potential inherent in the region. And it makes clear that solving the problem basically depends on the adoption of decisions modifying the strategies and policies which have helped to emphasize that vulnerability and to limit Latin America's possibilities of exercising its capacity for joint response.

For Latin America is suffering the effects not only of the international economic crisis but also—and this is even more tragic—of its own crisis in meeting it. In order to overcome its problems, Latin America must use this dual crisis as an opportunity and an incentive to reconsider those models and styles of development which have made it so vulnerable and dependent; to redefine its political and social objectives; to put into operation an integral action programme designed to strengthen regional co-operation and integration as pillars of its economic security and independence; and to realize its potential for joint negotiation with a view to correcting the pernicious asymmetrical structure of its external relations.

While both internal and external realities point to that path, the current situation is presenting us, in all its harshness, with evidence of the stagnation or failure of the integration schemes, doomed

by errors of commission or omission to recurrent dangerous crises, the weakening of many co-operation mechanisms, such as the Latin American multinational enterprises, for which it has not been favourable; and the deterioration of a good portion of intra-regional trade because of individual reactions to balance-of-payments problems.

In short, there has been a multiplicity of individual reactions which cause injury to all by attempting to meet separately a crisis whose origin and manifestations are common to all the countries of the region and, as a result, require co-ordination at the regional level, because in this context individual solutions are no longer viable.

Therefore, although there are no miracle answers to the immediate problems of Latin America, their solution does require immediate decisions and actions, which must necessarily be along the lines of fundamental solutions seeking to restructure the region's capacity to defend itself against the causes of its vulnerability, on the basis of regional complementation, and to consolidate its bargaining power by means of joint political efforts. Hence, our proposals go beyond the current economic situation, although they are of course designed to meet the current emergency.

The three levels of the Latin American response

Latin America cannot continue to wait for the solution of its problems to proceed from external stimuli alone. It was because of this passivity that the vulnerability of the region has increased in proportion as the national economies have opened up to an international economy that is transnationalized and in crisis. This facilitated the transmission of problems to the region and made the latter bear a disproportionate part of the cost of the industrialized countries' own adjustment process.

The development of Latin America will be a long task, based essentially on the internal effort of each country and on the reinforcement of Latin American co-operation and integration. It will depend to a large extent on whether Latin America can manage to check the draining of its resources currently caused by the asymmetrical pattern of its external trade and financial relations, and rechannel those resources to benefit its own development. It will also depend on whether it knows how to utilize its own regional market, which is already of sufficient magnitude to play an important support role as a dynamic element of expansion of the trade and industrial development of the region.

It is necessary therefore to define future Latin American action on three fronts with as many objectives.

In the *domestic sphere*, it is necessary to correct development strategies that are highly inequitable from the social point of view and are based predominantly on the consumption patterns of the high-income groups, involving excessive external dependency produced through raw materials exports, the industrial structure, or massive capital imports. This will mean adjusting development strategies to make more intensive use of the domestic and regional markets and to seek instead to meet the basic needs of the masses. Only in this way can society as a whole be asked to make the sacrifices needed to overcome the current economic situation, and only thus can the foundations of sustained and autonomous development be laid. It will also call for the internal generation of most of the resources needed for maintaining the investment levels required in order to transform the productive apparatus. This will not be possible without substantial containment of non-productive expenditures—which, because of the level and rate they have attained, are compromising the very objectives of security pursued—and of consumption which is only within the reach of limited social sectors.

In the *regional sphere*, the complementation of production, trade and services must be restructured on the basis of the principle of Latin American preferentiality. This will make it possible to increase intra-regional trade by turning aside imports which are now coming from other areas and which can be replaced by the region, to take advantage of existing idle capacity, and to tackle the worsening external imbalances. It is essentially a question of securing adequate complementation at

the regional level, while preserving the requirements of economic efficiency and equal benefits for all the countries of the region. This involves effectively linking up regional integration and co-operation and fully incorporating them into national policies.

Only in this way can the policies of inwardly-directed complementation and joint action *vis-à-vis* the rest of the world be affirmed, no longer as mere accessory elements of a strategy based on other principles, but now as vital supports for the autonomous orientation of the development which Latin America requires at the present time.

In the *international sphere* it is necessary to restructure the bases of the region's linkage with the industrialized countries and strengthen the bonds with other developing regions. In this way, and by organizing the region's joint bargaining power, it will be possible to correct the structural and conjunctural imbalances suffered by Latin America, and the continent will be able to contribute to the integral restructuring of the international economic system.

Latin America's firm support for the great objectives of the international dialogue proposed by the developing countries in international forums is here more essential than ever.

Towards a regional programme of action to meet the crisis

Any regional action programme should be based on shared values and criteria. In order for it to become a reality, it must necessarily enjoy the express and continued support of the highest political levels and the backing of all the social forces of each country. It should aim at satisfying the needs of each society, and be based on the criteria of harmony and justice in the distribution of efforts and benefits.

Those same criteria should also be applied in the regional sphere, putting into practice in Latin America what we justifiably preach to the outside world. In this connection, the economic problems of the smaller countries and those lacking natural resources require the co-ordinated action of all of Latin America, with the objective of supporting their development and bringing them the means they need in order to be able to participate fully in the regional integration process.

In this joint action proposal, it is also incumbent on the Latin American entrepreneurial and labour forces to play a promotional and executive role side by side with governments and regional bodies. This role should be recognized and encouraged by all the sectors of the new Latin American co-operation process and incorporated into the design and planning of its support and motivation schemes.

On the basis of these considerations, we believe it necessary, in the face of the compelling problems confronting the region, to focus our proposals on the problems arising from the burden of the external debt service and trade, and on the need for decisively taking the path of regional co-operation and integration, without prejudice, of course, to the importance of such topics as regional food security or energy co-operation, which are also considered in the attached document, or other areas, such as maritime transport, insurance and re-insurance, and technological development, which also call for joint action directed towards strengthening regional economic security.

The most urgent dilemma confronting Latin America is that while it needs resources in order to maintain a minimum of growth, the stage of external financing with which that growth was sustained in recent times has now come to an end. These resources cannot come from international trade as long as the industrialized countries do not overcome their current economic crisis. And international financial bodies are not currently in a position to provide them either.

We are watching with expectation the signs of recovery which are appearing in a few industrialized countries. We trust that they will become more definite, because in that case Latin America will be able to emerge from the current recession more rapidly. But even if this were to occur, the causes which led it to suffer the impact of this crisis so harshly will remain. For this reason, we believe that the solution can only come from determined joint action by the region.

Latin America has been helping to solve the economic problems of the industrialized countries through the lower prices paid for its exports and the higher interest rates it has had to pay on the

funds loaned to it. However, in view of the severity of the economic situation it is facing, it will be understood that it cannot go on making that sacrifice. On the contrary, we have reached a point at which it has become necessary above all to defend our national economies and protect the production apparatus.

Concerted action on the debt

For Latin America the main goal is to develop, and this means adjusting the servicing of the external debt to the present capacity of the debtor countries to pay, while spreading the accumulated debt appropriately over time so as to be able to keep up the level of essential imports. It means that the renegotiations must be carried out on new bases so that their cost to the debtor countries is less, the burden of the international adjustment required is distributed equitably and it is at least possible to conserve the standard of living of these countries, while safeguarding the independence of national decisions.

This goal calls for regional action which is co-ordinated at various levels and in respect of various actors in the international financial system: action aimed at ensuring that the developed world understands that the surest way to enable Latin America to service its debt is to promote its development, rather than to deprive it of the financial resources it requires.

In order to help reach these objectives, we consider it essential to establish information machinery on the Latin American external debt to facilitate the exchange among the countries of the region of information on the terms on which debts are being refinanced and on the evolution of the international financial markets, as well as, in certain cases, giving governments advisory assistance on handling their external debt and solving the problems derived from it.

Thus, there is an urgent need for concerted Latin American action at the political level to make possible joint consideration of a solution to the problem of external indebtedness, which is having such a severe impact on the majority of the countries in the region. Individual solutions should be based on mechanisms of a global nature, so that each case is no longer treated as though it were a question of a set of isolated financial crises which are unrelated both to each other and to the international scenario which produces them. Action of that kind should be accompanied by other measures aimed at improving the international financial system and providing the developing countries with additional financial resources.

The expansion of intra-Latin American trade

It is necessary, as a second objective, to intensify action on the whole unexplored potential of intra-Latin American trade with a view to at least doubling it in this decade and replacing extraregional imports —particularly imports of food, energy and capital goods— by imports which the region itself can furnish. This requires the adoption of an agreement to ensure that the terms on which the region's commodities gain access to any of the markets of Latin America will no longer keep on deteriorating, that regional trade preferences covering all Latin American countries will be adopted, and that the implementation of compensated partial bilateral agreements will be intensified, especially by increasing State purchases, but at the same time safeguarding the multilateral nature of regional trade.

To make this possible, it will be necessary to strengthen and extend the regional machinery for financing trade and clearing balances. Not only are these viable solutions to the region's conjunctural problem of scarce external resources, they are also points of departure for an accelerated process of regional integration which will permit the full use and expansion of the installed production capacity and the development of our resources. This will also make it possible to apply selective criteria in those cases in which discriminatory restrictions are imposed on Latin American exports and to create sufficient response capacity to ensure that coercive economic measures adopted by third countries can never again hurt a Latin American country.

In the face of the present crisis and the concerted action of the industrialized countries, the dispersion of the Latin American countries makes them ineffective in defending their interests. From the economic point of view, Latin America should organize itself as a unit. This will enable us to prepare ourselves to meet the future with an effective and dynamic structure of preferential complementarity, which will save us from the danger of being vulnerable to the policies followed by other countries and will be in keeping with the interests of the Latin American community.

The instrumentation of the programme of action

The instrumentation of these proposals urgently calls for a large-scale Latin American dialogue, of a type not hitherto seen, to be held in a spirit of understanding and harmony. In this connection we feel it might be appropriate to convene a Latin American Economic Conference. Within the framework of this conference, consideration could be given to the proposals made in the document accompanying this letter, together with such other proposals as may emerge from the initiative which Your Excellency has suggested to the Presidents of the Latin American countries.

This kind of conference should concentrate its efforts on the areas of development financing and intra-regional development and give new impetus to Latin American integration and co-operation. Full political support of its decisions would be of decisive help in putting into operation the mechanisms needed to ensure its prompt instrumentation.

At the same time, this conference could not only strengthen or integrate the existing machinery but also lay the foundations for future Latin American mechanisms for supporting the balance of payments, financing exports and raising the value of the commodities which the region exports. In these times when the Latin American countries are encountering serious financial problems, it may seem utopian to suggest the creation of new mechanisms requiring substantial resources. Experience teaches us, however, that it is at this very moment, when there is every evidence of the need for such machinery, that we must take up the challenge of creating it and that we should, as soon as we possibly can, provide it with the means needed for its operation.

The challenges we shall be facing at the beginning of the next century are being gestated right now. It seems that the last two decades of this century will mark the close of one era and the beginning of another. To embark on that era, it is essential to begin today to design and approve the foundations of the structure which Latin America needs. If this is not done, the growing impact of external factors will limit our possibilities for deciding our own destiny in the economic field and even in those of policy and strategy.

Latin America must answer this challenge in a spirit of unity, with the same solidarity with which it achieved its great accomplishments in the past and the same awareness of its collective interests which inspired it then. Moreover, these challenges are not confined to the area of economic co-operation. Sooner or later it will be necessary to extend and consolidate the Latin American dialogue in the political arena, in order to help Latin America become an area of peace and co-operation through all its length and breadth and between all the countries comprising it. Only in this way can an authentic Latin American community emerge.

This undertaking calls for great political will. We believe that this will is present and that it need only be summoned in order for it to take form. The initiative you have taken, Mr. President, in drawing attention to the gravity of the problems through which the region is passing and calling for concerted action, proves once again that our political leaders are aware of the times we are living in and ready to seek the solutions to the serious problems of today in Latin American unity. And this is how it must be. Rising above the short-term problems which may divide us today, the time has come to recover that collective vision which gave so much inspiration to our Liberators, who saw themselves not just as national emancipators, but as being at the service of the entire region.

To seize the moment in all its fullness is to win through concerted action the force which Simón Bolívar urged us to seek and is the greatest homage we can pay him at the bicentennial of his birth, which we are about to celebrate.

In closing, we wish to express once again to Your Excellency our profound gratitude for the inspiring mark of confidence conferred upon us and upon our institutions by the task which you have set us, and which we have tried to merit with all the intensity bestowed on us by our devotion to the Latin American ideal and our unquenchable faith in this region's destiny.

Accept, Sir, the expression of our highest consideration,



ENRIQUE V. IGLESIAS
Executive Secretary, Economic
Commission for Latin America (ECLA)



CARLOS ALZAMORA
Permanent Secretary, Latin
American Economic System (SELA)

Bases for a Latin American response to the international economic crisis

*Carlos Alzamora T.
and Enrique V. Iglesias*

I

Introduction

On 11 February 1983, the President of Ecuador, His Excellency Dr. Osvaldo Hurtado, sent us a letter in which, after emphasizing the seriousness of the present international economic situation, he noted that "the world has not known such a serious and prolonged crisis since the Great Depression of the 1930s".

In his communication President Hurtado made two statements of great significance. The first of these is that the magnitude and intensity of the crisis today facing Latin America are such that they severely jeopardize in the region, as never before, "...the social peace of nations and the stability of the democratic system: in brief, the fate of vast human communities which are seeing their unsolved social problems grow worse day by day, and are fearfully becoming aware of the possibility of total disaster". The second is that, despite the magnitude of these difficulties "the peoples of Latin America and the Caribbean have the necessary qualities for overcoming them".

It is on the basis of this clear perception of the world and regional situation that President Hurtado asked us, on behalf of the Government of Ecuador "...to prepare as soon as possible a set of proposals designed to develop the response capacity of Latin America and to consolidate its systems of co-operation".

It is in pursuance of such a clear mandate that we have prepared the present document, which reflects our own opinions, enriched by the contributions of the Secretariats of ECLA and SELA and the much appreciated collabora-

tion of the guiding bodies of the Latin American Integration Association (ALADI), the Board of the Cartagena Agreement (JUNAC), the Centre for Latin American Monetary Studies (CEMLA) and the Latin American Energy Organization (OLADE), which sent us valuable views and suggestions for which we are most grateful.

This document is centered on an idea which is clearly expressed in President Hurtado's letter and which we fully share: the economic crisis through which the region is passing is the severest suffered since the war: it affects all the Latin American countries, in different ways, with a previously unknown degree of universality, and its special features make it qualitatively different from any other recent experience.

In these circumstances, Latin America more than ever needs to make a profound and self-critical analysis of the development model based on a type of industrialization highly dependent on the exterior and on the consumption of the middle and upper strata of its societies and the maintenance of a very high share of basic commodities in the region's exports: —a model which furthermore, in recent years, has come to depend increasingly on the massive and increasing procurement of external resources.

Consequently, the urgent need to tackle the pressing problems of the short term should not divert us from the objectives of working to formulate new approaches which, as well as allowing us to face up to the crisis and preserve the economic and social advances achieved in the past, will help to lay the foundation for a new type of economic expansion which is more solid, more dynamic, less vulnerable and more equitable than that observed so far.

The very nature of the crisis means that it

goes beyond the strictly economic area, as President Hurtado also suggests in his letter. Thus, any solution to the present challenges will only be viable to the extent that it proposes acceptable formulas for the distribution of the burden of adjustment both between the different social groups within the countries and between the different nations. This task is ultimately the responsibility of the political organs, which are faced with complex dilemmas.

It is also well known that in spite of the common features which exist in the region, there are differences between the various Latin American countries and between the situations each of them is facing in the present crisis. Furthermore, despite the symptoms of recovery which the United States economy has begun to show since the beginning of the year, there is as yet no clear picture regarding the future evolution of the industrialized nations as a whole, and still less regarding the consequences of the significant changes taking place in their structures of production.

All these factors undoubtedly make it difficult to give general and definitive answers on how to tackle the complex and varied problems with which the present situation is facing the region. On the other hand, however, they also represent for us a renewal of the Latin American challenges which marked the birth of our institutions.

In the light of these considerations, we have prepared a report which seeks: i) to describe the nature and scope of the economic crisis affecting Latin America; ii) to question the present adjustment process, which, because of the insufficiency of international co-operation and its inappropriateness to the demands of the present situation, creates external conditions for the Latin American countries which heighten the economic and social costs they must pay in order to overcome the crisis; and iii) to identify some priority guidelines and pro-

posals to stimulate joint action by Latin America to overcome the crisis, particularly on the international and regional levels.

It should be noted, however, that the lines of action suggested in the present document have been prepared according to a deliberately selective criterion, and we have sought to avoid detailed consideration of a large number of measures of widely varying importance and nature. Moreover, in presenting these guidelines, analysis of their justification has generally been reduced very considerably in order to keep the length of the text within reasonable limits. For all these reasons, we have concentrated our efforts on suggesting some general bases which could serve, in our view, for the formulation of an actions programme aimed at taking full advantage of the opportunities open to Latin America for overcoming the repercussions of the international crisis, as we were requested to do by President Hurtado.

Our reflections are also inspired by the conviction that it is necessary to face up to the crisis by means of a response of a regional nature which enables us to avoid the risks of a fatalistic approach deriving from the pessimism naturally felt in the face of the long lists of demands which hardly seem compatible with the challenges and possibilities offered by the present situation. The power of negotiation of the Latin American countries could in fact be increased considerably by adopting a concerted position based on a selective programme of action with clear priorities, firmly resting on the idea of regional co-operation.

It is our view, then, that Latin America can use and mobilize its capacity to respond to the negative effects of the international crisis and can advance towards the establishment of a new Latin American economic and social order which is more dynamic, equitable and stable, as well as involving greater mutual support.

II

The nature and scope of the economic crisis affecting Latin America

A. THE INTERNATIONAL CRISIS

The 1980s has begun with an economic recession which is the longest and most intense suffered by the world economy since the war. In it, the negative effects associated with a downward phase in the economic cycle have been aggravated by the adjustment policies applied, by the intensification of some structural shortcomings in the central economies, and by certain uncorrected imbalances in international economic relations.

As well as being exceptionally severe, the present crisis has been very generalized. Thus, due mainly to the impressive internationalization of the individual economies in recent decades, only a few countries have escaped its effects, so that progress has suffered, albeit to different degrees, in both the developed and developing countries, the socialist and capitalist economies, the oil-exporting and oil-importing countries, and the large, medium-sized and small economies alike.

In the industrialized economies, the crisis has manifested itself in a decline in production, a sharp drop in investment—which will weaken their future growth rate—an exceptional increase in unemployment, and unusually severe and persistent inflation.

The most distinctive feature of the crisis, however, has been the exceptionally high level reached by real interest rates. As a result of the high priority which the industrialized countries have given in recent years to the reduction of inflation and of their considerable fiscal deficits, and above all the enormous emphasis given in this task in some of those countries to the control of the money supply, interest rates have risen markedly in the main international financial centres since 1978, and in the two-year period 1981-1982 they reached levels in real terms comparable only with those registered during the Great Depression. It is true that since the middle of last year nominal interest rates

have gone down, but as their decline has been accompanied by a considerable drop in inflation in most of the industrialized economies, they are still two or three times as high in real terms as the average levels prevailing since the war.

The persistence of abnormally high real interest rates has thus become a key element in the international economic situation, and such problems as the drop in productive investments—which have been incapable of competing with financial investments in recent years—are largely attributable to the levels of interest rates. In the international sphere, high interest rates—and above all the sharp variations in them—have been one of the main causes of the erratic movements of capital and, through these, the equally marked fluctuations in exchange rates. The exceptionally high level of real interest rates has also been a factor in the sharp reduction in the demand for stocks (including commodity stocks), and this in turn explains much of the deterioration in the terms of trade of the developing economies.

As already noted, since the beginning of this year there have been some signs of economic recovery in certain industrialized economies, especially the United States. Furthermore, the progress made in some central countries in the struggle against inflation has made possible a certain slackening of the monetary containment measures which has stimulated global demand and, in particular, purchases of certain consumer durables—an item of considerable importance in the dynamics of the economic cycle of those countries.

In certain circles, these indicators have given rise to relatively optimistic opinions regarding the possibility that the recovery of the industrialized economies may be consolidated and that its probable beneficial effects will spread—mainly through international trade

and the drop in interest rates— to the peripheral economies.

These views are far from being shared by all, however, and certain circles continue to be skeptical regarding the prospects of a general, intensive and durable reactivation of the industrialized economies. These circles note that generally speaking macroeconomic policies are still highly restrictive in the central countries, and they also emphasize that, mainly as a consequence of the high interest rates still prevailing in the United States, the external deficits of a number of industrialized countries continue to be very large. Furthermore, it is obvious that the recovery of levels of investment in those countries has been held up by the joint effect of high interest rates, the rather generalized excess of idle capacity in industry, and especially the pre-

vailing uncertainty regarding the future evolution of the economic situation.

Another limiting factor is the persistence of the conflicts between the trade policies of some central countries, which could even become more intense in the years to come unless there is a realignment of their currency values.

The two elements which cause most concern and which directly threaten the prompt recovery of the central countries, however, are the continued simultaneous application of recessive policies in most of them and their lack of willingness to begin to apply, in a simultaneous and coherent manner, policies aimed at generating the co-ordinated reactivation of their economies. This position is particularly serious in the case of those OECD member countries which have largely brought their inflation rates under control and have thus managed to reduce the size of their external deficits.

B. THE TRANSMISSION OF THE INTERNATIONAL CRISIS TO LATIN AMERICA

The nature of international economic relations is such that the recent negative evolution of the central economies has severely affected the performance of the developing countries and, in particular, that of Latin America, which became intensely integrated into the world economy in recent years through a varied range of mechanisms of trade, financial and technological relations.

The world economic crisis has spread over the region through three main channels.

The first of these was international trade. As in other recessions, the stagnation of the economic activity of the industrialized countries has had unfavourable effects on their demand for imports and, hence, on the growth rate of international trade. On this occasion, however, these adverse consequences have been reinforced by the resurgence of protectionist practices in the trade policies of many central economies, which became more frequent and severe as unemployment increased and the recession continued. In these circumstances, the volume of international trade—whose rapid expansion had played a fundamental part in world economic growth since the war—increased only

slightly in 1980, almost completely stagnated in 1981, and actually went down by 2% in 1982.

As was to be expected, this progressive loss of dynamism of world trade sharply affected both the volume and prices of Latin America's exports. Thus, with the persistence for the third year running of the recession in the industrialized countries and a drop in the volume of world trade in absolute terms, 1982 saw the complete disappearance of any expansion in real terms of Latin America's exports, which had increased between 1976 and 1981 at the exceptionally high rate of around 8% per year.

The contraction in world trade also led to a sharp deterioration in 1982 in Latin America's terms of trade. The decline was particularly serious in the case of the non-oil-exporting countries, since in them the 1982 drop came on top of those which had taken place in the previous four years. Consequently, the average value of their terms of trade in the three-year period 1980-1982 was even below that registered between the years 1931 and 1933, which represented the most critical period of the Great Depression.

The second transmission mechanism con-

sisted of the high interest rates prevailing on international financial markets. These helped to trigger and accentuate the Latin American crisis in two complementary ways. On the one hand, by hindering the recovery of the industrialized economies, they tended to reduce the latter's demand for Latin America's exports. On the other hand, by raising the external debt service burden—the size of which had already grown very rapidly in previous years—they helped to increase enormously the current account deficit and obliged the countries to make a correspondingly much greater real transfer of resources to the exterior.

It is worth recalling in this respect that, from the point of view of the debtor countries, the greater or lesser real sacrifice involved in the payment of interest on the external debt depends not only on the level of the nominal interest rate, but also on the relation between the latter and the variations in the prices of export products. In other words, the amount of real resources which the debtor country must transfer to the exterior in order to service the debt will be all the greater in proportion as the nominal interest rate rises and the average price of the debtor country's exports drops.

This was exactly the situation which Latin America had to face in the period 1981-1982. As already noted, not only did interest rates reach exceptionally high levels on international financial markets during this period, but there was simultaneously a sharp decline in the unit value of Latin American exports. The results of this coincidence were dramatic: the real rate of interest which Latin America had to pay was around 24%, thus making it four times as much as the rate payable in those years by debtors in the central countries, even though the latter rates, as already noted, were themselves the highest registered in the last half century.

Finally, a third way in which the recession spread from the central economies to Latin America was the abrupt reversal of the net flow of capital, mainly as a result of the radical change which took place in 1982 in the international commercial banks' ideas on the advisability of continuing the rapid increase in their loans to the region. Thus, the net inflow of capital, which had grown very fast between the mid-1970s and 1981, slumped dramatically in 1982

to a little over US\$ 19 billion, or less than half the level of the year before. This violent contraction in the net inflow of capital, together with the extraordinary increase in net remittances of profits and interest, more than offset the effects of the turnaround in the trade balance—which, after turning in a deficit of almost US\$ 2 billion in 1981, generated a surplus of US\$ 8.8 billion in 1982—and made it necessary to finance a considerable part of the current account imbalance from the international reserves. The payments problems were further aggravated by the simultaneous reduction in the average term of the external loans obtained.

The force with which the problems of the world economy made themselves felt in Latin America was also due partly, however, to the economic policies applied in many countries of the region from the mid-1970s onwards, which promoted a form of economic growth heavily dependent on the inflow of capital from the exterior.

In other words, it was the special combination of adverse changes on the international scene already described, long-standing structural problems, and economic policies excessively linked to financing from abroad which put an end, in the early 1980s, to the dynamic growth process registered by the economies of the region in general between 1950 and 1980, when the gross domestic product of Latin America increased fivefold, while manufacturing production grew more than sixfold.

From 1981 onwards there was a sharp drop in the growth rate of economic activity and in 1982 such activity even went down in absolute terms—something which had never happened in the previous 40 years. This marked loss of dynamism was accompanied by a sharp rise in the rates of open unemployment and an increase in the various forms of underemployment. At the same time, there was a trend towards the generalization of inflationary processes, which attained an intensity and persistence that it would have been difficult to imagine only a few years before. These unfavourable changes at the domestic level were closely linked with other no less serious changes in the external sector, the most obvious manifestations of which have been the severe balance-of-payments crises, the frequent and in some cases enormous

rises in exchange rates, and the drain on the international reserves.

A particularly disquieting phenomenon observed in recent years, however, has been the high level of external indebtedness affecting the region. The financial permissiveness shown by the international private banking system in the second half of the 1970s and the intense and persistent efforts it made to loan its financial surpluses to Latin America encouraged a policy of external indebtedness on a scale without any precedent in the region in the last half century. There were few countries in Latin America which did not follow this policy in order to finance domestic policies with widely varying aims, ranging from some which involved large investments that overestimated the future expansion of domestic and international markets to others which promoted and exaggerated expansion of consumption—especially of imported goods—or a big increase in defence spending. In recent years, furthermore, a considerable and growing proportion of the external financing was used to pay the servicing costs of the accumulated debt, so that this situation was accompanied in practice by a reduction in the real transfer of resources to Latin America.

In many Latin American economies the decline in economic activity has also been accompanied by profound crises in the system of production and the financial situation of enterprises, which have led to the bankruptcy or closing down of many production units in industry, agriculture and commerce. This in turn has helped to bring about a deterioration in the quality of bank loan portfolios and has finally affected the solvency and viability of much of

the private financial system. A situation of widespread insolvency has thus been created for which there is no precedent in the last half century both from the point of view of its quantitative dimensions and the number and variety of enterprises affected.

Another manifestation of the crisis has been the pronounced deterioration in many countries in the economic situation of the State, whose revenue has been affected by the drop in external trade and the stagnation or decline in domestic economic activity. All this has helped to generate big deficits in the public finances and to speed up the rates of inflation. In turn, attempts to bring the latter under control have frequently led to abrupt cuts in State spending, and especially in public investment, thus further depressing the levels of domestic activity.

In spite of this, in many countries there has at the same time been a tendency towards the acceleration of inflation. In particular, inflation has reached unprecedented levels of intensity in countries which have been forced to devalue their currencies abruptly in order to tackle severe disequilibria in their balance of payments.

As a result of the decline in economic activity, the simultaneous acceleration of inflation, and the orthodox-type stabilization policies applied in order to bring down the rate of price increases, there has been a marked deterioration, in many countries, in the living conditions of the poorer groups, which have been affected both by the pronounced declines in real wages and the rise in unemployment and underemployment.

III

The inequity of the current adjustment process and the need for an alternative approach

A. THE NATURE OF THE CURRENT ADJUSTMENT PROCESS

The present international crisis and the asymmetry of the adjustment process have drastically changed the conditions of external trade and fi-

ancing of Latin America, making inevitable the introduction of profound changes in the economic policy of the countries of the region.

This has had painful and inequitable economic and social consequences, while moreover the results obtained have not been in keeping with the efforts made.

In these circumstances, an important challenge facing economic policy is that of minimizing the social costs involved in the adjustment and distributing them more equitably both between creditor and debtor countries and between the various social groups and economic agents within the countries.

In recent months the International Monetary Fund has been participating actively in the design of adjustment programmes which provide for the reprogramming of external indebtedness, together with balance-of-payments support credits. Under these programmes, governments have not only received additional resources provided by the IMF, but have also had access to contributions from the private banks aimed at relieving the burden of external debt servicing in line with the terms of the negotiations furthered by the Fund itself. In almost all cases, the adjustment programmes thus agreed on stipulate that these external resources must be supplemented with surpluses on the balance-of-payments trade account, which the countries must generate principally through the adoption of suitable exchange rate, monetary and fiscal policies.

Although it must be admitted that the Fund has introduced a greater degree of flexibility into these programmes compared with its traditional terms, they are still based fundamentally on policies which must act through aggregate demand and necessarily include a pronounced recessive element, since it is largely through the reduction of domestic demand that it is hoped to generate the trade surpluses considered essential for facing up to the debt servicing.

This recessive element in the adjustment policies applied is determined, ultimately, by the magnitude of the external imbalances affecting the countries of Latin America and the particular state of their balance of payments. As already noted, the equilibrium of the external accounts has been affected by a number of factors which are beyond the direct action of the countries and which, in their turn, tend to reduce considerably the inflow of foreign exchange and

increase payments to the exterior. Thus, while the income from exports has gone down both because of drops in prices and reductions in the amounts exported, and the net procurement of capital has slumped violently, the outflow of foreign exchange has tended to increase as a result of the high spreads over basic interest rates and the management commissions charged by the banks in their refinancing programmes. In many cases, these higher costs have wiped out or at least partly neutralized the effect of the declines in nominal interest rates registered in recent months.

It must be concluded, then, that in spite of the additional resources provided or mobilized by the IMF, and mainly because of the enormous magnitude of the external debt servicing burden, the objective of bringing the external accounts into balance will call for some degree of recessive adjustment, through the compression of domestic economic activity.

There are three problems, however, which give rise to severe reservations regarding the adjustment processes now in progress. These are, firstly, the ineffectiveness so far shown by the policies applied in order to achieve the desired objectives; secondly, the considerable economic and social costs associated with these policies; and finally, the doubtful capacity of the countries to keep up these policies for more or less prolonged periods.

Thus, if these adjustment policies go beyond certain limits they may generate declines in economic activity, drops in investment, or even destroy the system of production, and this will seriously affect not only current levels of consumption and well-being, but also the capacity of the economies for future recovery.

Likewise, if the recessive situation of the international economy continues or its eventual reactivation does not rapidly make itself felt in the economies of the region, the continued application of such recessive policies could even threaten to overstep the limits of social and political tolerance of our societies, so that not only would such policies be difficult to apply, but their execution would have unforeseeable consequences both for the Latin American countries and for the international community.

The foregoing does not mean, of course, that we do not give due credit to the Trojan ef-

forts which the financial authorities and governments of our countries have been making to handle an extremely difficult external payments situation and honour the external commitments assumed, within the limited possibilities offered by the presently available international financial co-operation.

Special reference may be made, in this respect, to the enormous adjustment effort made by the countries of the region in 1982, which, as already noted, enabled them to replace the trade deficit of the year before with a trade surplus of some US\$ 8.8 billion.

Nor does it mean that we do not appreciate the imaginative initiatives put into practice by the International Monetary Fund in order to tackle the current payments problems, with the participation of the financial authorities of the industrialized countries, the Bank for International Settlements, and the private banking system.

What does worry us, however, are the limitations and inconsistencies of international support arrangements which do not seem to be qualitatively or quantitatively adequate to deal with the fundamental and generalized state of imbalance in which the countries of the region are sunk, and which, as already noted, cannot be compared with anything that has happened since the war.

We also have reservations regarding the viability of an adjustment based on contraction policies which must be undertaken by all countries together, aimed at collectively increasing exports and jointly reducing imports. It must be perfectly clear that unless there is a group of countries which is willing to accept a deficit on its trade account, it will not be possible for a numerous group of other countries to generate a surplus. Consequently, the efforts of the latter to expand their exports and compress their imports will simply aggravate the recession in them.

It is also clear that the possibility of solving in the medium term the financial problems raised by the accumulated external indebtedness is closely dependent on the possibilities of expanding the region's exports, and these, in turn, as they stand at present, are conditioned by the evolution of world trade. In the final analysis, if the acute financial problems of the

present time are to be overcome, it is indispensable that there should be a recovery in the prices and volumes of Latin America's exports. It is therefore a matter of the deepest concern that at the same time that our countries are shouldering the enormous costs involved in policies aimed at bringing the balance of payments into equilibrium and honouring their external financial commitments, the protectionist policies of the creditor countries should keep on growing ever stronger.

In our opinion, this failure to take much account in the adjustment programmes of the intimate links existing between the trade and financial aspects is undoubtedly one of their great shortcomings.

We also feel that the additional refinancing resources mobilized by the adjustment policies should be accompanied by long-term external funds for the support of domestic investment and development programmes. Unfortunately, in the present circumstances not only has there been a violent drop in private financial resources but there has been no corresponding strengthening of the international public financing agencies. On the contrary, it is increasingly difficult to obtain loans from such agencies and, at the same time, tendencies towards graduation are prevailing in them which, by definition, restrict the region's possibilities of gaining access to public international credit.

To sum up, then, the view prevails in international financing agencies and the governments of creditor countries that it is possible to handle the present balance-of-payments crisis through traditional support mechanisms, backed up by the recent policies of the IMF in association with the private banks. This position assumes explicitly or implicitly that there will be a prompt, strong and lasting recovery of the world economy.

These positions are controverted, however, by dissenting opinions within the central countries themselves which reflect concern over the intensity and duration of the adjustment being demanded from the developing countries, its social and political effects, and the disastrous consequences which a situation of general cessation of payments or panic could have for the international banking system and even the world economy as a whole. In view of these

concerns, global solutions of another type are advocated in which coping with the payments crisis of the developing countries becomes an essential part of the economic reactivation policies of the centres.

In order to honour their external commitments, the countries of the region have put into effect extremely painful adjustment processes which are severely affecting their economic structures and creating serious pressures on their social equilibrium. The viability of these adjustments depends on the margins of action permitted by the presently available international co-operation. In many Latin American countries, however, increasing doubts are arising regarding the social and political feasibility of this type of solution, the possibility of maintaining such policies for a significant length of

time, and the capacity of the economies of the region to comply with the agreements signed if the present conditions of the world economy continue.

We therefore feel that the time has come for the region, as well as drawing attention to the inadequacy of the present international co-operation machinery, to bring home to the authorities of the industrialized countries and raise in the appropriate forums the need to find sources of support additional to those at present existing, if a way out of the crisis is to be found. A solution of this nature would not only be in the interests of the Latin American countries but would also be in line with the interests of the international banking system and the reactivation policies of the centres.

B. TOWARDS AN ALTERNATIVE APPROACH

The foregoing considerations leave no doubt that at present Latin America is facing a serious dilemma characterized by three adverse factors which mutually reinforce each other: a severe world crisis from which it is still not clear how or when we are going to emerge; international co-operation which is inadequate both from the point of view of its size and its nature; and an adjustment process with recessive characteristics.

We wish to stress, however, that in our view the task of overcoming this extremely complex situation and carrying out in the years to come an adjustment process which will at the same time make it possible to restore the equilibrium of the external accounts and at least preserve the levels of per capita income constitutes only the most immediate challenge facing the countries of the region, for in the medium term they will have to try to overcome another challenge, no less complex and unavoidable, which is that of gradually but firmly changing the style of development which has prevailed up to now in the region in order to bring in a new kind of development which is more dynamic, less vulnerable, and above all more equitable.

In order to do this, the region must carry out intensive mobilization of its internal resources through regional co-operation, which is

currently subject to serious tensions deriving from the recessive forces imposed by the international situation itself. In this respect, we are convinced that the present time is a suitable one for making an appraisal of the achievements of regional co-operation, the difficulties it has run into, its present and future potential, and the most suitable means for making it more effective and decisively entering on a new stage in the process of regional integration.

Furthermore, in order to progress in overcoming the difficult problems at present affecting them, the countries of the region must coordinate their international action so as on the one hand to promote a reactivation of the world economy which provides a suitable external framework for them to attain reasonable economic growth, and on the other to secure the approval of a set of emergency measures by the international community which are compatible with the magnitude of the external payments crisis they are currently facing.

From Latin America's point of view, the desirability of securing the reactivation of the international economy stems from the need to bring about substantial changes in the external conditions of the region, which are essential in order to overcome many of the economic problems currently affecting it or at least bring them

down to a manageable size. It is for this reason that a co-ordinated programme of reactivation of the industrialized economies, which should be headed by those countries which have made most progress as regards restoring their internal stability and balance-of-payments equilibrium, is particularly necessary. These measures should be directed especially towards securing a sustained and substantial decline in real interest rates, without which no recovery can be really significant or stable.

The reactivation of the industrialized economies alone, however, will not be enough to establish a more dynamic, stable and equitable international setting. In order to advance in this direction we must at the same time incorporate into the economic policies of the central countries fundamental measures which permit the solution of the structural problems affecting international economic relations, so many times called for by the Third World in United Nations forums, and so many times postponed as regards their solution. Thus, a reactivation of the central economies which is not accompanied by significant changes in the fields of basic commodities, the opening up of markets, the checking of protectionist policies, or bigger transfers of financial resources would have little rele-

vance in overcoming the serious and sometimes desperate situation of the peripheral countries.

It is for this reason —although it is not necessary to go into details on this occasion— that we feel that the measures approved at the recent meetings of the Non-Aligned Countries in New Delhi and the Group of 77 in Buenos Aires —to which Latin America has given its unanimous support— are particularly pertinent.

In this respect, the forthcoming conference of UNCTAD provides a favourable occasion for demanding the definition and approval by the industrialized countries of a set of minimum actions to accompany their reactivation policies and make it possible, at the same time, to reverse the deterioration in the process of world economic development. A powerful presence of Latin America in this conference is therefore absolutely essential.

As well as supporting a world programme of "reactivation with development", Latin America's international action should centre its attention on establishing a dialogue with the industrialized countries with which the region maintains the bulk of its external trade and financial relations, in order to negotiate and agree on a set of emergency measures for the relief of its acute current problems.

IV

International action by Latin America to deal with the external indebtedness crisis

A. THE END OF A CYCLE IN REGIONAL EXTERNAL FINANCING

The handling of the region's external indebtedness against the background of the balance-of-payments crisis has become the most urgent economic problem facing the governments of Latin America. The distribution of the cost of the adjustment process and to some extent the opportunities for economic growth for the rest of the decade depend upon its solution. This growth will undoubtedly depend upon different patterns of financing from those of the past few years.

1. *The external debt and the balance-of-payments crisis*

This situation has been arrived at mainly because between 1975 and 1982 the total external debt of the region more than quadrupled, rising from US\$ 67 billion to nearly US\$ 300 billion. This growth was especially rapid between 1975 and 1980, when the external indebtedness rose at an average annual rate of nearly 25%, i.e., substantially faster than the also very high rate

of 18% at which the value of exports from the region expanded. This growth in the debt became significantly more moderate in 1982 due to the sharp drop in the net inflow of capital.

The expansion of the total debt was accompanied by a considerable change in its origin and composition. At the beginning of the past decade, private flows represented less than 40% of the total, while in recent years they exceeded 80%. At the same time medium- and long-term credits and those at concessional rates of interest were replaced by short- and medium-term credits and variable interest rates. This implied a sharp deterioration in the debt profile of Latin America —by far the least favourable of all the regions of the Third World— and gradually led to a sharp increase in the percentage of export income which had to be used to service the debt.

Seen from the perspective of the whole decade, the responsibility for the generation of the excessive external indebtedness was shared between the indebtedness policies of Latin American countries, the financial permissiveness of the private banking system, and the weaknesses and inadequacies of the international financial mechanisms.

In the expansive stage of the credit cycle, the private banks strenuously competed to invest in the region part of the enormous financial surpluses which they obtained in the international capital markets, especially in those of the principal oil-exporting countries. Furthermore, quite often certain banks did not make rigorous appraisals of creditworthiness, or they overestimated the capacity of the countries to absorb funds. At the same time, the combination of domestic interest rates higher than those prevailing in international markets and the abundant foreign reserves accumulated by the countries of the region helped encourage the flow of financial resources to be invested in these countries.

In addition, the inability of the machinery of the international financial institutions to recycle the huge surpluses of the oil countries meant that most of the transfers of resources during the 1970s were carried out by private banks.

This external framework, however, suddenly changed in recent years. The serious deterioration in the terms of trade of the region

and the paralysation of growth in the volume of exports coincided with a sharp rise in real interest rates. This changed the banks' perception of the payment capacity of various countries of the region and led to a sharp contraction in net movements of capital to Latin America.

This produced an external payments situation which was impossible to sustain for nearly all the countries of the region. To deal with it, many of them had to initiate adjustment processes based on the reduction of domestic demand, or they had to resort to the IMF. As a result, since 1981 both the level of domestic economic activity and the amount of imports have declined in a number of countries. When these expedients were exhausted, most of the Latin American countries had to make use of their reserves —which fell substantially in 1982— and initiate processes of renegotiation of the debt with their creditors, in most cases with the participation of the International Monetary Fund.

2. *The refinancing agreements*

In the process of refinancing, the private banks have assumed commitments to grant additional credits supplementing those provided by the IMF. The fact that the 'rescue package' includes the private banks is an important and innovative aspect of the exercises of reprogramming the external debt recently effected or now in progress.

However, the insufficiency of these mechanisms is obvious when some of their features are analysed, for the exercises in re-scheduling payments offer few prospects for economic growth, since the additional resources committed by the banks and the Fund are not sufficient to cover the payment of interests. At the same time, most of the cost of the adjustment and the effort to face the difficulties of debt servicing has fallen exclusively on the Latin American countries. Moreover, the high margins paid above the basic interest rates (spreads) and the additional commissions for management and service have more than doubled the cost of refinancing.

In addition, the negotiations carried out have not managed to reduce the uncertainty about the financial prospects of the countries because, on the one hand, they cover only the

debts maturing in the next one or two years and, on the other hand, because of the long period of time between the declaration of difficulties with respect to debt servicing and the final rescheduling agreement. Naturally, these uncertainties have had negative effects on the economies of the borrowing countries.

Some of the agreements have also been complicated by the policy of certain private banks of sharply cutting down or reducing the lines of trade credit, which are of great importance for maintaining the level of international trade.

Moreover, in spite of the intervention of

the IMF, the large number of participant banks, their different assessments and positions on the way of overcoming the problems of our countries, and the lack of experience in this type of operation have made it extremely difficult and laborious to secure the approval of these re-financing programmes.

Furthermore, there can be no doubt that as a result of the inadequacy of international co-operation in this area, the present refinancing procedures give much higher priority to the payment of the external debt commitments than to the requirements of the economic development process of the debtor countries.

B. NEW CONDITIONS FOR RESTRUCTURING THE EXTERNAL DEBT

As a result of the foregoing, there are serious doubts in some international and national circles regarding the real capacity of the Latin American countries to face up to the commitments assumed unless the international economic conditions undergo a substantial change and at the same time there is a reduction of the high economic and social costs associated with the present adjustment processes.

In our view, this points the way to the need for a constructive dialogue both among the countries of the region and between them and the creditor countries, in order to explore the viability of new terms and policies more in keeping with the mutual interests of all the parties concerned.

In order to put forward on a new basis a different approach to the challenge represented by the Latin American external debt, it is necessary to start by recognizing that the principles prevailing at present as regards the distribution of the adjustment cost between debtors and creditors are very biased.

This situation is in sharp contrast with what happened in the 1930s, for the Latin American external debt at that time had been contracted principally through the sale of bonds on world markets. Thus, when the debtor countries began to suffer from the external problems generated by the crisis, the price of the bonds fell sharply, due above all to the risk of non-pay-

ment. As a result of this, when the Latin American countries began to service their external debt again they were able to buy back the bonds at a fraction of their issued value. In this way, the cost of the adjustment was shared between creditors and debtors in line with the risk appraisal made on the international capital markets.

At the present time, in contrast, the creditors are mainly commercial banks, whose holdings are not easily tradeable and which, if they had to liquidate them in the market, would cause them substantial losses, jeopardizing their stability. Thus, the only option they have at present is to offer to the debtors in difficulties either a refinancing or rescheduling of the debt.

At the same time there is no suitable international mechanism to carry out renegotiation or refinancing processes other than the 'Paris Clubs' or aid consortiums, none of which deal with the debt with the private banks, which is what is of fundamental interest in the case of Latin America.

The present system of renegotiation, besides being inequitable, takes no account of the basic mutuality of interest which exist between the creditor countries and institutions and the debtor countries. The high social costs involved in the present adjustment could even lead to uncontrollable situations in the latter countries, and these would in turn have strong negative re-

percussions on the situation of the creditor countries and banks.

A new approach to the problems of the region's indebtedness based on criteria of equity and mutuality of interests should therefore tend towards solutions which would guarantee a more equitable international distribution of the adjustment and a continuation of the process of development of the debtor countries, as a way of preserving the standard of living in these countries and strengthening their future payment capacity.

Under these circumstances, for the Latin American indebtedness problem to be satisfactorily resolved in the future, it will be necessary to establish a mechanism which includes the following conditions:

a) it must provide for the establishment of an institutionalized procedure for restructuring the debt, perhaps as a joint effort between IMF and the World Bank;

b) the reprogramming should include maturities of several years, establishing longer amortization periods and possibly changing a substantial part of the short- and medium-term debt of certain countries into long-term obligations;

c) additional resources should be granted to take care of the accumulated debt servicing and to maintain the operative capacity of the countries to handle their external trade;

d) the cost of refinancing must be reduced; and

e) access to additional public credits to stimulate economic development should be facilitated.

1. *The need for new institutional mechanisms*

The prolonged nature of the refinancing exercises makes it advisable to promote the establishment at the international level of new operational mechanisms for co-operating with the developing countries in the reprogramming process, thus taking the place of the *ad hoc* mechanisms used up to now and taking advantage of the experience built up by IMF in these fields. A refinancing service within the framework of the existing multilateral institutions, with automatic voluntary access as a function of objective indicators and providing case-

by-case support for each country studied according to the circumstances would be a decisive link in the chain of international co-operation which the present crisis and the meagre prospects of the world economy make it essential to establish.

Moreover, since trade aspects are of crucial importance for the thorough solution of the problems of the debtor countries, consideration should be given to the possibility of arranging for the participation in these refinancing exercises of institutions connected with international trade, such as GATT and UNCTAD, with a view to obtaining special facilities on the trade level. Among these facilities could be temporary provisions to open up markets further, or not to make adverse changes (stand-still), so as to expand the payment capacity of the debtor countries by increasing their exports.

2. *New terms and conditions for restructuring the debt*

An important objective in the new approach should be the reprogramming of the debt servicing for longer periods than those now in effect.

Reprogramming which covers only the maturities of the next one or two years is not sufficient and subjects the debtor countries to a process of virtually non-stop refinancing. Likewise, the imminence of possible additional negotiations regarding the payment of capital and interest on the debt negatively affects the confidence of creditors and prejudices the restoration of an appropriate flow of additional credits to the debtor countries. We therefore feel that a more effective formula would be to reprogramme the corresponding maturities for a greater number of years than at present. The new payment schedules should also include longer grace periods and terms than those granted up to now. This will make it possible to create more suitable conditions for managing the balance of payments.

These terms should be established so that they allow the debtor countries to maintain their per capita income during the adjustment period. Such a principle would be more acceptable as a guiding criterion of the renegotiations if a special clause were included in the repro-

gramming agreements providing for the incorporation of some degree of flexibility into the schedule of refinanced capital and interest payments, depending on the economic conditions of the borrower country. If the latter conditions improve, part of the fruits of this more favourable situation would be shared with the creditor banks through a moderate acceleration of the amortization and interest payments.

For some heavily indebted countries, a solution worth exploring would be the possible conversion of part of their outstanding short- and medium-term external debt into long-term debt. These countries contracted short-term credits to finance investments which are socially beneficial but have a long maturation period. They therefore require an urgent reprogramming of this financing.

3. Additional resources for covering debt servicing and maintaining the operational capacity in external trade

The mere reprogramming of the amortization of the external debt is not enough, however. It is necessary to obtain new resources, since in the short term the capacity for achieving a substantial unilateral increase in the national saving of the Latin American countries is limited.

From the point of view of the region as a whole, and subject to reasonable assumptions about the probable evolution of the world economy in the next few years, the external financing requirements for making the debt servicing compatible with the maintenance of the per capita income, as a minimum goal, involve the mobilization of much larger additional resources than those currently being obtained through the refinancing agreements.

Suggestions have been made in this respect whose importance and viability warrant careful attention: the capitalization of a substantial part of the interest on the external debt; the payment of a variable proportion of the interest with bonds tradeable on the international capital market; and the establishment within IMF of a special facility for financing the balance-of-payments deficit caused by the rises in international interest rates, providing for the granting of compensatory loans to the debtor countries

during periods when these rates exceed their historical levels.

Together with these additional resources, it will be of fundamental importance to maintain the credits from the private banking system for the financing of external trade operations within reasonable margins. As already noted, recent experience shows that the severe cuts made in this type of financing have created extremely difficult situations at a time when only a major reactivation of the external trade of the region can make possible a real way out of the difficulties presently being faced.

4. Reducing the cost of refinancing

From the point of view of equity, the private banking system practice of sharply increasing the cost of external credit when it becomes necessary to reprogramme indebtedness seems highly questionable. In reality, the signing of a rescheduling agreement does not involve any additional risk for the private banks. Indeed, in practice, there is an improvement in the quality of an originally weak loan portfolio.

This is because, in the first place, when a rescheduling agreement is signed, all of the future payments generally have an official guarantee which also extends to private credits not always previously covered by such guarantees. Secondly, these agreements are normally accompanied by the financial support of the IMF and the resulting commitment of the debtor country to continue certain adjustment policies which guarantee that in the future they will be in a better position to pay for the debt servicing.

Under these circumstances, it is not justifiable to increase the cost of the credit by raising the charges, a practice which in some cases has cancelled out the greater part of the benefit which the debtor countries would otherwise have obtained from the lowering of the nominal interest rates.

5. The need for a considerable increase in public credit for development

The adjustment policies which the Latin American countries are presently being forced to follow require a sharp contraction of the fiscal def-

icit, which generally takes the form of a reduction in public investment rather than the containing of current expenditure. It is therefore important, in the present circumstances, to maintain an adequate and growing flow of long-term credits from the international financial institutions, with a view to maintaining a high level of public investment which will ensure the continuation of the development process. The present circumstances make it absolutely essential to strengthen the existing multilateral institutions, especially IBRD and IDB, so as to substantially increase their contribution to the financing of the economic and social development process of the region.

The impression seems to prevail in certain circles in the developed countries that these institutions are merely agents which transfer subsidized resources, and their role as stabilizers of the international financial system is ignored or underestimated, especially as regards the anti-cyclical role which they play as a counterweight to the pro-cyclical operations of the private banks. The multilateral agencies thus help to give greater confidence in private financial markets, assuring the developing and also the developed countries of smaller disturbances in the amounts and forms of capital flows.

Notwithstanding this, however, both IDB

and the World Bank have shown relatively sharp contractions in the loans they have authorized for the region. As a proportion of the region's current account deficit, the loans authorized by IDB have dropped from an average of 25% in 1965-1970 to 11% in 1975-1980; the corresponding figures for the World Bank are 21% and 12%, respectively.

It may be deduced from this that the doubling of the resources available for lending to Latin America on the part of these two institutions would be a reasonable minimum goal as a contribution to the medium- and long-term external capital required by the region.

The policies of these institutions would be much more positive if they led to the materialization of the old aspirations of the countries of the region that such agencies should modify the terms of their loans so as to provide a greater stimulus to domestic productive activity. This could be achieved by giving greater flexibility to a considerably higher proportion of their project loans, expanding access to economic programme credits, and increasing their capacity for financing local costs. Furthermore, in the case of programme loans, it would be desirable to seek closer co-operation between the World Bank, IDB, and the International Monetary Fund.

C. STRENGTHENING THE OPERATIONAL CAPACITY OF THE INTERNATIONAL FINANCING ORGANIZATIONS AND INTERNATIONAL LIQUIDITY

Many of the current problems resulting from the indebtedness of the developing countries could have been avoided if the international financial agencies had had the funds, recycling mechanisms and facilities needed to allow for an adequate and equitable adjustment process at the world level.

Instead, the financial power of the multilateral agencies has weakened significantly in the 1970s and particularly in the last few years. The International Monetary Fund has exhausted its uncommitted resources and the recently agreed increase in quotas will only come into effect at the beginning of 1984, while the amount involved will be no more than 20% of the deficit anticipated that year on the cur-

rent account of the developing countries, which is inadequate to take care of their external financing needs.

Similarly, it should be noted that IDB has had increasing difficulty in supplementing its ordinary capital resources, even though the great majority of its member countries have given strong support to this expansion. The agreements recently reached on this matter represent a step in the right direction, but they are insufficient.

We feel that the time has come to expand the operational capacity of the Inter-American Development Bank with resources from other sources or through the creation of new loan funds which will enable this institution to con-

siderably expand the flow of financial resources to Latin America.

In the case of the World Bank, the difficulties in restoring the operational capacity of the IDA are well known and are in addition to the restrictions on the mobilization of resources being experienced by the other multilateral agencies.

We believe that the idea so often expressed of expanding the loan capacity of these institutions by gradually increasing the asset/liability ratio with which they have come to operate would give them a considerable margin for expanding their credit activities.

In order to strengthen the presence of the multilateral agencies in the financing of Latin American development, special attention should be given to the co-financing arrangements which may be organized with private banks. In this way, the flow of resources to well-planned investment projects could be increased, and at the same time this would ensure the prompt materialization of these projects as well as transferring additional external resources which would make it possible to gradually im-

prove the debt profile of the Latin American countries.

With regard to the sharp drop in Latin America's foreign exchange reserves in 1982, it is interesting to note that this was part of a similar phenomenon at the world level. Thus, the official world foreign exchange reserves went down by over US\$ 13 billion during 1982 and are still sinking in 1983, consequently tending to weaken any trend towards reactivation.

This therefore seems a suitable moment to give decided support to the proposal to allocate Special Drawing Rights in order to increase international liquidity. This would make it possible to distribute the burden of the external adjustment more equitably and over a shorter period than that required in order to increase the ordinary resources of the IMF.

Furthermore, a direct 'link' between the allocation of SDRs and the financing of the development of the peripheral countries would be a more effective way of providing relief for the debtor countries while at the same time securing an orderly expansion of the financial system.

D. DOMESTIC POLICIES AND THE CONDITIONALITY OF INTERNATIONAL SUPPORT

In the present circumstances, when the debtor countries are adapting their domestic policies to the new conditions of the international economic situation and the difficulties in their balance of payments, the international agencies which guide the adjustment process, such as the IMF, should also modify the conditionality of their loans so as to avoid incompatibilities in world economic policy and ensure that such policy helps to stimulate global activity.

In accordance with this, it seems advisable that the IMF should make its theoretical concept of the adjustment process more flexible, so as to adapt it better to the different economic

and social goals of its increasingly heterogeneous member countries.

This suggests that less confidence should be placed in automatic adjustments through price incentives in private markets, and greater weight should be given to the guiding role of the State and direct instruments of adjustment which act on some of the main economic variables.

At the same time, the IMF should have at its disposal suitable mechanisms for promoting adjustment in countries which have a surplus on their external accounts, so that the costs of this process are shared more equitably between these countries and the deficit countries.

E. THE NEED FOR CO-ORDINATED REGIONAL ACTION IN FINANCIAL MATTERS

The diversity and complexity of the individual situations as regards external indebtedness should not stand in the way of a broadly concerted agreement to act jointly in international forums and in dealing with the governments of creditor countries when seeking solutions of mutual interest to the present financial situation of the region.

This would require, as a first step, a review of the proposals relating to the solution of the serious problems deriving from the external indebtedness of the region, with a special view towards co-ordinating the joint action needed in order to realize these proposals.

We also feel that this would be a good time to open a direct dialogue between the governments of the creditor countries and the Latin American governments acting as a co-ordinated group. This would represent a significant advance with respect to the present situation, in which the negotiations are being carried out fundamentally between the governments of the region on the one hand and the commercial banks and international financial institutions on the other.

This option would not only make it possible to promote basic solutions to the difficulties referred to earlier but would also make it possible to grasp the true magnitude of the international crisis and its possible remedies, taking into account the important political interests involved.

As an important supplement to these initiatives we recommend the creation of a Latin American external finance information centre, linked with one or more existing regional agencies, which would make possible an increase in the various Latin American countries' knowledge of the conditions in which the refinancing process and the financial market are operating. This centre could also serve to advise the governments on the handling and solution of their problems generated by the external debt.

Such strengthening of the regional information capacity would also be in keeping with the initiative presently being taken by the creditor banks to organize and co-ordinate their policies towards national debtors, for which purpose the industrialized countries have at their disposal the OECD and the Bank for International Settlements.

V

The strengthening of regional co-operation and integration

A. THE RECENT EVOLUTION OF THE INTEGRATION PROCESSES

Thanks in good measure to the operation of the subregional integration arrangements, reciprocal trade among the Latin American countries grew steadily until the mid-1970s. Moreover, since the beginning a high proportion of that trade has been constituted by manufactures, unlike exports to the industrialized countries, in which basic commodities and semi-manufactures predominate. Nevertheless, in recent years, beginning in the second half of the

1970s, the relative importance of intra-regional trade became erratic and it lost dynamism, thereby giving rise to a certain amount of skepticism concerning its possibilities.

It would be a long task to go in depth into the numerous factors which have had an effect on the evolution of each integration scheme and have contributed to its slackening off in recent years. Factors in this phenomenon have included the structural differences between the

countries, the heterogeneity of national economic policies and the difficulties inherent in processes of integration among developing countries. This process has also been affected, however, by other factors of a conjunctural nature characteristic of the economic evolution of Latin America in recent years, such as the availability of abundant external resources and the dynamic growth of Latin American exports outside the region, which promoted the expansion of trade to extra-regional markets and in some sectors made regional markets less interesting.

In addition, the advance of Latin American industrialization has, in recent years, been obstructed in some cases because some countries have suddenly opened their economies up to international competition, or in others because they have not yet succeeded in stabilizing and intensifying the process of industrialization owing to their backwardness in terms of the production of basic inputs and capital goods. In these ways, the capacity to supply manufactures to the regional market has suffered, as has the demand on that market for capital goods.

To say, therefore, that the integration movement has faltered only because of the way in which regional or subregional institutions or the legal instruments which govern them have operated would definitely constitute a severely limited view of the complex and varied origins of that phenomenon.

It should also be noted that the potential for co-operation does not depend only on the nature and scope of the integration instruments. In the past decade ways and means of co-operation have emerged in Latin America which are profoundly significant for the

economic linkage and progress of the countries of the region. Meaningful and promising examples of such ways are to be found in the binational projects to develop water resources, the improvement of the common transport and communications infrastructure, integration of border areas, the petroleum agreement to aid the Caribbean and Central American countries, joint ventures in several fields, and other forms of co-operation at the scientific and technological as well as the economic levels.

However, there has recently been widespread doubt concerning the present and future importance of regional co-operation. Moreover, the various regional integration schemes have, instead of becoming stronger and more effective, been going through a period of institutional lethargy or have come up against dangerous and recurrent crises which have resulted in the stagnation or even regression of the integration processes.

Those trends have in the present circumstances been aggravated by the impact of the unfavourable international economic situation and the payments difficulties now experienced by the great majority of the Latin American countries.

For this reason, unless there is a significant turnaround and a more positive attitude to regional co-operation is established, these negative elements will continue to erode the achievements made and there will be an increase in the skepticism shown by business groups and even by the governments themselves, which are, in the last analysis, the agents on whose action the broadening and strengthening of the process of regional integration depend.

B. THE URGENT NEED FOR REGIONAL INTEGRATION AND CO-OPERATION TODAY

Such a change of attitude is more vital than ever today, since intra-regional co-operation and especially reciprocal trade are acquiring special importance and urgency in view of the growing restrictions on the expansion of exports to the rest of the world and the priority given to a style of development which is more inward-looking

than the one which prevailed in the region during the decade preceding the current crisis.

Since the prospects for North-South co-operation are dim and the benefits which Latin America is likely to derive from the eventual economic reactivation of the great centres are long in coming, it becomes of vital importance

to look to the region anew and make regional integration and co-operation a basic factor in the effort to revitalize the Latin American economies.

In the present circumstances, a decided movement in this direction would make it possible to achieve three fundamental objectives: more intensive use of the region's idle or under-utilized productive capacity; increased efficiency through the use of economies of scale, which have been severely eroded by the drop in production, and, finally, a reduction in the regional use of foreign exchange per unit of production.

All this would be of decisive help in achieving greater collective economic security and would make a form of development increasingly based on regional demand more viable.

If, on the other hand, the integration movement is not revitalized (and it will not be unless the governments make a definite political commitment), the costs may well be very high. Because of the extremely unfavourable nature of the present international economic situation, the unilateral action which countries may take to improve their position in the international economic scenario might give rise to a ruinous process of competition between the countries of the region in terms, for example, of repeated devaluations or ever-increasing export subsidies.

In short, it may be said that now, more than ever, Latin America needs a regional-level production and complementarity programme with suitable promotion and protection instruments which simultaneously promote a more effective integration process and a more equitable distribution of the benefits of that process among all the countries of the region. This process should also be accompanied by policies whereby the Latin American countries concert their international action more closely, and it would constitute a basic element in increasing the degree of autonomy of the region's economic and social development.

In order to progress in this direction, we

consider that in the present circumstances it is essential to reaffirm those Latin American policies which are aimed at achieving:

a) as much complementarity as is possible in production, trade and the utilization of transport, insurance, technological and other services, on the basis of the principle of Latin American preferences and as a way of achieving an effective and efficient import substitution process at the regional level. To achieve this objective it will be necessary to act flexibly and pragmatically, making the fullest use of the existing integration instruments, special arrangements between governments and other economic agents, and all possible means of non-traditional co-operation;

b) the initiation of an effective process of institutional articulation and co-ordination among the various entities working in the field of regional integration and co-operation, with a view to lending consistency and direction to their initiatives and activities. This process may be long and complex, but it would make it possible to proceed clearly and firmly towards the building of an authentic regional economic community;

c) the consolidation and broadening of the joint bargaining power of the countries of the region so as to correct the structural and conjunctural asymmetry in their external economic relations and effectively defend their common interests, together with those of the other developing regions, against other countries or groups of countries.

In order to make progress towards the attainment of these objectives, it will be necessary in the first place to increase regional co-operation in the fields of trade, finance, the production and supply of food and energy, and the development of transport; secondly, there will be a need for stronger co-operation with the relatively less developed countries and with other developing regions; and, finally, it will be necessary to link up properly the Latin American institutions engaged in the processes of regional co-operation and integration.

C. THE DEFENCE AND EXPANSION OF INTRA-REGIONAL TRADE

As we already saw, intra-regional trade has tended to weaken in recent years. In order to reverse this trend and take full advantage of the potential offered by such trade, measures aimed at the following objectives should be adopted:

a) to defend the levels of intra-regional trade already reached and keep it from being subjected to new limitations or obstacles;

b) to establish a margin of regional preference;

c) to promote flexible forms of trade, agreed upon within the existing integration schemes, in the framework of multilateral disciplines.

a) *Strengthening intra-regional trade and preventing its erosion*

One of the first objectives should be to stop the erosion of terms of access in intra-regional trade and prevent the application of additional obstacles to its expansion.

To achieve this aim it is necessary to put into operation higher-level machinery for consultation among the officials responsible for foreign trade in the Latin American countries, in order to deal with any disputes which may arise, solve the administrative problems posed, provide information on any restrictions which are applied, become familiar with existing systems for export promotion, and explore ways to minimize the impact of the present economic situation and of the restrictive trade measures accompanying the severe balance-of-payments crises in our countries.

At the same time, it is indispensable to adopt a regional-level standstill commitment which would provide a basic foundation on which any additional phase of the trade aspects of regional integration could be built, thereby making it unnecessary to start once again to lift the measures imposed as a result of the generalization of restrictions among Latin American countries. An additional advantage of an agreement of this type would be that it would automatically constitute a form of preference compared with the treatment given to third countries.

This initiative could take the form of an administrative decision suspending the implementation of all measures for limiting intra-regional trade adopted by every Latin American country as from a certain date, on the basis of partial agreements or of a formal multilateral instrument.

b) *Establishment of Latin American preferences*

Regional Tariff Preferences (RTP) are envisaged in the 1980 Treaty of Montevideo establishing ALADI. For its part, resolution 5 of the Council of Ministers of that regional grouping states that the preferences "should extend as far as possible to the entire tariff universe". The RTP are destined in this way to provide a multilateral link among the member countries of ALADI.

We feel, however, that the establishment of Regional Tariff Preferences should lead to the introduction of trade integration machinery for the whole of Latin America. We therefore consider it desirable to formulate an *ad hoc* agreement for adoption by all the Latin American countries. In order to ensure its rapid implementation, it should not have to be ratified or adopted by the individual national legislations in the normal manner. It could consist of an agreement for the partial or total suspension—but only on a temporary basis—of customs duties.

Several studies have been prepared on the various options available for avoiding the difficulties raised by implementation of the RTP, particularly with regard to the heterogeneity of the tariff systems of the different member countries, the partial preferences already in force as a result of negotiations held within ALADI, and the preferences existing among the Andean countries. For all these cases, technically adequate solutions which would facilitate adoption of the preferences have been suggested.

The decisions recently taken within ALADI on negotiating the common heritage could pave the way for reaching, in the briefest time possible, the political decision to implement this system of preferences. Its importance

is all the greater today because of the need for maintaining clear and firm elements of multilaterality in a scheme of trade relations which necessarily is going to have to exploit, pragmatically and to the maximum, the opportunities offered by partial complementation agreements and bilateral processes for maintaining and expanding trade flows. Without disregarding the importance of the latter, it appears particularly vital, both politically and economically, for the region as a whole to establish regional preferential action which would lead to global-level trade integration machinery.

It is obvious, however, that under the current economic circumstances tariff machinery by itself would not be sufficient to avoid other obstacles opposing the expansion of intra-regional trade. However, tariff preferences can generate trade, both by encouraging exploration of new preferential markets and by improving the conditions of access to markets which are protected by relatively high tariff levels or by institutional features which make them nearly impenetrable to imports not coming from the industrialized countries.

Trade preferences may go beyond the tariff sphere and extend to a comprehensively Latin American outlook concerning preferences, as a result of which, under the present circumstances, they could become a fundamental anti-cyclical instrument for resisting the drop in exports to areas outside the region and also make possible a reduction in imports from outside Latin America.

This outlook concerning preferences could be firmly applied to the State purchases which currently make up a significant portion of the imports of most of the Latin American countries. Most of the large infrastructure works and the largest purchases of capital goods conducted in the region are in the hands of the State or of public enterprises, while in some other cases the investments are made by private enterprises, which enjoy official financing or guarantees. Therefore, a regional system of preferences in public tenders open to foreign enterprises may be extremely important in increasing trade and reactivating the demand for capital goods, which has decreased as a result of the cuts in public investment taking place in many countries in the region.

c) *New forms of regional trade*

In the current circumstances, ALADI offers a flexible legal framework for constructing an area of economic preference through a variety of mechanisms. Among other instruments, explicit recognition is given to the part which may be played by agreements of partial scope in diverting trade flows.

However, we believe that, while the 'realism' of the potential held by agreements of partial scope should be recognized, multilateral discipline should also be observed as a way of avoiding the re-introduction of competitive or exclusive bilateral trends which would check possible advances towards permanent multilateral forms and, eventually, towards a true regional economic community.

It is in this context that we should envisage the role of subregional, bilateral and partial agreements, and of the balanced or adjusted trade which has recently acquired new momentum.

It is true that the latter suffers from defects or elements of trade diversion that are not always effective or economically advisable. However, as recent trends in the international economy have demonstrated, these mechanisms are especially attractive as a response to the emergencies raised by the crises in the balance of payments and should be explored among the countries of the region. The food and fuel sectors provide a suitable area for this type of trade agreement.

For example, in 1979 the Latin American countries imported food and beverages in an amount of slightly more than US\$ 10 billion, of which only US\$ 3 billion came from other Latin American countries. That is to say, the extra-regional imports represented approximately two-thirds of the total Latin American imports of those products. In the same year the Latin American countries exported slightly more than US\$ 25 billion of those same products out of the region.

In the fuel area, it should be pointed out that in 1979 the Latin American countries imported US\$ 20.7 billion of such goods, of which only slightly more than US\$ 8 billion originated in the region. That is, 60% of the regional fuel imports came from the rest of the world, which

leaves an ample margin for developing reciprocal trade.

The extra-regional imports of these two product groups as a whole are equivalent to nearly the total figure for intra-Latin American trade, while exports of them out of the region are, in both cases, far higher than the extra-regional imports. This provides an idea of the opportunities existing for expanding trade among the Latin American countries, especially with respect to food and fuel, trade in which is to a large extent in the hands of public or State-controlled enterprises.

This shows how important it is to extend to the region as a whole the attempts already being made bilaterally to establish mechanisms for increasing opportunities for expanding balanced, compensated trade.

D. FINANCIAL CO-OPERATION

Examination of the current problems of regional trade and the limitations on its expansion points to the great importance of expanding and strengthening regional mechanisms for financial co-operation.

We consider it of high priority and feasible in the short run to revitalize and interconnect several already-existing intra-regional financing schemes. Among these are the multilateral payments mechanisms (Central American Clearinghouse, Caribbean Multilateral System of Compensatory Payments, and the ALADI System of Reciprocal Payments of Balance and Credits); the trade balance and balance-of-payments mechanisms (Santo Domingo Agree-

ment, Central American Monetary Stabilization Fund, and the Fund for Debit Balance Financing in the Central American Clearinghouse), and export credit financing and insurance (Latin American Export Bank, Andean Trade Financing System, and Latin American Association of Export Credit Insurance Agencies). These are initiatives which, for the most part, have already been studied and could increase their contribution to reciprocal trade and to the saving of foreign currency in the region.

In the area of project financing, it is worth while recalling that the region already has four subregional bodies —the Central American Bank for Economic Integration, the Caribbean Development Bank, the Andean Development Corporation and the River Plate Basin Financial Fund— all of which are in a position to absorb additional intra- and extra-regional resources. The latter resources could become a highly useful complement to the efforts in the area of domestic savings which the region must carry out in order to accelerate its development.

In the nearly 25 years of its existence, the Inter-American Development Bank has played a very significant role as a body for promoting the development of Latin America, combining resources from the countries of the region with those from outside the region. However, it would have even more importance in the Latin American integration process if it placed more emphasis on promoting the financing of intra-Latin American exports and expanded its action in favour of regional co-operation, including the promotion and financing of joint investment projects among several countries.

E. CO-OPERATION IN THE AREA OF FOOD, ENERGY AND TRANSPORT

Latin America is facing the risk of growing external dependency in satisfying its ever-increasing food consumption, for the prospects for the future evolution of demand and the production of food for the region as a whole indicate that, if current trends do not change, Latin America's net trade deficit of food products with the rest of the world will rise sharply. This will be serious not only in terms of its influence on the bal-

ance of payments but also with respect to the worsening of the external vulnerability of such a strategic sector as this.

Therefore, the Latin American countries have recently established, in the framework of SELA, an Action Committee whose objective is to develop a System of Regional Food Security. Under this Committee a programme of action has been established whose objectives are as am-

bitious as the food situation of the region is disturbing. In other words, in this area Latin America already has the institutional and planning framework necessary for meeting one of the most important challenges that it will have to face in the coming years. We therefore consider it of the highest importance for all the Latin American countries to participate actively in this venture and for its full implementation to be ensured through the granting of the political support which it deserves.

The situation is similar in the energy area. Through the Latin American Energy Organization (OLADE) and its Latin American Energy Co-operation Programme (PLACE), the Energy Co-operation Programme for the Countries of Central America and the Caribbean established by the San José Agreement, and various bilateral and even multinational initiatives, an extensive network of agreements and programmes of action has been established in the region, which should make it possible for Latin America to meet more adequately, in the future, the problems arising from its commercial and technological vulnerability in the energy sector.

Under the current circumstances, we feel that it is particularly important to give the political and financial support needed in order for these initiatives, and especially the Latin American Energy Co-operation Programme, to develop fully. Their influence on the economic reactivation of the region, the maintaining of the level of export income of the producer countries, the saving of foreign currency by the importing countries, and the consolidation of regional technical development is enormous, and it could be detrimental to Latin America to ig-

nore them when the contribution they can make is so great.

In the case of transport, many kinds of action may be taken to improve the administration and technology of the merchandise movements stemming from trade between the region and the rest of the world and in the region itself. It is mainly a question of reducing costs, improving competitiveness with respect to the services offered by third countries, and procuring a growing proportion of the extensive freight and insurance market, which is mainly in the hands of businesses outside of the region today. It is sufficient to point out that in 1982 the region paid to foreign enterprises approximately US\$ 8 billion in maritime freight, that is, approximately 70% of its total expenditure in this category.

In order to tackle these problems and seek suitable solutions for them, it is considered necessary to have a forum—which does not exist at present—in which to study at the regional level the questions of the institutional strengthening of sea transport and transport facilitation.

This forum, which could be institutionalized in the form of a Permanent Maritime Transport Committee within SELA, would enjoy the technical support of ECLA and of the regional integration bodies. Its objective would be the integral study of the problems affecting maritime transport and related matters in Latin America, with a view to promoting the development of national merchant marines, increasing the region's share in the movement of its international trade, and improving intra-regional maritime services.

F. LATIN AMERICAN CO-OPERATION WITH THE COUNTRIES OF CENTRAL AMERICA AND THE CARIBBEAN

It does not appear possible to achieve the dual ideal of accelerated and relatively autonomous development and greater regional equity without special help for the countries of Central America and the Caribbean, either within the respective integration schemes or by seeking *ad hoc* instruments which would allow non-member countries to associate themselves with them.

New geoeconomic spaces could be created in this way, enriching the possibilities of integration and co-operation and of regional political co-ordination.

To a great extent the legal infrastructure for this already exists, since the 1980 Treaty of Montevideo makes it possible to grant non-reciprocal preferential treatment to developing

non-member countries of ALADI, such as the Central American and Caribbean countries, and other non-members of integration schemes, such as Cuba, Haiti, Panama and the Dominican Republic. Although there are significant difficulties involved in an initiative designed to increase commercial and economic links between the countries of ALADI (which includes the Andean Group) and the Central American and Caribbean countries, we are also aware that the region will achieve its true political and economic significance only when there is a network of effective links uniting all the countries in the Latin American community, while avoiding the presence of elements which tend to reproduce inequitable relations between them.

In this framework of ideas, we consider this to be a particularly favourable occasion for making a special effort to fully incorporate the Caribbean and Central American countries into this process.

Central America is a zone that is especially affected by the international economic crisis and by serious political tensions which are threatening to destroy the region's peace. We believe that the rest of Latin America cannot remain indifferent towards that situation. We therefore propose that a Latin American emergency programme in support of Central America should be adopted, so that the countries of that subregion will be able to moderate the effects of the crisis and revitalize their economic and social development process. That programme could be based on two main groups of measures.

Firstly, Latin America should foster an initiative aimed at regional economic co-operation with the Central American countries, helping them to promote their economic growth and, in this way, relax political tensions. Although this action would call for some financial support from the other Latin American countries, its main virtue and potential would lie in the assis-

tance these countries would lend to help the Central American countries obtain a higher level of global external financing.

Secondly, in accordance with the stipulations of the 1980 Treaty of Montevideo setting up ALADI, the most developed countries in the region could facilitate the access of Central American products to their markets through preferential trade treatment.

In the case of the Caribbean countries, their history and rich cultural heritage differ in many aspects from those of the rest of the Latin American countries. As they have been gaining independence, they have been joining regional organizations, sharing with and within them their problems and aspirations. Under the present circumstances, these countries are fully aware of their region's special identity and of the need for strengthening their unity to meet the challenges of their economic, social and political development.

For their part, it is in the best interests of the other Latin American countries — particularly those in the vicinity of the Caribbean region — to make maximum efforts to support the economic development of the Caribbean countries and to strengthen the relevant co-operation structures.

In view of the seriousness of the international situation's repercussions on the economy of the Caribbean countries, we feel it is necessary for the Latin American countries with the greatest potentialities, despite their present economic limitations, to expand their facilities for supporting this subregion by means of an initiative to be analysed and projected jointly with the Caribbean countries.

The continuation of the energy co-operation programme of Mexico and Venezuela in favour of the Central American and Caribbean countries is very encouraging in this connection.

G. THE LACK OF CO-ORDINATION IN THE LATIN AMERICAN INSTITUTIONAL SYSTEM

There is one last aspect of Latin American co-operation which we would like to mention with special emphasis on this occasion, since we feel it is an important factor in determining the pos-

sibilities for strengthening regional co-operation. We refer to the present lack of co-ordination among Latin American institutions.

In recent years, many regional specialized

agencies have arisen, a large number of committees or bodies dependent upon these agencies have been established, and action plans and regional strategies related to the most varied areas have been set up. Many of these mechanisms duplicate or overlap those which have arisen in the framework of regional and subregional trade or physical integration agreements or the regional bodies and specialized agencies of the United Nations system or the inter-American system. Each of these institutions generally has its own governmental machinery and secretariat. All this constitutes a thickly interwoven institutional fabric which lacks joint structures and co-ordination. There is no mechanism for establishing any form of co-ordination among all or at least some of these institutions. Furthermore, many of these agencies often follow parallel and in some cases even contradictory paths.

All these facts make it advisable to establish some type of central mechanism for the adequate co-ordination and promotion, from a high political level, of the activities and initiatives being proposed by this variety of institutions. Rather than avocating collective control machinery, we are proposing that they should be integrated at the functional level and pro-

vided with common guidelines, thus reinforcing the value of the activities being developed by one or the other.

In accordance with its original mandates, SELA could assume the functions of guiding and co-ordinating those Latin American institutions which deal with negotiation activities, both in the harmonizing of common positions towards third countries and in regional integration and co-operation.

We feel that in this way more co-ordinated and effective attention would be given to many initiatives which often are not implemented effectively, due to the institutional weakness of their bases or because they compete with similar initiatives coming from other forums. Alternatively, it is necessary to ensure support for initiatives which lose vitality after being taken, since only through the support of the governments is it possible to ensure their survival and development.

The advance of the regional integration and co-operation processes towards their final goals must at the same time be linked up with the institutional structure called for by the development and consolidation of the Latin American community.

VI

Concerted regional action to deal with the problems of international trade

It seems clear that the basic balance-of-payments and indebtedness problems of the region can be solved in the medium and long term only by improving the terms of world trade and putting a sustained programme for the expansion of regional trade into effect. Unless the necessary external resources can be generated by means of trade, it will not be possible to find a solution to the present balance-of-payments bottlenecks or to cope with the debt servicing requirements.

It is probable that in the next few years the growth rate of international trade will be rela-

tively slow, more or less in line with the sluggish evolution of the world product projected by various specialized bodies. This is partly due to the loss of impetus suffered by the process of increasing trade openness of the industrialized centres which accompanied and promoted their rapid economic development in the period from the end of the war up to the mid-1970s. This has also held back the progress which was being made towards a new international division of labour at the world level.

Moreover, the principles and rules on trade liberalization which have governed inter-

national trade under the aegis of GATT for more than 30 years are being progressively eroded. It was impossible to reverse this negative tendency at the last ministerial meeting of GATT, held at the end of 1982. Thus, the increasingly discriminatory and covert nature of the measures which countries have been taking has meant that in practice the exceptions to the GATT regulations now cover a very high proportion of international trade, affecting Latin America in particular.

In order to cope with these unfavourable trends, Latin America can take three mutually complementary types of action. On the one hand, it can define and adopt policies aimed at strengthening its joint potential for responding to and negotiating with the industrialized centres. Secondly, it can use its presence in different multilateral and bilateral forums to put forward its claims more actively. Finally, it can diversify its markets in order to improve the possibilities for selling its exports.

A. STRENGTHENING LATIN AMERICA'S BARGAINING POWER

Latin American exports of basic commodities and manufactures—the expansion of which is essential for the region's development—face in the markets of the industrialized countries a set of tariff barriers (graded according to the degree of processing of the exports) as well as non-tariff barriers. Both types of protection have a limiting and discriminatory character and are gradually bringing about a situation where the central countries have acquired the capacity to manage as they wish their trade with the developing countries and especially Latin America. This management may take place in a selective and non-continuous manner or, if necessary, may be broader, more intensive and more frequent.

For these reasons, we consider that it is an essential task for the region to organize and take advantage of its bargaining capacity in order to have the real possibility of applying symmetrical trade treatment to exports originating from developed countries which apply protectionist policies: an aspiration which has been repeatedly manifested and approved by the Latin American countries.

In order to formulate and adopt these measures, however, it is necessary first of all to have timely and accurate information on the characteristics and scope of the protectionist instruments used by the industrialized nations, as well as the products or product groups in respect of which the Latin American countries could possibly apply compensatory measures. Subsequently, the application of such measures could be agreed and carried out in various alter-

native ways: one valid only for the Latin American countries affected by one or more specific forms of protectionism in the centres; another at the level of agreements taken within the existing subregional groupings, and a third, broader type which would constitute an agreement entered into by the entire region.

As regards basic commodities, since these represent around 80% of the total value of Latin American exports (approximately 40% if petroleum is excluded), it is immediately clear how vitally important and urgent it is to increase the level of their processing, to defend their international prices, and to organize greater and more stable bargaining power *vis-à-vis* the consumer countries.

Although basic commodities are so important to the developing countries, the main agents in world trade in this field are the developed market economy countries, which generate close to 60% of the world exports of these goods and absorb over 70% of the total imports of them. This means that in the case of some particular products such as cereals and cotton, the success of the measures proposed at the international level will depend on the degree to which the developing countries can organize their bargaining power to counterbalance that of the industrialized countries, either as producers or consumers. To this end, Latin America should define differentiated policies for each basic commodity or group of commodities, in line with their particular characteristics, the kind of action or measures to which they lend

themselves, and the role which the region could play in each case.

In this connection, there is an urgent need to support the commodity agreements as fully as possible, in line with the objectives our countries identified at the recent meeting held at Cartagena in preparation for the sixth session of UNCTAD, which were validated shortly afterwards when the Group of 77 met in Buenos Aires.

In those cases where there are no international agreements which meet the interests of the countries of the region adequately or where attempts to seek solutions through the traditional agreements have proved sterile, Latin America should make the most, at the bargaining table, of the opportunities available to it through its combined purchasing power. In this regard, it is urgent to broaden and strengthen the bargaining power of the existing producers' associations (GEPLACEA and UBEC) and of the multinational marketing firms (COMUN-

BANA and MULTIFER) so that the success of these may serve as a basis for the establishment of similar bodies for other commodities which are important to Latin America.

The commodity export strategy also calls for the systematic incorporation as one of its essential dimensions of rising degrees of national processing and marketing of such products. The measures defined in this direction—a number of which will affect the operations of the transnational corporations—will have a leading role to play in the formulation of an integral policy for the commodity-producing and exporting sectors. As some Latin American countries have already been doing, it would be desirable for national authorities to incorporate into their foreign investment policies measures aimed at inducing the transnational corporations to increase their industrial exports of manufactures or semi-manufactures and generate increasing trade surpluses in their operations.

B. ACTION IN MULTILATERAL AND BILATERAL FORUMS

We do not wish to repeat here the lines of action emphasized by the countries in the Group of 77 and the Latin American Group, but to lay stress only on those which are most urgent and relevant in the present circumstances. The region, in co-ordination with the Group of 77, should continue pressing for the consideration and negotiation, within the context of GATT, of the gradual reduction of the various types of tariff and non-tariff restrictions now being applied. At the same time, for the identification of the problems involved in this field and the adoption of common positions by the developing countries, the institutional facilities existing in UNCTAD offer a good alternative whose timeliness and appropriateness become all the more obvious in view of the current Sixth General Conference of this organization.

The countries of Latin America must also act together to ensure that the benefits deriving from the Generalized Systems of Preferences (GSP) are expanded. The various limitations from which these systems suffer from the point of view of their transitory nature, their unilat-

eral characteristics, their selectivity, the rules regarding origin and quantities permitted and their use of the system of graduation have caused widespread frustration. It is therefore urgently necessary to improve them through the UNCTAD multilateral forum, and for this purpose the joint determined action of the region is indispensable, albeit without prejudice to bilateral negotiations with each of the countries or regions of the industrialized world which operate GSP schemes.

One of the forms of protectionism practised by the developed countries which is most harmful because of its dimensions, diversification and negative effects on the economic activity of the region is that of the subsidies for production and exports granted by those countries to certain key production activities.

For these reasons, we consider that one of the crucial issues which can and must be negotiated with the developed countries is that of subsidies. These negotiations should be carried out in the appropriate forums and with a great sense of urgency, since the code on sub-

sidies currently in existence is inappropriate and ineffective. While these negotiations are in course it will be necessary to have some complementary operational support and technical analysis machinery within the framework of UNCTAD.

Furthermore, it is also essential to redouble efforts to strengthen and expand the Integrated Programme for Commodities agreed within UNCTAD, both as regards the gradual adoption of international agreements between

producers and consumers for 18 selected products and as regards the complementary initiative for the establishment of a Common Fund for commodities. Especially as regards the Common Fund, it is our firm belief that the Latin American countries can play an effective leadership role in the process of obtaining the signatures and ratifications required in order to complete the entry into force of the Agreement setting up this Fund.

C. THE NEED FOR DIVERSIFICATION OF THE MARKETS FOR LATIN AMERICAN EXPORTS

Because of the growing inability of the markets of the central industrialized countries to absorb additional Latin American exports, as well as the increasingly serious difficulties in gaining access to them, a policy aimed at the expansion and strengthening of other markets is clearly justified and of high priority. This policy should include exploration of the opportunities offered by trade with the centrally-planned economies, especially those of Eastern Europe which are members of the Council for Mutual Economic Assistance (CMEA). Trade with the CMEA countries has shown relatively rapid growth in recent years, although it is true that it started from a very low level. A considerable number of trade and payments agreements have been signed between countries of the two areas, many of which go beyond the purely trade area and

include matters of industrial, scientific and technological co-operation. The existing experience therefore gives grounds for viewing in a positive manner the prospects of greater expansion of reciprocal trade, although this may partly depend on the obtaining of satisfactory solutions for the establishment of multilateral agreements for settling trade balances.

It is worth noting that the Latin American countries are interested in diversifying their exports to the CMEA countries — which currently consist almost entirely of primary commodities— through the export of manufactures. In addition, the possibility should be explored of inducing the CMEA countries to grant long-term preferential contracts in respect of products of interest to the region, within a new system of international trade relations.

D. CO-OPERATION WITH OTHER DEVELOPING REGIONS

High priority should be given to strengthening the bonds of co-operation with other developing regions, pursuing the efforts already initiated with countries of Africa and Asia.

This co-operation should go beyond the purely commercial area so as to attain and operate in a broader context of reciprocal co-operation within a framework of integration where co-operation is promoted not only in trade but also in the fields of technology, transport, the exchange of experience and joint investments.

In this connection there are of course factors which restrict the possibility of expanding

trade relations, such as limited supplies for export; problems of transport, communications and financing; the absence of preferential arrangements and, above all, the shortage of reliable and timely information.

One of the priority tasks is to seize the opportunity available in the present circumstances to intensify the action taken in these fields of co-operation, within which the establishment of a global system of trade preferences among developing countries can play a significant role, as can the mobilization of the developing countries themselves through the existing regional institutions.

VII

The challenges raised by the crisis and a new form of development

The preceding analyses demonstrate the great external vulnerability of Latin America in the face of the international economic crisis and the limited possibilities offered by the current policy of the international financial agents. As a response, we advocate concerted Latin American action in the international sphere in order to obtain a thorough-going structural adjustment which will make it possible to defer over time and distribute more equitably the costs facing the countries of the region today.

Latin America has been meeting the crisis by rigorously adjusting its economies and facing up to high social and economic costs. Up to now, in most cases, the results do not appear to justify the sacrifices. If the current conditions continue, recovery will continue to be slow, and the social and political costs will be even higher.

Mobilization of the Latin American potential for international negotiation and regional co-operation is therefore becoming essential for achieving a more equitable distribution of costs among the countries of Central and Latin America. This redistribution of costs will expand the countries' degree of manoeuvrability, avoiding the creation of undesirable and dangerous social tensions. Although we have had to concentrate our recommendations on urgent current problems, and especially those arising from external relations, there is no doubt that action in the internal policy sphere is essential if the current recession is to be handled with fairness and a long-term view of the existing problems. Such an approach would also provide international action with appropriate domestic support in the political, social and economic sphere.

Taking a structural view of the problems afflicting us, the crisis has pointed up the long-term unfeasibility of development strategies which have once more proven their extreme external vulnerability and their tendency to create inequitable societies.

For this reason, in our approach to short-

term adjustment problems we would also like to call attention to the need for substantial changes in the current modalities of our economic and social development. In this context we believe that the measures being put forward in international and regional spheres should, while reducing short-term external imbalances, create the foundations for different forms of growth and distribution.

The new modality for development should aim at substantive changes in external economic relations, correcting the structural imbalances which have characterized them in the past. What is more, it should be acknowledged that, even if the hoped-for reactivation does occur, both in the economies of the centres and in world trade, the extra-regional relations of Latin America will make it necessary to envisage as restrictions the high initial indebtedness and a new international financial context. Even if the debt is successfully renegotiated, servicing it will continue to affect the Latin American economies, and it is highly improbable that net external financing will again play a role similar to that which it played during the 1970s. Furthermore, it is unlikely that protectionism and the instability of world trade will cease to be significant problems, which makes rather questionable the strategies basing the economic dynamism of the region on exports to the centres. Therefore, the new arrangements for development should be based more and more on the domestic and intra-regional markets and—to the extent that South-South relations become strengthened—on the markets of the rest of the developing world.

The needs and pressures connected with the crisis, by reducing considerably the import levels at which the previous forms of economic growth operated, once more open up possibilities for substitution in the national and regional spheres. Efficiency of operation, in our opinion, is indispensable in this new stage of import substitution. In any case, the serious cur-

rent economic deterioration does not leave room for wasting the scant resources available. Furthermore, we feel it is absolutely necessary to orient the production changes in the new modality of development towards a regional market. In this connection, the recommendations made concerning regional co-operation in trade, financing and other spheres should be considered as first stages in a long-term process of a multilateral nature.

The new modality of development must also meet other requirements in the domestic sphere. In the area of equity, a suitable policy should be developed for keeping up appropriate levels of consumption and employment opportunities for the broad masses. With regard to medium- and long-term expansion, it is indispensable to preserve the physical and industrial infrastructure which it cost so many years of effort to build. Furthermore, in the key sectors for the new economic expansion it is essential that levels of investment, which in some cases now threaten to be insufficient even for covering the depreciation of the existing production capacity, should be recovered as soon as possible.

These challenges are in many cases in open contrast with the previous patterns of consumption and savings. Thus, in our view, the new economic policies must aim at much greater austerity than in the past —austerity in both public and private consumption and, most especially, in that of the high-income strata. The reduction of these strata's diversified consumption, which is also highly dependent on the exterior, will not only facilitate the social consensus, but also make it possible to attain the objectives of domestic savings, relieve the pressure on the balance of payments, and make it easier to control inflation.

The complexity of the problems we are facing and the nature of the changes needed place very strict demands on the management

of the economy. However, the most difficult obstacles will arise at the political and institutional level. Both the short-term measures and the transition towards a new development strategy call for a firm and wise hand on the part of the State. The varied political experience of Latin America makes it clear that there are no mechanisms or institutions which, by themselves, can ensure that the economic process will proceed efficiently and properly.

The market has economic and political virtues, but these do not include the unaided ability to guide development or cope effectively with crises. We believe that in periods of crisis it is vital for the State to play a central role in the management of the economic process and in the co-ordination and harmonization of efforts. We must not, however, fall into the technocratic illusion of thinking that this kind of intervention alone is any guarantee of a reasonable degree of efficiency.

Co-ordination refers first and foremost to the need for the whole State apparatus —central and regional, administrative and decentralized— to act in an integrated and harmonious manner. Concerted action has to do in particular with the capacity of the State apparatus to reflect the interests of the social groups, guide their action and direct wills towards common goals.

Although the co-ordination of the State apparatus is the necessary and primary source of its efficiency, the harmonization of efforts between the public and private and the labour and entrepreneurial sectors is also an essential feature of the kind of planning which is so sorely needed at present.

Only by combined action directed towards common goals will societies be able to solve their pressing problems and provide an answer not only to the concerns of the moment but also to the challenges of the future.

The world crisis and Latin America

Conclusions of the meeting of leading personalities
convened by ECLA in Bogotá from 19 to 21 May 1983

A. ORGANIZATION OF THE MEETING

1. The Executive Secretary of ECLA called together a group of leading Latin American personalities* in order to analyse, on a strictly personal basis and without implying that their views were shared by their respective governments or institutions, the impact of the international economic crisis on Latin America and possible solutions to this problem. The meeting took place in Bogotá from 19 to 21 May 1983 and was officially opened by the President of Colombia, Dr. Belisario Betancur.
2. During this meeting the participants unanimously expressed their deep gratitude for the perceptive, warm and effective support received from the President of the Republic of Colombia, the different national authorities of that country, and its people as a whole.
3. The following are the main conclusions reached at the meeting.

B. CONCLUSIONS

4. As a result of the severe imbalances in the international economy and the build up of unresolved problems as regards their development strategies and domestic economic policies, the countries of Latin America are passing through the severest economic crisis experienced in the last fifty years. The sharp drop in commodity prices, the resurgence of protectionism in the industrial centres, the high real interest rates still prevailing on international financial markets, the violent contraction in the inflow of external private credits after a period in which such credits increased to an extraordinary degree, together with a great mass of problems of domestic origin, constitute factors which have combined to give rise to acute balance-of-payments crises and severe declines in growth rates—and even in absolute levels of economic activity—in most of the countries of the region.
5. The international economic crisis has been closely linked to the unfavourable economic performance of the industrialized market economy countries in recent years. The decline in their economic activity not only represents a sharp setback in the long cycle of expansion which began after the war, but is also a reflection of the effects of the structurally imbalanced markets built up by these countries over the years. The crisis of the industrialized countries has also been influenced, however, by the very restrictive monetary policies which they have applied in a context also characterized by big fiscal deficits. As a result, interest rates have reached unprecedented high levels which represent the main obstacle to the achievement of a vigorous and lasting recovery in the international economy, while they have increased to an extraordinary extent the cost of servicing the Latin American countries' external debt. Furthermore, because of their projections on domestic interest rates and the fact that in some countries they have coincided with policies of exaggerated financial liberalization, they have helped to weaken the solvency of enterprises and to make it more difficult to achieve a recovery in economic activity and employment in most of the countries of the region.
6. The contraction in the Latin American countries' external trade has been visible not only in their trade with the rest of the world but to an even greater extent at the intra-regional level. Thus, at a time when intra-Latin American co-operation is more necessary than ever, it is being the victim of the combined effects of the international economic crisis and of domestic factors which join with the recessive forces operating in the region to erode the co-operation process. The increasing re-

*See the list of participants at the end of this article.

restrictions on reciprocal trade which have been growing up in all the subregional integration groupings in Latin America are a source of particular concern.

7. It must also be acknowledged that the shortcomings in the economic policies applied by some countries of the region have played their part in the serious situation now being faced by them. Consequently, as well as adopting the immediate measures called for in order to face up to the crisis, the countries must gradually progress towards styles of development which are not only more in keeping with the more restrictive international context and the growing legitimate aspirations for social equity which will probably prevail in the future but are also based to a greater extent on domestic effort.

8. In order to face up to these challenges, it is necessary to make thorough-going changes in the current international economic order in line with the proposals repeatedly made by the developing countries in different international forums. It is essential, too, that in the immediate future the main developed countries should put into effect vigorous economic reactivation programmes through co-ordinated action which avoids the generation of new inflationary pressures. This reactivation policy must also include measures taking account of the legitimate interests and aspirations of the developing countries, so that the latter may play the dynamic role which corresponds to them in the international economy.

9. The developing countries, for their part, must decide on action aimed at reactivating their own economies both by taking advantage of the opportunities offered by the recovery of the world economy and by increasing the domestic demand of each country and of the region as a whole. Likewise, important changes are called for in the way the domestic economic policy of most of the Latin American countries is run, with the aim of bringing it in line with the new circumstances and effecting the structural changes needed in order to promote better income distribution and, through it, the achievement of the necessary social consensus.

10. All this calls for more effective and timely action on the part of the State, not only in order to face up to the crisis but also in order to ensure that, once it has been overcome, the economies will resume the process of economic growth on more stable, equitable and dynamic bases. In order to do this, it will be necessary to make more effective use of monetary, fiscal and exchange instruments, place domestic financial markets on a sounder basis, provide the public sector with non-inflationary sources of revenue, and bring about more equitable sharing both of the sacrifices involved in the adjustment process and the fruits of economic development.

11. The countries of the region have clearly expressed their firm will to honour the external commitments they have assumed. Even at the cost of extreme sacrifices, however, many of them are not likely to be in a position to pay their external debt servicing costs on the terms originally contracted. Moreover, some of the solutions reached so far seem rather to be mere expedients which could give rise to new and even more serious difficulties, while in the renegotiation processes the private commercial banks have excessively increased their commissions and surcharges in respect of the loans which have been refinanced.

12. The existing international financial institutions lack both the faculties and the resources needed to offer solutions which reconcile the fundamental interests of debtors and creditors. Furthermore, the conditions associated with the supply of emergency aid to debtor countries actually represent an expedient for rationing out the institutions meagre resources. These circumstances are leading to a still greater contraction of international trade which is aggravating the world crisis and increasing its social costs for our countries.

13. We are thus facing an intrinsically unstable situation. There is an increasingly general conviction that it is urgently necessary to achieve a real and lasting solution which will help to restore stability to international relations. In no way does this mean advocating a collective confrontation between the debtor and creditor countries, nor does it mean promoting the joint refinancing of the external debts of countries which are in very different situations. It is essential, however, to take political initiatives at the highest possible level in order to bring home to those responsible for running the international community both the serious consequences which could result from a further contraction

in the economic activity of the majority of the Latin American countries and the need to make available additional resources and create different conditions so that these countries may refinance their debts appropriately. As the President of Ecuador, Dr. Osvaldo Hurtado, has so perceptively understood, it is vitally important that these initiatives should stem from concerted action by the governments of the region, since the present dramatic situation not only affects them and their external creditors but also seriously limits the well-being and future prospects of hundreds of millions of Latin Americans.

14. For these reasons, it is essential that additional machinery should be set up, on top of that already in existence, in order to establish a more suitable international framework for the processes of renegotiation of the debt. These measures should include the participation of international financial organizations, the private banks, and the financial authorities of the creditor countries, and they should provide for the supply of additional resources in order to meet both the debt servicing commitments and the minimum financing needs for trade and development. At the same time, efforts should be made to reschedule debts for terms in keeping with the nature of the credits available and to bring about substantial reductions in interest rates, while the costs of the international adjustment process should also be distributed much more equitably between the creditor countries and banks and the debtor countries.

15. Along with the foregoing, it must be recognized that the fundamental balance-of-payments problems will not be finally solved unless conditions are created in international trade—especially as regards prices and openness of markets—which make it possible for the countries of the region to obtain the external resources they need to face up to their debt service commitments.

16. It is also desirable to reappraise the considerable potential offered by intra-regional co-operation, not only as an instrument for reducing the effects of the international recession and of the uncertainty over the future of the world economy, but also for aiding in the adoption of national development strategies which are in keeping with the new circumstances. In this connection, it is urgent to take concrete measures to avoid a further deterioration in the degree of economic interdependence already achieved within the existing subregional groupings and to halt and if possible reverse the harmful tendencies towards the imposition of additional restrictions on reciprocal trade observed in recent times. It is also necessary to approach the different forms of co-operation which could be tried by the Latin American countries with the greatest possible realism and flexibility. One of the aspects of the regional and subregional integration processes on which immediate action could be decided is that of the strengthening of the reciprocal payments systems in order to promote higher levels of intra-regional trade.

17. In addition, the external support policies needed in order to relieve the balance-of-payments problems of the Latin American countries must be accompanied by appropriate internal measures. In the short term, these measures should seek to promote the recovery of economic activity so as at least to conserve the basic levels of employment and consumption already achieved, while at the same time keeping in mind the standing objectives of the fight against inflation.

18. Both the measures adopted on the internal plane and the national policies designed to combat the crisis must be conceived in the light of the objectives, aspirations and proposals which the Latin American countries—and the developing countries in general—have long been advocating in various international forums with a view to promoting a thorough-going reorganization of the international economic order which will give them a more equitable and dynamic share in its functioning.

C. LIST OF PARTICIPANTS

BOTERO, Rodrigo (Colombia)	MENDES, Jorge (Colombia)
CASTILLO, Carlos Manuel (Costa Rica)	MINDLIN, José (Brazil)
CARRILLO FLORES, Antonio (Mexico)	MONCAYO, Jaime (Ecuador)
DEMAS, William (Trinidad and Tobago)	PALACIO RUDAS, Alfonso (Colombia)
ESPINOSA VALDERRAMA, Abdón (Colombia)	PEREZ GUERRERO, Manuel (Venezuela)
FERNANDEZ SAAVEDRA, Gustavo (Bolivia)	PIZANO SALAZAR, Diego (Colombia)
FERRER, Aldo (Argentina)	PREBISCH, Raúl (Argentina)
FURTADO, Celso (Brazil)	RAMIREZ OCAMPO, Jorge (Colombia)
GARAY, Luis Jorge (Colombia)	RODRIGUEZ, Carlos Rafael (Cuba)
HARF, Morris (Colombia)	SALGADO, Germánico (Ecuador)
IGUÍÑIZ, Javier (Peru)	SARMIENTO, Eduardo (Colombia)
JARQUIN, Edmundo (Nicaragua)	VALENCIA JARAMILLO, Jorge (Colombia)
KUCZYNSKI, Pedro Pablo (Peru)	WONSEWER, Israel (Uruguay)
MARSHALL, Jorge (Chile)	

The crisis of capitalism and international trade*

*Raúl Prebisch***

Full understanding of the nature of the present crisis calls for an interpretation which is at once broad enough to cover both the centres and the periphery and deep enough to penetrate beyond the superficial manifestations of the problem to the very heart of its causes.

In his search for such an interpretation, the author begins by analysing the internal structural imbalance of the centres, which consists, ultimately, of the disparity between the growth rate of consumption (both private and social, civil and military) and that of the accumulation of reproductive capital. This disparity lies at the root of inflation and of the fiscal deficit, which help to complicate the situation just as do the monetarist-type measures with which it is sought to combat them.

The author then goes on to deal with the structural imbalance between the periphery and the centres, in respect to which he examines the persistent problems of trade relations between them, and the conjunctural incidence of the crisis on the peripheral countries, in which connection he analyses the main short-term problems facing the countries of Latin America and the policy measures which should be used to tackle them, centered around the idea of reactivation. In the final chapter, on market laws and ideologies, he stresses the importance currently assumed by the ideological crisis, the complex manner in which it mingles with the other aspects of the crisis, and the need to overcome the state of intellectual dependence in which the periphery has lived in recent years.

*Document submitted to the Secretary-General of UNCTAD.

**Director, CEPAL Review.

I

The internal structural imbalance of the centres

1. *The crisis of the system and the crisis of ideas*

We are witnessing the end of an historic stage in the evolution of capitalism. After an enormous accumulation of capital over a prolonged period of time, and after having reached impressive levels of productivity, the latter is flagging and depression and unemployment are advancing upon us, with serious wastage of productive resources all over the world.

It is not a question of the final decadence of a system of enormous growth potential, since the vital elements which gave it great force persist, and the source of the incessant technological innovations is far from having dried up. It must be acknowledged, however, that the system is in crisis: it has strayed from its path and is suffering from structural imbalances which cannot be dealt with by ideas and forms of action that have been overtaken by events. The evolution of technology has brought with it great changes in the structure of society which have been matched by great changes in the structure of power, and no one is as yet certain how to deal with them. It is a crisis of the system and also a crisis of ideas, which have lagged behind the course of events.

All this is reflected in the disturbances in international trade and the persistent inflation, while the crisis has also acquired an institutional nature; GATT is crumbling, and monetary instruments have become ineffective and negative.

2. *The frustrations of GATT*

The concept behind the founding of GATT was based essentially on the free play of the market forces at the international level, but although it is true that GATT has had great importance for the centres, it is now on the verge of a serious setback. The recent meeting has been quite disconcerting: after the Kennedy and Tokyo rounds, where the great liberalization of the

centres' trade had been achieved, it might have been expected that GATT would be given its definitive consolidation. In fact, however, no undertakings whatever have been entered into to combat the drift back towards protectionism. Furthermore, while it is true that low tariffs have been maintained, various non-tariff restrictions have been growing up which seriously prejudice the liberalization achieved after such tenacious efforts.

These restrictions recall those of past times, which were not of course the result of arbitrary, irresponsible actions which spread over the whole world, but were imposed by the serious events set off by the great world depression.

Just as is happening today, the epicentre of this phenomenon was located in the United States, where the violent restriction of credit and the abrupt increase in customs duties did away with the multilateral system of trade and payments in a very short time. It took many years to restore this system, and GATT bore the important responsibility of gradually disentangling the mass of different protectionist measures and avoiding any subsequent backsliding: a responsibility which it has largely fulfilled.

It would seem, however, that GATT is losing its effectiveness for the centres, thus explaining the recent frustration at Geneva. How is this fact to be explained?

In a few words, it may be said that this institution has not been able to do something which it was in any case unreasonable to expect it to accomplish alone, for its effectiveness depends fundamentally on the expansion of the world economy. This is at present suffering a serious recession which is turning into a depression, however, and the spread of unemployment makes it increasingly difficult to struggle against the growing temptation of each country to defend itself from imports and from the consequences of monetary instability. Restrictions on one side provoke similar action on the other, and in this way the crisis is continually aggravated.

There can be no question of finding magic spells against this evil: the most that could be achieved through GATT is some degree of containment of these measures, for the problem is really quite different. It is necessary to go to its very roots, and these are once again to be found

in the United States, whence the economic recession set off by the anti-inflation policy is spreading to the other centres and to the rest of the world, with very serious consequences.

The effectiveness which GATT had for the centres did not extend to the periphery, since the original conception behind its establishment was in line with the interests of the former and did not allow for the systematic industrialization of the latter, although this initial attitude was subsequently adjusted to some extent. Industrialization took place as a result of the crisis of the centres (the two world wars and the great depression which occurred between them).

3. *The periphery and trade liberalization*

The periphery has been kept on the sidelines of the liberalization which took place among the centres, just as it had been kept on the sidelines of industrialization. In spite of determined efforts, it has not proved possible to secure any substantial liberalization of the attitude of the central countries to imports from the developing countries, even during the years of great prosperity of the former.

On the contrary, the developed countries maintained or even accentuated their restrictive measures during the period of prosperity which came to an end in the first half of the 1970s. Thus, the export successes of some developing countries were due primarily to the overall growth in demand, rather than to the elimination of restrictions. Be that as it may, the industrialization of the periphery is now causing serious problems for GATT. The centres had previously proclaimed the advantages of the international division of labour, when the periphery was not in a position to enjoy them as regards manufacture because it did not possess industries. Now, however, when the periphery does have industries, the centres are striving to find ways of refusing to recognize these advantages and are resorting to all kinds of restrictions outside the framework of the principles which gave rise to GATT: instead of the free play of the market forces, we now have 'managed trade', to use the very fitting expression coined by the UNCTAD secretariat. What was previously in keeping with the clear interests of the centres

now seems to have ceased to be so in view of the changes which have taken place, thanks to the spread of technology, in the structure of production of the peripheral countries.

The expansion of the world economy in the years after the Second World War created suitable conditions in the centres for the liberalization of their trade. There was a marked tendency in them towards homogeneity of production techniques, as the technical innovations of the United States spread to countries which had previously lagged behind and stimulated in them their own innovations. The transnational corporations played a very important role in this process. This was both a consequence and at the same time a contributing factor of the sustained growth in world demand and trade between the centres. And this trade was increasingly stimulated by the successive technological innovations. No matter how much the peripheral countries had progressed with their industrialization, they were still of course far from the stage at which they could participate actively in this movement. At the same time, however, they were increasingly developing the capacity to export manufactures, in some cases to an impressive extent. The manufactures involved consisted above all of goods which were either technologically less advanced or were produced by processes which had already ceased to be novel in the centres.

The great problem these manufactures have raised has been the need for a progressive reduction of the restrictions which do so much harm to the development of the periphery. There is no sign, however, that this is likely to occur in the present circumstances: on the contrary, serious setbacks are to be observed in this respect. Indeed, the talk is once again of reciprocity: that is to say, in order to secure the reduction of such restrictions on the part of the centres, the peripheral countries would have to make matching concessions. This simply means ignoring the great structural differences between the centre and the periphery which are due to the historic lag in the industrialization of the latter. We shall deal with this point in the following section.

4. *The structural imbalance of the centres*

We referred earlier to the resurgence of protectionism, and this fact must be acknowledged

quite frankly. It will be increasingly difficult to combat this trend if, in order to check inflation, the central countries insist on a restrictive monetary policy, especially through very high interest rates in the main dynamic centre of capitalism. Whichever way one looks at the matter, a reactivation policy is called for, but to what extent will it be possible to apply such a policy without sinking into a new wave of inflation? This is the disturbing question which it is impossible to avoid.

What has happened to the capitalism of the centres after such a long period of expansion? In order to answer this question, it is necessary to explain the serious structural imbalance which has occurred in those countries. This imbalance lies at the root of the new type of inflation which has appeared in this historic stage of capitalism. The attempt to tackle it through monetary policies has brought with it the present adverse situation which, as well as upsetting the trade of the centres, is making the external structural imbalance of the periphery even more pronounced.

Let us now try to explain what this structural imbalance consists of.

The considerable increase in productivity previously observed in capitalist development has gradually been slackening. This fact is closely related to the drop in the rate of accumulation of reproductive capital: that is to say, capital which multiplies employment and productivity through technical innovations and thus, in turn, constitutes the primary source of the growth of capital. This is a growth sequence which cannot be neglected without upsetting the functioning of the system.

The accumulation of reproductive capital has been based mainly on the primary appropriation of the fruits of growing productivity, especially by the upper strata of the social structure because of their economic, social and political power. The myth of the progressive spread of the fruits of technical process throughout society thanks to the laws of the market has not materialized, and only a portion of these fruits has been transferred to that part of the labour force which has the ever-higher qualifications demanded by technical progress. The portion which is not transferred remains, in the form of the economic surplus, mainly in the hands of the upper strata who own most of the means of production.

This form of appropriation of the surplus has made possible the process of intensive accumulation observed in the past in capitalist development. However, this process has become increasingly vulnerable in the course of the structural changes in the system and the consequent changes in the power relations.

Thus, the power of appropriation has been offset by growing power to force sharing of the fruits of productivity: on the one hand there has been an increase in the trade union and political power of the labour force, and on the other, in that of the State, in response both to this trade union and political power and to the demands of the growth of the State itself.

A struggle thus takes place which has positive effects until the system nears a certain critical limit, which occurs when the labour force and the State take for themselves such a proportion of the increase in productivity that the rate of appropriation begins to flag and, with it, the rate of reproductive accumulation. The growth of the system thus begins to slacken. Beyond this limit, the system reacts with a rise in prices, and this is followed by a rise in wages when the labour force has sufficient trade union and political power to achieve this. This gives rise to the phenomenon of spiralling inflation, which cannot be checked with monetary instruments without serious negative consequences.

These latter instruments were of proven effectiveness when there was no major counterweight to the dominant economic and political power of the upper strata, but they cease to be effective when the power relations change.

5. Consumption and accumulation

In order to gain a clearer picture of these phenomena, the struggle to share in the fruits of increased productivity should be viewed from another angle. Appropriation of the fruits of technical progress by the upper strata does not serve only to increase accumulation, but is generally accompanied by an exaggerated increase in consumption. Moreover, the increase in the wages of the labour force tends to expand consumption too as new forms of consumption arise in the upper strata, because of the unceasing diversification of goods and services brought by technological innovations, as well as

the increase in productivity. Social consumption also develops and grows, thanks to the political power of the labour force. This growth in both the private and social consumption of the labour force, however, does not usually take place at the expense of the consumption of the upper strata, but is superimposed on it. The same occurs in the case of the growing civil and military expenditure of the State.

All this reaches its most outstanding expression in the United States, where the image of bountiful prosperity has contributed markedly to this exuberant style of consumption.

It is hardly surprising, then, that this continual superimposition of different forms of consumption, together with the growth of different types of non-reproductive capital, is weakening the rate of accumulation of reproductive capital. The internal logic of the system thus tends towards an imbalance or maladjustment between the rate of consumption and the rate of accumulation of reproductive capital, or, in other words, between consumption and the saving necessary in order for consumption to keep up its rate of expansion.

It is easy to imagine this happening in the development of the periphery. What is hard to conceive, however, is that the internal logic of the system should tend towards this imbalance in the centres. Is it not true that the centres have achieved a considerable capacity for accumulation? And did not Keynes sustain, fifty years or so ago, that the system tended rather towards an excess of saving?

Whichever way we look at it, however, the full restoration of the growth rate of the system calls for the social reorganization of consumption in order to raise the rate of accumulation of reproductive capital sufficiently to increase employment and productivity. I do not wish to give the impression with this that there are not other adverse factors, but it does seem to me that the rate of accumulation of reproductive capital is of fundamental importance. There can be no doubt that successive technological innovations could increase the rate of productivity, but they also require the accumulation of capital.

The rate of accumulation can only be raised by reducing the growth rate or even the absolute level of consumption, depending on

the severity of the imbalance. In reality, however, the smaller amount of consumption on the one hand would be offset by additional consumption on the other, since the increase in the accumulation of reproductive capital makes it possible to increase employment and consumption by those who had previously been without work because of the structural imbalance or because they belong to the underprivileged social strata which had not been able to incorporate themselves into development at rising levels of productivity.

It is hardly necessary to show that changes of this kind in the social composition of consumption would run into formidable political obstacles. Is there any other way of solving this problem, then? The market laws do not solve it, nor does the social struggle to share in the fruits of progress. What is to be done, then?

The considerable fiscal deficit of the United States is an acute manifestation of structural imbalance. It has been acknowledged that consumption must be reduced in order to cover this deficit without causing inflationary effects. To this end, attempts are being made to attract savings from the public by offering extraordinarily high interest rates, which in turn means that bank interest rates on loans must be raised too, thus restricting credit to private activity, since otherwise bank money would be displaced towards the State, with inflationary effects. The depressive consequences of credit restrictions are well known and would be highly negative, since they would increase the deficit and diminish savings. Inflation could be reduced and possibly even eliminated through credit restrictions, but only at a very high social cost and, furthermore, without correcting the structural factors which give rise to it.

There has also been a good deal of discussion in the United States regarding the need to increase supply (i.e., the product) in order to check this phenomenon, in contradiction to the manipulation of demand advocated by the Keynesians. Indeed, if the product could be increased by greater accumulation, this would correct the structural imbalance which upsets the system. In order to achieve this purpose, however, it was maintained until very recently that it is necessary to reduce taxation on the upper strata so that they will accumulate more. Even if

they actually did this instead of increasing consumption which is highly problematical, this would not only mean promoting social inequity but would in its turn increase the fiscal deficit and its inflationary impact: that is to say, it would compress the consumption of the other social strata, and their members would try to make good their losses, thus accentuating the spiral.

It is interesting to note that an idea put forward a few years ago in a report prepared by experts of the United States Treasury Department now seems to have been forgotten. In this report, which was perhaps inspired by Lord Kaldor, it was advocated that there should be a radical modification of the tax system, whereby consumption would be taxed progressively instead of income: thus, that part of income which was not consumed would remain free of tax. Expressed in other terms, this tax on consumption would considerably encourage saving and accumulation. It seems strange to us that this proposal has not been discussed, in view of the tendency to an imbalance between accumulation and consumption. Of course I do not believe that this idea would solve the whole problem, but it would help to solve it if it were accompanied by other measures.

It must be understood, however, that—above all in a country accustomed to the indefinite expansion of consumption—this idea, like others aimed at the same objective, would run into very serious obstacles. Nevertheless, the truth is that there have not been any other proposals which really go to the root of the problem.

We also keep coming back to the suggestion that prices and wages should be controlled, but even if this had some temporary success, it could hardly be kept in effect for very long without serious difficulties.

To sum up, there has not yet been any clear discussion of the structural nature of the matter. The conventional doctrines represent a severe obstacle, which is as powerful as the interests which maintain it and promote it. Must we wait until the crisis gets worse, or until it repeats itself after we had had the illusion of having solved it, in order for new ideas and new forms of action to emerge?

6. *United States inflation and the Eurodollar market*

We shall now make special reference to inflation in the United States, not only because of the enormous importance of this country in the world economy but also because in the Bretton Woods agreements the dollar was given the role of an international currency in addition to its national role. Those were times when the dollar enjoyed great prestige, and very few people glimpsed the peril which this decision involved.

United States inflation goes back quite a long way, but it was moderate and tolerable until the social expenditure of President Johnson's 'New Society' and military spending gave rise to an inflationary deficit which subsequently got worse with the rise in petroleum prices in 1974. It may be noted in passing that this rise was not in itself responsible for the inflation, which had been provoked three years earlier by the abandonment of convertibility, but there can be no doubt that it helped to accentuate it.

This domestic inflation brought with it, as always, an external imbalance, but it was possible to cover this with dollars, that is to say, with mere monetary symbols. This meant that the domestic inflationary pressure on the product, together with part of the expenditure and investments abroad, could be covered with the product of the rest of the world.

If the dollar had not been playing this international role, the inflation suffered by the United States after the abandonment of convertibility would rapidly have resulted in devaluation of the currency, but this finally took place only after considerable delay, having finally been imposed by the external imbalance.

In the meantime, the overvaluation of the currency discouraged domestic investment by the transnational corporations, which preferred to make most of their investments abroad, to the detriment of the product of their own country. Thus, although the United States was able to enjoy the product of the rest of the world in exchange for dollars, this eventually adversely affected its own development.

In this way, inflation was spread to the rest of the world, although this does not mean that many countries, including those on the

periphery, were not already suffering from the inflation resulting from the distributive struggle. This inflation had also been developing in them too, but its external effects had been partly concealed, for the time being, through the inflow of US dollars.

This inflow, moreover, gave rise to something which had not been experienced up to then: the creation of the Eurodollar market. The monetary authorities of the other central countries, concerned at the expansive effects of the increase in reserves, viewed with favour the disposal of these resources on the Eurodollar market. In this way, the domestic inflation of credit was avoided or reduced, but only by transferring it to the international level. It was not only transferred but also increased, because for every dollar which entered the market in this way, the recipient banks increased their own creation of credit several times, as occurs with the increase of monetary reserves at the domestic level, but with the difference that within their own countries the monetary authorities had instruments for controlling this expansion of credit. In contrast, the Eurodollar operations were completely free of all regulation, and the consequences of this became very clear with the passage of time.

In this creation of money, no regulatory principle was followed at all, since this increase in the world money supply was the consequence of the domestic inflation of the United States, rather than an attempt to meet the demands of world development.

7. *The laws of the market and the IMF*

This was a lamentable setback in the monetary progress which had taken place over so many years. Long experience had established certain rules of domestic regulation deriving from the gold standard, and it had long been recognized that although the profit motive was important, it could not be allowed to determine the degree of expansion of credit without serious inflationary consequences. The dual role of the dollar enabled it to divorce itself completely from these regulatory principles in the Eurodollar market, where the desire of the great international banks for profits led to the creation of ad-

ditional Eurodollars, thus intensifying the original inflation.

The International Monetary Fund could have played a regulatory role, in view of the fact that it is not a profit-making institution, but no provision had been made for such a situation. In any case, it could hardly have done much, both because of the pressure of the banking groups in the centres and that of the debtor countries, which were able in this way to avoid the strict conditions of the IMF, whose attitude was marked by a singular degree of technocratic authoritarianism.

As we said earlier, one of the important conclusions deriving from long experience was that the creation of money could not be left to the dictates of the profit motive, since this would inevitably end in the abuse of credit and inflation, but this experience was not taken into account in the Eurodollar market, and even now, after such adverse results, many circles continue to insist on the prime role of the private international banks. In their view, the role of the IMF should only be to make loans at the last moment to avoid a serious international financial stampede. It should refrain from interfering in the free play of the market laws, only to intervene at the last moment in rescue operations!

At all events, I feel, the IMF should also make use of its own experience in order to play a leading role in the international monetary reform. Could this reform possibly be placed on a solid basis without changing the process of appropriation, accumulation and distribution in order to correct its growing vulnerability? I do not think so for one moment, for reasons which it is not necessary to repeat again here.

A clarification is called for at this point, however, even if only in passing. On more than one occasion, when I referred to the imbalance between consumption and the accumulation of reproductive capital, my opponents argued that the Eurodollar market represented a plentiful source of capital, but the fact is that this attitude represents a serious confusion of genuine capital with inflationary capital. The international loans represented genuine capital to the extent that those who received dollars in payment for exports refrained from consuming and instead made loans, but they did not represent such genuine capital when these loans were made

through the creation of additional credits in dollars in this singular market.

I do not mean to say by this that the Eurocurrency market has not been very useful to the extent that it has enabled certain countries to cover their purchases of petroleum with such credits without sacrificing other imports, at a time when they were not able to increase their exports. It is necessary to draw a distinction, however, between this situation and the easy and plentiful credit to which many countries resorted (especially in the case of Latin America) because of the extreme liberality of the banks operating in this market.

Looking back at events from a distance, it might have been assumed that the IMF and the World Bank would have played a very active role, especially in order to ensure that the financial surpluses from oil were used for genuine capital loans, avoiding the inflationary expansion of credit like that which occurred in the Eurodollar market.

The Fund could have contained these lamentable excesses by promoting the judicious use of the resources available on reasonable terms. This was to some extent prevented, however, by the conditions which this institution has set itself: conditions which —as far as I can remember— were never discussed with the developing countries. It is hardly surprising, then, that the countries wishing to obtain these resources saw an opportunity to get around these conditions by making use of the loans provided so liberally by the international private banking system. The latter, for its part, seems to have been guided by the incentive of making juicy profits rather than by the necessary sense of prudence and foresight.

In the light of past experience, the spreading concern about the reform of the international monetary system is perfectly understandable: I think such reform has to come and that the developing countries should be preparing themselves for taking part in its formulation.

The starting point should be the creation of a true international currency instead of the dollar. The Bretton Woods agreements gave the United States the privilege of providing currency for international transactions: that is to say, the privilege of seigniorage and also the responsibility for it. In the creation of an interna-

tional currency the responsibility should be collective and not given to a single country or a very small group of countries of great influence: it should be extended to all, so that it would thus cease to be a privilege.

Of course there are considerable obstacles to this, not only as regards the substitution of the dollar, for obvious reasons, but also because the proper functioning of a new system would demand the solution of the problem of the huge mass of dollars floating in the Eurodollar market. This would be a very difficult operation, not only because of what it signifies in itself, but also because these dollars represent a large debt on the part of the United States, on which that country does not pay interest.

Beyond all this, there is another consideration of fundamental importance. Could a new system function properly while the countries in the world which will carry most weight in its operation are unable to correct their own inflationary processes? Rising prices will call for the continual expansion of the international money supply, and these countries could agree among themselves to do so, even though this would heighten international inflation. In contrast

with what happened in a system based on the gold standard, where the loss of monetary resources tended to limit domestic monetary expansion, the deliberate creation of international currency would instead be the obvious 'solution' for bringing relief at the international level to important countries which had not been able to contain their domestic inflation.

It may be concluded from this that a good international monetary system could hardly function properly if these countries failed to tackle to the full their problems of structural inflation. If this were not done, then instead of the creation of dollars by the United States we would have the creation of international currency through the influence of countries interested in dealing with the external effects of their own inflation which they had not been able to contain.

A good international monetary system must be based on the transformation of the domestic process of appropriation, accumulation of reproductive capital and redistribution of income: consequently, a great deal must be done and renewed before this goal is reached.¹

II

The structural imbalance between the periphery and the centres

1. *The centres and the periphery*

The centres have always stubbornly refused to recognize their great structural differences from the periphery, which stem from the considerable lag in the latter's development. This lag is itself the consequence of the inherent dynamics of advanced capitalism: a centripetal type of dynamics which has always characterized the latter's development in the past and has not spread spontaneously to the rest of the world. The fruits of the increase in productivity due to their enormous technological progress have remained in the centres and have not spread further through the reduction of prices: a situation which has given great impetus to the ac-

¹These comments recall to me a significant episode which occurred in the early days of UNCTAD. A committee of independent experts recommended that a link should be established between the creation of Special Drawing Rights and the provision of financial co-operation to the developing countries. It was claimed at that time—in opposition to this idea—that the pressure of the latter countries would involve the risk of provoking international inflation. Finally, the link was not approved, but even so there was inflationary expansion of the dollar at the international level.

In this way, a very important opportunity to co-operate in the development of the periphery, subject to all the safeguards that seemed necessary, was thrown away. This shows once again that generally speaking the centres are not interested in the development of the periphery except to the extent that this serves their own interests.

cumulation of reproductive capital and the unceasing innovations of the centre. For better or for worse, this is how the capitalism of the centres has developed, with the periphery playing only the role of an appendix. This explains the historical lag in the latter's development and its great structural differences with the centres, which are manifested in three main points worth mentioning briefly here: the structural disparities in demand; the economic and technological inferiority of the periphery, which makes protection necessary; and the characteristic division of the periphery into relatively small units, which calls for integration measures.

2. *Structural disparities in demand*

With regard to the first point, in order for a country on the periphery to develop it is essential for it to change its structure of production in order to cope with the correlative changes in demand.

These changes can be oriented mainly towards the interior or towards the outside world, and the attitude of the centres has a dominant influence in this. There can be inward-oriented changes involving import substitution, or outward-oriented changes involving the export of manufactures. The latter option has become increasingly necessary because of the relative slowness with which exports of primary commodities generally tend to grow.

The increasing obstacles standing in the way of import substitution beyond certain limits are well known. The limits in question depend on the availability of natural resources and on technological considerations, thus making it necessary to combine import substitution with the export of manufactures.

To what extent can manufactures be exported? Over and above the question of the effort that a peripheral country is willing to make in this direction, this extent depends fundamentally on the receptiveness of the centres, which is influenced in turn by their rate of development and the intensity of their restrictions on imports from the periphery. As a general rule, it could be said that the greater the receptiveness of the centres in the light of these two

elements, the less need there will be to substitute imports on the periphery.

This, however, covers only one aspect of the matter; the other aspect concerns the changes in the composition of demand, which, as noted earlier, go hand in hand with development. In view of the well-known disparities in the income-elasticity of the demand for imports, the demand for the latter, which come primarily from the centres, will tend to grow more quickly than the demand for the exports of the periphery. Such is the effect of the technological innovations of the centres, which increasingly diversify goods and services, in contrast with the technological lag of the periphery. In order for the development of the latter to progress, it is essential that it should develop its exports of manufactures in order thus to correct the tendency towards an external structural imbalance caused by this disparity in elasticities. If it does not manage to do this, it will be forced to engage in import substitution, in view of the rate of development which is proposed to achieve.

3. *Import substitution and protection*

Now, import substitution calls for a certain amount of rational and moderate protection. And this is where we encounter a severe obstacle in the form of reciprocity, which is now being put forward once again as a condition for the centres to lower their levels of protection. It is worth going more deeply into this matter.

There is a fundamental difference which should not be overlooked: protection on the periphery is aimed at eliminating the tendency towards structural imbalance, whereas the protection of the centres tends to aggravate this tendency, to the detriment of peripheral development.

We have set forth our reasoning on this matter many times, but apparently we have not been persuasive enough. Reciprocity has been the most important reason why attempts have been made and continue to be made to extend the scope of GATT to the peripheral countries, so that they can participate in the negotiations based on this concept. It is not recognized that there is in fact already implicit reciprocity, since the more the developing countries export to the

centres, the more they will be able to import from the latter.

There is also another consideration which is often forgotten. No rational projection puts imports below the amount that is exported to the centres, taking account of financial remittances and other payments abroad: all that is changed is their composition. The difference is that through protection it is aimed to bring about a deliberate change in the composition of imports in order to promote change in the structure of production in line with the requirements of development. In the absence of such a policy, the composition of imports is determined by the international market forces and the transnational corporations which predominate in them, so that the structure of production is determined from the exterior, and this means that a country cannot develop faster than is permitted by the growth of its exports: that is to say, by the receptiveness of the centres.

Is protection really necessary in order to achieve these changes in the structure of production, however? The original concepts under which GATT was set up, based on the old fashioned scheme of the international division of labour, did not accept this, nor do the economists who still continue to preach the virtues of the free play of the market forces for the periphery. It is true that these economists recommend devaluation of the currency to carry out these changes without breaking these laws, but in order to simplify the argument, let us pass over the fact that devaluation is also a kind of intervention. We are not talking, of course, about devaluation to bring the external value of a currency in line with domestic inflation which is fully justified, but are referring to it as an economic policy expedient.

Applied with this criterion, devaluation has the virtue of making imports more expensive and thus promoting their substitution, and also stimulating the growth of exports through a reduction in their prices. It does this, of course, for the exports which require this stimulus, but it also affects the exports which were already competitive at the international level: that is to say, from their point of view, this type of change in the structure of production brings about a deterioration in the terms of trade when the growth of exports goes beyond certain limits: in

other words, it would be counterproductive from the point of view of development. It is true that a tax on exports is also advocated in order to avoid this, but would not this represent interference by the State with the market laws?

Furthermore, devaluation means altering all prices and costs in order to achieve effects on only a relatively small part of the global product of the economy. This is not all, however. It is well known that when the labour force has sufficient power to gain compensation for price rises it will demand a rise in wages, which will eventually wipe out the effects of the devaluation. Consequently, while protection and the corresponding subsidies seem to us to be inevitable, they must be rational and not arbitrary or excessive, as often happens.

In order to oppose the idea of protection, the old argument continues to be put forward that it is necessary to pay more for import substitution products than imports would cost. This reasoning fails to take account of two points of decisive importance, however.

First of all, there is the low income-elasticity of exports. If their volume is increased, their prices will go down, and after a certain point the periphery would suffer the phenomenon of a deterioration in the terms of trade, thus suffering heavier losses than the higher cost involved in the protection of import substitution activities.

Secondly, these activities make it possible, within certain limits, to achieve a higher growth rate of the global product which more than outweighs the higher cost involved. Protection is thus an economically sound solution, provided it is applied in a rational manner, as it is always necessary to insist.

Of course it is quite true that protection on the part of the periphery has infringed from the very beginning the free play of the international market forces on which the original concept of GATT was based.

4. *Protection in the centres*

All the foregoing concerns the periphery, but it would seem that the most difficult problems lie with the centres. It is hardly surprising that these should resort to restrictions outside the ambit of GATT when they are suffering from

serious unemployment. As already noted, however, they were very reluctant to liberalize their trade even during the years of prolonged prosperity and even in the case of countries suffering from a shortage of labour which threw wide their doors to immigrants. Nothing seems to indicate as yet that in the future, even when the current difficulties are overcome, the centres will be willing to make any really significant changes in their attitude. I think that this is a fundamental problem whose true significance has not been made fully clear. Yet it is essential that this should be done if we are to find solutions capable of reconciling the interests of the centres and the periphery in increasing growth. It is therefore worth going into more detail on this subject.

As already noted, in the past development of the centres the fabulous increase in productivity has not been reflected in a steady decline in prices, but has been retained internally. This is a structural phenomenon which has constituted a very important factor in the accumulation of capital and in the technological innovations made. The periphery has only participated to a marginal extent in this process, except insofar as it produced raw materials which the centres needed. It is doubtful whether capitalism would have been able to develop so vigorously if it had not been for this form of retention of the fruits of technical progress, especially in the upper strata.

The industrialization of the periphery was not a spontaneous consequence of this capitalist expansion, for the centres were only interested in investing in the periphery in order to obtain from it the primary commodities they needed: they had no intention of establishing industries there which could export anything other than primary products. For a number of reasons, they preferred to carry on industrial production in their own part of the world, and consequently the industrialization of the periphery was the result of its own decision in response to the severe crises in the centres already referred to: two great World Wars and a Great Depression between them.

Be that as it may, the periphery, which had first been forced to industrialize through import substitution because of these critical conditions in the centres, gradually learnt afterwards to ex-

port manufactures, thanks to the prosperity reigning in the centres, and through the use of deliberate promotional measures. If this prosperity were to return in a few years, although not necessarily at the same level as before, the question would arise of whether the centres would be willing to follow a liberalization policy such as they have put into effect among themselves. Let us examine this very important aspect for a moment.

Up to now, the exports of manufactures of the periphery have been carried out by a few countries only and have accounted for a relatively small part of its potential. Would the centres be willing to liberalize their imports if this export effort reached large dimensions?

Let us reflect on the following fact. If success was achieved in the export of manufactures, this was because the exporting countries were capable of adopting similar techniques to those of the centres (although corresponding to less advanced phases of the latter's development), to produce goods for which the demand tends to grow less rapidly than the demand for the increasingly technologically advanced goods coming from the innovations made in the centres.

It is hardly surprising, that the possibility of access to less advanced technologies and the lower level of wages have enabled the exporting countries to compete successfully with similar goods produced in the centres.

This fact could signify the beginning of a process of reversal of what has been occurring in the past in the development of the centres. It should be recalled that the fruits of technical progress have not been reflected in a corresponding reduction in prices, and that generally speaking the ability of the centres to open up external markets has not been due so much, to lower prices as to the unceasing diversification of goods deriving from their technological innovations. It would appear, however, that this is not the way in which the exports of the periphery have been competing in the centres: instead, they have been exploiting their lower prices.

Although this reaction of the periphery to this historical process has still not reached sufficient amplitude, in view of the growing export possibilities it is necessary to think seriously

about the possible consequences of the accentuation of this phenomenon which has now begun. What will the centres do in the face of this process? Will they continue to maintain and increase their restrictions, as they have been doing so far outside GATT? Or will they resort to the use of devaluation as an instrument, as the periphery has been recommended to do so many times?

As well as containing imports, devaluation would reduce the external prices of exports even when these were already fully competitive. The reason we mention this is not because we believe that it is likely to occur, but merely in order to emphasize the difficult choice which the centres have to face. On the one hand, they would continue to violate the principles of GATT which they have defended so much, while on the other they would have to resign themselves to losing, through the lower prices of their exports, part of the fruits of their technical progress, with all the great disturbances that that would imply.

5. *The international division of labour*

In the meantime, a comment is called for which is not without importance. The centres have always proclaimed to the periphery the advantages of the international division of labour within the system of market laws. This attitude was completely in line with their interests, although it prejudiced the development of the periphery, but now that the periphery has begun to export, the centres are departing from those principles on which the existence of GATT is based.

To tell the truth, those principles, although they continue to be of great validity in the centres, in spite of the conjunctural phenomena mentioned elsewhere, have not been in keeping with the requirements of peripheral development in the past, and at present they actually militate against such development because they outlaw protection.

On the other hand, it cannot be denied that the centres would be exposed to growing upheavals if, in this new stage of industrialization of the periphery, those principles continued to be fully valid. Let us recall the nature of the accumulation process, whose source lies

in the increase in productivity which is not passed on in the form of reduced prices but is reflected in the displacement of demand to increasingly diversified goods and services. Obviously, increased competition from imports through a reduction in their prices, far from generating investment resources in the enterprises, reduces their surplus to the prejudice of accumulation. This competition thus generates unemployment and weakens accumulation. In contrast, when the unemployment is due to increased productivity, this increase produces an accumulation potential which, if utilized, enables the unemployment to be offset.

This is the serious problem which is causing so much concern and which must be faced immediately if we are to find mutually advantageous solutions.

Clearly, it would suit the periphery much better to be able gradually to take advantage of the market of the centres without the need to resort to an exaggerated reduction of prices at the expense of the fruits of their technical progress, which would not suit the centres either. Up to now, without referring to the exports of the latter, we can say that they have tried to defend themselves through arrangements such as the Multifibres Agreement and the so-called voluntary accords in order to limit exports from the periphery. As well as constituting discriminatory actions—since they affect only the periphery and not the centres—these measures are not in line with the contractual system of GATT and are always subject to the threat of further unilateral decisions by the centres. Of course, fundamentally the principles of GATT are not applicable to these new tensions, which call for a new institutional system, as the UNCTAD Secretariat has suggested.

It is necessary, then, to explore other avenues which suit both the interests of the centres and those of the periphery. New ways of recognizing comparative advantages in practice are called for. There can be no doubt that it is in the interests of the periphery to gain access to the markets of the centres for goods which are in line with their technological capacity, so that they can import the other technologically advanced goods produced by the centres, which it would be very costly for them to substitute at the present stage of their technological develop-

ment. This would also mean clear advantages for the centres, because of the ever wider field thus offered for the exploitation of their technological innovations. In other words, it would suit the centres to export goods with a high technological content in exchange for imports of goods with a lower technological content from the periphery, and this would also be advantageous for the latter.

Of course I am not proposing concrete formulas, but simply stressing the need to explore them: what is needed is to reach formulas which gradually and progressively open up the markets of the centres without the risks of unlimited competition.

Clearly, the formulas needed are not static but eminently dynamic. Exports of manufactures by the countries of the periphery, together with import substitution, will enable their industrialization to be made increasingly efficient and, at the same time, promote their technological development. It will therefore be understood that this advance would make it possible to increase the exports of goods which are at present not technologically accessible to the periphery, as has already happened in the case of countries which, although once peripheral, have finally attained technological homogeneity and become integrated into trade with the centres.

The peripheral countries which are advancing in their industrialization are passing through a transitional period which is more or less prolonged, in line with the big differences existing between them. If this process is continued in a decisive manner, there will be a steady expansion in actual fact, and not just in a formal manner, in the scope of the international division of labour within GATT and the mutually advantageous observance of its principles, including eventually that of reciprocity.

The role of the centres will be of considerable importance during this transitional period: up to what point will they be able to open themselves up substantially to the periphery? In the light of what has been said before, there would appear to be serious doubts about this: there is nothing to indicate that, even in the best of cases, the periphery could dispatch to the centres all the exports it would need to make in

order to acquire there the enormous amounts of goods required for its development.

There is no justification for placing exaggerated emphasis on exports to the centres while failing to give sufficient importance to exports of manufactures within the periphery itself. The main obstacle continues to be the economic division of the periphery, which is a clear manifestation of the way in which the centres, through the very dynamics of their own development, have left the periphery on the sidelines of industrialization.

6. *The division of the periphery*

In the past system of the international division of labour, each peripheral country converged separately towards the centres, with very little intra-peripheral mutual trade. Import substitution used protection in a general manner, without establishing preferences among the developing countries, since on top of the violation of conventional principles represented by protection in itself, such preferences would have added something which the centres would have rejected as open discrimination. Thus, import substitution was carried out in watertight compartments and not much progress has been made in the arrangements arrived at over the course of time in order to try to gradually do away with these compartments.

One of the main reasons (although not the only one) why this division has lasted was the illusion, during the long years of prosperity of the centres, that the indefinite expansion of exports of manufactures made it unnecessary to continue with an active import substitution policy combined with mutual exports within the periphery. Furthermore, the centres either actively opposed measures aimed at correcting the division of the periphery or, even in the best of circumstances, were indifferent to them and failed to give them the support which would have been of great significance in this respect. This was yet another of the consequences of the centripetal growth pattern which first of all set aside the periphery from industrialization and subsequently kept it on the sidelines of trade in industrial products.

It is worth repeating once again that this centripetal growth pattern was a primary factor

in the centres' lack of any real interest in the development of the periphery, except inasmuch as it is of importance to their own development. I refer to the development of the periphery in all its social depth, that is to say, the process whereby the advantages of technical progress are spread throughout the structure of society and are not limited to a relatively small part of the labour force.

This assertion may seem surprising in view of the active role which the transnational corporations have played in the industrialization of the periphery in recent decades. At first, the centres opposed this development, but once the process was well under way and appeared to be irreversible, they stimulated the participation of these transnationals, which thus took advantage of import substitution after having previously opposed it. It was claimed that the transnationals would be agents of the internationalization of production, but their most important role has been to internationalize forms of consumption rather than those of production, since they have been an important factor in opening up the markets for the centres. In other words, without ignoring their technological contribution, the transnational corporations have nevertheless

taken advantage of the industrialization of the periphery without making any serious contribution towards offering it international horizons.

Very important changes are taking place in the world economy. Thus, we are at present witnessing, among other events which cause profound concern, the decline of productivity in the centres. The increase in productivity seems to have ceased to be a process which occurs automatically in the capitalist growth pattern. It must now be the result of a deliberate policy, in both the domestic and the international fields. It is therefore to be expected that new criteria should now be adopted in tackling the problem of relations with the periphery, including the question of comparative trade advantages. This problem must be approached, however, not in the previous ways, but in response to a situation which is very different from that which existed when the periphery began its industrialization. There is now no longer any doubt about its increasing capacity to achieve this, and it must therefore be allowed to participate in the sustained and growing process of comparative advantages, where it could make a notable contribution to increased productivity in the world economy.

III

The conjunctural effects of the crisis on the peripheral countries

1. *The recovery of the centres*

The consequences of the recession in the centres—which is tending to become an outright depression—are increasingly serious both in the centres themselves and in the rest of the world. We have already referred to the negative effects of monetary policy, which is largely responsible for this recession. The truth is, however, that inflation had been developing for some time past, and the rise in oil prices helped to intensify it. This is the structural phenomenon which it was attempted to tackle with this

policy. But how are we to set about the recovery of economic activity now?

The pressing need for recovery is acknowledged in all circles, and perhaps the most important factor which is holding up the essential expansion of credit is the fear of a new wave of inflation. This fear, in view of the vicissitudes which have taken place in recent times, is indeed not without foundation.

The fact is that some increase in prices would appear to be inevitable, in spite of the idle capacity of the economies. Indeed, it is necessary to increase the amount of profits in order

for enterprises to have the incentive and resources to increase their capital investment.

Herein lies the risk of a new inflationary spiral, and the possibility of avoiding this risk depends fundamentally on the ability to moderate the pressure of wages, especially when they have suffered some deterioration. There can be no doubt that if this pressure exceeds certain limits, the resulting rise in costs would lead to a rise in prices, and this in turn would bring about new demands for wage increases.

The danger does not lie only in this, however. The recession has brought about or aggravated a fiscal deficit, and the reluctance to take corrective measures which would intensify the recession is therefore understandable. If these measures are not taken, however, in proportion as the economy recovers there would at the same time be serious inflationary effects.

On the other hand, simply leaving the situation unchanged without taking any recovery measures is an attitude which is not acceptable from any point of view either. We are therefore faced with an unavoidable dilemma. Today, as in other eras, the consequences of a restrictive monetary policy fall on the labour force. From the point of view of recovery, it is no longer possible to recreate the times when the growth in accumulation was achieved largely at the expense of the labour force. What can we do, then, to reconcile this need for accumulation with the very understandable aspirations of the labour force to share in the fruits of the recovery?

Everything indicates that it will be impossible to avoid a new surge of inflation unless we face up to three requirements: the need for equity in distribution, the need for accumulation, and the need to correct the fiscal deficit as the recovery progresses.

This is not the place, of course, to go more deeply into these aspects regarding the centres. It is necessary, however, to emphasize their structural nature. We must not forget the vulnerability of the process of accumulation of reproductive capital as the struggle to share in the benefits progresses. We have not yet made sufficient progress in the interpretation of these phenomena, without which we cannot hope to change this process. This does not mean, how-

ever, that we cannot take a few initial steps in the light of a more integrated concept of incomes policy.

2. *The recovery of the periphery and the external imbalance*

Let us now go on to examine the case of the peripheral countries in very general terms. These countries have to face up to the consequences of the slow growth of the centres in the present decade and their protectionist practices, the consequences of these factors being aggravated by the deterioration in the terms of trade.

What does this deterioration signify? Quite simply, the answer is that the periphery is having to bear a substantial part of the heavy burden of the economic and social cost of the recession. This is recognized in a recent report by the Organization for Economic Co-operation and Development (OECD) in which it is stated that one third or more of the cost of bringing down inflation in the centres has fallen on commodity prices.²

These and other adverse consequences make it clear that the peripheral countries cannot simply remain inactive, waiting for the centres to recover: they must set about organizing their own recovery policy, and this task will be all the more difficult the longer it is delayed.

Despite the big differences between the countries of the periphery and their different levels of development, they have common problems of prime importance, without overlooking the special case of the oil-exporting countries. They suffer, above all, from an external imbalance. How is this problem to be tackled? In order to eliminate the imbalance it is essential to reduce imports and other external payments as long as the adverse external circumstances make it impossible to secure any substantial increase in exports or to procure a net contribution of financial resources from the exterior. There are

² "... a third or more of the decline in the inflation may be attributed to the weakness of primary product prices, which could be expected to recover in the event of a pick-up of activity", *OECD Economic Outlook* No. 32, Paris, 17 December 1982.

two ways of compressing imports, however: by bringing about a contraction in domestic activity until equilibrium is achieved, or by putting into practice a selective policy. The first of these approaches is in line with the conventional recommendation against any intervention of the State in order to regulate imports, but the economic and social cost of such a so-called 'spontaneous readjustment of the economy in line with the market laws' can be enormous. In spite of the fact that recommendations of this nature often come from the loftiest spheres, even in the times we are living in, it is simply not acceptable to follow this path towards the restoration of external equilibrium. It is therefore important to adopt a selective policy, and there is no reason to have any doctrinaire scruples in this respect when these stem from a mistaken and negative concept.

A selective import policy of a rational nature should aim to reduce or eliminate non-essential or unnecessary imports in order to use the countries' external payments capacity for those imports which are associated with economic activity and the well-being of the population. As the immediate objective of restoring equilibrium is achieved, there promptly arises another: to avoid a new imbalance brought about by the recovery policy itself.

This policy must be based on the cautious expansion of credit to stimulate demand and the utilization of the idle capacity of the economy. It may be noted in passing that the very high interest rates currently prevailing are a severe obstacle to the achievement of this objective. It is quite true that although a sharp reduction in them is advisable, this will stimulate the outflow of funds to the exterior, and this in turn could make it necessary to impose control measures which would also have to cover remittances of profits. At all events, moreover, no matter how prudent the reactivation policy is, it will bring with it an increased demand for imports beyond the countries' external payments capacity. The selective policy must therefore be applied with sufficient vigour to prevent new imbalances. This will by no means be an easy matter, especially in those countries —of which there are many— where margin for reducing imports has already been reduced to a relatively narrow one.

3. *Selectivity of imports and mutual trade*

This aspect constitutes one of the most significant differences compared with the Great Depression of the 1930s. Then, as now, it was necessary to adjust imports to the countries' external payments capacity. Unfortunately, at that time the restrictive measures were applied not only to the imports from the centres, where the main source of the imbalance lay, but also to the relatively small imports from other developing countries. In this way, the pressure of circumstances caused the possibility of promoting mutual trade, especially at the regional level, to be thrown away.

Nowadays, the situation is different, because this mutual trade has already developed and has great growth potential: it would therefore be extremely regrettable if the selective policy were to go astray once again. It will be no easy matter to avoid this, especially when the size of the imbalance is very substantial and there are also domestic considerations which might lead to such deviations from the right path. The need to promote the utilization of idle capacity and to increase employment, for example, could lead to a decision to do without imports from other peripheral countries, thus sacrificing the possibility of making exports in return.

Unfortunately, we find ourselves once again without suitable machinery for balancing trade at the regional level (or subregional, as appropriate) or beyond these levels. Little has been done in this respect, and we must therefore tackle new initiatives aimed at securing multilateral trade compensation.

This is not just a question of compensation machinery, but also of recognizing certain requirements for reciprocity, so that the more advanced countries, which take more advantage than the others of the trade in their respective areas, will have the responsibility for making or promoting investments in the weaker parts of the system, in order that the latter may also enjoy the advantages of reciprocity.

The absence or inadequacy of such machinery could lead, in some cases, to bilateral arrangements, as in earlier times. This is of course a very makeshift approach, but it would be preferable to completely sacrificing mutual

trade: it is therefore quite acceptable, provided that the need to eventually arrive at multilateral forms of trade compensation is borne in mind.

It may be recalled that the long years of prosperity of the centres not only discouraged import substitution on the basis of mutual trade, but also the development of machinery for such trade.

In this case, as in others, conjunctural measures must seek to pave the way for longer-term solutions. Thus, once the external imbalances of a conjunctural nature have been overcome, greater prominence will be assumed by the factors of structural imbalance to which so much significance has been attached in this study. The problem is how to overcome the structural tendency towards an external bottleneck. In view of the very slow rate of development of the centres and their protectionist practices, it will be essential, especially at the regional level, to tackle the substitution of imports of capital goods, intermediate goods and consumer durables originating from the technological innovations of the centres.

The structural nature of this substitution should not make us lose sight of certain immediate possibilities for contributing to the correction of the conjunctural imbalance by importing some of these goods from other countries of the periphery. As usually happens, some immediate drawbacks will be encountered in this. A country which imports essential goods from other developing countries instead of doing so from the centres will frequently have to pay higher prices, and as long as there is no reciprocity in the form of the export of other goods this will represent a drawback which could discourage similar operations. A country interested in making such exports within the periphery, however, could consider granting subsidies to bring their prices into line with those prevailing at the world level. This is a suggestion which is worth examining with a view to the development of mutual trade. Of course the centres will continue to oppose export subsidies, but I do not believe that this should induce the countries of the periphery to refrain from using this means of promotion, provided it is applied in line with suitable rules.

This remark applies equally, and perhaps even more so, to policies aimed at the substitu-

tion of essential goods, towards which development policy should necessarily strive. This is not a question of conjunctural emergency measures, but of structural adjustments. In proportion as vigorous efforts are made to increase exports of manufactures, as well as those of primary commodities, it will be necessary to initiate without delay investment plans for these products. It is essential to do this in order to gradually overcome the serious limitations imposed on development by the slow growth of the centres and their protectionist practices.

The reasons in favour of a policy of compensation or integration in the production of essential goods are well known. Instead of general formulas of scanty effectiveness, it is necessary to arrive at agreements between two or more countries for joint production and the promotion of mutual trade. These individual arrangements should of course be made within a general framework of incentives covering subsidies, preferential duties and financing, in line with the real requirements. It is also necessary to consider the desirability of multilateral compensation machinery, which, in this case, would have to be in keeping with structural requirements.

As regards financing, financial co-operation from abroad will be essential, especially while the developing countries are trying to correct the external imbalance and are still suffering from the limitations of domestic resources. The World Bank, and also the IMF, have finally recognized the need to participate in operations aimed at correcting external imbalances of a structural nature. Their financing of these operations, together with that provided by other bodies such as the regional banks, could make a very effective contribution to enable the private or public enterprises of our countries to take part in these joint production arrangements. Quite apart from its inherent importance, this financing will help to strengthen the bargaining power of such enterprises when there is a justification for the participation of foreign interests in financing and in providing technology.

It would be highly desirable for the centres to give their clear and explicit support to this policy of joint production and mutual trade among developing countries. Up to now they have been reluctant to do so because they have felt that this would unfavourably affect their ex-

port opportunities, but this is a mistake, because ultimately the intensity of the substitution policy depends on the degree of receptiveness of the centres to exports from the periphery. As already noted elsewhere, the more receptive the centres are, the more limited the scope of the substitution policy will be. If this policy is carried out on a rational basis, it could hardly include among its objectives that of reducing imports below the payments capacity of a country, but will be aimed rather at changing the domestic productive structure in the manner and to the extent needed to achieve a satisfactory rate of development.

In this substitution policy, high priority must be given to the needs for the supply of energy, either through oil production or through the development of other sources, and the stimulation of food production, without which the need to resort to imports from certain central countries would eventually assume unmanageable proportions.

So far, we have placed emphasis on substitution policy with respect to the centres, and this is indeed of prime importance. This in no way signifies, however, that other forms of integrated substitution should be overlooked. It must be acknowledged that in this respect the actual facts have lagged behind aspirations. In brief: although the substitution on a combined basis of certain basic goods is absolutely essential in view of the tendency towards imbalance with the centres, the substitution of other goods, although not so vital, is nevertheless extremely desirable from the point of view of the international division of labour. The experience accumulated so far gives grounds for both positive and negative conclusions which must be borne in mind when designing new policies in this respect. At all events, however, a rational order of priorities must be established.

4. *Recovery and inflation*

Let us now consider the possible inflationary consequences of a recovery policy. Here, observations similar to those made in the case of the centres are called for. After a short while, a structural imbalance will arise between the growth rate of consumption and the need to increase the accumulation of reproductive capital

in proportion as the idle capacity of the economy begins to be used up.

When discussing consumption, it is necessary to exercise caution regarding certain conclusions on the significance of the concept of austerity. Austerity to combat inflation may be economically and socially unacceptable. On the other hand, it is an essential element for containing inflationary tendencies in a recovery policy. It is not a question of restricting the total amount of consumption: on the contrary, an increase in consumption is indispensable for recovery. What is really called for is to change the social composition of consumption in the light of considerations of equity. While it is true that the rate of consumption of certain social groups must be limited in order to raise the rate of accumulation of reproductive capital, it is equally true that the greater accumulation will promote increased employment and hence increased consumption on the part of the social groups which are favoured in this way.

The increase in consumption by the labour force will have positive effects on recovery, above all when wages have suffered serious deterioration. Past experience must always be borne in mind, however. In general terms, it is not possible to improve the standard of living through wage rises, which, by raising the cost of production, inevitably result in a rise in prices followed by new wage rises, thus bringing about an inflationary spiral. Expansion will naturally bring about some rise in prices, and if wages are then increased, the spiral will become uncontrollable. We must therefore frankly ask ourselves a question which is usually left out of the reckoning. A rise in prices is essential in order to increase the profits of enterprises and hence their capacity for accumulation. The assertion of this need, however, does not mean that we should necessarily recognize the need to contain wage rises, either through a social compact or by authoritarian measures: this would mean making the social cost of the economic reactivation fall on the shoulders of the labour force. Consequently, both equity in distribution and the need to avoid the inflationary spiral make it desirable to find suitable ways of allowing the labour force to share in the fruits of the recovery in proportion as the financial gains of the enterprises increase, after taking account of the

accumulation requirements. We may also conceive the possibility of the labour force participating in the process of accumulation. This is not the place to go into details of the necessary machinery for this, but merely to stress this aspect of great importance. It could really be the forerunner of a policy of macroeconomic regulation of the rate of consumption and the rate of accumulation. In other words, we see once again that conjunctural measures should never lose sight of long-term considerations but should link up with them in advance without going against their significance.

5. *Financial adjustments*

In some countries of the periphery, and especially those of Latin America, the burden of external indebtedness has seriously aggravated the external imbalance. The action taken by the IMF is holding off a dangerous stampede that would adversely affect the interests of all, but the emergency arrangements arrived at are far from having solved the fundamental problem. It is necessary to speak out very clearly in this respect. It is inconceivable that the debtor countries should continue contracting more and more debts indefinitely in order to face up to the payments of interest, nor should they have to resort to extreme compression of their essential imports for the same purpose, to the serious prejudice of their domestic activity and their precarious employment situation.

It would therefore appear to be a matter of elementary prudence and foresight to arrive at credit arrangements for suitably extending the payment of debt service and reduce interest rates, which continue to be high in spite of their recent reduction, although it is doubtful whether this can be maintained if there is a new bout of inflation in the centres.

At the same time, it is worth recalling the opportunities which now exist for the creation of Special Drawing Rights. The present tightness of international liquidity seems to clearly point to the need for such monetary relief. This would be the right moment to insist on a link between this and development finance. The dimensions of this operation must be determined, however, in line with the demands of world

trade and not those of financing, since the latter would only be a by-product of the former.

In addition to the above-mentioned adjustment operations, a net increase is needed in the transfer of financial resources from the exterior, especially until such time as the centres once again attain a satisfactory growth rate, although this is unlikely to be as high as that achieved in their time of prosperity. Be that as it may, the reproductive investment of such resources would help the recovery of the centres too. Difficult though it may be in the present circumstances to comply with the recommendations made in this respect in the United Nations, it is reasonable to expect that at least a plan for the gradual attainment of this objective in the next years could be arrived at.

As regards resources of a conjunctural nature, it would appear that some degree of consensus has been arrived at regarding the expansion of the IMF quotas and also the transfer of resources from other sources, especially the big central banks.

This would also be the right moment to change the conditions imposed by the IMF in the light of experience, with the technical collaboration of suitable experts from the developing countries.

6. *The Sixth Session of UNCTAD*

While progress is made in the consideration of the international monetary reform, in which the periphery should play an active role, the Sixth Session of UNCTAD (June 1983) offers a favourable opportunity for considering the recovery policy advocated in the present article. There is a good deal of pessimism about the possibility of progressing in the consideration of the New International Economic Order, but such pessimism should not hold up the debates. On the contrary, this recession (or depression) which affects both the centres and the peripheral and socialist countries should be a suitable setting for considering the urgent and pressing problem of world recovery.

It is necessary to assert with the greatest vigour and confidence the genuine possibilities which exist for initiating and promoting this process for the benefit of all. There is no doubt at all that the foundations for this are already in

being, but the stubborn persistence in sticking to conventional ideas and forms of action is smothering these possibilities. Ideas in this field have lagged behind the enormous scientific progress made in other disciplines: it is therefore necessary to make innovations also in economic matters too, since the present forms of action prejudice the entire world economy. Much of what was achieved after the Second World War is now crumbling.

The time has come to launch new ideas and put forward new forms of action in line with the extraordinary consensus of interests demanding a recovery policy which must be begun without further anxiety-fraught delay. Our countries, together with the rest of the periphery, must make their voice heard: a voice which is increasingly powerful in the centres themselves.

Only the recovery of the developed countries will make it possible to overcome protectionism and the imminent risk that they too will become economically divided, with corresponding aggravation of the conflicts. Such a recovery will also reduce the great obstacles impeding the recovery policies of the periphery, which has been so seriously affected by the protectionism

of the centres. As the recovery of the latter progresses, it will be possible to avoid new measures standing in the way of imports from the periphery and to set off along the road towards structural liberalization measures. Progress in the recovery of the centres will also relieve the deterioration in the terms of trade of the peripheral countries. At the same time, financial co-operation will acquire great significance for both sides, since the greater external payments capacity of our countries and of the rest of the developing countries will make it possible to satisfy the huge import needs inherent in the recovery of the periphery (and its subsequent development), and this could make a notable contribution to the recovery of the centres themselves.

All in all, it is evident that there is a clear network of mutual interests which should be emphasized at the Sixth Session of UNCTAD. As a result, it would be possible to arrive eventually at consideration of the new world economic order, which by its very nature presupposes great structural changes. Nevertheless, conjunctural matters deserve high priority and should be dealt with first so as to open the way to large-scale structural measures.

IV

The market laws and ideologies

1. *The ideological crisis*

The impressive progress of technology has been accompanied by great changes in the structure of society and the power relations which take place within it. New and difficult problems have arisen, and the situation today is very different from that of yesterday, but there is something which has remained unchanged in all this: the ideologies followed and the forms of action deriving from them. They were effective in other phases of the development of society, when they were in keeping with the interests and aspirations of the dominant social groups in both the centres and the countries of the periphery. Now, however, as well as having become ineffec-

tive to deal with the new problems, they have actually become a negative factor because of the great damage which their application causes.

Not only have there been changes in the internal power relations, but also in the world structure, where moreover different ideas and forms of action from those prevailing in the past are gaining ground.

There is thus an ideological crisis which is further perturbing the crisis in real activities. As we said earlier in this article, we do not believe that we are witnessing the decline of capitalism, but this will become inevitable if we do not soon achieve a thoroughgoing renewal of conventional ways of thinking and also ways of acting in response to events, with a view to encompassing

certain rational objectives motivated by an ethical sense which cannot be absent from these new ways of thinking.

2. *The market and its structures*

In recent years there has once again been a tendency to proclaim the great virtues of the market laws, the 'magic of the market'. In the theories on which this concept is based there was indeed an underlying ethic, since it was held that if these laws were allowed to operate in an unrestricted manner, the system would tend towards a state of equilibrium in which income distribution was equitable and there were neither centres nor periphery. One must not deny the importance of the play of the market laws, but no matter how effective they may be economically, they lack social and ecological effectiveness.

Let us repeat once again: in reality, it is not just a question of the market, but of the structures which lie behind it and the great differences of power which stem from them. These considerations must no longer be left out of the reckoning if it is desired to understand the problems now facing us and clear the way towards solving them.

I fully acknowledge the great value of individual enterprise and the profit motive in economic activity, as well as in the promotion of technological innovations, but these are not enough to ensure the effectiveness of the market laws. This is a matter of great importance, and if we do not clarify it we cannot correctly interpret the present crisis of capitalism in the centres and the peripheral countries, as well as in the relations between them.

Some final reflections are therefore called for in the light of what was said earlier in this article. In order to avoid errors of interpretation, I wish to reaffirm that I assign great importance to the market not only in the economic but also in the political sphere. What is the reason, then, for the great faults in its operation?

3. *The market laws and distribution*

In my view, the main origin of these faults lies in the appropriation of the fruits of technical progress. According to theories which continue

to form the background for conventional thinking, the tendency is for the enterprises, guided by the profit motive, to distribute these fruits socially through the play of competition, either through the reduction of prices or through increased wages.

Well, I maintain that this is not so, because these fruits are largely retained by the upper strata by virtue of their economic, technological and political power. Within the growth pattern of the system, this is necessary in order for the accumulation of capital to increase, and this corresponds to a certain stage in the evolution of capitalism, since the changes in the structure of society open the way to the possibility of sharing in these fruits by the labour force and the State. This possibility runs counter to the power of appropriation, and as time goes on, it leads the system to an inflationary crisis. The accumulation process thus becomes increasingly vulnerable. According to conventional theory, this crisis is a consequence of the violation of the market laws by this power of sharing, but they conveniently forget, of course, the power of appropriation.

The system can operate quite smoothly as long as this power of appropriation prevails unchallenged, that is to say, when the power of sharing does not exist or is very weak. When the latter power develops and gains force, however, a crisis arises because of the structural imbalance between the rate of consumption and the rate of reproductive accumulation of the surplus, due to the inherent logic of the system.

There is an obvious contradiction in all this, for while the power of sharing is rejected on the grounds that it violates the market laws, no criticism is levelled at the original violation of these laws represented by the power of appropriation.

4. *The equivocality of technology*

In the free play of the market laws, the profit motive has stimulated technological research and its application to production, as is perfectly fit and proper. At the same time, however, because of the equivocality of technology, this same incentive has brought with it the irresponsible exploitation of non-renewable natural resources. Thus, oil prices went down while at the same time there was a spurious increase in pro-

ductivity. Such was the power of the dominant groups in the centres and the projection of their domination at the international level that this situation continued until, at a suitable historical moment, their power was offset by that of the producer countries and there was a rise in the price of this non-renewable resource with the consequent aggravation of inflation.

But this was not all. The decline in prices brought about by the play of the market forces (not without some manipulation on the part of the transnational corporations) brought with it very important consequences as regards technological research, which paid little attention to other sources of energy or to the use of renewable natural resources. Furthermore, this situation led technological research towards the abuse of energy through the exaggerated diversification of goods and services.

5. *The structural imbalance with the centres*

This imbalance is also observed in the relations of the periphery with the centres. Here again it is a question of power relations. In the past development of capitalism, the fruits of technical progress were concentrated and multiplied in the centres and the periphery was left on the sidelines of industrialization in the international play of the market laws. It was when the periphery began to industrialize that the tendency to the structural imbalance arose. The periphery tried to correct this first of all through import substitution and afterwards through the export of manufactures on the basis of the economic and technological power which it was acquiring. Weak though this power was, it began to have adverse effects on employment and to offset the process of accumulation. In other words, the market laws, which in other eras reflected the interests of the centres (in conjunction with the predominant groups of the periphery), are now causing problems for them. Their supremacy in the world, however, has enabled them to take unilateral measures to counteract these laws. As a result, both the centres and the periphery are losing the comparative advantages of trade which the central countries had so insistently proclaimed when the periphery was still excluded from industrialization.

How clearly all this shows the virtues of the market laws as regards the proper allocation of productive resources!

The economic incentive, once it has passed certain limits, has thus caused the deterioration of the environment thanks to the play of the market laws: yet another spurious element in the increase in productivity.

6. *The role of industrialization*

One of the manifestations of the dominant power of the centres over the periphery has been the ideologies imposed. Though they were previously effective in promoting the economic (and also the political) interests of the centres, the market laws at the international level no longer serve their purpose as well as before, and the centres are gradually diverging from them.

These ideologies also give rise to very serious contradictions. While the centres, because of the growth pattern inherent in their capitalist development, retained and continue to retain the fruits of their technical progress, the periphery has been forced, because of its structural lag, to transfer part of its increased productivity to the centres.

This is where the role of industrialization comes in. In spite of its great significance for the promotion of the development of the periphery, recent versions of the ideology of the free play of market forces, in an unexpected turnaround, have again rejected protection and advocate devaluation instead of it. If it follows this path, the periphery will once again be made to transfer to the exterior the fruits of the technical progress already achieved in its competitive exports.

Those in the centres who profess conventional theories and denounce measures aimed at containing the decline in agricultural prices in the European Economic Community and the United States because of increased productivity are taking a perfectly coherent approach. The only trouble is that governments respect but do not follow their urgings!

7. *The indifference of the centres*

The technologies of mass communication and transport also have a profound cultural influ-

ence on the periphery. They shorten distances and internationalize the awareness of development and of cultural identity, but the centres never take any serious and continued action to end the peripheral nature of the periphery with the passage of time. They continue to be indifferent to the final fate of its development. The periphery, for its part, has no power to overcome the indifference of the centres, but it does have power to cause problems. This is a contradiction which can have serious consequences for the centres. The truth is that the latter do not have a long-term perspective of their relations with the periphery.

The centres themselves will increasingly suffer on both the economic and political levels the absence of this long-term perspective. They did once have it when they had to tackle the rehabilitation of Europe after the war. For the periphery, however, they have lacked such a perspective except when it came to advocating birth control, and even then this was not as an element of a great policy of international co-operation, but rather by way of a substitute for this.

During the long years of prosperity of the centres, they did not bother with the periphery either, which was always exposed to the eventual return of obsolete ideologies. Now, however, the crisis of development and change has arrived at the centres themselves, and they too are victims of their own ideologies.

Both the centres and the periphery must learn from the lessons of their own experience. It is possible that this crisis may have the virtue of breaking the outworn moulds within which it was sought to confine a system which must inevitably be changed if it is to recover and increase its powerful growth potential.

8. *Differences and common denominators with the centres*

It is an interesting point that the vulnerability of the process of accumulation of reproductive capital, which is mainly responsible for this crisis of capitalism, is observed both in the centres and in the most advanced countries of the periphery, in spite of their considerable structural disparities. This is because there is a com-

mon denominator between these countries, namely, the tendency towards a structural imbalance between the rates of the different forms of consumption and the rate of accumulation of reproductive capital.

This common denominator conceals some fundamental differences, however. In the centres technological evolution constantly diversifies the consumption of goods and services, under the impulse of the powerful impetus of the system. This is a reflection of technical progress which, on the one hand, increases productivity and, on the other, encourages the use of that productivity for the diversified multiplication of consumption. In the imitative capitalism of the periphery, in contrast, we allow ourselves to be seduced by these forms of consumption without having reached the accumulation capacity needed to solve our grave problems of social inequity.

This propensity to imitate those forms of consumption has always existed. The urge to copy them was especially strong, however, during the long years of prosperity of the centres, when there was an increase not only in private consumption but also in social consumption as an integral part of the sharing process. In addition, of course, there was the imitation—very strong in some cases—of military consumption, which is a serious element in that structural imbalance.

Important countries of the periphery were precursors of the inflationary crisis of capitalism, and now, along with others, they are suffering the consequences of that same crisis of the centres and the extremely grave adverse effects of the policy with which it is sought, especially in the main dynamic centre, to check inflation. The consequences are equally grave for both the centres and the periphery.

Those long years of prosperity dazzled many countries of the latter, and in addition to being seduced by the attractions of consumption, they slackened or completely abandoned their substitution policy, which should have been combined with the export of manufactures and their efforts to promote mutual trade. The whole of the periphery, despite the great differences in its level of development, should pay great attention to this new and promising development horizon.

Countries which have been the birthplace of great technological innovations with enormous potential for increasing human well-being—limited at present to only a small part of the world's population—have not been capable of finding innovations in the theories of development, and hence in its practice too. Perhaps this

is because the prevailing interests promoted such technical innovations but seem to have dampened intellectual creation. It is not too bold, however, to think that the present crisis may encourage the birth of new ideas and also of new men capable of bringing these ideas to reality through political action.

Latin America: crisis, co-operation and development

*Guillermo Maldonado**
Eduardo Gana and
Armando Di Filippo

The present article is structured around several basic ideas. In the first place, attention is drawn to the twofold character of Latin American unity, with reference to the close interdependence between regional 'inward-directed' co-operation policies which foster development and 'outward-directed' concerted measures which reduce the region's external vulnerability. In addition, emphasis is placed on the structural root of that vulnerability, in the economic sphere, associated with Latin America's peripheral position in the international order, and reflected in the gradual dwindling of the share of Latin American exports in world trade. The structural resolution of this problem of peripheral status implies restoring the economic and social development of each and all of the Latin American countries to the central place that is due to it in the action taken by the State, by entrepreneurs and by the other social agents. The world order has entered upon a period of uncertainty which looks likely to be prolonged, and the Latin American countries must find a way to evade the danger of fragmentation and isolation by stepping up their efforts on behalf of regional co-operation and integration. The lethargy into which economic integration programmes have lapsed today is not attributable to 'an instrumental crisis' but, in essence, to the slackening of the drive for industrial development and the recent—but inevitably fleeting—phase of international financial permissiveness, which has sustained the equally fleeting development styles founded on international borrowing. It is also suggested in the introduction to the article that the strengthening of regional co-operation and integration does not imply increasing confrontation with the centres, but represents an additional and autochthonous way of reactivating and dynamizing the world economy, and buttressing a multipolar world, capable of counteracting the risks implicit in the present East-West confrontation, which are a threat to Latin America as well.

*Director, International Trade and Development Division of ECLA. Co-ordinator, Project on Regional Integration and Co-operation. Staff member, International Trade and Development Division.

I

Introduction

When the Executive Secretary of ECLA presented to the social communication media a provisional balance-sheet of the Latin American economy during the year 1982, he stated that in view of the gravity of the negative effects on the region produced by the international crisis, ECLA, in fulfilment of its responsibilities, would immediately embark upon an internal process of collective reflection with the aim of offering its ideas to the Latin American governments, as possible means of constructing a joint response on the part of the region to this dramatic conjuncture. The following pages are the authors' personal contribution to the exercise that ECLA is carrying out. Accordingly, they are open to constructive criticism for their improvement. It is hoped that some of the ideas expressed may give rise to fruitful discussion and that they may be of some use to the governments and to the private, academic and political sectors of the Latin American countries.

There are certain *idées-force* which serve as guidelines for the present study. The first of these is the need to reduce the region's external vulnerability, which has betrayed itself in its full dimensions in the recent international circumstances. Suffice it to refer here to the drastic proportions attained by the problem of external indebtedness in many of the Latin American countries and by the South Atlantic conflict. Both are attended by negative sequels which will hinder the recovery of regional development.

The second of the main ideas underlying the present article is that there is no clear-cut differentiation between regional 'inward-directed' co-operation policies and 'outward-directed' concerted measures, since the two are closely interdependent. Any 'inward-directed' progress—especially in the field of co-operation for development—has its 'outward-directed' projections, inasmuch as it enhances the region's importance in the world assemblage and increases its bargaining power in the sphere of international economic relations.

The third central idea relates to the structural character of this vulnerability. In other words, as long as Latin America's position in the

system of international economic relations is not rectified, there will always be a dangerous gap in its external sector, since world demand for its primary commodities is invariably less dynamic than Latin American demand for the manufactured products which it buys to enable it to keep up adequate levels of economic activity. In present circumstances this state of affairs has been aggravated, inasmuch as it is making itself collectively felt in all the developing countries because of the crisis by which the industrialized countries are affected, and as a result of which their demand for primary commodities has contracted and the protectionist trends that have traditionally hampered regional exports to their markets have been exacerbated.

Consequently, the study draws attention to a fourth *idée-force*: the need to change the nature of Latin America's insertion in the world economy, to which end the economic and social development of each and all of the Latin American countries must be reinstated in the central place it should occupy among the concerns of the States, the private sectors and the other social agents. This implies looking at renegotiation of the debt and external financing in their true perspective: as instruments of the countries' development and not as a set of problems with a life of its own, separate from the rest of the economy.

Furthermore, the study posits the need to reinvigorate regional co-operation and integration, as one of the most fitting means of making a joint response to the international crisis and securing for Latin America a more assured place and stronger voice in the concert of nations. This possibility would be favoured by the renewed importance that economic development—both national and regional—would acquire. The path of integrated economic development may lead to a change in the asymmetrical and vulnerable position of the peripheral region. This trend must be visualized as a long-term incentive to dynamism and structural equilibrium, based on the gradual elimination of the centre-periphery dichotomy, which implies asymmetries in power and distributive inequalities that are clearly untenable from a broader historical viewpoint.

The need to co-operate on the intra-regional level and to join forces for concerted ac-

tion in the international sphere is becoming a matter of urgency for the Latin American countries in the present historical conjuncture. The world order has entered upon a period of uncertainty which is likely to be prolonged. In the monetary and financial area, changes of importance will continue to take place both in the systems providing liquidity to world trade and in the structure of international financing itself. In the field of trade, patterns of 'balanced and managed' trade are being imposed in the industrial centres, in disregard of the norms laid down by GATT and of the claims voiced through UNCTAD by the peripheral countries. Moreover, in the area of production, the recessive anti-inflationary policies applied by the centres depress their levels of activity and employment, thus fostering the growth of protectionism. At a deeper level and in a longer-term perspective, there are signs of unpredictable changes in the technological sphere, which will affect the distribution of world production capacity. The fragmentation and isolation of the Latin American countries do not seem to afford the best means of coping with the vitally important changes whose advent is sooner or later to be expected. Co-operation is the way not only to promote more dynamic and equitable regional development, but also to ensure the increase—or at least to prevent the progressive deterioration—of Latin America's importance in the world order.

The study indicates the close interrelationship between industrialization and economic integration. The loss of dynamism in economic development caused a break, in its turn, in the constant support accorded by the Latin American countries to industrial development, which, to attain full viability, requires the integration of markets and the harmonization of national policies. This accounts for the present lethargic state of the economic integration schemes operating in the area.

On many occasions recourse has been had to the convenient argument that this is an 'instrumental crisis' of schemes that were conceived in international circumstances different from those of today and were endowed with implementation mechanisms which necessarily require bringing up to date. Thus no heed is taken of the reason really underlying the crisis of inte-

gration schemes: the weakening of the countries' economic and social development and consequently of the industrial development process. Of course, postulating so direct a relation between economic integration and industrialization by no means implies that integration can or should disregard other sectors of economic activity. On the contrary, experience points to the necessity of taking action quickly and in depth in the sphere of food and agriculture, for example.

As a corollary to the analysis and to the close interconnection of the guiding ideas behind the present article, the conclusion reached is that regional co-operation and integration, needs strengthening, and that this course should not be viewed by the industrialized countries as a form of confrontation on Latin America's part. Quite the contrary. A Latin America that formed a dynamic and constantly growing political whole would become a positive factor in the reactivation of the international economy, the only way to weather the present crisis. From a different angle, the region's greater capacity

to take joint measures would help to maintain a multipolar world which is a safeguard for the preservation of peace, especially in the context of the present East-West confrontation which now begins to loom threateningly over Latin America.

Inevitably, all this poses the question of how it is to be done. To that universal interrogative no categorical reply has been given, for the simple reason that there is no facile *nostrum* or miraculous panacea. In the present article, however, attention is drawn to possible joint measures in the fields of trade, financing, food and agriculture and energy, because these four are thought to constitute the essence of the region's economic security, indispensable for attenuating its external vulnerability.

In the framework of these reflections, the present article advocates regional co-operation and integration as a fruitful line of action which must be pursued more firmly and in greater depth in order to surmount on structural foundations the Latin American crisis of today.

II

Development and co-operation

1. *The frame of reference*

The economic crisis which in greater or lesser degree is affecting all the countries of Latin America and the Caribbean has had no precedent in depth and far-reaching extent since the time of the Great Depression. Not only the causes that have brought it about, but also policies for overcoming it, have thus become one of the burning questions of today.

Never have conceptual positions as to the economic policies to be pursued in this emergency been so sharply polarized in the region as now, when the singular and paramount point of departure is the immense burden of external debt carried by the great majority of the Latin American countries. This indebtedness and the indubitable responsibility borne by the internal policies applied, especially those with a

monetary bias that have accompanied the main economic decisions in recent times, are leading the national economies of the region into a painful and apparently inevitable process of adjustment, with the all-too-well-known consequences in the shape of a fall in the gross national product, unemployment, reduction of imports, bankruptcy of enterprises, etc.¹

A fuller appreciation of this crisis calls for a recapitulation, however brief, of the historical and structural content of the concept of development, with the object of making it the focal point of the argument.

The aim pursued here is to revert to

¹See ECLA, *Provisional balance-sheet of the Latin American economy during 1982*, E/CEPAL/L.279, 21 December 1982.

analytical viewpoints based on *'idées-force'*, deep-rooted in Latin America's and ECLA's economic and social thinking. Unfortunately, the repercussions of the world crisis on regional development have generated a certain 'immediatist' bedazzlement, which obscures the horizon of options and makes for a dangerous separation of efforts to overcome the serious effects—indebtedness, internal deficits, unemployment, etc.—of the crisis in question. This immediatist outlook also draws sustenance from the recent vigorous upsurge—or rather the fleeting revival—of economic theories based on a quest for ahistorical equilibria and on the study of static comparative advantages, operative in a 'perfectly competitive' world where the asymmetries of power are smoothed out and the significance of the historical and structural background of current processes is attenuated. All this is completely divorced from the concrete praxis of the relationship between Latin America and the centres.

In face of these peculiar circumstances, it is not idly repetitive to recall, at least in outline, the structural foundations of the contemporary economic development process, and the place in it occupied by Latin America. Thus the economic horizon is not reduced to the single theme of the 'adjustment' that is being made through restrictions on expenditure, depression of current levels of economic activity and, in consequence, discouragement of capital accumulation and economic development. The necessity of the 'adjustment' is not disregarded, but an attempt is made to define it in the setting of a long-term historical perspective of development.

Stress should be laid, therefore, on the priority which must be accorded to the matter of development, and which imparts rationale and perspective to the set of partial measures deriving from the present conjuncture. In strictly economic terms, development implies an increase in the productivity of labour and a diversification of overall production capacity stemming from the consolidation and strengthening of manufacturing industry. Underlying this process is the systematic and permanent introduction of technical progress, linked to increasing labour skills and to reproductive capital accumulation.

2. *The peripheral position of Latin America*

It would perhaps be superfluous to dwell very much on the worldwide repercussions of the Industrial Revolution, but a brief general recapitulation may be useful as a frame for the argument put forward here. In the course of the nineteenth century an international economic order gradually took shape, made up, on the one hand, of the central economies—deeply involved with the Industrial Revolution—and, on the other hand, the peripheral economies, which, left on the sidelines of this industrialization process, did no more than purchase manufactures in exchange for their primary commodities.

The central societies succeeded in fully assimilating the fruits of economic development: they enlarged their quotas of non-agricultural product and employment; left behind the stages of downtrodden subjection in their rural and urban class structures; speeded up their urbanization processes, absorbing migrants from rural areas; did away with illiteracy and systematically raised their levels of education; placed scientific progress at the service of economic development; achieved an occupational differentiation which reflected the higher levels of education and the diversification of production; completed the process of demographic transition and stabilization; and, in the international sphere, forged spectacularly far ahead of the peripheral countries in terms of per capita productive capacity and purchasing power.

The process which was born and thrived in Western Europe then spread to North America and subsequently to Japan. The Soviet Union, in its turn, succeeded in joining the group of industrial societies and after the Second World War became the 'centre' of the international economic system of the socialist countries.

There can be no need to repeat that the starting-point for a proper understanding of many of Latin America's current economic difficulties must be its peripheral position in relation to this international economic order: a position that is not called in question by its being classed as a 'middle-income' region, according to quantitative stratifications which must blind no-one to the basic fact of its subordinate insertion in

the world economy. It is precisely this subordination which, together with the colonial heritage of the past, sets its mark on the structuration of Latin American societies.

These latter assimilated in partial and slanted fashion the technical progress transferred from the centres; maintained rural societies with a strong aftertaste of colonialism, especially in the Andean and tropical areas; generated urbanization processes characterized by hypertrophy, centralization and lack of synchronization with industrial development; failed to make a definite break with the pre-capitalist stages of their rural class structures; continued to show high rates of illiteracy and imbalances in the development of education; absorbed technology in such a way that the successive waves of modernization did not sweep along with them the whole of the productive system; and as exporters of primary commodities, witnessed a high degree of dissociation between their basic production and consumption structures; while the heterogeneity of their productive systems consolidated broad occupational strata in which productivity and income were minimal. In short, they gradually acquired the features proper to their status as peripheral societies.

The region's history seems to suggest that great structural 'leaps and bounds' in the development of the Latin American economy have always taken place in response to international crises and convulsions. This is what happened in the nineteenth century, with the beginning of its political independence; and in the twentieth century, with the first steps and further advances in its industrialization process, historically associated with the two world wars and the Great Depression of the 1930s. The intensive regional economic growth of the past three decades was achieved under the 'leadership' of the expansion of manufacturing industry, and implied an increase in the region's aggregate product which exceeded the purchasing power deriving from its exports. Nevertheless, this manifest progress in industrialization and development did not succeed in changing Latin America's peripheral position in the international economic order. In essence, the region continues to be an exporter of primary commodities, and this is the key factor determining its peripheral situation in the world economy,

reflected in the chronic asymmetry and deficits in its trade with the centres.

Since the Second World War, the share of primary commodities in world trade—even including petroleum—has declined and, in consequence, the same thing is true of the participation of the peripheral regions in the trade in question.

According to the statistical data available, the billions of people sunk in poverty in the lower-income countries are to be found in the economies with the least degree of diversification of production, whose almost exclusive support is their export trade in primary commodities. These are the countries which have most rapidly lost ground in the general ranking by per capita product and share in world exports. Their economies show a high agricultural component in the value of their total product; it reached 51% in 1960, and 20 years later had decreased to 34%. Data published by the World Bank² show that the share of manufacturing industry in their regional product rose by only 2 percentage points in the past two decades, from 11% to 13%. In 1979, the average per capita product of this group of countries amounted to US\$ 230 and the size of their population exceeded 2 billion persons.

Those of the middle-income developing countries that are not oil exporters—to use the World Bank terminology—which include many of the Latin American countries, have a per capita product six times higher than that of the first group. And in contrast to what happened in these latter economies, in which the growth of manufacturing industry slowed down in the 1970s and dropped below their aggregate product, the greater dynamism of the middle-income countries was due to the vigorous expansion of their manufacturing industry. Some of them, like the South-East Asian countries, Spain and Portugal—and more incipiently Brazil—had managed to export manufactures on a significant scale to the markets of the developed countries, especially during the second half of the 1970s.

Nevertheless, the share of Latin America

²World Bank, *World Development Report 1981*, Washington D.C., August 1981.

as a whole in world exports fell from 11% in 1950 to 5% in 1980, a contraction which was due mainly to the fact that despite the progress in industrialization recorded in the countries of the region, no substantial change was introduced into the structure of exports, a high proportion of which —about 80% in recent years— still consisted in primary commodities. Although in the 1970s the region's exports of manufactures increased their relative share in world exports of industrial goods, from 1% in 1970 to 1.4% in 1978, this was not enough to offset the deterioration in the terms of trade for the basic products that the Latin American countries sell on the world market, even taking into consideration that a sizeable proportion of these commodities consists in hydrocarbons.

Of course, the income-elasticity of demand is higher in the case of manufactures than in that of primary commodities, and, basically for that reason, trade deficits and indebtedness are chronic features of the position of the peripheries in the international order. The sole 'adjustment' capable of definitively doing away with this asymmetry can only derive from a structural change in the specialization characterizing the production and trade of Latin America —and of the periphery in general— whereby their production and exports of manufactures can be expanded. Strictly speaking, international co-operation on the part of the centres in the sphere of trade becomes coherent over the long-term only if it is directed towards the expansion of industrial production and export capacity, and is carried out on terms and in conditions which make it possible to attain these objectives. Otherwise, the trade deficits and chronic indebtedness of the peripheral countries, including those of Latin America, will remain inherent in the logic of the world economy, as long as its present structural dynamic persists.

The following sections of the present chapter re-state the advantages of regional co-operation and integration for the promotion of a development style which will enhance Latin America's autonomy in the world order, which is based on a renewal of industrial expansion and which follows the paths of its own creativity in quest of social justice. This enunciation of values, which pertains to the realm of the desir-

able, is nevertheless an essential point of reference for estimating the viability of specific measures directed towards the end in view.

3. Co-operation, autonomy and bargaining power

As regards the future outlook, the long-term relations of Latin America —and of the periphery in general— with the centres will probably be marked by a high degree of uncertainty, not only in the monetary and financial spheres and in the area of trade, but also with respect to the directions that will be taken by the future structuration of production in the developed world. From now on —and for a period which it is difficult to determine exactly, but which is quite likely to be prolonged— the international order will be passing through a hazardous interregnum. In the monetary sphere it will probably be necessary to replace the dollar by a different and less conflictive symbol that is internationally acceptable, and to strengthen the institutions which give liquidity to the system and regulate imbalances in world trade. Undoubtedly, the present operation of IMF will have to be overhauled with a view to increasing the weight it carries and reorienting the unsuitable adjustment strategies that it is currently recommending to the peripheral world. In the area of trade, the system of regulations centralized today in GATT and concurrently discussed in other world forums such as UNCTAD will have to be reconsidered. The increasing protectionism of the centres is reflected in the various forms assumed by the 'managed trade' which is gaining ground in the developed world. In the sphere of production, the deep-seated and prolonged recession not only reflects *volte faces* —and perplexities— in the economic policy of the centres, but also foreshadows profound long-term changes in technology, linked to the shift in sources of energy, to the automation and robotization of production processes, to achievements in genetic engineering and in information techniques, etc. It seems obvious that these revolutionary advances will bring about radical although as yet unidentified, alterations in the structure and regional distribution of world production capacity.

It must be emphasized that at the national level the Latin American countries will be able

to exert scant influence on the profound changes in the international order that are infallibly approaching. Not even the larger economies of the region can individually affect the trends followed by these changes in such a way as to safeguard their own national interests.

Will the Latin American countries, then, be isolated lookers-on, trusting merely in the comparative advantages inherent in the past in their peripheral position? Will they confine themselves to ritual demands for the benefits of an international co-operation which is asymmetrically dependent upon the will of the centres? Will they surrender leadership in the orientation of regional manufacturing industry to the criterion of the transnational corporations?

Questions of this type could be spun out further, but to do so would be a mere rhetorical flourish. It seems legitimate, however, to posit that the real and institutional achievements of Latin American co-operation and integration are the starting-point—both desirable and viable—from which to increase the region's capacity for defence and reaction *vis-à-vis* the disquieting changes that are looming up in the international order. This is obviously the external facet of Latin American unity, more necessary today than ever.

a) *Trends in world trade*

It seems unnecessary to recapitulate the characteristics and magnitude of the new protectionist measures which have been and still are being applied by the industrialized countries and to insist on the flagrant contradiction this implies with the postulates of trade liberalization set up as basic objectives of the international community. ECLA has devoted close attention to the subject³ and has transmitted its conclusions and recommendations to the governments.

In the crisis that is currently affecting the world economy, the protectionism of the North acts as a serious constraint on the development of the South, whose exports it reduces in various 'sophisticated' ways. This reduction, in turn,

brings down the foreign exchange income which the developing countries need to satisfy their import requirements, a key element in the maintenance of an acceptable rate of economic activity. To close the external sector gap, countries have progressively resorted to external credit, which has increased inordinately, while it is no longer possible to service the debt by using export earnings, as should be the normal procedure.

Consequently, the trade protectionism of the market-economy industrialized countries is one of the major causes of the bottleneck in the external sector of the developing countries, including those of Latin America. Apart from the fact that the protectionist measures in question imply an infringement of GATT's express provisions, they boomerang against the interests of the industrialized countries themselves, which are prevented from keeping up an export rate that would enable them to dynamize their economies and substantially reduce unemployment. For example, 40% of the United States' exports are destined for the developing countries.

Furthermore, 1981 and 1982 were years in which world trade declined, this being one of the peculiar features of the international crisis. The result has been a certain loss of confidence in the international trade system, to which testimony is borne by the decrease in the rate of investment in the industrial countries themselves and by the open conflict that has arisen among them with regard to their trade.

This last is another of the special features of the world economic crisis. The GATT Meeting at Ministerial Level, held in Geneva at the end of November 1982, was the first to be convened at that level in the past nine years, and its results were disappointing for the developing countries, since their chief aspirations were brushed aside, owing to the focusing of discussion on topics of importance to Japan, the United States and the European Economic Community (EEC). But the most interesting part of the whole business is what has happened in subsequent months, outside GATT. There is an obvious swing-round from a theoretical free trade to a 'managed' trade, as it has come to be called. For example, the agreement reached by EEC with Japan, early in February of the pres-

³See, for example, ECLA, *The external economic relations of Latin America in the 1980s*, E/CEPAL/G.1160, 1981.

ent year, is a serious step in that direction, since for the first time Japan has negotiated a voluntary restriction of its exports to the community as a whole rather than to its individual member countries. The same may be said of the agreement between the United States and Japan aimed at securing equilibrium in their reciprocal trade balance; to that end Japan has lifted some of the protectionist measures which it was applying for the benefit of its agricultural sector.

In short, despite the rhetorical utterances of the GATT Meeting at Ministerial Level, agreements restricting the expansion of trade are proliferating, to the detriment of certain dynamic comparative advantages, as well as of the consumer in developed countries, who will have to pay higher prices.

In Latin America, the international crisis and the huge external debt have imposed adjustment policies based on a drastic reduction of imports as the most direct means of saving foreign exchange and using it for debt servicing. Through the adoption of this course, traditional intra-regional trade flows have been affected and commitments assumed by countries under the region's existing integration programmes have been vulnerated. This has been turned to account as one of the most cogent arguments adduced against the validity of such programmes as suitable means of coping not only with the international crisis but with the very development of Latin America itself.

In this context, the region must view international trade prospects as a major challenge in two directions. First, to consolidate, maintain and expand to the fullest possible extent intra-Latin American trade, resorting for that purpose to all the multilateral and bilateral mechanisms. Secondly, to construct, organize and exercise a collective bargaining power which will enable it to keep up a balanced trade with all parts of the world, in line with the trends of the moment, giving preference, of course, to the interests of the region and its linkages with other developing countries.

The expansion of intra-regional trade implies, in addition to a firm political will to achieve it, the need to call into play such trade measures as novel and efficient financial mechanisms which will make it easier and more

attractive to import from Latin America than from third countries. Keeping up a balanced trade with other countries or groupings of countries requires great internal solidarity and the determination to exercise collective bargaining power in order to attain objectives of common interest to all the Latin American countries.

b) *Latin America's capacity for economic defence*

In line with the trends of the world economy, as set forth in the preceding paragraphs, much of the region's capacity for defence and reaction must come from the concerting of unified efforts in the spheres of trade, finance and production.

In the field of trade, protection of the prices of the primary commodities exported by the region necessitates the adoption of joint positions in the framework of global approaches which do not 'pigeonhole' problems to an undue extent. Weight may also be carried in negotiation forums by the unification of purchasing power *vis-à-vis* the centres, in order both to obtain better terms of sale for the products that Latin America exports and imports, and to concert measures retorting to the protectionist behaviour of the North towards Latin American commodities and manufactures. The concept of regional priority in supplies of primary commodities is closely connected with questions of regional economic security, which opens up promising areas of regional co-operation in respect of food and fuels, for example. In short, it seems obvious that in this field fuller and firmer regional co-operation is the most meaningful way of overcoming the atomization and isolation which undermine the countries' bargaining positions *vis-à-vis* the centres.

In the area of finance, indebtedness to the private international banking system will drag on with its present weight and structure for a relatively lengthy period. The primary need is a dynamic approach to the problem; the first requisite for coping with debt servicing is the ability to go on growing and exporting. In default of quantitative and qualitative changes both within the countries and in the international sphere, exercises in the rescheduling of payments are precarious and short-lived. Payments

will therefore have to be subject to the expansion advocated here. An elementary form of financial co-operation among the Latin American countries is to agree upon common norms for the renegotiation of the debt which abide by this principle and withstand the imposition of interest and surcharges that are calculated on bases completely divorced from the real potentialities of world development and trade and that exceed the costs initially envisaged when the debt was contracted. At the regional level, plenty of possibilities are opened up for progress towards the perfecting of payments clearing mechanisms, the adoption of a regional unit of account, and other measures which, by sparing the use of convertible currencies, may facilitate intra-regional trade. Similarly, steps should be taken to strengthen credit instruments for financing economic development and the expansion of export capacity. All these lines of action will help to lessen the region's economic vulnerability *vis-à-vis* the centres.

In the sphere of production, too, regional co-operation has an 'external facet' which increases Latin America's power of defence and bargaining in its relations with the centres. Thus, one of the few conceivable ways of securing a permanent 'symmetrical' linkage with the said centres is the development of productive and technological capacities of the region's own, which will meet some of the following requisites: a) that they be diversified, i.e., that they comprise both traditional and modern branches of production; b) that they develop in depth, i.e., that their coverage shall extend from basic inputs to final goods, using as far as possible capital goods of regional origin; c) that they be harmonious, in that there should be no marked disequilibria in productivity and growth between the various sectors and branches of the economy; and d) that they be self-supporting, so that, primarily on the basis of each country's domestic demand, supplemented with regional and world demand, they can meet basic national needs, and can steadily grow and improve.

It can safely be asserted that no country in the region, however large, can attain such an objective on its own account. Accordingly, co-operation and integration among the Latin American countries are undoubtedly efficacious instruments for bringing this goal within reach.

In each of the fields mentioned, examples could be cited in greater depth and detail, but for the time being it will suffice to ratify the central message in this connection. The international order has entered upon a period of uncertainty which is likely to be prolonged, and in which the bases of international co-operation have been and will be severely tried. In view of these circumstances, the Latin American societies can find a twofold and interdependent argument for co-operation and integration. Internally, their task is to strengthen a dynamic and equitable regional development; externally, it is to increase their autonomy and bargaining power in the world order.

4. *The linkage between industrialization and integration*

a) *Conditions for integration*

Economic integration is a political and instrumental response to the development requirements of countries where industrialization is accorded high priority. In other words, it is economic development that opens the way for economic integration, not the reverse: i.e., formal integration cannot suffice by itself to sustain economic development in depth. It should be made clear from the outset that the assumption on which the present argument is based is that industrialization is the dynamic nucleus of economic development, as has been shown by the experience of the centres itself, and, more recently, by that of the so-called 'newly industrialized countries'. It is worth while to state explicitly that the priority of industrial development by no means implies a voluntary and still less a strategic neglect of the other sectors of the economy, in particular that of food and agriculture.

The foregoing assertion is based on the relatively short but enlightening history of the efforts made in Latin America to establish free-trade areas and common markets, as in the case of European integration.

The classic tariff instruments on the basis of which Latin American integration has been promoted are oriented in two complementary directions. On the one hand, their long-term aim is a common external tariff, and on the

other, they tend to eliminate the tariff barriers which convert the domestic markets into 'water-tight compartments'. Integration, in various degrees and patterns, makes for the formation of a regional market which is not only enlarged but also protected. This protection may indubitably reach levels which are favourable to import substitution and therefore give impetus to industrialization. That is, industrialization and integration interact and stimulate each other.

Past experience of integration programmes, however, bears witness to the fact that they represent a higher and later phase of industrialization processes previously carried out at the national level. In particular, among the large and middle-sized countries of Latin America integration began with the Latin American Free Trade Association (ALALC), which had behind it a considerable prior degree of industrial diversification.

The course of events in the region has shown that in periods when industrial development has proceeded more rapidly and in greater depth, the economic and in particular the trade links between the countries members of integration schemes have notably increased. The Central American Common Market (CACM); the Latin American Free Trade Association (ALALC), today the Latin American Integration Association (ALADI); the Andean Group and the Caribbean Community (CARICOM), are good illustrations of what has just been said, in the sense that while industrialization was a central and top-priority objective of their member countries, integration at the same time reached the acme of its vigour, and, as its most visible expression, intra-subregional trade rapidly expanded.

The reason for this lies not only in the specific changes undergone by the manufacturing and other economic sectors when the industrialization process is launched and makes headway, but also in the resulting diversification and expansion of the exportable supply. Hence industrial complementarity and specialization among countries with similar or not very different degrees of development are seen to be viable and worth while. In contrast, when industrial development is sluggish or the impulse to promote it is lost, at the same time expectations built on the fruits of integration vanish into thin

air. Thus, an extreme case of the impracticability of integrationist prospects occurs in economies that are simply and solely exporters of primary commodities.

In the Central American Common Market, for example, the 1960s undoubtedly witnessed the greatest advances in integration, in respect both of instrumental improvements and of expanding intra-subregional trade, which climbed steadily from 6.7% of total exports in 1960 to 26.1% in 1970. This dynamism of trade within CACM coincided with a vigorous industrial development drive, since the manufacturing industry of the five member countries (Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua) increased their output at a cumulative average annual rate of 8.6% between 1960 and 1970, whereas the gross domestic product rose at a rate of 5.9%. In the 1970s, however, a marked decline in the industrial development coefficient took place correlatively with the drop in the percentage of reciprocal trade.

In its turn, the Cartagena Agreement, the ruling instrument of the Andean Group, accorded the industrial development of its member countries a leading role in the Andean integration process. Of the region's integration schemes this is undoubtedly the one that has attempted to go farthest in joint industrial programming, with the aim of securing economies of scale, more efficient utilization of the subregion's resource endowment, and greater specialization and bigger volumes of production. In fact, in 1969, the year in which the Cartagena Agreement was signed, out of an intra-subregional trade of US\$ 96 million, 50% was represented by traditional products, whereas in 1980, when subregional trade amounted to US\$ 1 113 million (excluding petroleum), non-traditional exports —mainly manufactures— accounted for as much as 88%.

It is worth while to point out that for the purposes of the present study what is meant by industrialization is the development and transformation of the manufacturing sector and its linkage with the modifications brought about in the rest of the economic activities by the action and influence of the change in industry itself. This sector draws labour out of the agricultural sector and in return gives it inputs and equip-

ment for its modernization; generates activities producing the services required for the production, marketing and financing of manufactures, a process which in turn feeds back into industrial expansion; urbanizes and alters the transport and communications infrastructure; and influences, directly or indirectly, the orientation and growth of the public sector. Directly, through the requirements it creates in respect of physical and educational infrastructure, *inter alia*; and indirectly, through the social change induced by growth. This latter is reflected in the spheres of trade-union, party, regional, consumer-organization and other forms of social groupings which help to stimulate and channel the expansion of the public sector.⁴

It is the development and diversification of the economy caused by industrial development that provide the motive power behind more extensive and more varied trade among the countries members of an economic integration scheme. Of course this does not exclude the further possibility that integration, in attempting to create wider economic spaces than the domestic markets, may permit fuller and more efficient utilization of the existing installed capacity, through complementarity and specialization in industrial production and, in some cases, the creation of new productive capacities. It is unlikely, however, that this can take the place of industrialization as an essential spur to greater dynamism in the integration process.

It should be recalled, moreover, that since a start was made on the recycling of the financial resources deriving from the increased income of the petroleum-exporting countries, changes of singular importance have been brought about in the economic policies of many Latin American countries. One of the salient features of these was the tendency to overvaluation of national currencies and liberalization of imports, which was largely due to the copious inflow of financial resources stemming from the aforesaid recycling, and undermined the validity of the most classic integration instruments, such as tariff preferences and the financing of intra-subregional trade.

Overvalued currencies and tariff reductions implied, in practice, a lowering of consumer prices for merchandise from any source, which detracted from the efficacy of the tariff preferences established in favour of other countries members of the corresponding integration agreements. Similarly, the ease with which financing could be obtained for imports from industrialized countries tended to minimize the region's efforts to build up the equivalent of these credit facilities. The figures for the Latin American countries' external debt —about US\$ 300 billion at the end of 1982— speak for themselves as to the influence that must have been exerted by these financial resources on the orientation of the policies and instruments which animate reciprocal trade. There can be no doubt that the flow of external financial resources has done much to deprive the regional integration programmes of vigour and support.

The return to tighter conditions in respect of the international availability of new financial resources and the high level of indebtedness of the great majority of the countries of the region may perhaps restore the political will to revert to development patterns where industrialization and integration regain their priority. Otherwise, the critical phase through which most of the Latin American integration programmes are passing will continue, and no improvement or change in their instrumental structure will suffice in itself to counteract the standstills or setbacks that they are suffering.

Thus, for example, the outcome of the transformation of ALALC into ALADI has been an agreement for whose objectives no explicit time horizon has been established, whose Secretariat is relatively weak, and whose terms largely correspond to the limited scope attributed to integration in the present conjuncture by several of the countries members of the scheme in question. The problem of infusing new energy into the process will therefore be resolved only in so far as there is a vigorous resurgence, in all spheres, of concern for economic development in its long-term integrated projection and industrialization is accorded a preponderant place therein. An attempt to rescue integration from its present state of languor by reconstituting its instrumental mechanisms may represent an immense ef-

⁴In this connection, see F. Fajnzylber, *La industrialización trunca de América Latina*, Mexico, Editorial Nueva Imagen, 1983, chapters III and V.

fort, and one that is not even very viable, unless international events compel the member countries to redefine development priorities and strategies.

To all this must be added the need for certain countries of the region which have shown that they are in the van of industrial development to express their political will in favour of integration and co-operation measures which will revive the potential of the corresponding programmes existing in Latin America today.

The foregoing observations on the new operational and development conditions in the world economy, the need for Latin America to embark upon innovative development strategies, and the unquestionable interaction between industrialization and integration, suggest that a qualitative change may be expected in the guiding principles and practices of integration in Latin America.

It should be recognized that the so-called 'crisis of integration' is nothing more or less than a 'crisis of development' and of development policies. The loss of a long-term perspective and therefore of a minimum of guidance for reproductive investment, as well as the apparent boom conjured up by the copious inflow of external financial resources in the recent past, have confronted integration programmes in Latin America with a number of successive tests of viability. Their very survival is a phenomenon worthy of note, notwithstanding that some programmes have emerged in a considerably enfeebled state from this veritable 'intensive treatment' and will probably take a long time to recover their strength sufficiently to assist in steering a new integration strategy, more in keeping with the prospects of the international economy and with the real national circumstances of the Latin American countries.

At the same time, there is indubitably ample scope for co-operation among the sub-regional schemes and within each individual programme. Some of these fields of co-operation have already been described in a recent ECLA document.⁵ It should be repeated, how-

ever, that the launching of a great collective integration effort largely depends upon the measures adopted to give back their leading role to development and industrialization, in their true and complex political, social and economic dimensions.

It seems advisable, therefore, to seek indicators in the orientation and content of the Latin American countries' overall development policies of how far the integration enterprise upon which Latin America embarked two decades ago is viable, and what are the bounds of possibility. While no doubt is cast on the idea that integration increases the feasibility of achieving a more efficient type of development, which certainly improves the prospects of a better-balanced insertion in a world of economic and political blocs, the question that arises is how far these evident advantages can outweigh the fact that certain domestic policies take a dubious view of mutual co-operation or the attitude of certain governments whose short-sighted outlook is almost always baffled by the speed of events.

On no account is it the intention of these comments to strike a note of pessimism as to the future of the linkages between the countries of the region. On the contrary, they aim at clarifying certain causal relations, useful for delimiting the frontier within which co-operation and integration can be expected to function, and thus averting unnecessary frustrations and futile illusions.

Identifying not only the genuine political will that is concerned for the progress and consolidation of integration —i.e., the real existence of a 'vocation' for development and industrialization—, but also those top-priority areas of co-operation where joint and solidary action should be taken, ought to be a task of paramount urgency in Latin America. Simultaneously, this study may lead to the conclusion that a regrouping of the countries participating in each integration scheme or the establishment of closer links between the most industrially developed Latin American countries and the existing subregional agreements, might impart

⁵See ECLA, *Integración y cooperación regionales en los años ochenta*, in *Estudios e Informes de la CEPAL N° 8*, Santiago, Chile, 1982. (English version only in mimeographed text,

under the title "Regional integration and co-operation in the 1980s", E/CEPAL/G.1151.)

greater homogeneity and vigour to the regional integration process.

Furthermore, the countries that have displayed most dynamism in their industrial development are those best fitted to assume leadership in the consolidation and expansion of regional markets; it will also be incumbent upon them to help to create opportunities and options for the less developed countries or those whose development potential is limited.

From another angle, the truncation of industrial development in Latin America by its relative backwardness in production of certain intermediate inputs and of capital goods allows plenty of room for its acceleration and for increasing the autonomy of the industrial structure. Joint action in this field among various countries of the region confers their true dimension on such concepts as complementarity, specialization and programming, which otherwise appear *ex post* as unrealistic; while at the same time it can bring to life an authentic integration deeply rooted in the national and regional development potential.

An additional conditioning factor, to which history bears witness, consists in that as long as industrial development is exclusive and tied to the consumer demand of certain limited sectors of the population, this state of affairs will tend to reproduce itself, thus reducing still

further the participation of the various social actors in the different negotiating and operational organs of integration. All this would mean that both processes — industrialization and integration — would rapidly peter out.

Lastly, it should be noted that industrial development, like every evolutionary process, passes through its indispensable 'learning' phases in an ordered sequence, starting with its establishment on a firm footing in the domestic market and then reaching out to markets presenting increasing difficulty in respect of access and 'sophistication' of demand. In this context, the Latin American integration agreements have shown that they are an appropriate means of effecting a gradual and natural transition towards fulfilment of the aspirations focused upon increasing the manufactures component in the region's exports. The figures speak for themselves in this respect, since about half the intra-zonal exports of the ALADI countries consists of manufactures, whereas these products represent only one-fourth of exports to the developed countries. In addition to this important qualitative fact, a point that will have to be borne in mind is the potential dynamism of the Latin American countries' reciprocal trade, which at present amounts to only one-sixth of the total trade of the region.

III

International and regional co-operation potential

1. *Latin America's responses to the crisis*

a) *Trade and development*

The role of regional co-operation and integration can be approached either in the light of the present international conjuncture or in the framework of the structural conditions of regional and world development.

From the first angle, any spur to international demand which may afford support to Latin American exports will obviously be desirable in face of the severity of the depression.

The Latin American market can to some extent compensate the contraction in demand on the part of the centres, if part of its trade is diverted towards regional suppliers. This diversion of trade is, first and foremost, a defence mechanism which at the regional level should be complementary to the equally necessary import substitution process at the national level. As long as the restrictive trade and financial conditions originating in the developed countries are maintained, these defence mechanisms seem economically needful and ethically legitimate.

The long-term role of integration in world

economic development should be regarded as necessary and fitting. Strictly speaking, there should be no incompatibility of opinion between the centre and the periphery as regards the mutual advantages that would derive from a strengthening of regional integration. But obviously, too, any assertion to that effect reflects a specific conception of the most desirable form of international system, and of the best way to deal with the deep-rooted structural crisis in the international order.

If the developed countries acknowledge the need to do away with the present centre-periphery dichotomy, they should show their willingness to agree in future upon a more homogeneous and equitable distribution of world production capacity and to collaborate in the promotion of a system made up of a number of economic regions capable of achieving a diversification of production and exports in keeping with the requirements of an expansion of world trade. Accordingly, they should accept integration among the developing countries as a positive step towards the attainment of a more dynamic, more balanced and more equitable world economy. More dynamic, because what is at issue is not a static optimization of the level of trade as it is structured today, but its expansion in consonance with the requirements of world development. More balanced, because stable participation in an expanding trade calls for the elimination of the structural constraints inherent in the peripheral countries' position in the world economy; otherwise, the economies that find rigidities obstructing the progressive diversification of their production and exports would relapse into the familiar pattern of deficits and indebtedness. More equitable, because an advance would be made towards definitively overcoming the international vulnerability and subordination peculiar to countries like those of Latin America.

In so far as economic integration has proved decisively beneficial, over the long term, to Latin America's exports of manufactures, it has also contributed to the attainment of these goals.

In the long run it is to everybody's interest that the growth of international trade should be dynamic and that all countries should be able to enjoy a stable share in this expansion. It should

be recalled that a substantial proportion of the existing problems stem from the trade deficits which affect the economies of most of the developing countries. To the equally permanent surpluses recorded by the central economies in that trade with the periphery, were of course added, in the 1970s, those originating in the petroleum-exporting countries. Setting aside the historically specific question of petroleum, trade between the industrial centres — from the post-war period to the beginning of the petroleum crisis— increased faster than world trade, since —as is worth repeating— trade in manufactures grows at a higher speed than trade in basic products at the international level, by virtue of the respective income-elasticities of demand for each of these groups of goods.⁶

The diversification of production and export structures is a prerequisite for dynamic participation in the world market. By failing to expand sufficiently its sales of manufactures to the centres, Latin America has lost one-half of its share in world trade during the last 30 years. Except during the 'open and permissive' period which generated much of the present regional indebtedness in the second half of the 1970s, the Latin American market has been the main motive force behind Latin America's exports of manufactures.

In short, if they are not to continue losing ground in the world market, the countries of the region must increase their efficiency and competitiveness in the production and export of manufactures. The regional market itself is the economic space in which exports of manufactures can be kept up in the present critical circumstances, and consolidated in the longer run, thus acquiring increasing viability in the world market.

b) *The debt problem*

It has been remarked that the unity of Latin America has two facets. On the one hand,

⁶This is an argument of key importance, the validity of which has been amply confirmed by postwar trends in world trade. Among the more recent contributions to the study of structural disparities between centres and peripheries, see Raúl Prebisch, *Capitalismo periférico: Crisis y transformación*, Part Four, Mexico, Fondo de Cultura Económica, 1981.

the growth of regional co-operation fosters and multiplies the development potentialities of each individual country; on the other hand, joint and concerted international action increases the region's capacity for defence and riposte in the thrust and parry of world power relations.

The present international financial conjuncture affords a perfect illustration of this second facet of Latin American unity. The external debt problem ought not to be tackled separately by our countries, at least in two of its major aspects. In the first place, its renegotiation should not be dealt with piecemeal, country by country, either *vis-à-vis* private international creditors, or in the case of the International Monetary Fund. Secondly, the debt problem cannot be dissociated from the critical conditions at present besetting Latin American and world development.

In relation to the renegotiation of the debt, and in face of the high degree of accord reached by the international private banks, there is a virtually obvious need for joint exploration, discovery, organization and application of specific multilateral renegotiation mechanisms—or, at least, certain common basic criteria—which will enable the Latin American countries to increase their capacity for defence and reaction in their individual renegotiation of their external debt.

The common criteria for rescheduling external debt payments should avoid falling into the trap of treating the financial problem as divorced from world and regional development prospects. Nor is the application of the conditionality of the Fund acceptable, designed as it was precisely for the purpose for dealing with specific cases, not to cope with the manifold economic, social and political repercussions of the world financial crisis. The economic philosophy on which this conditionality is based, which has always been theoretically open to question, in present circumstances is inadmissible. A passive acceptance not only of the rates of interest applied without regard to the Latin American countries' growth and export possibilities, but also of the recessive adjustment policies imposed by the Fund—which, paradoxically, prevent the expansion in question—, will signify, firstly, mortgaging the development process and, secondly, seriously jeopardizing the

economic and political systems of the Latin American societies, particularly of those countries that are endeavouring to establish democratic systems on a firm footing.

The recessive adjustment policies that our countries are being compelled to adopt not only imply an intolerably burdensome share in the costs of the world crisis, but shape a mistaken and counterproductive strategy for the recovery of the Latin American economy.

Accordingly, this is no mere matter of a 'financial problem' which is the responsibility of the debtor country. It is the very foundations of the international order—in its productive, trade, financial and political facets—that are at stake. Joint and high-level political solutions, therefore, must be urgently sought.

2. Possibilities of action in the sphere of trade

a) Background data

Intra-Latin American exports currently account for about 16% of the total exports of the countries of the region as a whole. Exports of manufactures to the region itself amount to about 50% of total intra-regional exports. Thus, there are obvious possibilities of much more thoroughgoing integration in the field of trade. It should be noted, for example, that the intra-regional trade of the European Economic Community countries represents approximately 50% of their total exports. Although Latin America has not the same reciprocal trade potential as the EEC countries are afforded by their great diversification of production, the region is obviously in a position to intensify its integration through a reorganization of its existing trade flows. For instance, notwithstanding its very high degree of capacity to produce primary commodities, only one-fifth of the value of total imports of such goods—excluding petroleum—came from the region itself in 1980, which means that here too a vast potential is opened up for the expansion of reciprocal trade.

Co-operation in the sphere of trade can also be used to take advantage of a unified regional purchasing power, through joint imports.

This is where the other aspect of Latin American co-operation comes definitely to the

fore: the increase in bargaining power *vis-à-vis* the developed countries. In this domain, Latin America's potential in relation to the centres is not impressive, from the standpoint of the relative importance of its market and their sales. But the absolute figures involved are very high, and the significance of the regional market for some of the industrialized countries must be considerable in the case of certain specific products which it is necessary and possible to identify.

It is with the United States that Latin America's chief trade links have been forged. Out of North America's total exports to the world —the data used here include Canada— approximately 15% is absorbed by Latin America, or, more precisely, by Central and South America. The importance of the Latin American market, in percentage terms, for the other industrial regions is as follows: Japan, 6%; Western Europe, 3%.

Thus, Latin America's market carries more relative weight in the United States' total exports than in those of other industrialized regions. From the point of view of dynamism, an increase is also observable in Latin America's importance as a customer of the United States.⁷ As a buyer, its share in the expansion of the United States' total exports was as indicated below for the corresponding years: 1968-1973: 10%; 1973-1977: 14%; 1977-1978: 16%; 1978-1979: 15%; 1979-1980: 21%; 1980-1981: 20%.

Furthermore, the North American market —including Canada— absorbs 35% of Latin America's total exports. The significance of the markets of the other developed countries in relation to these exports is 4% in the case of Japan, 22% for the countries of Western Europe in the aggregate, and 8% for the countries of the East.⁸

Furthermore, it must be realized that any measure aimed at a reorganization of Latin American trade —both in its intra-regional and in its extra-regional effects— will depend deci-

sively upon the behaviour of certain large and medium-sized countries of the region. Recognition of this fact is indispensable for a proper appraisal of the regional market potentialities that do effectively exist, and of the most appropriate strategies for turning them to account.

In Latin America's purchases from the rest of the world, the share of the three leading importers —Brazil, Mexico and Venezuela— was 57% in 1981. If Argentina, Chile and Colombia are added to the group of countries carrying most weight, the conclusion is reached that only six countries account for 76.4% of Latin America's total imports. Incidentally, it is in these same countries —with the exception of Colombia— that the biggest percentage of Latin America's external debt to the international private banking system is concentrated. Consideration of Latin America's trade and financial problems in combination might be productive of favourable results in the corresponding negotiations, given the political will and active co-operation of these countries, because of their importance in the region's external relations.

The same thing happens in intra-Latin American trade within ALADI. Of the latter's total intra-zonal exports those of Argentina, Brazil, Mexico and Venezuela represented 73% in 1981; and the same countries absorbed 53% of intra-ALADI imports. Taken in the above order, their trade surpluses in that same year, expressed in terms of dollars at current prices (FOB), amounted to US\$ 796, US\$ 965, US\$ 79 and US\$ 534 million, respectively. Colombia and Chile, for their part, showed deficits. The surpluses of Argentina, Brazil and Venezuela in the aggregate were equivalent to 19% of total intra-ALADI exports. Consequently, any significant effort to divert trade into ALADI will depend decisively upon the behaviour of the large and medium-sized countries, as regards both stepping up the percentage of their transactions and stabilizing their balances with the Area.

b) Possible lines of action

Among multilateral measures to preserve and expand intra-regional trade, the regional tariff preference to which the Montevideo Treaty of 1980 refers is an instrument that might exemplify, firstly the will to intensify the inte-

⁷Throughout the 1970s the *de facto* devaluation of the dollar as against the European and Japanese currencies made for a shift of Latin American imports from those markets of origin to the United States suppliers.

⁸See GATT *International trade in 1981/1982*, Geneva, 1982.

gration of the countries members of ALADI and, secondly, the determination to adopt joint and solidary Latin American positions in negotiations with the rest of the world. To ensure that the agreements reached are not merely symbolical, it will be necessary to attain, even if only gradually, substantial margins of preference, capable of producing significant effects on the creation or diversion of trade, in keeping with the international difficulties of today.

This mechanism has an eminently multilateral character and should be promoted as a means of complementing the recent bilateral agreements concluded in ALADI. It is desirable, in this connection, that the success of partial agreements should not attenuate the need for active convergence towards more advanced stages of regional integration, which can only emerge from global commitments and agreements of a multilateral character.

The utilization of mechanisms of this type, however, may not suffice to sustain and promote trade in the present world conjuncture. It must not be forgotten that in recessive situations like that of today the Latin American countries may harden their positions in respect of trade reciprocity, in an attempt to reduce and increase, respectively, their extra-regional imports and exports. This increases the risk that in face of the existing difficulties administrative mechanisms and other non-tariff instruments may be more intensively applied, and may counteract or annul the trade concessions deriving from integration programmes. In order that full use may be made of the capacity for defence against adverse external circumstances implicit in regional integration potential, such measures should be selective and discriminatory. Selective, because preference needs to be given to capital goods and intermediate inputs; discriminatory, because they should not be applied to the countries of the region.

In addition to the efforts already made in the field of trade through various integration schemes, new measures can be tried out in respect of the diversion and creation of trade for the benefit of the region itself.

The diversion and creation of trade in favour of Latin American suppliers would help to palliate the chronic deficits in the balance of merchandise trade *vis-à-vis* the industrial

centres, to save foreign exchange through the machinery for clearing payments and to reanimate regional production, by encouraging, as a first step, full utilization of existing installed capacity. But, in addition to these results, the option of diverting trade into the region—especially in strategic items of great importance in regional demand—would be an instrument that would strengthen the region's bargaining power *vis-à-vis* the rest of the world in general and the developed countries in particular.

This instrument, which consists in Latin America's collective ability to restrict or suspend its purchases of certain lines of manufactures exported by the centres, can be turned to account both in keeping up the volumes and prices of Latin American commodity exports and in promoting the penetration of the region's manufactures into the developed countries' markets, where today they are subject to a variety of 'sophisticated' restrictions.

This type of regional concerting of policy has close precedents in decision 44 of the Council of the Latin American Economic System (SELA), adopted in 1979 and referring to the relations between Latin America and the European Economic Community. This decision lays it down that if measures adopted by the EEC—including the establishment or extension of self-regulation agreements—should have unfavourable effects on exports of Latin American products, the Latin American country or countries directly concerned shall, if they think it desirable, and irrespective of any bilateral measures they may deem fitting, consult with the other interested Latin American States, in order to determine the possibility of defining and, where appropriate, undertaking suitable joint action. This may include, among other economic, financial or trade measures, application of which would be voluntary, the following: a) symmetrical treatment applicable to exports from EEC or from one or several of its regions; b) directives for restricting or encouraging Latin American imports from those same markets of origin.

The intensification of protectionism and of 'balanced and managed' trade currently observable among the industrialized countries suggests the possibility that Latin America might put into effect measures such as those established in decision 44 of SELA, but of more

generalized scope. Mechanisms of this type can be made operative at the regional level only on the basis of full solidarity among the Latin American countries, with the support of a centralized and up-to-date information system, which will enable them to adopt decisions and take action in conjunction. The individual countries should make a careful and systematic survey of the markets of origin of their imports, which should be carried out for every product representing a significant proportion of the value of Latin America's global imports. In this way it would be possible to ascertain what repercussions would be felt in the centres if concerted measures were adopted to restrict or suspend imports of products from specific markets of origin, as has been done in their own reciprocal trade by Japan, the EEC and the United States, cases in point having been analysed in a wealth of detail in the European and American press in recent months.

This centralized, updated and permanent record of trade information should operate on the basis of official data furnished by the countries themselves, or through additional agreements with multilateral agencies. Irrespective of the options as to the specific location of this information service, what does seem unquestionable is the need to create it, if it is hoped to set the joint machinery in motion.

Another point to consider in the sphere of trade is the necessity of closely following trends in trade balances between the region and the main world industrial centres. This would make it possible to take timely decisions as to the opening of negotiations with countries maintaining excessively large trade surpluses with Latin America. In face of an aggravation of imbalances of this type, the Latin American countries could exercise their joint purchasing power, to which reference has been made, or apply discriminatory prohibitions or restrictions designed to restore the balance of trade, as is being done with increasing frequency by the industrialized countries.

The diversion of trade towards Latin American suppliers might gain significant and rapid impetus if government entities took part in it, according preference to regional sources for their imports of inputs and other requirements, irrespective of a possible increase in their

purchases from their own national suppliers.⁹ An intergovernmental agreement on this subject might be a decisive factor in giving a vigorous initial impulse to the diversion of trade from the industrial centres to Latin America, on the basis of purchases by the public sector.

In this connection, it is worth while to note certain orders of magnitude. State purchases constitute approximately 40% of the total imports of the ALADI countries; in 1981, these imports amounted to about US\$ 95 billion, of which roughly US\$ 38 billion were therefore government imports. The magnitude of this figure can be better assessed if it is further recalled that intra-ALADI exports in that year amounted to about US\$ 12 billion. It must be borne in mind that of those US\$ 38 billion only 4%, i.e., US\$ 1.5 billion, came from the region itself.¹⁰ If this proportion were raised to 30%, which does not seem unusually high over the medium term, the share of intra-ALADI trade in the member countries' total imports would be doubled.

Only 11% of the Latin American government imports correspond to 'tied' loans, and the remainder is subject to international standards of competition; of that remainder, almost one-third is financed by IDB and the World Bank. In the area of capital goods, these two official banks finance three-quarters of non-tied and State imports. This implies the existence of a great potential for diversion of government trade in capital goods which deserves careful exploration. Here three possible lines of action are combined which in present circumstances should be encouraged: i.e., diverting trade *en masse*, providing incentives to Latin American production of capital goods, and obtaining financing for that purpose from the major official development banks.

Here it is worth noting that the main beneficiaries of a reorientation of public-sector imports towards Latin American suppliers would be private entrepreneurs in activities producing

⁹Approximately 75% of State purchases favour their own national suppliers; this average obviously leaves room for substantial discrepancies from one country to another.

¹⁰See Guillermo Ondarts and Carlos Correa, *Compras estatales e integración económica*, Buenos Aires, IDB-INTAL, Colección Cooperación Empresaria II, p. 49.

tradeable goods, and the services which support and complement these. In this case there is obviously a perfect complementarity, reciprocally fruitful, between the public sector and the private sector, in which the former can contribute its immense purchasing power to bolster up the low levels of activity and the export potential of Latin American private entrepreneurs.

This section should not be concluded without express mention of two instruments of a partial character. The first consists in bilateral agreements on trade co-operation between pairs of countries; these agreements generally establish schedules of products subject to total or partial elimination of tariff duties and to periodic negotiations to bring them up to date. Measures of this type, falling legally within the definition of the agreements of partial scope for which provision is made in the 1980 Montevideo Treaty, are adversely affected by the occurrence of drastic modifications in exchange rates which abruptly alter the terms of trade. In such circumstances, tariff reductions lose their efficacy as means of promoting and diverting trade, and it becomes necessary to explore other possibilities. Long-term bilateral agreements may prove a suitable instrument for maintaining and expanding intra-Latin American trade, granting credit facilities and alleviating the existing payments problems by saving foreign exchange, inasmuch as the parties can buy and sell in the regional market, where merchandise can be cleared against merchandise. There is a vast field of application for mechanisms of this type, not only in relation to manufactures, but also in respect of primary commodities, and even the exchange of the one type of product for the other. Of course, measures of this sort are justifiable only in the framework of a set of mechanisms and agreements—both multilateral and partial—which will ensure the smaller countries similar opportunities to diversify their own production systems and increase their intra-regional exports of manufactures.

As regards these relatively less developed countries, the fields might be identified in which the collaboration of the more developed countries of the region could be of assistance in surmounting obstacles proper to underdevelopment or to special situations such as an imbalance in fuel and/or power supplies, landlocked

conditions, small domestic markets, lack of natural resources or shortage of skilled personnel.

What is needed, therefore, is to explore, from a practical point of view, new production and export possibilities for the countries in question, particularly in the sphere of primary commodities and of manufacturing industries connected with their processing. Collaboration with the smaller countries of the region must be oriented not only towards remedying their weaknesses or deficiencies, but also towards more systematic and exhaustive utilization of their own potentialities. The results obtained at the last ALADI Conference with respect to a total opening-up of markets to lists of products of special interest to Bolivia, Ecuador and Paraguay, while not fully satisfying the aspirations of those countries, represent a wise step in this direction.

3. *Possibilities for action in the financial sphere*

Of unquestionable priority in this field are the monetary and financial mechanisms that are aimed at facilitating the expansion of intra-regional trade and strengthening Latin America's financial autonomy and security at the international level, albeit mention will also be made of those financial mechanisms that are intended to encourage economic development.

In the first of these connections, the payments clearance mechanisms currently in operation have made it possible to save convertible currencies in the settling of reciprocal balances in intra-Latin American trade. At the end of each period the balances outstanding between pairs of central banks are determined, and the net balances of each participant *vis-à-vis* the others as a whole. Obviously, the smaller each one's balances with the group as a whole, the smaller too will be the amounts of international currency effectively involved in the clearance operations. Similarly, the more liberal the credit lines reciprocally granted and the longer the repayment period, the smaller will be the quantity of foreign exchange effectively brought into play.

The clearing system of ALADI (which includes the Dominican Republic) is now almost complete, since of the 66 possible agreements between pairs of Central Banks, 62 have been

signed. In 1981 the total amount of credit granted under the system exceeded US\$ 9.3 billion, i.e., virtually financed three-quarters of that year's trade.

As stated in a recent report, through this system, from the time of its entry into operation up to the year 1982 inclusive, operations have been channelled amounting to more than US\$ 50 billion, only about 25% being required on an average for the settlement of net debtor balances in the corresponding repayment periods.

It is also pointed out in the report referred to that the difficulties encountered as the years went by have generally been of little importance, and the amount of annual operations has been steadily growing from the outset up to the present decade, reaching the above-mentioned figure in 1981. In 1982, however, the upward trend in the channelling of operations was reversed, and their volume decreased on account of the international crisis, its effects on the economies of the countries members of the system and the adjustment measures adopted, the consequences of which it is hoped will be only temporary. The corresponding figure is approximately US\$ 7 billion.¹¹

A special aspect of this mechanism, which should be developed in greater depth, relates to the exchange of services, including tourism, on the basis of the use of a special means of payment. This might be, for example, a Latin American travellers' cheque. A saving of foreign exchange could thus be effected, since only payments for the services in question would have to be covered, and such balances could perfectly well be incorporated into the existing clearing mechanisms, together with those of intra-Latin American merchandise trade, should the countries so decide.

It is in trade in goods, however, that the principal benefits of this mechanism can be reaped. A dynamic expansion of each Latin American country's trade with the other members of the corresponding integration area, combined with a substantial increase in the amounts and maturities of reciprocal credits, would be a

relief in face of the impoverishment of reserves and the growing indebtedness of the Latin American economies. Furthermore, if the repayment period in the ALADI system were extended, for example, to six months, it could be interconnected with that operating in the Central American Common Market, provided that an agreement were reached on the rates of interest in force in each case.

In short, given the political will and the determination necessary for rapid and effective action, a combination of the mechanisms for encouraging reciprocal intra-regional trade and financing may generate an ever-widening 'virtuous circle'. A balanced expansion of intra-regional trade would make it possible to increase the advantages already implicit in the payments clearance mechanisms, and, reciprocally, an extension of the maturities and enlargement of the amounts of financing, together with the interconnection of payments systems, would enable reciprocal trade flows to expand and gain in flexibility. The result would be a steady decrease in the vulnerability of the trade and financial positions of the Latin American countries *vis-à-vis* the rest of the world.

Another pertinent mechanism is the Santo Domingo Agreement on Support of the Balance of Payments, which has worked satisfactorily on several occasions, and affords financing for countries with balance-of-payments problems on the basis of maturities and amounts that are still very limited, but are potentially susceptible of increase. It differs from the payments clearance mechanism, however, in that the present generalized situation of depleted reserves and acute indebtedness obstructs, in the short run, any device that implies additional transfers of internationally convertible currencies.

Much the same thing happens in the case of another interesting proposal formulated by ECLA, for the establishment of a financial safety net in Latin America, consisting of a commitment on the part of the official financial institutions of the region to act as 'last-resource lenders' for a member country in financial straits that had exhausted the possibilities open to it in other extra-regional sources of financing. This, like the preceding proposal, is designed to provide financial assistance to separate countries, but not to cope with a crisis like that of today, which affects almost all the countries

¹¹See *Evaluación del funcionamiento del convenio de pagos y créditos recíprocos, y eventuales medidas destinadas a su perfeccionamiento*, ALADI/CAFM/III/Doc.2, 21 January 1983.

of the region simultaneously and in conjunction.

It seems better worth while, in the existing circumstances, to explore Latin America's possibilities of participating more actively in inter-regional financial institutions —such as Arabank today, established on the basis of Arab and Latin American capital— which operate by tapping resources not only in Latin America but in other international financial markets.

While encouragement should be given to these and any other initiatives capable of improving the foreign exchange position of Latin America without subjecting it to terms that are incompatible with its necessary economic reactivation and growth, the most viable measures in the present situation are those which help to save the use of foreign exchange in reciprocal payments and those which permit the granting of reciprocal credits in the sphere of trade, on a longer-term basis than under the existing payments clearance systems, but organically linked with them.

In particular, while some Latin American countries have at their disposal banks of international standing, the region as such has no institution in the field of commercial banking which is represented outside Latin America.¹²

This is a serious lack. A regional multinational bank, based on capital contributed by public and private banks in Latin America and even by the Inter-American Development Bank, and operating in the big financial centres both in the area of trade and in that of the sale of securities, would decisively reinforce the external economic security of the region, by serving as a bridge for co-operation among various regional and subregional financial institutions and supplementing the work done by IDB as a development bank. A bank of this type would facilitate the identification of areas in which regional co-operation could be pursued in greater depth; it would improve access to more diversified sources of funds; it would reduce the so-called 'country risk' for foreign suppliers of resources; and would provide support to public

and private financial institutions at both the technical and the financial level. But it could also be of major assistance in future renegotiation or refinancing processes.

If a specified proportion of the Latin American countries' reserves were deposited for administration in this bank, it would be provided with a solid basis of operations, which would shortly make it an outstanding institution in the banking field in relation to trade and the sale of securities, thus facilitating the removal of constraints which today hamper Latin America's access to certain capital markets.¹³ A bank of this kind could play a decisive part in the promotion of intra-Latin American trade. In particular, it could serve as a clearing-house for long-term financial documents, arising out of reciprocal merchandise trade and expressed in a unit of account of the region's own, so as to make the greatest possible use of national currencies.

It would not take too much effort, in terms of time or resources, to formulate a specific proposal which could be subjected to the consideration of governments; but this would require the necessary political impulse.

In the present conjuncture, consideration should also be given to the possibility of establishing a regional unit of account which would facilitate the settlement of balances in services trade, including tourism, and of financial documents deriving from intra-regional merchandise trade. As regards services, a system is conceivable under which each individual country would issue documents expressed in a common unit of account, with its guarantee, convertible into each country's currency in accordance with the exchange provisions and rates in force in the country concerned. The same thing could be done in the case of documents underwriting long-term payments for intra-regional exports of goods, so as to facilitate this form of financing.

A bank such as that proposed, as well as

¹²A considerable proportion of the following statements and proposals are based on notes prepared by Carlos Massad, Director, Joint UNDP/ECLA Project on Implications for Latin America of the Situation of the International Monetary and Financial System.

¹³There is a very close precedent for this proposal in the ambit of the countries members of the Cartagena Agreement: i.e., the Andean Reserve Fund, which has played a salient role in the present conjuncture, by providing resources to some of the member countries, without subjection to 'conditionalities' of any kind.

the common unit of account, may have dynamic effects on regional integration.¹⁴

In the field of financial co-operation to promote development, the loss of importance of the international public banks in the present structure of international financing is a very serious matter. Latin America must strive to reinforce the Inter-American Development Bank financially, so that in its turn it can strengthen its role as promoter of regional investment.

There is an obvious need for long-term capital contributions, such as those made by IDB, to promote co-operation in areas where production must be vigorously encouraged. Cases in point are the capital goods, energy and food security sectors.

At the Annual Meeting of the Board of Governors of the Bank, held in Panama early in 1973, the Sixth Replenishment of Resources was approved, in a resolution adopted by the Committee of the Board of Governors. The increase provided for is US\$ 15 billion in the authorized capital and 703 million in the resources of the Fund for Special Operations. Another subject of discussion was the creation of a mechanism—the Inter-American Investment Corporation—directed towards financing Latin American enterprises, with particular emphasis on the private area.

There is another special aspect of IDB's action which would also repay overhauling. The Bank's technical co-operation programme, which is generally run by consultants from the non-borrowing countries, could make more room for the participation of consultant firms from the Latin American countries, at least in respect of that part of financing which does not correspond to trust funds. This idea is prompted by the increase that has taken place in the proportion of the goods and services purchased with the Bank's convertible currency resources

represented by those of extra-regional origin—a trend clearly at variance with co-operation and integration efforts at the regional level. In 1973, purchases from extra-regional markets of origin amounted to 40% of those effected with funds lent by the Bank, and in 1981 this proportion rose to almost 60%.¹⁵ It would be advisable to reverse this trend, above all if the purchasing power of the Latin American governments is to be used to divert trade towards regional suppliers.

A common strategy needs to be concerted, which would make it possible to enlarge the institution's regular funds, and at the same time permit increased participation of regional firms of consultants in the formulation of new investment projects.

By way of corollary, it may be asserted that financial co-operation at the Latin American level has become an imperative need. Since capital resources have to serve as the means to attainment of specific economic and social development objectives, it is urgently necessary to initiate at the earliest possible moment, a preparatory phase of consultations at the political and technical level, which would be the prelude to an eventual meeting of the regions' Ministers of Finance where specific proposals like those mentioned could be put forward, so as to permit the adoption of decisions appropriate to present circumstances and to world and regional economic prospects.

4. *Possibilities of action in the sphere of regional development and economic security*

There are measures associated with regional co-operation which are of great importance for buttressing the economic and social structuration of the Latin American countries, and which affect, in the long run, the autonomy, the dynamism and even the equity of Latin American development. The aim of this section is to set forth a group of areas of particular significance for the economic security and the development of Latin America as a whole.

¹⁴What would be needed would be the political decision on the part of the governments to tackle such a proposal, and they would have to take into account that this is no mere matter of creating a new Latin American institution, but a question of filling an existing gap. They may even take a gradual succession of steps in this direction, should it not be possible or viable to assign such a bank all its functions simultaneously.

¹⁵See G. Ondarts and C. Correa, *Compras estatales e integración económica*, *op. cit.*, p. 45.

a) *Regional co-operation in the field of capital goods*¹⁶

The region as a whole constitutes an important market for capital goods. In the first nine years of the 1970s, investment in machinery and equipment on the part of 8 countries (Argentina, Brazil, Mexico, and the five members of the Andean Group) averaged an annual sum of US\$ 40 billion (at 1980 prices), and in 1978 exceeded 50 billion. Not more than 50% of aggregate demand is met from within the region itself, which points to the existence of a considerable field for the application of concerted measures.

A substantial proportion of purchases of goods of this type is effected by State or State-controlled entities, which, in view of the small number of actors involved, would facilitate a possible co-ordination of measures, given the existence of the necessary political will.

These measures might be directed towards the following ends:

i) Obtaining better terms for external supplies, by demonstrating the magnitude of regional demand through *joint purchasing* programmes, a step which, furthermore, would permit the real exercise of a purchasing power with modalities and purposes already commented upon in earlier pages;

ii) Partly reorienting this demand towards the region itself, by raising —qualitatively and quantitatively— the level of activity of the local metalworking industry.

In both respects, more significant results will be obtained in so far as very specific information is available on equipment requirements and local capacity to meet them.

Some countries promote local production of capital goods through organizations grouping the public and private entities that are interested in the progress of the sector. The encouragement of such promotional entities and their

systematic interrelationship will conduce to a more lively perception of the opportunities opened up by joint activity, as regards both bargaining with third parties and forming combinations of production capacity; it will also facilitate removal of the obstacles which prevent these opportunities from being turned to account. Outstanding among such difficulties is the lack of financing mechanisms for internal sales, and the consequent hindrance of Latin American industry from participating in the construction and sale of whatever equipment it is capable of offering in conditions comparable, in terms of quality and price, with the external supply.

In the unfavourable conjuncture through which Latin America is passing today, not only is it harder for the capital goods industry to make headway, but the very survival of the manufacturing capacity that has by now been achieved in some countries is being jeopardized. A joint survey of the region's requirements as compared with its own capacities might help to avert the loss, in consequence of the present recession, of assets which it would be difficult to recover, such as specialized teams whose education training and maturation entail more time and effort than are necessary to ensure the availability of physical production equipment.

All this should be regarded as a problem of regional interest. A weakening of the industrial base would reduce the region's capacity for self-determination and would signify a general impoverishment; but it is also obvious that a collective effort to forestall such harm entails a certain measure of shared sacrifice, which could only be secured if compensatory mechanisms existed in favour of countries where manufacturing industry does not exist or is still embryonic.

In the case of certain sectors of demand linked with large-scale projects, clearly located in time and space, consideration might be given to mechanisms deriving precisely from the execution of works that help to distribute the benefits of collective action.

An outstanding case in point is that of hydroelectricity, since in the first place, it involves less likelihood of over-investment and, secondly, the repercussions of the corresponding civil engineering works may have a positive impact on various important sectors that also need activation —steel-making, cement and construc-

¹⁶A substantial part of the following material is based on notes prepared by Salvador Lluch, Co-ordinator of the ECLA Project on Capital Goods. For a more complete analysis of the subject, see Jorge Beckel and Salvador Lluch, "Capital Goods. Size of markets, sectoral structure and demand prospects in Latin America", *CEPAL Review* No. 17, August 1982.

tion: equipment, *inter alia*—, with the consequent increase in employment.

For co-operation in the field of capital goods to become more deeply and firmly rooted in the economic life of the Latin American countries, its promotion will have to be continued on the basis of active participation by the entities grouping private enterprises set up with Latin American capital. These, in turn, could unify their purchasing power in the world market and participate in it on preferential terms as Latin American sellers of the same goods. In particular, regional private enterprises supplying capital goods could join up with one another in entrepreneurial associations of a regional character. There they could unify positions, concert common strategies in their bargaining with the transnational corporations and identify manifold forms of co-operation which would enable them to increase their competitiveness at the regional and international level.

b) *Co-operation in the field of food security*¹⁷

In Latin America the production and marketing of food products—at the regional level—betray features that are clearly unsatisfactory and susceptible of improvement through co-operation.

It is easy to see how important the subject is, not only for regional economic security as a whole, but also with respect to combating the critical poverty which is still deplorably prevalent in Latin America.

Although the growth of production outstrips that of the population, it does not suffice to meet the increase in the effective demand for food and, still less that of potential demand, represented by over 50 million victims of malnutrition who lack the necessary purchasing power to carry any weight in the market, because of the vices apparent in income distribution. Actual output falls far short of production capacity, of which only one-third is utilized. Peasant farmers have lacked adequate access to appropriate forms of land tenure, as well as to technical advisory assistance in the spheres of

production, marketing and financing, in contradistinction to entrepreneurs in the modern sector of regional agriculture. This has aggravated the polarization of agricultural producers.

There are some Latin American countries suffering from food shortages which import from the world market the very same products that, concurrently, other Latin American countries with surpluses are exporting. Recognition of this fact is essential for the formulation of guidelines in the sphere of co-operation in production and trade. On the one hand, the region's capacity for food production is underutilized, and on the other, the contribution of imports to regional food supply rose from 9% to 13% in the past seven years. Intra-regional trade in food—which accounts for 30% of total Latin American imports of such products—is therefore susceptible of a vigorous forward thrust.

Almost two-thirds of these imports come from the developed countries and are concentrated in a few types of food—cereals, oilseeds and milk products—, which shapes the form of food dependence faced by the region as a whole. This dependence is aggravated by the concentration of such supplies in a small group of transnational corporations—especially in the case of cereals—and by subsidies to production and exports in the countries of origin, circumstances which distort competition and discourage the corresponding national lines of production.

In short, Latin America needs to step up, at the regional level, its quantum of food production and self-sufficiency, both in order to meet its own unsatisfied demand and with a view to reducing vulnerabilities which might, in certain situations, affect regional economic security and the attributes of national sovereignty. The expansion of food production should lie at the basis of every social nutrition policy aimed at overcoming the serious regional dearths in this field. The diversion and creation of trade flows in food among the Latin American countries may thus give considerable impetus to Latin American co-operation and integration.

The main causes of food insecurity—insufficient production, aggravated by cumulative annual shortages, inadequate or non-existent reserves and emergency imports at relatively

¹⁷Much of the following material is based on notes prepared by Luis López Cordovez, Director, Joint ECLA/FAO Division, on the subject of food security.

high costs— are common to most of the countries of the region, a fact which unquestionably facilitates concerted measures in this field. Information and alerting systems are necessary which will enable deficit countries to obtain imports more rapidly from other Latin American countries with surpluses. Here too comes into play the possibility of improving bargaining conditions in the world market through joint purchases. Last but not least, concerted efforts must be made to increase food production through the exchange of experience, technologies and specialists, as well as through common programmes to induce the utilization of idle production capacity. Perhaps in the short run regional co-operation with emphasis on pre-production aspects —regionalization, credit, productivity, etc.— may have more beneficial effects on regional food security.

c) *Co-operation in the field of energy*

It would be hard to overlook the supreme significance of the energy question in the study of the dynamics and orientation of Latin America's economic development. The importance of hydrocarbons in fuel supplies and their rising costs on the world market have involved, for many countries, familiar problems in the shape of trade deficits, inflationary pressures and inadequate supplies of fuel.

The inescapable need to diversify sources of energy has a variety of repercussions on the patterns of Latin America's future development. The lengthy period during which the world enjoyed mass supplies of petroleum at unjustifiably low prices whipped up a wave of products deriving from the petrochemical industry —or containing various inputs of petrochemical origin—, such as plastics, detergents, fertilizers and various types of man-made fibres. The greater part of overland, air and maritime transport was based on fuels obtained from petroleum, and many of the technologies applied in the construction of housing and in the production of durable goods made abundant use of materials of petrochemical origin. The preference for private cars, and the types of material used as inputs in their production, are of course among the consequences of the past era of cheap petroleum.

Coal, natural gas and various organic compounds of agricultural origin are competing with petroleum in the generation of fuels for internal-combustion engines and in the processing of materials which used to be the exclusive domain of the petrochemical industry. Similarly, solar, aeolian and nuclear energy are gaining ground in the energy panorama of today.

In the case of Latin America, a separate paragraph is deserved by the generation of hydroelectric energy, in view of the immense potential available.

Impressive progress has been made on some of these fronts during the past decade; cases in point are the Itaipú, Yacretá and Salto Grande projects, and others envisaged in the field of joint utilization of hydro resources.

Great strides have also been made in respect of petroleum. The PETROLATIN project sponsored by the petroleum enterprises of Brazil, Mexico and Venezuela, as well as the association between Mexico and Venezuela is an aid programme for supplying petroleum to Central America and the Caribbean (San José Agreement), are examples of what Latin America can do in the sphere of energy, given the necessary political will on the part of its governments.

The development of energy resources on bilateral, multinational or regional bases is not easy to concert, but may have beneficial repercussions on the profitability of investment and security of supplies.

In the area of hydroelectric energy, Latin America was utilizing, at the end of the 1970s, less than 10% of its available potential. There is an obvious need to advance along this path by establishing co-operation systems for the evaluation and planning of hydroelectric resources; for the more efficient utilization, management and conservation of hydrographic basins pertaining to two or more countries; for the interconnection of hydroelectric systems; for the development of the engineering and of the firms of consultants that these purposes require; for the improvement of bargaining capacity in respect of the purchase of equipment not available in Latin America; for the training of personnel in the hydropower area, etc.

For many of these objects of concern provision is made in a Latin American programme

on co-operation in the field of energy (Programa Latinoamericano de Cooperación Energética - PLACE), adopted at a meeting at ministerial level of the Latin American Energy Organization (Organización Latinoamericana de Energía - OLADE) held in Santo Domingo in 1981. It should be mentioned that OLADE—which co-ordinates the activities of PLACE—was founded in 1973, before the outbreak of the petroleum crisis, thus giving proof of early regional concern with the energy problem. Today, in the era of the quest for new sources of energy, the role of OLADE is revitalized in everything relating to regional co-operation in this field.

d) *Final considerations*

Unquestionably, the areas of co-operation described above are only some of the spheres in which concerted regional action can be taken to the benefit of the economic security of the Latin American countries and of the fuller and more diversified development of their production systems. At all events, the areas selected—trade, financing, food and energy—are the cornerstones of any programme aimed at reducing the region's external vulnerability. The capital goods industry, too, is one of the least advanced branches of production in the Latin American manufacturing sector, so that its development should be made one of the key objectives of regional co-operation.

It would seem inappropriate to bring this essay to an end without first stressing an aspect which has traditionally hindered the multilateral undertakings upon which Latin America has embarked: i.e., the well-known heterogeneity of the countries forming the region. The inequalities in the extent of their territories and in the size of their populations, as well as the differences in their degrees of development and their institutional and political structures make it essential to take a realistic view of the effective capacity for concerted action of this part of the developing world. At all events, as these characteristics not only exist but have been gradually aggravated in the course of Latin America's history, it is possible that the force of circumstances created by the crisis may induce governments and peoples to adopt a more 'Latin-Americanist' position, which will enable the region to surmount the obstacles raised by heterogeneity and make unhampered use of its joint potentialities.

This will mean that in programming to find a way out of the economic and social emergency priority will have to be given to considering the situation of the economically less developed Latin American countries, so that they may not be so much harder hit by the crisis than the rest, and proof may be afforded that the solidarity asked from the developed world also 'begins at home'.

Renegotiation of Latin America's debt:

An analysis of the monopoly
power of private banks

*Robert T. Devlin**

In 1982 Latin America began to encounter serious difficulties in servicing its external debt and by mid-year most of the countries heavily in debt to the international private banks—their leading creditors—initiated negotiations to reprogramme payments. The Latin American debt was contracted during the 1970s in a highly competitive and expanding capital market, which afforded the countries an opportunity to obtain abundant loans on favourable terms. In view of the present depressive international conjuncture, however, many banks have stopped lending to Latin America. The flow of credit has therefore been severely reduced, and the market has been left in the hands of a few large international banks whose main activity has been the administration of their existing portfolio through the reprogramming of amortization and the refinancing of part of the interest payments, which has led to a drastic deterioration of credit terms and a substantial rise in the cost of borrowing. The present study maintains that this increase in the cost of the debt as a result of the renegotiation is nothing but a monopoly rent which is extracted from the countries by virtue of the emergence of a non-competitive capital market. It is suggested here that countries should explore ways of eliminating—totally or partly—these superprofits, because, in so far as they are rents, their non-payment should not prevent reprogramming of the debt or future access to credit.

In contrast to what happened during the 1930s, the so far abrupt of the cost of weathering the financial crisis has been borne by the debtor countries, a politically untenable situation. To forestall the defaults that everyone would wish to prevent, formulas are suggested which may perhaps permit a more equitable distribution of the cost among the banks, their governments and the debtor countries.

*Economic Development Division, ECLA.

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I

Introduction

Latin America's present debt crisis is very widespread. Since mid-1982 more than half the countries of the region have sought debt relief from their main foreign creditors: the international private banks (see table 1). Whereas the scope of the present crisis has had no precedent since the Second World War, there is nothing new, in contrast, about the problem of servicing bank debt, or the consequent need to reprogramme it. Before payments difficulties—which were highlighted in August 1982 when Mexican authorities officially recognized servicing problems—began to be a matter of general concern, a good many countries of the region which had contracted substantial debts with the private banks had already been faced with a debt crisis. During the 1970s Peru, Nicaragua, Bolivia and Jamaica were unable to meet their external debt commitments and accordingly decided to request from their private creditors a common formula for the relief of their situation.

Although the majority of the new requests for rescheduling are still being dealt with, they largely follow the general lines laid down by the private banks when the above-mentioned countries found themselves up against debt crises in the 1970s. Table 2 presents selected data on the agreements reached with the private banks by those Latin American countries that met with payments difficulties during the past decade. The study of these cases—together with others outside Latin America, such as those of Zaire and Sudan—makes it possible to sketch some essential features which give an idea of the character of the agreements concluded:

a) Negotiations between the private banks and the debtor country constituted a very slow and at times highly conflictive process and it took one or two years to reach the final agreements;¹

¹See W. Glasser and D. Roberts, "Bank lending to developing countries. Problems and prospects", in *Federal Reserve Bank of New York Quarterly Review*, Autumn, 1982, p. 27; and R. Devlin, *Los bancos transnacionales y el financiamiento externo de América Latina: La experiencia del Perú, 1965-1976*, Santiago, Chile, United Nations, 1980, E/CEPAL/G.1124, pp. 201-204.

Table 1
LATIN AMERICA: PROVISIONAL DATA ON THE RENEGOTIATION OF THE
EXTERNAL DEBT OF SELECTED COUNTRIES TO PRIVATE BANKS

(Billions of dollars)

Country	Global debt at end of		Renegotiation of the debt ^a			Credits approved during 1982 and January-April 1983			
	1981	1982	Initiation of negotiations	Amount	Maturities rescheduled	IMF BIS USA			New private bank credits
Argentina	35.7	38.7	Sept. 1982	13.00 ^b	Sept. 1982-1983	2.2	0.5(s)	—	1.1 bridge loan, 1.5(s)
Bolivia	2.5	2.8	Oct. 1982	... ^c	...	0.3(s)	—	—	—
Brazil	71.9	80.2	Dec. 1982	4.70 ^d	1983	6.0	1.2	1.5	4.4
Costa Rica	3.5	4.2	Sept. 1981	0.70 ^e	1982-1983	0.1	—	—	—
Cuba	3.2	...	Sept. 1982	0.34 ^f	Sept. 1982-1983	—	—	—	—
Chile	15.9	17.3	Jan. 1983	3.30 ^g	1983-1984	0.88	0.3	—	1.3(s)
Ecuador	5.9	6.3	Oct. 1982	2.48 ^h	Nov. 1982-1983	0.17	—	—	—
Honduras	1.7	1.9	July 1982	0.23	...	0.11	—	—	—
Mexico	72.0	81.4	Aug. 1982	20.00 ⁱ	Aug. 1982-1984	3.97	1.85	2.0	5.0
Nicaragua	2.2	2.4	... 1982	0.56 ^j	...	—	—	—	—
Peru	9.7	11.6	Jan. 1983	2.40 ^k	1983	0.94	—	—	0.45(s)
Dominican Republic	1.9	1.9	... 1982	0.15	...	0.46	—	—	—
Uruguay	3.1	4.0	Feb. 1983	0.71 ^l	1983-1984	0.46	—	—	0.24
Venezuela	28.0	30.0	Oct. 1982	15.80 ^m	1983-1984	2.8(s)	—	—	—

Source: ECLA, on the basis of official information supplied by countries and by various national and international sources.

Note: New credits are those granted by the international banks during the renegotiation process; (s) = solicited credits; BIS = Bank of International Settlements.

- ^a As at 30 April 1983, most of the countries were in the midst of renegotiation operations, and although significant progress had been made, the process had not been finalized.
- ^b Corresponds to amortization of public debt from 1982 and that falling due up to December 1983 (US\$ 6 billion). It also includes the private external debt guaranteed by Central Bank exchange rate insurance and maturing as from November 1982 (US\$ 5.5 billion), as well as to maturities relating to "swaps" (US\$ 1.5 billion).
- ^c At the end of March 1983 the international banks agreed to defer amortization and interest payments amounting to US\$ 460 million, a plan that will be formalized by the signature of an agreement.
- ^d At the end of 1982 a request was submitted to the foreign banks for new loans and refinancing amounting to US\$ 4.4 billion and US\$ 4.7 billion respectively. In February 1983 the international banks acceded to this request.
- ^e At the end of April 1983 it was reported that a provisional agreement had been signed with the leading creditor banks.
- ^f In August 1982 a request was submitted for postponement of the external debt service payments falling due between September 1982 and December 1983. In March 1983 an agreement was reached with the creditor banks for refinancing to the amount of US\$ 140 million.
- ^g Includes amortization payments falling due in the course of 1983 and 1984 (US\$ 2.1 billion) and the restructuring of short-term financial credits (US\$ 1.2 billion). At the end of April the government stated that it had reached an agreement with the 12 principal creditor banks on debt rescheduling and that negotiations were continuing with a view to obtaining new credits. While the renegotiation process is being completed the banks will extend for a further three months the postponement of payments granted on 1 February 1983.
- ^h Corresponds to servicing of the public debt between 1 November 1982 and 31 December 1983 (US\$ 1 220 million) and about 80% of the private debt (US\$ 1 260 million). In January 1983 an agreement was concluded with the international banks for the renegotiation of the public debt. Between October 1982 and January 1983 Ecuador, by common agreement with its creditors, had made no payments against the public debt.
- ⁱ Corresponds to the postponement of amortization payments authorized by the international banks on 20 August 1982 for a period of three months, subsequently extended to 23 March 1983. In February 1983 part of the external debt was renegotiated, at a period of eight years (a four-year grace period), being secured for the payment of US\$ 20 billion representing commitments between August 1982 and December 1984. Since renegotiation has not been fully completed, a further extension of the postponement of amortization payments up to August 1983 was requested.
- ^j During 1982 renegotiation for this sum was concluded.
- ^k This refers to the refinancing of short-term debt to the amount of US\$ 2 billion obtained in March 1983 and a request to refinance amortization representing US\$ 430 million in the same year.
- ^l Corresponds to 90% of the amortization of short- and medium-term credits falling due in 1983 and 1984. At the beginning of March payments had been postponed for 90 days in agreement with the creditor banks. In April 1983 an agreement was reached with the committee of creditor banks.
- ^m Relates to the short- and medium-term public and private debt which it is desired to convert into a long-term debt with new guarantees. At the end of March the government stated that it will postpone amortization payments corresponding to April-June 1983.

Table 2
LATIN AMERICA AND THE CARIBBEAN: DEBT RENEGOTIATION AGREEMENTS WITH
PRIVATE BANKS THAT PRECEDED THE MEXICAN CRISIS

Country	Year	Amount reprogrammed ^a (millions of dollars)	Period covered by extension of maturities (number of years)	Amortization period (number of years)	Grace period (number of years)	Margin over LIBOR (%)	Commissions ^b (%)
Peru	1976	430	1	5	(2)	2 1/4	1 1/2
	1978	720	2	7	...	1 7/8	1/2
Nicaragua	1980	480	c	12	(5)	1-1 3/4 ^d	—
Bolivia	1981	250	2	7	(4)	2 1/4	1 1/8
Jamaica	1982	88	2	5	(2)	2	1 1/2
							1 1/2 ^e

Source: Peru: R. Devlin, *Los bancos transnacionales y el financiamiento externo de América Latina: La experiencia del Perú, 1965-1976*, Santiago, Chile, United Nations, 1980, E/CEPAL/G.1124, pp. 170 and 203.

Nicaragua: R. Weinert, "Nicaragua's debt renegotiations", in *Cambridge Journal of Economics*, Vol. 5, No. 2, June 1981, pp. 187-192.

Bolivia: R. Devlin and M. Mortimore, *Los bancos transnacionales, el Estado y el endeudamiento externo de Bolivia*, Santiago, Chile, United Nations, Estudios e Informes de la CEPAL, No. 26, E/CEPAL/G.1251, 1983, p. 67.

Jamaica: Q. Peck Lin, "The borrower's trump card is his weakness", in *Euromoney*, October 1982, p. 37.

^a Excluding amounts and terms of payment for that part of the debt which was in arrears.

^b Expressed as percentages of the face value of the loan and represents a flat payment at the time of signing the contract.

^c The entire outstanding balance of the bank debt was rescheduled.

^d The margin gradually increases from 1% to 1.75% while the agreement is in force, ending with an average of under 1.5%. Nicaragua pays a maximum rate of 7% up to the end of 1985. The difference between the current interest rate and the 7% ceiling will be capitalized and amortized between 1986 and 1990.

^e Paid at each maturity date.

b) Whereas the countries had originally contracted their debt in the highly competitive and dynamic credit market of the 1970s, when they began to have difficulties with debt servicing the credit environment deteriorated, since each bank attempted, on its own account, to reduce the borrower's participation in its loan portfolio; thus it was only a small group of very large banks that had to assume responsibility for seeking a common formula to tackle the problem;²

c) The time horizon of the private banks' plan was very limited; i.e., the relief formula provided for an extension of only one or two years of maturities; furthermore, only amortizations were reprogrammed, since the banks insisted that the borrower should not alter the schedule of interest payments;

d) The renegotiation of the debt was

linked to the attainment of a stand-by programme with the IMF;

e) The 'rescue' of borrowers did not include new loans; in effect, the renegotiation *per se* had a negative impact on a country's creditworthiness. Only in one case (Peru) was the borrower subsequently able to regain normal access to external credit; and this, owing to a vigorous reactivation of the country's external sector—mainly thanks to a rise in the prices of mining products, especially petroleum, in 1979-1980—which revived bankers' interests in loan operations;³

f) In renegotiation agreements the countries had to reckon with substantial increases in spreads over the London Interbank Offer Rate (LIBOR) and pay heavy commissions to the private banks on the occasion of signing the corresponding contracts;

²R. Devlin, "Commercial bank finance from the North and the economic development of the South: congruence and conflict", in *CEPAL Review* No. 9, Santiago, 1979, p. 69.

³See R. Devlin, *Los bancos transnacionales...*, E/CEPAL/G.1124, *op. cit.*, p. 204; and W. Glasser and D. Roberts, *op. cit.*, p. 27.

g) During negotiations the private banks exerted influence, in various ways, on the economic policy of the country concerned;⁴ and, lastly,

h) As a rule, the original renegotiations were followed by successive similar operations,⁵ since the relief afforded by the private banks did not lighten the debt burden sufficiently to prevent a rapid recrudescence of debt servicing difficulties; all this, of course, resulted in additional costs for the borrower.

A very significant departure from this general pattern is to be found in one case, that of Nicaragua. The agreement concluded by the Nicaraguan Government in 1981 is of great importance because it established a new principle in the field of renegotiation of external debt. When other countries encountered payments difficulties, the banks rescheduled the debt to avert the precedent of a default. But when they granted a restructuring of maturities, they applied strictly private payment criteria; that is, their aim was to minimize their own risks, to maintain or increase the rate of return on their assets and to impose a measure of 'discipline' on the borrower. The resulting agreement was extremely burdensome for the debtor, and left little or no room for economic growth. In con-

trast, the reprogramming of Nicaragua's debt was largely based on development criteria, as is reflected in the fact that it included a lengthy postponement of a considerable proportion of interest payments and unusually long maturities.

The characteristics of the Nicaraguan agreement can be appreciated in table 2 and in the article by R. Weinert cited in that table. For the purposes of the present paper, a singular feature should be highlighted: the economic authorities of Nicaragua managed to pay neither an increase in the margin over LIBOR nor commissions to the banks on the amount of the rescheduled debt. The present analysis — although it is in any event only a first step in complicated terrain — argues that commissions, increased spreads over LIBOR, and other forms of raising the cost of credit on rescheduled debt are no other than monopoly rents, or superprofits, gained by the private banks. Consequently, the Latin American countries that are currently renegotiating their debt might seriously explore means of totally or partly eliminating these rents — as Nicaragua has already done —, through negotiation of debt reschedulings that do not imply the payment of commissions or increases in the margin over LIBOR.

II

Is there any economic justification for the spreads and commissions charged by the private banks in debt reschedulings?

The Nicaraguan plan should have served as a general pattern for the rescheduling of Latin America's external debt; but unfortunately this has not happened. The renegotiation which im-

mediately followed that of Nicaragua was the one embarked upon by the Bolivian military government under the presidency of General García Meza, in 1980-1981. This country showed many signs of insolvency which made it eligible for a relief formula in the spirit of the Nicaraguan agreement. But that shaky government, which was seeking international legitimation, was willing to accept a rescheduling arrangement at virtually any price. The result was an unrealistic reprogramming of the debt which did nothing to help stabilize the balance of pay-

⁴See R. Devlin, *Los bancos transnacionales...*, *op. cit.*, pp. 162-204; and R. Devlin and M. Mortimore, *Los bancos transnacionales, el Estado y el endeudamiento externo en Bolivia*, Santiago, United Nations, Estudios e Informes de la Cepal, No. 26, E/CEPAL/G.1251, 1983, Chapter 4.

⁵See W. Glasser and D. Roberts, *op. cit.*, p. 27.

ments, and of which, moreover, the cost for the country was very high (see again table 2).⁶

During the present debt crisis, Mexico is the country that seems to be nearest to finalizing a reprogramming operation with the private banks. But once again the terms of the agreement are very burdensome. According to provisional data, the US\$ 20 billions of amortization payments subject to reprogramming will be financed at the cost of a margin of 1.88% over LIBOR and flat commissions of 1% on the amount rescheduled.⁷ Furthermore, the private banks will grant a 'new' loan for US\$ 5 billion, which in practice is a disguised way of rescheduling part of the interest payments on the outstanding debt. The cost of this last 'loan' will be 2.25% over LIBOR and flat commissions of 1.25%.⁸ And since Mexico was accustomed to paying an average margin of approximately 0.65% over LIBOR and commissions of 0.7%, the need to reschedule the debt induced that part of the cost of credit which is subject to negotiation to increase by over 180%⁹ (see table 3).

In most respects the rescheduling of Mexico's debt follows the general pattern outlined in the introduction. Its new feature is that the private banks—under severe pressure from the International Monetary Fund—are now granting the aforesaid 'new' loans to accompany the rescheduling of certain maturities. But, as was also pointed out above, the loan does not imply additional net autonomous resources for investment or for the accumulation of international reserves; rather it is administratively designed by the bankers to permit normal payment of interest in the absence of an official rescheduling of these commitments.¹⁰

In some circles the Mexican formula has

⁶See R. Devlin and M. Mortimore, *op. cit.*, chapter 7.

⁷See *Latin American Weekly Report*, London, 24 December 1982, p. 1.

⁸*Ibidem.*

⁹LIBOR is determined by the forces of supply and demand in the financial market. The cost components subject to negotiation are the following: the margin over LIBOR, flat commissions and the amortization period.

¹⁰Up to now the private bankers have firmly adhered to the principle that interest payments must not be reprogrammed. This attitude partly reflects their concern lest if they reschedule interest payments their government ban-

king authorities may classify loans as non-performing assets. Thus they resort to indirect procedures to serve the same end.

been mentioned as the model that should be followed by other countries in the region for rescheduling their payments to the private banks. In practice, as is clear from table 3, this model is pretty close to what is actually happening in Latin America. Reprogramming terms are very similar for all countries despite the considerable differences in their capacities to pay. The relative deterioration of credit terms for the other countries of the region is not as grave as for Mexico, inasmuch as the latter started with more favourable terms of borrowing; but in any event, the deterioration is serious in almost all cases.

Obviously, the Mexican model ought not to have been taken as a reference point for considering the terms of the region's debt rescheduling. Mexico accepted a substantial rise in the spread over LIBOR and the payment of commissions on the reprogrammed debt. As will be explained later, in that country's particular circumstances it may possibly have been expedient for the authorities to accept these costs; but it is not necessarily the correct formula for all the other Latin American countries.

While ethical arguments can be invoked to dissuade the private banks from increasing the cost of rescheduled debts, there is also an economic argument which calls this practice in question. Higher spreads and commissions paid on reprogrammed debt and interest represent monopoly rents for the private banks, which theoretically, and in practice too, can be appropriated by the borrower countries. It is possible, moreover, that non-payment of these rents may have no significant negative effect on the supply of external financing.

In the first place, the margin over the base interest rate and the commissions are components of the 'negotiated' cost of credit.¹¹ In a normal international credit market this cost is established in a distinctly competitive environment, since a solvent borrower country has many potential creditors.¹² Accordingly, in a

king authorities may classify loans as non-performing assets. Thus they resort to indirect procedures to serve the same end.

¹¹See again footnote 9.

¹²A country like Bolivia, whose prestige in international financial markets has always been relatively low, had

Table 3
LATIN AMERICA: PROVISIONAL DATA ON TERMS OF DEBT RESCHEDULING^a

Country	Margin over LIBOR (percentage)			Amortization period (number of years)			Grace period (number of years)			Commissions ^b			Deterioration of terms (percentage) (2):(1) ^c
	1980-1981	R	AC	1980-1981	R	AC	1980-1981	R	AC	1980-1981	R	AC	
	(1)	(2)		(1)	(2)		(1)	(2)		(1)	(2)		
Argentina	0.67	2.13	2.5	7.5	7.0	5.0	...	3.0	3.0	1.09	...	1.25	...
Brazil	1.62	2.50	2.13	8.5	8.0	8.0	...	2.5	2.5	2.01	1.50	1.50	44
Chile	0.91	2.13	2.25	7.6	8.0	7.0	...	4.0	4.0	0.81	1.25	1.25	125
Costa Rica	1.13	2.25	-	6.0	8.5	-	...	3.0	-	1.23	...	-	...
Cuba	1.00	2.25	-	5.0	8.0	-	...	3.2 ^d	-	0.88	1.25	-	28
Ecuador	0.74	2.25	-	8.0	9.0	-	...	2.0	-	0.97	1.25	-	146
Mexico	0.65	1.88	2.25	7.6	8.0	6.0	...	4.0	3.0	0.70	1.0	1.25	181
Peru	1.12	2.25	2.25	8.2	8.0	8.0	...	3.0	3.0	1.07	1.25	1.25	97
Uruguay	0.98	2.25	2.25	9.1	6.0	6.0	...	2.0	2

Source: ECLA, on the basis of official data and information supplied by various national and international sources.

^a This information is provisional and subject to revision. Columns headed 1980-1981 show average credit terms in 1980 and the first half of 1981. Columns headed R relate to rescheduled maturities. Columns headed AC relate to terms for additional credits. It should be noted that by the end of April 1983 most of the new credits had not been agreed upon and were still at the proposal stage.

^b Calculated as percentages of the face value of the loans and represents a flat payment at the time of signing the loan contracts.

^c Based on an index of the cost components of credit that are subject to negotiation

$$\frac{\frac{C_2 + M_2}{P_2}}{\frac{C_1 + M_1}{P_1}} - 1$$

where:

C = commissions; P = amortization period; M = margin over LIBOR; all of which are weighted by the amount of the loan. It should be noted that the relative deterioration is not in itself an indicator of the quality of an individual country's negotiation, since it is strongly influenced by the initial position of the borrower.

^d Weighted average.

competitive setting like that in which most of the debt was contracted, the spread and commissions paid by the borrower must generate what for the private banks approximates a 'normal rate of profit', which takes into account a margin to cover risks.

In an advanced phase of the credit cycle, however, the borrowing country may find itself faced with debt service difficulties. In these circumstances, the financial market drastically tightens since many private banks try to reduce the amount of their portfolio in the country concerned. As was pointed out before, the country then finds itself in a non-competitive mar-

ket; the cost of credit will now be largely decided by the few large creditor banks that form a committee for negotiating *en bloc* with the borrower.¹³ The collusive nature of the committee invests the private banks with a monopoly power that did not exist at the time when the borrower originally contracted its debt.

In reality, this situation approximates a bilateral monopoly. In other words, the banks and the borrower country open negotiations with one another to decide how the losses will be shared out. The outcome of this situation is uncertain. But the action of the private banks is clear: raising the price of credit on rescheduled debt is a device for shifting on to the debtor

more than a hundred private creditors in 1974-1978. See R. Devlin and M. Mortimore, *op. cit.*, p. 69. Countries whose prestige in financial markets is traditionally high could deal with more than a thousand private banks.

¹³See R. Devlin, "Los bancos comerciales...", *op. cit.*, p. 84. For an analysis of a specific case, see, by the same author, *Los bancos transnacionales...*, *op. cit.*, pp. 163-173.

much of the cost of a weak loan portfolio. In so far as the bank avoids losses—or manages to obtain positive returns—on its weak portfolio, it gains profits tantamount to a monopoly rent.

When a bank issues a loan in a normal market, the risk is theoretically covered by credit rationing, and the charge of a margin over the base interest rate, plus commissions. In other words, at the time of granting a loan, the bank already takes into account the possibility of not recovering it, or at least foresees that the mobility of its portfolio may be affected by a rescheduling of payments. Thus, when a borrower country cannot meet its debt service commitments, the cost to the bank must already have been included in the charges for the original loan. And as regards the reprogramming of the debt *per se* (or of the interest on it, either directly or indirectly), there is no real 'credit' transaction with a supply price, since the operation consists simply in the administration of a loan already granted and not immediately recoverable. Nor does rescheduling imply an additional risk, as bankers assert, since the alternative is a total stoppage of payments and the complete liquidation of part of the portfolio; in practice, rescheduling effectively reduces the risk of default and therefore of major losses. As for the outlays on telex, cables, travel, etc., connected with the negotiation of a rescheduling operation, the banks have already provided for their coverage in the loan contracts, in separate clauses under the head of 'miscellaneous expenses'. Thus, any increase in the margin over the base interest rate and payment of commissions on the amount reprogrammed signifies rent; that is, it constitutes an income in excess of economic costs, which is generated by virtue of the bargaining power of the few large banks that control access to credit for a country of questionable creditworthiness. Looked at from another angle, rent is any payment over and above what is required to induce an economic agent to act as it does. In this case, the bank charges extra for an administrative operation (the rescheduling of debt service) which is necessary in any event to avoid a total loss; therefore, the additional income it receives on reprogramming the debt is a superprofit.

What happened during the 1930s, i.e., when the debtor countries ceased to liquidate

their bonds unilaterally, demonstrates how, in similar competitive conditions, banks would have to accept the losses deriving from the development of an unsatisfactory portfolio, a course which would imply easing the debt burden of the borrower countries and would facilitate their economic recovery. Unlike the current financial instrument, the bond is a means of borrowing in which case the creditors are anonymous, many, and widely scattered, so that it is difficult for them to organize themselves and reach a collusive agreement *vis-à-vis* the debtors. Bondholders were left with no other alternative than to accept the losses determined by the market in the shape of a reduction of the value of their assets.¹⁴

Today, borrowing is channelled mainly through the private banks, and these institutions are in a position to co-ordinate their activities in the international scene in such a way that they can form a monopolistic bloc organized with the aim of averting, or minimizing, losses through: i) reschedulings of the debt and of interest payments; and ii) charging onerous spreads and commissions. In other words, in contrast to what happened during the 1930s, the cost of the adjustment necessitated by a less than adequate management of an international portfolio is now borne by the debtors and not, as before, by the creditors.

In certain circumstances it would be expedient for the borrower country to attempt, as Nicaragua did, to eliminate or reduce the rent paid to the private banks. This is feasible because, as will be seen later, a decline in the superprofits of the private banks, given specific situations, would not necessarily affect the supply of financing.

When debt servicing becomes impossible, the borrower country loses its creditworthiness and therewith its access to autonomous loans from the private banks. It seems that many countries accept the increase in the cost of credit in a reprogramming operation—i.e., pay the rents—in the fear that if they refuse to do so they will forfeit their chances of obtaining fi-

¹⁴This last aspect is discussed in a working paper by Carlos Massad.

nancing in the future.¹⁵ But in normal circumstances the flow of loans is not tied to the concession or non-concession of rents to creditors. Access to credit will then depend upon sound creditworthiness; in so far as a country can recover it, the number of private banks interested in lending to it will increase and the resurgence of competition among them will generate new loans at lower costs.¹⁶ And notwithstanding the negative attitude of bankers towards debt rescheduling, a major factor in the real recovery of creditworthiness is still—in addition to disciplined economic policies, of course—renegotiation of debt servicing in such a way as to reduce the burden it represents; this,

in turn, entails the borrower's not paying the rents and transferring to the lender some of the corresponding losses. Hitherto the creditor has avoided losses and has managed to oblige the debtor to pay rents which have militated against a recovery of creditworthiness and have been partly responsible for the necessity of multiple reschedulings with their additional costs for the borrower.¹⁷ In fact, instead of being a problem for the banks, rescheduling has definitely been 'good business'; thus a paradoxical situation arises where in the midst of a very serious deterioration of their international loan portfolio, the private banks are reporting to their shareholders very high rates of profit.¹⁸

III

Incentives to reduce the cost of rescheduling debt

In the short run, the incentives that the various countries have to accept the higher cost of borrowing involved in renegotiations may differ considerably, and this has major repercussions on rescheduling trends in the region.

In the case of the large countries with a very high absolute level of indebtedness—such as Mexico and Brazil—payment of the higher cost of credit might be expedient. And this because even in an 'administered' credit market,

which characterizes the situation for a State whose creditworthiness is precarious, the economic authorities may possibly think that a substantial volume of new loans can gradually be obtained, since, up to a point, the financial system is a 'hostage' to the borrower: a default by a major debtor would be a threat to the very survival of many banks. Thus, the economic authorities might feel that acceptance of the increase in the cost of outstanding debts would make it easier for them to use their considerable

¹⁵Another reason that may explain, if only in part, why some countries have paid the rent in question is that hitherto, in many instances, negotiations with the private banks have been co-ordinated by national technocrats (not by politicians) who have strong professional links with the international financial community. This situation makes for protection of the *statu quo* as regards debt rescheduling.

¹⁶Peru affords a case in point. Between 1976 and 1978 it had extremely serious conflicts with its private creditors and received no new loans for nearly two years. But despite its troubled relations with the private banks, the country found itself back in their good books when an unexpected rise in its export prices boosted its external sector and, therefore, its image of creditworthiness. See R. Devlin, *Los bancos transnacionales...*, *op. cit.*, pp. 167-172, and 201-204.

¹⁷In so far as the banks increase the cost of credit in a rescheduling operation, the recovery of creditworthiness becomes more difficult, since the borrower country will have to expand its exports still further and reduce its imports in order to cope with debt servicing. Creditworthiness is also prejudiced inasmuch as the cost of the debt rises when the internal rate of return is, in all probability, very low.

¹⁸See R. Lambert, "New York banks show strong gains", in *Financial Times*, 19 January 1983, p. 32; R. Banner, "Banks gain from fees by altering Latin debt", *New York Times*, 10 January 1983, p. D.3; J. Plender, "Of profits and imprudence", *Financial Times*, 18 February 1983, p. 5; and R. Wilkinson, "Banks greedy over Third World", *Financial Times*, 31 March 1983, p. 10.

leverage to extract increasing amounts of new credit from a non-competitive market.¹⁹ Another factor that perhaps influences the decisions of these relatively more developed countries is the consideration that they will be the first to benefit by the positive impulses of any world economic recovery that may occur in 1983 and 1984, with the consequent improvement of their creditworthiness accompanied by a renewed autonomous credit flow and the reduction in costs which this implies. Undoubtedly Mexico, when accepting the cost of its debt re-scheduling, assumed that it would relatively rapidly regain its access to credit, through autonomous or administered channels. If within a very short time there is no new net inflow of loans (i.e., a volume of credit in excess of amortization and interest payments), the cost of renegotiation will be more clearly revealed as a monopoly rent and, probably, in that case, the Mexican Government will reconsider its strategy for negotiation with the private banks.

While in the short run the most heavily indebted countries may have their reasons for accepting a rise in the cost of their debt, the creditor banks have motives for augmenting those costs to an onerous degree. And this because they know that the terms of payment established with the major debtors—which are also the countries with the best prospects of regaining their creditworthiness—will form the 'floor' for subsequent negotiations with smaller debtors that are less attractive customers. Thus, the strategies of the banks and of the major debtors in the region join forces in pushing up the cost of the debt for everyone. This, of course, has negative repercussions on the remaining countries.

As regards the small and medium-sized debtor countries, the potential benefits of paying the higher cost demanded by the banks are even more problematical. These countries'

chances of obtaining net inflows of resources through the private banks are much smaller. In a climate of administered credit they have not enough leverage to obtain more money for investment purposes, since individually their debt does not represent a high proportion of the banks' portfolio; in the last instance, creditors could cope with a unilateral moratorium on the part of a small debtor without endangering their own survival.²⁰ Thus, the banks have a firm foundation on which to resist a significant expansion of their portfolio in the country. But still more important is the fact that these countries will be the last to benefit by the return to a normalized international credit market when the world economy recovers. In the case of countries with structural debt problems—for example, Bolivia, Chile, Jamaica, Costa Rica—, even if the international conjuncture takes a favourable turn it will not necessarily suffice to restore their creditworthiness and give them renewed access to autonomous credit.

The preceding remarks suggest that these latter borrowers have less reason to accept the increase in the cost of debt currently at issue in the renegotiations; if they do so, in face of their poor prospects of a rapid and intensive recovery of creditworthiness—necessary for their reinsertion in a competitive credit market—they have few possibilities of demanding as a counterpart any very significant net flow of new loans. If the borrower holds out against an increase in the cost of the debt, its rescheduling will not necessarily be prevented. And this because, although the banks could absorb the losses that would derive from a formal declaration of default on any one country, it is very much in their interest to forestall a precedent of this kind. In the first place, such a declaration might lead to a similar standstill of debt payments on the part of other countries which, as a whole, certainly would represent a threat to the viability of the private banks. And secondly, since it is monopoly rents that are at stake, a policy that tries to obtain debt rescheduling without an increase in the cost of credit still affords the

¹⁹Resources are often extracted indirectly. Initially the country establishes very optimistic balance-of-payments targets in order to conclude a rescheduling agreement with the private banks. Subsequently the targets are not met with the consequent enlargement of the deficit on current account, which is in any event financed by the private banks (or by their governments) on the grounds of not inducing a moratorium in payments.

²⁰See for example, the cases of Peru and Bolivia, in R. Devlin, *Los bancos transnacionales...*, *op. cit.*, pp. 114 to 120, and R. Devlin and M. Mortimore, *op. cit.*, pp. 111 to 116, respectively.

private banks an opportunity to 'gain', i.e., substantially to minimize their losses. All that is really involved is a better distribution of costs between debtor and creditor, as compared with the situation in the 1930s, when the brunt of the

adjustment was borne by the creditors (who were not only banks), and with the present situation, which is characterized by the transfer of the cost of a weak portfolio to the debtor countries.

IV

Concluding remarks

It is worth while to recapitulate what has been said so far. The hypothesis upon which the present article is based calls in question the current practices of the private banks in renegotiation of the external debt, hitherto more or less taken for granted in many circles alike in the North and in the South. Obviously, this is only a first approximation to the subject, and the analytical framework should be extended in the near future both in depth and in breadth. In any case, the increase in the price of credit in current reschedulings of Latin America's debt is a clever tactic on the part of the private banks to evade the costs associated with a less than adequate international lending policy. Their capacity to raise the borrower's costs derives from the monopolistic power which characterizes an administered capital market; and the costs themselves would be rents.

The payment of rents has different effects on the two parties involved in the renegotiation. In the case of the banks, their rates of profit are high even in the face of a marked deterioration in the quality of their portfolio. And the debtors, for their part, are faced with a steep rise in the cost of the debt when their rate of return on investments can no longer carry the burden of servicing it; moreover, payment of the higher cost necessitates an increase in exports and a reduction of imports which are difficult for each country to achieve separately, and virtually impossible for all the debtors as a whole. It has also been noted that, paradoxically, in the short run it is the countries with the most bargaining power that have an incentive to initially shoulder the burden of the increased cost of credit, whereas the debtors with less leverage have less reason to

do so, and are in a better position to resist it forthwith.

Up to now the small and medium-sized debtor countries of Latin America have adopted a distinctly passive position *vis-à-vis* the demands of the private banks for exceptional increases in the margins over LIBOR and for the payment of commissions on the reprogrammed debt.²¹ But perhaps they ought to reconsider their strategy and explore other ways of negotiating a reduction or elimination of the rents paid to these transnational financial enterprises, as many of them have already done in the past with respect to direct investment by the non-financial transnational corporations. And as happened in the latter case, the possibilities of negotiating better terms will depend upon the specific political and economic circumstances of each individual country, on its capacity to co-operate with other debtors and on its success in obtaining the necessary backing from international forums concerned with co-operation and economic development in order to pressure the private banks to change their rescheduling policies.

As a minimum criterion it might be proposed that the negotiated cost of a reprogrammed debt should not be higher than the average of the original negotiated cost on the rescheduled maturities. And in the case of coun-

²¹Even an organ of the international financial press—the *Financial Times* of London—remarked in an editorial that the developing countries have a great deal of leverage with the private banks, but have shown little imagination in taking advantage of it. See "Third World leverage", *Financial Times*, 12 February 1983, p. 12.

tries with structural debt problems, a postponement of interest payments would be necessary, although a still more appropriate measure would be a significant reduction of the cost of credit, i.e., a 'concessionary' interest rate. Furthermore, the formula is not without precedent, since the private banks commonly grant 'soft' credit terms to their domestic customers with debt repayment difficulties, as is exemplified by the treatment of the Real Estate Investment Trusts in the United States.²² A yet more important point however, is that reduction of the rents implicit in the current debt rescheduling formulas still affords the banks an opportunity to avoid most of the losses that creditors would normally incur in a competitive capital market. It is simply a matter of a better sharing-out of the cost of a mismanaged portfolio between creditor and debtor, whereby both parties 'gain'. In addition, this improved distribution of the cost will make for a more rapid restoration of the creditworthiness of the debtors and will thereby enable the private banks to infuse new dynamism into their portfolio.

In conclusion, it is important to mention that the central argument of the foregoing analysis with respect to the cost of debt rescheduling is highly sensitive to the assumptions adopted in relation to risk. It has been assumed that the private banks had already taken into account the risks of default at the actual time of granting loans to the debtor countries. But there are bankers and regulatory bank authorities who assert that the former spreads over LIBOR and commissions were insufficient to cover these risks; and this phenomenon is often attributed to the 'fierce competition' among banks during the 1970s. Thus, it is maintained that the current increase in the cost of credit on rescheduling a debt is nothing but an 'adjustment' on account of the insufficient price of the credit granted during the competitive phase of the international credit market.

This argument is not very convincing. If the negotiated price of credit was insufficient in the 1970s, the cause was not the existence of a highly competitive market; rather it must be at-

tributed to a faulty assessment of risk. The private banks made their loans in the 1970s on the basis of a principle which was then widely accepted by the financial community: that countries (sovereign borrowers) never go bankrupt.²³ This assumption is technically correct, but as a general criterion for loans it seriously underestimates the potential costs involved in the development of a portfolio in developing countries.

In any event, let us assume that —whatever may have been the reasons— in the 1970s the price of credit was not high enough to ensure the long-term stability of the international financial system. Why should the developing countries be responsible for bearing the cost implied in remedying the situation? If the international financial system did not function efficiently during the past decade, in a civilized and interdependent world it is incumbent upon all the members of that system —private banks, central governments, debtor countries— to seek solutions and share the cost. Shifting the cost on to the debtors alone —as is occurring today— is questionable from the point of view of equity and ethics. But it is also questionable from the standpoint of the economic interests of the creditors and their governments: many debtors are clearly unable to bear the whole cost of the adjustment, and, failing more equitable solutions, the dynamics of their internal politics would ultimately involve them in prolonged moratoria which nobody wants to see on the international scene. Accordingly, the present cost that would be implied for the banks in sharing the burden of the adjustment is much lower than might be the future cost of perpetuating the practices now current.²⁴

²³See Morgan Guaranty Trust, *World Financial Markets*, March 1983, pp. 4-5; and Pedro-Pablo Kuczynski, "Latin American debt", in *Foreign Affairs*, Winter 1983, p. 352.

²⁴Fred Bergston, formerly Assistant Secretary for International Economic Affairs of the United States Department of the Treasury, under the James Carter administration, is very well aware of the danger: "...a moratorium by any significant debtor would have a demonstration effect on other debtors, or at least on opposition politicians in such countries, to emulate such behaviour. A 'debtors' OPEC' is unlikely to emerge by design, but could develop via chain reaction". See F. Bergston, "Can we prevent a world

²²See R. Weinert, "Banks and bankruptcy", *Foreign Policy*, No. 50, 1983, pp. 138 to 149.

Of course it is possible that the international banks are not financially in a position to take on the whole of their share of the cost of adjustment with the debtors; if this is the case, it will fall to the central governments to absorb it. There are already a good many proposals that advocate the transfer of much of the international financial problem to the centre's public sector.²⁵ For example, Professor Peter Kenen, of Princeton University, has suggested that the World Bank might purchase a proportion of the banks' portfolio at a discount, which would enable the creditors to divest themselves of weak loans (although, of course, at a partial loss).²⁶ Thus, an international public institution such as the World Bank, which perceives risk in a

broader perspective than private banks would help the debtors to find more satisfactory formulas for the relief of their situation. Again, the Government of Mexico has proposed that the International Monetary Fund provide a special service for the financing of balance-of-payments deficits due to increases in international interest rates; this would make it possible to grant compensatory loans to the debtor countries during the period in which interest rates exceed 'normal' levels, i.e., 2-3% in real terms. There are also other interesting proposals for palliating the pressures faced today by the international financial system and the debt crisis of the periphery. All that is wanting is the political capacity to adopt the appropriate decisions. The underlying reason for the proposal considered here in relation to the creditors' governments is analogous to that adduced in the case of the banks: the cost of sharing the burden of the adjustment between the banks, their governments and the debtor countries would now be much less than it would be in the future in the event of the creditors' perpetuating their current practices, which are seriously prejudicial to Latin America's economic and social development and are politically untenable for the debtor countries.

economic crisis?", in *Challenge*, January-February 1983, p. 10. Furthermore, the potential for setting up a 'debtors' OPEC' in Latin America is very great, since over 90% of the net bank debt of the periphery is to be found in the region. See R. Devlin and M. Mortimore, *op. cit.*, table 1.

²⁵See, for example, "Bad debtors' charter", in *The Economist*, 19-25 February 1983, p. 79.

²⁶R. Weinert, *op. cit.*, also puts forward an excellent practical proposal implying the transfer of part of the private banks' portfolio to the World Bank.

Wages and employment in international recessions:

Recent Latin American experience

*Victor E. Tokman**

This article takes as its working hypothesis the postulation that while the international recession makes it necessary to effect internal adjustments involving a lower level of activity, there are various alternative ways of tackling the situation, these options being partly determined by the structural characteristics of the economy, but also depending on the set of policies applied. In order to corroborate the hypothesis, the adjustment policies followed by various Latin American countries in the last two crises are analysed, and it is concluded from this that if we leave out the group of countries which are so small and open that they have little autonomy in facing the crisis, the economic history of the last five years shows the failure both of the global monetary policies followed in the Southern Cone and of the expansive policies of the oil-exporting countries. The more eclectic models applied by other countries, although markedly different from each other, appear to have been most effective in reducing or at least postponing the cost of the adjustment and sharing it out more equitably.

Two specific aspects are also analysed: the repercussions of the increase in interest rates on the Latin American economies, and the adjustment of the labour market, which takes different forms from one country to another. In some countries, this adjustment takes place through an increase in open unemployment; in others, through an increase in underemployment, and in yet others, through a combination of both factors. The reasons why the adjustment takes these different forms are analysed, together with the implications of this fact. It is postulated that in fact the reduction in the income of those working in own-account occupations plays the role of a collective unemployment insurance policy and constitutes in practice a second-best solution from a welfare point of view.

*Director, Regional Employment Programme for Latin America and the Caribbean (PREALC).

I Introduction

Latin America and the Caribbean, like the rest of the world, have gone through several international crises during the last decade which have made it necessary to introduce adjustment policies in the economy. Adjustment is of course inevitable, since it is necessary that the national economies adapt themselves to a reduced availability of real resources. Nevertheless, there is more than one possible adjustment policy and, given this diversity as well as the varying modes of application, different results may be produced.

In the first place, as regards the period required to produce results, there is a difference between policies that affect the level of expenditure and policies that operate through changes in relative prices as the principal mechanism for shifting resources from the production of goods for domestic utilization to the production of tradeables. Generally speaking, the trend in the reduction of domestic expenditure should be to concentrate on lowering consumption rather than investment, so as to avoid eventual adverse effects upon economic growth. At the same time, however, adjustment to the international recession has coincided with inflation in most Latin American and Caribbean countries, making it necessary to apply both adjustments simultaneously. The final result is that adjustment policies cease to be neutral and basically hit wages and employment levels. Wages suffer because they are usually regarded as the key variable for stabilization of price levels, for fostering an improvement in international competitiveness, and for inducing a contraction in the level of consumption. Employment levels are affected, for their part, because a lower level of domestic expenditure generates a higher level of open unemployment.

The current world crisis, as well as that suffered at the beginning of the 1970s, is different from other international fluctuations to which the economies of the region and the developing world have been historically subject, for the size and depth of these recent crises have affected not only developing countries but also those at the centre. In this connection, a comparison is increasingly being drawn between the

present recessive conjuncture and that experienced in the 1930s.

There are at least two important differences between the Great Depression of over half a century ago and the present recessive situation, however. In the first place, given the crucial role currently played by the rise in oil prices, the question of whether a country produces it or not and exports it or not furnishes a first major differentiation between economies, irrespective of whether they are located in the north or in the south. In the region, this differentiation can be clearly perceived in the dissimilar performance in the present crisis of the oil-exporting economies as compared with the rest of the continent.

In the second place, in contrast with the 1930s, the present international recession and the one before it have been accompanied with inflation in the developed world. This has at least two direct implications. On the one hand, the deterioration in the terms of trade of the non-oil-exporting countries of the region is at present greater than that observed in the 1930s. The terms of trade of the Latin American countries decreased at an annual rate of 6.7% between 1930 and 1933, whereas this deterioration attained an annual rate of 8.4% in the 1974-1975 crisis and 9.6% from 1978 to 1981, in the non-oil-exporting group. Even so, in contrast with what happened in the 1930s the decline in the purchasing power of the region's exports has been less severe, and even in the current crisis the expansion of the export quantum has more than compensated for the fall in the terms of trade.

On the other hand, the policies pursued in the central countries and especially in the United States during the present recession have involved a considerable rise in nominal interest rates, this occurring at a time when the foreign indebtedness of the countries of the Region has increased significantly. This rise exceeds the rate of growth of the export prices of the non-oil-exporting Latin American countries, and amounted between 1978 and 1981 to an increase of 47.5% in the prime rate and of 32.6%

in the rate applicable to Eurodollars, both in real terms.

The aim of this paper is to review the relationships between the aforesaid variables, which summarize the effects of the international recession on the economy of the countries in the region, and the behaviour of wages and employment. To this end, special attention will be paid to the periods 1973-1975 and from 1979 to the present. On the basis of this review, the different reactions of various countries of the region to the international situation can be identified as well as the extent to which the latter has affected wages and employment. With this in view, and given the difficulties that would be involved in analysing all countries of the region, a broad typology of situations will be made and illustrated by an analysis of some particular cases. The discussion, moreover, will necessarily be restricted, since a comprehensive analysis of the adjustment process, given its macroeconomic character, would take us beyond the limited objectives of this paper.

We take as a working hypothesis the postulation that, although the international recession necessarily entails adjustments that imply a relatively lower level of activity, there are various alternative options for dealing with the situation, which in fact has already been experienced by the countries of the region. These options are in part determined by the structural features of the individual economies, but they also depend on the policy package that is applied. In this context, wage policy comes to play an important part in short-run adjustments and in effect determines the distribution of the cost involved in the adjustment among the different groups of the population.

In addition, two other aspects will be dealt with. The first is the impact of the rise in interest rates on the Latin American economies, since as mentioned above, this is a new and distinguishing factor of the present crisis. The second is the adjustment of the labour market, because of its implications on income levels and distribution.

II

The external adjustment and wages

1. *The case of small open countries*

There is a first group of countries in the region which are of small size and have an openness coefficient (i.e., a ratio of exports to gross national product) of between 20 and 30%. They had these same structural features already in the 1930s, and when faced with the international crisis at that time they had to remain tied to the gold standard while waiting for the automatic adjustment to operate. On that occasion, they suffered a considerable cost as a result of not being able to design policies that would attenuate the effect of the international crisis. The present situation seems to be basically the same. The full impact of world recessions falls upon these economies, which must inevitably absorb the deterioration in the terms of trade and reduce real wages whenever an international situation of this sort occurs.

Central America and the Caribbean provide numerous examples of this type of economy, where the possibility of an autonomous policy is slight. In particular, if we examine the performance of Costa Rica and Honduras in the 1973-1975 crisis and in the present one, since 1979, we can see that in both countries the fall in the terms of trade has brought with it a decline in real wages. Thus, in Honduras the first recession implied a loss of around 6.3% in the growth rate of the product owing to the fall in the terms of trade and a reduction of 2.9% in industrial sector real wages during the same period. The present recession has meant up to 1981 a fall in the growth rate of the product of around 8.2% and an 8.1% drop in industrial real wages (see table 1).

In Costa Rica there are similar links between the negative effect of the decline in the terms of trade and the decrease in real wages during the two international crises. In this country there has also been a further reduction in real wages stemming from an upsurge of inflation in an economy that had not previously experienced high inflation rates. The 1973-1975 recession there coincided with an inflation rate of 25%, while in the present crisis the annual in-

flation rate averaged 30% between 1979 and 1981, the rate for the latter year being 65%.

2. *The case of medium-sized and large countries*

Already in the recession of the 1930s, and to an even greater extent in more recent international crises, the other countries of the region have displayed a certain degree of autonomy which has enabled them to a certain extent to reduce and control the impact of international crises of this magnitude. This group of countries comprises those of a larger size, generally less open to international trade and with a higher degree of urbanization and modernization. Hence, exports hardly exceed 10% of the product, the proportion of modern urban activities in employment reaches between 50 and 60% of the total labour force, and employment in modern industry comprises between 20 and 28% of the non-agricultural labour force. It is precisely in this group of countries that wages come to be a representative variable, given the greater coverage of wage-labour as a direct result of the higher degree of modernization. Included in this group are the Southern Cone countries (Argentina, Chile and Uruguay), Brazil, Colombia, Mexico and Venezuela, among others.

By way of introduction, it is worth reviewing the performance of these countries in the crisis of the 1930s and the policies they applied.¹ In the first place, those Latin American countries that enjoyed some degree of autonomy went through this crisis at a lower cost than the other countries of the region and even than the United States and Canada. In general, they grew more rapidly than the latter two countries in the period following the crisis (1932-1939); they recovered sooner; their contraction was not so pronounced as in Northern

¹The analysis of the performance of these countries and the policies followed during the 1930s crisis closely follows the work of C. Díaz-Alejandro: *Latin America in the 1930s* (New Haven, Yale University Economic Growth Center, 1981).

Table 1
EXTERNAL ADJUSTMENT, WAGES AND PRICES IN SOME
LATIN AMERICAN COUNTRIES
(Percentages)

	Terms of trade a	Degree of openness b	Effect on product c	Purchasing power of exports a	Wages ^d			Domestic prices ^d
					Urban minimum	Industrial	Construction	
<i>Small open countries</i>								
Costa Rica								
1973-1975	-9.2	27.6	-2.5	-7.1	-7.4	-9.0	-6.1	25.4
1975-1978	40.1	21.2	8.5	55.2	25.3	31.3	34.9	5.9
1978-1981	-29.2	21.8	-6.4	-10.5	-8.3	-12.2	-11.2	30.1
1973-1981	-9.8	23.5	-2.3	29.7	6.3	4.9	12.7	19.3
Honduras								
1973-1975	-23.1	27.1	-6.3	-20.2	-7.2	-2.9	-31.9	10.4
1975-1978	23.3	24.1	5.6	60.5	-15.6	12.0	77.5	6.2
1978-1981	-23.7	27.1	-8.2	-1.0	-6.2	-8.1	-24.4	14.3
1973-1981	-27.6	26.1	-7.2	32.2	-26.5	-	-8.6	10.2
<i>Medium-sized and large countries</i>								
Oil-dependent								
Brazil								
1973-1975	-21.2	6.9	-1.5	14.7	-2.3	12.1	6.9	32.5
1975-1978	2.6	6.2	0.2	24.7	3.5	13.3	12.0	42.0
1978-1981	-42.7	7.0	-3.0	6.3	1.1	8.1	-1.9	87.3
1973-1981	-53.7	6.5	-3.5	16.0	2.3	37.3	17.4	54.8
Relatively self-sufficient								
With substantial economic policy changes								
Argentina								
1973-1975	-30.0	5.5	-1.7	-45.9	-8.9	1.7	33.3	173.8
1975-1978	-19.2	9.2	-1.8	87.2	-50.4	-54.9	-55.9	211.5
1978-1981	-8.4	8.1	-0.7	-3.3	6.3	14.7	-3.2	118.2
1973-1981	-48.2	7.5	-3.6	24.0	-52.0	-20.6	-43.1	163.9
Chile								
1970-1975	-46.8	15.3	-7.2	-28.7	-41.1	-41.8	-18.3	233.1
1975-1978	-0.6	21.2	-0.1	27.1	29.9	44.3	4.2	80.1
1978-1981	-14.0	24.6	-3.4	13.7	-1.5	38.0	27.0	25.9
1970-1981	-57.2	20.4	-11.7	3.0	-24.7	15.9	8.1	98.9
Without substantial economic policy changes								
Colombia								
1973-1975	-19.9	14.8	-2.9	0.4	16.4	-8.0	7.3	22.3
1975-1978	64.7	7.4	4.8	51.7	9.4	13.3	5.1	24.2
1978-1981	-32.4	6.9	-2.2	-23.8	17.6	7.2	17.6	27.7
1973-1981	-7.4	9.7	-0.7	16.1	49.7	11.7	32.6	25.0
<i>Oil-exporting countries</i>								
Ecuador								
1973-1975	36.3	18.1	6.6	16.5	9.3	7.3	...	17.1
1975-1978	8.7	12.4	1.1	27.7	-8.0	8.4	...	11.6
1978-1981	31.1	11.4	3.6	28.1	111.3	22.9	...	13.7
1973-1981	94.3	14.0	13.2	96.0	112.5	43.0	...	13.7
Mexico								
1973-1975	3.6	7.3	0.3	2.5	16.9	8.6	5.8	15.8
1975-1978	12.2	7.0	0.8	82.3	7.9	8.0	9.1	21.3
1978-1981	47.6	7.4	3.5	140.6	-8.4	-1.7	1.6	26.1
1973-1981	71.5	7.2	5.1	349.8	15.6	14.0	17.3	21.7

Table 1 (Concl.)

	Terms of trade a	Degree of openness b	Effect on product c	Purchasing power of exports a	Wages ^a			Domestic prices d
					Urban minimum	Industrial	Construction	
Venezuela								
1973-1975	97.6	14.3	14.0	30.3	-9.3	13.1	...	9.8
1975-1978	-13.9	9.5	-1.3	-20.4	-19.6	2.1	...	7.3
1978-1981	114.2	8.1	9.3	77.2	17.7	-1.1	-5.2	17.8
1973-1981	264.4	10.6	28.0	102.3	-14.2	14.2	...	11.8

Source: Prepared by PREALC on the basis of national data.

^a Changes between the initial and final year of each period.

^b Relation between exports and gross domestic product.

^c Obtained by multiplying the change in the terms of trade by the coefficient of openness.

^d Annual cumulative rates referring to changes December to December.

America; and manufacturing industry, which became the leading sector in these economies, grew steadily at an annual rate of between 8 and 13%, whereas in the United States the manufacturing sector remained stagnant.

The policies pursued by this group of countries during the 1930s were characteristically heterodox, in defiance of the conventional prescriptions of monetarist experts of the time ('money doctors', as Carlos Díaz-Alejandro calls them). Concerning the balance of payments, there were currency devaluations and multiple exchange rate systems were established, with a higher rate for imports, a medium rate for exports and a preferential rate for servicing the external debt. Likewise, most of these countries renegotiated their debt unilaterally, only Argentina, Haiti and the Dominican Republic continuing to service the debt on its original terms. The effect of devaluation was not inflationary and helped to increase competitiveness through a change in the relation between the exchange rate and wages, basically through an increase in the former since the latter remained stable in real terms. These measures were accompanied by exchange controls and tariff adjustments that raised the level of protection.

The monetary and fiscal policies applied at that time had a clear expansionary effect. The real money supply increased, basically owing to the decline in nominal prices, and the stock of money was increased against bonds, independently of the gold standard that had been in force up to that time. In several countries, a moratorium on the internal debt was declared

and financial institutions were supported to prevent bankruptcy by means of diverse measures ranging from special rediscount lines to, in some cases, the freezing of savings deposits. Fiscal policy acquired distinct anticyclical features: there was no attempt to balance the budget, and a deficit was maintained, basically financed by delays in payments and an increase in short-term borrowing. Likewise, public expenditure was increased in order to avoid a contraction of economic activity.

Finally, the combined effect of these measures was to produce a far-reaching structural transformation which still characterizes the economies of these countries up to the present and basically consisted of a rapid expansion of the manufacturing sector, together with a higher degree of State intervention in economic activity.

At present, the countries in this group have begun to develop differences owing chiefly to the different impact of oil prices in the more recent international crises. Hence, a distinction must be made between the oil-exporting countries, those which are largely dependent on imported fuel, and those which have some degree of autonomy because they are relatively self-sufficient. Ecuador, Mexico and Venezuela are among the oil-exporting countries, while Brazil is particularly heavily dependent on fuel imports. Finally, in the group of relatively self-sufficient countries a distinction must be made between those which in the past decade have applied structural policies of price stabilization and external openness (basically, those of the South-

ern Cone) and those which have pursued more conventional policies, such as Colombia.

3. *The oil-exporting countries*

These countries benefited from the rise in the price of oil, which caused a remarkable improvement in their terms of trade, combined in some cases, such as that of Mexico, with a considerable expansion in the export volume of this product. The improvement was particularly marked in the case of Ecuador, Mexico and Venezuela, which were able to apply a policy of real wage increases owing to the favourable international situation, so that a high correlation between the rise in the terms of trade and increases in real wages is observed (see table 1).

However, there was a growing tendency in these countries to overexpand domestic expenditure and to increase the money supply as a result of the aforesaid oil boom, resulting in accelerated inflation and/or balance-of-payments problems. These were paradoxical results, since these economies had historically exhibited low rates of inflation, while moreover their greatest boom in recent decades was followed by the emergence of a balance-of-payments deficit. They were thus compelled to resort to adjustment policies involving a reduction of expenditure and wage controls, as in Mexico and Venezuela since 1979. As a result, real wages tended to contract despite the improvement in the terms of trade.

Ultimately, although during the period 1973-1981 wages benefited from the oil boom, the actual benefits were diminished owing to the aforesaid internal disequilibria, especially inflation, whose effects were particularly negative because these economies had little previous experience of this problem and hence lacked systems of wage indexation. Thus, in Venezuela, despite an expansion of the order of 28% in the product due to improvements in the terms of trade, real wages in the industrial sector increased by only 14% during the same period.

4. *The non-oil-exporting countries*

a) *Countries dependent on oil imports*

By far the most important country in this group is Brazil, which is relatively autonomous

in the design of its economic policy but is heavily dependent on oil imports. This country made active use of its possibilities of increasing the external debt in order to cushion the economy from the recessive impact caused by the pronounced fall in its terms of trade.

As a result of these policies, during the period 1973-1975 Brazil was able to raise industrial real wages by around 12%, even though the terms of trade fell by approximately 21%. With the further fall in its terms of trade from 1978 onwards, however, the growth in real wages has considerably slackened (see table 1).

It is clear that Brazil gradually lost flexibility in its handling of international crises both through the emergence of internal imbalances chiefly observable in the inflationary upsurge of recent years and through the greater cost associated with the increase in real interest rates, given its high degree of indebtedness. Thus, if the growth in the nominal interest rate applied by commercial banks to their best customers (prime rate) and in that applied to three-month deposits in Eurodollars is compared with the growth in the price of Brazilian exports, it will be seen that the former rose during 1978-1981 by 59% and the latter by only 43% (both in real terms). Given that 84% of Brazil's external debt has been contracted at variable interest rates and that it constitutes around 25% of the gross national product, and taking into account that the rate prevailing in 1978 was around 10%, it can be estimated that the rise in international interest rates has produced a deterioration of around 11% in the product, which is almost four times the deterioration in the product attributable to the fall in the terms of trade during the period 1978-1981.

Nevertheless, despite the unfavourable situation confronted by Brazil, analysis of the period 1973-1981 shows that, although this country had to face a deterioration in the terms of trade that implied a decrease in the rate of growth of the product of around 3.5%, the domestic policies applied not only protected wages from a similar reduction but actually permitted a rise of around 37% in the average real wage paid in the industrial sector. This is undoubtedly a clear illustration of policies capable of coping with the international recession without shifting the burden of the adjustment

primarily on to wages. It is still too early, however, to evaluate the net effect, since this country must face up to a heavy external debt which was, in fact, one of the factors that made possible the economic policy approach adopted.

b) *Countries not dependent on oil*

i) *Countries without substantial changes in economic policy.* A case that illustrates this type of situation is Colombia. Its terms of trade were adversely affected both in the 1973-1975 crisis and in that beginning in 1978. Notwithstanding the negative impact of the international situation, the economic policies adopted fostered an expansion in the quantum of exports and thus neutralized the adverse effect of international prices, at the same time permitting a significant rise in real wages during the period 1973-1981. Thus, in contrast with a potential decline in the product of around 1%, attributable to the decline in the terms of trade, urban minimum wages rose by 50%, industrial wages by 12% and those in construction by 33% (all in real terms) over the same period (see table 1).

ii) *Countries with marked changes in economic policy.* This group includes Argentina, Chile and Uruguay,² which during the decade pursued policies of price stabilization and external openness of their economies. It is outside the objectives of this paper to comment here on these policies or on their main effects.³ We shall concentrate instead on the degree of autonomy of these countries regarding the taking of domestic economic policy decisions and on the consequences of the policies adopted.

First, the fact that these countries possess some degree of autonomy in their economic-policy decisions and are not entirely subject to international fluctuations is clearly illustrated by the case of Argentina, which during the 1973-1975 crisis succeeded in at least maintaining wages in real terms, despite a deterioration in its

²It should be noted that the three countries have different degrees of dependence on imported oil. Argentina is practically self-sufficient, while Uruguay is highly dependent. Chile's position is intermediate.

³See, for example, PREALC: *Políticas de estabilización y empleo en América Latina*, Investigaciones Sobre Empleo Series, No. 22 (Santiago, PREALC, 1982).

terms of trade of around 30%. Similarly, Chile in the recession beginning in 1978 succeeded in preventing the deterioration in the terms of trade from being transferred to wages. It should be noted in this latter case that the increase in real wages during the more recent period was largely due to the slowdown in the inflation rate, which in an indexed economy automatically amounts to a rise in real wages.

Secondly, wages became a basic variable in the economic and social policies adopted by these countries. Wage control was a basic policy instrument in the effort to achieve price stabilization and an improvement in international competitiveness, especially during the quite long periods when fixed exchange rate policies were applied (or, more generally, overvaluation of the local currency), when it was sought to achieve, by reducing wages, a shift of resources towards the production of tradeables. Wage control was also used as a social objective for disciplining the labour force, since in both countries it was sought by this means to avoid pressures that might challenge the economic and political decisions being applied. In particular, this economic strategy resulted in a disarticulation of the trade-union movement, basically through the anti-industrial and anti-employment bias introduced by the policy.⁴ This made possible effective reductions in real wages without major resistance arising within the system.

The result of these policies was a reduction in wages that apparently exceeded the cost that would have been involved in absorbing the deterioration of the terms of trade. Thus, in Argentina between 1973 and 1981 the decline in the terms of trade implied a reduction in the growth rate of the product of around 3.6%, but wages in the industrial sector fell during that period by around 21%. In Chile between 1970 and 1975, the negative effect of the terms of trade implied a fall in the product of around 7%, but industrial wages contracted during that period by over 41% (see table 1).

In both countries, however, real industrial wages rose between 1978 and 1981 in spite of a deterioration in the terms of trade. This wage

⁴R. Lagos and V.E. Tokman: *Global monetarism, employment and social stratification*, Trabajos Ocasionales Series, No. 47, Rev.1 (Santiago, PREALC, 1982).

behaviour conceals the real effect of the policies followed, for various reasons. The first is that 1981 was a year in which wages were at their maximum, but only temporarily, since real industrial wages fell during 1982 by 10.5 and 3% in Argentina and Chile, respectively. The second reason is that the adjustment operated mainly through reductions in the levels of total employment, especially that in manufacturing industry, rather than through reductions in wages. Manufacturing employment in Argentina fell in absolute terms between 1973 and 1981 by 32.8% (37.2%, if 1982 is included) and by 21.2% between 1978 and 1981 (26.2%, if 1982 is included). In Chile, the reduction between 1970 and 1981 was around 17% (28%, if 1982 is included) and 8% between 1978 and 1981 (20.4%, if 1982 is included). Lastly, in the particular case of Chile, the adjustment implied a substantial increase in the rate of open unemployment and in occupations in emergency programmes at remunerations of around one-third of the minimum wage. Open unemployment, including this minimum employment, increased fivefold between 1970 and 1981 and reached 28.4% of the labour force in 1982.

5. *Tentative conclusions*

To sum up, the experience of different countries in the region suggests that, although in the face of adverse international developments the countries have no option other than to adjust their economies, and that this implies adopting policies that result in a fall in real wages, this occurs automatically only in a small group of countries which, because of their size and de-

gree of openness, do not possess the autonomy to alter this result.

There are, however, numerous countries in the region that have in the past shown a certain degree of autonomy and have controlled the domestic adjustment to international recessions by influencing the distribution of the cost of adjustment, the period during which it is applied and, finally, the different mechanisms through which their economies adjust to external crises. Experience also shows that some countries have succeeded in applying an expansive wage policy during adverse international conditions, just as there are others which, in similar circumstances, have accentuated the cost of adjustment by introducing substantial changes in their economic policies. Finally, the oil-exporting countries are a special case in which, although it is possible in principle (and so it has been done) to pass on the international bonanza in the form of real wage increases, internal and sometimes external imbalances arise that eventually limit this possibility, so that finally wages actually expand less than would have been theoretically feasible.

In short, the economic history of the last five years points to the failure of two kinds of policies: the contractionary global monetarist policy followed in the Southern Cone, and the expansive policy of the oil-exporting countries. The more eclectic models followed by other countries, although markedly different from each other, seem to have been more effective in reducing or at least postponing, the cost of the adjustment and distributing it in a more equitable manner.

III

The increase in international interest rates

The present world recession differs from earlier ones in that it has not only produced a major fall in the region's terms of trade but also been accompanied by a rise in the interest rate applicable to the external debt service. Thus, between 1978 and 1981 the rate applicable to best debt-

ors by North American banks (prime rate) rose by 72.3% and the rate applicable to three-month deposits in Eurodollars rose by 54.9%.

This considerable increase in nominal interest rates entails an additional outflow of financial resources for the countries of the re-

Table 2
EFFECT OF THE CHANGE IN INTERNATIONAL INTEREST RATES, 1978-1981

	i_1	i_2	i_1	i_2	Percentage of the external debt		Loss of growth due to interest rate rises ^c	Ratio of loss of growth due to interest rate rises to terms-of-trade effect ^d
	P_x	P_x	P_i/t_c	P_i/t_c	With respect to the gross national product ^a	Subject to variable interest rates ^b		
	(1)	(2)	(3)	(4)				
Argentina	5.9	17.8	-57.3	-47.5	41.1	80.0	-3.9	5.6
Brazil	42.9	58.9	26.1	40.3	24.9	84.0	-10.7	3.6
Chile	22.1	35.8	-14.4	-4.8	35.6	65.6	-6.8	2.0
Colombia	68.1	86.9	7.2	19.2	22.8	58.3	-10.3	4.7
Costa Rica	56.0	73.6	99.4	125.5	49.3	62.4	-19.9	3.1
Honduras	49.9	66.7	8.0	20.2	59.6	45.8	-15.9	1.9

Source: Prepared by PREALC on the basis of information from the countries.

i_1 = variation in the interest rate on Eurodollar deposits for 90 days.

i_2 = variation in the prime interest rate.

P_x = changes in export prices.

P_i = changes in domestic prices.

t_c = changes in the exchange rate.

^a Refers to 1980.

^b Refers to the average for the period 1978-1980.

^c Calculated by applying the mean variation in the real interest rate (1) and (2) to the percentage of the debt with respect to the product (5), adjusted by the percentage of the debt subject to variable interest rates.

^d Relation between (7) and the loss due to the terms of trade as estimated in table 1.

gion. It has been estimated that in 1981 each additional percentage point on the nominal interest rate implied an increase in interest payments of US\$ 2 250 million for the region as a whole. This amount is equivalent to 2.6% of the value of Latin America's exports of goods, reaching a proportion of 3.3% of total annual export value in the case of Mexico and around 3% in that of Argentina and Brazil.

To assess the pressure on resources implied by this increase in the nominal interest rate, it must be compared with the evolution of export prices in the region during the same period. When this is done, the situation becomes more diversified, according to the particular features of each country. In the case of the region's oil-exporting economies, their export prices grew faster than the increase in the nominal interest rate during the period, and the variation in the real interest rate has consequently been negative. In the remaining countries of the region, the effect of the change in the real interest rate has affected growth of the product differently according to the evolution of export

prices, the ratio of the external debt to the gross national product, and the proportion of the debt contracted at variable interest rates.

Firstly, there is a group of countries where the rise in nominal interest rates was combined with a fall in export prices, at the same time that the external debt amounted to a high percentage of the gross national product. This is typically the case of the Central American economies, among them Costa Rica and Honduras. As a result of the rise in real interest rates⁵ the growth possibilities diminished by 20% in Costa Rica and by 16% in Honduras during the period 1978-1981 (see table 2). Secondly, there is another group of countries where the rise in nominal interest rates was

⁵The method used to calculate this effect consisted of estimating the proportion of the debt subject to variable interest rates in relation to the gross domestic product and applying to this coefficient the rate of growth of the interest rate in real terms, defined as the variation in the international interest rate, deflated by the variation in the export prices of the respective country.

combined with virtually stationary export prices and the burden of the external debt as a proportion of the national product is around 25% but it is largely contracted at variable interest rates. This group includes Brazil and Colombia, where the effect of the potential loss of growth of the product was around 10% during the same period. Finally, we have a group of countries in which the increase in nominal interest rates was largely offset by an improvement in export prices, but which nevertheless exhibit a heavy burden of external debt as a percentage of the national product (of the order of 40%), with around 80% of the debt contracted at variable interest rates. This is the case of Argentina and Chile, with a potential loss of growth of the product of 4% in the former and 7% in the latter.

On the other hand, to gain an approximate idea of the effect of the rise in real interest rates as compared with that attributable to the deterioration of the terms of trade, it is convenient to relate both effects to the potential growth of the national product. This shows that during the period 1978-1981 the size of the effect associated with real interest rates varied among different countries from 1.9 to 5.6 times the terms-of-trade effect. At one extreme we find Argentina and Colombia, where the real interest-rate effect is around five times that linked with the terms of trade. They are followed by an intermediate group including Brazil and Costa Rica, where the effect of the former is around three times that of the latter, and a third group, made up of countries like Chile and Honduras, where the difference is around two to one (see table 2).

Lastly, it should be noted that the most significant change in the structure of the region's external debt in recent years has been the increase in the proportion of private funds in the total, both as regards their origin and their destination. There has been a particularly sharp increase in the proportion of private sector credits without public sector guarantee. This has brought about a change in the characteristics of the external indebtedness, which is increasingly contracted at variable interest rates (85% of the total by 1981), thereby making the economies more vulnerable to the variations in interest rates on the international markets.

From a distributive viewpoint, the effect of the rise in the international nominal interest rates should be related to the evolution of those particular prices which are significant for national private borrowers. For them, the relevant prices are given by the changes in domestic prices in relation to the changes in the exchange rate. From this comparison, it will be seen that the effect of the rise in nominal interest rates has not in general been passed on to the national private borrowers, since most of the countries in the region exhibit either a fixed exchange rate with increases in domestic prices, or exchange-rate depreciation lagging behind domestic inflation.

Clear example of fixed exchange rates with domestic inflation are provided by the oil-exporting countries, especially Mexico and Venezuela, together with small and open economies such as Honduras, which also maintained a fixed exchange rate against upward variations in domestic prices. From the standpoint of those who incur debts in dollars, this results in a negative real interest rate. The same has occurred in Argentina and Chile, since both countries applied during this period stabilization policies which made use either of a fixed exchange rate or lagging devaluation as instruments for reducing inflationary pressures. In these two cases, the real interest rate for dollar debtors is also negative. In Brazil and Colombia, where lags in foreign-exchange-rate depreciation are also found, but to a lesser degree than in the countries mentioned before, the effect was to reduce the increase in the real interest rate by about a half in Brazil and by one ninth in Colombia. Lastly, there are countries such as Costa Rica, where the rise in nominal interest rates has been combined with an appreciation in real terms of the exchange rate, this resulting in a positive real interest rate that is higher for the private debtor than for the country as a whole.

In sum, it is clear that the rise which has recently occurred in international nominal interest rates amounts to an additional substantial burden for the countries of the region, which at the same time are being forced to adjust their economies to a recessive situation. Nevertheless, on analysing the effect of the rise of interest rates in real terms, the situations of particular countries are found to differ according to the

evolution of their export prices, the weight of the debt in relation to the national product, and the proportion of the debt subject to variable interest rates. Finally, the actual incidence of the increase in nominal interest rates upon the national private sector depends on the exchange policy applied in each country and on the evolu-

tion of domestic prices, the result being in most cases a lesser burden than that determined by the variation in the interest rate in the international financial markets, while in some countries this has even been transformed from a burden into a subsidy.

IV

The economic adjustment and the labour market

It is increasingly argued that higher real wages are one of the principal factors behind the growth of open unemployment. This line of argument, whose theoretical basis is highly questionable in view of the assumptions put forward to justify it, is not borne out by the existing data.

On analysing the variation in wages (whether the urban minimum, those in manufacturing industry or in construction) in relation to the changes in open unemployment during two sub-periods of the past decade, the results clearly show that no such relationship exists. The information on 12 Latin American countries for the periods 1975-1978 and 1978-1981, selected because of the different international situation prevailing in each one, clearly confirms this assertion (see table 3).

Thus, during the first period only in one country (Venezuela) was the fall in urban minimum wages accompanied by a significant decrease in the rate of open unemployment. Even in this case, however, this relationship no longer holds good in connection with the change in industrial wages. Moreover, there is no country where an increase in real wages is seen to be associated with a significant rise (over one percentage point) in open unemployment. On the contrary, in 6 out of the 12 countries considered we find the opposite association, that is to say increases in real wages accompanied by significant decreases in the rate of open unemployment rate or decreases in the former together with a significant rise in open unemployment.

In the period 1978-1981 only two countries show a simultaneous fall in real wages and in open unemployment when both urban mini-

mum wages and industrial wages are considered. Similarly, if we analyse movements in the same direction (i.e., increases in real wages together with increases in open unemployment) the number of cases observed is three for the urban minimum wage, but there is no significant case in relation to wages in industry and construction. In contrast, there is a greater number of countries showing opposite movements in real wages and the rate of open unemployment, whatever the type of wage considered.

This scanty relation between changes in the real wage and changes in open unemployment, and indeed the observation of considerable evidence to the contrary, points to the need to investigate the likelihood of other determinant factors. In particular, changes in the level of economic activity can induce variations in the open-unemployment rates. This statement is based not only on an important current of theoretical interpretation but also on the available evidence for short-term variations, which seems to suggest the existence of a high correlation of this sort. On relating information on the growth of the gross domestic product with changes in the rate of open unemployment (see table 3), it is observed that in the period 1975-1978, in 5 of the 12 countries for which information is available there was a positive correlation between accelerated growth and decreases in the unemployment rate, or between a contraction in the product and an increase in the unemployment rate. Again, in the period 1978-1981, in 5 of the 12 countries considered this relationship holds good. It is clear, then, that

Table 3
LATIN AMERICA AND THE CARIBBEAN: REAL WAGES ACTIVITY LEVELS
AND OPEN UNEMPLOYMENT

	1975-1978					1978-1981				
	Growth of product ^a	Changes in wages ^b			Changes in open unemployment ^c	Growth of product ^a	Changes in wages ^b			Changes in open unemployment ^c
		w _m	w _i	w _c			w _m	w _i	w _c	
Argentina	1.6	-50.4	-54.9	-55.9	0.2	0.2	8.9	19.9	-	0.7 ^d
Brazil	6.6	3.5	13.3	12.0	0.6	3.5	-10.2	-6.3	-15.5	1.7 ^c
Colombia	6.1	9.4	13.3	5.1	-2.0	4.1	20.3	7.4	14.3	-0.8
Costa Rica	6.9	25.3	31.3	34.9	0.4	0.6	1.8	0.7	1.4	3.3
Chile	7.2	30.0	20.6	44.4	-1.7	6.7	-0.6	18.1	23.6	-4.3
Jamaica	-2.1	-17.2 ^f			4.0	-3.8 ^d	-12.0 ^f			5.0 ^d
Mexico	6.6	7.9	8.0	-	-0.3	8.5	-9.0	-5.7	-	-2.4
Panama	3.6	-11.7	-	-11.7	1.0	5.0	2.1	-	-2.5	2.0 ^g
Peru	0.5	-32.0	-27.4	-38.6	0.5	3.9	13.8	2.6	2.6	-1.2
Trinidad & Tobago	9.9	8.8 ^f			-1.7	4.9 ^d	5.1 ^d			1.8 ^d
Uruguay	4.1	-16.8	-26.3	-25.9	1.6	4.1	-15.1	-15.0	-13.6	-3.4
Venezuela	6.1	-19.6	2.1	-	-3.2	-0.1	-3.0	-12.8	-	1.9

Source: PREALC figures on the basis of information from the countries.

^a Annual growth rates.

^b w_m : urban minimum wages.

w_i : wages in manufacturing industry.

w_c : wages in construction. Percentage variation during the period.

^c Changes, in percentage points, between the first and the last years.

^d Refers to 1978-1980.

^e Preliminary estimate.

^f Refers to total wages.

^g Refers to 1978-1979.

there is in the short run an appreciable degree of correlation between the level of economic activity and the rate of open unemployment, though in some cases a high growth rate is associated with a constant unemployment rate.

The preceding analysis consequently suggests that the open-unemployment rate appears to be more responsive to changes in the activity level than to variations in real wages. However, the possibility of explaining changes in the labour market through the mere observation of variations in open unemployment is indeed limited for economies like those of the region, where there is a significant amount of underemployment. Adjustment in heterogeneous labour markets may take various forms: changes in open unemployment, variations in underemployment or a combination of both. Let us illustrate the reaction of the labour market to a recessive conjunction by looking at four Latin American countries presenting different conditions.

For this purpose, we chose Argentina in the period 1974-1980, Chile during the past decade, and Venezuela and Costa Rica as from 1978. The first two cases were selected because they combine external adjustment with profound changes in economic policy, mainly directed towards achieving price stabilization and a higher degree of openness. The third case illustrates the experience of an oil-exporting country combining an oil boom with economic policies aimed at correcting some internal disequilibria mainly reflected in an upsurge of inflation compared with previous historical patterns. The last country illustrates the case of a small open economy facing balance-of-payments problems and inflationary pressures.

As may be seen from table 4, the four cases present common features. On the one hand, the rate of growth of the product is low, and even negative in Venezuela. On the other hand, all these economies exhibit inflationary problems, though in differing degrees. In Costa Rica and

Table 4
LATIN AMERICA: THREE TYPES OF LABOUR MARKET ADJUSTMENT

	Annual rate of growth of product	Annual rate of growth of prices	Variation in real wages over whole period (%)	Changes over whole period in:		Annual growth of non-agri- cultural EAP (%)	Ratio of in- comes in the informal sec- tor to modern sector ^a
	(%)	(%)	(%)	Open unem- ployment (Percentage points)	Share of urban informal sector		
<i>Case 1</i> Argentina (1974-1980)	1.9	156.3	-46.9 ^b	- 0.3	4.0	0.6	1.03
<i>Case 2</i> Costa Rica (1978-1981)	0.6	30.1	-11.2	3.7	-0.1	5.2	0.71
Chile (1970-1980)	2.7	79.1	-21.4	14.5 ^c	0.1	2.7	0.73-0.80
<i>Case 3</i> Venezuela (1978-1981)	-0.6	16.9	- 6.7	2.3	3.0	4.5	0.86

Source: Prepared by PREALC on the basis of national statistics.

^a Because of the difficulty of obtaining income data disaggregated by sectors, the definitions are not exactly identical in the four cases, but they represent acceptable approximations.

^b Wages in manufacturing industry.

^c Includes those occupied in the Minimum Employment Plan (PEM).

Venezuela, although the price increases might be considered relatively moderate, the annual rates registered were four and even five times as high as the historic inflation rate. Finally, during the periods under analysis, real wages are seen to decline in all four cases. These common features reflect in fact similar economic policy decisions designed to control domestic demand and wages with a view to reducing price increases.⁶

However, the labour market reacted quite differently in each case. In Argentina, the adjustment took place via an increase in the proportion of those employed in the urban informal sector, while the open-unemployment rate remained virtually constant throughout the period. In Chile and Costa Rica, on the contrary, the adjustment proceeded almost entirely through a rise in the open-unemployment rate, while the proportion of the urban informal sec-

tor remained constant. The labour market in Venezuela, for its part, adjusted in an intermediate manner, showing a rise both in the open-unemployment rate and in the proportion of those employed in the urban informal sector. The first of these cases illustrates an adjustment entirely achieved by way of an increase in underemployment; in Chile and Costa Rica there was an increase in open unemployment; and in Venezuela the adjustment operated through both open unemployment and underemployment.

At this point, one might ask what it is that determines these distinctly different types of adjustment in the labour market. Given the similarity between the four countries under analysis in respect of the magnitude of the informal sector, the difference might be traced to the average level of income prevailing in this sector. Both in Argentina and in Venezuela, the average income obtained by informal workers is only slightly different from that corresponding to occupations in modern activities. In Chile and Costa Rica, however, the difference is as high as 30%. This seems to imply that those who are unable to find work in the modern sector because of the adjustment in the labour market prefer to remain in active search for a job when the other employment opportunities open to them would

⁶It should be noted that the capacity of changes in real wages and in the level of activity to provide useful explanations when analysing variations in open unemployment is extremely limited, and indeed they often give contradictory answers. Thus, although real wages went down in all four cases, the rate of unemployment remained unchanged or went up in all cases.

entail a considerably smaller income. In contrast, when the difference is not so marked the option of working in the informal sector until the labour market becomes normal appears a valid alternative.

Finally, it is interesting to compare the adjustment of the labour market in developing countries like those analysed above with a developed country, say, the United States during the same period. For this country, the data show that the non-agricultural population grew by 2.8% per year between 1978 and 1981, the number of unemployed rose by 10.5% per year, and the non-professional self-employed and unpaid family workers diminished by 6.3% per year. It is clearly a case of adjustment through increases in the open unemployment rate. Since income differentials in the United States are small, or at any rate smaller than in Argentina and Venezuela, one would have *a priori* expected also an expansion of non-wage occupations, but the real difference lies in the existence of an unemployment insurance which in the United States covers more than 40% of the un-

employed. For these people, unemployment does not mean zero income, since they receive a guaranteed income while actively searching for new jobs.

Apart from illustrating differences in types of adjustment of the labour market, the comparative analysis made above suggests that the distributive effects in each case are different. Thus, the existence of unemployment insurance with wide coverage at normal income levels minimizes the direct effect on the distribution of income. At the other extreme, an increase in the number of unemployed without any welfare aid, as in Chile and Costa Rica, leads to a drastic deterioration in the distribution, while the intermediate cases of adjustment through expansion of less remunerated occupations also affect negatively the distribution of income, albeit in a milder way. In this latter case, the reduction of the average income of the self-employed plays the role of a collective unemployment insurance, constituting in practice a second-best solution from a welfare point of view.

Is there a fair and democratic way out of the crisis?

Some proposals in the light of the ECLA philosophy

*Adolfo Gurrieri and Pedro Sáinz**

The monetary, financial and trade imbalances which have caused or aggravated the present crisis are being tackled in most of the Latin American countries through conventional adjustment policies. These policies, which do not always achieve the hoped-for results, impose enormous economic and social sacrifices, not only because of their consequences for the system of production, economic activity and the level of employment, but also because of their marked tendency to share the costs of the crisis inequitably among the different social groups.

In these circumstances, the authors hold that it is necessary to work out other policy systems which, being based on different normative principles, will make it possible not only to overcome the crisis but also to reorient development so as to correct its structural problems. This article, which they hope may make a contribution to this objective, outlines an alternative policy scheme based on some central ideas of the ECLA thinking on development. In section I, they describe the main features of the crisis and make a critical analysis of the adjustment processes now in progress; in sections II and III they set forth in a general manner the form of development which they suggest and the structural changes which should be carried out; in section IV they examine the short-term policies which should be followed, and the final section contains some reflections on the institutional order which should govern the political process of taking decisions on the crucial issues regarding the crisis and development.

*Technical Secretary of *CEPAL Review* and Deputy Director of the ECLA Economic Projections Centre, respectively. Both the authors wish to express their gratitude to Claudio Marinho for his comments and suggestions.

Introduction

Latin America is currently facing the most serious economic and social situation since the war, in which negative factors of both external and domestic origin have combined in a cumulative manner.¹ In many cases the damage done by the crisis affecting the developed countries has been aggravated by the application of domestic policies which have further intensified the economic depression and its effects on employment and income. These factors have once again highlighted the persistence of long-standing structural problems which the high economic growth rates registered in the boom years were not enough to overcome.

The combination of unsolved structural problems with unsuitable policies and an unfavourable external context has led to a crisis which has not only been manifested in the economic indicators and political events but has also struck deeply into the hearts of all. The man in the street is overcome by a mixture of frustration, confusion and impotence as he sees his vital projects collapsing and his hopes for a better life disappearing. In the ruling circles, perplexity and disorientation reign: understandable reactions to a crisis which has shaken the most solid beliefs.

In these circumstances, it is urgently necessary to put forward a set of ideas which could form a suitable instrument for interpreting and tackling the present problems. In normal times, and in the face of normal problems, mankind usually follows the paths already traced by previous generations, and all that it is necessary to do in such cases is to hasten one's step by advancing with greater energy. In times of crisis

¹This topic has also been dealt with in a number of articles published recently in *CEPAL Review*. In addition to the other articles in the present issue, see in particular Enrique V. Iglesias, "The international recession in Latin America" (*CEPAL Review* No. 17, August 1982, pp. 153-162); ECLA Economic Projections Centre, "Latin American development problems and the world economic crisis" (No. 19, April 1983, pp. 51-83); R. Prebisch, "A historic turning point for the Latin American periphery" (No. 18, December 1982, pp. 7-24); and Pedro Sáinz, "Adjustment, redeployment or transformation? Background and options in the current situation" (No. 18, December 1982, pp. 25-44).

this is not enough, however: it is necessary to know where one is going and, if the wrong road is being followed, to correct it.

Times of crisis, then, call for serious reflection to clarify the nature and failings of the prevailing situation and also the basic outlines of the world it is desired to build. This article aims to make a contribution to this task through a criticism and a proposal. The criticism is that attempts have been made to tackle the crisis by following the broad lines of a type of economic and social policy which has failed in practice. The proposal is for profound changes in this type of policy to open up the possibility of a way out of the crisis.

From 1965 onwards, the rapid growth of international trade and the economic progress of many countries of the region gave rise to some questioning of ECLA's assertions regarding the need to change economic relations at the international, regional and national levels. From the mid-1970s onwards, the abundant external financing available accentuated the belief that the best solution to the problem of the external imbalance would be the liberalization of international trade, since it was felt that in orienting productive activities, growing importance should be given to external market demands. By following this path, it was argued, in the long run there would be a reduction in external vulnerability, and an increase in independence of the exterior and in economic growth, while ultimately greater social equity would be achieved.

The crisis blew away these hopes, and the doubts raised by the ECLA interpretation as regards the validity of this line of approach returned, so that there is now renewed interest in the lines of action proposed by ECLA.

Like all relevant interpretations regarding development, the ECLA approach is a combination of normative principles, suggestions of ways of orienting the analysis, proposals regarding empirical facts, and action proposals. The tremendous speed of economic and social changes makes it necessary to carry out a continual review of the analytical suggestions, the empirical proposals and the proposals for practical action in order to systematically appraise their validity and modify them whenever necessary. The normative principles which are the

basic elements in the ECLA thinking still retain their validity and topicality, however. Thus, the need to establish more autonomous and equitable international economic relations, to reduce social inequality and improve the living conditions of the poorer strata, to promote economic growth in order to absorb the entire labour force in productive jobs, and to consolidate a more democratic political order is undoubtedly just as important today as it was in the past.

The presentation of these principles in full would require considerable more space and effort than can be given to them in this article, but there are some principles of a social and political nature which are worthy of special emphasis, since, together with economic factors, they have always played a leading role in the ECLA approach.

Special emphasis must therefore be given to the principle of equity, which should be present in all social relations. In the international field, the emphasis placed on the unequal distribution of technical progress and its fruits has been perhaps the most salient feature of ECLA's interpretations, and the need for the establishment of an international economic order in which these are shared out more equitably has been its main watchword.

The creation of a new and more equitable international order in which all countries will have a similar level of economic and social development, however, calls for profound changes in the international distribution of power, so that the developing countries can have a greater degree of autonomy in their decisions. It is well known that the political bargaining power of a government *vis-à-vis* other governments, transnational corporations and international organizations will depend largely on the political support it enjoys domestically, in the region, and in the rest of the developing world. Ultimately—and this is what the principle of international equity aims at—the political power of the developing countries should be strengthened until new rules are established for international economic relations. Whatever the progress made on the national, regional and international political levels, the increase in the degree of autonomy of the economies on the periphery will encounter a limitation in their external vulnerability. In other words, the Latin American

countries' relationship of trade and financial dependence has always been a formidable obstacle to their achieving greater autonomy, and overcoming this should be a main policy objective of all governments.

In domestic economic relations, too, the principle of equity should occupy a central place. Economic development calls for a sustained effort to accumulate capital, and this should be carried out through procedures which strengthen equity. The incorporation of technical progress should be carried out in such a way as to reduce regional, sectoral and social heterogeneity, and should manifest itself in the absorption of the entire labour force into productive jobs; the distribution of the fruits of this development should also be equitable, to which end it is necessary to place emphasis on mechanisms tending towards a homogeneous distribution of technical progress, as well as on direct distribution and redistribution measures. Likewise, equity should be expressed through wide social mobility which permits all members of society to have equal opportunities to reach higher levels, to reduce the present social inequalities, and to satisfy the elementary needs of the underprivileged.

The principle of equity is also closely linked with the principle of democracy, which means the establishment of a form of social or-

ganization where there is a more equalitarian distribution of power.² As already noted, at the international level equity and democracy must mutually support each other, and it was noted from the very first ECLA writings onwards that behind distributive inequality lay the inequality of power among the nations, which would only be corrected if the underprivileged nations were capable, through their own efforts, of changing the economic role and function which they play: the new international economic order thus also calls for a new world political order. At the level of domestic political relations, the initial ECLA political position stressed the need to ensure that the State gave the right orientation to development, but this position already contained the seeds of the democratic principle, for this State orientation was necessary in order for the State institutions to be able, at least potentially, to assume fuller representation of the general interests of society than the private groups which based their influence on the control of the economic process. With the passage of time, the democratic principle has gradually been consolidating its position in ECLA's thinking as the experience built up by the Latin American countries has repeatedly confirmed that if an equitable form of development is desired, this must be managed by a democratic State.

I

The crisis and the adjustment process

In the present situation, it is essential to clarify the nature of the crisis. As from 1974, Latin America entered upon a period of instability and uncertainty; the changes which took place in the international context have not all been interpreted in the same way, nor has there been unanimity in the forecasts regarding the evolution of the developed economies.

There is no doubt that the Latin American countries have been affected in very different ways by the new external situation and that their reactions have also been very different. For some of them, such as the net oil-exporters, it

seemed that a new stage of their development was beginning in which balance-of-payments restrictions would be just a bad memory. Others sought to face up to these restrictions through bold attempts to transform their structure of production so as to substitute imported basic in-

²The development of democratic ideas in ECLA's thinking was largely due to Medina Echavarría. See, *La obra de José Medina Echavarría* (Selección y estudio preliminar por Adolfo Gurrieri), Madrid, Ediciones Cultura Hispánica, 1980.

puts and achieve a rapid increase in exports. Finally, others believed that what had happened with oil marked the beginning of a new commodity boom and, dazzled by the easy availability of external financing, they liberalized their economies in the belief that through the old trade schemes based on static comparative advantages they could restore their economic growth.

In spite of this, between 1975 and 1980 there was a decline in the economic growth rate of the region, and if some countries were able to maintain their economic growth, albeit at a reduced level, this was due to the systematic application of policies aimed at securing this objective and, above all, to the support provided by plentiful external financing. Most of the countries, however, seemed to remain convinced that the developed world was gradually getting over the increase in oil prices—which was supposed to be the main reason for its problems—and that it would therefore resume a rate of growth similar to that of the period 1965-1973 and give a similar impulse to world trade. In reality, although they based their approaches on different interpretations and applied different policies, for the most part the governments of the region were fairly optimistic towards the end of the last decade about the possibilities of expansion offered by the prevailing form of development.

During the 1970s, the ECLA Secretariat was entrusted, by a mandate from the General Assembly, with the appraisal of the region's development every two years. In the midst of an optimistic atmosphere, these appraisals always struck a discordant note, for although ECLA acknowledged that important progress had been made in many fields, it could not avoid pointing out, with the far-sighted economic and social vision which is characteristic of it, that the same old structural problems still persisted or were even getting worse. Thus, in its appraisal of the 1970s³ it noted that the three main problems faced by the region were: the formation of extremely inequitable societies, the decline in the

economic growth rate and its consequences for employment and income distribution, and the persistence of a situation of inequality and vulnerability as regards the region's external economic relations.

These appraisals revealed a great contradiction. The region as a whole was increasing its production and technological capacity and showed that it possessed great productive and export potential. This growing capacity was unable, however, to solve the structural problems of economic growth, social inequality, external vulnerability and dependence, and regional disarticulation. In short, Latin America was not succeeding in integrating itself at either the national or regional levels.

It was for these reasons that, in the early 1980s, the ECLA Secretariat asserted that the region was in the midst of a process whose trends did not show favourable prospects, and it recommended the countries of Latin America to reorient this process in order to guide it towards economic development and social change.

In view of these appraisals, the problems which have arisen since 1981 cannot be interpreted as the transient crisis of a form of development which could be described as successful in general terms. On the contrary, the negative effects caused in the external sectors of the countries of Latin America by the second oil price rise and the economic policy of the Reagan administration merely accelerated and aggravated an external crisis which it would at all events have been difficult to avoid. There can be no doubt that in formulating their economic policy the countries must now take as their starting point a structural situation involving more serious problems than those of 1980. Even before that year there were few possibilities of solving the economic and social problems through the prevailing form of development, but now it is obvious that the strategies for facing up for these problems call for a thoroughgoing review: it is the glaring facts themselves, rather than any doctrinaire convictions, which now make it essential to carry out this review.

It is generally accepted that the event which set off the present crisis was the extraordinary increase in the external imbalance which began in 1981 and later got worse. The truth is that there had been a marked external imbalance

³ECLA, *Latin American development in the 1980s*, Estudios e Informes de la CEPAL series, No. 5, December 1981.

ance of structural origin for years past, the best proof of this being the heavy external indebtedness which had been accumulated. As far back as 1978 the level and profile of this indebtedness caused ECLA to conclude that it would be impossible in the medium term to maintain the trends which had characterized the second half of the 1970s in this respect.⁴ Nevertheless, up to 1981 the international banking system considered that the situation was evolving favourably and thus continued to finance the heavy current account deficits. Two contrasting events took place, however, when the increase in real interest rates, the high level of indebtedness (much of it with very short maturities) and the interruption in the growth rate (if not a fall in absolute terms) of the volume and value of exports all coincided. These events were the considerable increase in the debt servicing costs, and the loss of the confidence which the international banking system had previously had in the solvency of the countries of the region. Within the space of a few months, these countries found it impossible to fulfill their external commitments, and they had to begin the difficult process of renegotiation.

It is interesting to note, by the way, that the possibility that the countries of the region may not fulfill these commitments, with obvious consequences for international economic relations, is seen by important circles in the centre and in Latin America as a dangerous menace striking at the very heart of the system. Paradoxically, however, during the 1970s and at this very moment the fact that 40% of the population of Latin America is in a state of extreme poverty has not caused any alarm at all in these circles.

In view of the importance attached to the external imbalance, the main objective of the 'adjustment process' has been to balance the external accounts, in which task the governments of the region, the international banking system and the International Monetary Fund have actively participated. The renegotiation of the debt is essential in order to achieve this objective, and for this purpose the international banking system seeks to impose conditions on

the domestic and external policy of the countries of the region in order to guarantee fulfilment of the new commitments deriving from the renegotiation; in order to backup these conditions it usually demands that each country should sign an agreement, or Letter of Intent, with the IMF as a prerequisite for renegotiation.

The general tenor of these agreements is similar to that of the traditional doctrine advocated by the IMF. As regards the general orientation of development, this doctrine reaffirms the supposed advantages of liberalization of the economy, reduction of the public sector and expansion of private enterprise, while it stresses the important role which international trade should play in guiding the allocation of resources. In its interpretation of the crisis, it emphasizes the excessive public spending and the unsuitability of the price system, and especially of the exchange rate, to the new circumstances. As a corollary, acceptable national policies generally aim to reduce the fiscal deficit and the real level of wages, to limit the expansion of domestic credit and public sector indebtedness, to increase some taxes, to raise or free controlled prices, to eliminate subsidies, to resume payment of the external debt, and to achieve a surplus on the trade account. When these agreements are compared with those of other periods, some change of emphasis is noted, since now the central question for the IMF is that of restoring the external balance, a somewhat more flexible position being adopted on some domestic targets such as those connected with the fiscal deficit or inflation.

This orientation of the adjustment processes was already the subject of much criticism in the past.⁵ Now, however, its recommendations seem to be particularly unfortunate.

To begin with, although we are witnessing the profound disarticulation of international

⁴ECLA, *Long-term trends and prospects of the development of Latin America*, E/CEPAL/1076 (1979).

⁵Raúl Prebisch, "Monetarism, open-economy policies and the ideological crisis", *CEPAL Review*, No. 17, Santiago, Chile, August 1982; Sidney Dell, "On being grandmotherly: the evolution of IMF conditionality", *CEPAL Review*, No. 16, Santiago, Chile, April 1981; Octavio Rodríguez, "La teoría del subdesarrollo de la CEPAL", Mexico City, Siglo XXI Editores, 1980; Samuel Lichtensztejn, "Sobre el enfoque y el papel de las políticas de estabilización en América Latina", *Economía de América Latina*, No. 1, September 1978.

trade and its utter failure as a stimulus for development, the IMF gives these facts a merely conjunctural character and reiterates its principles regarding the liberalization of external economic relations for the developing countries at a time when protectionism on the part of the centres is becoming increasingly marked.

Secondly, it proposes a distribution of the costs of the crisis which heavily punishes the Latin American countries and rewards the international banking system. The renegotiations are carried out as though the faulty assignment of the loans had been the exclusive responsibility of the debtors and there were no losses at all which should be shared. Furthermore, in these renegotiations the banks are applying surcharges, fines and costs which raise still higher the interest rates and potential profits of the banks. Moreover, it is well known that the international banking system is exerting pressure to obtain a State guarantee for credits which it originally granted to the private sector without any such safeguard.⁶

Thirdly, the use made of the economic policy instruments seems to be in line with a theory of operation of the economy which is no longer valid in the present situation. Generally speaking, the heterogeneity of the Latin American economies, the consequences of which have become still more marked during the crisis, makes it necessary to use less homogeneous policy instruments. Furthermore, as the crisis deepens these measures not only prejudice the economic flows but may also affect the net assets and productive capacity of the economies. In these circumstances, it is necessary to exercise great selectivity which the orthodox policy instruments are incapable of offering, at least to the necessary extent.

Let us take, for example, the effect likely to be produced by an across-the-board change in the rate of exchange for the entire economy which is not accompanied at least by corrective measures for particular sectors or groups of operations. On the one hand, this would not make it possible to increase the value of commodity exports, since if such measures were applied more or less simultaneously by all the develop-

ing countries —at a time when the developed countries are reducing their demand, running down their commodity stocks and establishing every kind of protectionist measure— all that would be achieved would be to damage the terms of trade for commodities without achieving any increase in the volume exported. On the other hand, in economies which have liberalized their domestic and external financial markets and in which indebtedness in foreign currency has become widespread, devaluation brings about tremendous upheavals in financial and business circles which eventually depress production for reasons which have no direct connection with demand or with the supply of imported inputs. Furthermore, in countries where the capacity of the groups affected by devaluation to defend their own interest has been underestimated, the effect of devaluations have rapidly been passed on to prices, and finally, the indirect negative economic and social effects of the devaluation on production, employment and real wages seem to have been underestimated in many cases.

Fourthly, it is extremely ill-advised to seek to restrict the action of the State at a time when the magnitude of the problems faced prevents an adequate reaction on the part of the private sectors, which in most cases are exhausted by the crisis and are crying out for public action.

It is therefore hardly surprising that the policies adopted have brought about consequences which are unsatisfactory in many aspects. Basically, either because of overestimating the action capacity of governments, underestimating the side effects of the policies, or assuming unrealistic financing conditions for the economies, their results have been far from meeting the targets and objectives originally proposed. Frequently, the agreements have proved impossible to fulfill only shortly after they have been signed, thus giving rise to a constant process of signing and revision.

Furthermore, these policies have shared out the external and domestic costs of the crisis in an inequitable manner. Reference has already been made to the unjust nature of the renegotiation of the external debt; at the domestic level, a large part of the cost has been transmitted to the sectors with the lowest incomes, eloquent proof of this being the high prevailing

⁶See the article by Robert Devlin in the present issue of *CEPAL Review*.

indexes of unemployment and the declines in real wages.

The drop in production, too, has usually exceeded the amounts originally bargained for, and instead of recovery the first half of 1983 shows only stagnation or aggravation of the depression. These results clearly reflect the stubborn effort to achieve a surplus on the balance of trade in goods and services. Likewise, the depression is having serious effects on the productive capacity of the countries. In some cases, factories have been dismantled, in a process which threatens to spread; in others, expansion projects have been abandoned because of the discouragement felt by businessmen. It is difficult to make an accurate forecast of the consequences of this attitude at the moment, but there seems no doubt that the policies applied have caused an appreciable drop in investment in many areas of production.

Perhaps the consequence of these policies with the greatest long-term significance, however, lies in the aggravation of some problems which were already serious before the adjustment process began. The net external indebtedness of Latin America is estimated to have increased over the period 1981-1983 by around US\$ 90 billion, while open unemployment and underemployment, which were already considered to be very serious problems in 1980, are estimated to have increased still further. The natural increase in the labour force due to population growth alone represents an increase of over 7 percentage points, and it should be borne in mind that the available information indicates that in many cases the absolute number of jobs

has not only failed to increase but has probably actually gone down. Likewise, the drop in the levels of investment has put off the possibility of attaining in the near future the level of economic growth which was considered essential at the beginning of the 1980s in order to give productive employment to the labour force and solve the main social problems of the region.

Finally, every day the functioning of the economies is becoming more costly and inefficient. The financial problems of the business sectors are getting steadily worse as demand either fails to recover or else shrinks even further, and their main concern is shifted from the problems of production to the struggle to obtain public resources to insure their survival: all considerations of efficiency or serious economic calculations lose importance compared with the need to keep their heads above water. The State for its part, subjected as it is to multiple demands, has often been obliged to allocate resources in line with criteria which have more to do with the economic and political power of those requesting them than a long-term view of the development process, and this has gradually reduced its operative capacity. The depression of production activities and its sequel have caused an increase in demands for new expenditure, while at the same time they have eroded both tax and non-tax sources of public revenue. In practice, quite independently of any ideological positions, everyone is calling for State intervention to save the situation, precisely at the time when the situation is depriving the State of resources.

II

Towards a new form of development

An analysis of the economic and social evolution of the Latin American countries from the 1970s up to the present crisis permits three main conclusions to be drawn:

a) The prevailing form of development was already in crisis at the end of the past decade, and the recession of the early 1980s has

simply accentuated the external and internal difficulties because its cost is being distributed unequally, both between the central countries and the periphery and within the countries of the latter;

b) The so-called 'adjustment policies' have been incapable of coping successfully with

the crisis: indeed, in reality they have instead intensified the structural shortcomings while being unable to check the deterioration in the situation; and

c) It would no longer be enough to be able to go back to the previous situation, since the crisis has increased the severity of some problems—such as external indebtedness, external vulnerability, levels of unemployment and underemployment, faulty income distribution, and the deterioration in production capacity—and these would not be automatically solved if the external situation as regards demand and prices returned to what it had been at the end of the previous decade. Nor indeed is it desirable to go back to that situation, since the crisis has shown up the defects of a form of development which the evolution of the 1970s temporarily and partially concealed.

It is therefore necessary to reorient economic and social policy towards a new form of development. This reorientation calls for a big effort in many respects, both as regards intellectual reflection and practical action. In the field of reflection, there are two main tasks to be accomplished: defining the broad outlines of the society which it is desired to build, and formulating criteria for advancing in the desired direction. In formulating these criteria, account must be taken from the very start of the restrictions and possibilities of the present moment, in order that the proposals may be given a pragmatic sense.

Naturally, this reorientation will only be viable if it can gain the majority support of the population, since this is an eminently political task. At the same time, however, the usefulness of the intellectual tasks should not be underestimated. With a view to collaborating in them, some ideas which could possibly be of use in the formulation of an economic and social policy in keeping with a new form of development are put forward in the following pages.

These ideas, as could hardly be otherwise, are of a general nature and are based on the principles mentioned in the introduction to this article. In translating them into concrete policies, the particular characteristics of each country and the specific problems faced in the short run must be taken into account. This has been the usual way in which ECLA has formulated its

suggestions, since although it has striven to find common denominators for all the countries of Latin America, it has also emphasized the need to take account of the differences between them, whether of a structural or conjunctural nature. The fact that there are problems common to the whole of Latin America justifies the suggestion of general ideas for tackling them, but the heterogeneity of situations between and within the countries means that caution must be exercised in making generalizations, and concrete policies must be of a specific nature.

When most of the countries are suffering from economic and social problems and short-term restrictions of a very similar nature, this favours policy proposals of a general type. Thus, the generalized nature of the problems and restrictions during the present crisis facilitates the sketching of some ideas for reorienting the process of economic and social change.

In this respect, two different areas may be distinguished:

a) Structural policies concerning the allocation of resources for long periods in basic areas of development where long lead times are required in order to obtain the desired results. These policies may be considered as intermediate links between the basic principles and the short-term policies. Outstanding examples of them are the policies regarding changes in production, the external sector, employment and productivity, capital accumulation and income distribution.

b) Short-term policies designed to relieve the most serious conjunctural problems such as the levels of consumption and employment of lower and middle strata, the deterioration of the production capacity, imbalances in the external sector, the financial insolvency of a large number of enterprises, public finance problems, inflation, and the definition of the role of the public sector in the crisis.

Before briefly setting forth some ideas in these two areas, it should be reiterated that the establishment of a new form of development is a long-term task which must be guided by the general principles regarding the formation of economically developed societies which are less dependent and less vulnerable with respect to the exterior, have a more equitable distribution

of wealth and income, and a democratic form of political organization.

Although many development strategies accept these principles, however, they often give very different priorities to them. Thus, for example, in the last decade many strategies were put into practice which considered economic growth to be the central objective because they assumed that it would enable the other objectives to be reached in the long run more or less automatically.

The development model suggested here, in contrast, gives top priority to the principle of equity from the start, considering that this is not only an end in itself but also an indispensable means for advancing towards the achievement of the other objectives. It is indeed true that, in view of its many-faceted character, equity can have a decisive influence on all policy orientations.

III

Structural policies

1. *International economic relations*

During the 1970s, Latin America changed its form of insertion into the international framework; in most cases, encouraged by the dynamism of international trade and the abundant supply of external financing, governments liberalized their international economic relations. To a greater or lesser degree, the liberalization schemes were based on a theoretical approach, advocated by important circles in the centres, which gives a central role in the organization of international trade and production to more or less static versions of the principle of comparative advantages. In the second half of the past decade the belief that liberalization was giving very positive results also spread: the volume of exports was growing at a high rate, and thanks to the abundant supply of external financing the region was apparently avoiding the effects of the decline in growth of the central countries. The Latin American countries which had been most seriously affected by the first increase in fuel prices seemed to be absorbing its impact, while those which had gone further in the process of industrialization were managing to change the structure of their exports and incorporate significant proportions of manufactures and semimanufactures in them.

All these changes were hailed as successes in the progress towards more dynamic incorporation into international trade and as notable advances in the region's defence capacity *vis-à-*

vis the cycles suffered by the centres. Unfortunately, the present crisis has made it clear that although some progress was indeed achieved, none of the great efforts made in this direction have materially altered the asymmetry of external trade relations, while on the contrary the new financial relations have increased the region's external vulnerability.⁷

Thus, it can be seen today that almost two-thirds of the region's exports continue to be made up of raw materials and fuels sold to the developed countries and that, in spite of the success achieved by some countries in their efforts to change the composition of their exports, the trade of the region as a whole continues to be essentially asymmetrical. The present situation has also once again brought out the costs of this situation, since the apparent advantages of the boom periods are seen to have been more than offset by the serious damage done in the periods of decline. There can be no doubt that the views which the developing countries have repeatedly set forth in the International Development Strategies, calling for a new international order

⁷The significance of international economic relations in the development of Latin America has been examined most searchingly by Aníbal Pinto. See this author's articles, "The periphery and the internationalization of the world economy: significance and consequences", *CEPAL Review*, No. 9, Santiago, Chile, December 1979, and "The opening up of Latin America to the exterior", *CEPAL Review*, No. 11, Santiago, Chile, August 1980.

with a more symmetrical distribution of production and trade, have gained renewed significance after the experience of the 1970s and the present crisis.

By the force of events, the present situation is restoring the importance of regional industrialization and trade, since the impossibility of relying now on the supply of imports available in the latter years of the past decade is once again establishing a potential space for Latin American industry. The trade restrictions of the centres are making clear the need to replace extra-regional trade to some extent by intra-regional trade. In the latter, special attention must be paid to the trade in manufactures, since it is here that the biggest supply problems exist, because of the impossibility of keeping up the previous levels of trade with the centres and because of the fact that, as regards raw materials, the most obvious opportunities have already been exploited. Naturally, the bigger countries and the transnational corporations will be better prepared, in principle, to take advantage of these opportunities, but they should share these possibilities with the rest of the region. One way of achieving this would be to provide selected incentives for the smaller countries to advance in the industrial processing of their natural resources and to help their raw materials or energy sources to find markets in the larger countries, of which in many cases they are only marginal suppliers, while above all the possibilities offered by compensation machinery should be fully used. The basic objective is thus to provide a stable long-term horizon for a process which is becoming a necessity through the force of circumstances.

The asymmetry of the relations in the financial field is even more marked. The crisis affecting the international monetary and financial arrangements is well known, but a constant factor in the system seems to be the concentration of the decision-making power in the hands of a few countries, and especially of the United States. The present effects of the monetary policy imposed by that country are an excellent illustration of the way in which the periphery is being affected by that policy without, of course, having been able to play any part in its formulation.

By heavily indebting itself with the inter-

national private banking system during the 1970s on terms and for periods very different from those agreed in the years following the war, the region became extremely vulnerable to the fluctuations in the international financial markets. Thus, although it was able to defend itself from the drop in the growth rate of the central countries in the second half of the 1970s it became very dependent on the fate of a system which was beyond its control. As the recession in the centres caused a drop in the value of Latin America's exports, it became evident that the level of indebtedness had gone beyond prudent limits. At the same time, the region lost its creditworthiness with the private banks, thus bringing about a sharp drop in net external financing which further aggravated the regional economic situation.

It then became clear that the liberalization of financial markets, far from having given rise to efficient policies as a result of the predominance of the private sector in the international banking market, had led to the unsuitable use of resources and had placed the economies of the region in a dramatic external and internal dilemma. In contrast with what had happened in previous decades, when the resources of the international public banking system, which had made up the bulk of the external financing, were supplied in most cases for carrying out big projects on economically viable terms as regards repayment periods and interest rates, in the 1970s the resources were distributed in an unsuitable manner for the economy, were not always used to finance investment, and—in the last few years—were granted at costs so high that few economic activities which were not of a speculative nature could expect to pay them. As a result, the present crisis spread to all types of activities and meant that the adoption of classical measures for tackling balance-of-payments problems, such as devaluation, brought about negative domestic effects of a magnitude never experienced since the end of the war.

In short, the crisis has shown up the fundamentally faulty operation of the international monetary and financial system. The urgent need for change is now clear. In addition to the need to share losses, extend repayment periods and reduce interest rates—essential measures for tackling the external debt problem—it is

necessary to put forward once again the many proposals which the region made in the past and which should be taken up again today with such changes as the circumstances make advisable. In this respect, the restoration of the dominant role of regional and international public bodies and the reform of the rules in order to give due participation to the periphery are some of the central criteria which should guide the restructuring of the international financial system. The urgent application of measures to deal with the present situation such as the expansion of the resources of the International Monetary Fund, the World Bank and the regional banks and the increased issue of Special Drawing Rights linked with the development of the periphery should be only the beginning of a process of reform which is vitally needed today.

2. *Changes in production*

The main features of the transformation of Latin American production since the war have been rapid industrial expansion and the modernization of part of the primary and services sectors. In contrast with what happened in the early stages in the developed countries, however, this progress in the region did not bring with it a significant degree of inter- or intra-sectoral integration, while the heterogeneity of production methods within and between the different branches grew still more pronounced.⁸ Nor did this development bring about any significant change in external trade, and except for some isolated praiseworthy efforts, external trade continued to be characterized by its asymmetry. Efforts to break this asymmetry, especially in the field of manufactures, have run into the growing protectionism of the centres. These phenomena can largely be explained by the unequal distribution of income, which created a domestic market in which the demand for most lines of production, taking similar per capita income groups, was smaller and more dispersed than for the same goods in the developed countries.

⁸ECLA, *Estrategias de desarrollo sectorial para los años ochenta: Industria y agricultura*, Estudios e Informes de la CEPAL series, No. 9, 1981.

As from 1975, changes are to be seen in the nature of the transformation of the system of production. The liberalization of the rules governing external trade and/or external financing, at a time when there was an abundant supply of external financing and a sharp export drive by the central countries, weakened both the incentive to industrialize and economic dynamism in general, while strengthening commercial and financial activities, especially those connected with external trade. At the beginning of the 1980s, the need to restrict imports already bore witness to the increase in external vulnerability, and in 1982 the most serious depression of production since the end of the war took place.

The great influence exerted on the structure and evolution of production by income distribution and by the form of insertion of the region into the external economy are thus obvious.

The policies aimed at changing the system of production which should prevail in a new form of development should be based essentially on the principles of greater equity and autonomy and less external vulnerability. Considerations of distributive equity should guide the public and private accumulation effort and the restructuring of the installed capacity. Support for peasant agriculture and for the types of industry and services supplying goods for the broad masses would impart a new structure to employment which, together with the adoption of income distribution measures, would generate national demand compatible with a more homogeneous and less vulnerable structure of production.

Demand would be concentrated on fewer production, which should be less complex technically and should therefore call for fewer imported inputs. This would facilitate greater concentration of the industrial effort on groups of products of widespread use, with greater vertical integration of supply. In this way, industry could supply an appreciable proportion of domestic demand and at the same time reduce the asymmetry of trade in industrial products with the exterior. Public consumption, especially of goods and services generally destined for groups of lower income and, in particular, those living in situations of extreme poverty,

should naturally play a central role in the new structure of demand.

A new form of insertion into the international and regional economy would also help to reorient the transformation of production. External restrictions have already significantly affected the level of imports, and everything seems to indicate that these restrictions will largely persist in the next few years. This consequently opens up a new opportunity for import substitution processes. If these processes are combined with greater regional integration and with domestic markets which are in line with more equitable income distribution, then their influence and scope will be broader than those of the period after the war. Furthermore, if the region manages to change the protectionist rules currently governing international trade, it will be able to give a higher degree of processing to the primary products which it exports.

The experience of countries which are now developed shows that an effort of this type, although calling for persistence, is no pipe dream. Indeed, in certain lines of industrial production some Latin American countries have had considerable success where their domestic markets are big enough and when they have made persistent efforts to enter world markets.

The transformation of production thus proposed calls for a physical and industrial infrastructure and financial support which only the State can make possible. If public action were concentrated on these broad tasks and the necessary resources were made available, considerable successes could be achieved.

In this respect, the regional demand for capital goods such as those connected with transport of energy generation offers great prospect for the efficient substitution of imports at the regional level. The complexity which characterizes industrial development will make it necessary to accompany the traditional measures to promote the sector with others connected with programmed public sector purchases, the creation of long-term financing systems, avoidance of the acquisition of foreign technology in 'packages', and promotion of the participation of regional engineering skills in

the design of factories and production programmes.

3. *Economic growth and the absorption of the labour force in productive work*

Among the most decisive economic and social criteria for guiding the long-term policies to deal with the crisis, special consideration must be given to the need to give productive employment to the largest possible proportion of the labour force. One of the most stubborn problems in the development of Latin America has been the inability of economic systems (to varying extents, depending on the countries) to give productive employment to all persons of working age who are looking for jobs. As a result of this, unemployment, underemployment and over-manning persist, the latter especially in the tertiary sector. The causes of this problem are to be sought in the scanty relative dynamism of the economic process, the structural heterogeneity of the system of production, and the rapid population growth rate. This latter, furthered by economic and social development itself, which has contributed so notably to the reduction of mortality rates, has made it very difficult to absorb the whole working population in productive jobs. This is not only because the Latin American population growth rate is one of the highest in the world, but also because its consequences as regards the increase in the labour force still manifest themselves many years after there has been a drop in fertility. Furthermore, rapid urbanization has changed the distribution of the labour force, highlighting in urban areas problems which were less evident in rural zones.

The present crisis has aggravated this problem in at least two main ways: it has prevented the region from continuing the previous rate of absorption of labour in productive jobs—which, although insufficient, was nevertheless quite high⁹ and it has stimulated technical change in the developed centres tending towards the more intensive use of capital. In many of the central countries there is a clear aware-

⁹Norberto E. García, "Growing labour absorption with persistent underemployment", *CEPAL Review*, No. 18, Santiago, Chile, December 1982.

ness that one of the main causes of the crisis at present being experienced is the slackening in the growth rate of productivity, and that an increase in this rate is an essential condition for emerging from this situation. Whatever the economic mechanisms used to achieve this objective, there can be no doubt that sooner or later they will take the form of technological changes which involve the highly intensive use of capital, and they may even give rise to a third industrial revolution.

Latin America will be no stranger to these changes from the point of view of consumption, and it should not be so from the point of view of being a producer and exporter of manufactures either; if it wishes to gradually increase its importance as an exporter of these goods, it must make enormous efforts of accumulation, modernization of its physical resources, and training of its labour force, at least in those sectors where it currently has relatively greater potential, in order to go along with the technological changes which are looming up on the horizon.

How are these enormous and unavoidable efforts to reactivate crisis-wracked economies and to participate in the new forms of production which are taking shape in the developed countries to be reconciled with the need to give productive employment to a large and, for many years to come, still growing labour force?

The experience of the last years has left us some lessons in this respect. To begin with, it is necessary to discard once and for all the idea that the growth of one or several sectors will automatically bring with it the development of the most backward ones: such automatic mechanisms simply have not worked in the countries of Latin America, where there is still a high degree of sectoral, social and regional heterogeneity in the distribution of levels of productivity and average income.

In view of these facts, some development strategies have been formulated which have sought to promote the 'spearhead' sectors and at the same time establish procedures for distributing part of the surplus generated in these among the rural and urban groups which were being increasingly left behind, with the aim of improving their living conditions. These strategies do have the positive feature of being concerned to combine economic growth with social

equity, but they do not give due attention to the fact that the firmest foundation for equitable distribution of the fruits of development lies in the systematic effort to overcome structural heterogeneity by raising the productivity of the entire labour force. In this respect, strategies aimed at coping with such complex demands as those for economic growth in an era of profound technological changes and absorption of all workers into productive jobs in a period of rapid growth of the labour force must at the same time be able to give very selective stimulation to this growth and establish deliberate arrangements whereby part of the surpluses generated by the most dynamic branches can help to raise the levels of productivity and living conditions of those lagging behind. In this respect, giving high priority to agricultural development in line with the potential of the sector itself and of its population is both vital and urgent for most of the countries of Latin America.

4. *Capital accumulation and income distribution*

Another fundamental aspect of the policies which should be applied in order to emerge from the crisis and reorient development is that regarding the domestic accumulation of capital, since it is clear that external saving will not have the dynamic role in the immediate future which it had in past years. As regards the volume of capital which should be accumulated, the answer is very simple: as much as is socially and politically possible. Even before the present crisis the ECLA appraisals considered that the effort being made in this respect was not sufficient to give productive employment to the entire labour force and to improve the living conditions of the neediest citizens, and the deterioration which has taken place in the situation since then means that efforts must now be redoubled.

In reality, the most crucial questions regarding capital accumulation are of a political nature: which social groups are to bear the burden of this accumulation? who is it to benefit?

The recent years offer some very useful lessons in this respect too, which make it necessary to discard conventional answers to these questions because they tend to be inequitable, inefficient and undemocratic. When the respon-

sibility for domestic saving and productive investment fell on the economically powerful groups, the expected results were not attained, because these groups often preferred to engage in conspicuous consumption imitating the life styles of developed countries, speculation and unproductive investment. It is therefore neither socially just nor economically efficient to seek to increase domestic saving through conventional policies aimed at transferring income from the rest of society to the wealthy groups in order that the latter may invest in priority economic and social areas in line with the demands of the crisis and the needs of development. Furthermore, in many Latin American societies it does not seem that these policies could any longer be easily applied, because of the defence capacity of wage earners, the already very considerable reduction in the real income of the latter as a result of stabilization policies, and the existence of democratic governments which rely on these wage-earning groups for an important part of their political support.

It is also important to note that conventional policies are usually imposed as if they were the expression of objective and neutral technical criteria: the impression is fostered that the social distribution of the costs involved in them should be accepted as the inevitable manifestation of a natural law. There can be no doubt that there are important technical criteria which deserve to be taken into consideration, whatever the socio-political structure in which the policies are applied, but the social distribution of the costs is above all a question of political decisions: presenting it as a purely technical question means concealing the political content of the decision.

It is therefore necessary to increase the degree of transparency of the entire process of decision-making on such crucial issues. Such greater transparency of the technical and political aspects would enable all social groups to define their interests and orientations clearly, thus laying the bases for a social compact which would reflect a higher level of political rationality and democracy.

If conventional capital accumulation policies are to be rejected for the above reasons, then what path should be followed?

As regards the social origin of the re-

sources, it should be emphasized from the very beginning that both the measures on accumulation and distribution and those on fiscal and monetary matters should be taken within the framework of a policy of general austerity, since the crisis and development call for inevitable sacrifices. The austerity should be equitably shared, however, that is to say, it should demand more from those who have more, while its demands should gradually be reduced in proportion as the level of family income goes down. This policy of procurement of resources should be accompanied by dynamic redistribution so as to raise the income of the lower strata as a matter of priority, when economic evolution permits this.

As regards the non-conventional mechanisms of appropriation and allocation which should be used, the experience of some capitalist central countries suggests that emphasis should be placed on the tax system; in the most successful cases, a combination of high taxes on profits and on the consumption of the high-income groups and strong incentives to selectively oriented productive investments has been used. Even if the tax instrument could be effectively used in Latin America, however, it should be noted that although the path chosen by those countries has helped to promote accumulation and economic growth in them, it has also caused great concentration of the means of production, and in the long run this could create important obstacles to the democratic process.

These considerations show how important it is that the capital accumulation process should also help to create and strengthen equitable distribution of wealth; if conventional and Keynesian policies have tended to concentrate this, those which should be applied now should promote the reduction of such trends. Measures should be taken in two mutually supporting areas to this end.

On the one hand, the State should play an important role in the processes of appropriation and allocation of resources, but for this purpose it is essential that it should be democratized, that is to say, that the decisions taken in these matters should be the result of institutional procedures in which the whole community feels itself to be fully represented. In reality, the State has

not always wanted or been able to appropriate the necessary resources for accumulation, and frequently it has not allocated them in line with the needs of development. This behaviour is explained above all by the fact that in the appropriation and allocation of public resources there is often a struggle between different élites seeking to orient these resources for the benefit of their own needs and interests rather than those of society as a whole. The democratic machinery should prevent the exertion of any decisive influence on these processes by such sectoral élites, whether private or public, civil or military.

On the other hand, the public allocation of resources for capital accumulation does not mean that there should be a tendency towards State control of the production apparatus. Instead, in the new form of development different forms of organization of production combining State, private and co-operative ownership and management should exist side by side. Democratization of the State, co-management in State and private enterprises, and co-operative forms of production are those which give the greatest hopes of true democratization of ownership and management, and should therefore be promoted in a priority manner.¹⁰

IV

Short-term policies

It has already been noted that the economic and social situation of Latin America as a whole in the first half of 1983 does not, in general terms, show any signs of improvement over 1982. Indeed, in many cases it has deteriorated in such aspects as unemployment, inflation or the decline in productive activity. The living conditions of most of the population have deteriorated even more, which is a serious matter, especially bearing in mind the low level at which they already stood at the beginning of the 1980s. As already explained, the adjustment policies have not had the desired results. In these circumstances, there is generalized awareness that it is urgent to take measures in the short term; thus, although formulating a new type of development takes a long time, measures in keeping with the new priorities should be taken soon, above all in order to bring some relief as a first priority to the situation of the most underprivileged strata. In addition, and simultaneously with the application of these priority measures, others should be taken in the areas where it appears to be essential to bring about some improvement or change the line of approach. The most important of these areas concern the defence of the national economy at the popular level and the establishment of a situation as regards domestic prices and financing

which will enable an acceptable level of economic success to be achieved in the production sector; the procurement of sufficient foreign exchange to make possible a level of imports capable of guaranteeing minimum targets of production, essential consumption and employment, and the preservation of production capacity in the economic and social infrastructure and in the sectors governing mass consumption, exports and investments which are not very demanding in terms of external resources.

1. *Defence of the national economy at the popular level*

The crisis has made the problems of the lower-income groups still more acute. There are many ways in which the effects of the crisis are transferred to the mass of the people: price rises, drops in real wages, increased unemployment, and reduction in public expenditure, which, in addition to its economic effects, brings about a consequent deterioration in educational services, health, nutrition, housing, etc. The low-

¹⁰Raúl Prebisch, *Capitalismo periférico. Crisis y transformación*. Mexico City, Fondo de Cultura Económica, 1981.

income non-wage earning groups are also affected by the difficulties which exist in transferring monetary income to them to compensate at least partly for their problems, and they also suffer when, for budgetary reasons, it is decided to do away with subsidies or price controls in respect of basic consumer items such as bread and widely used fuels. While acknowledging the variety of situations registered in the different countries, it nevertheless seems essential to design emergency programmes to help the groups most seriously affected by the crisis.

Thus, it is urgently necessary to make changes in incomes policy. Measures of a macroeconomic nature aimed at reducing public expenditure should be replaced—or complemented, depending on the particular cases—by others which increase the expenditure aimed at certain groups and reduce that oriented to others. In this respect, wage and price policies should be handled with great selectivity. The drop in the real wages of the lowest income groups has drastically reduced, in many cases, the demand for goods which have a low import content and involve high labour density; in contrast, other groups with more capacity to stand up to the crisis—partly because of the possibility of resorting to income drawn from their wealth—have kept up a form of demand which seriously affects the balance of payments and generates little employment. In general it would be desirable to achieve some recovery in the real wages of the lower income groups, but the wide variety of national situations does not permit of generalizations. The selective management of prices is also called for if it is desired to promote one particular 'shopping basket' of goods rather than another and if it is desired to defend the groups whose income does not come from formal occupations. Naturally, increasing employment—especially that of less-skilled workers—will play an important role in improving family income. At the same time, it is necessary to pay special attention to the defence of employment and wage rights won through trade-union activities; in many cases the high level of unemployment has created suitable conditions for the employer sector to reduce real wages and employment in unacceptable ways.

The consumption of the lower income

groups is moreover usually considerably influenced by public expenditure, and the latter should therefore be handled with extremely selective criteria. On the one hand, investments should be selected with a keen eye to employment criteria, while on the other, as regards public consumption, it is desirable at least to keep up the level of that destined for the groups most severely affected by the crisis. There are cases where the supply of mass consumption products depends on imports or State subsidies; in these cases, there is every justification for the execution of programmes aimed at guaranteeing such supply by giving access to these goods to the poorest sectors and avoiding the seepage of subsidies to other social groups.

The same policy criteria should be applied as regards social public expenditure. In a crisis situation it will be very difficult to increase the proportion of such expenditure in the total, so that policies should be aimed at redirecting its allocation in order to make it more equitable.

Social policies in Latin America have been criticized for many years past on the grounds that they have tended to favour the middle strata in particular, to the disadvantage of the lower strata. If a change in this orientation in line with criteria of greater equity was already necessary before the crisis, then it is much more so now, when resources are tighter and it is not possible to satisfy the needs and demands of the poorest groups through further expansion of social public expenditure.

2. Domestic financing

The present crisis has given rise to extremely serious domestic financial imbalances. There are many situations where it would be impossible to apply policies aimed at increasing production or tackling balance-of-payments problems without first of all solving the financial imbalances. This problem stems from two main sources: external indebtedness, and domestic policies.

The main features of the external indebtedness are its large size and the fact that the credits have been obtained at extremely high interest rates. The ways in which these credits are passed on to domestic users vary from country to country. Sometimes the dollar or another for-

eign currency is used as the unit of calculation, while in other cases the exchange risk is absorbed by the State or financial intermediaries. Interest rates are likewise dealt with in different ways: sometimes they are transferred directly to users; in other cases they are fixed by domestic financial intermediaries and are considerably higher than external rates; while in many cases the State subsidizes users by lowering the rates.

In these circumstances, the sharp devaluations and acute processes of inflation caused by the external sector crisis have led to all kinds of transfers of wealth and profound changes have taken place in the operational situation and net worth of persons and enterprises. Some have suffered heavy losses, while others have had big gains, and this has given rise to liquidity whose use is very difficult to control today.

The situation has also been very diverse as regards domestic financing policies. In many countries, systems of contracting credits were introduced which involved clauses linking the debts to foreign currencies, thus making them subject to exchange risk. Loans in national currencies, too, have been granted on very varied terms which have included high real interest rates, credits indexed to inflation, and negative real rates of interest. To the extent that the crisis has speeded up inflation or forced devaluations, the combination of these elements has also brought about substantial transfers between sectors.

As might be expected, the public budget did not remain unaffected by these upheavals. In some cases it has absorbed the external problems of the productive and financial agents and has come to the rescue of the most seriously affected sectors in a makeshift fashion and under the pressure of events. The reduction in the level of activity has brought with it a drop in tax and non-tax revenue, while at the same time the crisis has been increasing pressure for greater expenditure, although many of the adjustment programmes seek to reduce this. In these circumstances, fiscal policy has sometimes been handled more in the light of economic and political pressures than in line with a programme having clear objectives.

The economic situation has also suffered considerable changes at the level of the middle and high income groups. Unfortunately,

speculative investment has been in vogue in many countries: there are now appreciable amounts of funds in the hands of the private sector which move with great flexibility among activities connected with speculative sectors, emergency loans to the most seriously affected sectors at high real interest rates, pressure on the foreign currency market, and other investments of a speculative nature.

In short, a domestic financial situation has been created which is very difficult to handle. Frequently, businessmen have been forced to replace sound economic calculations with considerations based solely on the need to gain access, at any cost, to resources—especially public resources—which will enable them to survive; many have done this in the hope that future financial arrangements will enable them to transfer these costs to other sectors.

In some countries it is urgently necessary to put an end to this situation so that the State can recover control of the financial market and neutralize the enormous mass of resources used to stimulate speculative activities. In order to do this, the State must prohibit the possibilities of speculating (when these exist legally) and create one or more preferential long-term saving options which enjoy its backing.

Reduction of the real interest rate is also of the greatest urgency, since in some countries there are still interest rates which are completely out of keeping with any reasonable possibility of return. In this respect, however, it is necessary to apply a selective criterion regarding credit. Its allocation cannot be left in the hands of financial groups which are themselves in a compromised situation, and it is also evident that not all sectors or enterprises can be saved; the establishment of a reasonable real interest rate is only compatible with the forced and selective restriction of demand for credit.

The public budget also calls for reorganization. As regards revenue, the conventional procurement measures are not enough: policy in this field should be aimed at the application of measures to procure revenue from the groups which still have a high level of consumption and have liquid assets available for speculation.

Public expenditure, too, should be oriented in line with the principle of social

equity and linked with the priorities approved for the productive sector; it is not possible to satisfy the demands of all sectors at once, and any attempt in this direction would necessarily bring about an increase in inflation caused by the bigger fiscal deficits.

Only a selective financial and fiscal approach can restore the levels of production, budgeting and prices which will make possible non-speculative economic calculations: an essential condition for the rational functioning of mixed economies in which the private sector has an important economic role.

As already noted, the problem of wages and employment constitutes a challenge for the inflation control policies which may be adopted in the new form of development. There can be no doubt that in countries where unemployment has reached very high levels, this problem should be solved before tackling that of the drop in real wages; nevertheless, this latter problem is bound to arise in all countries when designing policy. Keeping real wages within limits compatible with domestic and external supply is an absolute necessity if it is desired to avoid hyperinflation. In democratic societies, however, the wage-earning groups can hardly be expected to accept a sacrifice comparable with that which has been demanded from them in the past unless at least two requirements are fulfilled: the biggest sacrifice must be made by the groups with the highest income, and capital accumulation formulas must be applied in which the wage-earning groups feel themselves to be authentic participants, not only in the sacrifices but also in the benefits.

3. *The balance of payments*

There are two short-term priority objectives in this area: to reduce as much as possible the pressure of the external indebtedness, and to find a way of handling the trade balance on goods and services which is compatible with the selective policies applied in the production and financing areas.

In the short term, the pressure of the external debt servicing is manifested in two ways. One of them, which is of a fundamental nature, lies in the impossibility of honouring the short-term commitments, while the other which is of

a formal nature, is connected with the problems of living in a situation of constant crisis which makes it necessary to have recourse to partial negotiations, bridging loans and other emergency solutions.

The problem of the external debt is very complex, as are its solutions; when discussing the latter, some questions arise which are worth setting out briefly:

i) Should the Latin American countries negotiate separately, together, or separately but using common criteria?

ii) Will the transnational banking system accept capital losses as the national banks are doing at the domestic level?

iii) Will the renegotiation cover the short-term credits whose renewal means keeping the crisis still latently in being?

iv) How much net external financing will the international public and private banking system be willing to provide?

v) What additional costs in respect of interests, fines, etc., should be accepted in the renegotiation?

vi) How are the results of the renegotiation of the external debt to be passed on within the economies?

vii) Should public backing be given for the private external debt?

viii) Should formulas be applied which could relieve the short-term situation, such as periods of grace, linking of payments with the terms of trade, or other measures connected with the value of exports?

ix) What domestic policy measures should accompany the renegotiation, special importance being assumed in this respect by the efforts to achieve trade surpluses which will help pay the cost of recessive policies?

It is not possible to answer all these questions, but from the point of view of a new form of development some general considerations may be mentioned which could serve to orient a renegotiation policy.

On the one hand, the bargaining power of governments should be strengthened in proportion as political processes are democratized, since it will be clear to creditors that it is impossible to apply policies which impose new sacrifices on the population; a similar effect will be produced by progress in regional co-operation and

integration. On the other hand, the possibility of the countries facing up to their debts without the foreign banking system accepting any capital losses or the State giving its backing to private debts could only be justified to some extent if the renegotiation were sufficiently flexible to avoid any accentuation of recessive policies, if reasonable periods of grace were given, if real interest rates which are impossible to pay except through speculative ventures were eschewed, and if the creditors agreed to make the payment of the debt conditional upon an improvement in foreign trade as regards volumes and prices. If the negotiations do not include these conditions, they will be proposing unrealistic solutions and will be placing a millstone around the neck of the Latin American countries, with the corresponding social and political consequences.

At all events, it seems illusory to expect any spectacular results in this field in the short term; the situation of crisis will continue for quite a long time in most of the countries, obliging to manage their foreign trade under totally abnormal conditions.

In the field of international trade it must be noted from the very beginning that exports are faced with very diverse situations. There are a large number of products, especially commodities, where export incentives do not produce any significant effects as regards an increase in the volume or value exported; the problem in these cases lies in the depressed demand of the developed countries and the protectionist measures which they have taken. Consequently, for these kinds of exports a devaluation in real terms or some other financial incentive is normally only translated into an internal transfer of resources and has few repercussions on the trade balance. For other products, however, especially those of industrial origin, State support may be of great importance, both in the negotiations for tackling the protectionism of the centres and as regards the application of financial incentives which will enable countries to maintain and increase their competitiveness. Consequently, this field requires different measures, and a homogeneous set of measures may not therefore be effective.

Until now, imports have been one of the central concerns of adjustment policies, for their reduction with a view to achieving a trade

surplus has been seen as an indispensable element for balancing the economy. The means used for this are varied: some of them are selective, such as the prohibition of certain imports considered to be non-essential, differential increases in tariffs, or the differential handling of the different items in the public budget; others are of a general nature, such as devaluations; while in some cases, through the financial and monetary policies applied, sharp depressions have been provoked which have affected the economy as a whole.

According to the new form of development proposed here, it is not acceptable to apply measures of a homogeneous nature which provoke sharp recessions in production with inequitable imposition of the costs mainly on the least privileged groups. Such groups, which have little wealth to use as a buffer mechanism, are severely affected by unemployment or drops in real wages. The system of production, too, suffers severely from this type of measure. It is therefore advisable to apply selective import restriction and export promotion policies which are in line with measures of the same type taken at the domestic level, all these actions being aimed at guaranteeing certain minimum levels of production and consumption.

If policies to increase domestic saving and productive activity are applied, the selective import policy must be complementary to these, for limitations on consumption by the high income groups should coincide with a drop in non-essential imports, and difficulty in importing should open the way to import-substitution policies and greater domestic production activity.

4. *Maintaining production capacity*

It is probably unanimously agreed that it would be desirable to increase production and reduce unemployment, but there may be doubts regarding both the possibility of doing this and its consequences. It should therefore be stressed that reactivation is both possible and necessary, while its concrete significance should not be left in doubt. Thus, reactivation is usually used in the sense of restoring the previous level of functioning of the economy in all sectors and branches, but in the present circumstances this is an unrealistic aim and attempts to achieve this have

brought about a rapid increase in both the domestic and external imbalances.

What is possible, is to reactivate the level of production of certain branches, while accepting that it will not be possible to reactivate others, such as commercial and financial branches aimed at supporting the consumption of imported goods by the high income groups.

The first set of branches of production which should be stimulated is that serving to satisfy the 'shopping basket' of goods and services which form the basis of mass consumption; many of the branches of the agricultural sector are concrete examples of this. The need to ensure in the short term both the supply of goods of agricultural origin and the productive absorption of a high proportion of the rural labour force make it desirable to attach priority attention to the recovery of this sector.

Likewise, the physical and industrial infrastructure must be preserved: the creative effort and accumulation of many generations

which have gone into these constitute a national heritage which cannot be sacrificed in the pursuit of short-term macroeconomic goals.

A third group of branches whose production should be stimulated are those whose exports could be affected by their present cost structure. Special attention should be given here to those manufactures which won markets for the region during the 1970s and which must now be defended.

Finally, it is necessary to stimulate investments which are not only identified with the objectives of the new form of development but also have external financing from international public agencies, use few imported inputs or make very intensive use of labour. In all these cases it is a question of stimulating sectors selected because of their contribution to the new form of development. Thus, the short term is seen as the launching period of a new style and not merely as a time for the emergency rescue of the old form of economic and social administration.

V

The essential political direction

The criteria proposed for orienting economic and social policy call for firm and deliberate direction on the part of the State. The varied political experience of Latin America makes it clear, however, that there are no private or public mechanisms or institutions which alone can ensure the efficient execution and proper orientation of the economic process. There has often been a seesaw movement in ideas which has led to the State or the market, democratic or authoritarian institutions being presented either as a *deus ex machina*, which solves everything by its mere presence, or as the guilty parties responsible for all political and economic problems.

This to-and-fro movement is closely related to the historical process. The crisis of the 1930s led to generalized pessimism regarding the market mechanisms and gave rise to politico-institutional arrangements in which the State and planning played the decisive role; the crisis of these latter elements restored faith in

the virtues of the former, and now again, in their turn, these have been deeply discredited by the present disequilibria. Similarly, the confidence placed a few decades ago in the mutually fruitful relationship between economic development and democracy was eroded by the difficulties of reformist and populist régimes and gave way to the rediscovery of the assumed virtues of social discipline and authoritarianism, which now, once again, are threatened by the growing impetus of democratic ideals.

In these circumstances, the present economic crisis has once again raised the old question of which is the most favourable politico-institutional system for promoting development and facing up to the aggravated conflicts of the present time. If we look back at the history of Latin America in search of an answer, the initial impression obtained coincides with what was stated earlier to the effect that neither greater State intervention, nor a return to

democratic principles, nor much less the predominance of an authoritarian order or of the market laws are sufficient on their own to guarantee the proper performance and orientation of the economic process. The problem of the coherence of the economic and political institutions and processes does not allow of simplistic and unilateral solutions, but requires instead that each of these institutions should be objectively appraised with regard to its achievements and failures, its possibilities and limitations.

As is well known, the reappraisal in recent years of the role of the market in various countries of the region was based on the conviction that its free operation would guide the main economic decisions better, since in addition to its supposed virtues in achieving the efficient allocation of resources and the equitable distribution of income, it was believed that this mechanism would avoid abuses of power through its impersonal objectivity based on respect for economic laws.

The economic crisis of the countries which placed their trust in the market mechanisms has once again revealed the true nature of the market, which is simply that of a mechanism subordinated to the existing economic structure. In view of this, it cannot direct the process of development, since this process has economic, social and political objectives which deliberately seek to bring about changes in that structure. The current generalized abandonment of market mechanisms in favour of growing State intervention in order to face the crisis is further confirmation that while the market may have economic and political virtues, these do not include the power to direct development properly or to tackle crises effectively alone.

Because of the limitations of the market, it is essential that the State should have a decisive role in the running of the economic process, above all in times of crisis. It is important, however, not to fall into the technocratic illusion that the mere fact of State intervention can guarantee a reasonable degree of efficiency and legitimacy: State intervention in the economy can also be inefficient and inequitable. The problem is that the State has frequently been under the influence of economic and political

power groups: instead of leading them it has been led by them.

The actual performance of the State and the market in the reorientation of development depends to a large extent on the structures on which they are based. Thus, the market could play a role in the efficient orientation of production and consumption if it were based on an economic structure in which wealth and income are distributed in an equitable manner. Similarly, in order to be the proper expression of the interests and demands of the majority of the population, the State apparatus must not only be based on a democratic political system but must also democratize itself.

In this respect, in order to achieve a higher degree of efficiency and legitimacy many Latin American States should improve their performance as regards co-ordination and concertation. Co-ordination refers above all to the need for the State apparatus as a whole—central and regional, administrative and decentralized—to have a co-ordinated manner of operation. There can be no doubt that in some countries of the region the effects of the crisis have been aggravated because of the disjointed action of the State apparatus, which of course reflects not only the existence of technical and political problems but also, and above all, sectoral bureaucratic interests in the main public sector institutions and enterprises. Concertation is connected in particular with the capacity of the State apparatus to reflect the interests of social groups, orient their action and unite their will for the purpose of achieving common objectives. While the co-ordination of the State apparatus is a necessary and principal condition for its efficiency, concertation lies at the heart of the legitimacy of the State in pluralistic mixed-economy societies like the majority of those in Latin America. As is well known, co-ordination and concertation form the essence of planning, which has a fresh opportunity to show its usefulness in the present circumstances of Latin America.

There can be no possible concertation without institutional machinery which permits and guarantees the participation of the various social groups in all important State decisions. Thus, in order to control the authoritarian and technocratic tendencies which usually arise

among those responsible for running the State apparatus it is necessary to consolidate the democratic institutions: only these can prevent State intervention from being merely the expression of the arbitrary desires of powerful groups, whether they be civil or military, State or private. As already noted, however, the return to democracy does not guarantee that a satisfactory degree of efficiency will be achieved in State action: the contrary could take place if all the social groups believe that this return is a suitable opportunity for ensuring that their own unfulfilled demands are satisfied. This is a crucial issue, since the 'ungovernability' of democracies has always been the main justification adopted by authoritarian régimes.

For both valuative and practical reasons, democracy is the most suitable framework for development, but it must ensure an orderly performance which, by the very nature of this political system, cannot be based only or even mainly on coercion, but above all on the spontaneous consent of the governed. The support which the governed give to democratic institutions and the decisions which emerge from the latter depend on at least two essential conditions, however: firstly, participation in the decisions must be on a broad scale and these decisions must be connected with the great national problems, and secondly, the democratic institutions must remain in force for a prolonged period in order that they may be consolidated as the pillars of political tradition. Strong democratic institutions can be of great assistance in helping the citizens to overcome the effects of the conflicts and imbalances which accompany all crises.

Policies for tackling the crisis and reorienting development call for dramatic decisions which, as already noted, will profoundly alter the economies and societies of the Latin American countries. These decisions, in turn, call for a State which is capable of carrying them out, and this capacity not only implies that the State must attain maximum efficiency in its action, but also and above all, that it must achieve a social consensus which will serve as its political support;

without this support the State will be simply an instrument of sectoral interests and will not be able to carry out the task with which the present challenge faces it.

Furthermore, in societies like those of Latin America, where democratic ideals are deeply rooted, the social consensus will not be achieved by force, but only by the spontaneous and responsible obedience of the governed. This, in its turn, will only result from full participation in the taking of decisions and from the inner conviction that the sacrifices which have to be imposed are inevitable and are distributed equitably among all.¹¹

¹¹In his analysis of the present situation in Spain, which combines the need to face a crisis with the need to strengthen democracy, Fuentes Quintana has put forward some suggestions which seem to be largely valid also for most of the Latin American countries.

"It is evident that a policy designed to adjust to the crisis seems to call for the fulfilment of three vital conditions: clear recognition of the situation (*telling the country the truth, not concealing the crisis as though it were an incurable disease of which it is better not to speak*); *transparency and equity in the distribution of its heavy costs* (the crisis cannot be passed on to others in an impossible and suicidal kind of *saave qui peut*); and the creation or achievement of a sense of common purpose on the part of all social and political groups in order to *reach constructive answers to the main problems through negotiation and agreement*. In other words, overcoming the economic crisis and building democracy is a policy which calls for a high sense of the importance of the State rather than of one's own party in the approaches to it and the solutions proposed for the different problems by the social and political groups. If this sense of common purpose is not created, if the political parties foment a desperate class struggle in the midst of the crisis, if entrepreneurs and workers fail to define the minimum conditions for making possible the development of the country's enterprises, if those who enjoy privileged economic positions refuse to have anything to do with solutions calling for some sacrifice on their part, then the crisis will get worse and will make it insolubly difficult to cope with this combination of a crisis plus the need to build democracy, on which the whole future of Spain depends." Enrique Fuentes Quintana, "La prioridad política de la economía en la transición española", *Pensamiento Iberoamericano*, No. 3, Madrid, January-June 1983, p.127.

The external debt and the financial problems of Latin America*

*Carlos Massad***

The external debt is perhaps the most striking manifestation of the crisis through which the countries of Latin America are passing and is one of the problems whose solution is a necessary condition in order for these countries to be able to emerge from their present predicament.

The article begins by presenting some general data on the evolution of the total debt in the last decade to its present critical level equivalent to some 30% of the gross domestic product. It goes on to examine the reasons for this increase, dealing with them in terms of the increases in the supply of external credits and the demand for them, and placing particular emphasis in this respect on changes in relative domestic prices, exchange policy, excessive public and private spending, the rise in oil prices and its impact on international liquidity, etc. The author then goes on to deal with some consequences of the increase in the debt—such as restrictions on domestic policy, the transfer of resources abroad and external vulnerability—and the conditions on which this debt could be tolerable. These conditions are, essentially, the sustained growth of the world economy, continuity of the flow of external credit, and the expansion of exports, none of which are being fulfilled at present. He therefore suggests some emergency measures, including in particular the equitable renegotiation of the debt between debtors and creditors, an increase in the resources of the IMF and in its influence over creditor countries, and an increase in international liquidity, concluding that these measures, together with others in the medium term, are an urgent necessity at the present time.

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**The author is Co-ordinator of a joint UNDP/ECLA project and Professor of the Department of Economics of the University of Santiago, Chile.

I

Introduction

The external debt is a subject which is very much in fashion, and for this reason it is very dangerous: readers probably know just as much about it as the author, if not more. We all of us read, talk and are well informed on subjects of this type, and above all we sometimes hold very clear and well-defined ideas on them. I shall try to sum up these clear and well-defined ideas in order to give you the perspective at which my own experience and work have enabled me to arrive.

I shall refer first of all to the broad magnitudes involved in the financial problems of Latin America, then to the increase in the Latin American external debt and the reasons why this debt has gone up, after which I shall deal with the consequences of the increase in indebtedness and analyse the question of whether this debt is sustainable or not at its present level. Finally, I shall put forward some emergency and medium-term solutions at both the national and international levels and outline the prospects for the near future.

II

The magnitudes involved

Let us first look at the magnitudes involved in the Latin American financial problem. It is well known that there is a sharp and growing deficit on the region's balance-of-payments current account, that is to say, essentially on our purchases from and sales to the exterior, plus payments in respect of interests and tourism. For 18 non-oil-exporting countries, this deficit, which was around US\$ 2 billion in 1970, kept within the range of 10 digits until 1978, when it came to some US\$ 8 billion, but the following year it rose to US\$ 14 billion, and in 1981 it reached a peak of US\$ 27 billion. In other words, over a period of 11 years the external deficit on the current account of the 18 non-oil-exporting

countries increased by a factor of 13, from US\$ 2 billion to US\$ 27 billion.

Income on the capital account helped to finance this deficit, however: although on the one hand there was a deficit on the current account, since Latin America was buying more than it was selling, on the other hand this was financed with net income on the capital account. This income was consistently greater than the deficit on current account, so that it was possible to pay off this deficit and still accumulate reserves. Thus, for example, whereas in 1970 there was a current account deficit of US\$ 2 100 million, the surplus on the capital account was US\$ 2 800 million, so that there were US\$ 700 million left to improve the reserve position of this group of countries. This situation continued until 1979, when the current account deficit came to US\$ 14 billion, whereas the capital account surplus was US\$ 17 800 million. In 1980 and 1981, but above all in 1982, however, the situation was completely reversed, and in these three years the accumulated current account deficit was almost US\$ 15 billion more than the net inflow of capital, thus meaning a loss of reserves by our countries, since only part of the current account deficit could be financed with capital income and the remainder had to be covered by making use of our own reserves. In 1982, for example, there was a current account deficit of US\$ 25 billion, whereas the capital account surplus was only US\$ 16 700 million: that is to say, in that year alone there was net depletion of the reserves by almost US\$ 9 billion.

This inflow of capital comes basically from two sources: on the one hand, from direct foreign investment, which does not generate indebtedness; and on the other hand, from medium- and long-term foreign loans, which are accounted as such in the balance of payments.

While the debt grew, foreign investment was becoming less and less substantial. There are many reasons for this: on the one hand, very good investment opportunities arose in other

countries, as for example in Asia (Korea, Taiwan, Singapore, and now also Thailand, *inter alia*); on the other hand, it must be recalled that between the mid-1960s and perhaps the mid-1970s in Latin America there was a wave of nationalizations in most of the countries, in which foreign investments were expropriated. In some cases these nationalizations took place on account of the excesses of investors, whereas in others the motives were different. But the mere fact that nationalization took place, whatever its cause and almost regardless of the compensation paid, led to the discouragement of new investment. Consequently, the inflow of capital was increasingly acquiring the nature of straightforward indebtedness.

In order to gain an idea of the level of the debt, it may be compared with the total product of the countries. Latin America's total debt is at the present moment something over US\$ 300 billion. In 1970, the total public and private short-, medium- and long-term external debt was equivalent to only a little under 12% of Latin America's gross domestic product, but towards the end of 1982 it was equivalent to around 30% of the product.

Furthermore, in proportion as the debt grew there was necessarily also an increase in the cost of servicing it, particularly as regards payments of interest, which grew for two reasons: because the level of indebtedness was rising, and also because interest rates rose sharply during this period. Expressed as a proportion of exports of goods and services, interest payments represented around 7% in 1970, but at the end of 1982 they came to almost 40%: that is to say, in 1982 it was necessary to use almost 40% of the resources obtained from our exports simply in order to pay the interest on the debt.

The figures thus show that the debt grew rapidly and that its cost is high. We must now ask ourselves why the debt increased: what happened in those 12 or 13 years to make it grow so rapidly.

III

Why the debt increased

Let us classify the reasons for the increase in the debt under two traditional categories of economic analysis: demand and supply. First of all we will see what happened on the demand side to cause the growth of the debt, and then what reasons there were on the supply side for its increase.

1. *The reasons on the demand side*

Various reasons of different types may be mentioned on the demand side: the first to be referred to are the domestic policies or events which increased real domestic interest rates, for when these rates increase, there is a greater incentive to seek loans abroad. Consequently, any element which helps to bring about an increase in real domestic interest rates automatically results in a greater incentive to seek loans abroad.

a) *The anti-inflation campaign and economic changes*

The first element to be noted here is the struggle against inflation. Practically all the countries of the region carried on an active campaign against inflation during this period. Such a struggle naturally means, among other things, a relatively restrictive monetary policy, and this in turn brings about an increase in interest rates.

At the same time, during this period most of the countries of the region embarked on policies of profound economic change in which they reviewed their tariffs or financial systems, general incentives, systems of taxation, social security, etc.

These policies of change not only have long-term effects, but also certain short-term effects which may also involve costs. Thus, for example, a policy of change normally brings about variations in relative prices, which are the indicators used by the economy in allocating its resources.

In the case of those goods whose relative prices rise, the situation is often resolved by way

of external trade. If there is a greater demand for certain products which causes their relative price to rise, then this rise will probably be attenuated by way of external trade, because a sufficient amount of those products will be imported to satisfy demand or at least relieve the excess demand generated. In the case of a drop in relative prices, however, which would represent a sign that resources should be taken away from that activity and transferred to others where the prices are more favourable, the effect does not take place as rapidly, since the normal reaction of enterprises is not to immediately reduce their activities, but rather to ask for loans from the banking system in order in this way to overcome what they consider to be a temporary unfavourable situation, although in reality it may be a question of a longer-term change in relative prices in the country.

As enterprises approach the banking system, this system will respond—if they have appropriate guarantees—by granting them credit, and in this way the demand for credit will be increased. On the other hand, those enterprises whose relative prices are increasing will also want to expand and will then exert pressure on the banking system too, so that an abrupt change in relative prices in an economy normally brings with it an acceleration in the demand for credit, that is to say, greater pressure on the banking system. This pressure in turn will have the result of causing a rise in interest rates within the context of a given monetary policy. Indeed, it may be noted that it is precisely in those countries where there has been the biggest effort to make changes that there have also been the biggest rises in real interest rates. When such higher real domestic interest rates exist, this naturally constitutes a strong incentive to seek loans abroad, where rates are more favourable.

In this way, policies aimed at economic change tend, in the short term, to increase the demand for credit and to generate high domestic interest rates.

b) *The link between financial and non-financial enterprises*

Within this same field, we must consider the fact that in certain cases a link is formed between the bank and the enterprise making use of credit; the enterprise obtains credit in preference to other enterprises, and it can therefore work with relatively smaller capital in relation to its debt. In other words, the enterprise risks very little: the smaller the capital is in relation to the debt, the smaller the amount risked by the enterprise, and if it is only risking a small amount, then it will be willing to pay higher interest rates in order to procure financing to keep in business, even at difficult times. Thus the fact that there is a link between the banking system and the production sector gives rise to an incentive to enterprises to accept higher interest rates than they would otherwise be willing to agree to. As is only natural, this once again generates higher domestic interest rates and incentives for seeking loans abroad.

c) *Exchange policy*

Another important element in this picture is exchange policy. If, in a country suffering from inflation, the exchange rate is fixed at a certain nominal rate and remains stable while inflation continues, what will happen is that the *nominal* domestic rates, which are already high because of inflation, will be converted into high *real* interest rates in dollar terms. For example, if there is a fixed exchange rate for the dollar, with inflation of 20% and an interest rate of 25%, this means that the real rate of interest, measured in terms of national currency, is only 5%, whereas its equivalent in terms of dollars would be 25%, because the exchange rate for the dollar is fixed. Consequently, if it is possible to obtain loans abroad in dollars at an interest rate of 12%, this would be equivalent to paying only half the domestic rate and hence, in an economy suffering from inflation, the fact of keeping the exchange rate stable for a long period is a further incentive to seek loans abroad, because the dollar interest is lower than the domestic real interest rate.

All these elements help to increase the

domestic real interest rate and tend to generate an incentive to seek loans abroad.

d) *Excessive public sector spending*

A second set of elements which explains the demand for external indebtedness is linked with the elimination of restrictions on expenditure. Here, the orthodox or classic case is that in which the government spends more than its income. The following is a typical example: there is a fiscal deficit financed by the Central Bank; the excess monetary emission generates an excess of money supply over demand; and this excess of money supply is manifested in the rest of the markets through excess demand for goods and securities. The excess demand for goods corresponds to a deficit on the current account of the balance of payments, while the excess demand for securities has its counterpart in an outflow of capital from the country, so that in turn it is reflected in a deficit on the capital account of the balance of payments. A global deficit is thus produced which the authorities have to finance. Excessive public spending, then, financed by emission by the Central Bank, means a loss of foreign exchange and the State has to go outside the country, normally through the Central Bank, in order to obtain the resources needed to finance this deficit. This is where the phenomenon known in the United States as 'crowding out' takes place: that is to say, when the State goes out looking for loans it pushes the private sector aside into a corner and the latter sector is not able to obtain the credits it needs. Such is the traditional or orthodox case.

e) *Excessive private sector spending*

It also seems appropriate, however, to briefly analyse some non-traditional or what we might call heterodox cases, where the 'crowding out' takes place in the opposite direction: here, it is the private sector which crowds out the public sector. Let us look at an example. Suppose that for some reason the private sector decides to increase its expenditure and finds possibilities of financing this increased expenditure abroad. The increase in private spending will then be reflected in a deficit on the current account, since

the private sector seeks to buy more goods than are available in the market and must therefore import the additional goods. A deficit is caused on the current account, and this is automatically financed because the private sector itself seeks the necessary financing for its excess spending abroad. It might happen, however, that not all this financing goes to buy imported goods, but part of it is also used to buy domestic products, so that in this case part of the financing obtained would cover the current account, while the rest would increase the country's reserves.

Thus, through excessive private spending, a phenomenon of current account imbalance and external indebtedness is created which is identical to that occurring in the case of the public sector. Where there are possibilities of financing it abroad, excessive private sector spending can be just as dangerous as excessive public sector spending financed from the resources of the Central Bank.

The increase in the external debt in order to finance private spending will be reflected in the statistics, and it is probably to be expected that in those countries where the increase in the debt was due above all to excessive private spending, the external debt or the increase in it will be fundamentally of a private nature. In contrast, in those countries where the increased expenditure was due basically to excessive public spending, it is the Central Bank or the government itself which will have to seek financing, and consequently the external debt or the increase in it will be mainly of a public nature. If we look at the statistics of those countries which observe 'good conduct' in fiscal matters in the traditional sense of maintaining a relatively balanced budget, but where there is excessive private spending, we will mainly find an increase in the external debt of the private sector, whereas in those cases where the fiscal deficit predominates, it will be seen that the increase in indebtedness is essentially public.

In cases where there is an imbalance on the current account due to an increase in private expenditure financed from inflows of capital, then if part of these dollars is not used to finance import but to finance domestic expenditure, the prices of the so-called 'non-tradeable' goods will tend to go up, meaning that in reality the exchange rate is lagging behind. We thus observe

that there is an increase in the debt and that, by lagging behind, the exchange rate accentuates the current account imbalance. We then have a phenomenon where excessive private spending, financed by indebtedness which increases the reserves but leaves the exchange rate lagging behind, will again increase the imbalance on current account.

2. *Reasons on the supply side*

Let us leave aside at this point the reasons on the demand side which explain the indebtedness and look for a moment at the reasons on the supply side which show how this high indebtedness was able to take place.

The elements on the supply side are basically linked with the two 'impacts' of the oil price rises. These two great increases, in 1973-1974 and in 1978-1979, generated enormous surpluses on the accounts of the oil-exporting countries. These surpluses affected both the supply of funds and the demand for them. On the one hand, they generated a supply of funds, since the oil-exporting countries, especially those of the Middle East, have a great preference for liquidity in their holdings of foreign assets and they have preferred to put their liquid resources in bank accounts rather than in other types of investments, especially at the beginning of this process. At the same time that these countries were depositing these resources in the banking system, however, the oil-importing countries needed to finance their accounts, which had been unbalanced by the deficit.

There were thus simultaneous increases in both the supply of funds in the international field and in the demand for them. The oil-exporting countries deposited these resources in the private banking system operating at the international level, and this system expanded with striking speed. For a moment, it seemed that the system would not be capable of achieving the so-called 'recycling', that is to say, the reallocation of the funds from the oil-exporting countries to the oil-importing countries, yet this recycling grew between 1970 and 1981 at an annual rate of 20%. Almost all the available indicators, whether regarding the total assets of the international private banking system, its external as-

sets or its foreign exchange assets, show growth rate averages of 20% per year.

The surplus accumulated by the oil-exporting countries between 1974 and 1981 came to US\$ 433 billion, while the total net external assets of the banks reporting to the Bank for International Settlements in Basle are of the order of one million dollars.

With these resources, the Euromarkets expanded rapidly, at an average of 20% per year; the European banks expanded by 18%, the Eurocurrency market by 19%, the total assets of

the banks reporting to the Bank for International Settlements in Basle by 21.5%, etc.; all these rates of similar magnitude point to an unprecedented expansion in external financing.

Thus, on the one hand, our countries found themselves needing more resources, while on the other hand they had greater resources available to them: indeed, many foreign banks offered loans even when traditionally they would have taken the opposite view. This custom was reversed in the following years, however.

IV

The consequences of the increase in indebtedness

Let us now look at the consequences of the increase in indebtedness, the main figures for which we gave earlier. In order to analyse them, we should perhaps think in terms of an enterprise facing its banker. Let us assume that it is a solvent enterprise dealing with a banker with whom it has been working for many years, but that it now has a relatively high level of indebtedness. It is possible that in these circumstances the banker may say that before the enterprise undertakes new investments or expansion programmes, it should inform him in detail regarding its situation, because since it has quite a high level of indebtedness it is compromising a high proportion of the bank's resources, so that the bank is beginning to take a very close interest in the enterprise's evolution and risks.

From the point of view of a country, this means that certain restrictions on domestic policies come into being through the mere fact of having a large debt which has to be continually renewed. We may recall in passing that debts now have much shorter maturities than they had ten years ago, because they are mainly from private and not official sources. Ten years ago, most of the Latin American debt —perhaps 80% of the total— came from institutions like the World Bank, the Inter-American Development Bank, AID, etc.: all official institutions which loan for long periods at fixed interest

rates. Now, however, the relationship has been completely reversed: 80% of the debt is with private institutions which, by their very nature, loan for shorter periods and at floating interest rates whose consequences we shall analyse later.

1. *The restrictions on domestic policy*

In the first place, the level of the debt imposes certain restrictions on domestic policy. Obviously, it is not possible to apply whatever policy one likes: the policies must be such as to make possible the regular renewal of at least the level of credit already received, and this imposes restrictions on monetary, exchange and interest rate policies; it is not that these restrictions are directly imposed by the creditor banks, but they result from the force of circumstances, since the banks are looking at certain indicators to decide whether the economic management of a country will allow it to pay its commitments or not: if these indicators give a negative answer to this question, the bank will become very reluctant to renew its commitments and will begin to demand payment or increase the guarantees requested, just as it would do if it were dealing with an enterprise; in contrast, if these indicators give favourable answers, the bank will probably prove to be quite willing to grant new credits, to renew existing ones, etc. It is worth repeating that it is not a question of the bank

making direct demands to the authorities, but rather that the banks take into account the way certain indicators are evolving. For example, if the international reserves are going down, this is a bad sign to the bank, and if a country has a very large debt it can therefore hardly apply policies which involve the reduction of its reserves. The banks also consider the situation of the balance-of-payments current account: if this shows much of a deficit, it will be more difficult to renew credits or obtain new ones. In short, countries must seek policies which do not give rise to excessively large deficits on their current accounts. These are just a few examples, since the range of possibilities is very wide. At all events, the main point which I wish to bring out is that a high level of indebtedness, by its very nature, imposes restrictions on domestic policies and it is only possible to apply those which cause the indicators of solvency examined with such care by the banks to move in favourable directions which will make it possible to renew credits or obtain new ones.

2. *The real transfer of resources to the exterior*

A second consequence of a large debt is that it makes a real transfer of resources to the exterior a definite probability. Asking for loans means obtaining more resources than one possesses; a country which asks for loans does so in order to spend more than it has. In this way, a loan from abroad means a real transfer of resources from the exterior to the debtor country. At the same time, however, when the debt is paid back to the exterior the real transfer of resources is reversed. Transferring real resources means having fewer shoes, less clothing, less food: it is not something vague but something very concrete and effective; transferring real resources to the exterior means sending abroad assets which are then no longer available for consumption within the country, just as assets were *received* from the exterior when a loan was obtained. The developing countries are traditionally recipients of capital, however, and by the nature of their development they are in a position to offer better investment conditions or terms than others, so that for a very long time they will be receiving net capital from the ex-

terior, that is to say, real resources which are added to their own, in order to keep up levels of consumption and investment.

When the debt becomes very high, a country runs the imminent risk that the debt will have to be reduced, and this means that there will have to be domestic restrictions in order to send to the exterior the real resources with which the debt is paid.

Furthermore, the higher the debt, the higher too will be the interest, and this forms part of the current payments of a country, so that the greater the debt, the greater the probability will be of a deficit on current account due to the interest payments, and consequently there will also be greater probability that it will not be possible to obtain as many loans as before and that it will be necessary to transfer resources to the exterior. To take an example, let us assume that the external debt of a country is equal to its national product, that this product is growing at a rate of 5% per year, and that the real interest on the debt is also 5% per year; this would mean that the country would have to pay to the exterior real resources equivalent to the entire growth of its economy for ever, since these are payments of interest and not of capital.

3. *A new source of external vulnerability*

Furthermore, and as a consequence of the rapid growth of the debt, this has been contracted for shorter terms, because the commercial banks lend for shorter periods than AID or IDB, and also at higher costs, because they must not only cover their costs but also make a profit. Since the debt is for a shorter term and is more costly, this increases the possibility of a real transfer of resources to the exterior when the countries have to pay interest or pay back the capital of the debt itself. What makes the situation even more complex, however, is that the interest on private debts is not fixed like that on loans from IDB or AID, but floating, that is to say, it is usually varied every three or six months in line with the market. This means that the effects of the interest rate do not fall only on new loans. When a rate is fixed—9%, for example—and afterwards the rate is raised to 10%, this does not increase the rate on existing loans, which remains at 9%, since the rate of 10% is

only applied to new loans obtained. When the rate is floating, however, a rise in it from 9% to 10% means that the latter rate will be applied to the entire debt, and not only to the new debt contracted. Since nowadays practically 80% of the Latin American external debt is subject to floating interest rates, this means that a rise in the rate from 9% to 10% involves an extra expense of US\$ 2 400 million for Latin America as a whole.

In addition, however, the fact that the entire debt is subject to floating interest rates constitutes a new way for the international transmission of imbalances. The traditional ways in which international imbalances are transmitted are very well known. When the United States is going through a recession, for example, the prices of commodity exports fall even though those of the developing countries' imports keep on rising, and the deterioration in the terms of trade means that we receive less for our exports, so that the imbalance is transmitted to our economy through the terms of trade.

During a recession, the imports of the developed countries often go down, which means that our exports go down too. Thus, the effects of the international recession are also transferred to our economies through the volume of exports.

When the developed countries are applying a restrictive monetary policy, interest rates go up, and a higher rate of interest tends to bring about a reduction in investments in our countries, so that, because of the smaller expenditure brought about by high international interest rates, this is another way in which part of the recession is transferred to our economies. When there is a recession in the United States, the exchange rate of the dollar improves with respect to other currencies, and as our currencies are normally linked to the dollar this constitutes a kind of revaluation through which international imbalances are also transmitted to our economies.

Now, however, with the floating interest

rates which affect the whole of the debt, there is a new and non-traditional way for the international transmission of imbalances, namely, through movements in interest rates. When interest rates rise in the United States because that country is applying a restrictive monetary policy, two things happen at once: the United States economy is slowed down, so that all the other traditional effects already mentioned take place, yet at the same time interest rates rise, thus directly increasing the interest payments on current account. Consequently, interest rates not only have an indirect effect through the spending of the economy, but also a direct effect through the current account imbalance caused by the need to make larger interest payments.

4. *Another new source of vulnerability*

Given the importance of the external debt and its level, there is another non-traditional mechanism for the transmission of international imbalances: deterioration in the portfolios of banks in the exterior. Let us suppose, for example, that there is a recession in the United States; this leads to a deterioration in the portfolios of the banks of that country, so that they are much more reluctant to lend money and thus reduce the level of their loans. A country with a high level of indebtedness, however, has to pay high interest rates which it needs to finance, and it must renew its credits in order at least to keep up the level of its debt, yet it is precisely at this time that the banks become reluctant to lend, when interest rates are simultaneously rising because of the external recession. Thus, at one and the same time there is a deterioration in the terms of trade, all the other traditional ways of transmitting imbalances make themselves felt, and moreover the non-traditional methods of transmission of imbalances, which operate through the deterioration of the bank portfolios with consequent forced reduction of their lending activities, also come into action, leading to contraction in the international financial system.

V

Is the present level of indebtedness sustainable?

After looking at all these negative aspects, it would seem appropriate to analyse the question of whether the present level of indebtedness of Latin America can be sustained or not. I shall then suggest what could be done to deal with the situation. For the moment, however, it is worth stopping at this point to determine under what conditions the level of Latin American external indebtedness can be sustained.

1. *The growth rate of the world economy*

The first condition in order for this level to be sustainable is that the world economy should recover, that is to say, that it should have a steady growth rate. Indeed, the National Security Council of the United States estimates that if the economies of the OECD countries grew at a rate of 4.2% per year, the problem of the external debt would be perfectly bearable for the debtor countries taken as a whole. Naturally, there are cases where the difficulties in doing so would be greater, but taking the countries as a whole, a sustained 4.2% growth rate by the OECD countries would make it possible to face up to this level of indebtedness because it would mean higher prices for exports, bigger exports for the debtor countries, lower interest rates, etc.

2. *The level of external real interest rates*

The second condition is that interest rates should go down in real terms to their traditional level. If we look at the last few decades in the United States and Europe, we see that real interest rates were between 1% and 2%, with the exception of Japan, where real rates were higher because of the great productivity of that country's economy. Economies cannot resist long periods in which real interest rates are much over 1% or 2%, because in such an event the depositors in banks would be the owners of the entire national wealth within the relatively short space of three or four generations; since interest keeps building up, after less than a century a million dollars would be turned into a thousand

million dollars if the interest rate were 7% per year. Real interest rates, which were quite low in the past, are now of the order of 7%, which is an absolutely abnormal level. Thus, if the growth rate of the world economy were between 4% and 5% and real external interest rates were more than 1% or 2%, the debt would be perfectly sustainable.

3. *Continuity in the flow of external credit*

A third condition is that the flow of bank credit should be relatively continuous and not interrupted. Another problem arises here, because numerous banks which are relatively small by international standards have entered the field of international financing and are operating behind the big banks or in conjunction with them. These small banks entered this field because there was great liquidity in the system and this enabled them to find a safety valve for their resources, but they do not have the capacity to evaluate clients in other countries; they lack a team of experts who can maintain an updated view of the economies of other countries and of individual foreign clients, so that they have to rely on the judgement and criteria of the big banks. The small banks are also weak, however, and a small error in their portfolio can mean very serious difficulties for them, so that they go in together behind the big banks and also leave the field together at the first sign of difficulties. The big banks, which have their own teams for evaluating the situation, do not display such erratic reactions, or at any rate would have fewer reasons to do so, whereas the smaller banks enter and leave the field *en masse*. This attitude causes difficulties with regard to the flow of bank credit resources, and in particular it causes serious difficulties in the present renegotiation of the debt. The banking system shows a strong gregarious instinct, acting together one way or another. Thus, it acted in one direction between 1975 and 1981, and in the opposite direction in 1982.

4. *The expansion of exports*

Another necessary condition is that there should be a steady expansion of the exports of debtor countries. If the economies of the other countries in the world are growing, this will enable exports to be expanded, but in order to do this it is necessary to have production capacity. In other words, it is necessary to have made intelligent use of the resources obtained through domestic saving and indebtedness. It cannot, however, be asserted that these resources have been intelligently used in all cases. In reality, when we look closely into the matter we find that in various cases external saving was used as a substitute for domestic saving instead of being a complement to it: that is to say, external saving led to a reduction of domestic saving. Investment did not grow as much as it should have done with these resources, so that not all countries are in a position to increase their exports, even if the world were to grow at a sufficient rate to absorb them.

It is also necessary to take into account the marked protectionist trends observed in almost all countries of the world. Although governments try to resist protectionist pressures, the combination of unemployment and external imbalances in the OECD countries causes these pressures to be successful. In recent years world trade has practically stagnated, and in reality for at least the past year world trade has been going down, in terms of both volume and prices, for the first time in a great many years.

Unfortunately, protectionist tendencies in countries are not easy to reverse. Once established, a series of vested interests are created in connection with them: those of the workers and owners of the enterprises receiving protection, the enterprises connected with them, the interests of the geographical areas where these are located, etc. This makes it very difficult to do away with protectionist measures once they have been adopted.

5. *Fulfilment of the conditions*

As a result of the world recession, these four conditions which are necessary in order for the external debt to be sustainable in a normal manner are not being fulfilled. Unfortunately, the

world economy is not growing, or else is only doing so very slowly. The gross national product of the industrialized countries as a whole, which grew by 1.3% in 1980 and 1.2% in 1981, shrank by 0.3% in 1982, and while in 1983 some growth is hoped for, this is at present nothing but a hope, so that it is clear that the world economy is not growing at the rate of 4% or 5% which would be needed in order to make the present level of indebtedness bearable.

Furthermore, there has been an important change in the surplus/deficit distribution in the world. With the failure of the oil cartel, the oil-exporting countries have ceased to register big surpluses; it will be recalled that they had accumulated almost US\$ 500 billion in surpluses which they were mostly keeping on deposit in the banking system. Now, however, these countries have a deficit: the figures show that in 1982, for example, the oil-exporting countries had a deficit of US\$ 2 billion on their external accounts, and a deficit of US\$ 27 billion is expected for 1983, so that these countries will no longer be making extra contributions to world liquidity. In 1982, the industrial countries registered a deficit of US\$ 1 400 million, while the non-oil-exporting developing countries showed a deficit of US\$ 87 billion. For 1983, the industrial countries expect a surplus, thus changing the current account situation, but these countries are much less inclined than the oil-exporting countries to keep their resources in liquid form in the banks. It is therefore improbable that the latter can expect additional liquid resources, and it is also consequently improbable that the international financial system will grow again at the rates at which it had been expanding. Indeed, in the last few months of 1982, the international financial system showed a slight decline in its figures, instead of growth.

As a result of the world recession (trade stagnation and protectionism were already referred to earlier), world trade declined in terms of volume by 2.5% in 1982, and by 4% in terms of unit values. It may be noted that up to 1981 it had grown steadily. Real interest rates, for their part, have risen from 1% or 2% to around 7%.

In short, it is becoming increasingly difficult to export; real interest rates are rising in the exterior; and domestic and foreign bank

portfolios are deteriorating so that the supply of external credit is shrinking. One set of figures serves to illustrate the importance of several of these factors for the Latin American countries: if the terms of trade had kept the levels they had in 1965-1969 and interest rates had not varied from the average level of 1978, then the current account deficit of the 18 main Latin American non-oil-exporting countries would have gone down from the US\$ 25 billion which it reached at the end of 1982 to only US\$ 1 billion. Of course, if the terms of trade and interest rates

had been different, then many other things would have been different too. This calculation at least gives us an order of magnitude by which to appreciate the importance of the figures involved, however.

This set of factors means that, because of its form, maturities and amounts of interest payments, the present level of indebtedness is not sustainable and demands priority attention on the part of Ministers of Finance and Presidents of Central Banks.

VI

How is the problem to be faced?

A problem of the magnitude, scope and complexity of the present one does not admit of simple or rapid solutions. On the contrary, it calls for action on various planes and for the adoption of measures whose effects will take place at different moments in time. Any orderly solution of the problem of indebtedness calls, in the first place, for the adoption of certain emergency measures which will give time for the measures of a more definitive nature to come into effect.

1. *Emergency actions*

a) *Renegotiation of the debt*

Many countries have initiated action designed to reprogramme, refinance or renegotiate (however one wishes to call it) their commitments in respect of the external debt which fall due in the next twelve months or two years. Through such action, in agreement with creditors, it is hoped to reduce the amortization burden on the balance of payments during the next year or two years. It is spread out over the future, with some period of grace, because it is expected that the conditions of the national and world economy will be more favourable in the years to come.

The first experiences of renegotiation show a marked increase in the cost of the renegotiated debt. This increase is based on the

argument that the risk for the creditor has increased. In reality, however, it may be asserted that such risk has perhaps even gone down, since the renegotiations have been accompanied by sharp increases in the guarantees provided by the debtor countries, at the demand of the creditor institutions. Furthermore, the real option which the creditor has is not the choice between obtaining punctual payment or renegotiating, but rather the choice between renegotiating or not collecting the amounts due at all. This situation is not due to the ill will of the debtors, but to the material impossibility of paying in the manner originally agreed. The initial cost of the credit already included a certain 'risk premium', in line with the normal conditions of the credit market. Consequently, when the risk materializes the debtors should content themselves with the premium which has already been paid, and not increase the cost of the credit still further with higher spreads, flat surcharges, etc.

The renegotiation will lead the creditor banks to take a great interest in the domestic policies of the country concerned, because it is important for them to know whether such policies will ensure that the debt can eventually be paid off promptly on normal terms. This is where the real restrictions on domestic policies appear when the debt is large, as already noted. It is worth adding that in normal relations between debtors and creditors, when the former

cannot pay their debts as scheduled an agreement is reached which lightens the burden of the debt for the debtor, thus sharing the problem with the creditor. In the present circumstances there is no machinery for achieving such an objective, although such machinery existed in the past, before the Second World War, when most of the external debt took the form of bonds sold on the London and New York markets. If the debtors ran into difficulties, the price of the bonds fell and the debtors could buy back the bonds they had issued (i.e., their debt) at a fraction of their original value, so that the burden of the debt was shared between creditors and debtors. Bank portfolios, however, cannot easily be bought and sold on the market, and this type of machinery for sharing the burden of the debt has consequently disappeared.

In short, renegotiation is the first emergency action to be taken, but it should be subject to a warning: neither creditors nor debtors should take an exaggerated attitude as regards the cost of the debt.

b) *Expansion of the resources of the International Monetary Fund and the need for an even-handed attitude by it to both creditors and debtors*

A second type of emergency action consists of the expansion of the International Monetary Fund, which has just increased its regular resources by 47.5%, representing the addition of some US\$ 15 billion to the resources which it has available for lending. This sum, however, is insignificant compared with the magnitude of the problem, so that if the Fund does not act in other ways also, it will very soon find itself without resources once again. The International Monetary Fund is an absolutely essential institution in this process, and in my opinion it has played a key role in completing or helping to complete the renegotiations which have been effected so far. The Managing Director of the Fund has personally seen to it that the banks agree to assemble the additional resources needed to make up what each country requires to finance its needs.

This situation means that the Fund must take into account the fact that there are limits to

the policies which a country can adopt in order to make its programme acceptable. Here, there is a certain bias in the situation: in the present circumstances I consider that the Fund is not in a position to apply the same pressure to creditor countries as to debtors, so that there is a recessive bias in the Fund's policy. If it could apply the same pressure to creditor countries, it would tell them that they must apply expansive policies in order to make the world economy grow and permit an increase in the trade of the developing countries, especially Latin America. If this could be done, the burden of adjusting the Latin American economy to the new situation would be considerably lightened. In my personal opinion, the International Monetary Fund needs to seek extra resources quickly and to find some system which will enable it to exert pressure on the creditor countries in the same way that it exerts it on debtors. I consider that much still remains to be done in this respect.

c) *The growth of world liquidity*

When we look at the figures, we see that the world's international reserves are going down. In the case of Latin America, its gross reserves went down by US\$ 12 billion in a little over one year, without counting the changes in the price of gold. The world as a whole has lost an even larger sum and continues to lose reserves, so that a substantial additional allocation of Special Drawing Rights would be justified from every point of view. These Rights were created precisely in order to supplement international liquidity at a time when the other sources of liquidity were not capable of satisfying requirements. Today they are clearly not capable of doing so either, and in my opinion there is therefore every justification for issuing Special Drawing Rights. The argument originally given for not continuing to issue them was that the banking system was growing so rapidly that it could take care of all financing needs, but this is no longer the case. The growth of the banking system has been paralysed, and there therefore does not seem to be any convincing argument against an additional allocation of Special Drawing Rights.

This would solve many problems. Firstly, it

would raise the level of world liquidity to support the continued expansion of trade; secondly, it would tend to redistribute the debt payment burden since, to the extent that a country receives as a 'gift' a certain amount of resources, it is being permitted to transfer fewer real resources in order to pay its external debt. Furthermore, it is my understanding that increasing the amount of Special Drawing Rights does not require special legislation in any country, including the United States, where it does not even need to be submitted to Congress, as is required in the case of an increase in the International Monetary Fund quotas.

It is well worth supporting the studies which are being embarked upon at this moment in the Fund to consider the possibility of making a fresh issue of Special Drawing Rights.

2. *Medium-term solutions*

a) *At the national level*

Let us now look at the medium-term solutions and the panorama offered by the future. These medium-term solutions call for action at both the national and the regional and international levels.

At the national level, I consider that the coming year will witness policies aimed at promoting the growth of exports and import substitution. This is one way of assigning more resources to the so-called tradeable goods sector and thus accumulating greater resources for reducing the debt in relative terms. In reality the objective should not necessarily be to reduce the level of the debt in absolute terms, but an effort should be made to reduce it as regards its relative magnitude with respect to exports and the national product, which are the indicators most commonly used in this respect.

b) *At the regional level*

A second element which will probably make its appearance in national policies will be the use as far as possible of the regional markets and the regional and subregional integration agreements. This represents a still unexplored field which could be used for the common bene-

fit of all the countries. In order to do this, it will be necessary to strengthen the regional co-operation machinery in both its trade and financial aspects. This topic is quite well known and has been studied by various bodies, so that it is not appropriate to consider it in detail here. Moreover, there is evidence that some subregional bodies are already acting in this direction.

At the regional level, a further expansion of the Inter-American Development Bank, its regular capital and its additional funds would be particularly important. There are some difficulties standing in the way of expanding the regular capital of the Bank, but it is to be hoped that these will be overcome and that the countries which have encountered problems in this respect will be able to eliminate the restrictions limiting its growth.

c) *At the international level*

At the international level, I believe that the expansion of the International Monetary Fund would be an extremely favourable element, provided that this expansion was much greater than recently agreed upon: US\$ 15 billion is a drop in the ocean compared with the present financial difficulties; probably the size of the Fund ought to be doubled, or more than doubled, yet so far it is only being increased by 47.5%.

The expansion of the World Bank would also be very favourable, provided that the Bank eliminates or ceases to apply a principle which it has been using in recent years: namely, the 'principle of graduality' whereby, in proportion as the per capita income of a country rises, that country ceases to be eligible for obtaining World Bank loans.

One of the important elements for the future is that there should be a change in the composition of the external liabilities of the countries. In other words, instead of having so much debt from private sources, as they do now, the countries should have more external investment and less external debt, while there should be relatively more debt from official sources and consequently less from private sources. An external liability structure in which there is relatively more investment and loans from official sources

offers much greater stability for the total financial resources and the total portfolio of external liabilities of the countries. Changes in interest rates would not then affect them so much, since official loans normally carry a fixed interest rate, and a problem of instability would thus be relieved. At the same time, foreign investment should behave in keeping with the economic cycles, that is to say, when a country suffers economic difficulties it should not have to pay profits to the exterior. Thus, remittances of profits on investments would be smaller when the economic situation was unfavourable, and greater when it was favourable, or at least incentives could be established to encourage this approach, which would help to relieve the external financing problem instead of complicating it.

3. New instruments for co-operation

Generally speaking, probably what is needed are not new institutions for co-operation, but merely new instruments for it. In this respect, I should like to mention first of all the question of exchange systems. It would be desirable that exchange rates should not float as much as they do now, but should be more 'viscous' as Giscard D'Estaing called them or 'guided' as Carlos Sanguinetti suggested. These two terms imply an exchange system which does not fluctuate sharply or erratically in the world but has some degree of inertia, so that these fluctuations do not discourage the allocation of resources to activities connected with international trade.

In the case of Latin America, consideration could be given to new instruments of co-operation such as the possibility of establishing a common unit of account for the payment of services. Let us assume that the countries agree to establish a unit of account with a well-defined physical existence with which they could make their payments in respect of tourism, for example, with these payments being settled among the countries at the end of a certain length of

time. Each country would issue its own units of account, and each one would treat them as though they were foreign exchange, subject to the same restrictions and regulations. At the end of a certain length of time, such as three or six months, there would be a settlement of accounts in respect of these resources and only the outstanding differences would be paid in foreign exchange. This could save a really considerable volume of foreign exchange resources and consequently relieve the pressure on the reserves.

Furthermore, it is necessary to exchange financial information, for the countries know little or nothing about what is happening in other countries. The result of this is, for example, that at a given moment a country decides to come on the market with a bond issue on the same day that this is being done by another country, thus causing a drop in the price of the bonds and an increase in the cost for the issuer. If they had exchanged information they would simply have come to an agreement not to come on to the market at the same time. The manner of negotiation or renegotiation with the exterior could also be known by the countries, so that after a prior exchange of information they can each negotiate their own situation with fuller knowledge of the circumstances. Thus, some formula for the exchange of information could be extremely useful for all. Thought could also be given to the possibility of coming on to external markets not as individual banks, but perhaps as multinational enterprises. Why not form multinational enterprises in the financial field which can come on to international financial markets in that form instead of doing so, as happens at present, as individual banks which have much less capital, much less backing and run much greater risks because they are linked to the fate of a single country? In contrast, if multinational enterprises were formed, they would have behind them a group of countries which could diversify the risk much better.

VII

The future prospects

After taking due account of the nature of the possible short and medium-term solutions, I consider that in looking forward to the future we must have in mind one important concept: austerity. I have the impression that, in view of our level of imbalance, our level of indebtedness and the likelihood of a slow recovery of the world economy, our countries must necessarily look forward to a period of austerity. The way out of this problem will not be rapid, but slow and difficult. It is necessary to increase domestic saving, and in order to do this public and private consumption must suffer, in order to leave a margin for the growth of production in the area of tradeable goods and take advantage of the prospects of an eventual recovery of the world economy. The need for efficiency in the allocation of resources and in the social evaluation of projects will, I believe, become quite painfully evident. The more difficulties there are in a family, the greater care is exercised in the use of resources, and the same occurs with an enterprise or a country. This implies obligations and responsibilities not only for the government but also for each and every one of the citizens.

Finally, more austerity also calls for great concern to ensure the social distribution of the burden. If austerity and demands for effort and sacrifice are imposed in a manner which lacks equity, they will not be sustainable: they could be maintained for six months or a year, but finally the countries would not accept a type of austerity which only affects some citizens but not all.

In the final analysis, however, I am optimistic. Latin America has gone through difficult times in the past; we may recall that this is not the first crisis faced by the world economy. There was another very great crisis in the 1930s, and although it is true that the circumstances were different, that crisis left some lessons for us. It began at the end of 1929, yet in 1939, at the beginning of the war, unemployment in the industrialized countries was still very great. In 1941, when the United States entered the war, unemployment in that country was still running at 14% of the labour force although ten years had passed by then. We have learnt more now than we knew then, and we have other institutions, so that it will not be ten years this time, but even so the time needed to emerge from this problem must be reckoned in years rather than months.

Fortunately, signs of recovery of the world economy are already to be glimpsed. They are neither very marked nor very brilliant or dramatic, but they are nevertheless there. Order books are growing in the United States, stocks are dropping and have probably reached their lowest level, while housing construction is beginning to show some recovery. These are positive symptoms: of course they do not herald an easy or triumphant outcome, but they do represent an incentive for setting about the inevitable task of austere and equitable sacrifice so necessary for supporting us in our present difficulties.

Some CEPAL publications

El desarrollo de América Latina y sus repercusiones en la educación (Latin American development and its repercussions on education), "Cuadernos de la CEPAL" series, No. 41, Santiago, Chile, 1982, 246 pages.

This publication comprises two studies on educational problems in the context of Latin American development. The first, entitled "Estructura y dinámica del desarrollo en América Latina y el Caribe y sus repercusiones para la educación", is a document presented by the ECLA Secretariat at the Conference of Ministers of Education and Ministers Responsible for Economic Planning of the Latin American and Caribbean Member States convened by UNESCO in Mexico City from 4 to 15 December 1979. This is a general study which examines the incidence of the most important economic and social processes of the development of the region on the structure and dynamics of educational activity. In short, it is a profile of the economic and social conditions which affect education.

The second study — "Alfabetismo y escolaridad básica de los jóvenes en América Latina" — deals with a problem which is more specific and restricted, although no less important. Its subject is literacy and basic education in school-age population groups, with the study broken down by countries, which are ordered in turn according to the values of the various indicators used. This is an empirically-oriented analysis based on unpublished statistical material which was specially processed in order to go more deeply into the problem. This work was prepared originally for the UNESCO/ECLA/UNDP project on development and education in Latin America and the Caribbean.

The connection between the general and comprehensive approach of the first of these studies, dealt with mainly from outside the educational situation, and the specific problems examined in the second study lies above all in their progression from the general to the particular. The study on literacy and basic education has been selected to accompany the global diagnosis because it is considered that these topics constitute the biggest problems faced by the region at present.

América Latina y la economía mundial del café (Latin America and the world coffee industry), "Cuadernos de la CEPAL" series, No. 42, Santiago, Chile, 1982, 46 pages.

This study seeks to give the fullest possible picture of the mechanisms and relations governing the production, trading, processing and consumption of coffee at the world level.

For lack of data, it has not been possible to analyse in depth certain aspects of this extremely complex situation, but at least the processes of price formation and distribution

of profits at the world level have been fully clarified, which was the main objective of the study.

The conclusions drawn from this are applicable at the domestic and the international levels. At the domestic level, it would appear that the Latin American producer countries suffer considerably from the weight of tradition, which is felt particularly intensely in the case of coffee. Thus, the domestic marketing structures have remained practically unchanged, except in a very few cases, for several decades. Some of the undesirable effects of this predominant inertia are connected with: i) the persistence of the old laws of the 'coffee cycle' (long crises of overproduction interrupted by short periods of excessively high prices), the harmful nature of which for the producer countries hardly needs to be demonstrated; ii) controversies over the domestic distribution of the profits from coffee growing, especially in periods of high prices; and iii) the apparently very limited adaptability of the marketing systems (higher degree of processing, producers' associations, 'open market operations').

At the international level, the oligopolistic structure of the coffee industry in the consumer countries is made clear. Thus, although the transnational corporations do not intervene in the phases prior to the importation of coffee beans, they have a very high degree of control over the consumer market, which they manipulate largely through very high expenditure on promotion and publicity. The effects of this situation are clearly shown by the fact that in the period 1976-1979 the 'industry spread' for the coffee industry increased out of all proportion to the increase in raw material costs.

The foregoing, together with the evolution of prices and the scanty participation of the producer countries in the final retail price, in spite of the small amount of industrial processing given to a product such as coffee, makes up a situation which is prejudicial to the interests of the exporting countries. Solutions must therefore be sought at the level of long-term agreements (whose revitalization would make it possible to overcome the present problems of overproduction) and new forms of intervention in the market by the producer countries, which should have a more concrete presence in the consumer countries.

Among these latter solutions, one must not reject out of hand the idea of once again proposing the establishment of a producers' association, making the fullest possible use of the experience accumulated by the Bogotá group, especially if the International Coffee Agreement runs into difficulties which reduce its practical effectiveness.

Even outside the strict context of a producers' association, it would be very desirable for there to be greater collaboration among the developing countries, both of Latin America and of other regions, within the framework of the International Coffee Agreement and in the formulation of global policies for the coffee sector at the world level.

El ciclo ganadero y la economía argentina (The stock-raising cycle and the Argentine economy), "Estudios e Informes de la CEPAL" series, No. 43, Santiago, Chile, 1983.

The stock-raising cycle is manifested through the recurrent fluctuations in a set of interrelated phenomena, among

them the size and composition of the stocks of cattle, slaughtering and the destination of the meat produced, and relative livestock prices.

These fluctuations produce disturbances in the Argentine economy. Within the sector, there are recurrent changes in the allocation of resources, with underutilization of the latter, causing short and long-term effects on supply and on the specialization of enterprises, while in the economy as a whole the fluctuations make themselves felt mainly through their effects on exports and prices: meat prices rise, especially in periods of reduced slaughtering, the cost of living increases, and the profit margins of the export meat packing industry go down (for given levels of the exchange rate and of international prices). These factors condition economic policy, which has frequently had to choose between domestic consumption and export.

The importance of this phenomenon has given rise to numerous studies from the 1960s onwards. On this basis, using more detailed primary information and employing processing methods which are considered to be more efficient in view of the characteristics of this information, the ECLA Office in Buenos Aires has prepared the present special study which forms part of a more general analysis of trends and fluctuations in agricultural sector activities.

Analysis of the stock-raising cycle involves the prior solution of some problems of information and methodology. In the first place, there is a lack of reliable data series on cattle slaughtering and stocks for long periods. Secondly, if it is desired to analyse periods of less than one year (months, quarters, etc.) before 1970 it is necessary first of all to compile and process series on slaughtering taken from different sources. Finally, it is necessary to solve some methodological problems in order to construct indicators which make it possible to describe the cycle (series on exports, consumption, prices, etc.). In this report, a solution is offered for these problems, the result being series of basic data on slaughtering and stocks—corrected in order to make them mutually compatible—and a set of indicators on the stock-raising cycle.

In addition, a first analysis of the fluctuations in stocks is made on the basis of the indicators thus constructed and some comments are given on long-term growth.

El financiamiento de las exportaciones en América Latina
(Export financing in Latin America), "Estudios e Informes de la CEPAL" series, No. 18, Santiago, Chile, 1983, 212 pages.

A fundamental characteristic of the development of Latin American exports in the last few years has been the growing importance of exports of manufactures. This change in the structure of the region's exports has accentuated the need for the availability of increasingly broad and highly perfected machinery to provide financial support for the essential expansion and diversification both of the goods and services offered and of the Latin American external markets.

In order for exporters to be able to compete on similar terms to those prevailing on the increasingly demanding international markets, the countries and various regional bodies have been adopting, within their export promotion

policies, assistance measures in the financial sphere which have given rise to various systems for promoting export financing and credit insurance.

The main objective of this study is precisely to describe the situation as regards the different financial assistance schemes which exist in Latin America. It is hoped that the contribution it may make to the knowledge and wider awareness of the schemes in force may help to improve and expand the use of these mechanisms and intensify regional co-operation in these important matters.

The document is divided into four chapters and two annexes.

The first chapter, "General considerations on exports of manufactures and their financing" describes the general tendencies observed in the region's exports of manufactures and the most salient features which may be expected in the years to come. It also describes the limitations and demands imposed by the world economic situation, with special emphasis on the considerable growth which has taken place in financial assistance as a sales promotion mechanism on external markets.

The second chapter, "Export finance and credit insurance promotion systems" is the longest, since it describes the instruments and modalities of national, subregional and regional arrangements for these two forms of financial support for exports. The chapter bases its description on the whole set of mechanisms and corresponding criteria applied in the different systems and does not consist of an individual description of each one of them. Such a description is given in annex I.

In the third chapter, "Scope of export finance and credit insurance promotion systems", an examination is made of various elements which enable a better idea of the significance of these systems to be gained. In this connection, the main limitations observed in the functioning of the systems are analysed.

On the basis of the experience described earlier, the fourth chapter "Lines of action for regional co-operation" underlines the importance of joint Latin American action for future progress in the expansion and diversification of exports and suggests the main areas where financial co-operation can provide the Latin American countries with interesting mutual benefits in the short term.

Annex I, "National, subregional and regional export financing and credit insurance promotion systems", presents twelve monographs setting forth in a schematic manner the main characteristics of each of the preference systems existing in the region. Annex II, for its part, reproduces the Articles of Association of the Latin American Association of Export Credit Insurance Bodies (ALOSECE), whose recent establishment marks an important step forward in regional financial co-operation.

The measurement of rural employment and income, "Estudios e Informes de la CEPAL" series, No. 19, Santiago, Chile, 1983.

Planners concerned with employment and living conditions and social scientists engaged in the study of these subjects in the countries of Latin America have repeatedly expressed

their dissatisfaction with the results of measurements of employment and income in rural areas carried out through censuses and surveys. This study seeks to identify the causes of such dissatisfaction by contrasting the statistical requirements deriving from the analytical purposes which have guided the construction of the conceptual frameworks used for the analysis of rural employment and income with the measurements of those variables obtained through economic censuses, household surveys and economic surveys, which in practice serve as the main sources of statistical information on these subjects in the region. To this end, the study discusses the adaptation of the nominal and operational concepts and definitions, research techniques, and data collection instruments most frequently used in the investigation of rural employment and income to the analytical and policy purposes which provide the most important frameworks for the orientation of such researchs. On this basis, suggestions are made and alternative procedures proposed for overcoming some of the most outstanding obstacles hindering the advance of research in this field.

The study consists of seven chapters and an annex of tables. The first chapter analyses the place occupied by research on employment and income in the framework of the general concern felt in developing societies for growth and equity. It also discusses the most important analytical purposes deriving from this general concern, namely, determination of the well-being of the population, the level and efficiency of utilization of the labour force, the availability of labour, and imbalances in the labour markets. Since the more general conceptual framework and the purposes which orient and give their significance to research in this field are equally pertinent in the measurement of employment and income in both urban and rural areas, no distinction is drawn between these areas in this first discussion. In contrast, the description of the special features of rural areas and the particular characteristics assumed there by the problems of well-being, utilization and availability of labour and labour markets constitute the central purpose of the second chapter. The third chapter is devoted to an analysis of the criteria for identifying the agricultural labour force, with particular emphasis on discussion of the boundaries of production and the dividing lines between economic activity and inactivity. The fourth chapter examines the conventional classifications of branches of activity, occupations and occupational categories; some changes are then proposed in the prevailing classifications and additional classifications are suggested which would make it possible to improve the registration of certain aspects of agricultural work in Latin America which are significant in the light of the discussions described in the earlier chapters. In the fifth chapter, an explanation is given of the concepts currently used to measure the phenomena of underutilization of labour and they are reviewed in the light of the specific problems raised by their application to the study of agricultural sector employment, while some new approaches for conceptual formulation in this field are proposed, specially those placing greater emphasis on aspects connected with the availability of labour. The sixth chapter deals with the measurement of rural income from a viewpoint which integrates its investigation with that of activities and employment. The conceptual framework to which the measurements should refer is

explained and the different forms of rural income and the problems raised by their measurement are analysed. In the seventh chapter, the possibilities and limitations of different sources are considered and some actions are suggested for facilitating their linking up and possible integration, as a way of overcoming the limitations raised by each of them separately for the measurement and investigation of rural employment and income. In order to facilitate the reading of the study, the tables describing the main national measurement practices in this field in the countries of Latin America for the decade beginning in 1970 are assembled in an annex.

Efectos macroeconómicos de cambios en las barreras al comercio y al movimiento de capitales: un modelo de simulación (Macroeconomic effects of changes in barriers to trade and to the movement of capital: a simulation model), "Estudios e Informes de la CEPAL" series, No. 20, Santiago, Chile, 68 pages.

In recent years there has been renewed interest in the problem of the opening up of national economies to the world economy through the liberalization of trade and capital movements in the developing countries, including many Latin American ones. Although there are a number of different reasons for this interest, there are three which can reasonably be considered as of outstanding importance.

First of all, there is the so-called 'demonstration effect' exerted by the economic performance of a small group of developing countries, above all in Southeast Asia, in which the growth of trade has played a leading role. Secondly, in some countries there has been a movement aimed at enhancing the importance of the role of the market forces in the functioning of the economic system, and this has led to renewed interest in the theory of 'trade benefits'. Thirdly, the greater integration of the world economy, both in the markets for goods and for capital, has meant that whether countries like it or not they have had to establish closer international links.

It could be said that a combination of these factors has led several Latin American countries to increase the openness of their economies to international competition. Most developing countries, however, are reluctant to embark on the liberalization of their systems of trade and of international capital flows; among the reasons for this reluctance, mention may be made above all of the fact that many government policies, including controls on trade and the movement of capital, may have been carried out in full awareness of the fact that they would probably have adverse effects on the allocation of resources and on efficiency, if measured in term of market prices. Equally important are the arguments based on the externalities created by offering incentives for domestic production instead of importation, thus achieving minimum levels of industrialization.

There can be no doubt that long-term factors such as those indicated above may inhibit the opening up of an economy, but one must not reject out of hand the short and medium-term effects which also derive from the adoption of such a strategy. The most cursory observation shows that heavy costs are incurred when a country moves from a relatively closed economy to a more open one, among these

costs being losses of production and employment, balance-of-payments current account deficits, drops in fiscal revenue, increases in external indebtedness, etc. Whatever the long-term effects in net terms, these short-term costs may represent an effective obstacle to initiating a process of opening up the economy to the exterior. The identification of such costs, both at the macroeconomic and micro-economic levels, and the determination of their generality or specificity by countries is therefore of the greatest importance, but information on these matters is very scarce.

This study is therefore devoted to an analysis of the shorter-term aspects of liberalization policy, with a view to shedding some light on their magnitude and importance.

La empresa pública en la economía: la experiencia argentina (Public enterprises and the economy: the Argentine experience), "Estudios e Informes de la CEPAL" series, No. 21, Santiago, Chile, 1983, 134 pages.

The subject of public enterprises forms a distinguished part of the current political controversy in Latin America. On the one hand, the justification for their existence is questioned, even in the case of those which may be considered as part of the traditional activities of the State, because it is held that as productive bodies they disturb the normal functioning of the market, on account of the oligopolistic or monopolistic positions they enjoy, and also have an adverse effect on the allocation of resources, thus causing the functioning of the economy to be inefficient. On the other hand, while recognizing the need to rationalize their operation and increase their efficiency, they are considered to be indispensable instruments for achieving objectives of economic and social development.

This controversy has been present within the general topic of economic policy and development ever since the end of the war, with the tone varying according to the countries concerned and according to the political and economic circumstances through which they were passing. Nevertheless, the weight of public enterprises in the system of production of the region generally remains at a high and sometimes growing level, especially in the case of certain sectors such as those of the economic infrastructure (transport, communications and energy), economic and social services (electricity, drinking water, etc.), and mining (especially the oil industry), as well as in the iron and steel industry, petrochemicals and the manufacture of military equipment, in some of the most highly developed countries of Latin America.

For these reasons, this topic is being increasingly considered by academic and government circles in Latin America, since they are obliged to take decisions in which public enterprises play a leading role. Many of these decisions, however, are based on a very shaky knowledge of the operation of these enterprises and their links with the rest of the economy, since the various economic studies have not gone into the analysis of the State as an entrepreneur as deeply as the importance of this subject warrants, due, *inter alia*, to the scarcity of systematic data with the degree of detail, accuracy and timeliness necessary.

This study represents an effort to seek, for the case of

Argentina, to make good the lack of statistical data which hinders analysis of public enterprises.

Which are the main Argentine public enterprises? What sectors do they belong to? How are they linked with the public sector, with the productive sectors and with the overall national economy? How are they financed? These are the questions which the statistics contained in this study help to answer.

Las empresas transnacionales en la economía de Chile (1974-1980) (Transnational enterprises in the Chilean economy (1974-1980)), "Estudios e Informes de la CEPAL" series, No. 22, Santiago, Chile, 1983, 178 pages.

The foreign investment policy of the present administration in Chile is based on three fundamental principles: equal treatment for national and foreign investors; free access to the various markets and economic sectors for foreign investors; and partial withdrawal by the State from intervention in the activities of foreign investors. This is a policy favourable to foreign investment which is based on a specific diagnosis of the advantages which such investment is held to bring for the country: expansion of markets, improvement of the technological level, and an increase in the rate of national investment.

The objective of this study is to analyse some results of this policy by examining the presence and impact of transnational corporations in the Chilean economy during the period 1974-1980.

The study consists of three sections. The first section analyses the guiding principles of government policy on foreign investment, using a concept of public policies which includes the various types of regulations directly or indirectly dealing with this subject and the current administrative practices. The second section gives details of the main variations undergone by foreign investment as regards its flow and accumulated value; its sectoral distribution, national origin and composition; and its destination by enterprises and the types of organization used by transnational corporations. The policies of the countries of origin of this investment are also analysed. In the third part of the study, the significance of transnational corporations for the Chilean economy is examined and a study is made of the participation of such enterprises in some fundamental macroeconomic variables—capital, profits, employment, sales, investment, credit and wages—and in the national external sector as well as in the various sectors of the economy: industry, finance, mining, agriculture, fisheries, energy and hotels.

La gestión y la informática en las empresas ferroviarias de América Latina y España (Management and information science in the railway companies of Latin America and Spain), "Estudios e Informes de la CEPAL" series, No. 23, Santiago, Chile 1983, 195 pages.

The growing importance of information systems as supporting tools for the taking of management decisions is the reason for the interest of regional bodies such as the Latin American Railways Association (ALAF) and ECLA in

strengthening co-operation between the railway companies of Latin America and Spain in the search for improvements in the design and application of their information systems. These common interests have led these two bodies to undertake a series of joint activities, notably the initiation in 1977 by ALAF, the World Bank and ECLA of a horizontal co-operation project on railway information systems (the SINFER project). The various parts of this study are made up of contributions effected within the framework of this project.

The monograph which forms the first part of this study contains a brief review of the characteristics of a railway company from the point of view of information processing, hypothetical management models, according to the type of objective, and details of those already in use in the railway companies of Latin America and Spain, all against the background of a hypothesis which sees the institutional environment as a conditioning factor in railway management. An analysis is then made of the general considerations which it is desirable to take into account in the design of information systems to support railway management in the light of the external conditioning factors. Finally, the possibilities for technical co-operation between the railways of Latin America and Spain as regards the development of their information systems are analysed and guidelines are set forth for the continuation of the SINFER project.

The second part consists of the monographs presented at the first expert meeting by some of the enterprises participating in the SINFER project. These monographs describe some of the computational applications developed for management control at the executive level and for the operative management of such aspects as passenger seat reservation, wagon control, and management of stocks of spare parts and materials.

In addition, two appendices were prepared which it was felt might be useful for the companies participating in the SINFER project. The first of these sets forth a model programme contract designed to define the relations between the government and the railway company, while the other describes a conceptual model for the organization of a data base.

PLANINDEX. Resúmenes de documentos sobre planificación (PLANINDEX. Summaries of documents on planning), Vol. 3, No. 1, July 1982, ECLA/CLADES/ILPES, Santiago, Chile, 1982, 327 pages.

This is a six-monthly periodic publication each issue of which assembles details of the documentation on planning processed and entered into the CLADES data base, which is fed through the joint efforts of CLADES and the Caribbean Documentation Centre (CDC) of the ECLA Office in Port of Spain. For this reason, the summaries describing the contents of the documents appear in either Spanish or English, according to the source of the information.

During the years 1979 and 1980, the processing of documentation was restricted exclusively to that produced by central planning offices, in order to create a basic nucleus of information of use to planners.

This issue of PLANINDEX refers to part of the documentation existing in the collections of the ECLA Li-

brary, CLADES and the ECLA Documentation Centre in Port of Spain.

As this publication is a working tool through which it is possible to learn of publications which have been issued on the subject of planning and also select in a more informed manner the information needed by the planner, CLADES and the Caribbean Documentation Centre (CDC)¹ offer those interested the possibility of receiving total or partial photocopies, depending on their length, of the documents mentioned therein.

As the data base is centralized in Santiago, CLADES will be able in the future to offer other services resulting from the utilization of this base, namely:

a) Preparation of monthly lists of the information entered during that period into the computer, as an advanced version of PLANINDEX. These lists will be distributed at the request of the countries.

b) Specialized bibliographies prepared by computer search in response to express requests from users.

In order to obtain these services, application should be made to:

ECLA/CLADES
Casilla 179-D
Santiago, Chile.

Boletín de Planificación (Planning Bulletin) of the Latin American Institute for Economic and Social Planning (ILPES), No. 16, Santiago, Chile, October 1982, 188 pages.

This issue of *Boletín de Planificación* is devoted to a single country and subject. Because of its special features and progress in the field of planning Brazil is a case of particular interest, and the topic of regional development represents a priority area within the global objectives of development.

Between 30 November and 4 December 1981, the First Latin American Seminar on Regional and State Planning was held in Brasilia under the auspices of the Training Centre for Economic Development (CENDEC), in collaboration with ILPES, ECLA, UNDP and the Department of Liaison with States and Municipalities (SAREM). This seminar represented the second step as regards meetings on the problems of regional and State planning, the first step having been taken with the International Seminar on State Planning held at Guanajuato, Mexico, in May 1980 and organized jointly by the Mexican Centre for Development Training (CECADE) and ILPES.

At the Brasilia Seminar, some general problems of subnational planning were discussed and the experience accumulated in this field by certain countries was reviewed.

Since it is impossible to publish all the documents presented, this issue only includes a few of them, but future issues of the *Boletín de Planificación* will reproduce other papers which, because of their subjects, are of interest for the rest of the region.

¹The address of the Caribbean Documentation Centre is P.O. Box 1113, Port of Spain, Trinidad and Tobago.