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False dilemmas and real options in current Latin American debate

Aníbal Pinto*

This article points out the apparent inevitability that any controversy will lead to a *reductio ad absurdum*, that is to say that the points of view under discussion will be carried to an extreme which distorts them and renders the discussion sterile. This seems to apply to a number of dilemmas which taken to their opposing extremes, become false dilemmas or disjunctive propositions which do not reflect the true nature of the options and causes at the heart of the real controversy.

In developing his argument the author selects four highly topical subjects of current debate in Latin America. The first is the controversy concerning the roles of the State and the market in the economic process, a distinction being drawn between the situations which arise in the central economies and those in the developing and socialist economies. The second section contains an analysis of the opposed criteria relating to protectionism, and outlines the form these take in the industrialized and in the developing economies. The third deals with accepted views and disagreements concerning comparative advantages, with emphasis on the specific form in which these are found in Latin America. Finally, the author considers the problem of the opening up of economies to external trade and identifies the different meanings which are attributed to this phenomenon, citing the Brazilian experience in this regard.

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I

The market versus the State, planning, interventionism, and so forth**

Of course, this choice between alternatives is essentially fictitious, since the terms in question have coexisted, influenced, reinforced or contrasted with each other ever since they became crystallized in history. Whether in the capitalist or in the socialist structure, the *institution of the State* necessarily influences the *mechanism of the market*, just as the market influences the specific behaviour of the State —and all this occurs in different forms, directions and degrees depending on specific social circumstances, as will be illustrated below.

Although it is not the main purpose of this paper to embark on an examination of the nature of these concepts and the relations between them, a number of basic elements must be borne in mind.

To begin with, it is well known that the market —independently and in spite of the forces bearing upon it— fundamentally follows the dictates of “economic power”, in other words the purchasing power of individuals or of groups of persons organized in various forms. The so-called “sovereignty of the consumer” is exercised strictly in relation to the purchasing power available, in other words the distribution of income. To paraphrase Orwell, although all are sovereign some are more sovereign than others (and some, the underprivileged, have no sovereignty at all). The set of circumstances which influence their decisions

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—publicity, the demonstration effect, natural or cultural characteristics, and so on— affect this basic rule but do not contradict it. Thus, though some hold that the market's function is to satisfy needs, they often forget to add that this is true only for needs which are backed up by purchasing power. Moreover, in a capitalist (and not a mere barter) society, this will occur only on condition that the operation is profitable for those involved. There is therefore a *double mediation* between the functioning of the mechanism and the overall objective of satisfying demand.¹

Of course, these are obvious and familiar points, but that has not prevented them from being avoided and scorned in the orthodox approach which focuses attention on the abstract *homo oeconomicus* of traditional legend.

The State is a more complex organism, whose purposes and motivations go beyond

¹ An opposing view of the market, which could in some respects be described as "starry-eyed", can be gained from this description by an orthodox economist:

"As everyone knows, the economic system is essentially based on the market: in other words, the volume of items produced (and their prices) and the factors of production used (and the amounts paid for them) are determined in the market. What does this mean? Simply that we citizens, through our purchasing power, make our preferences known in the market by giving "signals" to the producers — by means of the prices we are willing to pay for goods and services — indicating what items must be produced in greater quantities and what items in lesser quantities. "High" prices mean that more must be produced, and "low" prices that less must be produced. If prices are "high", the producers will make money, and this will give them an incentive to produce more. In sectors where prices are "high", production will increase and so will demand for productive resources, including labour. This will tend to raise wages and salaries in the sector in question, and this in turn will create the incentives needed to increase supply." (Rolf Lüders, in the newspaper *La Tercera de la Hora* (Santiago, Chile), 23 August 1978.)

the strictly economic in many senses. Its links with the market have changed considerably through time, from the all-embracing tutelage of the pre-capitalist State to the laissez-faire approach of the nineteenth-century liberal State, which gave the market free rein while providing it with substantial support. However, what is of interest to us is the modern capitalist State, and particularly the power groupings which affect its relations. Even though it is possible to discern here the decisive influence of the groups and interests which correspond to the "economic power" of the market, it is nonetheless true that these are offset by other focuses of influence — trade unions, churches, technical circles and the bureaucracy, the intelligentsia, and so on. The balance will depend on the different power groupings and the degree of representativeness of the system. The State, consequently, is not a mere reflection of the power which prevails in the market: there is a more ambiguous relationship, which does not oppose this mechanism but uses the authority of the State to achieve specific ends not promoted by the market or to prevent consequences which it does produce. There is no need to point out that the underlying purpose behind all this is to strengthen the capitalist system, and not to destroy it.²

1. The causes of intervention

The growing intervention of the State in the functioning of the market mechanism has well-known causes extending beyond the list of its "imperfections",³ which Dr.

² The problem understandably looks very different in the socialist economies, to which we will refer in the final part of this section.

³ As H. Chenery pointed out some time ago, it would have been more useful if orthodox thinkers had started from the reality of an "imperfect" market, instead of becoming obsessed with the eventual (and impossible) elimination of the "imperfections" and persisting in speculation on the theoretical (?) premise of perfect competition.

Prebisch boiled down to two main elements: the lack of a social horizon, and the lack of a time or historical horizon, in other words a long-term view.

The first element, as already pointed out, is mainly due to the fundamental influence of income distribution and the derived effect of "circular and cumulative causation", according to the category established by G. Myrdal, but it extends further, to its economic and technocratic limitations, which undervalue or ignore a variety of ethical, cultural, psychological and other aspects crucial to living in society and often contradicted by the logic of the market.

The extensive critical literature on the traditional acceptance of the concept of growth and the contradictions of the "affluent society" offer sufficient evidence of this first of the market's vulnerable flanks.

The limitations of its temporal horizon are also transparent. To save argument it is perhaps sufficient to refer to another continuing discussion, on the "limits to growth". Whatever the particular assessment of the criteria involved, the various analyses have made clear the market's lack of sensitivity as regards taking account of damage to the natural environment and anticipating the many problems which inevitably accompany the historical pattern of development, particularly in those centres of population which are supposed to represent the pinnacles of progress.

The gap between the postulates of the orthodox approach concerning the nature, functions and effectiveness of the market mechanism and the real objective circumstances — those relating to economic, social and political issues, external links, and so

on — is even more flagrant if the actual situation in the peripheral countries is considered.

On this subject, in order not to dwell on already familiar side issues, it is useful to reread Dudley Seers' article on "The limitations of the special case".⁴ This article systematically sets out the characteristics which — in real or hypothetical terms — underpinned the orthodox theoretical edifice, and brings out their obvious contrasts with the context of the underdeveloped countries.

Moreover, the criticisms of the social indifference and the short-sightedness of the market mechanism which have been put forward in the central economies — precisely the scenarios where it has worked with the best results — are of even greater validity in the peripheral countries, where the problems which this mechanism creates or fails to solve (poverty, unfairness, destruction of natural resources, dehumanization at the national and cultural levels, and so on) are so much more serious.

These, then, are the reasons which have led to general agreement that it is the responsibility of the State — and, in current versions, of its most refined instrument, planning — to introduce or expand the time or social horizons of the market mechanism.

2. *The defence of the market*

Nevertheless, this clear trend has not prevented the orthodox ideology from persisting in its assertion of the supremacy of the market as the guiding force in the economic process and rejecting the idea of increasingly intensive and widespread participation by the authorities.

A most important fact stands out at the outset: that the present revival of the orthodox canons concerning the role of "market forces" is occurring in historical circumstances where the prevailing view is one of clear criticism not only of the sovereign market's effectiveness but even of its very

Bulletin of the Oxford Institute of Economics and Statistics, May 1963. This article forms part of the bibliography used for the courses given by the Latin American Institute for Economic and Social Planning (ILPES).

existence, at least in the original, "textual" theoretical conception. Going beyond the myriad arguments and proofs about the imperfections of the market and its remoteness from the pseudo-academic fiction of "perfect competition", some writers have even postulated, from various points of view, the existence of a "postmarket economy".⁵

Another striking fact is the growing concern in the central countries about the desirability, dangers and possibility of ad-

aptation of planning techniques in capitalist economies: a field in which, of course, the major corporations have already built up considerable experience. Not for nothing did J.K. Galbraith call them "private planning agencies". All this, as is obvious, implies a redefinition of the functions of the State and an increase in its already decisive influence on the management of the economic system.⁶

E pur si move... This clear trend has not, however, prevented the orthodox ideology on the subject from persisting, and although it has become weaker over the long term, it has temporarily gained strength from time to time in favourable economic and/or political circumstances. What is the reason for this contradiction?

A major reason is that the market mechanism which regulates the distribution of a society's resources, is very far from having reached —to use the Marxist metaphor— the moment of relegation, like some other institutions, to the "dustbin of history". And as long as an economy limited in some form and degree by scarcity exists, it appears certain that the market will continue to play a very important role, even though debate will continue on its relative significance and its ultimate fate if circumstances arise which are radically different from those characterizing the economy of the present and the foreseeable future.

A lesser explanation, but one which is nevertheless significant and reflects the influence of passing conditions, lies in the evident fact that the periods of "resurrection" of the market dogma —which like all dogmas is transitory— usually follow periods of crisis in heterodox policies. This is so, for example, in the case of the inadequacy or loss of momentum of the Key-

⁵One advocate of this concept, Ronald Muller of the American University in the United States, summarizes it in the following terms in his article on "National economic growth and stabilization policy in the age of multinational corporations: the challenge of our post-market economy":

"Let us reemphasize what is meant by a post-market economy. It is one in which the social function of the market, as an institution for equilibrating the economy, has been negated. Yes, there are markets in the sense of a 'commodity-space' indicating the total number of goods produced or consumed, but in the institutional, functional sense, which is explicit in the classical and neoclassical foundations of macro-policy, the market has largely been negated. The function of the market as a social institution is to generate price signals through the forces of supply and demand as carried out by independent buyers and sellers. In the Keynesian synthesis, these signals are relied upon by private business people, unions, and public policy-makers as indicators for decisions which govern the allocation of resources and the distribution of income. Where the market is operative, these decisions theoretically should result in full employment, price stability, and balance of payments equilibrium. Systematically, i.e., neither by intent nor design, but by the outcome of modern corporate competition, MNCs (multinational corporations) are a major source of market negation. They are so first, by the process of increasing aggregate concentration accompanying their expansion which increasingly distorts price signals. Second intracorporate transactions negate the market's social function, by definition, because they completely bypass the market. Market negation is another significant aspect of the Post World War II structural transformation of the United States political economy which has yet to be met by a transformed public policy outlook."

⁶See *Perspectivas económicas* (United States Information Agency, Washington), N° 15 (1976), issue devoted to "El debate de la planificación en los Estados Unidos".

nesian variant in some central countries, or the failure of some populist or revolutionary experiments elsewhere. The return to the theories of the past, which some advocates curiously describe as a step forward to the future, is reminiscent of a movement observable in the history of European culture, especially at the end of the last century, when the exhaustion of artistic creativity led to a new vogue for the Graeco-Roman heritage as a source of inspiration.

3. Possible forms of intervention

Leaving behind the previous discussions, and accepting as a fact the increasing regulation of the market mechanism, we must now briefly consider the forms which such regulation may take. Thus, we may say that the regulation takes place *through, outside or against* the market.

The terms involved, when put in this way, are to some extent artificial, since it is not at all difficult to imagine real situations where these possibilities exist or arise in combination. Furthermore, it can be held that whatever measure is taken the market will always be involved to some extent. Let us suppose, for example, that certain goods are directly distributed, free, to an underprivileged sector. Although it might be maintained that such an action avoids or goes against the market forces, it is nonetheless linked with such forces in reality, inasmuch as the products must be purchased, and this will have various effects on supply and demand, prices and so on.

Without prejudice to these objections, there is nevertheless a valid and significant difference between decisions by the authorities which encourage and are grounded in the "spontaneous" operation of the mechanism and those which, in different forms and degrees, deviate from or run counter to its inherent tendencies.

In order to illustrate this we may consider a capitalist economy and see how this non-

exclusive choice between distinct alternatives arises.

At the outset (and subject to the inclusion of other considerations later) let us note that, in a system of this type, the market falls within an institutional framework characterized by private or corporate ownership of the means of production. This framework is fundamental to its mode of operation.

Having established this basic premise, let us imagine the possible aims of a system of planning as conceived in some European countries. On the one hand, its dominant intention is *indicative*, that is, to make good or correct cases of temporary short-sightedness of the market by identifying signals and pointers towards the future which ease the task of decision-making and ensure that the decisions are consistent. On the other hand, however, the plans are *mandatory* as far as social expenditure and investment, for example, are concerned, and from this angle they correct or contradict the original scheme of distribution laid down by the market by its own "will" or, better, through the influence of the tendencies rooted in the existing structure of distribution.

The problem arises in a different way in the "developing" capitalist economies. The institutional basis may be similar, but there is fairly wide agreement that the market's imperfections are much greater and, as a result, its relative effectiveness substantially lower.⁷ In addition, while in the central countries the changes are planned within a context of relative continuity, in the others they generally involve discontinuities or breaks whose specific purpose

⁷ For a thorough discussion of this topic, see Raúl Prebisch, "A critique of peripheral capitalism", CEPAL Review, No 1 (First half of 1976) (United Nations publication, Sales No: E. 76. II. G.2) and the comments thereon in CEPAL Review, No 4 (Second half of 1977) (United Nations publication, Sales No: E. 77. II. G. 5).

is to eliminate the structural characteristics of underdevelopment. Thus, the allocation or reallocation of resources calls for mandatory changes when this aim is absent from, or runs counter to, the inclination of the market mechanism.

In order to illustrate this fundamental question it is sufficient to compare the very narrow margins of argument or disagreement involved in programmes for economic and social development in, for example, the countries of northern Europe, with those which are implied in principle *or in practice* by policies for Latin American development in such aspects as social implications, external linkages, and so on. The discussions concerning styles of development offer good evidence of this. In short, the mandatory component will tend to be larger than the indicative element in public policies which represent alternatives to the "free" operation of the market. At the same time, it is vital not to ignore or underestimate the complex and much discussed problems of the legitimacy and representativity of the forces which aim to offset or correct the logic of the market.

This argument does not imply, of course, that the desired transformation cannot, as far as is possible and necessary, be effected *through* the market, and still less that the latter's existence and power should be ignored; but the strategy of transformation will have a limited range of influence if it is not combined with action in two main directions.

The first of these directions is that of making some of the resources to be allocated more "independent" of the rule of the market. This is what happens in practice with the social expenditure and basic investment of the State. These are allocations which are *outside* and even, in a certain sense, *against* the market, but although their results will depend on the vigour, effectiveness and permanence of the decisions taken, they will nevertheless obviously

have limits deriving from the nature of the capitalist economy itself and also other more obvious restrictions, such as the availability of resources, consistency between action, dependence on external elements, and so on.

The second basic direction is aimed at a more radical purpose: that of modifying the structural conditions which determine the specific nature and functioning of the market.

Income distribution strategies may serve as an example to illustrate this issue. As already noted in some CEPAL works; it is essential in this area to distinguish measures with a redistributive purpose from those which are strictly distributive. "Distributive policies are those which have the aim or result of modifying the conditions which determine the "original" distribution of income. Redistributive policies imply only changes in this distribution effected after the fact. Of course, these are not watertight categories, and in reality policies of a mixed type may be identified."

Clearly, the distributive strategy goes beyond the economic framework. Consequently, the paper referred to above distinguishes three principal aspects. The first relates to the structures of production, which are characterized by the coexistence of technological strata ranging from the "primitive" (including even pre-Columbian) forms of existence to the modern sector, where productivity is similar to the averages achieved in the central countries. The second aspect relates to the nature of the typical social relationships in the various productive strata, which have to do with the

⁹See in this connexion Aníbal Pinto and Armando Di Filippo, "Notas sobre la estrategia de la distribución y la redistribución del ingreso en América Latina", *Trimestre Económico* (Mexico City), vol. XLI (2), N° 162 (April-June 1974). This paper was presented at the Seminar on income distribution and development, held in Santiago, Chile, in March 1973.

relationships of labour and ownership and the bargaining power of various groups and classes. The third aspect arises from the power structure, and can be seen first and foremost at the political level, involving as it does the representativeness and legitimacy of the institutional systems.

There is no need to repeat that actions aimed at achieving the transformation of these circumstances are not generally planned through the market, although they may make use of it. Indeed, it could hardly be otherwise, since they imply and demand both a modification of the very basis of the market mechanism, as it exists at a given moment, and a limitation of its application with the purpose of introducing certain social and time horizons, to which reference has already been made. These are the crucial responsibilities which must be assumed by the State and the planning machinery, to the extent, of course, that the political nature of the former and the efficiency of the latter make it possible to assume and discharge them.

Perhaps, on the basis of the above discussion, we can now reformulate the false dilemma between State and market in terms closer to the real situation in modern capitalist societies. On the one hand, it is clear that the State has an indispensable and unavoidable role to play in laying down major social objectives and ensuring that the market forces adjust as far as possible to them. On the other hand, in the efforts to secure this it is impossible to ignore the historical validity of the market in a society dominated by scarcity, so that what is done to modify its basis and redirect its thrust cannot reach the extreme of provoking what—in the light of various historical examples—might well be described as the “revenge” of the market.

4. *The situation in the socialist economies*

In order to round out the discussion and further clarify this complex problem, it

may be useful to refer briefly to the corresponding situation in the socialist economies, in order both to gauge the contrast and to indicate certain similarities.

If we take as an example the historical evolution of the Soviet Union, few will dispute that the basic instrument for the allocation of resources has been the five-year plans, backed by the absolute political power of the State and the Communist Party, and also by the public ownership of the means of production, subject to a few exceptions—as in certain minor aspects of agriculture—which do not alter the main fact. These were the institutional means used to achieve the priority economic and social objectives, and they made it possible to ensure consistency among these objectives in macroeconomic, technological and material terms to a degree compatible with the functioning and expansion of the system.

Income distribution and expenditure on consumption were also strictly controlled through drastic restriction of the “sovereign” operation of the market, partly by means of rationing but most importantly by “manipulation” of relative prices using indirect taxation and/or price fixing by administrative means. From this latter point of view it might well be said that secondary means were used for acting *through* the market.

It is fairly generally agreed that, more recently, the considerable diversification and greater complexity of the Soviet economy had led to a change in the relative importance of policies “independent” of the market—outside or against it—and those which make use of it within the parameters laid down by the plan and the institutional structure.

While we will leave aside discussion of the general significance of this change, it is worthwhile elaborating on this point in

the light of a recent study⁹ by a Soviet economist concerning the problems posed by, and means required for, adjustments to the structures of supply and demand, specifically in relation to the new circumstances in which this issue is arising in the USSR.

The author draws a distinction, of course, between questions relating to aggregate demand and questions of demand for specific goods or services. Concerning the former, there is no need to linger over criteria which are already quite familiar.¹⁰ Of greater relevance to the present discussion are those related to "the control of the microstructure of demand". According to the author, the task is not only to satisfy total effective demand; "the most important thing is the kind of commodities that the consumer will find in the store and the degree to which he will be satisfied with their assortment and quality". After referring to the extremely clear and crucial significance of transformations in the volume and

composition of supply and of technological progress — matters which are largely the responsibility of the planning system — he highlights the importance of the mechanism of retail prices, the use of which:

"is based on the interrelationship between the level of the retail price of a commodity and the magnitude of demand for it, which, as we know, is characterized by an inverse dependence... This circumstance makes it possible to stimulate (and sometimes to restrain) the demand for commodities through planned changes in the retail prices of individual commodities."

Finally, Levin draws attention to the important role of the means required to influence the choices of the individual consumer. In this context he states that: "the task of controlling demand through social and indoctrinational measures boils down to influencing the consumer's choice by shaping the preferences, opinions and tastes of individual consumers and to directing this choice into a sensible framework for the satisfaction of the normal needs of the members of socialist society, in keeping with ethical and moral demands".

We find ourselves, as we can see, on familiar ground. Nevertheless, the similarity to the use of the market mechanism should not lead us to forget the substantial differences in the basic context in which processes operate. From this point of view one can certainly defend the view that this use of the market is complementary and subordinate to the State-Planning complex, in other words that the situation is more or less the reverse of that prevailing in a capitalist economy.

This particular type of relationship among the terms in question has often been the subject of criticism, even in socialist circles, as regards its efficiency in the allocation and proper administration of resources. Without lingering on this point,

⁹ A. Levin, "Problems in the control of consumer demand", *Problems of Economics*, vol. XVI, No 8 (December 1973), pp. 81-104.

¹⁰ In this regard Levin writes:

"The control of aggregate effective demand is a part of the problem of controlling the process of socialist reproduction on the whole. In the given instance the most effective means of controlling demand is the mechanism of planned formation and alteration of the most important national economic proportions. The point is that the dynamics of aggregate effective demand and its quantitative dimensions and boundaries are largely the accumulation fund and the consumption fund, determined by the development of all social production, by the basic proportions of the national economy, and in particular, by the proportions between Group A and Group B in industry, between the accumulation fund and the consumption fund, between the growth of the production of consumer goods and the money incomes of the population, etc. Therefore, by shaping these key proportions in social production on a planned basis it is possible to control the dynamics of the aggregate effective demand of the population and to assure its correspondence to the supply of commodities" (*ibid.*, p. 84).

it is worth noting that the criticisms have largely concentrated on the so-called "microstructure of demand" referred to above. On the other hand, it would be difficult to extend them to the consistency of means and ends or to the overall adjustment of the system. As is generally accepted, the achievements are considerable, as regards both the development of the productive potential and the satisfaction of what are

known nowadays as "basic needs". In this last sense, with average income levels much lower than those in the advanced capitalist economies, the socialist countries have achieved standards of education and health, for example, which compare favourably with the highest in the capitalist world. In other words, they have undoubtedly been "efficient" from the social point of view.¹¹

II

Protectionism versus... what? Elimination of all protective barriers? Complete liberalization?

Unquestionably the dilemma has no meaning in the form given above, and what is actually involved — particularly in the developing economies — is the various ways and means of reconciling enlightened protectionism with the possible benefits of external links and the international division of labour.

As a start to the discussion it may be useful to introduce into the analysis a few relevant observations emanating from CEPAL, although these certainly do not add up to a general theory on the subject.

On the one hand stands the historical fact that the instruments of protection (tariffs, the exchange rate, administrative provisions) applied during the post-crisis period, which established the "protectionist situation", were on the whole not attributable to the aim of developing import-substituting industrialization, but were due to two intertwined elements: shortages arising from external imbalance, and discrimination in the use of absolutely or relatively scarce foreign exchange to meet domestic demand. From this point of view, this policy differed substantially from

the cases of spasmodic determination to impose "deliberate protectionism" for the benefit of certain industrial activities in the era of externally oriented growth. Consequently, the post-crisis practices constituted "protectionism by derivation", and became crystallized in a protective structure which was much more all-embracing and had very high defensive barriers

¹¹ Returning to an aspect mentioned above in passing (see page 4), it should not be forgotten that the element of profit or gain, although it has acquired greater importance with the growth and diversification of the socialist economies, is still not a decisive factor in the drawing up of objectives and priorities for the system. It has a clearly significant role, however, in assessing efficiency in the use of resources, contributing to adjustments in the microstructure of demand and serving as an additional incentive for managers and workers. Here, to use a classification by Pigou, there continues to be a fundamental difference between the "fact of profit" — as a basic guide for the allocation of resources in a capitalist or market economy — and the "profit motive", which signifies only the quest for personal benefit (see P. Sweezy, *The present as history*, New York, The Monthly Review Press, 1970).

which had little to do with the actual requirements of industrial promotion or other threatened activities. This general verdict is not invalidated by the existence of certain exceptions —as in Argentina and Brazil— which show a clear industrialization aim.

These facts were pointed out in numerous CEPAL documents as early as the 1950s.¹² From this viewpoint, then, there would be justification for efforts to “rationalize” the inherited protectionist system, as regards both tariffs and other measures permitting greater use of administrative discretion. However, this possible approach certainly does not imply the negation of the general protectionist argument, which has a solid and well-known basis, to which reference will be made below. To think otherwise would be equivalent to “throwing the baby out with the bath water”.

Another outstanding aspect is the old CEPAL argument concerning the difference in the nature and effects of protectionist measures as between industrialized and under-developed economies. To sum up: when applied on the periphery these measures have no overall restrictive effects on external trade, as is unequivocally demonstrated by the chronic tendency of the countries of the periphery to record a deficit on external transactions. In contrast, they usually do have such effects when they are introduced by the central economies. In other words, while in the latter they tend to reduce imports (and as an indirect consequence the exports of the affected parties), in the former they essentially affect not the *magnitude* but the *composition* of purchases abroad.

A rather extreme case which illustrates the contradictions that arise when this distinction is ignored may be found in recent statements by United States representatives concerning the need for Brazil to “liberalize” its import policies.¹³ It is obvious that this demand cannot be linked with any restrictive impact — the usual pretext in this type of behaviour — in view of Brazil’s persistent large current account deficit in recent years, but must be linked rather to discrimination affecting the composition of purchases made abroad.

Looking at the same problem from another point of view, this failure to distinguish between the specific circumstances of the centre and the periphery leads to a paradoxical situation. While criticism of the protectionism (using unconventional means) practised in the industrialized economies is increasing and reviving, and is focusing on the economies with persistent surpluses (the Federal Republic of Germany and Japan), the anti-protectionist trend is also gaining strength in some Latin American circles, even though the circumstances are fundamentally different in the two cases.

As has been argued, here we have two trends with quite distinct origins and objectives. In the first case, it seems clear that the aim is to *increase* trade flows and to help to achieve a return to balance in transactions between the centre and the periphery and between the central countries themselves. In the second, it is difficult to imagine effects on the volume of foreign trade, but it is possible to see clearly the effects on the *composition* of imports, which would inevitably tend to reflect the “market forces” (i.e., income distribution) and to diverge

¹²See *En torno a las ideas de la CEPAL: Problemas de la industrialización en América Latina, Cuadernos de la CEPAL* N° 14 (Santiago, Chile, CEPAL, 1977), especially chapter II, “Industrialización y protección”.

¹³For example, a speech by the Assistant Secretary of the Treasury of the United States, C. Fred Bergsten, to the American Chamber of Commerce in São Paulo on 8 December 1977.

from the aims of any deliberate effort in the field of socio-economic policy. The isolated attempts in this direction speak so clearly for themselves that further argument is unnecessary.

The mere fact that protectionist backsliding is persisting where it is most difficult to justify it — because of the high average productivity of the economies and their greater structural flexibility in adjusting to new circumstances — is a convincing argument in favour of the legitimacy of defensive measures in cases where the facts are appreciably different in these two respects.

Undoubtedly, behind the variety of excuses put forward, ranging from opportunities for infant industries to considerations of strategy and sovereignty, two fundamental interrelated facts stand out. One is the large "productivity gap" between the under-developed and the central economies, which justifies the principle of un-

equal conduct or treatment between non-equals. The other is the no less obvious fact that the activities where this gap is absent or minimal — and which therefore require no protection — are small segments of the economy, principally primary activities, which would not allow the system as a whole to be extended (even unequally) and would be incapable of absorbing the labour force. It goes without saying that these are two key points in CEPAL's treatment of this subject.

It is clear, moreover, that these two points are not put forward to justify indiscriminate protectionism, but merely a rational application of the basic principle that the numerous economic, social and cultural influences and the historical and political context must be taken into account in each period or moment. This very general formulation can be greatly clarified if the following "dilemmas" are examined.

III

Comparative advantages versus... what? Non-comparability of advantages? Absence of coercion in the allocation of resources?

The *reductio ad absurdum* in this field has meant that a fundamental and extraordinarily complex issue threatens to become an ideological myth or oversimplification.

David Ricardo cannot be held in any way responsible for this. Like other great representatives of classical thinking, he carried out a highly abstract exercise in the light of assumptions and objective data which were clearly identified as regards their nature and historical setting. The

profound change in circumstances which has taken place does not negate the truth or relative accuracy of his deductions, though it does substantially reduce their explanatory and normative force.

In the course of this process of change, comparative advantages based on the natural environment or a specific historical (and static) situation were superseded (but not negated, in the dialectical sense) by the so-called acquired advantages. The

latter, which are a pre-eminently dynamic concept, are the product not only of technical progress and its spread, but also of political decisions which are essentially voluntaristic — not in the pejorative meaning of the term, but in the senses bounded by the limits of what is possible and desirable. Japan's experience is always cited as an example of this evolution, but in modern development there are many other cases where natural and acquired advantages combine in various forms and proportions. From this viewpoint, certainly, one must not forget many Latin American countries in which the relative proportions of innate and acquired advantages have changed radically, especially during the past 50 years.

So far we have not mentioned anything new, but the review is useful in bringing us closer to the nub of the discussion.

Whatever the relative importance of the components, it is certain that the problem of comparability — the problem of allocating resources in the future (or reallocating the use of existing capacity) in line with the criterion of differential advantages — remains in effect.

The most orthodox view upholds a guiding criterion which is very clear and categorical (at least in its ideological presentation): namely, that of comparison with international standards, which are basically determined by the levels of productivity and prices prevailing in the central economies. Greater or lesser competitiveness as compared with this point of reference will determine the "economic viability" or "efficiency" of the activities in question. "Comparability" with these levels will justify their existence; "comparative disadvantages", their elimination.¹⁴

¹⁴In certain ways this operation would appear to imply the "end of under-development", in so far as its fundamental features refer to the productivity (and income) gap compared with the

This is, of course, the extreme version of a "Darwinian" logic which has never actually prevailed. However, it would be a mistake to underestimate the past and present importance of this view in international economic development, particularly in the peripheral countries. Springing up as it did in the favourable soil of imperial Britain, it is another of those spectres which are still haunting the world.

In its literature CEPAL necessarily had to face up to this topic when advocating industrialization and criticizing the "outdated model" (Prebisch) of the international division of labour.¹⁵ In these notes it is not necessary to recapitulate the reasoning in detail, but it is worth while summing up the central argument, the essential point of which is not so much the productivity-price comparisons with alternative items from abroad as the contribution to domestic supply which can be made by labour which is unemployed, underemployed or vegetating in activities with insignificant productivity and social priority.

Clearly, this valid option does not mean that any kind of initiative whatever is permissible. Apart from physical, technological, market-size and other limitations, the predominant considerations will be those rooted in the different social marginal productivity of the aims¹⁶ or other criteria,

centre, and structural heterogeneity. Unfortunately, it is not very clear what would happen to the "inefficient" activities and the work force associated with them.

¹⁵See, for example, CEPAL, *Theoretical and practical problems of economic growth* (E/CN.12/221), chapters II and III.

¹⁶On this subject, Prebisch points out that: "The increment of capital should be utilized so as to maximize production, which is only possible when the marginal productivity of the different investments is equalized... "This criterion offers a basis on which to determine the best means of utilizing the limited capacity to import, that is, which

which may also be non-economic. Here, then, lies the principal criterion which defines "comparative advantages" and by derivation — and this must be borne in mind — also serves as a guide for rationalized protectionism.

The above considerations obviously correspond to the discussions on import-substituting industrialization in circumstances where the capacity to import is evolving unsatisfactorily. The extraordinary growth of international trade and/or external credit in the period beginning in the second half of the 1960s restated the problem of comparative advantages in terms of another pair of options: not so much the choice between the waste of idle or underused resources and the opportunities created by protected and "inefficient" industry as the choice between an allocation of resources which economizes on foreign exchange (and frees it for other purposes) through substitutive production, and the generation of foreign exchange by means of a rise in exports and in external loans and investment.

products that were formerly imported should be replaced by domestic production, and which it is more advisable to continue importing. The advantage of developing an iron and steel industry instead of a heavy chemical industry, or of developing domestic production of all the footwear required by the population, or of the cultivation of all the wheat at present imported, will depend on the comparative increases of production which can be obtained in the different activities, according to the diverse alternatives open to the investment of the available capital besides other conditions influencing productive efficiency. If the same amount of capital as is required by an iron and steel industry gives rise to higher productivity in that industry than that in other activities replacing imports, its development will be economic, despite the fact that its cost may be higher than that of the imported product. It may be higher, but not so high as in other cases, given the average level of productivity in the country." (E/CN.12/221, p. 42.)

Basically the change is very deceptive, since the second dilemma reconstructs the argument of the defenders of the "outdated model". Nevertheless, there is no doubt that the events of the past decade referred to above have put new life into the orthodox position. Moreover, since the much maligned import-substituting industrialization of the past has now made it possible to broaden the exporting base with various manufactures (which for Latin America already represent about a fifth of the total), its Victorian view of the international division of labour has in part been rejuvenated.

This new angle to the problem prompts many observations. First and foremost, the revised version rests on a record of world economic and commercial performance which has been modified considerably since the oil crisis, and even before, as a result of the difficulties encountered by the central countries in maintaining a stable high rate of activity; I refer, of course, to the phenomenon of "stagflation".

A second observation, which is probably more important for the discussion, lies in the fact that even if one takes a cautiously optimistic view of the matter, either concerning the prospects of the industrialized economies, or concerning the margins within which the peripheral countries are likely to have opportunities other than those referred to above to continue to increase and diversify their exports, questions of fundamental importance still remain concerning the nature and consequences of industrialization-oriented policies.

Two versions of this approach may immediately be imagined. In the first, the dilemma of whether to obtain foreign exchange by means of exports or through "internally oriented" industrialization is resolved and dissolved by the fusion of the terms of the choice, which instead of being mutually exclusive strengthen one another. It is recognized that an effort to industrial-

ize may have as a consequence a prompt or eventual increase in exports (as has usually happened in practice), in the same way that progress in exporting may also promote industrialization through its forward or backward linkages (as has also happened in some cases).

However, in the other version — situated at the opposite extreme — the dilemma tends not towards a synthesis of (relative) opposites but towards the full blooming of their antagonism. From this viewpoint, import-substituting industrialization (past and future) is rejected as a matter of principle — unless it meets the strict and limiting requirement of international competitiveness,¹⁷ which in many cases will imply foreign control. The backbone of the policy will therefore be promotion of exports, and particularly exports from the primary or mining sector where natural comparative advantages are greatest. For a substantial proportion of these exports — for example exports of mineral origin — foreign investment will be clearly predominant.

In summary, this second route would involve a revival of the classical model in broadened and modernized form, with roughly similar social and political consequences — insufficient employment, highly unequal distribution, a radical split be-

tween the structures of production and consumption, and considerable internal and external tensions.

As already noted, this is a choice between extremes, but it may be useful in identifying various specific models, depending on whether they approach or differ from the standard model.

In closing this brief examination it is worth noting a clear and fundamental aspect: analysis of these and other related issues cannot make much progress without considering the great differences in national circumstances. As is obvious — and this is confirmed by international experience — each of these dilemmas assumes very specific features depending on the present or potential size of the domestic market. There is little doubt that there is a clear, though variable, link between this factor and the degree of openness of the economies (including the levels and forms of protection and the nature of the options as far as comparative advantages are concerned). Even so, the most fortunate cases of countries with relatively small domestic markets (such as the Scandinavian countries) unequivocally show their closeness to the first version we described, i.e., that in which industrialization and openness to the exterior combine instead of clashing.¹⁸

¹⁷ It should be noted that this competitiveness may not depend solely on real or physical productivity, or at least not so much on this as on, for example, a level of wages so low that import-substituting industrialization becomes economic from the "competitive" business viewpoint.

¹⁸ In Sweden, for example, exports represent about a quarter of the DGDP, which demonstrates the importance of internally oriented industrialization. And even where the proportion of exports is much higher, as in Norway (about 40%), this goes hand in hand with, and is backed by, intensive industrialization aimed at the domestic market.

IV

“Openness” versus . . . what? Autarky?
Unwillingness to increase or diversify exports?
or to expand imports?¹⁹

Obviously, the controversy is not put in such uncompromising terms.

Basically, in spite of all claims to the contrary, almost everyone is a supporter of openness, for various reasons, to different extents and in different ways, and this was the traditional attitude adopted in work carried out in CEPAL.

It so happens that some views of this phenomenon fit it the straitjacket of the orthodox criteria concerning comparative advantages, and are thus merely used to legitimize those export activities founded on natural and other resources which are profitable because of derisory wage levels,²⁰ or because of the ubiquitous participation of foreign managers. Taking a different view, however, openness should be a means of simultaneously accentuating the diversification and specialization of production, raising standards of productivity and levels of income and taking advantage of opportunities offered by new forms of insertion in the international division of labour.

¹⁹Various very important aspects of this subject are dealt with by Héctor Assael in an article entitled “The internationalization of the Latin American economies: some reservations”, to be published in issue N° 7 of *CEPAL Review*.

²⁰It seems evident that wage levels will be lower than in the highly developed economies—as always happens with the so-called late-comers—but there is no valid reason why they should not eventually equal or exceed the averages in the original developed countries.

The position of the supporters of openness is based on very clearly justified considerations.

With regard principally to the countries with currently or potentially large domestic market, the expansion and resulting essential diversification of exports is a prerequisite for enjoying the growing volume of imports which are necessary for reasonably dynamic growth in the “internally oriented” product (which certainly does not mean ignoring the incentive effect of external demand). This may mean rises or falls in the import coefficient, depending on circumstances, which include the characteristics of the external market and the possibility of securing additional resources by means of loans or investment. The smaller the possibility of using the second option (or the less it is wished to rely on it), the greater will be the need to stimulate exports.

Moreover—and this relates principally to economies with a fairly small domestic market, although it is also true of the above-mentioned situation too—the fundamental fact is that external demand plays a decisive and *direct* role in the vitality of the system. To a greater or lesser extent it makes up for any unreliability of domestic support, and in this way permits activities to develop which could not have done so otherwise.²¹

²¹The general characteristics of the two types of economies reminds one of Professor Arthur Lewis’s penetrating observation to the effect that the “motor” of economic growth is technical prog-

Continuing this argument it might be held, and rightly so, that the size of the market is one of the principal comparative advantages, since it makes it easier to develop or assimilate the so-called acquired advantages. Expansion of domestic demand to the maximum and the creation of complementarities through regional agreements are options which are not incompatible with openness towards the rest of the world but on the contrary establish a firmer base of support for this objective, as is shown by experience in Europe, including the socialist countries.

The main disagreements emerge once one moves beyond these observations.

A principal disagreement —and one which has already been mentioned, though in a different context— arises from the relationship between export promotion and the nature of imports. For some, “openness” is desirable to the extent that it makes it possible to increase external purchases of goods and services of greater social productivity, be they for investment or consumption. For others, the principal ingredient of this policy is “liberalization”, that is, the drastic relaxation or abandonment of any measures which discriminate against this trend, thus implying the general and substantial reduction of all tariff or non-tariff obstacles to this objective.

In Latin America we have seen more or less pronounced varieties of both kinds of “openness”, and it is clear that the focus of the discussion lies in the assessment of the “developmental” or social repercussions of this type of policy. The

dilemma, then, lies not in an abstract choice between whether to open up the economy or not (in the senses already indicated), but in the objectives and consequences of the different versions of the policy in question.

Asymmetry in openness: the Brazilian experience

Further aspects of the problem may be discerned when examining some particular cases in the region, such as that of Brazil, which is often considered a good example in this regard because of its well-timed and determined adaptation to the expansionary conditions which emerged in the world economy in the second half of the 1960s. I should like to refer here to a previous work²² in order to discuss the nature of this case and its lessons.

These favourable winds from outside were the basic support for what was termed an “outward-looking” policy of opening up to the outside, as opposed to the “inward-looking” policies of the past. The policy combined three closely related elements: vigorous promotion of non-traditional exports of both manufactures and raw materials; a substantial flow of foreign credit and capital; and a sustained increase in imports of intermediate and capital goods.²³

For the purposes of analysis it is necessary to bear in mind both the evolution of exports and imports and that of financial flows.²⁴

²² *Desarrollo, industrialización y comercio exterior, Cuadernos de la CEPAL*, N° 13 (Santiago, Chile, CEPAL, 1977).

²³ Brazil did not apply the criteria of “liberalization” of imports in the sense used earlier in the article, although purchases of consumer goods increased considerably in absolute terms.

²⁴ The data, which refer to the period 1970-1974, are taken from the work referred to above and from the *Economic Survey of Latin America, 1976* (United Nations publication, Sales N°: E.78.II.G.1).

ress and that external trade should serve as its lubricant and not as its fuel, although obviously the relative importance of these functions will vary with the circumstances of the countries as regards size, variety of resources, geographical position, and so on (this theory was set out in his Janeway Lectures at Princeton in 1977).

It is well known that exports increased rapidly between 1970 and 1974, at an annual average rate of just over 10%. This rise was almost identical to the rise in the total product, so that the relation between the two magnitudes did not change. In other words, the respective importance of external and domestic demand did not alter, and as a result the principal "motor of growth" continued to be the domestic market, or "internally oriented development".

Another view is gained by examining the sectoral breakdown of the domestic product and of exports. The most interesting point here, for present purposes, is that the vigorous growth in the manufacturing product between 1970 and 1974, which reached 12% a year, was easily outstripped by the growth of exports from that sector, which rose by nearly 20% a year. In some particularly dynamic areas, such as metal manufactures and machinery and chemicals, the corresponding rises were 15 and 20% and 13 and 32%.

From this viewpoint, then, not only was there an opening up to external trade in both absolute and relative terms, but it was accompanied by a thrust towards industrialization aimed at the domestic market, to such an extent that —notwithstanding the advances recorded in the previous paragraph— in 1974 domestic demand absorbed 86% of an industrial product which had itself, as we have seen, grown considerably during the period under consideration.

To return to a point raised above, this experience appears to resemble one of the versions identified in connexion with the links between industrialization and export promotion. However, other elements arise when the performance of imports and external financing is taken into account.

Thus, if the growth rates of the domestic product and imports over this period are compared, the contrast is striking: imports increased by 22% a year compared with

10.7% for the product. Accordingly the relation of imports to GDP rose from 7% in 1970 to 10.4% in 1974 as against 5.5% in the period 1964-1969. There is no doubt, then, that from this point of view the trend was markedly outward-oriented.

The imbalance can be seen more clearly if one considers the manufacturing sector and some of its main branches. For the sector as a whole the relation of imports to the total product rose from 14% in 1970 to almost 24% in 1974, and more or less the same change occurred in branches such as metal manufactures and machinery and chemicals. At any rate, it is important to remember that exports of manufactures rose during this period at double the average rate for the economy as a whole.

Even so, it seems clear that in this case, which might be called a textbook instance of opening up of the economy, there emerged a contradiction which has been the subject of constant attention in CEPAL: namely, the more or less pronounced asymmetry between the demand for imports which is generated by, and characteristic of, the dominant mode of growth in Latin America, and the capacity of this mode of growth to create sufficient foreign exchange to fulfil foreign commitments.

Of course, Brazil took a well-known way out: foreign investment, and particularly borrowing. The latter (State-guaranteed private and public foreign debts) rose from US\$ 5,295 million in 1970 to US\$ 31,200 million in 1977.²⁵ However, not all countries were in or can achieve the same position; and in the case of Brazil itself, events after 1974 made it necessary to subject the asynchronous type of opening up practised until then to thorough revision, from which lessons were drawn which it is

²⁵ See *Economic Survey of Latin America, 1977* (E/CEPAL/1050).

worth recalling in discussions on this subject.²⁶

Of course, the propensity to external disequilibrium characterizing the countries which embark on expansion of their economies may be dealt with in different ways. From the most orthodox viewpoint, the prescribed treatment is well known: reduction of levels of activity, employment, investment, public expenditure, and so on, up to the limit dictated by the external position, and essentially by the capacity to import.²⁷

In general, Latin American countries did not follow this path in the phases of depression, war or external strangulation which they had to face in the 1930s, 1940s, 1950s and part of the 1960s. Instead of deflating their economies and resigning themselves to the vicissitudes and poor opportunities of external trade, the larger countries—with greater opportunities for proceeding thus—contrived to grow at reasonable rates as compared with the historical average, and certainly at rates higher than those which the traditional doctrine would have considered possible and appropriate. In practice, between

1950 and 1965, for example, while Latin America's domestic product increased by 5.2% a year, its capacity to import rose by only 1.9%.²⁸

Because of the oil crisis and the fall in some commodity prices, the problem arose in a very severe form in 1974-1975. While some countries strove to accommodate themselves to the situation, by doing their best to reconcile the somewhat conflicting basic objectives of growth, employment, stability and external equilibrium, others tended to give priority only to those objectives which were associated with the balance of payments and inflation, introducing restrictive policies in an exaggerated version of the orthodox remedy, which led to unusual drops in their levels of economic activity and employment. The first strategy, as is evident, involved rejecting the orthodox models already referred to, for example by discriminating in the use of foreign exchange in such a way as to achieve the greatest degree of reactivation of the economy and the least effect on the external imbalance. In other cases, ideological resistance inevitably led to the opposite result, with high social costs.

²⁶ It is obvious that the rise in oil prices in 1973-1974 had an appreciable impact on this process. However, this factor acted more as the spark igniting the process of disequilibrium which had already been building up. In reality, between 1970 and 1974 the value of petroleum imports rose from some US\$ 600 million to US\$ 2,600 million while total purchases increased from US\$ 6,200 million to US\$ 12,600 million. In other words, higher expenditure on petroleum made up less than a third

of the total increase (see *Economic Survey of Latin America, 1975*, United Nations publications, Sales No. E.77.II.G.1).

²⁷ Obviously, we are not talking here about what might be termed a "critical disequilibrium" in the external balance, such as that which is caused, for example, by a process of runaway inflation.

²⁸ See, *Desarrollo, industrialización y comercio exterior*, op. cit.