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## INTRODUCTION

It is a matter of particular satisfaction for "Planning Bulletin" to offer in this special number a select group of articles on economic theory and its application in economic and social development policy. In the light of Latin American and Caribbean experience, all these articles provide valuable material for helping to understand the relation between social programmes and their economic implications and to evaluate the welfare effects hoped for from all economic policies. In the discussion of the different topics a leading role has been assigned to the conceptual and technical elements involved in the process of planning and generating employment, which is a fundamental objective of all policies for eradicating poverty.

This issue also includes valuable contributions by distinguished economists and sociologists on topics of fundamental importance for the design of the development strategy for the 1980s. Special mention may be made of such topics as social policy alternatives, the importance of social indicators in development planning, the political viability of social development, and some considerations on a pioneer work by Ragnar Frisch in the field of planning.

In addition, this number contains an article that describes and analyzes economic policy and performance in Jamaica in the 1972-1980 period. We believe that this effort constitutes a valuable contribution to the comprehension of this chapter in Jamaican economic history.

Finally, as is customary, this issue includes summaries of the articles which appeared in edition N° 16 of CEPAL Review.



## THE POLITICAL FEASIBILITY OF SOCIAL DEVELOPMENT \*/

Vaughn A. Lewis \*\*/

This paper concerns the political-economic constraints on policy-making relating to social development. We write with special reference to the Caribbean area, and in particular with that part of it which has acceded to independence in the post-World War Two period - the Commonwealth Caribbean or Caribbean Community (CARICOM) area. As will be indicated below, the populations of these states forced the concession of sovereign independence from the British metropole through the use of the mechanism of universal suffrage. This implied that the indigenous political leaders who acceded to control in these territories, did so on the basis of mass support; and on the basis of promising certain specific improvements in economic and social welfare to the masses.

For the populations of these states then, the expectation of persistently improving levels of economic and social development is embedded in the origins of the system. Such expectations provide an important part of the legitimacy of the political system. Further, because economic and social improvement constituted the prior claims of the majority of the population, the initially preferred mechanism - permitted within the system of colonial government of the time - was the trades union organisation, based on craft or occupational lines as was the case in the United Kingdom, or as territory-wide organisations - 'blanket unions'.

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\*/ Paper submitted to the "International Symposium on Social Development Policies in Latin America and the Caribbean during 1980's". Santiago, Chile, 12-15 April 1982. Not to be quoted without the permission of the author. The opinions expressed in this paper are the exclusive responsibility of the author and do not necessarily reflect the opinion of the institution to which he is attached.

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Such trade unions, which often commenced their activity by seeking improvements - increased wages, better working conditions - in particular economic spheres, tended subsequently to generalise their demands. In the process of such generalisation, the conclusion tended to be drawn that a political instrument for representation of these wide social demands was required. Thus the union base was used as the fulcrum for organisation of the mass political party. The union leadership and the new political party leadership tended then to be constituted of the same individuals. The political party was perceived by the union membership as one of the direct weapons in the struggle for social improvement.

Since the countries in question were in the main dominated by agricultural economies of the plantation type, the conditions of work of agricultural labour became a central preoccupation of the union leadership. While on the other hand, the large, relatively homogenous work force characteristic of the plantation (sugar, banana), constituted a ready-made force available to the political party.

This inter-relationship between agricultural labour and the political party, meant that changes in the nature of the plantation system were seen as among the immediately required results to be attained by the union-party leadership when universal suffrage was granted - and the indigenous population given some participation in the decision-making of the system of colonial government in the territories.

It should be noted however, that once, after the Second World War, the British Government conceded the complete legitimacy of union activity, and conceded that indigenous personnel would come to dominate the formal political and legal institutions of the territories, it sought to guide the development of unions and parties according to principles and practices developed and functioning in the United Kingdom.

The plantation-type agricultural socio-economic systems that dominated the colonial territories in the Caribbean sub-region were the dominant type of system. But mention should be made of the existence of important mineral industries in some territories (petroleum in Trinidad, bauxite in Jamaica and Guyana) employing smaller numbers of people than the agricultural enterprise, though at much higher-wage rates; and providing the relevant Governments with higher levels of income than those dependent mainly on the agricultural export trade. Because of certain similarities in the dynamics of their functioning, Caribbean economics specialists of the post-independence period have labelled both the agricultural and mineral economies as plantation systems.

It should in this context, then, also be noted that the Caribbean territories were the early location (like certain other colonial territories in Africa and the Pacific and South Asia) of a type of economic exploitation system which was the subject of extensive analysis in the 1960's and 1970's: the vertically-integrated corporation conducting activities over a widespread multicountry geographical space - the transnational corporation (TNC), like Tate and Lyle, the sugar producing enterprise.



In the English-speaking Caribbean area, the nationality of the TNC's tended at first to be British, reflecting the character of political dominance. In the middle 1950's, and then the 1960's, TNCs from the United States began to locate in this part of the Caribbean. This reflected also the beginning of a gradual British withdrawal from the sub-region, and the corresponding de facto increase in United States dominance as that country sought to fill any existing gaps in the Western Hemisphere strategic system.

The implication of all this was (and remains) that any attempt by the new indigenous political parties to substantially change this socioeconomic system, meant that the parties were involving themselves not simply in challenging the domestic systems of the countries, but came up immediately against the international system of which the TNCs are an important component. The feasibility, then, of inducing major domestic change, was partly a function of the strength of the relevant international environment. We have elsewhere summarised this phenomenon by saying that for the Caribbean political leadership, any intervention in domestic political economy would tend to involve an intervention in international economy. This process is reinforced by the 'open system' character of the Caribbean socio-economic systems.

We should briefly describe some characteristics and domestic implications of the transnational corporations existing in different types of environments in the Caribbean:

(i) In the case of the agricultural plantation system, the plantation tended to be spread widely over the physical space of the country, though it existed in some measure as a self-sufficient entity.

(ii) In the mineral economy or that dominated by tourism, the system tended to be located in isolated areas -enclaves; these were again substantially self-sufficient, and not in any major way dependent on the local government or economy for provision of goods and services.

(iii) In the agricultural enterprises -sugar, bananas, citrus, cocoa - there was large-scale employment of labour at relatively low wage rates; basically homogeneous in functional capabilities, and concentrated.

(iv) The mineral enterprises were characterised by employment of a relatively (to size of the labour force) small labour force, at high wage rates, and with functionally specialised skills and tasks.

(v) Until well into the period of national independence; both the mineral and agricultural systems were managed at the territorial level by expatriate (non-indigenous) individuals. This survived longer in the mineral and tourism systems, than in the agricultural systems.

(vi) The two major types of enterprises (agricultural, mineral) gave rise to the formation of trade unions with different types of memberships. Unions dominated by agricultural labour tended to be large mass organisations; those dominated by mineral systems tended to be smaller though wealthier, with a membership subject to the process of embourgeoisment, and somewhat apolitical. The important consequence of this distinction for the Caribbean socio-political system, was that it was the agriculturally based unions which tended to constitute the basis of the mass political movements. Mineral and service-based unions were secondary elements of the mass movements, though often providing leadership cadres, and being sometimes strategic for the crippling of the colonial (and even independence period) law and order system (we refer here to, for example, the strategic importance in 'national' strikes of ports and telecommunications systems).

The existence and dynamic development of, in particular, mineral and industrial (manufacturing import-substitution) enterprises, has given rise to various phenomena (problems):

(i) Widening gaps in the income rewards going to the different sectors of the labour force, involving the growth in some degree of a sense of "relative deprivation".

(ii) The development, therefore, of distortions in the wage structure as the demand for employment in mineral enterprises bid up the "reserve price of labour" - thus creating rigidities in the labour market and the phenomenon of unemployment in zones where there is an unfulfilled demand for labour. Distortions also arise in the demographic structure of the countries, as migration to 'company towns' occurs, and traditional patterns of settlement become disturbed.

As a consequence of the development of such phenomena, pressures have developed on the post-independence, union-based government to "equalise" the differential rewards from TNC investment. Here arises the attempt by such Governments to 'redistribute' the income, employment and psychic rewards available in the system. Thus the appearance which these governments have, of being distributionist, as against productionist (new investment) in their policy emphases.

Since the political directorate is one based on the universal suffrage, competitive party model, it feels it necessary to intervene in the previously agreed system of TNC-Government relations, and exert pressure on the TNCs in a number of ways; particularly where, as in the case of certain mineral commodities, demand for the TNC's product is at a high level:

(i) By seeking ever greater monetary income from the TNC, through negotiation for increased taxes or royalties. In Jamaica, for example, every electoral change of government has been accompanied by a renegotiation of the taxation-royalty agreements then in existence.

(ii) By seeking a wider representation in the structure of employment for its nationals engaged in the industry and employed by the TNC.

(iii) By seeking to induce the TNC to provide greater spill-offs for the rest of the economy; in particular through the creation of backward linkages that would, inter alia, induce the growth of an indigenous entrepreneurial class.

The purpose of seeking increased taxes or royalties from the TNCs, is to provide government with greater budgetary flexibility for servicing the demands of the mass population. This is especially important in circumstances where the Government has found itself incapable of generating major employment opportunities for relatively rapidly-growing populations.

And if we examine this form of pressure along with the others, it might be noted that they service different kinds of local constituencies. The first is, in effect, a form of mass-based pressure, with implications for the formation in the national communities of a kind of populist economic nationalism. The second mode of pressure, that relating to widening representation in the employment structure, is in fact the basis for a narrower corporate nationalism, induced by and intended to reward a more highly skilled, and a higher income, grouping in the local community.

The strategies of deriving greater rewards from the TNC system, and therefore, the political feasibility of achieving success in this endeavour, is therefore in part a function of the character of the local constituency that government intervention is intended to service. Different sectors of the work force employed by the TNC will not necessarily be in harmony with the negotiating strategy, since their differential location in the TNC's employment structure induces differing perspectives on the possibilities of success by government, in conditions that will not negatively affect the TNC's commitment to continued investment in the particular State.

To the extent then, that important financial resources for governmental use for social development derives from the local (that is, not including official external aid) budget; and to the extent that a major part of national income and foreign exchange resources derive from a single major economic activity (probably foreign-owned) in these mono-crop economies; to that extent will the political feasibility for deriving such resources be conditioned by the following:

(i) The structure of the major industry (economic activity) and the strategic character of the demand for its product in the international system;

(ii) The TNC's assessment of the development in the host country, and its assessment of the nature of both populist and corporate nationalism. This is usually what is meant by the euphemisms "political climate" or "political risk of investment" in the host country.

(iii) The Government's assessment of the vulnerability of the sources of both populist and corporate nationalism to internal or external pressure during the course of negotiation.

#### GOVERNMENT POLICY AND POPULIST NATIONALISM

Mass support is, of course, the base of populist nationalism. In the English-speaking Caribbean the unionisation of the labour force after the late 1930's, and the frequent transformation of the labour leadership into a political directorate after the grant of universal suffrage, led to the formation of governments espousing what today might be called a philosophy of labourism. At the time (especially in the 1940's and 1950's), this was referred to as socialism -encompassing a demand for better economic conditions (economic justice) for the labour force; secure and new employment for unemployed and under-employed; the transformation by gradual means of the essentially agricultural economies into industrialising economies. Such economies would be 'mixed' in two senses: they would be public/private sector economies, and they would be agricultural/industrial economies. And all this was to be accomplished within the framework of some form of parliamentary democracy.

In pursuit of these objectives, the 'labour-based' political directorates adopted policies of 'industrialisation by invitation', directed to the rapid increase in employment. This foreign investment-induced strategy turned out to be, in the larger countries, of the import-substituting kind (as in much of South America) based not, as originally expected, on regionally integrated national economic systems, but on separate economic systems of limited market size.

Though in fact there was an expansion of employment opportunities in these countries, the rapid growth of populations (therefore labour forces) due to better Government-provided medical and health facilities, in addition to the limits to import-substituted growth, led to the phenomenon of larger, unemployable labour forces. Relatively rapid economic growth (dominated by new enclave industries) accompanied by an expanding service class-middle sector, in the context of growing pools of unemployed fed by persistent rural-urban migration, led to serious perceptions of relative deprivation within these small communities.

By the end of the 1960's the political directorate, the rationale for whose existence was their promise to improve the conditions of labour, were widely perceived to have created a system in which the main beneficiaries were the entrepreneurial and middle sectors. Further, the legitimacy of the union-party nexus as the fulcrum of national politics, was increasingly questioned, as it became apparent that a major part of the 'labour force' was not only not unionised, but unemployed and not therefore capable of unionisation. This force - a veritable lumpen-proletariat - however, was fully enfranchised.

Now, the demographic structure of the Caribbean population as a whole had (has) also become progressively skewed towards the younger age groups. This additional factor means that there is now posed not simply a problem of the potential capability of the system for providing employment, but also of the more general capacity of the political system for providing social service and welfare arrangements for this group; and of the system's capacity to provide appropriate education towards employability in the economic system.

The dimensions of the problem are suggested in the statement in the World Bank's recently published study 1/ on the CARICOM area, that "on average" 46 percent of the populations of the CARICOM countries are under the age of 15. According to this report, "in Belize, Guyana, Jamaica and the Windward Islands children under 15 years account for almost half of the total increase in population", though "in Barbados and Montserrat they are less than 40 percent of the total" (p.58).

The problem has not, to this writer's knowledge, been more sharply posed in recent times, than in the Five Year Plan 1978-82 for Jamaica, published by the Government in 1979. 2/ The Plan notes in one of its projections - a projection of declining fertility for Jamaica (Projection 11) - that there is a large (25 percent of the 1975 population) and accelerating (32 percent by 1983) population grouping in the 15-29 age group. Secondly, the Plan gives a present estimate of 40 percent "functional illiteracy" for the population as a whole.

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1/ S. Chernick, The Commonwealth Caribbean: The Integration Experience, IBRD/John Hopkins University Press, 1978.

2/ What follows is drawn from my extended review of the Plan, in Social and Economic Studies, 1980 (ISER, University of the West Indies).

Now Jamaica has in recent years devoted substantial resources to the effort to make a major assault on its inherited literacy problem. Yet by 1978, the authors of the Five Year Plan could still make the following observation:

"In 1972 it was estimated that between 400 000 and 500 000 persons over 15 years old were functionally illiterate, and according to JAMAL reports, 168 000 have been made literate through the programme. However, due to the fact that about 40 percent of those leaving the formal education system are still functionally illiterate, the estimated number of illiterate adults is almost the same as it was in 1972".

Dealing further with the age group 15-19, the observation is made that:

"These ages include the critical periods of skill acquisition, entry into the labour force and the development of work habits and social attitudes... (but) the structure of the economy, the absolute size of the age group, and the prevalence of illiteracy makes absorption of youth into the socio-economic life of the country difficult".

A reading of the Plan indicated a more than inferential linkage between employment, the development of small-scale agricultural, agro-industrial, and industrial activities, the resolution of the problem of functional illiteracy, and the prospects for social peace and order.

For most of the Caribbean countries, the inferences must be more or less the same. A 1979 World Bank Report on St. Lucia, noting that two-thirds of the population of this country is under 25, goes on to observe that:

"The youthfulness of the population... has led to a steady stream of school leavers who have caused the labour force to increase at a much faster rate (than the annual rate of population growth). The pace of economic development has not been sufficient to generate adequate employment for the burgeoning labour force. The trend has been exacerbated by declining production in agriculture and the inability of the tourism and manufacturing sectors to take up the slack as well as by declining rates of emigration in the 1970's."

In the face of such descriptions, it is not difficult to find, nor need one seek, deep explanations of political volatility in these countries.

This group of young, mostly functionally illiterate individuals, functions within the competitive political systems of the Caribbean as an essentially destabilising force, as politicians have fought either to absorb or suppress it, depending on their, and its, location in the extant political system. The Caribbean political directorate has for most part come to the conclusion that a way must be found of absorbing the group into the socio-economic system, if the political system and therefore the policy-making process are not to be subject to continual instability. The appropriate absorption of the youth population into employment is, in fact, the central contemporary problem of economic planning in the sub-Region. And insofar as in some of the countries, it is compounded by the problem of functional illiteracy, then the question of the link between the form of education provided, and the character of the employment intended, is an important aspect of the problem.

On the other hand, this youth grouping is now the basis of much of what is called populist politics in the sub-Region. And political parties, operating within the framework of the competitive party system that still has much legitimacy in the countries, function, and propose policies in such a manner as to suggest that the policy options for solution of these problems are in fact much wider than they really are. In the contemporary period, characterised by unstable international economic conditions and lessening financial flexibility in their domestic systems, the constraints which they have discovered in exercising policy options, have forced the politicians to seek unorthodox (within the history of these political systems) solutions. What then appear to the metropolitan policy-makers as conscious ideological choices, are in fact pragmatic courses, taken under pressure from disappointed populist forces.

#### INTERNATIONAL SYSTEM, SOCIAL SECTORS AND POLICY CONSTRAINTS

Populist pressures, whether in Jamaica, Trinidad or Guyana, in the late 1960's and 70's, have induced the political directorate engaged in the strategy of industrialisation-by-invitation and import substitution, to seek additional financial resources which can be diverted to the long- and short-term needs of the mass populations. The industrialisation strategy had meant that Governments chose to forego, through the grant of various kinds of incentives to both local entrepreneurs and manufacturing TNCs, revenue that might have been obtained, among other ways, through corporate taxation. The justification was that such a strategy was, for a region of small economic size and limited material resources, the only way of inducing the TNCs into investment whose ultimate rationale was (from the point of view of the Governments) local employment.

Governments had two additional sources of revenue for social expenditures. One was through recourse to assistance from regional and international economic institutions, such as the Inter-American Development Bank (IADB) and the World Bank (IBRD), and the various United Nations institutions concerned with development aid. The construction of schools and health facilities is indicative of this kind of assistance for investment in physical and human resources.

One impediment, however, to this assistance for the sub-Regional states, was the difficulty of obtaining funds from the 'soft loan windows' of the financial institutions, on the grounds that their per capita incomes (high relative to most Third World countries) placed them outside the category entitled to such assistance. Another impediment for one specific state, Guyana, was a function of geopolitics: the Venezuelan territorial claim against Guyana barring that country from membership of the OAS and therefore (until recently), from the IADB.

The independent countries of the sub-Region at that time, were in fact beneficiaries of the era of relative plentifulness in official aid deriving from the Alliance for Progress philosophy. Though, one state, Trinidad and Tobago, was to complain in the late 1960's, that precisely at the time when its foreign exchange reserves were minimal (as a consequence of the decline of her major export staple), and when therefore, such external assistance was really needed, the 'conditionalities' attaching to assistance inhibited the Government from availing itself of it.

The second source of revenue for major social expenditure, has been foreign exchange from windfall gains deriving from periodic high prices or high demand for the local export staple. Very often in the 1970's, Governments have used such financial resources to meet short-term (immediate) mass demands (food subsidies, special employment programmes). Such allocations have served the purpose not only of raising living levels (albeit temporarily as some would claim), but also of stabilising the political system under pressure from the deprived. Such allocations have also been made often against the advice to bureaucrats concerned with both budgetary control and long-term development planning; and of private entrepreneurs concerned with maximising subsidies to the private sector. Both of these groups tend to claim that Government should make more 'rational' allocations of such unexpected, and historically transitory resources.

Experience has been that with the end of favourable international trade circumstances, and the decline of the windfall gains, the strain on national income and the budget to maintain these 'short-term' allocations, has led to excessive deficit financing, foreign exchange crises, and consequent pressure from both internal and external sectors to exercise financial constraint through the reduction of social expenditure. In the



late 1970's, non-oil producing states have been the objects of such pressures, as even the relative stability of the post-war international economic system came to an end. For such countries, there occurred a conjuncture of both unfavourable international and domestic conditions.

The situation of Jamaica in the late 1970's is indicative of this situation; though other states in the sub-Region were also subject to it. 3/ The unfavourable international conditions had two aspects:

(i) A global situation in which the metropolises were characterized by inflation, increasing unemployment, adjustment to the monetary effects of the transfer of resources to the oil-producing states, less buoyant international trade and therefore less demand for developing country products in general;

(ii) With particular reference to Jamaica, instability and declining demand for the country's major foreign exchange earner - bauxite-alumina. The imposition of higher taxation on the TNCs, appears simply to have reinforced their inclination to reduce investment and exploitation of the product.

Unfavourable domestic conditions (a process) included:

(i) Decreasing buoyancy of the local economy, increasing unemployment, increasing lack of flexibility in using the normal mechanisms of economic policy because of inadequate foreign exchange reserves;

(ii) Increasing dependence on official external sources for meeting immediated government revenue demands.

Such a conjuncture led (in the case of Jamaica) to an increasing paralysis of the economic policy-making machinery, as Government became subject to conflicting demands from its populist support base on the one hand, and the domestic private sector and the political factions representing them, and the international financial institutions, on the other. External demands focussed, inter alia on the area of reduction of short-term social expenditure, leading to a political situation far from optimal for a Government operating within the competitive party system. In the clash between competing sectors, some of which in this open system are abetted from 'outside' the system, the weaker and socially-deprived sectors, and the political factions representing them, are invariably defeated in the struggle over the budgetary allocation process. 4/

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3/ Discussion of some of these factors can be found in N. Girvan et al., "The IMF and the Third World: The Case of Jamaica 1974-80", Development Dialogue, 1980:2, pp. 113.155; and in Adlith Brown, "Jamaican Economic Policy in the 1970's", ISER, UWI (mimeo), 1979.

4/ The work of Markos Mamalakis on the theory of sectoral clashes is instructive and helpful in this regard.

## SOCIAL POLICY PRIORITIES IN AN UNFAVOURABLE INTERNATIONAL ENVIRONMENT

The instability of the economic growth process (periodic recession) in the major metropolises, with its concomitant effect on international trade, has not only contributed to the slowing of the growth process in many Third World states. It has also provided a rationale for metropolitan Government's desires to reduce their contributions to the international aid programmes, both bilateral and multilateral.

At the same time, Third World countries, including those in the Caribbean have, with the decline in the scope for import-substitution and the pressure on foreign exchange resources, decided to pursue the path of export (manufacturers) - led growth - preferably for the smaller economies, through the joint-venture process. The political directorate is of course aware that dependence on the major traditional staples (bauxita, tourism, sugar, bananas), and thus the revival of international trade, are still crucial short-run factors for them.

There is, nevertheless, an awareness that with the deliberate official bias towards raising the level of manufactured exports, with its consequent bias in incentives towards the private sector industrializer and the agents of direct foreign investment, some care should be taken to ensure the social development of the actual and potential labour force - if only to equip them physically and technically for the possibility of employment in the industrial sector. (In most of the Caribbean states, it is conceded that for the long-term, agriculture of the plantation type will not be a major employer of labour; yet, apart from a recent rhetorical commitment to the necessity for food production, there is little detailed emphasis on the methodology of agro-industry production).

With the scarce financial resource situation in a context of growing youth populations, international assistance programmes to Governments would seem to need to be directed to ensuring the provision of (a) basic needs for these populations and (b) appropriate educational (technical and vocational) training and facilities for small-scale employment in both urban and rural areas.

The rationale for this approach is as follows (and is deducible from what has been said above). In the sectoral struggle for scarce budgetary resources in a period of relative financial deprivation, Governments' commitments to export led growth biases budgetary expenditure and governmental attention towards the private entrepreneurial sector. It is true that the maintenance of existing health and educational infrastructures consumes a major proportion of national budgets. These infrastructures however, still service an insufficient proportion of the urban and rural poor. In addition, educational structures are largely

of the traditional kind, and largely incapable of dealing with the existing functional illiteracy problem. Little too, has been done in these countries to attempt to determine what mix of educational skills is most appropriate to what form of existing or potential employment.

A bias in international assistance towards the areas outlined above would, therefore, be useful for two reasons. First, it would rebalance the weight and influence of the rural-urban poor in the resource allocation system, and ensure a reasonable allocation of resources towards that sector. Secondly, it would ensure some modicum of continuity and stability in the resources allocated to these sectors, isolating them somewhat from the tendency to treat them as 'first victims' of budget-paring processes.

#### SYSTEMS OF REPRESENTATION AND INFLUENCE ON POLICY MAKING

As we have intimated above, the necessity for Government to give priority to the industrialization process, and to open the channels of influence in a substantial way, has lessened the role and influence of the labour movement over these labour-based Governments. Within the essentially Westminster parliamentary systems which exist in the CARICOM area, parliamentary representatives and the Executive arrogate to themselves the major roles in decision-making. They use the labour movement as a support battalion when necessary; but essentially relegating it to the status of one pressure group among others. The historical primacy of labour in the process of attainment of independence is not necessarily acknowledged as relevant to the contemporary period; though labour's support is momentarily required at election periods.

In the 1960's, labour as an institutional economic sector was called upon by Governments to give support to the attempt to establish institutions to control the alleged excessive growth of wage costs in the production system; and thus to help ensure external competitiveness. This was the period of incomes policies, paralleling similar innovations occurring in the United Kingdom and elsewhere in the metropolitan world.

Here was an attempt, in effect, to establish a corporate system, parallel to the Westminster political system, for purposes of economic decision-making - or better said, for purposes of legitimising Governmental decision-making. In this system, labour and capital as the major institutional groups, were to have equal institutional weight in the system, the price of which for labour was the trading off of 'excessive' wage claims against the promise of long-term stability in employment and real income. In constitutional terms, Government's objective was the establishment of some form of National Economic Development Councils. (It should be noted however, that in the Westminster system, the process of budget formulation is a highly secretive one. Discussion of Governmental proposals is therefore extremely limited. Though there is

extensive discussion in parliamentary committees after the announcement of the Budget, Government is by then firmly committed to the main lines of its budgetary policy).

In many countries, this attempt to induce labour into the decision-making system was not successful. In Trinidad and Tobago, for example, its failure was marked by the establishment of the Industrial Stabilisation Act, involving the legislation of wage-setting procedures and appropriate sanctions. This had the effect there of further alienating a major part of the labour movement, eventually setting Government and labour in conflict, with private sector supporting Government.

In Jamaica in the late 1970's, the International Monetary Fund's insistence on severe budgetary restrictions, forced the Government, in its pursuit of national support for such policies, to entertain a wide measure of public discussion of economic proposals, before their formal enunciation. But the division of the labour movement in that country along party-competitive lines, inhibited the process of decisional commitment that was the desired outcome.

The problem of various socio-economic sectors' influence in economic and social decision-making processes, and its relation to the Westminster parliamentary-executive system's insistence that it should retain institutional primacy is still an unresolved one. This general problem is often discussed as if the Caribbean country's politico-economic system is de facto an autonomous one, not subject to major external institutional and processual influence.

One consequence is, that while the Executive is asserting its right to virtually exclusive decision-making at the expense of labour, external decision-makers are simultaneously exerting major influence on the same decision-making process. And to the extent that the local entrepreneurial sector has historically had, and maintains, strong channels of mutual influence to external decision-makers, the institutional bias against the influence of labour is further exacerbated.

ALTERNATIVES OF SOCIAL POLICIES FOR LATIN AMERICA  
AND THE CARIBBEAN IN THE EIGHTIES \*/

Don Mills \*\*/

In the face of the complex issues which are the subject of our discussions I have no prescriptions or formula to offer. I shall express some thoughts which reflect my own deep concern about the future of development in Latin America and the Caribbean.

Almost all of the countries of the region have attained independence, some a considerable time ago, others, notably in the Caribbean, in relatively recent years. They have concentrated their energies on the struggle for development, and for a just international economic order. In the process these countries have, in general, achieved some considerable successes. But such progress has often been won at a high cost in social terms.

The countries of the region are now confronted with the circumstances of a world which is going through a process of rapid transformation. It is a period of grave economic difficulties, and of considerable tension within societies and countries, and between countries with open conflicts in some instances. Underlying all of this is the rising demand for political expression and participation and for social advancement.

In the words of Mahbub ul Haq:

"Our age has been described variously as the Age of Technology, the Age of Anarchy, the Age of Uncertainty. If we are to survive at all as the human race, we must graduate into an Age of Equality, since equality of opportunity has increasingly become the central issue of our time".

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\*/ Paper submitted to the "International Symposium on Social Development Policies in Latin America and the Caribbean during 1980's". Santiago, Chile, 12-15 April 1982.

\*\*/ Former Secretary of State (Jamaica). The opinions expressed in this paper are of exclusive responsibility of the author and do not necessarily reflect the opinion of the institution to which he is attached.

For Latin America and the Caribbean the problems and challenges are no less than elsewhere. In my own view the decade of the 1980's will be a most difficult one for the region: no problem facing these countries is greater than that which relates to the issue which is the subject of our discussion -namely how will they create and sustain truly equitable societies. While the countries of the region share some of the problems of the other parts of the world, they also face some circumstances of a special nature. These include the composition of their populations and in particular the pre-Colombian peoples, the large inflows of population from Europe, from Africa and in some cases from Asia; the evolution of a variety of political institutions and forms of Government; and the very nature of the economic development in the countries, especially in the post-World War II years.

The demand for a greater degree of equity is universal. It is no respecter of political or economic systems.

One of the major lessons of the past 30 years, a period which has witnessed great concern and considerable effort in respect of economic development at the national, regional and global levels, is the paradox, the contradiction between economic growth and social justice. It is no wonder then that there has been in more recent years a growing preoccupation with the issue of the gaps - in income, in opportunity, in technology, in education, in information - between North and South, but also within countries.

The industrialized countries, as their economies have advanced, have used a variety of devices to limit or to narrow the gap between sectors of their populations, or between regions of their countries. It is interesting to observe also that some services concern has been expressed about the gaps in development and income between the more and the less affluent countries of the European Community

The industrialized countries today face a serious dilemma. The social provisions, the welfare systems, which have been taken to such lengths, in some instances, during the boom period of economic growth of the 1950's to the early 1970's, are now threatened by the prolonged economic crisis. Deep differences have existed between OECD countries over economic policies related to the high levels of unemployment now being experienced.

It has been argued, by some prominent leaders in the North, that the "industrialized democracies", the one-man-one-vote-countries, have largely based their social provisions on the expectation of continued significant economic growth. In the face of what might prove to be a period of slow growth, or no growth, these countries face the necessity of cutting back on the social and welfare benefits and expenditures, and with that their governments face the possibility of being voted out of power.

But this dilemma is not confined to the richer countries. The situation is basically the same in Jamaica and other countries of the Caribbean and in many Latin American countries.

Indeed to a degree it faces all countries, whether they are described as democracies or not. The significant point made by the persons in the North expressing these concerns is that such situations can erode the foundations of the democratic system, since in times of hardship it is almost impossible for a government to carry out what it might regard as strong measures of economic management.

It is in these circumstances that we are considering what Latin America and the Caribbean can do in the 1980's to significantly advance its performance in the field of social development.

The situation in Latin America has been summed up by Enrique Iglesias as follows:

"one of the major contradictions in Latin America in recent years is that in spite of its achievements in figures and indicators, the social situation of the region has improved only for certain minority groups and very little for the rest".

It has been projected that by the year 2000 A.D. most of Latin America will have reached a per capita GNP of US\$2 000, that is about the same as Europe in 1960. There will still be many countries of the world with a far lower per capita GNP. Is Latin America likely to achieve a balance between economic growth and social development over the next two decades that will allow a favourable comparison with the Europe of 1960? To do so, or do better than that, will require significant changes in perception in policies and in political and governmental system. In any event the comparison with Europe may be of little value.

I believe that the issue of social justice is at the root of the tensions and upheaves in Central America today, and the problems of the Caribbean countries. Inevitably, there are other factors involved, but a mis-reading of the real root causes will diminish greatly the prospect of effective solutions.

There is no lack of recognition of these issues in international fora. The International Development Strategy for the Decade of the 1980's was approved by the U.N. General Assembly in October 1980. The strategy was prepared against the background of the ongoing crisis in the international economic system, the deteriorating position of developing countries as a whole, the rising tension in many parts of the world, the erosion of economic and social gains, and the diminishing prospects of those who had so far only the hope of such gains. The preparation of the Strategy involved meetings at the regional level, and gave Latin American countries and others the opportunity of contributing ideas and proposals.

The Strategy inevitably uses moderate language and speaks in general terms on such issues as the urgent need to achieve real social progress in developing countries.

"It is for each country to establish adequate national objectives for the promotion of human and social development within the framework of its development plans. The final aim of development must be the continuing increase in the well-being of the entire population on the basis of its full participation in the process of development and a fair distribution of the benefits therefrom".

The Strategy goes on to deal with some of the critical requirements:

- the reduction and elimination of poverty;
- the achievement of full employment;
- the implementation of the recommendations of the World Population Plan of Action;
- the development of human resources, by education and other means, to enhance the capacity of people to participate constructively in the development process;
- the attainment by the year 2000 of a level of health that will permit all peoples of the world to lead a socially and economically productive life;
- the provision of basic shelter and infrastructure for all people in rural as well as urban areas;
- the securing of equal participation by women both as agents and as beneficiaries, in all sectors and at all levels of the development process.

Although some specific targets are contained in the Strategy, these aims are in the main stated in general terms. Moreover it clearly emphasises "that each country will freely determine and implement appropriate policies for social development within the framework of its development plans and priorities and in accordance with its cultural identity, socio-economic structure and stage of development".

The approach embodied in the Strategy has been described as "the utopian-normative approach" and a comment on the Strategy for the 1970's may be recalled here.

"Its shortcomings when pursued in isolation (or its illegitimate uses as an evasion of reality) are cruelly exposed in a world in which the dimensions of injustice insecurity and violence continue to grow while the list of "rights" to which all human beings are entitled by the votes of their governments continues to lengthen". <sup>1/</sup>

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<sup>1/</sup> Marshall Wolfe, "Approaches to Development: Who is Approaching What?" in CEPAL Review. First half of 1976.



Attempts have been made to establish a clear connection between this issue of social development and the call for the New International Economic Order. Some interests in industrialized countries have gone so far as to virtually imply that evidence of movement toward the achieving of social justice in developing countries should be a precondition for movement on North/South propositions. While such a condition is unacceptable the fact is that there must be a clear connection. The search for global equity must be a part and a vital part at that, of the concern for the improvement in the condition of the individual human being. These movements, toward equity and social and economic justice within countries, represent two of the major forces which will affect all countries in the years ahead. Together they represent a formidable combination which could affect Latin America and the Caribbean deeply.

The issue of basic needs came to prominence in the context of the North/South discussions. It has been the subject of suspicion as to the motives of some of those in the North who pressed the idea. In fact there has been more than an element of oversimplification in the presentation of this issue by some. A proposition which clearly has its merits, seems to have been regarded by these persons as a total development thesis - rather than a very important element in a much more complex political, social and economic effort.

The view of the World Bank is that the issue of growth versus basic needs must be carefully analysed and that good performance in meeting basic needs does not cause lower growth rates. The Bank has stated that "total attention to increasing the rate of growth of GNP without explicit attention to the problem of absolute poverty and basic needs would cause important opportunities for making immediate benefits available to the poor to be missed. In addition, adherence to the idea of growth now, alleviation of poverty later "could cause the development of an entrenched middle-class favoured by government services, and make reallocation of resources at a later date just that much more difficult"... "the more pressing needs of ... societies", the Bank states "can be met at low levels of national income".

But the question that arises is this. Can you change the distribution of income and opportunity and of power in a community in a fundamental way through a programme which concentrates on meeting basic needs? Whatever good may be achieved through such an approach, may it not leave much of the basic social and economic structure virtually intact?

Here it should be noted that there are those in industrialized countries who are quite willing to assist in improving conditions in developing countries but who have shown no inclination to address the structural factors which are at the root of the imbalances and inequities in the relations between North and South. And as we call on the industrialized countries to exercise the political will to face and to deal with these factors, we have to ask whether developing countries will summon the political will to carry out the structural and other changes required in their communities in the interests of social justice.

## SOCIAL INDICATORS AND DEVELOPMENT PLANNING \*/

Christian Leipert and  
Udo Ernst Simonis \*\*/

### 1. Social indicators - what for?

There is no generally recognized definition of social indicators. However, there is a large measure of agreement, in the planning literature and in the practical work of national and international organizations, that social indicators should record the results of socio-economic, social and political processes which fall outside the areas normally covered by economic indicators (Leipert 1978: 91 et seq.; Peters and Zeugin 1979; 45 et seq.). Moreover, these results are required to provide also information on aspects of social and/or individual welfare (quality of life, conditions of life, level of living) which are not recorded by traditional economic reporting (national accounts, management accounting). Demarcation from economic reporting - a characteristic feature of many attempts to define social indicators - points at the same time to the conditions of scientific and social origin behind the demand for the development of social indicators and their use in practice. Furthermore, the increasing awareness, at the end of the '60s, of unfavourable concomitants of rapid economic growth in the industrial countries also resulted in criticism of the established method of measuring growth (= welfare). In the economic policy of the industrial countries a high rate of growth of the gross national product (i.e. all of the goods and services produced within an economy over a period, which are used for purposes of consumption, investment and export, valued at market

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prices) had become the predominant objective-variable and parameter of success (on its measurement, cf. Brümmerhoff 1975). The planners and decision-makers of economic policy associated or identified a high growth-rate of the gross national product (GNP) in real terms, explicitly or implicitly, with a high growth-rate of social and individual welfare. It was precisely this equation of economic growth with increased welfare that caused the criticism of the measurement of economic growth and the demand for liberation of welfare-measurement from the confines of the economic reference-frame, by means of social indicators.

Criticism was expressed at two levels. Sociologists pointed, with a view to criticism of ideology, to the "economistic reduction of the welfare-concept", as they called, in the current use of economic variables (GNP, in particular) as welfare indicators. In their view, the prerequisites for measuring welfare by means of economic variables no longer existed. Clear signs of this were the adverse effects which accompanied economic growth, in relation to the social and physical environment, these are not recorded in economic reporting or are only falsified as favourable effects. In the view of this line of criticism, for more comprehensive and less biased measurement of welfare it was necessary to construct a system of welfare (or social) reporting, with which the quality of life and its trends could be revealed, beyond the narrower economic sphere.

The second line of criticism worked out mainly the actual inadequacies of the GNP as the predominant measure of welfare. This debate took place largely within economic science, with some of those taking part advocating improvement of the GNP-concept, in the sense of making it more adaptable as a welfare indicator. In the course of this debate, Sametz (1968), Nordhaus/Tobin (1972) and the Japanese NNW study group (Economic Council of Japan 1973) submitted calculations of a revised, welfare-oriented national-product-variable (net national welfare index), in which "negative" welfare items (such as environmental maintenance costs, environmental pollution, losses due to urbanization) were deducted from the conventional GNP, and "positive" welfare items (such as monetary equivalents of leisure and non-market activities) were added (Simonis 1980). The potential of this revised approach for development planning is not yet fully known, one reason being the high degree of consensus that is necessary for extension of the monetary approach to non-market spheres of human behaviour (cf. more detail on this in: Leipert 1975: 160 et. seq.). Yet, even economists and planners who tend to be sceptical about the possibilities of an agreement on new conventions for more extensive monetary welfare-measurement, advocate adding to traditional economic reporting social indicators which can express the non-economic aspects of the quality of life more clearly and more directly than seems to be possible with non-market phenomena expressed in monetary terms.

## 2. Reasons for the use of social indicators in development planning

The criticism of economic growth that started at the end of the '60s and beginning of the '70s was not confined to the industrial countries. At the same time as the welfare effects of economic growth were being questioned in the industrial countries, a debate arose in the developing countries, in the international institutions and in economic science, on the success or failure of growth policy in the developing countries and on the suitability of GNP as the most important indicator of development.

In an atmosphere of euphoria over modernization, development planning in many countries of the Third World was based upon the development theories borrowed from Western countries and upon the strategies of growth-maximization that derived from them. Development assistance, too, was based upon the "trickle-down" postulate of the theory of economic growth. This was the notion that the maximization of GNP in a developing country would set in motion a chain of structural changes which, in turn, would ensure that the 'fruits of growth' are passed on to the mass of the population. This "trickle-down" postulate is rooted in neo-classical growth theory and abstracted in the Harrod-Domar model which formed the theoretical basis of most development plans in the '50s and '60s. The Harrod-Domar model in simplified form is based upon the assumption that growth depends upon the accumulation of capital - and, in expanded form, upon the availability of foreign exchange and the domestic capacity to save (saving-accumulation). Development assistance as financial aid and the role of industrialization as a motive force for growth are rooted in these assumptions.

On average, the developing countries have achieved high rates of growth of GNP; yet the 'fruits of growth' have not reached the mass of the population - on the contrary; the gap between the "haves" and the "have-nots", between the urban elites and the rural poor, the educated and the illiterate, the employed and the unemployed has widened. Three decades of statistically measured economic growth have in many cases not led to "development", and this may be proved by a few facts: about 1,000 million people in the world are undernourished in the sense of suffering from extensive deficiencies of calories and protein; 1,000 million people are inadequately housed; 1,000 million are illiterate; 1,300 million people earn less than the equivalent of 90 dollars a year and thus form the hard core of poverty; 1,500 million people have no access to medical care, 1,700 million no access to clean drinking water, and for about 1,700 million people life expectancy is less than 60 years (McHale and McHale 1979).

Thus, the expected results from policy programmed for a high rate of economic growth (GNP) did not materialize. Whereas in the industrial countries, in particular, disillusionment set in connection with increasing environmental pollution resulting from high growth-rates and

the structure of production and consumption, in the developing countries the main reason was the experience of deteriorating patterns of distribution in the course of growth - or, in concrete terms, inadequate conversion of the results of economic growth in reducing absolute poverty and satisfying basic human needs.

## 2.1. The unsatisfactory results of growth-oriented development planning

Development planning and development policy stamped with Western growth-theory ideas were directed mainly towards promotion of the so-called modern (formal) sector of the economy (cg. Addicks/Bünning 1979: 12 et seq.). A process of self-sustaining growth was to be set in motion in the modern sector by means of a high rate of investment; it is being assumed that the transmission of the growth-stimuli to the traditional (informal) sector, largely being unintegrated in the money-based economy, would bring about improvement of the conditions of development there also.

However, in most developing countries the upswing in the economy that was produced in the so-called modern (formal) sector resulted in accentuation of the overall disparities in the conditions of life. On the one hand, only relatively few people profited from the expansion of the mostly capital-intensive market production and market income. On the other hand, for parts of the population in the traditional sector the conditions of life deteriorated owing to adverse repercussions of expansion of the modernized, monetary sector of the economy. The migratory movement of 'downgraded' parts of the rural population into the 'cancerously' expanding conurbations, or the increasing use of agricultural land for export-oriented production accompanied by neglect of domestic supplies, are examples of adverse effects of a growth policy which was one-sided, disregarding the social consequences.

When it was observed that the economic and social inequalities of a growth policy directed primarily towards capital accumulation in the modern sector were becoming more pronounced, problems arose regarding both the development policy and planning practised hitherto and also the current measurement of development by means of indicators of the traditional national accounts; the economic orientation of the development concept fell into the crossfire of criticism (on this, Tévoédjré 1980 is excellent).

The adoption of Western production and consumption models, the application of capital-intensive techniques and the influence of Western institutions were interpreted as expropriation of autochthonous skills and cultural values. The debate then began as to what should be understood by development and by the main objectives of development in the developing countries; sociological, psychological theories and theories of comparative cultural anthropology gained in significance. A characteristic feature here was a recall of own cultural traditions, which had been devalued, as barriers to development, in the course of modernization.

## 2.2. The move towards basic needs-oriented development planning

In the debate on development policy, this new sensitivity to the inadequacies of a "transplanted" growth policy and to the desirability of preserving cultural traditions led to a new paradigm of development. As an alternative to traditional growth-oriented development strategy and the trickle-down paradigm, since the beginning of the '70s development planning has been directed increasingly towards "basic needs" and "redistribution with growth". The new concept is focussed upon the situation with which traditional, growth-oriented policy was unable to deal, namely inadequate satisfaction of basic needs for large parts of the population. Under this new conception, the elimination of the inadequacies in the satisfaction of basic needs is to be the principal task of development planning and the main criterion in the selection of development projects and programmes.

A basic-needs policy, of course, is not incompatible with growth per se; the two concepts are established at different levels or are directed towards different priorities. Traditional economic growth policy has social consequences which are reflected in, among other things, the (low) level of satisfaction of basic needs. The basic needs-oriented policy has economic consequences (and preconditions) which can be measured by, amongst other means, the absolute level, the formative structure and (above all) the distribution of real economic growth. Basic needs-orientation therefore means at least that the priorities of economic activity are set differently and that attention is devoted primarily to the distribution of produced goods and services. A growth of economic production could be aimed at, the pattern and distribution of which bring about the maximum effect in reducing poverty and satisfying basic human needs. It is, in this sense, an attempt to synthesize the growth-objective with the objectives of redistribution and the creation of jobs through the production of goods and services for the satisfaction of basic needs.

A prerequisite for the realization of this kind of new development pattern is institutional change (e.g. the redistribution of arable land). Political and/or economic power-structures often stand in the way of a more even distribution of goods and services and a pattern of production directed towards basic needs. It would therefore be naive to deal with a concept of basic needs-orientation to the exclusion of the dominant power structure and special-interest situations in a given developing country. It is precisely this disregard of the political and institutional factors that is characteristic of the traditional growth-oriented approaches of development planning; although this may be more understandable there, because the growth-oriented concepts are usually based upon the existing power structures.

The basic needs-strategy adopted by the World Employment Conference of 1976 and confirmed by the UN General Assembly, includes the notion that satisfaction of the basic needs of the population must be the primary objective of development planning and of any actual development plan

(Article 1). According to the definition adopted by the World Employment Conference, basic needs embrace: the regular minimum requirement of food, housing and clothing for the individual and his family, and also vital public services, especially drinking water, sanitary installations, public transport and health and educational facilities (Article 2).

Development planning which is concerned with the fulfilment of these basic requirements cannot determine at all or can determine only inadequately, by means of the available traditional economic reporting, the situation within the different areas of basic needs and also the success of development projects and programmes for selective covering of basic needs. It requires additional, different data, an information system which measures directly the social consequences of economic growth in general and of development planning in particular. This means that a system of social indicators is required, with the aid of which the actual situation, the desired situation, the deficiency of supply in each particular case and the success of special measures in the various areas of basic needs can be determined and evaluated (Addicks 1977: 297 et seq.; Morris 1979; Lisk 1979: 241 et seq.).

In Table 1, for a number of selected countries, some social indicators related to basic needs are presented, the values of which were collected by the World Bank. In accordance with the basic needs-concept, the indicators have to be able to provide information particularly on the distribution-situation in the respective areas. The policy of basic needs-orientation therefore has a basic egalitarian feature in that it is essentially a question of fulfilment of the minimum welfare standard for all in the different areas. From the egalitarian standpoint, there is improvement in the welfare situation only if representative social indicators indicate an increase in the proportion of the population that has this minimum of provision. This is the case for Nos. 4, 6 and 7 of the social indicators shown in Table 1. Below, we shall discuss in more detail the distribution aspect and other aspects of an appropriate system of social indicators for developing countries, with several examples.

### 3. A social indicator system of welfare measurement for developing countries - the Drewnowski model

The Drewnowski system-model (1974) was evolved at the United Nations Research Institute for Social Development (UNRISD), which provided important stimuli for constructing the methodological and empirical basis of development measurement. It aims at quantification of those social and economic goals striven after by development planning oriented directly towards improvement of the level of living of all members of society (Drewnowski 1974).

The system of indicators is only one - although very important - part of a comprehensive methodological, statistical concept of socially-oriented development planning. The variables of the indicator-system work within the



scope of the intended new paradigm as arguments of an extended objective-  
function of development planning. Effects of economic growth upon the many different components of welfare (particularly also from distribution aspects) are thus revealed and become controllable by means of statistical measures.

Drewnowski evolved, for the purpose of political evaluation of the new measuring tools, an interdependence table which is modelled on the Leontief-type input-output table (p.106 et seq.). This is intended to represent, in model-form, the interrelationships between the economic production and consumption variables, which are measured by means of the economic indicators (such as gross and net national product, consumption, investment), and the components of the quality of life, measured by means of the social indicators. For overall valuation of success in converting output into welfare-relevant results, the concept "welfare effect" is evolved, while for overall valuation of the influences (feedback effects) of the welfare components upon the conditions of production, the concept "productivity effect" is evolved. The possibility of constructing a "welfare generation function" (effects of production upon welfare) and a "social production function" (effects of the welfare situation upon production) is mentioned.

Using the interdependence tables as his basis, Drewnowski - for simplicity reasons - evolved a linear model of social development planning. It differs basically in two characteristics from purely economic planning models. On the one hand, social variables which represent welfare objectives directly are integral constituents of the objective function; on the other, explicit account is taken of the interdependence between economic and social variables (p.130 et seq.).

The aspects of the quality of life that are to be incorporated in the system of indicators should be observable and relevant to the whole society, and quantifiable and interpretable as indices of improvement or deterioration of the conditions of life. They are, on the one hand, flow variables and, on the other, stock variables. Flow variables are combined in an index of the level of living (= of the flow of welfare) and stock variables in an index of the state of welfare. (In what follows, we concentrate upon the proposals for quantification of the level of living). The level of living is accordingly synonymous with the degree of satisfaction of needs which results from consumption of the goods and services produced within the actual period and other non-produced conditions of life. The state of welfare reflects, at a particular point in time, specific characteristics of the population which has experienced the effective flow of welfare for a substantial time.

The quantification of the level-of-living index conforms to an activity-concept. Starting-points are the production processes by means of which the respective needs are to be satisfied. Admittedly, only those areas are incorporated in which the political system obviously influences the conditions of life quite directly. The indicators reflect primarily the individuals' disposal over resources which they use and consume, not necessarily the direct satisfaction of individual needs.

The selected nine components of the indicator system can be assigned to three groups. In the first, those categories of basic needs are combined which in the general view should not be absent from any conceptualization and measurement of the level of living: (1) nutrition, (2) clothing, (3) shelter, (4) health, (5) education. The second group contains two components, namely (6) leisure and (7) security. Underlying them is the need for protection and safety which is expected to be guaranteed by society: protection against intensity and duration of work that are excessive (harmful to health) and against the social hazards to which the population is potentially exposed. The third group relates to the environment in which the members of society live. It consists of two components, namely (8) social environment (incl. recreation) and (9) physical environment. On the basis of the conviction that satisfactory relations with other members of society are a basic human need, in component (8) the question is asked as to how far the population is satisfied with its life in society and with its social communication. The subject of component (9), on the other hand, is how far the population is satisfied with the natural environment in which it lives. These nine components of the indicator system are made operational by means of 27 indicators (cf. Drewnowski, Synopsis 1).

For overall valuation of the trend of the level of living, aggregation of the different indicators into an overall index is thought to be necessary. For this, the results in the different components of the indicator system are valued and weighted on the basis of a framework of "critical points"; the latter refer to characteristic threshold values of the satisfaction of needs. Scientifically-founded, objective threshold values - e.g. in the sense of minimum requirements for a life fit for human beings - are fixed for few areas only (the area of nutrition is probably the best example here). In the other areas, they must be supplemented by socially justified norms based upon the views on "minimum standards", "adequate standards" and "affluent standards" of satisfaction of needs which prevail in society (or at least are predominant). In view of the fact that the relative weight of a component varies for the individual and the whole society with increasing satisfaction of respective needs, Drewnowski decides in favour of a sliding weighting-scale.

#### 4. A physical quality-of-life index for developing countries - the Morris model

Morris et. al. make an approach to development planning which is less ambitious than Drewnowski's, but nevertheless interesting, with the physical quality of life index (PQLI). They find that GNP is still the most commonly used measure of "development", but criticize its structural weakness and conclude that in so far as development planners in developing countries and donor countries base their work more upon the distribution effects of projects and on the fulfilment of basic needs, they need not only new strategies, but also additional measuring systems (Morris 1979: p.95).

A measure of development which, in particular, allows international comparisons must satisfy a variety of criteria: it should not only allow one development-path to be taken and should avoid ethnocentrism (i.e. standards which reflect the values of particular societies or social groups); it should measure results, not inputs, and be able to indicate their level and distribution; it should be easy to construct and understand (in the sense of Johan Galtung's statement: "An indicator which anyone with five years of schooling cannot understand within five minutes is not an indicator, but an instrument of control"). Morris et al. consider these criteria to be fulfilled for three social criteria: "life expectancy", "infant mortality", "reading and writing ability", which make them useful indicators for measuring physical well-being and for measuring success in relation to identifiable goals. The position with regard to the data basis for these indicators must be considered to be more or less satisfactory; they are not ethnocentric, they are objectively measurable and internationally comparable.

The average "life expectancy" at the age of one and "infant mortality" can be considered good indicators of important aspects of development; they express, so to say, the sum of the effects of nutrition, health, income and environment. The reading and writing ability of poor groups of the population ("literacy rate") indicates in a way the extent to which they participate or can participate in the economic and social development process.

The PQLI-model, however, follows the fascination GNP as a unique measure has, by the formation of a composite index (overall index). For each of the three individual indicators mentioned, the respective degrees of fulfilment of the countries (regions, tribes, social groups) that are to be compared are first plotted on a scale from 0 to 100, in which "0" is the lowest and "100" the highest degree of fulfilment. An overall index is then obtained on this basis, consisting of the simple arithmetic mean of the three (equally weighted) indicators. This procedure makes it possible to carry out international (national, regional) comparative surveys (cross-sectional comparison).

In Table 2 a cross-sectional comparison of this kind is presented for a number of selected countries, and they are also related to or contrasted with the traditional GNP-indicator. (The methodological problems involved in the production of a time-series comparison of the three individual indicators and of the overall indicator are more complex and require more space than is available here. They will therefore not be described here; the reader should refer to the relevant literature).

The PQLI, based upon three different social indicators, which in turn provide important information on social processes, is the sum of complex relationships for which no theoretical explanation provides clear-cut weightings; its components are therefore given the same weight in each particular case. Owing to the fixing of a lower and an upper limit, the PQLI measures only the position within a certain range, in contrast to the GNP-index, which is open-ended at the top. Generally speaking, this index can provide an important guide for development planning, as to when and

the extend to which achieving a high index-value conforms to a consensus-agreed development-objective not only nationally (regionally) but also internationally.

In contrast to the GNP-indicator, the PQLI-approach also makes it possible to close the existing "gaps" (international, national, regional) - which means that it allows objectives to be defined which are in fact achievable. It does not convey the picture of a "hopeless race" - even though a few generations will probably pass before this development index is rendered unnecessary.

The PQLI-index is interesting also in the sense of the question as to whether and in what way it correlates with GNP. The studies on this question have shown that GNP per capita does not explain the degree of fulfilment of the PQL-index well - an indirect pointer to the potential significance of this planning method for development policy. (Morris paraphrases this conclusion in one sentence: "Money is not everything"). This significance can lie also in further diversification of the model: its use with regard to other intranational aspects, such as income-groups, ethnic groups, other social groups, town/country-sectors, etc.

#### 5. Growth and distribution index

As has already been shown, it is possible to use for purposes of development planning an index which reflects several goals at the same time. A development index which combines the growth objective and the distribution objective (or an economic indicator and a social indicator) is contained in a joint study by the Institute of Development Studies in Sussex, England, and the Development Research Center of the World Bank (Chenery et al. 1974).

If we take as starting-point the following simple welfare function of a society:

$$G = W_1 G_1 + W_2 G_2 + W_3 G_3 + W_4 G_4 + W_5 G_5$$

in which G is the index of the increase in total welfare,  $W_1$  the weight of group 1 and  $G_1$  the rate of increase in income of a particular group over a particular period of time (year), the GNP is the case of an index in which (in this example) the weight for the increase in income of each group, e.g. one-fifth of the population, is assumed to be simply the portion of the total income (GNP) in each particular case that this one-fifth represents. If, in contrast to this assumption, we consider the actual pattern of distribution of GNP in the developing countries as a whole, the problems of the GNP-approach for development planning become obvious:

One-fifth	1	2	3	4	5	Total
Share of national income (in %)	53	22	13	7	5	100

According to these figures, the share of the national income in the developing countries that is allocated to and represented by the upper two-fifths of the population is approximately 75%.

Thus, in this respect the growth rate of GNP is essentially a measure only of the increase in income of the upper two-fifths of the population, while the remaining 60 per cent of the population (the majority) is accordingly hardly of any significance. The problems of the, historically speaking, most important development indicator GNP, thus again become clear - in another way.

An alternative "measure of welfare" might be to distribute the weights  $W$  in the above function equation proportionally, for example (in this sense conforming to the democratic principle of "one man - one vote"), i.e. equal weight for each one-fifth of the population. On the basis of economic reality (ratio between the upper fifth and the lower fifth on the income scale 53:5 or approx. 11:1), in the case of such an equal-weights-index (EWI) an increase in income in the lower fifth would in fact be given eleven times more importance than an increase in income in the upper fifth of the population.

If we replace the relatively abstract one-fifths of national income with actual social groups - e.g. small farmers, the urban poor, etc. - then the great potential for development policy of this proposed methodological approach of combining growth objectives with distribution objectives becomes even more obvious.

If, in view of the disastrous distribution situation in most developing countries, the planners (the government, the donor country, the international institution, etc.) were of the opinion that the task of planning primarily should be one of increasing the income of the above mentioned social groups (or that of the lower 40% of income-recipients, for example), then the measures and programmes of economic and social policy would have to be formulated accordingly - i.e. a low weight or no weight at all would have to be given on the further income-increase of the upper economic and social groups (regions countries), for example. The practical importance of such a "poverty-weights-index" (PWI) could thus be considerable.

Weighted indices of this type (or of a similar type) offer, in our view, a wide range of possibilities of systematic analysis and planning of development processes which conform far more closely to the actual conditions and needs of the development countries than does the (inadequate) theoretical framework which has hitherto mostly formed the basis of planning in the developing countries and of international development assistance. (The reader might also just ponder the possible significance of such a diversified approach for development policy in the industrial countries.).

## 6. Theoretical models and reality of development policy - a look to the future

For the ex post analysis of development and the ex ante planning of the future development of a country (a region, etc.), it is necessary to re-define the concept of development. In the '50s, '60s and '70s it was, and today it still is, widespread practice to equate "development" with "economic growth", expressed as the increase in the gross national product (GNP) or increase in income per capita. The experience of seeing no alleviation from the many serious problems in the developing countries despite the growth of GNP, in some cases resulted in gradual questioning of the validity of this key "development"-indicator and in increasing scepticism as to the favourable effects of the traditional growth policy based on it.

A social indicator-movement arose which attained some momentum, being fed intellectually from individuals, university and research institutions. In association with this, the typology of developing countries was refined and development strategies were theoretically diversified; the debate concerning target group-oriented development assistance began, while in the North-South dialogue the debate on the "New International Economic Order" started.

Nevertheless, it was and is most certainly too early to start talking already about a U-turn in practical development planning in the sense of our topic. Despite all the fundamental criticism, the traditional economic indicators - particularly the GNP-index - continue to predominate in most national and regional development plans, and also in international development assistance which is based primarily upon economic indicators in regard to recipients, projects and programmes. The social indicator movement has formulated new questions and has revealed many weaknesses of traditional planning; but in the actual development planning of most developing countries and international planning institutions, social indicators have at best assumed a supplementary, not dominant, function. To inquire into the causes of this means pointing out not only deficiencies of research, but also serious problems of method associated with the development and use of social indicators. Our examples have demonstrated some of these problems; nevertheless, the possible practical importance of these (and similar) approaches to the reform of development planning seems to us to be no means played out.

For reasons of substance as well as of method, and for reasons of necessary co-operation between the scientific disciplines and integration of technical planning, we consider the debate on our topic - social indicators in development planning - still to be important. The decision as to what development is or should be has not been made once and for all. This decision is still under discussion, repeatedly.

## NOTE

\* Modified version of an article published in D. Nohlen, F. Nuscheler (Eds.): Handbuch der Dritten Welt (Handbook on the Third World), vol. 1, 2nd ed., Hamburg: Hoffmann & Campe, 1982.

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Table 1

SOCIAL INDICATORS FOR LIFE EXPECTANCY, HEALTH AND  
EDUCATION, SELECTED COUNTRIES

	Ethiopia	Bangladesh	Malaysia	Mexico	Zambia	Sri Lanka	Tunisia	Germany, Fed. Rep.
1. Life expectancy at birth (years) (1978)	30	47	67	65	48	69	57	72
2. Infant mortality rate (at age 0-1) (1978) <sup>1</sup>	126	139	31	60	...	63	123	15
3. Population per physician (1977)	76,320	9,260	4,350	1,820	10 190	6,270	4 800	490
4. Percentage of the population with access to safe water (1975)	6	53	62	62	42	20	70	...
5. Daily calorie supply per capita as percentage of requirement (1977)	75	78	117	114	87	96	112	127
6. Adult literacy rate (percent) (1975) <sup>4</sup>	10	26	60	76	39	78	55	99
7. Number enrolled in primary school as percentage of age group (1977) <sup>2</sup>	26	81	93	116	95	86	100	90
8. Number enrolled in secondary school as percentage of age group (1977) <sup>3</sup>	8	23	43	39	16	47	22	84

<sup>1</sup> The infant mortality rate is the number of infants who die before reaching 1 year of age, per thousand live births in a given year.

<sup>2</sup> An age-range of 6 to 11 years generally in considered as primary-school age.

<sup>3</sup> An age-range from 12 to 17 years is generally assumed.

<sup>4</sup> The adult literacy rate is the percentage of the total population represented by persons aged 15 and more who can read and write.  
<sup>5</sup> 1960.

Source: World Bank, World Development Report 1980, Washington, D.C. 1980, p. 150 et seq.

Table 2  
ECONOMIC AND SOCIAL INDICATORS FOR SELECTED COUNTRIES  
(BEGINNING OF THE '70)

	GNP per capita 1974 (in \$)	PQLI (index)	Life ex- pectancy at birth (years)	Infant mortality (per 1000 births)	Literacy rate (in %)
Afghanistan	110	19	40	182	8
Pakistan	130	37	50	124	16
Sri Lanka	130	83	68	45	81
India	140	41	50	139	34
Kerala State	c 125	68	61	58	60
Tanzania	160	28	44	162	15-20
Kenya	200	40	50	119	20-25
Central African Rep.	210	18	41	190	5-10
Bolivia	280	45	47	108	40
Nigeria	290	25	41	180	25
Ghana	430	31	44	156	25
Korea, Rep. of	480	80	61	47	88
Cuba	640	86	70	29	78
Algeria	710	42	53	126	26
Taiwan	810	88	69	26	85
Mexico	1,090	75	63	61	74
Iran	1,250	38	51	139	23
Gabon	1,960	21	41	178	12
Ireland	2,320	96	72	17	98
Libya	4,640	42	53	130	27
Netherlands	5,250	99	74	11	98
United States	6,670	96	71	17	99
Qatar	8,560	32	47	138	10-15
United Arab Emirates	11,710	34	47	138	20

Source: Sewell et. al. 1977.

Synopsis 1

LEVEL OF LIVING INDEX: COMPUTATION TABLE

Critical points of indicators		"O"		"100" "M"		"A"	
Designation of Sub-ranges of cardinal indicators expressing respective levels of need satisfaction		Intolerable	Inadequate			Adequate	Affluent
Corresponding grades of ordinal indicators		IV	III	II		I	
Intermediate indicator index values for cardinal indicators		0	0	0 < I' < 100	100	100 < I' < I' A	I' A
Intermediate conventional index values for ordinal indicators		0	0	50	100	150	200
Components	Indicators	Units of Measurement		Determination of cardinal indicators sub-ranges and ordinal indicator grades			
1. Nutrition (food intake)	a) Calories intake	Calories intake per day per head as percentage of norm	Below 60 % of norm	60 % and more but less than 100 % of norm	100 % and more but less than 133 % of norm	133 % and more	
	b) Protein intake	Protein intake per day per head as percentage of norm	Below 60 % of norm	60 % and more but less than 100 % of norm	100 % and more but less than 200 % of norm	200 % and more	
	c) Percent of non-starchy calories	Percent of non-starchy calories in food intake	Less than 10 %	10 % and more but less than 40 %	40 % and more but less than 60 %	60 % and more	

# Synopsis 1 (continued)

2. Clothing (use of clothes)	a) Cloth consumption	Cloth used for clothing sold to consumers and twined into ready- to-wear garments per year per head	none	Less than 15 m <sup>2</sup>	15 m <sup>2</sup> and more but less than 50 m <sup>2</sup>	50 m <sup>2</sup> and more
	b) Footwear consumption	Footwear pairs sold to consumers per year per head	none	Less than 3 pairs	3 pairs and more but less than 6 pairs	6 pairs and more
	c) Quality of clothing	Ord. ind.	Most primitive	Poor	Satisfactory	Sumptuous
3. Shelter (occupancy of dwellings)	a) Services of dwellings	Ord. ind.	No permanent dwelling	Rustic or unfit for habitation	Conventional fit for habitation	Conventional with all amenities
	b) Density of occupancy	Rooms per inhabitant	Less than 1/4	1/4 and more but less than one	1 and more but less than 1/2	1 1/2 and more
	c) Independent use of dwellings	Housing units per household	Housing unit unidentifiable or less than 1/2 housing unit per household	Less than one but more than 1/2 housing unit per household	One housing unit per household	More than one housing unit per household
4. Health (health services received)	a) Access to medical care	Ord. ind.	No access whatsoever	Access limited	Access adequate	All needs for medical care fully satisfied
	b) Prevention of infection and parasitic disease	Percentage of deaths not due to infection or parasitic disease	Below 66 %	66 % and more but less than 96 %	96 % and more but less than 99 %	99 % and more
	c) Proportional mortality ratio	Percentage of deaths which occur at the age of 50 years and over to the total number of deaths	0 %	Less than 80 %	80 % and more, but less than 90 %	90 % and over

# Synopsis 1 (continued)

Components	Indicators	Units of Measurement	Determination of cardinal indicators sub-ranges and ordinal indicator grades			
5. Education (education received)	a) School enrolment ratio	Enrolment as percentage of norm	No enrolment	Less than 100 %	100 % or more but less than 150 %	150 % and more
	b) School output ratio	Not dropped out as percentage of enrolled	All dropped out	Less than 90 %	90 % and more but less than 100 %	100 %
	c) Teacher/pupil ratio	Teacher/pupil ratio as percentage of norm	Tuition not received	Teacher/pupil ratio below 100 % of norm	Teacher/pupil ratio at or above 100 % of norm but below 200 % of norm	Teacher/pupil ratio at or above 200 % of norm
6. Leisure (protection from overwork)	a) Leisure time	Hours free from work per year	Less than 3640 hours free from work per year (Badly overworked)	3640 hrs and more but less than 6336 hrs free from work per year (Overworked)	6336 hrs. or more but less than 6816 hrs. free from work per year (Not overworked)	6816 hrs. or more free from work per year (Comfortable)
7. Security (security assured)	a) Security of the person	Ord. ind.	Law and order broken down (war, civil war, regime of terror)	Law and order badly maintained (riots, gangsterism, hooliganism)	Law and order adequately maintained	Law and order well maintained
	b) Security of the way of life	Ord. ind.	Economic chaos	No employment or sickness insurance, no pension schemes, not sufficient savings	Unemployment and sickness insurance, pension schemes and/or savings sufficient to maintain a minimum level of living	Complete coverage by insurance or pension schemes and/or savings sufficient to maintain the present way of life

# Synopsis 1 (continued)

8. Social environment (social contacts and recreation)	a) Labour relations	Ord. in.	Riots, Repeated strikes and lockouts	Tension in labour relations	Labour relations satisfactory	Labour relations good
	b) Conditions for social and economic activity	Ord. in.	Political oppression rampant	Difficult conditions for social and political activity	Satisfactory conditions for social and political activity	Good conditions for social and political activity
	c) Information and Communication	Ord. in.	Isolation within a village community	Information and communication restricted	Information and communication satisfactory	Information and communication ample
	d) Recreation: cultural activities (music, theatre, cinema, visual arts, book reading)	Ord. in.	Lack of cultural activities	Rudiments of cultural activities	Cultural activities adequately developed	Cultural activities well-developed
	e) Recreation: travel	Ord. ind.	Immobility	Travel occasional with a limited perimeter	Participation popular	Participation enthusiastic and active
	f) Recreation: sport and physical exercise	Ord. ind.	No participation whatsoever	Occasional participation	Frequent travel by various means mostly within the home country	Frequent travel of distinct educational and cultural value within the home country and abroad
9. Physical environment	a) Cleaness and quietness	Ord. ind.	Conditions unbearable	Conditions unsatisfactory	Conditions satisfactory	Conditions good
	b) Public amenities in the neighbourhood	Ord. ind.	No amenities	Amenities inadequate	Amenities adequate	Amenities good
	c) Beauty of the environment	Ord. ind.	Depressing ugliness	Mediocre	Acceptable	Inspiring

RAGNAR FRISCH: ECONOMETRICS AND THE  
POLITICAL ECONOMY OF PLANNING

Frank Long \*/

ABSTRACT. Ragnar Frisch's main contributions are in the field of econometrics. This paper discusses Frisch's contribution to the political economy of planning. It argues that although planning was not a special feature of classical political economy, Frisch nonetheless shared in the broader social and moral aspirations of political economy; for Frisch, these were the ultimate objectives of planning. To this end the paper discusses Frisch's approach to the formalization of society's preferences. This approach involves an interactive mechanism in which politicians and technical experts participate. Against the political economy aspirations of Frisch, some behavioral shortcomings of his framework are briefly discussed.

I. INTRODUCTION

Ragnar Frisch is invariably associated with his contribution to econometrics. He was one of the founding fathers of the Econometric Society, and was awarded the Nobel Prize in Economics for his contribution to quantitative work in economic science. Frisch's major works in econometrics date back to the early part of this century. Both Frisch and Jan Tinbergen helped to set the initial foundations for what is now called Econometrics (1). Without Frisch's pioneering contributions, however, it seems unlikely that quantitative economics would have been as firmly established as it is currently.

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A somewhat obscure aspect of Frisch's work constitutes what may be called "the political economy of planning". This contribution by Frisch to political economy arises mainly from a conscious and systematic attempt on his part at formalizing societal preferences. The means to this are a combination of technocratic and political considerations. Both of these considerations constitute an essential feature of Frisch's planning methodology. In this brief exposition, our aim is two-fold. First, we make note of Frisch's approach to the formalization of societal preferences; and in particular the incorporation of the political system to this end. Second, we attempt to show the relevance of Frisch's ideas to political economy while at the same time drawing attention to some behavioral limitations which inhere his framework.

## II. WELFARE ECONOMICS: A NOTE

The question of social preferences has, for some time now, been a special feature of welfare economics. It is therefore worthwhile to deal briefly with some points relating to this.

It is commonly accepted in the tradition of welfare economics that the welfare of the community is dependent on the welfare of the individuals comprising it. Under certain assumptions, such as a given distribution of income, rationality, non-satiation, transitivity, continuity of indifference curves, non-inter-dependence of individual utilities, etc., it is possible to arrive at a welfare preference function of society at large. Such a function can be written as follows:

$$1) \quad \sum U = U(X_1 \dots\dots X_n)$$

where symbols  $\sum U$  = national welfare and  $U(X_1 \dots\dots X_n)$  = measurable welfare of the entire population.

This type of social welfare function was first expounded by Bergson in 1938 (2). It was later explored more formally by Arrow, Samuelson and others. Essentially, Bergson's welfare function was not designed to rank all combinations of individual welfares, but the combinations of particular goods consumed and services rendered by each of the individuals in the society (3).

Arrow, in taking up a mathematical treatment of the above, concluded that, in general, a rule for passing from individual orderings to social orderings cannot be found in a free market type economy (4). Hence his Impossibility Theorem. Consequently these two orderings can only take place if there is an imposed social welfare function. The question Arrow asked was the following: suppose there are  $x$  distinct social states attainable, and suppose that there are  $n$  different ways of ordering these social states, the real question to be answered is, regardless of these



different ways chosen by each of the individuals, will it be possible as a result of rules ethically acceptable to a free society to construct a corresponding social ordering of  $x$  social states?

Apart from the Bergson tradition, most of the post-1939 attention in welfare economics represents different formulations of the Pareto optimal condition. This condition is defined as one from which it is not possible by any reallocation of factors to make anyone better off without making at least one person worse off (5). Meanwhile, A. C. Pigou's "The Economics of Welfare", is invariably associated with the controversies of the 1930s over interpersonal comparison of utilities. But as Mishan argues, Pigou's main contribution is to be found in the emphasis of the vital distinction between social and private valuations of economic activities (6). This still features in contemporary analysis of welfare economics with reference to "external effects", or "external economies or diseconomies of production and consumption", for instance.

### III. RAGNAR FRISCH AND THE FORMALIZATION OF SOCIETAL PREFERENCES

Frisch, in a sense, represents a slightly different tradition to the Bergson-type social welfare function. Viewed from Arrow's position, his approach to the formalization problem represents an imposition. Arrow felt such an imposition was a contravention to free market type principles of decision making. However, Frisch was not concerned with the Bergson type welfare function. His formalized preference function is something quite different. Essentially, such a function can be described with reference to a given time period as follows:

$$2) \quad S_p = f(P_v, T_o)$$

Where  $S_p$  represents a vector whose constituent elements are political preferences  $(P_v)$  and technocratic choices subject to political parameters  $(T_o)$ .

$P_v$ , essentially, is determined by a decision making machinery which is the political party in power. It is not removed from "social claims" of a normative type, since, ostensibly, politicians come to power by winning votes from the political market place. In other words, by appealing to popular support. In principle, this process could be likened to a Walrasian type auctioneering-Tatonement, where producers (the competing political parties) and consumers (the electorate) decide, via some form of political price bidding, what bundles of social goods and services will be delivered in a given time period. If social demands are unable to be satisfied, in principle, by the offer curve of party  $y$ , then that party will not have the mandate to formalize the social preferences of society at large. The reason being, that it will not come to power. This is, however, a pseudo-equilibrium, when viewed in strictly Walrasian terms: aggregate demand

and supply do not really match, since in a democracy, political parties are never able to capture the entire market when offering "political prices" in exchange for political support. Also, political tend not to be "tentative prices" of the Walrasian auctioneer, but once for all in the form of set programs.

Be that as it may, in its ideal form, the political preferences of the party will tend to serve as a reasonably approximate common denominator of what society wants in broad terms. The more overwhelming is the support the less inapproximate, is the denominator. To, on the other hand, is representative of the technocratic machinery made up of planning experts. In the main, these are involved in the planning process, and in particular, the formulation of the plan. Efficient allocation of resources, least cost ways of attaining special objectives, and efficiency in terms of utilization of time, namely meeting targets, are important considerations here.

Frisch posits that the political system is indeed responsible for settling different systems of preferences. As he argues, "the political system whatever it may be is intended just in order to settle such differences. What we have to do in Econometrics is to apply this very system for the formalization of the preferences to go with our models. Thus, the preference function as it appears in our model is an expression for the preferences of the decision making authority..." (7).

For Frisch, the task of formalizing the political preferences for purposes of planning could be broken down into the following phases: First, there is a systematic attempt by the technocracy to appraise the overall political climate in the country; especially that of the political party in power. This will then enable the expert to obtain some idea of the preference range of the political system. Such a range will in turn enable the expert to have a tentative idea of what his model should look like.

Following a tentative formalization of these preferences, a semi-Socratic approach (interview/questions) is adopted by the expert vis-a-vis the political decision makers. This is intended to bring about a more definitive formalization of the preferences in question. Essentially, the idea here is to arrive at a type of policy indifference curve. Thus, Frisch contends,

As a simple example for an interview/question, we may take the following: What would you politicians choose if you had a choice between two packages of economic results, for instance one package with say 3 percent unemployment and an annual inflation rate of 5 percent, and another package with say 10 percent unemployment and an inflation rate of 1 percent. By repeating this question but with different figures involved, it will be relatively easy to reach a situation where the interviewed person would say: It is all the same which one of the two packages I decide. The point of indifference is precisely what the expert is aiming at. Similarly, for other kinds of comparisons, there will be a whole series of such partial package the expert will be able to build a preference function (8).

Or more accurately, to give formal content to such a function. The third phase represents itself as a more definite quantitative preference formalization. This is based on the above considerations, and its main operational use is to be an input for the planning model. From this, a solution will eventually emerge in the form of some optimal development path for the economy, with optimality defined in terms of (a) the preferences of the political party; (b) the preference formalization which the expert has eventually reached; (c) and the best ways of implementing these in the socio-economic system. All in all, the expert tries to formalize this function in free form and wherever convenient in reduced form. For a schematic elucidation see Table 1.

In terms of what has been said so far, it must be noted that the process of interview/questions continues at different levels until a satisfactory and workable preference function, in formalized form, is reached, both from the standpoint of the political machinery and the technocracy. The process of preference formalization does not really stop until a unified or macro system of preferences emerges. Such a unified formalized preference function would then represent a "compromise formalization" involving various subsets of the political machinery (for example, different political offices) and the relevant experts. The optimal solution, mentioned previously, is then an optimum based on technical and political compromises.

In a sense, therefore, the Walrasian type Tatonement does not stop in the political market place where contending parties try to sell their respective programs to the electorate. The bidding process continues throughout and is particularly marked on an exploratory phase such as the second outlined in this section; this time between experts and politicians. Seen in the foregoing light, Frisch's framework has greater operational content as it is part of a planning process, it is more politically and institutionally oriented, and it has greater technical complexities than the preference function of the Bergson type which is common to welfare economics.

Where the welfare function in welfare economics is measurable in monetary terms, generally speaking, the formalized social preference of the Frisch type is essentially a function of non-market forces of the effective demand type, in the immediate instance. Social preferences in Frisch's framework are often extendable to non-economic magnitudes. However, the obverse is generally true of revealed preferences in welfare economics. Such preferences are in the main registered through the price system. In fact, Frisch's formalization attempts to amend some of the inadequacies of the price mechanism, in satisfying social well-being in society.

So far for some comparisons between aspects of the Bergson type welfare preference function in welfare economics and Frisch's attempt at formalizing social preferences. An attempt is now made to situate Frisch within the framework of political economy.

Table 1  
CONDENSED TABLE OF TYPES OF

The core may be of the following two kinds:	The core may be of the following two kinds:
<p><i>The Institutionally Stable Core</i> (or shorter: the stable core) Those equations and/or bounds which we have to accept if we confine the analyses to the institutional and political setting which it is out of the question to change within the time horizon of the analyses. Can also be termed the <i>obligatory core</i>, or the <i>obligatory conditions</i>, or again the conditions that are invariant under a change in the <i>facultative</i> conditions.</p>	<p><i>No preference function</i></p>
<p><i>The purely descriptive stable model</i> Leads to the concept of <i>dependent</i> (endogenous) and <i>free</i> (exogenous) variables. The number of the free variables is equal to the number of degrees of freedom of the core. The concept of <i>targets</i> cannot be derived from the model. The only legitimate use of this kind of model is for presenting a sample of <i>alternative</i> constellations of the economy, or for answering questions of this sort: What will happen if...? Even such limited uses of the model may have considerable practical importance.</p>	<p><i>The free form of the preference function</i> The free form of the preference function is particularly useful when forming interview questions to the responsible politicians. In principle the complete knowledge of the free form is sufficient to formulate an optimization problem. The expert will then often transform the free form to a reduced form because he finds this convenient.</p>
<p><i>The Institutionally Sensible Core</i> (or shorter: the sensitive core) Equations and/or bounds some of which are sensitive to such institutional and political changes, that might be considered within the time horizon of the analyses. When comparing the effects of such institutional or political changes, it is necessary to have a stable core as a fixed point of reference.</p>	<p><i>The free form of the preference function as applied to a sensitive core</i> Same as above but now the free form of the preference function may contain a greater number of variables. Statistical difficulties of the same sort as mentioned in the case to the left, and mathematical difficulties as mentioned in the case to the left, and mathematical difficulties as mentioned in the case to the right.</p>
<p><i>The free form of the preference function</i> The free form of the preference function is particularly useful when forming interview questions to the responsible politicians. In principle the complete knowledge of the free form is sufficient to formulate an optimization problem. The expert will then often transform the free form to a reduced form because he finds this convenient.</p>	<p><i>No preference function</i></p>
<p><i>The purely descriptive stable model</i> Leads to the concept of <i>dependent</i> (endogenous) and <i>free</i> (exogenous) variables. The number of the free variables is equal to the number of degrees of freedom of the core. The concept of <i>targets</i> cannot be derived from the model. The only legitimate use of this kind of model is for presenting a sample of <i>alternative</i> constellations of the economy, or for answering questions of this sort: What will happen if...? Even such limited uses of the model may have considerable practical importance.</p>	<p><i>The free form of the preference function as applied to a sensitive core</i> Same as above but now the free form of the preference function may contain a greater number of variables. Statistical difficulties of the same sort as mentioned in the case to the left, and mathematical difficulties as mentioned in the case to the left, and mathematical difficulties as mentioned in the case to the right.</p>
<p><i>The Institutionally Sensible Core</i> (or shorter: the sensitive core) Equations and/or bounds some of which are sensitive to such institutional and political changes, that might be considered within the time horizon of the analyses. When comparing the effects of such institutional or political changes, it is necessary to have a stable core as a fixed point of reference.</p>	<p><i>The free form of the preference function as applied to a sensitive core</i> Same as above but now the free form of the preference function may contain a greater number of variables. Statistical difficulties of the same sort as mentioned in the case to the left, and mathematical difficulties as mentioned in the case to the left, and mathematical difficulties as mentioned in the case to the right.</p>

Source: F. Long, ed., *Ragnar Frisch Economic Planning Studies* (Preface by Jan Tinbergen) (Dordrecht: Boston: D. Reidel Publishing Co., 1976), pp. 20-21.

#### IV. FRISCH AND POLITICAL ECONOMY

Classical political economy was generally concerned with issues relating to value, distribution and capital. It did not encompass planning in any systematic way. Indeed, planning became only a legitimate concern of present day economics during the latter half of this century. Several factors could be held accountable for the non-incorporation of planning in classical political economy. Of these the following seem worthy of note.

In the first place, there was the prevailing that the market mechanism or Adam Smith's invisible hand was sufficient, in itself, to resolve important questions like production, distribution, consumption and resource allocation. This view was taken to the extreme by laissez faire exponents; but was also firmly held by mercantilists in spite of the deep seated advocacy that the State should intervene to protect the interests of the society. This intervention was, however, never conceptualised as planning in the way the term is currently used. In the case of Karl Marx, who did not adhere to the principles of the free market system, the primary concern was not planning as a way of improving the social and economic efficiency of capitalism, but something else. He was mainly preoccupied in explaining the capitalist mode of production (its origins and modus operandi), and an explanation for the inevitable downfall of the capitalist society. It is clear that, within a non-market system of the type advocated by Marx, there would be no room for Adam Smith and his invisible hand. However planning within the context of socialism or communism which Marx advocated was not of operational interest to him. It was, for example, left to a later generation of socialist economists to fill this conceptual gap.

Secondly, classical political economy was not theoretically constructed with a statistical or quantitative framework in mind. While it is true that this does not affect conceptualising about planning as such, as it does to the operational aspects of a plan (for instance, one may conceive of a plan without statistics; that is, however, a different matter from putting a plan into operation), it is probably true that the awareness of quantitative techniques can enable one to realize the practical usefulness of such. As Frisch himself reminds us, "the architectural plan for theory had so to speak not made room for this verification" (9).

Lastly, a matter related to the above, is that quantitative facilities such as national income statistics, computer networks, and econometrics for example meant that statistical infrastructure was poor to start with. How can you plan without data if planning has to deal with targets and measuring results against these?

If then classical political economy was not preoccupied with planning, how does one fit Frisch and planning into the mold of political economy? What is more, the growth of quantitative methods in economics is often cited as a contravention of the basic outlines of political economy. The point being that the former is deprived of the broad social and human

framework which characterised the writings of Mill, Smith, Malthus, Ricardo and others who helped in the development of political economy.

The answer to the above lies mainly in conceptualization and in scope. The central issues of political economy, for example, are basically incorporated in Frisch's framework. Let us illustrate briefly. Frisch saw the role of planning in economic activity as an organic link with an overall societal process. Consider, for instance, the question of decision making in society and the formalization of societal preferences, dealt with above. Here Frisch argues "... political discussions today come dangerously close to resembling a dog fight where the global battles of and inter-connections between the basic questions have a tendency to get lost and only shouting about striking partial aspects of inefficiencies and injustices count. All this calls for a radical and unconventional approach about the decision making in society at large. The preference function is a tool for defining the goal..." (10).

Thus, in human welfare terms, Frisch sees co-operation between experts and politicians in the formalization of society's preferences as being necessary to obtain an improved quality of socio economic and political life in society at large. In other words, achieving appropriate decisions, which in the ultimate analysis, reflect the wishes of the human population. More than that, such co-operation tends to politicise experts by creating political awareness of the technical and policy implications of political preferences.

#### V. FRISCH AND DEMOCRATIC PLANNING

It is often claimed by modern day critics of bureaucracy that a major problem is that bureaucrats often lack a full appreciation of the wider consequences of the day-to-day decisions taken. As a result, such decisions are not necessarily in the best interests of the community at large. In principle, this criticism would seem to apply less to Frisch's experts, given the type of political environment and interactions taking place in the determination of technical choices.

Aside from the formalization of society's preference function as such, it is worth quoting Frisch in terms of what he considers to be the ultimate objective of planning. This is necessary since the preference function is situated within a planning context. Both should therefore subscribe to one common philosophy or idealized end state. Frisch affirms:

My purpose is to make economic planning at a high aspiration level, the pillars of a living democracy. I want a society which is a living democracy ... a democracy that is living in the sense of actively engaging as many as possible of the citizens to take an active part in the affairs of the small community where they are living, and also to take an active part in the affairs of the nation as a whole. (11).

This certainly attests to a philosophy of planning which is by no means limited to manipulation of data. It certainly bears echo of present-day critics of neo-classical and Keynesian type economics, who clamor for the return of the "human element" in the study of "ends and scarce means which have alternative uses", namely economics.

On other count, it is clear that, in terms of consistency with Frisch's planning philosophy outlined above, elements such as redistribution of income, satisfaction of basic needs and the like, could be built into the formalization of societal preferences.

Seen in the foregoing light, therefore, planning within Frisch's framework is consistent with the broad dimensions of classical political economy. A quotation from John Stuart Mill suffices to bring this out: "In so far as the economic conditions of nations turn upon the state of physical knowledge, it is a subject of the physical sciences and arts founded on them. But in so far as the causes are moral or psychological, dependent on institutions and social relations, on the principle of human nature, their investigation belongs not to the physical but to moral and social sciences, and it is the object of what is called political economy". The questions of morality and social and political justice are central questions to Frisch. It is why he is at home with Mill.

Frisch is therefore an example of a highly specialized and quantitative economist who was able to bring such techniques to the service of political economy. It is, however, true that his efforts were largely in the realm of developing a planning methodology per se, rather than locating that methodology within economic philosophy of the classical variant. This latter neglect explains why, as an economic thinker, Frisch has been seldom known. Given, however, Frisch's initial contribution to both empirical and theoretical aspects of planning, and the fact that he was among the first Western econometricians to regard planning in a broad societal and moral context, it is probably no exaggeration to regard him as a founding father not only of the Econometric Society, but of the Political Economy of Planning.

## VI. FRISCH-SOME BEHAVIORAL LIMITATIONS

An elementary feature of any plan is the conscious mobilization of social productive agents for the attainment of certain goals. As Frisch would argue, planning is ultimately aimed at improving the quality of life of the human population. In terms of the latter, it is important that the planning process functionally recognizes, and indeed provides a meaningful framework for, such a realization. With this in mind, this section aims at pointing out some behavioral limitations of Frisch's framework.

Behavioral considerations, for some time now, have formed a core of what can be called management science (12). Their relevance stems from the recognition that a full understanding of human agents, engaged in productive

and other pursuits, must take one into the realm of social psychology. It is only when one is equipped with this understanding, it is argued, that the human contribution to a particular task can be made fully optimal. This is so because action depends on motivation, and motivation in turn depends on need fulfillment. Simon and others have used behavioral considerations in an attempt to enrich economic analysis. In other words, going behind the customary assumptions of "rationality". Little work, on the other hand, has been attempted in the area of planning and human behavior, although it has for some time now been recognized that human considerations often play an important role in explaining the failure of plans.

In the above light, Frisch's framework does not guarantee that political choices accurately reflect societal preferences. In real terms, the political machinery is supposed to serve as a proxy for such preferences. But as we observed earlier a Walrasian Tatonnement does not really exist in a Frisch type political market place. Also, there is no guarantee that pre-election political preferences will obtain when party y assumes power. Of more practical interest, in conditions of uneven socio-economic relationships in a given society; a ruling party that draws its support mainly from a particular class is likely to inject a preference bias in terms of particular societal aspirations and interests.

Consider, for example, an agricultural development project in a developing country which reflects the preferences of a landed aristocracy from which the ruling party draws its support. Social groups in the agricultural sector such as landless laborers, small peasants and rural unemployed labor will tend to be of peripheral concern. From a social welfare point of view, there are strong reasons why such a situation should not obtain. Put differently, the aggregate welfare needs of the socially peripheral groups will tend to be greater simply because the level of poverty (absolute and relative) will be greatest among these groups. This type of asymmetry is indeed a real problem in terms of policy formulation in most Third World countries, given grossly uneven social relationships, which obtain there. The situation has resulted in the advocacy of a basic needs development strategy for the Third World, by a number of international organizations. We cite the Third World, simply because of wider social discrepancies prevailing there; in principle the problem obtains in all societal environments where groups of people have uneven access to the political machinery.

Secondly, is a point not removed from the foregoing. Frisch advocates citizen participation in the planning process, at least in broad outline. Note his concern for citizen involvement in human affairs which was quoted earlier. However, in his formalization process, which operationally sets the broad parameters of government policy, no systematic attempt is made to deal with this question. Indeed, there are strong reasons to expect that, in the type of machinery where politicians and technocrats interact to determine the societal preference



function, this could at best lead to a pseudo-social preference function. The reason being that the mechanism does not make room for participative planning. The only real link, in the formalization process, between the wider society and the planning machinery is the political system. The inadequacy of this tenuous link has already been mentioned, namely as a registration device it is not fully reflective of the broad interests of society at large; also political preferences are subject to change during a period of political rule. The end result is likely to be discontinuity in the planning process in so far as the interests of community are concerned.

In a slightly different vein, Frisch's approach does not deal substantially with the role of the human agent in the operationalization of the plan. How does one optimize the human contribution to planning, in a similar way as behavioral theorists were asking, how does one optimize the human contribution to organizational performance? At what levels of the formalization process for example? This is necessary since it cannot be asked of people to participate fully in something, which in a sense has been imposed upon them, unless the imposed preference is coincidental with theirs. This is unlikely when divergent group interests prevail. These points seem critical since planning in the final analysis is a human activity and should therefore embrace socio-psychological, cultural and political, in addition to economic and technical interests. It seems necessary for econometricians to pay more serious attention to what are normally regarded as "exogenous variables" as they go a considerable way in explaining the failure of plans which operate within a western type political economic environment.

The limitations raised here no doubt stem from the fact that Frisch was in the first instance an econometrician. He was primarily concerned with technical details even though he tried to keep these in a human and societal perspective.

- (1) Tinbergen shared the Nobel Prize jointly with Frisch.
- (2) See A. Bergson, "A Reformulation of Certain Aspects of Welfare Economics", Quarterly Journal of Economics, Vol. LII, pp. 310-34, 1938.
- (3) See E.J. Mishan, "A Survey of Welfare Economics, 1939-59", in Surveys of Economic Theory, Vol. 1, The Royal Economic Society and The American Economic Association (London: Macmillan, 1965) for a discussion of some of the finer points.
- (4) K. Arrow, Social Choice and Individual Values (New York: 1951).
- (5) For instance Kahn, Hicks, Little, Kaldor, Graaff.
- (6) Mishan, op. cit.
- (7) F. Long, ed. (Preface by Jan Tinbergen), Ragnar Frisch Economic Planning Studies (Dordrecht: Boston: D. Reidel Publishing Company, 1976), p. 25.
- (8) Ibid, p. 29.

- (9) Ibid, p. 11.
- (10) Ibid, p. 41.
- (11) Ibid, p. 27.
- (12) See for example: A. Maslow, Motivation and Personality (New York: Harper and Row, 1954).

#### A GUIDE TO COMMUNIST ECONOMIES

Soviet-type Economic Systems: A Guide to Information Sources, an annotated bibliography 1/, is designed to help the researcher avoid the laborious process of searching through many books and journals for material relevant to a specific topic or sub-area of interest. Covering what are commonly referred to as socialist or communist economies, the book cites books and articles dealing with the functioning economies of Bulgaria, Czechoslovakia, East Germany, Hungary, Poland, Rumania, and the Soviet Union. Also covered in the guide are works referring to theoretical concepts or models of centrally planned, command, or Soviet-type economies. It is edited by Z. Edward O'Relly.

All of the words cited in the bibliography are available in English and include some translations from works originally published in other languages. Citations emphasize the economic, as opposed to the accounting or business, aspects of the economies. Since many of the Soviet-type economies follow a similar economic process, material in the guide is organized primarily according to functional categories instead of particular countries.

Fourteen chapters cover sub-topics of major interest to researchers in Soviet-type economic systems: Overview... Economic Organizations and Structure... Western Theories of Socialism... Growth and Development... Planning Theory, Practices, and Methods... Prices and Inflation... Capital and Investment... Population and Labor Force... Wages and Consumer Welfare ... Efficiency and Productivity... Sectoral Problems and Accomplishments (includes Agriculture, Industry, Transport and Communication, Energy and other Natural Resources, and Services)... Monetary and Fiscal Theory, Practices, and Institutions... Foreign Trade... Economic Reforms.

Author, Title, and Subject Indexes complete the guide, which is Volume 12 in Economics Information Guide Series, part of the Gale Information Guide Library.

(From Tom Romig for the company).

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1/ Soviet-type Economic System: A Guide to Information Sources.  
 Edited by Z. Edward O'Relly, associate professor of economics, North Dakota State University, Fargo. (Detroit, Mich. 48226: Gale Research Co., 1978, xii + 228 pp., \$22.).

ECONOMIC CONSIDERATIONS FOR SOCIAL POLICY AND THE SOCIAL  
DIMENSION OF ECONOMIC POLICY \*/

Jorge Méndez Munévar and  
Alvaro García Hurtado \*\*/

INTRODUCTION

During recent decades many Latin American countries appear to have encountered a formidable dilemma in the field of economic and social development policy. On the one side there is neo-classicism, which, applied as a doctrine in which purely economic considerations should prevail, does not satisfy the aspirations of the popular classes for change and participation. On the other side there is social change accelerated at times in the form of populism, which can lead to a decline in the economic process and the rate of growth. Experience shows that both the one and the other can bring about an impairment of democracy and hence restrictions on individual liberty.

The fact that this dilemma tends to persist and that consequently each of the two extremes frequently causes an increase in social discontent may be largely explained by the lack of appreciation of the relations between social aims and their economic aspects. The solution of social problems, as for example the relief of extreme poverty, has an undoubted economic value in terms of the greater productive capacity of those benefited. On the other hand, social benefits involve expense and generally imply a transference of resources from some sectors of society to others. It is important, when taking decisions on social expenditure, to bear in mind both the potential economic value of the results of that expenditure, and the

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effects of the cost incurred in terms of the growth rate of the economy as a whole. At the present stage of economic science and of development policies in practice, neither the one nor the other is usually taken sufficiently into account.

The ideal for Latin America and for all developing countries would be to achieve the introduction of policies which would at the same time allow for an increased growth of investment and preferential attention to the needs of the great majorities of the poor, all this within a framework of individual freedom. Throughout Latin America this ideal has been earnestly sought, but generally without the desired success. As already said, the high growth rates achieved for a time in some countries have not succeeded in alleviating the social problems, and on the other side, the attempts at mass solution of the social problems have been accompanied by economic difficulties.

Those who have followed with interest the efforts of the countries of the region in the field of development policy concur in view that all this denotes a serious gap in conceptual, technical and operational awareness which should be most urgently filled. This paper, which might serve as a basis for a detailed research project on the subject, aims to set out the main areas in which the relationship between social programmes and their economic implications is most evident.

#### I. TOWARDS AN OPERATIVE DEFINITION OF THE SOCIAL PROBLEM <sup>1/</sup>

We are called upon to deal with the subject of social programmes in their relation to the economic question. It seems appropriate therefore, to begin by asking what is meant by the term "social problem". In reply there immediately comes to mind a vision of our familiar human dramas: poverty, marginality, uncertainty and other such manifestations of injustice in a continent which has the resources and conditions to free its population from these miseries. These images of the social problem, however are not sufficient to define the characteristics that social programmes should possess, understanding by these the programmes designed to overcome these problems.

The actual and objective reality that causes our concern is the existence in Latin America of more than 100 million people who have no access to a range of goods and services indispensable for subsistence in conditions compatible with human dignity. Our concern is reinforced by the fact that, after a successful period of economic growth -as in the

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<sup>1/</sup> In this paper there are no quotations, although direct references are made to various authors. This, however, by no means implies that the writers claim the authorship of all the ideas contained here. On the contrary, the absence of literal quotations arises from the impossibility of citing in a work of this type the rich and vast literature that exists on most of these topics without leaving serious gaps.

decade of the 60s, when a growth rate of the product for the region of almost 6 per cent per annum was attained- the absolute number of persons in a state of poverty remained unchanged. This is all the more serious when it is realized, as various studies attest, that the region actually possesses the resources needed to overcome the problem of poverty. Indeed, in most of the countries for which information is available, the existing conditions are propitious for the total elimination of poverty by means of a transfer of resources from the sectors which enjoy high standards of living. Such transfers would not need to be, on average, more than 12 per cent of the available income of the richest 10 per cent of the population. The first characteristic of social problems becomes patently obvious: it is, fundamentally, a matter of distribution of wealth and well-being, and not necessarily one of an increase in the availability of resources.

This inequality in the distribution of income and wealth is based on the action of an economic system which excludes large sectors of the population from the benefits of growth. In fact, an examination of the characteristics of the social groups affected by the social problem reveals that those who cannot adequately meet their basic needs tend to be those who have employment problems. The most direct linkage is seen to be between poverty and underemployment, especially in the rural sector. In its turn, the employment problem is linked with two determinative concepts in Latin America today, one being structural heterogeneity and the other differentiated labour and employment markets.

For many years now CEPAL has maintained that a central characteristic of the economic system prevailing in the countries of the region is its structural heterogeneity. In this situation the modern sector of the economy concentrates technical progress within itself, excluding from it large social and productive sectors. In these conditions the process is reinforced and intensified, and thus the dynamic of the economies of the region tends to be concentrative and exclusive.

In its turn, PREALC has pointed out that the heterogeneity of the economic structure results in a heterogeneous situation in employment. In other words, there is a small sector, comprising those who work in the most modern strata, which records a high productivity and high levels of remuneration; and another and larger sector, consisting of those employed in the intermediate strata, with lower levels of income and productivity. This feature of the economic system, existing in practically all the countries of the region, results in the employment of small proportion of the work force in the modern sector, whereas the majority are obliged to work in the traditional sector in conditions of low productivity and, in general, with low and fluctuating levels of income.

We see, then, that a second root of the social problem is the existence of an economic system that concentrates technical progress and, in consequence, generates a heterogeneous employment structure. This circumstance, added to the high concentration of income and wealth,

explains why the region, despite its high economic growth, irradiates this growth over an unduly restricted social field. The employment problem becomes especially important from this standpoint, particularly the underemployment that affects a high porportion of the labour force in Latin America. In view of the circular causation between the different levels of structural heterogeneity (technology, productivity, labour segmentation, poverty) it becomes essential for any social policy to combat the problems arising from the existing employment structure and, above all, to encourage a partial reassignment of the economic surplus towards those productive sectors with least capacity for accumulation and therefore with the highest indexes of underemployment of labour.

A large part of the social problem, therefore, lies in the form in which the economic process functions and evolves. This implies that social problems cannot be fully solved merely by programmes aimed at the relief of the symptoms of poverty; rather must the prevailing economic model correct its tendency to concentrate wealth and to exclude great masses of the population from participation in the fruits of growth. In this respect, the relation between the social and the economic elements is crucial, and should be stressed whenever social programmes are proposed. But there is a second aspect in this relationship which is equally pertinent and important social programmes, and changes in the economic model aiming at greater social justice, have costs in economic terms, and these also must be taken into account. We shall return to this important question later on.

At the same time, when the imbalances in the distribution of wealth reach the magnitude they have attained in Latin America, with the result that approximately 40 por cent of the population lives in a state of poverty, we cannot regard the problem as a purely economic one. Obviously society, must have political mechanisms to cope with this situation and, in the face of such imbalances, to seek a genuine social integration. Consequently, a basis must be sought in this political machinery for the understanding and, subsequently, the alleviation of these imbalances.

Political power is founded on a juridico-legal structure which enables the different social groups to formulate and exert pressure for the satisfaction of their needs and aspirations. This possibility of participating, and the advantage taken of it, determines the amount of representation that the different social groups posses in the definition of the modus operandi of society, and hence in the degree of efficacy with which society satisfies their needs. From this standpoint we can speak of political poverty, referring to the situation of those sectors of civil society which have none of the elements of power (organization, representation, self-awareness) nor the basic conditions (education, information, health, income) for taking part in the decision-making which determines the future of the country and its human and material environment, thus maintaining the possibilities of being active subjects of their own development.

Moreover, the State is the fundamental instrument for the expression of political power. Through its actions -economic and political- it implements and gives cohesion to a political project, which obviously does not respond lineally to a single group of interests but which tends to represent the interests of the relatively more powerful groups. Thus the State becomes an instrument of integration and maintenance of political order which is used to promote a national project; in practice through planning -understood as the technical instrumentation of a political project- it has a decisive effect on the economic order and hence on the relative well-being of the different social groups. We see, as a third characteristic of the social problem, that its solution are related to the differentiated access of the different social sectors to the institutions which constitute and express political power and, in very practical terms, to the State.

The magnitude of the social problem in the region and its economic-structural and political roots lead to the conclusion that a development strategy aiming to overcome it will need to have global or structural characteristics in which the three great components specifically the economic, the political and the social, must be simultaneously taken into account.

As a logical conclusion of the foregoing it becomes apparent, on the one hand, that social policies should be invested with the power to make the productive and distributive structure compatible with the objectives of well-being for the majorities. And on the other hand it becomes necessary for the political power of the State to be based on a broad social coalition in which the interests of the majorities are duly represented and effective channels of communication exist between these groups of society and the various institutions of the State. Consequently, social policy should certainly not be a compensatory and subsidiary element of economic growth. Rather should it be understood as a set of procedures which modify the structural factors behind the market, and which transform the modalities of the assignment of resources -apart from redirecting public expenditure- and of the social product with a view on the one hand, to the more immediate benefit of those who are poorest politically and economically and, on the other, to the creation of structural conditions that will ensure the permanent and increasing well-being of the community as a whole.

In other words, the success of social policy depends on the technical coherence with which the structural conditioners of the social problem, such as the direct palliative action of the State, are dealt with, and secondly, on the political will to carry out this task. The "social" aspect, therefore, cannot be isolated from the economic and political; otherwise the policy will be diluted and fragmented and result merely in a prolongation of the uncertainty, marginality and poverty in which more than 100 million Latin Americans live. In theoretical terms,

however, two areas of concern for the solution of the social problem can be distinguished: one, the coherence and technical efficiency of the procedures designed to overcome it; and, two, the construction and expression of a political will to accompany and support these procedures. Since the main object of this seminar is to consider the first of these topics, the present paper will be devoted entirely to this. Nonetheless, this fact should certainly not be construed as evidence that the authors think that political considerations should take second place. On the contrary, we are convinced that social change is only possible if the great majorities have effective access to the organs of political power, thus becoming active subjects of the necessary process of reform.

## II. THEORY AND PRACTICE OF ECONOMIC DEVELOPMENT AND THE OVERCOMING OF THE SOCIAL PROBLEM IN LATIN AMERICA

Our contention, then is, that in an economic and social situation which is complex, multidimensional and above all inter-dependent, such as the one in which we find ourselves, the "social problem" cannot be thought of in isolation. When we attempt an analysis of the ways of overcoming the social problem in our region we must therefore include both the theory and practice of economic development and the distribution of its benefits. Indeed, the conceptions held about economic growth have a powerful influence on the measures designed to surmount the problems and, viceversa, the social procedures can have a profound effect on the intensity and the characteristics of growth.

### 1. Conceptions on the relation between economic growth and the overcoming of the social problems

In Latin America there is certainly no single theory and practice of economic and social development. Very much to the contrary, throughout its history, in one country or another, there have been many and varied national development projects, depending naturally on different bases of social support and different modalities for obtaining their objectives. In a recent document produced by ILPES, "The State of Planning in Latin America and the Caribbean", a lengthy account is given of the various forms adopted by the theory and practice of development policies, or, as it was expressed in the said document, the different styles of planning prevalent in Latin America. In this study ILPES referred to the existence of four styles of planning which, in their turn, defined the various theories and modalities for overcoming the social problem which are practiced in the region today.

It is unnecessary to repeat here the analysis of planning styles made by ILPES in the above-mentioned document. On the basis of this, however, we can distinguish two important forms of approach to the relation between growth and the mastery of the social problem. Each of these approaches



incorporates two of the four planning styles recognized by ILPES. Moreover, in describing these approaches we shall refer only to the relationship postulated between growth and well-being and, in consequence, to the mechanisms deriving from this for the attainment of social well-being and income distribution.

The first of these approaches, based on traditional economic theory and, fundamentally, on its neo-classic version, postulates a mechanical equivalence between growth and the well-being of the population as a whole, and therefore gives priority to growth. In other words, this approach assumes that growth, through its "spill-over effects", automatically benefits the whole population and that therefore the most efficient method of overcoming the social problem is to speed up the growth rate. Even so, this approach recognizes that the State -without interfering in the market decisions concerning the assignment of resources- must supply certain social services that the market does not provide. Thus it accepts the existence of a "social policy" confined to certain spheres and subsidiary to the growth objective. The importance and magnitude given to these policies generate differences between the various countries which are implementing, or have implemented, this approach; but in essence they all believe that growth -in the medium or long-term- constitutes the best solution to the problem of poverty.

The second approach does not accept the direct and automatic link between growth and social well-being and therefore postulates the need for direct State intervention in order to guarantee certain substantial increases in the standard of living of the population and, in particular, of the sectors with least resources. Within this concept there are differences in respect of the quantity and depth of the transformation in the economic, political and social structure needed to attain the social goals. At all events, it is recognized that social aims have a central place in development strategy, since they will not derive automatically from growth, and moreover, that the State has an essential role to play in the creation of conditions which will make viable the attainment of these aims.

## 2. Some criticisms of the neo-classic conception

As already said, the first of these conceptions claims that the market -except in certain special circumstances- freely and spontaneously attains an ideal level and composition of the product. This is a situation, as defined by Pigou, in which there is no alternative form of production obtainable through a reassignment of resources among the different productive units which could provide the community with better conditions than those established by the market. This definition gives rise to the

"neutral" character required of State action, <sup>1/</sup> that it should not interfere in the process of assignment of resources that arised from market relations. Any intervention, it is claimed, would so affect the members of society that those who "gain" from the changes produced would be unable to compensate those who "lose", and hence there would be no net gain for society.

We believe that this conception can be criticized from two viewpoints: first, its ethical basis, which we consider incompatible with the aims of equality and social justice; and, second, the fact it does not take into account the characteristics of the economic and social structures of Latin America.

Our disagreement on the ethical plane with the traditional economic theory is simply our refusal to accept Bentham's concept that the algebraic sum of the interests of individuals is equal to the interest of society, which leads to the postulate that the individual who looks after his own interests also serves the interests of society. This claim, moreover, is seem to be linked with a hedonistic vision of the human being, which would keep him completely absorbed in the task of obtaining for himself an ever-increasing material well-being. To this he subordinates his life, rejecting a social-community dimension which, in our view, is an essential part of humanity. All this, incidentally, is the basis on which the traditional economic theory feels able to absolve itself from the distributive problem. Indeed, if it is held that a man derives no pleasure from the fact that a fellow-being more needy than himself should satisfy his whole or partial needs, there can be no justification for the transference of resources from those who have their needs satisfied to those who have not. In its own terms, the marginal profit on income is no greater for the poorest groups, and, consequently, the "social utility" does not increase with such transferences.

We see, then, that the ethical concept underlying the traditional economic theory -and especially its neo-classical version- is incompatible with a model or style of socioeconomic development- of which the central motivation is the search for an equality of opportunity to realize in the fullest possible way the true and multiple dimensions of humanity. These views of ours on the "ethical" in economy, and on the ideas of Jeremy Bentham, might seem to some a trifle anachronist. They have, however, an amazing actuality. During recent years, and especially in Latin America, there has been a great resurgence of utilitarian ideas that seemed to

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<sup>1/</sup> We are not overlooking the fact that this theory accepts the need for State intervention in certain exceptional cases. These will be described and discussed in the third chapter of this paper.

have been buried under the enormous accretion of economic events in the 19th., and the first half of the 20th century, and crushed by the advances in philosophy and social sciences generally.

Our second disagreement with traditional economic theory derives from the reality of the structural roots of the social problem in Latin America. As already said one of the central characteristics of the countries of the region is their enormous economic and social heterogeneity. We believe that this is largely the cause of the existing social inequality and the chief barrier to surmounting it. The extremely deficient economic productivity of the lower strata condemns them to a state of poverty and unfulfilment of their basic needs. Likewise, it is common knowledge that the heterogeneous and unequal distribution of productive capital, technical skill and education normally introduces "segmentations" into the labour markets which give a permanent character to the original unequal distribution of incomes and wealth. Lastly, the composition of the supply of goods to the end-consumer conform to patterns of demand which derive from a highly concentrated distributive structure, thus strengthening the existing criteria for the assignment of material and human resources, and, in dynamic terms, a concentrative and exclusive model of economic growth.

This brief outline of the consequential relationship between the structural heterogeneity of the Latin American countries, the form acquired by profit distribution, the structure of demand, the composition of supply and the assignment of resources, is designed to show the incapacity of the market to correct these inequalities. In fact, as already said, the market, functioning spontaneously, tends to reaffirm and reproduce or intensify the existing structure with its consequent injustice and social inefficiency. Apart from this, the situation is clear from the results of economic growth in the countries of the region. Even in the period of greatest growth, and when the State was also playing a part in correcting social imbalances, as in the 60s, the number of people who could not meet their basic needs remains unaltered. The reason for this was the fact that no changes were made in the structural conditioners of unemployment and underemployment, of the distorted prices of capital, of the concentration of wealth and various other causes of the social problem.

For these two reasons, among others which it would take too long to mention, we are convinced that the development strategies based on the free play of market forces and on the expectation of a "spill-over effect" of economic growth will not be capable of eliminating the social inequalities which are manifest today in the poverty, marginality and uncertainty in which somewhat more than 100 million Latin Americans are still submerged. The solution of social problems requires a dynamic and deliberate process of structural change -and therefore of the basic economic and political processes- which will alter the relations of the different socioeconomic strata among themselves and with the productive structure. It is a question of producing certain fundamental changes in the socioeconomic structure,

thereby achieving a socioeconomic model which would allow for the dynamic incorporation of all members of society.

### 3. The requirements of social change

The realization of this process of change requires, on the one hand, a certain normative relationship in the direction of the transformation and, on the other, a planned action designed to implement the "socioeconomic model selected". It is important to be clear and, we repeat, rational in the task of defining the aims and criteria which will govern the procedures destined to transform the socioeconomic structure so that it will meet the needs of the whole population. Hence the proposal is to carry into effect what most of the Latin American nations have determined to do, but in vague terms and without all the necessary instruments; namely, to make an integrated and continuing effort to combat the state of social inequality, with its resulting poverty, marginality and uncertainty.

The forms and tempo of structural change will depend on the social, economic and political situation in each country. Hence it is impossible and certainly not desirable to define common criteria -except those of a theoretico-methodological nature- for the programming and realization of this endeavour.

In the theoretico-methodological field, however, we are convinced that there is still much work to be done, particularly with reference to a multidisciplinary definition of the theory of economic and social development. This compels us to think of an integrated or (as the United Nations proposed at the beginning of the 60s.) a unified version of development where economic growth and social progress are not only understood to be mutually interdependent, but also to be organically related in an integrated development process.

In what follows we shall concentrate on a discussion of the conditions required for an integration of economic and social problems. We shall try to analyse the social implications of economic policies and the economic dimension of social policies. This analysis, we trust will help to delimit the large areas included in the field of the interrelation existing between the economic and social aspects of planning and in the adoption of development policies.

### III. THE SOCIAL IMPLICATIONS OF ECONOMIC POLICY

#### 1. General background

Economic and social policies, whether directly or indirectly, attempt to achieve the same end which is the development of the well-being and potentialities of the human being. It should be evident, therefore, that economic policy has social implications and that social policies, in their turn, have an economic dimension and implications of a depth which cannot be ignored or minimized. These relationships, which are so patently obvious, have often been markedly absent from Latin America Planning and in general from the formulation and adoption of economic and social policies.

We shall attempt to highlight the importance of the links, between the economic and social elements to point out the most important aspects to be taken into account, and to indicate the areas of research and decision-making which seem to have priority in the advance towards a definition of an integrated approach to economic and social development. Naturally we shall not attempt to mention here all the possible relationships, much less to deal with each of them in depth.

The economic problem is in effect a social problem, both in its nature and its conditionings and consequences. Hence it is impossible to think of the two subjects separately. Nonetheless, economic policy in practice - powerfully influenced by traditional economic theory - has minimized the importance of this relationship.

In respect of their social effects, three types of economic policy can be distinguished: those which tend to affect the primary distribution of income; those which tend to correct the differences between private and social costs of prices and, lastly, those which are traditionally called economic policies, namely those related to the achievement of objectives such as growth, price, stability, etc., and which have social implications through the natural participation of the members of society, including the poorest, in the prosperity or deterioration of the economy.

All these policies, as we have seen, can alleviate the social problem through increasing the level of income and hence the capacity of consumption of the basic needs of the lower income groups. With regard to the specific aim of income-redistribution, there are many procedures for achieving it: for example, those which directly redistribute primary resources; those which transform the supply structure by stimulating the production of goods consumed by the lower income groups; and those involving technologies which promote a greater use of unskilled labour, etc. All these have as common denominator the fact that they increase the consumption capacity of the poorer groups in the short term. All of them, too, have profound and reciprocal relations with the investment decisions of the community with the way in which these investments are carried out, and with the types of production achieved in the process of investment saving.

For example, to achieve the aim of dynamically increasing the capacity of the lower income groups for consumption of their basic needs, the redistribution must not hamper the rate of growth or at least it must ensure that in the long term the income level of the most disadvantaged group is not lower in real terms than it would have been without the intervention of redistribution. Similarly, the productive structure, both in the type of technology it uses and in the type of goods it produces, must progressively adapt itself to the capacities (human resources) and needs (structure of demand) of the lower income groups, while at the same time avoiding an unfavourable effect on the average, productivity of the economy.

We must emphasize that among the elements which satisfy basic needs we include employment, not only because of its capacity to generate income but also because it is creative by nature and incorporates the individual into the community. Work has the power to develop man's potential and thus, to complete and fulfil him. Likewise, when an individual performs a socially useful task, it satisfies his need for social appreciation or to belong to and form part of a society or group on which he depends and to which he contributes. Hence it is not a question of just any type of employment but of one which enables a person to develop his potentialities and which produces socially useful results.

Having touched on these general considerations, we shall proceed to outline by way of example the social implications of different types of economic policy.

## 2. Economic policies which transform the primary distribution of income

Policies of this type are those which modify the conditions determining the original sharing out of income. Thus they centre around the phases of generation and appropriation of incomes and their effect is permanent; that is, once the transformation has been made -provided there are no new changes- it continues indefinitely. This is undoubtedly the most direct, effective and permanent method of improving the situation of the lower income groups. The doubt which persists in connection with the use of these mechanism -apart from the basic conditions of a political nature- concerns their effect on the growth rate.

We will analyse briefly the situation -in this respect- of the four areas of intervention through which the government can achieve a redistribution of income.

### (a) Ownership and control of assets

This is the fundamental area, since it largely determines the form in which the revenues of society are distributed among individual. In Latin America a consideration of the distribution of assets is particularly important since all the studies on the subject point out that their concentration is greater than that of incomes and at the same time is the chief cause of the concentration of the latter.

Changes in ownership and control of assets can be achieved by means of a redistribution of existing assets or -what is politically less conflictive in dynamic form by way of changes in the pattern of accumulation which is that which determines the growth of the different assets of course of time.

The redistribution of existing assets can be made through collectivization or through their redistribution towards the lower income groups. Both modalities have been tried in Latin America, with very varied results. As regards their relation to economic growth, perhaps the only general lesson that can be learnt from these experiments is that, as far as public enterprises are concerned, their efficiency largely depends on the clarity with which their functions are defined, whether these are financial accumulation, consolidation and/or promotion of development or income distribution. There are many examples of success in the fulfilment of each of these functions. But there are also many records of failure which impose burdens sometimes very heavy, on the exchequer. At all events, to the extent that the function of the public enterprise is clear and, of course, advantageous for the lower income groups, it would seem that this can efficiently fulfil its social role.

With reference to the transference of assets towards the poorest groups, the chief lesson seems to be that this process is inadequate and undesirable -from the growth point of view- unless it is accompanied by programmes of technical and financial assistance and of provision of resources complementary to production. It is axiomatic that the lower income groups not only have fewer means of production but also less capital -in the broad sense of the term- for the necessary investment and the maintenance of production. Hence, unless these are provided for them, production will fall and the income level of the supposedly favoured groups may be reduced.

The dynamic redistribution of assets, moreover (that is, the reorientation of the pattern of investment of the economy), can be promoted or induced by the government through a gradual socialization of the assets, or through policies of support for direct investments destined to raise the lowest incomes.

The option of gradual socialization is what has been operating, probably unconsciously, in Latin America. This means the growing participation of the public sector in the investment rate and, in some cases, the imposition of restrictions on the activity of the private sector in certain areas. From the point of view of distribution and growth this option is subject to the same conditions as already described in the case of public enterprises; that is, it depends on productive efficiency and on the identity of the direct and indirect beneficiaries of the activities. In any event, it should be noted that in Latin America public investment -although almost always financed by taxes- has been a complement, not a substitute, for private investment. As was demonstrated in the case of some of the Southern Cone countries, a reduction in taxations, and hence in public investment, implies a fall in the overall rate of investment.

This occurs, as every economic primer will tell us, because the tendency to save the additional income is undoubtedly less than the unit. From this viewpoint, therefore, the increase in the public investment rate has given an impetus to economic growth.

In some degree the policies of support for the direct investments of the lower income groups tend to surmount another of the basic causes of poverty in Latin America. This is the lack of access of the poor to fiscal and financing capital; to the acquisition of human capital, to infrastructure and a wide range of complementary inputs. It is a question, therefore of correcting the factors which prolong this structural fault, thereby directly benefiting the target group, and at the same time creating the conditions for the gradual raising of their income level. This type of action, at a low political cost, can obtain excellent results from the redistribution viewpoint. In terms of its effect on growth, this will depend on the relative productivity of the capital in the redistribution options compared with the other possibilities of investment in the economy.

Within the investment options mentioned in the previous paragraph that of human capital should also be considered. There are some who argue that the patterns of concentration of human skills are as important a cause of inequality of income as the concentration of physical assets. Although recognising the immense importance of education -above all if this acquires a functional character strictly linked with the requirements arising from the assignment of resources- we consider that this policy like all so-called "social" policies implemented in isolation, is clearly insufficient, since in not changing the productive structure it would not affect the demand for human capital, thus maintaining the heterogeneous labour market with its "pockets" of low productivity and underemployment, with low incomes as the inevitable result.

These options of direct investment in the target group incorporate in part the traditionally accepted social policies, to which we will return later on. They should also incorporate -a fact which has not been often enough observed in the region- policies tending to support the informal urban sector and the traditional rural sector. The immense importance of these policies, from the standpoint of redistribution and growth, has been duly pointed out by PREALC and we do not think it necessary to repeat it. However, we wish to emphasize that this is probably one of the most effective ways of advancing towards the dynamic satisfaction of basic needs, above all in the political climate of Latin America today.

Finally, it is our view that from the standpoint of economic theory -including the traditional- the alteration of the patterns of concentration of assets constitutes an important instrument in promoting redistribution objectives. Moreover, empirical studies such as those carried out, among others, by Irma Adelman, have demonstrated that it is the only way to achieve a model of equitable growth.



Nevertheless, traditional economic theory has neglected this area, concentrating almost exclusively on questions concerning the fixing of prices in relation to factors and employment. This is particularly surprising when one considers that the policies for redistribution of assets, as opposed to others, fulfil the basic premises of the traditional theory concerning assignment of resources. That is to say, they have no direct effect on the price system nor on the free functioning of the market. Consequently, in terms of the Walrasian analysis, this type of policy reconciles technical and economic efficiency with social efficiency.

(b) Direct action on the factors of production market is normally aimed at varying the prices and/or the levels of utilization of the factors, thereby transforming the level of income these obtain. From a social viewpoint the object of this policy would be to increase the level of employment and/or wage of the lower income groups. As we have seen in Latin America a majority of those who cannot satisfy the basic needs are in employment, but they spend less time and effort (human and technical) than is required to produce an income adequate for SBN (satisfaction of basic needs). We are thinking therefore, of the underemployed rather than unemployed -although the latter also affect in greater proportion the lower income groups- who need to increase their income. This can be achieved through the creation of more productive jobs or through an increase in real wages. The latter, however, if not based on the former, usually has a negative effect on the employment level, resulting therefore in an uncertain surplus over the aggregate income level of the poorest.

The policies of intervention in the factor market traditionally applied in Latin America have frequently had a negative effect on the employment level. These policies have basically been of two types: those which affect the level of wages (minimum salaries and taxes on the payroll) and those which have an impact on the cost of capital (exchange rate, tariffs or import quotas and interest rate). It can be shown that both the policies of minimum wages and "pay as you earn" and those of capital subsidy -in the form of credit, tariffs or undervaluation of the exchange rate- tend to create a distortion in the factor market which results in a style of growth more capital-intensive than the available resources in Latin America justify.

The aforesaid policies, therefore, have had a negative effect on the employment level. Nonetheless, their substitution or elimination might also have possible social repercussions.

In effect, in respect of policies affecting the level of wages or the cost of labour, it should be noted that, although they have probably had a negative impact on employment, they have undoubtedly brought considerable benefit to the population employed in the formal sector of society. A reduction in real wages will only have a redistributive effect if the elasticity of technical substitution among factors is higher than one. On this point, the technological conditions prevailing in Latin America, particularly in the formal sector, would suggest that this elasticity

is inferior to the unit and therefore the elimination of the policy of minimum wages would only produce a redistribution within the working class; <sup>1/</sup> that is if the formal sector actually contracts at the levels of the minimum wage. In many cases it would seem that this is not so, since in order to reduce the cost of staff turnover the entrepreneur prefers to pay a higher wage. Evidently this considerably reduces the impact of a wages liberalization policy. In any case, this is an area where there has been practically no research that would enable definitive conclusions to be drawn on such an important matter. At the same time, the policies which tend to reduce the cost of labour -through a reduction in social lows- have a negative effect on the financing of the public sector. This could result in inflation, a reduction in the social services in the public sector or in another type of solution, -increase in income-tax or reduction of expenditure on items not affecting the poorest groups- which would not have a negative social impact.

Lastly, still referring to wages, the literature has on various occasions suggested the possibility of creating posts in public employment -which also might produce social goods or services- at a minimum wage level adequate for SBN; or, to that end the subsidizing of the free private wage to bring it up to the same level. This solution, while not introducing distortions in the factor market, has the double advantage of increasing the employment level and probably the income level of at least, some of those employed. Despite its great attraction in theory, however, the subject has not been treated in empirical studies which might determine its viability. At all events, the few studies available suggest that from a fiscal point of view at least, this option seems feasible. In the case of Chile for example, a recent study indicates that 4 per cent of the public revenue would be enough to finance, at an income level adequate for the SBN, the whole of the unemployed labour force.

Similarly, the policies of capital subsidy are regarded as a method of boosting growth and hence employment. Nevertheless, there are models for promoting growth more in keeping with the available resources and therefore more efficient and more effective in terms of employment. A case

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<sup>1/</sup> It should be remembered that the really important factor in defining the effect on employment of a wages policy is the price elasticity of the demand for labour. On this point Vine, among others have indicated that the elimination or diminution of the minimum wage can increase the total payment for wages and the employment in the modern sector and improve the equality of distribution between the workers in the modern and the traditional sectors even if the elasticity of substitution is less than the unit -always provided that the elasticity of substitution is higher than the participation of capital in the modern sector. In its turn, this argument has received a series of criticism which it would take too long to enumerate here.

in point might be the support of small and medium industries. For instance in Colombia and Ecuador there have been studies of case showing the viability of generating productive employment with an investment of 1 000 to 1 500 dollars per job, which is considerably lower than the average for the most modern and sophisticated sectors. Another study by PREALC for Bolivia reveals that the mere deconcentration of subsidized credit would have a marked effect on employment.

Finally, the highly heterogeneous character of the capital market in the countries of the region should not be overlooked. This generally results in the simultaneous existence of an undervaluation of the price of capital in the modern sector and an overvaluation in the informal and traditional sector. This situation discriminates against the use of labour in two ways: it induces a greater use of capital in the modern sector and inhibits the expansion of the sectors of small and medium industry, which make a more intensive use of labour. Consequently a policy socially (and economically) sound in respect of the cost of capital should place this on a level adjusted to the available resources at national level and furthermore, endeavour to make the market homogeneous or even introduce preferential conditions for the small and medium producer.

Closely related to the aspect described above is the third form of redistributive policy, which is concerned with technology. The state of technology determines - among other things - the level of total production and the degree of substitution between factors. This directly affects the generation of income in the factor market and the relative prices in the goods market, producing an immediate impact on income distribution and the availability of goods and services.

Nevertheless, as has already been said - and several studies have demonstrated it - technological change can have a negative effect on the lower income groups. This might occur because it promotes the production of goods which are not related to the needs of the poorest and/or because the productive process is not adjusted to the existing availability of resources. In general, the lack of technological policy in the region - although a growing interest in the subject can be observed - has meant that the technology has been taken up in countries with resources and demand structures very different from those of Latin America, and therefore its use has had a negative impact on the social question.

This circumstance has induced various States to play a more effective part in research, dissemination and information on the available technologies and in the production of capital goods. It must be remembered, however, that the countries of the region only invest between 0.15 and 0.30 per cent of the product in research, dissemination and production of technology. This figure is extraordinarily low when compared with the 1 or 2 per cent spent on the same activities in the developed countries.

This is not the moment to repeat the important suggestions made by ILPES concerning the form in which policies on science and technology

should be linked with the planning process. We wish to mention, however, that this link appears to us to be indispensable in promoting technological development in accordance with the social needs of the countries of the region.

(c) Modification of the structure of supply of goods and services

In this case the government -basically through its expenditure and investment policy- attempts to redirect production in favour of goods produced by enterprises using labour-intensive technologies and which, moreover, do not show high degrees of concentration. Likewise, an endeavour is made to induce the generation of a supply structure adjusted to the satisfaction of basic needs.

In general, the governments of the region have used this criterion to define their expenditure policy only in the case of public investment. But it could also be applied to give an impulse to those private sectors which fulfil the prescribed conditions as for example construction, agriculture, agroindustry and the basic services, which figure among the most suitable for this purpose.

An interesting experiment in this respect is that of the policy of prices of support and purchase of basic foods by the National Production Council of Costa Rica. In this case it was evident that those agricultural products which benefited from this policy were precisely those that increased their production at a greater rate. However, in some cases -sorgum, for example- the products were not directly or indirectly consumed by the lower income groups; and in others -rice for instance- though they were a basic food for those groups, they were not exactly those which were produced in small or medium farms, nor the most intensive in the use of labour. The incorporation of these considerations in the selection of the production items benefited by the public expenditure policy might have appreciably increased the social irradiation of the production growth.

In addition to the policies mentioned, the government can achieve similar effects on the supply structure by means of indirect taxes and/or controls on the production of luxury goods. Although the literature has demonstrated the difficulty in defining luxury goods, this course of action might prove to be an interesting way of promoting a convenient reassignment of resources. However, considerable further research is still needed as to which goods to boost and which to restrict, and on the effects this intervention has on the efficient assignment of resources and on economic growth.

All the foregoing indicates the great potential for redistribution in the policies of the public sector, and at the same time the insufficiencies in terms of existing empirical research and the need to correct these in order that the achievement of the social aims of the redistributive policy may be compatible with economic growth and the dynamic satisfaction of basic needs.

### 3. The correction of market imperfections

Even traditional economic theory recognizes the incapacity of the market to ensure, in certain circumstances, an efficient assignment of resources. Among the imperfections of the market there is, for example, the existence of employment and capital markets which are non-homogeneous and segmented. On this point, however, we shall limit ourselves to commenting on those situations which are schools of economics openly condemn and which should therefore motivate some kind of intervention. The remaining situations have already been discussed or will be in the following sections. In view of the wide knowledge and agreement on these obvious "areas of intervention" by the State, we shall not examine any of them in depth, but merely mention them as a matter of record, since we think that in general there is an awareness of the need to act in these areas, though very little is being done in the matter.

(a) The markets which present some degree of concentration or centralization can lead to a poor assignment of resources and an inequitable distribution of income. Traditional economic theory suggests direct action to restructure the market in question or the application of taxes. To equalize the private marginal cost with the social cost. Despite the clarity of theory in connection with the detrimental effects of concentration, this continues to exist with harmful effects, particularly in modern industry and in the financial systems of the countries of the region.

It is also clear that the concentration and/or centralization of production or demand not only generates economic and distributive problems, but also supplies instruments of political power to those groups which possess the economic power that enables them to perpetuate their privileges.

(b) The second case for intervention accepted by traditional micro-economic theory and which, in our region, is closely linked with the former, is that of the existence of economies of scale. To the extent that there are increasing returns to scale, that is, that the marginal cost is lower than the average cost it would benefit the country to increase production (if there is a market for its products) in this way to the point at which the marginal cost is equal to the marginal product. To achieve this, however, production will probably have to be subsidized to the extent of covering the difference between the marginal cost and the average.

The presence of economies of scale is frequent in modern industry. This however, because of restrictions in the size of the market, normally leads to the existence of monopolistic or oligopolistic situations. Only with this supply structure are the firm or firms in a position to expand their production at least to the point where the marginal cost exceed the average. In this way a positive advantage is reaped from the economy of scale, but its fruit are not normally enjoyed by the population. Hence

the presence of economies of scale in small markets constitutes one of the fundamental barriers to the existence of competitive markets.

A third case is that of public goods, for which a zero price is suggested and which therefore are naturally provided directly by the State or through State subsidies to the private enterprise charged with their production and production and supply. Pure air, parks, and the defence and security of the population are clear examples of this type of goods.

The States of Latin America have always directly provided certain public goods, thus benefiting the entire population. It is clear, however, that not all the population, has equality of access or of interest to "consume" particular types of public goods. The construction of roads, public beaches, a certain type of basic infrastructure, etc., benefits only the population that lives in or frequents the place in which they were constructed. When there is a great territorial inequality in the provision of these public goods -as is clearly evidenced in Latin American cities- this expenditure on the part of the State can become an additional source of concentration of income and well-being. This fact should motivate the development of techniques of assessment of the social impact of public goods, so as to give priority to those activities of more direct benefit to the lower income groups.

Another area of intervention accepted by traditional economic theory is that which has to do with the existence of externalities in the production or consumption of goods and services. A typical case of externalities in production occurs in the exploitation of certain natural resources, where the participation of a large number of producers tends to increase the cost of each one in particular (fishing, for example). Another of these cases is education where economic theory postulated that the social cost of education is less than the private cost because of the greater contribution to society that a person with a higher level of education can make.

Additionally there is the whole environmental problem which, in large measure, is created by externalities to the production and consumption of certain goods.

In all these cases economic theory proposes the intervention of the State to equalizes -through taxes and/or subsidies and/or through direct action- the private and social cost. Even so, as in the case of the provision of public goods, the benefits derived -through subsidies- from positive externalities or the compensation obtained -financed by taxes- for negative externalities can sometimes aggravate the existing social imbalances.

A clear example of this is the immense concern of the States of the region to provide mass higher education either free or highly subsidized which is mainly to the advantage of the higher income groups in society.

It is clear that the list of situations in which economic theory proposes State intervention has certain potential for improving the general well-being of the population. These forms of intervention,

however are not always guided by criteria of equity and therefore do not always lead to a more equitable distribution of income. In Latin America some types of intervention have probably tended to reinforce rather than diminish social inequalities.

#### 4. Traditional economic policies

Within this context it is possible to identify the measure of economic policy designed and applied to influence different quantitative variables in terms of the "growth with stability" objective. The achievement of this objective brings with it social repercussions. An exposition of what these are makes a useful contribution to the search for an economic growth model which will at the same time promote the achievement of equity and the overcoming of social problems.

##### (a) Policies for the promotion of production and employment

The basic principle which has hitherto defined the orientation of these policies in the region is the attainment of an adequate level and structure of investment, both public and private. This should lead to the greater possible growth of the product, given the availability of resources. According to the form adopted by these policies a specific distribution will result between the various factors of production.

For these effects the State has recourse to mechanisms which can be divided into two large groups: those of direct investment, whether in production, infrastructure or human capital; and those affecting the performance of private agents, such as taxes and subsidies, restrictions on foreign trade, credit policy, etc. Through these two main channels the State in Latin America has had a great influence on the definition of the characteristics of investment. This, in its turn, has a decisive effect both on the level and composition of the product and on the level and structure of employment and wages. Thus it has a direct effect on income distribution. Furthermore, as was pointed out in the previous section, investment defines the style of development and consequently the characteristics of dynamism and equity that the system can acquire.

The decision as to what to produce -whether to incentivize the production of mass-consumption goods or luxury goods, of goods for export or domestic consumption and in what proportion, whether industrial production with a high added value or raw-material production with little added value for example- increases or restricts the consumption capacity of the lower income sectors in accordance with the levels of employment and income generated and the range of goods placed at their disposal.

Similarly, the technology selected for use in production determines the proportion in which the basic productive factors are used. That is, the level of employment and the distribution of income which each level of activity creates.

Finally, the ownership of the means of production benefited by the new public investments or by the public incentives to increase private

investment, reinforces or alters the patterns of income distribution defined in the productive process, inasmuch as it defines the destination of the surpluses or utilities generated by the activity in question.

This set of relationships largely determines the levels and structure of employment and income and these, in their turn, have a definitive influence on the structure of demand.

Hence, the economic policy which directly or indirectly seeks to guide private investment and also to complement it with public investment has a great impact on the social structure. In this connection there can be no doubt -and numerous cases in Latin America corroborate it- that the economic and social structure which has emerged after decades of intensive public intervention leaves much to be desired from the standpoint of social equity. One cannot conclude from this, however, that the State should not intervene. Very much to the contrary, in a situation of unequal income distribution, such as that which is prevalent in the region, the disappearance of the State as a factor influencing investment would lead to even greater degrees of inequality, since the only guide to the assignment of resources would be the prevailing demand structure which in its turn, would clearly mirror the existing inequalities and basically represent the preferences of the higher income groups.

Public intervention, therefore, is necessary for the guidance of investment and growth. This action, however, should keep in view the objectives of redistribution and the conditions needed to obtain them as presented at the beginning of this chapter.

#### (b) Income policies and fiscal expenditure

As we have said, these are used in part to correct a series of phenomena of an economic nature which the market by itself is not able to control. Among these are activities which directly affect the social milieu such as education and health, and others which have an indirect impact.

Fiscal policy affects the social problem in two ways. The first, as we have shown, depends on the destination of expenditure, the second, on the origin of fiscal revenues that is, on the taxation structure.

(i) With regard to the sources of public revenue or taxation policies, there have been several studies on the effects of taxation which attempt to establish the way in which taxes affect the different social groups by their effect either on their income or on their expenditure. These studies have enabled us to define with relative clarity the conditions which could lead to an equitable tax structure. Among these the following may be mentioned:

- There should be an increase in the proportion of total fiscal revenue derived from personal income tax. This is undoubtedly the most progressive tax but it generally represents only a small fraction of the total revenue.

- The same might be said of taxes on property. In general these are insignificant in the countries of the region. Particularly important



in this respect is the designing of adequate systems of land taxation which would improve the use of the land and reduce the economic profit derived from the mere ownership of this asset.

- In general, taxes on consumption which today finance a significant portion of expenditure, are regressive in character; that is they have a greater impact on the lower income groups.

- Taxes on sales appear to be neutral. Even so, neutrality when it is a matter of correcting the existing income distribution is regressive in character.

- There should be an increase in the contribution of taxes on inheritance and on donations which at present represent a negligible percentage of the tax structure. This is particularly important since inheritances and donation constitute a privileged institutional mechanism for the transference of inequality.

The above-mentioned studies agree in also pointing out the regressive character of the tax burden in most of the countries of the region. These statements of a general nature should certainly be validated and individualized in the case of each country. The researches already carried out are of a macro and subregional nature and should therefore be complemented by more specific studies on taxation effects.

(ii) In respect of the incidence of fiscal expenditure there are relatively few studies, and generally those which exist do not examine the situation in Latin America. The only studies on Latin America deal with Colombia, Chile and Ecuador. These studies indicate that the expenditure -and specially the social expenditure- in on the whole progressive or rather messocratic in that the average benefit per family is less for the poorest groups. In other words, 60 per cent of the lower-income population receives less than 60 per cent of the benefits of public expenditure. It is also noteworthy that in the countries analysed both the taxation system and the fiscal expenditure are more regressive in character than in the developed countries. For these reasons it appears urgent to introduce clear criteria as regards the equitable character that public expenditure should assume in the region. Various studies have referred to the regressive character of the large sums assigned to general expenditure (administration, defence, etc.) and to certain public programmes (promotion of the production of certain goods, provision of infrastructure for transport and of air and road transport in itself, etc.). On the other hand mention has been made of the progressive character of the greater part of "social expenditure" (health, food, housing, etc.). At all events, we shall return to this aspect in discussing the economic dimension in social policies.

There are basically two types of price policy. The first aims at a greater stability, which ought to have -depending on the instruments utilized- a positive effect on income distribution, since inflation tends to be regressive. Nonetheless, the importance of the stabilization programme has to be offset by the social impact of the reduction of

inflation. It is clear that, as in the case of Chile, the counterpart of stabilization is a drop in production levels, in employment and in real wages, which negates any redistributive effect of the programme. The second attempt to solve certain social problems by fixing the prices of the goods or services which have an important place in the shopping-basket of the lower income groups.

In connection with this second form of intervention in the price system, there has been a lengthy discussion. On the one side it is argued that prices, in competitive markets, reflect relative scarcity, since to ignore and distort this "signal" is prejudicial to the social objective of the efficient assignment of resources. On the other side it is contended, and rightly, that in general the markets are not competitive. Evidence of this is the segmentation in the labour and capital markets and the existence of concentration and centralization in various markets of goods and services, both in respect of supply and demand. In addition to these distortions incorporated into the price system there are the cases, already referred to, of externalities, public goods and economies of scale. It seems, therefore, that there should be some form of intervention to achieve a degree of social efficiency in the assignment of resources. This intervention, however should not necessarily affect the goods which form part of the basic shopping-basket. To extend the consumption of this type of goods it seems preferable to apply subsidies which do not generate distortions in the price system and therefore do not impede the efficient assignment of resources.

In respect of the stabilization policy, it is generally argued that this benefits the lower income sectors. At the same time, however, it is pointed out -and experience corroborates it- that there is a certain "trade-off" between stability and employment. All those anti-inflation policies which generate high levels of unemployment will have a regressive impact on income distribution. A clear example of this as had been said before, is what happened in some Latin American countries during the last years of the 1970s. On the other hand, the high inflation rates which affected most of the Latin American countries in the middle of the past decade clearly indicated the regressive character of the inflationary periods.

It would seem, then, that there is a difficult field of manoeuvre between the problems of inflation and unemployment. To ignore the importance of either would have unfavourable consequences for the lower income groups. This last fact indicates the urgent need -which has not been generally observed- to analyse in detail the social impact of the policies both of stabilization and expansion so that they can be compared and suitable action taken.

(c) Foreign trade policy covers such a large number of aspects -some of which have already been mentioned- that we can only refer in broad outline to the relations of one or another of these with the social problem.

The different types of exchange policy (fixed exchange, free or floating rates), for example, have different effects on inflation and thereby influence income distribution. An exchange policy which has, in the medium and long term, a lesser inflationary impact, and which obviously does not signify the existence of external uncontrollable imbalances, will be more progressive than one which generates more inflation. Furthermore, the over or undervaluation of the real exchange rate, the former being expansive and the latter depressive, will affect the sectors dealing in exports and import substitutes, and hence the level of employment and remuneration.

In its turn, the tariff policy affects the consumer goods available to the population. In a free market the access to imported goods will be in terms of income distribution, since this will determine the structure of demand for imports. For this reason, given the inequitable character of income distribution in the countries of the region, it is at least probable that the free market leads to high levels of luxury consumption. This not only fails to benefit the lower income groups, but it can also be to their detriment in that a proportion of scarce foreign assets is used for this type of consumption instead of for obtaining capital goods to increase production and employment. Similarly, the fixing of high tariffs may have kept many national enterprises functioning at low levels of efficiency with a resulting loss to the consumer in the sense that he might have obtained the same goods at a much lower cost.

Additionally, in many cases, these high tariffs have created a bias in favour of the import of capital goods which are unsuitable for the resources available in our countries. This has affected the relative use of productive factors and, hence, the level of employment and the distribution of income. Thus, although we are convinced that some level of protection is necessary, both from the argument of the "infant industry" and from considerations of political autonomy, it must be borne in mind that excesses in this field can have a high social cost.

Considerations of this kind are also relevant in respect of the volume and areas of foreign investment. In this case, moreover, consideration must be given to the problems of alternative availability of capital as a substitute for credit or foreign aid the problem of national appropriation of surpluses and the contribution of "know-how", which these investments imply. These considerations can have the effect of maximizing the social benefit of foreign investment or of restricting it in certain areas.

## 5. Construction of indicators expressing economic and social progress

When economic and social development is thought of in integrated form the need at once arises for indicators to express social progress.

It was more than ten years ago that Dudley Seers, in discussing the meaning of the concept of development asked himself: "What are we trying to measure?" His reply was: "The capacity of a man to develop himself to the full". Development, therefore, according to this author, should be assessed according to the following criteria: whether there has been a reduction in (i) poverty; (ii) unemployment, and (iii) inequality. From this standpoint he criticized the gross national product as the only development indicator, since this can grow without any improvement in the areas mentioned above.

As already said, the situation in Latin America has shown that good economic performances are not necessarily accompanied by an improvement in the lot of the great majorities; in fact, there are cases where this has worsened. Hence, it is particularly important to have indicators which will effectively express economic and social progress.

To this end there have been proposals from many sources. Among others we might mention the indicators of basic needs used -among many- by Drewnowski: the "rates of reduction of social disparity" designed by Grant; and the "index of the physical quality of life" proposed by Morris of the Overseas Development Council. It is clear, therefore, that methodologies exist which might replace or at least complement the present inappropriate development indicators.

With this in view it will be necessary, apart from enlisting the good will of the governments of the region, to answer many questions -especially those of a microeconomic nature- which we present in the following section in discussing the economic dimension of social policies.

#### IV. ECONOMIC CONSIDERATIONS IN THE DESIGNING OF SOCIAL POLICY

##### 1. General exposition

Before suggesting the type of economic considerations which should be taken into account in the designing of efficient social policies we must lay emphasis on the systemic character of every social problem, and this, in a double sense, in its interrelation with the rest of the economic system and likewise in its interrelation with the rest of human needs.

##### (a) The systemic character of social problems

All the social problems that are rooted in the fact that a social group has no access to a range of "satisfiers" of a basic need (food in the case of nutrition, dwelling and basic infrastructure in the case of housing, for example) can be understood to be inserted into a chain or system of production, distribution and consumption of the said satisfiers. The systemic character of the social problem, in terms of the economic process as a whole, is therefore related to the range of macroeconomic interrelations implicit in the origin and search for solutions of the social problem. The housing problem, for example, must not only be thought of in terms of the number of square meters per person -or rather traditional indicators for measuring the satisfaction of housing needs- which have to be built up, but in terms of all the inputs required, their internal or external availability, the construction technology suitable for the raw materials and labour available, the financing system, etc. In other words, it is a case of inserting the solution of the social problem into the chain of production-distribution-consumption of "satisfiers" of the basic need in question.

##### (b) The complementary character of the process of satisfying basic needs

The second form of overall interrelation to be taken into account in designing a specific social policy is concerned with the so-called "social areas". The need to think of the relations and interdependence of the different basic needs arises from two factors which have been stressed in numerous studies on the subject. The first of these relates to the complementary character of the process of satisfying basic needs. In other words, the joint provision of "satisfiers" of different needs multiplies the efficiency of each individual satisfier. For example, if the nutrition programmes include the provision of certain basic sanitation services, it has been estimated that the amount of food needed to achieve a satisfactory level of calories and nutrients drops by approximately 15 per cent, since adequate sanitary conditions increase the capacity of absorption of the calories and nutrients contained in the food.

The second factor referred to above is connected with the overall deficit of "satisfiers" in the lower income groups. This global deficiency makes it necessary to elaborate "packets" of social policies

having a complementary character, since the target group itself tends to redistribute the benefits of a direct social policy towards other expenses. For example, if an official policy concentrates on the distribution of food packets it is probable that the target group will reduce the amount of food it bought before and use the surplus income for the purchase of other basic goods or services. Obviously in this case the effect of the complementary food policy on the state of nutrition would be nil or negligible. On this point it should be noted that only the poorest groups are deficient in their overall basic needs. The rest of the population which in some degree has unsatisfied needs will only show deficiencies in some of them, and therefore the packet of policies will be inefficient in economic terms since it will provide goods and services that are not strictly necessary. This situation indicates the need to define as precisely as possible the characteristics of the target-group for social policies.

In general, social policy in Latin America has not been systematically thought out in either of the two senses just discussed. This is probably one of the basic causes of at least two of the problems invariably involved in the implementation of these policies. The first is the very high cost of reaching a member of the target-group with the adequate amount of goods and services. This occurs basically because of the poor definition of the normal target-group and, as a result, the considerable filtrations to which these programmes are liable; and further, because of the displacement of the benefits towards other unsatisfied needs of the target-group. The second problem usually encountered by social programmes is the scarcity of resources or the appearance of "bottlenecks" which hamper the execution of the programme. In many cases this occurs because insufficient consideration has been given to the need for resources and the chain effects (especially backwards) that the provision of these resources will require. Thus unexpected "bottlenecks" arise which halt the execution of the programme or increase the cost of its implementation, making still more scarce the resources which in most cases are already in short supply.

(c) The macroeconomic impact of social programmes

The third and perhaps the most important reason for undertaking social planning in a systemic form is connected with the macroeconomic impact of social programmes. The problem of unsatisfied basic needs is so great in Latin America that its solution requires -and in fact implies- the mobilization or transference of resources in sufficiently large quantities to generate profound macroeconomic effects. Indeed, public expenditure in the social field represents an average around 10 per cent of the gross domestic product of the region. Its financing, therefore, can have an important effect both on the income of the poorest and on the savings and investments of the richest, that is, of those who run the so-called "modern sector" of the economy (depending on the social impact of the taxation policy). This social expenditure can also have significant effects on the price system (depending on the size of the public deficit

and the relation between the structure of demand and supply of the goods and services required by the public sector).

In addition to these questions, there is traditional concern about the alternative cost of present consumption, namely investment and consequently growth. In recent years there has been a large number of studies -mainly theoretical and not necessarily referring to Latin America- on these topics. Most of them concur in pointing out that a substantial increase in public expenditure -enough to satisfy basic needs- would result in a slight decrease, in the short term, in the growth rate of the product (1 or 2 per cent) which could be offset by an increase in foreign indebtedness or by emission with its resulting although slight inflationary effect. All these studies -among which mention might be made of those by Lance Taylor both for their representativeness and for their quality- also coincide in indicating the importance of producing an initial redistribution in financial, physical and human capital to enable the economic system to acquire a dynamism that would strengthen the equitable character of growth. This is because income distribution by stages seems to be more difficult to alter by means of direct social policies. Hence, unless action is taken on the mechanisms determining the primary distribution of income, the system -in effect the market- will reproduce and reinforce the structure which existed before the public intervention in the final distribution of income.

Lastly, the studies carried out on the subject also point out that a partial analysis (whether it be on the effect of isolated policies or involving only some of the productive sectors) tends to lead to incorrect conclusions on the impact of public intervention in the social field. If the analysis is made on the economic-social system as a whole, important differences can be detected in the impact produced by specific programmes, not only in respect of size but also in the direction, of the effects. This occurs because the effect of the interaction of policies -not only social- is important; that is to say, the result of the application of public policies taken together is different from the sum of the components of each one. These conclusions, therefore, tend to reinforce the need to use a systemic approach to planning for the satisfaction of basic needs.

Although the theoretical literature on social planning has in recent times repeatedly stressed the urgent need to use this systemic approach, little or nothing has been done in Latin America in this respect. This has had the twofold effect of conserving a sectoralized style of social policy which is known to be inadequate and inefficient and, at the same time, of inhibiting progress in the formulation and subsequent application of empirical models which take account of the range of interrelations existing between the social and economic variables. A noteworthy and significant exception to this is the recent announcement and implementation of the "Mexican Nutrition System". This is probably the only experiment in social policy in Latin America that has taken into account the need in a mixed economy, to relate systematically the different variables

mentioned. The excellence of this experiment and of the concept of a nutrition system may become an example of what the Latin American countries could do in this field.

The effective integration of the solution to the social problem or what we shall henceforth regard as synonymous with the satisfaction of basic needs within a systemic framework, requires the elucidation of various uncertainties. The great majority of these refer to the interrelations between the satisfaction of a single need or of basic needs in general and the economic problem. We shall now attempt to indicate the basic questions which arise -given the experience in the implementation of social policies or the theoretical studies of research-workers- in attempting to establish and define this interrelation. To facilitate this exposition we shall discuss independently the considerations and interrelations of a macro-economic and microeconomic type. Lastly, a basic aim which we shall keep in mind in making this exposition will be to point out what are in our view the chief gaps in terms of the designing of efficient social policies.

## 2. Macroeconomic considerations in the designing of social policies

### (a) Calculation of the magnitude of resources required to solve the social problem

This is probably the field in which, thanks to the CEPAL project on "Critical Poverty", there has been most progress in Latin America, but there is no doubt that much remains to be done. It seems unnecessary to demonstrate the importance of having a clear idea of the size of the problem to be overcome; this is necessarily the first step in defining the form which the actions destined to solve the social problems should take; the periods in which they will be solved; their viability; the proportion of available resources required and, consequently, the impact these programmes can be expected to have on different macroeconomic variables (basically investment, prices, foreign trade and growth). Without this type of information it is impossible to envisage genuine social planning. The few indicators available today, however, are based on a type of information which makes them highly suspect. This is fundamentally because of the quality of the basic information, but also because most of the indicators constructed have used an indirect method of calculating gaps, which is by means of income, or rather, of family expenditure on "satisfiers" of basic needs. It does not seem necessary to repeat here the possible defects of this type of indicator and the consequent need to make efforts to construct indicators of gaps based on the actual consumption of "satisfiers".

(b) The foregoing takes us directly to the second topic, which is the improvement and systematization of statistical information. The direction of this improvement should derive, moreover, from the already mentioned problem of the quality of information in terms of the systemic approach explained above. This means an integration of the currently uncoordinated



information on the production and consumption of satisfiers and the addition of a system of classification by social groups. An excellent general framework for the definition of the type of information required is the so-called "Matrices of Social Accounting" which unfortunately has received little attention in Latin America.

The importance of producing a linkage in the compilation of information on the production and consumption of "satisfiers" is clearly illustrated by the following example on the nutritional situation in Costa Rica. By the middle of the 70s the information on domestic supply and availability of foodstuffs (balance sheet) indicated that this had increased considerably; but the information on consumption (surveys on family income and expenditure) showed that this had appreciably decreased. In view of the models for compiling and producing statistical data in Costa Rica -as in all the Latin American countries- it is absolutely impossible to compare these two figures and hence to reach a conclusion as to what is really happening with regard to the nutritional problem in that country.

(c) Once the statistical information system has been integrated a matrix of social accounting could be constructed which would explain the inter-connections found between the productive system and demand structure on the one hand and the situation of different social groups on the other. This would enable a great advance to be made in planning for the satisfaction of basic needs.

This type of information, organized in a matrix of social accounting, could determine, for example the impact of an increase in the supply of popular dwellings on production, the consumption of other goods or investment in the sector and on the economy as a whole. Or from the other standpoint, it would be possible to determine the impact of changes in different economic variables, such as production, modalities of marketing or patterns of consumption of one particular need, such as the nutritional state of individuals or at least of households disaggregated by social groups and geographic regions.

Traditionally when these relations have been established, it has been done in a partial manner. For example: what is the effect of a housing subsidy on the demand for dwellings? Or: How does the supply of foodstuffs increase when the State fixes a "support price"? This type of partial analysis obviously provides only partial replies and thus conceals important aspects such as -returning to our examples -the effects of the policies on the nutritional state of the target-group or in the characteristics of the housing of the same group. Furthermore, it conceals all the indirect and basic effects of these policies on, say, employment, investment, the availability of foreign currency, etc. Most of these effects could have an impact on the target-group equal to or even exceeding that of the social policy itself, and, what is more, not necessarily in the same direction.

(d) This last point leads us directly to the need for planning models. The traditional models of general balance or imbalance would have to be

complemented, of course, by considerations proper to the analysis of basic needs. Among the most important of these are the linkages between the satisfaction of needs and the achievement of economic results. There are various studies which show, for example, how labour productivity increases when the nutritional state of the workers is improved; and others which indicate the relation between the development of human capacities and the stimulation received (through education, basically) in the early years of life.

Moreover, among other things, the dynamic character of needs must be incorporated, that is, the fact that they change in the course of time. Only thus can these models offer great advantages for the analysis of the effect of the different social policies on the economy as a whole, and reveal the great impact of a social policy on the target-group, and hence assess its usefulness. We have already mentioned that a social policy does not only bring direct benefits to a fraction of the population but also indirectly affects the population as a whole. The direction of this indirect effect will depend, among other things, on the form of financing of the policy (if it is taxation it could affect the level of income and/or of savings of the poorest groups and, on the other side, the capacity or will to invest of the richest groups; if it is through emission, it would affect the stability of prices and, through this, the income level of the groups with less negotiating power, etc.); on the effect on employment -direct and indirect- that this could have; on the quantity of imported resources required; etc. On many occasions these indirect effects can have an impact as great as, or greater than, that of the direct action on the target-group and sometimes in the opposite direction, thus halting the effects of the social policy on the aims for which it was designed. Moreover, the dynamization of these models discloses the total effect of these policies in the long term.

Finally, the construction and use of these models makes it possible to assess the relative efficiency of different policies; to foresee the effect of the absence of social policies and to calculate the volume of resources that should be assigned to achieving as rapidly as possible the satisfaction of basic needs. The failure to use this type of instrument has probably been one of the basic causes of the collapse of great projects of social reform undertaken by progressive governments in Latin America. On many occasions these social goals have resulted in inflation or stagnation of investment, or an intensification of the problems of scarcity of foreign currency or growth of external indebtedness. We are convinced that a general and systematic analysis of the requirements and impacts of a programme of social change could be of great help in avoiding these problems.

In Latin America various models of this type have been designed which would help us to visualize the overall impact and relative efficacy of different social policies. In Colombia, Brazil and Ecuador, among others, dynamic simulation and long-term models have been or are in process of

being completed which include subroutines on demography, economy, employment, distribution of income and of consumption and satisfaction of basic needs, and which would permit the assessment of the relative efficiency of different economic and social policies and of global development policies in terms of the achievement of the social goals of growth.

These models, however, have usually been developed by research institutes or international organizations -especially the Institute of Social Studies of The Hague and the ILO- and have not yet been formally adopted in official planning circles. The search for a greater integration between national and international circles and a closer link between the researches made by international bodies (inside and outside the region) and the planning offices and agencies responsible for implementing social policies can be very useful for the designing and adoption of this type of model.

### 3. Microeconomic consideration in the designing of social policies

From the microeconomic standpoint there are two large areas of attention that help towards the efficient definition and implementation of social policies in the systemic context which we have in mind. The first relates to the technical and productive characteristics of the units responsible for the process of production and/or distribution of satisfiers of basic needs. The second concerns the determinants of the patterns of consumption of satisfiers by the target-population and the relation between the consumption of these and the degree of satisfaction of basic needs.

As in the case of the macroeconomic considerations for the designing of social policies the criteria and suggestions we wish to present by way of example are valid both for the design and for the assessment of social policies. This is because the criteria and objectives used in the designing of policies -especially when emphasis is laid on the efficiency criterion- should be the same as those used later for the evaluation of the efficiency of these policies.

#### (a) Microeconomic aspects of the production and distribution of satisfiers

This is probably one of the areas where there are the greatest gaps in the knowledge of the Latin American situation in relation to the designing and implementation of social policies. In general economic and social development theory has made little attempt to ascertain the elements which determine the performance of the economic agents responsible for the production and distribution of goods and services, and in particular the incentives or disincentives which really motivate changes in the performance of these units. Nonetheless, Latin America is rich in experience of policies destined to produce changes in the performance of the private producer or distributor (subsidies, price and/or standard fixing, rationing or fixing of quotas, tariffs, etc.) and also in

experience of public action aiming to substitute or complement private action directly (marketing claims, free distribution of goods, financing or production programmes or direct provision of satisfiers, etc.).

These experiences undoubtedly offer a rich field for investigating the relative efficiency of the different forms of intervention and the importance of taking action in these areas. These inquiries however, can only be dealt with in a really thorough manner by means of empirical research, since there are no instruments or information which could permit a prior assessment of the efficiency of these policies or forms of intervention.

In addition to the intervention policies aimed at inducing or substituting private sector action there can be actions destined to complement it. An example of this is the activity -still by no means sufficient- that in most of the countries of the region has been initiated by the "National Science and Technology Councils", or the international agreements concerning price stability and supply of certain basic consumer goods (particularly food). Once again, however, there has been very little research on the incidence of this type of policy on the agents responsible for the production or distribution of satisfiers. At all events, there are some studies on these topics which constitute a good guide for their future development and, moreover, demonstrate the usefulness of continuing the effort of research. As an example of these there are the studies on the subject of the so-called "green revolution". This topic is particularly suggestive because it deals not only with the procedure for considerably increasing the supply of basic foods by means of new technologies, but also with the effect of these technologies (improved seeds and use of synthetic fertilizers and herbicides) on aspects of production which had profound social significance. The reason for this, among other things, was that they were neutral in terms of scale of production and therefore it was assumed that they could be utilized by small farmers, which would permit a more rapid increase in the income level of the marginated groups of the population.

A detailed study on the subject however, disclosed that the idea of a "neutrality of scale" was mistaken. In fact, the new technologies were capital-intensive and therefore required a working capital and additionally a series of complementary investments (fundamentally to regulate the supply of water). The productive and institutional conditions of the small producer made it difficult for him to utilize the new technologies since he had not the capacity for saving or indebtedness. Moreover, certain scruples of a "cultural" nature were detected when it came to introducing radical and drastic changes in the productive technologies used. In short, most of the studies conclude that the green revolution tended to polarize still more the social difference in the rural areas, thus largely dissappointing the original expectations.

There is still a need, however, to ascertain the nutritional impact of these policies and how this compares with the results achieved by direct policies of complementary feeding or others of the same type.

(b) Microeconomic aspects which define the pattern of consumption of satisfiers

This is a problem which has traditionally occupied an important place in economic theory. Notwithstanding, the concept of "rational economic man" -he who takes decisions which maximize his gains- which informs traditional economic theory on the one hand and the insufficiency of statistical information on the other, have hindered the development of a conceptual frame which would explain more globally and organically the performance of the consumer.

The situation in our region, moreover has demonstrated the invalidity of this concept of "rational economic man", at least in respect of the consumption of satisfiers of basic needs. There are innumerable cases in which goods, which are indispensable for human development are neglected, whereas others which apparently at least, are superfluities are consumed. Furthermore, many cases are observed of poor distribution of satisfiers within the home; the classic example of this is the case of those families in which there is an overfed adult (usually the wage-earner) alongside an undernourished child. Indeed, there are countless problems of this type which demonstrate the need for more detailed study of the motives which determine the preferences of the consumer.

With reference to the consumption of satisfiers of basic needs there are at least three areas which it would be advisable to study in more detail.

(i) The relation between modernization with its demonstration effects and the consumption of satisfiers of basic needs

Traditional theory contends that it is relative prices and the level of consumption that determine the performance of the consumer. Practically all the other social sciences have concurred in pointing out the importance of other elements such as education, propaganda and in general, all those connected with the socio-cultural conditioning that society exercises on individuals. There are several studies, including some by economists, which tend to support the latter proposition. By way of example, mention can be made of a recent study on the patterns of food consumption of the indigenous population of Mexico and Guatemala.

The conclusion is reached that to the extent that these communities were "penetrated by civilization" there was a rapid substitution of the traditional foods by others whose cost per unit of calories and nutrients was generally considerably higher. Even so, these foods (white bread, for example) represented a symbol of progress. This substitution process in every case would result in the generation or intensification of the nutritional problem.

A clear identification of this question seems important for the understanding of the overall impact of modernization and for defining the relative efficiency of policies of redistribution by way of money-income, goods or education and training. There are countless policy experiments which offer a fertile field for these investigations. For instance, as already mentioned, the effect on employment and income of the green revolution or the programmes of integrated rural development seem to be relatively well defined. It would cost little, therefore, to analyse how these resulted in an increased consumption of satisfiers and, through these in a greater degree of satisfaction of basic needs.

(ii) Distribution within the home of the consumption of satisfiers

In general the measurements of the degree of satisfaction of basic needs disclose important differences between the age groups, and, further, that it is the passive portion of the population that is most often affected by the lack of satisfaction of their needs. Though it is true that all this appears to be corroborated by the studies on the subject, there are on the whole no researches which explain the reasons for this phenomenon and thus point out the courses of action required to overcome it.

This shortage of studies on the subject has meant that nutritional policies, for instance, are increasingly aimed at a specific age group. This in its turn implies that the costs per beneficiary increase as much as the coverage of the programmes tends to diminish, probably, to a lower level than when subject to all kinds of filtration. Thus we see that in most of the countries of the region non-selective programmes subsidizing food and distribution of milk (subject to filtrations and displacements) have given way to programmes of distribution of fortified foods (which by not being mass-consumption foods are less liable to filtrations, but are also less consumed by the target-group and continue to be affected by the problem of displacement) and, lastly, to canteen programmes, which are more than five times as expensive (per caloric unit per beneficiary) as the initial programmes.

Investment in researches which would result in progress in this field, although these are costly and complex, would probably yield high returns through the volume of public resources that would be saved and because they would ensure an effective penetration to the target-group with the satisfiers they need and are prepared to consume.

(c) Microeconomic aspects of the relation between consumption of satisfiers and satisfaction of basic needs

The literature on the satisfaction of basic needs has traditionally distinguished between two types of indicators: those of input and those of result. The former relate to the amount of goods and/or services that should be "consumed" so that a person satisfies his needs (for example, daily calories per capita, square meters built per capita, etc.); the latter relate to the actual situation in the satisfaction of needs (for example, anthropometric measurements of the population, degree of crowding, etc.). In most cases, and basically determined by the type of

statistical information available, use has been made of the input indicators as representative of the result indicators, which are those which it is of real interest to know. The relation between these two situations (input and result) is however, very complex, and indeed on this depends the efficacy of a policy which by providing inputs expects to achieve certain results. Consequently an adequate knowledge of this relationship is essential for the designing and evaluation of social policies. Among the most important aspects that should be investigated in order to define this relationship are the following three:

(i) Definition of standards of satisfaction of basic needs

Standards or norms constitute the basic information for the all-round planning of basic needs. For this reason there have appeared several studies in recent times proposing such standards for the various basic needs. These studies however, are still incomplete in the sense that they only refer to certain needs (food and in some form health and housing) leaving to "value judgements" the definition of the rest. This is especially complicated when definitions are made for populations on average when in fact, they are enormously heterogeneous.

There can be no doubt that standards of basic needs vary according to the type of work, the region in which the people live, certain characteristics of a cultural nature, etc., and hence it seems impossible to think of homogeneous standards for countries and indeed for Latin America as a whole, as some studies propose. Only when the specific characteristics of each group are taken into account is it possible to construct better indicators of result.

In addition to the lack of representativeness in many of the standards used today there are also certain problem in the form in which they are elaborated. The first and most important is that they are founded on value judgements which, in many cases, may not represent the real interests of the community and the target-group. The adoption of these value judgements should be based on participation, so as to effectively represent the needs felt by the population. Moreover, although there has been a certain degree of technical sectoralization in the definition of standards (nutritionists define food standards, physicians health standards, etc.) the truth is that the relation between input and result depends on many factors which are outside the scope of any single discipline.

An effort, therefore, must be deployed which is multidisciplinary, participatory and based on a profound knowledge of reality, in order to define the standards which will enable the gaps in the satisfaction of needs to be assessed and a range of actions devised which will close each gap.

(ii) Constant evaluation of the satisfaction of basic needs

This evaluation should be made in such a way as to ascertain the progress of the target-group on receiving the benefits of the social policies and at the same time discover how and through what factors

-apart from direct action- the satisfaction of the basic needs is significantly affected in the short term.

These tasks have been seldom performed in Latin America. The reasons for this might be, first, because in most cases there are no adequate methodologies for doing the work and secondly, because most of the social programmes have not been formulated on the basis of an evaluation of the degree of satisfaction of basic needs. Thus although indicators of result exist, there is nothing with which to compare them.

Fortunately, in recent years there has been appreciable progress in the definition of indicators and instruments which are serviceable for tracing the course of the situation of the population. As an example there are the periodic studies on health and nutrition produced by many of the Ministers of Health in the region. As yet, however, there has been practically no study in depth on, say, the macroeconomic linkages between the different social problems or the microeconomic details of the state of satisfaction of basic needs of the different social groups. This hampers the designing of really efficient policies and limits the knowledge of the effect of the policies implemented.

An interesting step in this direction, though limited in scope was the elaboration for Brazil, Costa Rica, Chile and Panama among others, of Maps of Extreme Poverty. These studies however, have been made only once and it seems that there was not sufficient interest to keep them up to date. Keeping them up to date would enable the efficacy of the policies to be assessed and new areas defined where direct action is necessary.

(iii) The economic consequences of social problems

One of the criteria which can best serve to guide decisions on social policy is that of the economic consequences in terms of lost production or a decrease in the growth rate attainable, lack of satisfaction of basic needs or failure to solve social problems in general.

The advances made in the region in the field of measurement or forecasting of the economic consequences of social backwardness have been very limited, attention to these being confined to very partial aspects. Indeed, the studies on this subject usually refer to a restricted (and therefore unrepresentative) social group or to a particular problem or need.

Even so some significant progress has been made, especially in the areas of health, education and nutrition. In education, for example, many countries of the region have adapted international measurement scales (such as the Gessel or the Terman Merrill) to measure the motor development of social language and of intersensory organization. The application of these measurement scales has revealed a marked correlation between the degrees of development in the different areas and the levels of income.

It would therefore be feasible to have quantitative approximations on the effect on production of a certain degree of satisfaction of basic needs, measured by income level. In the case of nutrition, various studies have shown that caloric-protein undernutrition and deficiencies in the



consumption of iron and codine can have a marked effect on a person's mental and physical development and hence on his capacity for economic production. The same studies have shown that undernourished children have a response level lower than the stimuli of their environment, a factor which undoubtedly affects their learning capacity and hence their psychomotor and social development. These interrelations, however, have not been utilized as fully as they might have been, so that definite conclusions cannot be drawn as to the effects for example, of the nutritional or educational problem on different economic variables.

At all events, the researches coincide in pointing out that the failure to satisfy a basic need (especially in the first years of life) definitely marks an individual in terms of preventing him from fully developing his potentialities. There can be no doubt that this is a negative externality of the social problem whose cost is not only paid by the person affected but also to society as a whole. The magnitude of these costs -although in view of our very low level of knowledge on the subject it cannot be regarded as the only criterion- ought to bring about an advance in the definition of standards of satisfaction of basic needs, in the definition of the volume of resources destined for the solution of the various social problems and in the priority given to these actions.

Finally, it seems important to mention the studies on these topics initiated by Julian Steward. An attempt is made in these to integrate all the determinative aspects and the consequences of the nutritional state in a model of society as a whole. This activity, though difficult and costly, has the great advantage of avoiding the errors of omission of the focalized and sectoralized studies which have been made in the region.

These topics have received the attention of social and biological scientists in recent years. There has been a marked absense of economists, however, in these researches. This may be partly explained by the fact that the said researches deal with subjects which normally lie outside the scope of economics. Nonetheless, considering that the results of these researches are, or rather should be, used by economists in planning actions aiming to solve social problems, it seems essential that they should play a more direct part in the interdisciplinary enterprise needed for the definition of standards, the monitoring and the study of the economic consequences of social problems.

#### 4. Criteria for the economic evaluation of social policies and programmes

The basic criteria for evaluating social policies from an economic standpoint have now been presented. It remains to define the methodology of evaluation most suitable for utilizing these criteria. We can think of three ways of tackling the problem: cost-benefit analysis; the "planning balance" developed by Lichfield; and cost-efficiency analysis.

These methodologies are still deficient in some respects, the basic reason being the difficulty of quantifying in monetary terms the impact of social policies. They seem, however, to offer a good starting point for the development of a task -such as evaluation- which is fundamental for achieving a substantial improvement in the efficiency of social programmes.

This economic assessment of social programmes needs very special attention, both because of the importance of an efficient use of available resources, so scarce in relation to such urgent problems, and in order to give a greater impetus to the authorities and society in general to find a solution for these problems. This last involves the countering of the view held by many today that funds allotted to social assistance are a form of charity which brings no benefit to society as a whole. Let us see, what methodologies of evaluation are available today.

(i) Cost-benefit analysis, particularly in its version of the social assessment of projects, is probably the most complete and ambitious methodology for measuring the efficiency and equity of social policies. In practice, however, it runs into several problems. The first of these is that the greater part of future benefits cannot really be measured in monetary terms, either because they are unknown (product of ignorance of the results of the lack of satisfaction of needs) or because they are intangible (the evaluation, for example, of a housing programme aiming to create a friendly and peaceful neighbourhood); and there are others which for very good reasons are not considerable measurable in money (life, for example). Apart from this serious problem of the impossibility of measuring certain benefits in money terms, it must be remembered that to achieve a "maximum of efficiency" a function of cost and benefit must be defined. The definition of this function creates even more problems for its calculation, especially that of benefit; but here we shall only refer the reader to the abundant literature on the subject.

Another basic problem for cost-benefit analysis is that of equity. To deal with this, the use of distribution weightings has been proposed; that is, that those goods or processes which benefit the lower income groups more than proportionally should have their "value" multiplied by a specific weighting. The calculation of these, as has frequently been shown in the literature, can have no objective basis, so that value judgements are employed when using them.

It would seem, then that the social evaluation of projects presents an interesting methodological scheme, but still insufficient for the assessment of social programmes and policies.

(ii) The "planning balance" aims to establish the profits and losses for particular groups arising out of the programme or policies. This scheme has many of the disadvantages of the cost-benefit analysis, but, in not attempting to achieve a "maximum" but only to specify the groups which will gain or lose, it suppresses at least the use of general distribution weightings.

Moreover, this scheme can be expanded to incorporate the indirect effects of investment on social activities, as already described in the case of the matrices of social accounting. In this sense this methodology is rather a form of organizing existing information than a list of criteria for assessing or deciding between the alternatives of social action.

- Cost-efficiency analysis has been used in various countries to measure the relative efficacy of a project or programme in achieving a specific standard, and is basically a simplified version of cost-benefit analysis. In face of the impossibility of measuring benefits, a standard is determined (in terms of a completely inelastic benefit at a certain level) which an attempt is made to reach at a minimum social cost. In so far as the cost of the projects and programmes is effectively measured at social prices efficient solutions will be obtained.

This alternative seems to be the most realistic in view of the type of information available in Latin America today. The possibility of using it depends basically on the filling in of gaps in the macro and microeconomic information described in the preceding paragraphs.

Finally, we wish to emphasize that the fixing of social standards -especially in view of our very limited knowledge of the consequences of social problems- requires a certain social consensus of opinion, which brings us to the need for organized participation in development planning. Although we shall not deal with this important subject in the present paper, we are convinced that the only way to ensure that social standards really reflect the levels socially desired is through the conscious participation of the population in the decision-making process. This conscious participation is achieved in two ways, which should be pursued conjointly: one is an intensive campaign to provide the basic conditions for this participation (education, mainly), and the other is the creation of channels of democratic participation which would enable the State to become the effective political expression of the organized community as a whole.

## SOME GENERAL CONSIDERATIONS

All that has been said can be summed up in the conclusion that the enormous changes and exertions required of Latin America to solve its social problems have great economic implications, which must be taken into account in systematic form. These changes and exertions do not only involve the amount of financial resources that must be utilized to meet the social challenge, but, over and above this, the social, political and structural transformations needed to stimulate, and to make viable and effective, a development strategy capable of satisfying the basic needs of the whole population. Nonetheless, the financial aspects are important. We consider that social policy cannot only be a compensatory action, subsidiary to economic growth, but that the economic model in force should be propitious and conducive to the integral solution of social problems. From this standpoint it is essential to ensure that its functioning is compatible with the objectives of well-being for the majorities. To achieve this, consideration might be given to the following five aspects which seems to us fundamental:

(1) The enormous scope of the theoretic work required to incorporate the economic and social variables into development planning and the inadequacy of traditional economic theory and instrumentation for carrying out this task. Hitherto development planning has devoted perhaps too much attention to supporting the prolongation, or intensification, of a process of growth, without sufficiently considering the need to transform the existing structure. The reason for this is that in many cases it is assumed that growth will automatically result in the solution of the existing social problems.

The first task of a new mode of "thinking" the economic problem is to analyse situations as they are, accepting, therefore, the diversity and particularity of the problems and the ways of solving them with which the different countries of the region are faced. There are indeed in Latin America very differing degrees of social inequality.

There are countries where social development is extremely low; developing countries with considerable nuclei of social backwardness; and more developed countries which still have foci of social backwardness and factors that can unleash social imbalances. In each of these situations economic and social policies will need to be defined in accordance with their specific characteristics.

The market is not a complete and sufficient arbiter of social values, and hence the need arises to define in democratic form, and with the participation of the State, the values that should be sought. Access to an adequate standard of living becomes a right and the economy and society should be organized to achieve it for the majorities. Planning and economic policy should therefore be guided by certain socially accepted values and should seek for society a better economic and social situation. This

"better" situation should envisage such objectives as the reduction of poverty, a more equitable distribution of income, an increase in productive employment, and other more traditional aims such as price stability and economic growth. The attainment of these goals cannot be left to the possible imperfections of the market or to the fluctuations of the world economy.

It is a question of promoting a social view of the economy and of discarding the traditional patterns that inhibit the advance towards a more egalitarian society. This new view should be based on the idea that social problems are surmountable provided that the appropriate transformations are made. The role of a "social economy" will be to direct a multidisciplinary enterprise in the definition of new development styles and the selection of the ways in which to achieve them.

(2) In this connection, the analysis made in this paper of the economic considerations in the designing of social policy and the social implication of economic policy demonstrates the importance of proceeding along these lines in order to achieve efficient action in the practical field of social programmes and policies.

In fact, as we have said, the economic implications of social programmes and policies, especially in developing regions such as Latin America, are particularly important, both from the perspective of the costs incurred and from the standpoint of the beneficial effects these programmes and policies can have on production and on the dynamism of growth in general. To ensure the efficient designing and execution of social policies these economic implications must be adequately taken into account. This requires an understanding of the interrelations between the programmes with social aims and a whole series of realities in relation to investment and production on the one hand, and, on the other, between the purely economic strategies and policies and their social effects.

Without a sufficient understanding of these interrelations, development planning in Latin America, which should combine social and economic objectives, will run into great difficulties. This is partly because it does not consider the structural conditioners of the economic and social problems that keep the region in its underdeveloped state (which has hitherto meant that the public policies applied have in many cases not created a situation which would ensure the dynamic satisfaction of the basic needs of the whole population). Moreover, a segmented view of the economic and social problem can lead, and in fact has often led, to two types of imbalance, both having serious effects on the proposal to build dynamic equitable and democratic societies. One of these occurs when economic policies, through the absence of considerations or measures to correct the social disequilibria, lead to an aggravation of the social problems instead of their solution or alleviation. The second imbalance, on the other hand, occurs when the measures of social change, the social programmes, the policies of assistance for the poorest groups, are less

beneficial than their authors had planned, either because the priorities of the actual projects had not been well chosen, or because the projects themselves had not been efficiently organized or financed, or because the transfers of resources representing the social cost has a negative effect on the overall economic growth, thus affecting employment and the availability of additional resources to continue pursuing the solution of social problems.

The complexity of these interrelations is very great, and there have been only brief references in this paper to some of the aspects which need consideration. At all events, it seems clear that economic science has lagged behind on these problems, and the governments have been tardy in showing a practical will to take account of them in their development plans and policies. The clearest example of this is that in most of the university study programmes, as in practically all the formulated development plans that include programmes, policies and projections on social problems, there is no articulation between the social and the economic aspects, so that the greater part of the interrelations mentioned or described in this paper have not been the object of formal consideration in academic circles or in development plans or policies. It could be said that, up to a certain point, those concerned with the theory and practice of social planning form a group apart from those who perform similar tasks in the economic field, which inevitably results in a failure to profit from the reciprocal complementarities between the projects on behalf of social change and those on the side of growth and stability.

The present paper should be regarded essentially as an attempt to highlight the problems and to suggest the type of research needed to analyse in detail the relation between social and economic policies and objectives.

(3) Employment constitutes one of the central links between the economic and the social problem. It seems impossible to eradicate poverty in Latin America without surmounting the problem of unemployment and, above all, underemployment. Consequently employment is the aspect which perhaps should receive special attention in a strategy directed towards the satisfaction of basic needs. In this connection we should recognize the contribution made by PREALC in defining the characteristics and conditioners of the employment problem in Latin America and in suggesting policies destined to overcome it. We believe that this line of activity should be given the fullest support.

(4) Another central feature of the social problem is the regional dimension of inequality and poverty. It seems to us indispensable that economic and social development planning should be based on a substantive redefinition of the use of regional territories, of the assignment of resources among these, of the population flows and the policies of human settlements. Unless economic and social policies explicitly include the regional dimension of the social policy and the differentiated impact that these have on the different regions, it will be impossible to

implement a more equitable development style. We believe, therefore, that support should be given to the efforts -mainly stimulated by ILPES- which aim to operationalize regional planning and to integrate it effectively into national planning.

(5) Finally we wish to stress the importance of the crucial subject of the political viability of social objectives. We believe that this fundamentally depends on the basing of the political power of the State on a broad social coalition in which the interests of the lower income majorities are adequately represented and in which there are effective channels of communication between these groups of society and the various institutions of the State. An essential condition for the achievement of the social aims of development is the construction of an effectively democratic and representational society.





## JAMAICA. ECONOMIC POLICY AND ECONOMIC PERFORMANCE IN THE 1972-1980 PERIOD: AN INTERPRETATION

*Richard Lynn Ground\**

### 1. Recent economic trends: Introduction and summary

In 1980 the gross domestic product at factor cost (GDP) decreased 3.5% according to preliminary calculations, marking the seventh straight year in which this indicator has either stagnated or declined.<sup>1</sup> Over the course of this period the GDP has dropped by somewhat over 18%, while the per capita GDP has sunk by well over 25% (see table 1).

In addition to the severe foreign exchange constraint that has depressed the level of output throughout this period, but especially since 1976, other factors which disrupted economic activity in 1980 were recurrent adverse weather conditions and an accentuation of the already turbulent social climate. Hurricane Allen caused big losses in agriculture, including the obliteration of between 75% and 90% of the banana trees that remained standing in the wake of Hurricane David in 1979, and overall agricultural production dropped almost 9%, following the 7% reduction in 1979. Manufacturing output fell over 5%, while construction activity plunged by one-fifth, owing in large part to a cutback in government-sponsored projects. Of the goods-producing sectors, only mining showed a gain (7.5%) in 1980. This performance was conditioned largely by the 26% rise in the relative international price of bauxite, although the reduction of the bauxite levy in late 1979 also may have played a role. As far as the rest of the economy is concerned, the level of production diminished about 2%.

As a result of the further contraction of economic activity, especially in agriculture, the rate of unemployment climbed well above 30% towards the end of the year, according to provisional estimates, while the rate of inflation accelerated from around 20% to 30%, owing in large measure to the pronounced intensification of external inflation. Indeed, the increase in the import price index (22.5%) was the largest since 1974. Another contributory factor, however, was the marked expansion of domestic credit, which maintained or even increased the level of domestic demand while domestic supply was declining. This occurred because the deficit of the central government was greater, and its foreign borrowing lower, than projected. In the circumstances, the authorities resolved to accommodate both the central government's financing requirements and the private sector's demand for credit, rather than reduce the availability of credit to the private sector and risk an even larger downturn in economic activity. Compensatory measures, such as ceilings on consumer credit (which were not respected) and price controls, were relied on to mitigate and repress inflationary pressures.

The balance of payments result for 1980 was perhaps less than hoped for but probably considerably more favourable than could have been expected when the government decided to break off negotiations for an interim standby agreement with the IMF in March. At the time the Bank of Jamaica possessed liquid reserves of only some US\$ 25 million (or less than one week of

<sup>1</sup>In fact, it declined in every year of this period with the exception of 1977, when it was stationary.

\* Economist, in the Economic Development Division, Economic Commission for Latin America. This study originally appeared in Part Three of the United Nations, Economic Commission for Latin America, *Economic Survey of Latin America, 1980*, Santiago, Chile, 1982. The text has not been altered.

Table 1

## JAMAICA: MAIN ECONOMIC INDICATORS

	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980(a)
<b>A. Basic economic indicators</b>										
Gross domestic product at factor cost (millions of dollars at 1970 prices)	1 318	1 447	1 463	1 406	1 384	1 298	1 298	1 294	1 237	1 194
Population (millions of inhabitants)	1.89	1.93	1.97	2.01	2.04	2.07	2.09	2.11	2.14	2.17
Per capita gross domestic product (dollars at 1970 prices)	697	750	742	700	678	627	621	613	578	550
<b>B. Short-run economic indicators</b>										
	<u>Growth rates</u>									
Gross domestic product	2.3	9.8	1.2	-3.9	-1.6	-6.2	-	-0.4	-4.3	-3.5
Per capita gross domestic product	0.1	7.6	-1.1	-5.3	-3.1	-7.5	-1.0	-2.2	-5.7	-4.9
Gross income (b)	1.2	11.4	-2.0	3.1	2.9	-9.2	1.9	-3.7	-6.0	-2.1
Terms of trade of goods and services	-2.7	3.8	-7.7	18.1	13.5	-8.1	6.5	-10.6	-4.5	3.2
Current value of exports of goods and services	4.4	13.2	2.5	63.3	6.7	-15.1	4.9	14.6	7.6	23.6
Current value of imports of goods and services	6.1	12.8	8.1	39.6	21.1	-13.8	-17.5	13.6	16.3	23.1
Consumer price index										
December - December	5.1	9.3	29.5	20.6	15.7	8.3	14.1	49.4	19.8	29.5
Variation between annual averages	4.6	4.6	19.8	24.4	17.4	9.6	11.4	34.9	29.1	26.8
Money	24.5	10.3	20.8	27.3	20.2	2.4	37.6	17.6	7.6	35.5
Wages and salaries (c)	...	7.3	-6.2	18.6	6.2	4.5	-7.8	-14.0	-12.0	...
Rate of unemployment (d)	...	23.2	21.9	21.2	20.5	22.4	24.2	24.5	27.8	29.5
Current income of government	13.3	16.1	21.2	48.8	23.8	-5.3	7.5	59.0	7.8	-2.3
Total expenditure of government	16.2	21.0	23.5	59.0	32.5	21.1	3.1	36.9	11.9	14.2
Fiscal deficit/total expenditure of government (d)	17.2	20.5	22.1	26.6	31.4	46.3	44.0	34.9	37.2	46.2
<b>C. External sector</b>										
	<u>Millions of dollars</u>									
Trade balance (goods and services)	-131.9	-151.9	-178.3	-49.2	-207.7	-193.0	50.1	66.1	-20.3	-19.0
Balance on current account	-166.8	-190.0	-240.3	-82.9	-287.8	-306.6	-73.1	-97.4	-153.0	-213.0
Variation in international reserves	25.6	-22.1	-65.0	67.1	-33.5	-186.8	-12.0	-55.8	-162.7	83.3
External debt (e)	148	210	354	528	706	965	1 052	1 236	1 495	1 607

Source: CEPAL, on the basis of official data.

(a) Preliminary figures.

(b) Gross domestic product plus terms-of-trade effect.

(c) Real wages and salaries.

(d) Percentage.

(e) Public debt plus State-guaranteed private debt; and use of IMF credit (disbursed only).

imports), while the economy faced an overall balance of payments deficit in the neighbourhood of US\$ 300 million (or more than 10% of GDP), if the decline in output were to be held to manageable proportions. Yet it proved possible to maintain the existing volume of imports and record a surplus in the balance of payments (for the first time since 1974). Several developments were involved here: the 34% hike in the unit price of merchandise exports; the emergency arrangement to defer the amortization of loans falling due to foreign commercial banks; an upturn in official capital inflows; the further accumulation of arrears; and a sizeable increase in the foreign exchange earnings of the parallel economy. As a result, the current account deficit turned out to be US\$ 213 million, or about half the amount that was originally forecast, and the overall balance of payments surplus was US\$ 85 million, one-half of which corresponded to the accumulation of arrears and the other to a reduction in outstanding obligations with the IMF.

In February 1980, the then Prime Minister announced that elections were to be held ahead of schedule and as soon as possible, in order to resolve the basic economic issues facing the country in the wake of the suspension of access to the IMF's Extended Fund Facility (EFF) in December 1979 and the failure of the stabilization plan adopted in connexion with the EFF to halt the contraction of the economy. In March, the Government informed the nation that it had resolved to stop negotiations for a new agreement with the IMF, because it would be impossible to comply with the performance criteria sought by the Fund. An alternative economic programme, designed to maintain the existing level of activity until the elections were held, was then adopted. The elections took place in October and the governing party was defeated. The new Government indicated that it would seek a fresh accord with the IMF in the context of its strategy for economic recovery.

In addition to the discussion and analysis of the evolution of economic activity during the past year, this survey includes a description and interpretation of some of the outstanding aspects of the evolution of the Jamaican economy over the course of the 1972-1980 period.

## 2. Trends in economic activity

### (a) *Total supply and demand*

The evolution of total supply and demand is shown in table 2, which gives the percentage breakdown (current prices) for 1970 and 1979 and the growth (in constant prices) of the main components in recent years. Only a few of the principal aggregates are available for 1980. During the year, total supply dropped by close on 3%, following no change in 1979 and a modest increase in 1978. In 1978 and 1979 the increase in the quantum of imports was large enough to offset the decline in the GDP, but the import volume could not be augmented in 1980, owing to the exacerbation of the foreign exchange constraint in the wake of the breakdown of the IMF accord and to a marked upturn in international inflation. Data on the evolution of consumption and investment in 1980 are not available, but indirect indicators strongly suggest that investment amounted for more than a proportionate share of the downturn in demand, following a partial recovery of investment activity in 1979.

As may be appreciated from the data in table 2, the structure of demand underwent big modifications over the course of the 1970s. The large increase in the participation of the external sector in the economy was accounted for by the systematic contraction of the GDP after 1973 and by the pronounced change in relative prices, rather than by any real increase in exports and imports. The reduction of the resource gap likewise occurred because of a variation in relative prices (i.e., due to the improvement of the terms of trade). The marked shift in domestic demand was first a cause and later a consequence of the depression of economic activity. Investment demand, which averaged around one-quarter of the product between 1950 and 1970, peaked in 1969/1970 when it soared to more than 31% of the product. It fell appreciably in 1971 (to 27.8% of GDP) and again in 1972 (to 25.5%), as the investment cycle in the mining sector came to a close and an expansionary phase in tourism waned. This presented a major challenge to the country, inasmuch as the high rates of growth of the economy during the preceding two decades were attributable in large part to the creation and successive waves of expansion of the mining industry and tourism.

The new government elected in 1972 expected to offset the autonomous reduction in investment and foreign capital inflows by an expansion of public sector capital formation financed by external borrowing, and by big joint venture projects with foreign firms in oil refining and with other countries in bauxite. Initially, it was possible to mitigate the extent of the decline in investment and capital inflows. Between 1972 and 1975 in spite of a notable rise in consumption, the investment coefficient was maintained relatively high and international reserves at adequate levels, through a big increase in the government capital expenditure programme, foreign borrowing, the internationalization via the Bauxite Levy of a sizeable proportion of the mining sector rents that had previously accrued to foreign-owned bauxite companies, and a marked improve-

Table 2

## JAMAICA: TOTAL SUPPLY AND DEMAND

	Percentage breakdown (a)		Growth rates (b)		
	1970	1979	1975	1979	1980
<u>Total supply</u>	<u>137.4</u>	<u>150.4</u>	<u>1.3</u>	<u>-</u>	<u>-2.6</u>
Gross domestic product at market prices	100.0	100.0	-0.5	-2.0	-3.5
Imports of goods and services	37.4	50.4	6.1	5.2	0.4
<u>Total demand</u>	<u>137.4</u>	<u>150.4</u>	<u>1.3</u>	<u>-</u>	<u>-2.6</u>
Domestic demand	104.2	101.6	-3.9	-2.3	...
Gross domestic investment	31.6	19.0	7.8	16.7	...
Gross fixed investment	31.4	17.6	2.5	20.4	...
Changes in stocks	0.2	1.4	122.4	-20.2	...
Total consumption	72.6	82.6	-5.4	-4.9	...
General government	11.7	19.6	3.9	-0.2	...
Private	60.9	63.0	-8.1	-6.5	...
<u>Exports of goods and services</u>	<u>33.2</u>	<u>48.8</u>	<u>19.7</u>	<u>2.0</u>	<u>-2.3</u>
<u>Income terms of trade</u>			<u>7.0</u>	<u>-2.6</u>	<u>0.9</u>

Source: Jamaica, Department of Statistics, *National Income and Product, 1979*; Bank of Jamaica, *Report and Statement of Accounts, 1980*.

(a) Current prices.

(b) Constant prices.

ment in the terms of trade. In the meantime, however, the oil refinery project was cancelled as a result of the petroleum crisis, and the multinational aluminium project did not get beyond the planning stage.

On another front, investment by the local private sector had begun to decline in the wake of escalating wage settlements. Then, in 1976, a severe economic crisis broke out. As output and income plunged, both the private and public sectors moved to protect existing levels of consumption, and that year investment fell below 17% of GDP (against almost 24% in 1975) and international reserves were virtually exhausted. In 1977 the economy remained depressed, but the prevailing level of consumption was maintained even though real wages and salaries were slashed. The rate of investment dropped to less than 12%, and net savings became negative.<sup>2</sup> Subsequently, one of the primary aims of economic policy was to reduce consumption in favour of investments and exports. Some success was achieved, as investment rose to 17.6% of the product (in 1979) and the resource gap diminished (in 1978) but the objective of halting the decline in output and commencing economy recovery was not achieved.

#### (b) *Evolution of the main sectors*

(i) *Introduction.* In 1980 all of the goods-producing sectors, with the exception of mining, registered production declines. The decreases ranged from over 5% in manufacturing to close to 9% in agriculture and as much as 20% in construction. On the other hand, mining output rose 7.5%. Overall, the value of output in the goods-producing segment of the economy dropped about 6%. A breakdown of the results for services is not available, but the total value of production of services contracted somewhat less than 2% (see table 3).

The systematic contraction of the level of economic activity since 1973 has affected every major sector of the private area of the economy with the exception of agriculture, which expanded appreciably until the severe weather conditions of 1979 and 1980. On the other hand, some of the service subsectors (e.g., transportation, storage and communications) were still producing more at

<sup>2</sup>Between 1975 and 1977 investment was cut by more than one-half in real terms.

Table 3

## JAMAICA: DOMESTIC PRODUCT, BY KIND OF ECONOMIC ACTIVITY, AT FACTOR COST

	Millions of constant Jamaica dollars			Percentage breakdown		Growth rates		
	1978	1979	1980(a)	1970	1980	1978	1979	1980(a)
Total gross domestic product	1 973	1 934	1 866	100.0	100.0	-0.4	-2.0	-3.5
Goods	807	767	720	45.1	38.6	0.6	-5.0	-6.1
Agriculture	187	174	159	7.5	8.5	9.4	-7.0	-8.6
Mining	149	147	158	6.9	8.5	1.4	-1.3	7.5
Manufacturing	333	316	299	17.5	16.0	-4.9	-5.1	-5.4
Construction	138	131	104	13.2	5.6	3.0	-5.8	-20.0
Basic services	153	158		6.3		0.7	3.3	
Electricity and water	24	22		0.8		4.3	-8.3	
Transport, storage and communications	129	136		5.5		-	5.4	
Other services	1 013	1 009	1 146	48.6	61.4	-1.3	-0.4	-1.8
Commerce and finance	403	376		25.7		-4.5	-8.2	
Real estate and business services	210	215		9.8		-3.2	2.9	
Public administration and defence	344	363		9.1		4.6	5.5	
Miscellaneous services (b)	56	60		4.1		-3.4	7.1	

Source: Jamaica, Department of Statistics, National Income and Product, 1979; Bank of Jamaica, Report and Statement of Accounts, 1980.

(a) Preliminary figures.

(b) Includes miscellaneous services and household and private non-profit institutions, less imputed service charges.

the end of the decade than in 1973, but no complete sector recorded growth over the course of this period. The reductions in output were especially marked in construction (60% between 1971 and 1980); in commerce (40% between 1972 and 1979); and manufacturing (25% between 1973 and 1980). In contrast, the value of production in the public area of the economy climbed over three-quarters in the period in question.<sup>3</sup> Initially, the expansion of the public sector was intended to stimulate and complement growth in the private sector. Subsequently, the Government indicated that the public sector would assume a much greater role in the economy, in connexion with the pursuit of its objectives in the areas of growth and employment, income distribution, and external economic relations, but by the middle of the decade the course of events had placed the public sector in a position in which it was struggling to offset the decline in private sector output. The size of the reductions to be counter-balanced, the numbers of entrepreneurs, managers and skilled workers to be replaced, and in particular the magnitude of the foreign exchange gap to be filled, however, made this task impossible to achieve, in spite of the fact that the Government was able to increase substantially its command over domestic resources and mobilize a considerable amount of international sympathy.

(ii) *Agriculture*. In 1979 Jamaica was ravaged by recurrent floods caused by heavy rain, including the especially intense flooding provoked by Hurricane David in June. Losses in agriculture were extremely high.<sup>4</sup> Especially hard-hit was the banana subsector, as approximately

<sup>3</sup>Between 1970 and 1979, the proportion of GDP accounted for by the public sector rose from 9.1% to 18.8%.

<sup>4</sup>The following quotation extracted from a special study on the effects of the June 1979 rains sheds light on the severity of the flooding and recalls the devastation major hurricanes can wreak on small island economies: "The year 1979 was the wettest year for the decade of the 1970s. There were four periods of heavy rainfall and of these the ones on June 12 were the most severe in terms of the amount and the effect on the spatial economy. Flash floods, debris wash and landslides disrupted physical communications, destroying or blocking roads and bridges and completely cut off the Western end of the

one-third of the banana stands was simply annihilated. Also, the harvesting operations in sugar cane were disrupted. Overall, more than 20 million dollars' worth of exports were foregone, while as a whole the crop losses translated into a reduction of almost 7% in the sector's output (see table 4). Furthermore, the flood damage to farm installations and rural infrastructure, which was appreciably greater than originally estimated, continued to hamper farm operations and reduce crop yields into 1980. As a result, by the end of the first half of the year it was estimated that total output would fall at least another 2% in 1980. And then Hurricane Allen struck the island in August. Preliminary tabulations suggest that the extent of the destruction of property and the loss of output was even more severe than that of the previous year. Damage to farms and infrastructure was placed at well over J\$ 500 million (J\$ 1.78 = US\$ 1), while the devastation of crops translated into a loss of exports valued at some US\$ 30 million. The banana subsector again bore the brunt of the onslaught: this time, however, fully three-quarters of the stands were wiped out. Moreover, the havoc wreaked on coffee farms was just as intense.

Production data for the principal export crops are given in table 4. As may be seen, with the exception of citrus, which turned in a strong performance, all of the commodities shown suffered substantial downturns. In the case of bananas (exports only) the drop amounted to 46%; in that of coffee, more than 55%. The outputs of copra, cocoa and pimento decreased by proportions ranging from 14% to 25%. The decline in sugar cane, however, was under 8%, or substantially less than the 19% reduction registered in 1979. Greater losses in 1980 were avoided only because the bulk of the crop had already been harvested when Hurricane Allen hit the island.

Overall, the preliminary data reveal that the cutback in production approached 9% in 1980, following the 7% contraction of the previous year.

Given the existing dearth of resources on the one hand, and the extreme dislocations caused by the weather on the other, public and private efforts were directed mainly at overcoming emergency situations and restoring damaged or destroyed production capacity. In the case of banana acreage, the damage made necessary two massive replanting operations, the second of which was initiated shortly before the end of the year. Owing to the multiplicity of needs and acute scarcity of resources, several urgent problems could not be fully attended to. Thus, for instance, in some areas plant diseases began to spread: sugar cane was plagued by rust and smut disease, bananas by leaf-spot blight, and tobacco by blue mould disease. However, in the last quarter, when the resource constraint eased somewhat, a rehabilitation programme in agriculture was begun. Under it some 120 000 acres of sugar cane, or about 80% of the area currently devoted to the crop, are to be replanted with disease-resistant varieties. The programme also financed the replacement of the destroyed banana stands.

While the pronounced decreases suffered in 1979/1980 forced total agricultural output back to the levels recorded at the beginning of the 1970s, it may be recalled that between 1972 and 1978

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island from vehicular traffic. Reports vary as to the actual volume of water which fell. The estimated return period for similar or greater rainfall in the four western parishes ... varies from 50 to 150 years.

The rains gave rise to about 125 separate bodies of water; of significance was the flooding in Chigivell where water rose to 8.25 feet. At New Market the lake which was formed attained a maximum height of 11.168 feet. The town became non-functional as houses and public buildings were inundated or submerged. In all, the June rains resulted in damage to a land area of approximately 975 square miles (almost a quarter of the area of the island). Between 130 000 and 160 000 persons were directly affected in some 1 150 villages and towns. The death toll was forty-one.

It has been assessed by the Geological Survey Department that no feasible drainage system could have adequately coped with the large volumes of surface run-off generated ...

The Ministry of Works estimated that islandwide damage to roads and bridges, for which they are responsible, amounted to 20 million dollars ... (This damage) created dislocation in many communities which were cut off by inundation, landslips, breakaways of the roadside and roads which were completely washed away ...

Damage to railways in the West was estimated to be 1.2 million dollars ...

Approximately 60-70% of the water systems in the West were rendered non-operational and many others were badly damaged.

It is estimated that most of the damage to housing was due to flash floods simply washing away houses."

Jamaica, National Planning Agency, *Economic and Social Survey, Jamaica, 1979*, Jamaica, 1980, pp. 271-276.

Table 4

JAMAICA: INDICATORS OF AGRICULTURAL PRODUCTION  
(1970 = 100)

	1977	1978	1979	1980(a)	Growth rates			
					1977	1978	1979	1980(a)
Index of agriculture, forestry and fishing production	114.0	124.6	116.1	106.1	7.9	9.3	-6.8	-8.6
Agriculture	134.0	158.3	149.7	...	9.1	18.1	-5.4	...
Export	74.6	84.3	75.1	...	-17.8	13.0	-10.9	...
Domestic	151.0	181.5	175.3	...	25.1	20.2	3.4	...
Livestock	109.5	105.6	93.7	...	8.3	-3.6	-11.3	...
Forestry	78.2	45.5	29.8	...	-9.2	-41.8	-34.5	...
Fishing	115.6	115.6	94.6	...	2.8	-	-18.2	...
Production of some important export crops								
Sugar cane (milled)	3 252	3 641	2 965	2 744	-11.1	12.0	-18.6	-7.4
Bananas (b)	80	75	69	33(c)	3.8	-6.3	-8.0	-45.9(d)
Citrus (e)	63	69	50	79	-3.8	10.0	-27.8	58.2
Pimento	2 022	2 585	1 255	943	-52.8	27.8	-51.5	-24.9
Copra	3 090	1 927	1 835	1 577	-39.1	-37.6	-4.8	-14.1
Cocoa	4 502	4 493	3 416	2 627	2.6	-0.2	-24.0	-23.1
Coffee	1 208	1 504	2 267	1 011	35.6	24.5	50.7	-55.4

Source: Jamaica, Department of Statistics, National Income and Product, 1979 and Production Statistics, 1979; Jamaica National Planning Agency, Economic and Social Survey, 1979; and data supplied to CEPAL.

(a) Preliminary figures.

(b) Exports only.

(c) January-October only.

(d) January-October 1980 compared to January-October 1979.

(e) Oranges and grapefruits only.

the production performance of this sector—in contrast to that of the rest of the economy—was on the whole satisfactory and—in the case of crops destined for the domestic consumption—impressive. Furthermore, it showed a notable improvement over that recorded in the previous decade.

During the course of the 1960s as a whole the agricultural sector (including forestry and fishing) stagnated in per capita terms, even though the rate of growth of the population was relatively modest. Agriculture proper, in fact, registered a reduction in total output in this period, owing mainly to an acute contraction of export commodities but also to a generalized drop-off in crop production in the second half of the decade. Thus, the outputs of sugar cane and bananas, the first and second most important crops, plunged from 500 000 to 370 000 tons and from 235 000 to 134 000 tons, respectively, between 1965 and 1970. As a consequence of the stagnation of total production per inhabitant and the rise of 3.4% per annum in gross domestic income per capita in the 1960s, Jamaica became, for the first time, a net importer of agricultural products in 1970. This turnaround, which persisted in subsequent years, was one of the important underlying factors involved in the progressive deterioration of the balance of payments that commenced with the foreign exchange squeeze in the second half of 1972 and the devaluation of the Jamaican dollar at the beginning of 1973, about a year before the initial round of oil price hikes in December 1973.

Some of the causes of the decline of agriculture were explored in previous economic surveys. Suffice it to note here that an intensive structural and geographic shift of the population led to a shortage of labour at wages which farmers, if not estate-owners, could offer without producing at a loss, notwithstanding the exceptionally elevated and increasing level of unemployment prevailing in the economy as a whole. This, coupled with the declining marginal fertility of the land, an inadequate allocation of resources to support activities—which led to a gradual multiplication and intensification of institutional and infrastructural bottlenecks and thus rising production costs, and

diverse policy measures that placed agriculture at a competitive disadvantage, left the sector in a position in which it was unable to respond adequately to changing market conditions. Moreover, with the recurrent adverse weather conditions in the last half of the 1960s, output fell appreciably.

In view of the highly unsatisfactory production performance of agriculture and its repercussions on rural poverty, growth of urban population and unemployment, and the balance of payments on the one hand; and the sector's considerable potential for output growth, as suggested by the underemployment of both land and labour and good-to-excellent market opportunities on the other, the Government which assumed power in early 1972 resolved to attach high priority to increasing agricultural production.

Following an exhaustive study of the sector commissioned by the Government and carried out by the World Bank and a team of experts headed by Arthur Lewis, a host of measures designed to overcome agricultural stagnation were acted on. The most important among these included the extensive reorganization and upgrading of the Ministry of Agriculture and other agencies responsible for making agricultural policy and providing support services to the sector; stepped-up central government investment in infrastructure; the expansion and reorientation of credit as a function of market opportunities; an integrated rural development project; the "land-lease programme", designed to match idle and abandoned farmland with underemployed farm labour; and the rehabilitation of the sugar industry.<sup>5</sup>

The degree to which each of these and other measures were implemented varied substantially, but as from 1974 and especially from 1976 onward the execution of a host of policies, programmes and projects was interrupted or delayed by the loss of professional staff, the growing frequency and length of strikes, the acute shortage of foreign exchange and, eventually, budgetary cutbacks. One of the most successful programmes, in terms of the proportion of the agricultural labour force benefitted and the production gains realized, was the "land-lease programme". Between 1972 and December 1979 some 36 500 farmers and agricultural labourers—a number equivalent to fully 19.5% of the population economically active in agriculture in 1970 and 23.5% in 1979 benefitted from the "land-lease" scheme under which the Government acquired arable but idle farm land for leasing to underemployed farmers and selected landless agricultural labourers. In addition it provided necessary support services to the beneficiaries, including guidance in the selection of the output mix.<sup>6</sup> As well as encouraging more efficient utilization of land and labour, the authorities sought to increase the output of crops aimed at satisfying the domestic demand for food, and in this respect they achieved substantial advances, to the extent that the appreciable expansion of domestic agriculture (i.e., those crops consumed domestically) is attributable to the "land-lease" and other programmes. In any event, the output of domestic agriculture climbed almost 82% between 1970 and 1978, and until the second half of 1979 this notable gain more than compensated the marked cutbacks in food imports forced by the foreign exchange crisis and thus permitted the maintenance of generally adequate food supplies at approximately constant relative prices.

In contrast, efforts to arrest the deterioration of export agriculture were unsuccessful. Thus, sugar cane output had already dropped an additional 15% between 1970 and 1978, before the sharp contraction suffered in 1979/1980. Forestry output, together with construction activity, fell drastically from 1974 onward, while the output of the livestock and fishing subsectors rose only marginally between 1970 and 1978. Overall agricultural output rose somewhat less than one-quarter between 1970 and 1978, and because of the appreciable reductions in both 1979 and 1980, the level of production in 1980 was a mere 6% above that recorded in 1970.

(iii) *Mining.* The volume of output in the bauxite industry rose 7.5% in 1980, following a modest downturn in 1979. The increase in bauxite production was somewhat less than 6%, while

<sup>5</sup>For further details on these and other programmes, see, for example, Jamaica, National Planning Agency, *Economic and Social Survey of Jamaica*, 1972, Jamaica, 1974, especially pp. 130-131.

<sup>6</sup>Over 67 500 acres, or about 31% of the arable land identified as abandoned in the 1970 agricultural census, had been incorporated into the programme as of December 1979.



that of alumina expanded 18% (see table 5). Nevertheless, owing to the dramatic production cutbacks of 1975/1976, the output of the former was still 19%, and that of the latter 12%, below the respective peak production levels recorded in 1974.

The improvement of the sector's production performance in 1980 may be attributed mainly to the upturn of one-quarter in the relative international price of bauxite, but it is also due to the apparent resolution of long-standing differences between the Government and the transnational corporations which control the industry. In this latter regard the most important development was the agreement concerning the modification of the Bauxite Levy in late 1979. Previously, this levy, which was imposed by the Government in 1974 following inconclusive talks with the bauxite corporations on new contracts, was applied at the rate of 7.5% of the average realized price of primary aluminium, divided, by a factor of 4.3, which is the rate of conversion of bauxite into aluminium.

Under the new accord, arrived at through negotiations between the Government and the corporations, the revised levy is linked to the world market price of aluminium and to the rate of utilization of capacity (in each enterprise).

As the average realized price of aluminium rises, the marginal levy declines. Up to 53 US cents per pound, the levy is 7.5%; between 53 cents and 58 cents the levy drops to 6.8%, and at higher prices a dual formula is applied involving a base, or "cap" price. Between 58 cents and 63 cents, the cap price is 58 cents; between 63 cents and 68 cents, it is 59 cents; and so on. A cap price of 58 cents or 59 cents draws a base levy rate of 6.8%; higher cap prices draw a base levy rate of 6.5%. The difference between the cap price and the average realized price is assessed at a rate that commences at 5% in the 58 cents to 63 cents range and falls to 3% in the 83 cents to 88 cents range (where the cap price is 63 cents and the base levy is 6.5%).

Table 5

JAMAICA: MINING PRODUCTION

	Thousands of metric ton			Growth rates		
	1978	1979	1980	1978	1979	1980
Bauxite	11 736	11 505	12 150	2.6	-2.0	5.6
Alumina	2 114	2 096	2 475	3.2	-0.9	18.1
Gypsum	135	66	...	-35.4	-51.1	...

Source: Jamaica, Department of Statistics, *Production Statistics*, 1979, and Central Bank of Jamaica, *Statistical Digest*, January 1981.

These rates also vary according to production levels: as output rises above a floor equal to 85% of each firm's capacity, the marginal levy likewise decreases. Up to the floor level production is assessed at 100% of the rates quoted above. For the first increment of 200 000 tons above it the levy is reduced to 75% of the rate applicable given the average realized price. For the next increment of 400 000 tons, the levy is reduced to 50% of the applicable rate. The assessment on further increases will be subject to negotiation.

According to the agreement, the new levy system will be reviewed in January 1980, or when the average realized price reaches 85 cents, whichever occurs first.

In order to compare this somewhat involved formula with the previous straight 7.5% levy, the price of aluminium and the expectations of its future evolution prevailing at the time the new agreement was reached (October 1979) must be taken into account.

First, it may be noted that the price of aluminium in the world market has risen continuously since 1972 and has been above 53 cents —or the level at which the levy falls below 7.5%— since the third quarter of 1977. Between then and the fourth quarter of 1979, the price climbed more than 39%, to 74.5 cents, or the level where the next to lowest levy rates obtain under the new formula. At that price, and assuming capacity utilization were 85%, the effective levy would be

5.95%. Furthermore, the price prospects for aluminium in the foreseeable future are highly favourable, owing mainly to the increasing substitution of aluminium for other, heavier metals.

In the light of these factors, the new levy system represents a substantial concession to the bauxite corporations. It translated into a reduction of more than 20% in the levy rate at the moment the agreement was concluded, and will permit the bauxite companies to capture a progressively increasing proportion of the expected windfall gains. In exchange, the firms made informal commitments to expand production and capacity.

In 1980 aluminium prices averaged 85.4 cents or some 22% more than in 1979. At that price the levy fell to 5.52%. Nevertheless, owing to the marked increase in price and the sizeable upturn in production, the nominal value of the revenue from the levy decreased by only 3.5%. In the third quarter of 1980 the international price of aluminium surpassed the 85 cents mark that would normally trigger a new round of negotiations over levy rates under the October 1979 agreement. Because of the pressing obligations associated with the elections in October 1980 and the resultant change in administrations, however, the negotiations were postponed until 1981. Presumably it was the same confluence of events that led the bauxite corporations to delay the implementation of their informal commitments to expand capacity.<sup>7</sup> On the other hand, the appreciable reduction in the levy rate may have encouraged the firms to expand output in 1980. But, as suggested at the outset of this section, the principal inducement seems to have been the steep rise in aluminium prices.

The creation and expansion of the bauxite industry was the principal source of the 6.5% per annum growth obtained between the early 1950s and the early 1970s in Jamaica. During this period the increases in the rate of investment (in several years over 30% of the product); the level of capital inflows (which accounted for an average of 32% of total investment); the growth of exports (6.8% per year), and the growth of the overall external sector (7.5% per year) were all generated primarily by successive cyclical expansions (roughly in 1953/1957, 1961/1965 and 1967/1972) in the bauxite sector. Thus, in addition to the direct (over 18%) and indirect (e.g., via the stimulation of the construction industry) contribution to growth, the product and capital flows that the sector occasioned entailed both a large and persistent deficit on the current account and a sizeable and consistent surplus on the overall balance of payments. During the course of the last expansionary phase in bauxite —the final year of which coincided with the first election of the previous Government— the extent of the sector's contribution to the 7.4% per annum growth of total output and to the buoyancy of the external sector (gross reserves almost doubled) assumed even greater proportions. In effect, investment in bauxite and alumina alone accounted for fully one-third of investment; the increase in its product provided almost 27% of the rise in the GDP; and the increment in the value of bauxite and alumina exports provided more than two-thirds of overall export growth. And in 1973/1974, when the rest of the economy began to contract in the wake of the pronounced acceleration of inflation, a marked drop in construction-related investment, and the stagnation of import volume, mining output still climbed an additional 26%.

In the light of these facts it can be appreciated that the bauxite corporations' decision to slash production was a heavy blow to the economy. The real value of the industry's output plunged 21% in 1975; the following year it dropped a further 21%. The rest of the economy was in fact recovering from the 1974 recession when mining production first tumbled. In 1976, however, output in the rest of the economy dropped almost 6%, as import volume was compressed more than 16%, and at the end of the year operations in the foreign exchange market were suspended because the gross international reserves were nearing depletion.

While other factors, such as the international recession, the multiplication of petroleum prices, labour/management disputes and an explosion in Alcoa's alumina refinery (1976) also incited in the severe cutback in bauxite mining and refining in 1975/1976, the principal factor involved appears to have been the extremely adverse reaction of the transnationals to the

<sup>7</sup>In this connexion, it may be mentioned that long-planned construction by the Government of a US\$ 550-600 million, 600 ton refinery at South Manchester was delayed once again because the required additional financing —some US\$ 250 million— did not materialize.

Government's decision to enact the bauxite levy (which was followed by the Caribbean producing countries but not other major producers). With respect to the question of its effects on corporate investment in the sector, however, it should be noted that the various companies did not have any existing plans to undertake a further expansion of their respective mining and refining capacities in Jamaica. Indeed, and notwithstanding the last round of expansions there in 1967/1972, the bauxite firms had begun intensive development of sources outside Jamaica (and outside the Caribbean in general) in the mid-1960s, even though Jamaica was the lowest-cost producer. As early as 1971 Australia had already overtaken Jamaica as the world's principal producer of bauxite, and by 1974 it accounted for 24.4% of world supply, against the 18.7% share originating from Jamaica. On the other hand, the controversy over the levy definitively precluded any additional transnational investment in Jamaican bauxite.

The value of mining output (in constant terms) not realized between 1975 and 1980—calculated as the difference between actual and 1974 production—equalled an average of 2.5% of GDP in that period.<sup>8</sup> In terms of GNP, the proportion falls to 1.6%, owing to the remittances of profits which the added production would have occasioned.<sup>9</sup> In spite of the dimensions of these losses they were more than offset by the total value (in constant terms) of the bauxite levy collected during the period. In effect, levy income exceeded the value of production lost by almost 37% and was more than double the proportion that would have remained in Jamaica.<sup>10</sup> But these resources were not employed to enlarge the mining industry's production capacity, nor directly utilized in development projects, as was originally intended. Instead, the course of events made necessary the use of the levy income to finance part of the fiscal deficit.

(iv) *Manufacturing*. Preliminary data show a downturn in excess of 5% in manufacturing in 1980 (see table 6). The sector's output had declined systematically since 1976, with the cumulative reduction approaching 25%. Moreover, the level of output in 1980 was about 16% below the 1970 figure. The depression of manufacturing accounted for almost 26% of the drop in GDP experienced between 1973 and 1980 and well over 33% of that registered between 1975 and 1980. The results for some specific products in 1980 are shown in tables 7 and 8. However, data on performance by subsectors are not yet available. As of 1979, eleven of the sixteen principal industrial branches were producing less than in 1970. The proportions involved ranged from -51% (furniture and fixtures) to -9% (food). Moreover, the real extent of the cutbacks was generally even greater, because production peaked around 1972/1973 in most branches. In this connexion it may be observed that the only branch to reach its maximum production level in 1979 was tobacco and tobacco products.

Between 1960 and 1972 five other sectors of the economy registered growth rates greater than that of manufacturing. Nevertheless, the 6.3% per annum increase obtained in that sector was higher than the economy-wide average. Also, manufacturing accounted for one-sixth of the expansion of GNP—a contribution which was surpassed only by that of mining—while it provided over one-third of the jobs created during the period and the increase in manufacturing employment was equivalent to fully 84% of the net gain in jobs.

Owing to diverse factors, such as the dearth of opportunities to achieve economies of scale, the country's brief industrial history, and incentives schemes that encouraged the manufacture of a broad range of products, the industrial sector that developed in Jamaica depended heavily on the external market for input supply and on the internal market for output demand. Thus, in 1972, for example, imports attributable to the sector totalled about one-half of the value of its production, while the domestic market absorbed some 83% of the value of its output. In that same year the sector's imports gave rise to almost 28% of total imports, but manufactured exports provided only slightly over 13% of total exports. The trade deficit thus generated by the sector was equivalent to

<sup>8</sup>In 1974 the sector's output reached almost 91% of capacity.

<sup>9</sup>The ratio of profit remittances to product was taken from the 1970/1973 accounts. The data are from the World Bank.

<sup>10</sup>If the comparisons are limited to 1975-1980, the above figures become 7% and 72%.

more than one-third of the value of its output, and equalled the entire amount of the overall trade deficit.

Given these characteristics, the subsequent depression of manufacturing activity is traceable primarily to developments in the rest of the economy, namely, the collapse of investment demand in construction and mining; the balance of payments crisis; and the deflation of consumer demand. Thus, the close of investment cycles in construction and mining, together with the first squeeze on the balance of payments, led to a decline in manufacturing growth from almost 12% in 1972 to less than 1% in 1973 and in 1974 the sector's output dropped 3.5%. With the transitory let-up in the pressure on the external sector, which translated into a 5% rise in import volume following two years of stagnation, manufacturing rebounded slightly to record an increase of somewhat more than 2% in 1975. However, the full-fledged balance of payments crisis that surfaced in 1976 forced a reduction in import volume amounting to fully 37% in 1976/1977. This severe blow, which was accentuated in 1976 by the first important reduction in the domestic demand for consumer goods, provoked a decline in manufacturing of 5% in 1976 and almost 7% in 1977. In 1978/1979 the additional 9% decrease was a result mainly of the deflationary policies adopted under the IMF accords. The intensification of the severe slump in manufacturing activity in 1980 was as much a consequence of the persistent contraction of domestic demand as of another marked cutback in the supply of imported intermediate inputs.

Table 6  
JAMAICA: MANUFACTURING OUTPUT BY SUBSECTOR  
(1970 = 100)

	1977	1978	1979	1980	Growth rates			
					1977	1978	1979	1980
Index of manufacturing production (1973)	100.6	95.7	90.8	85.9	-6.8	-4.9	-5.2	-5.4
Food (1972)	117.9	108.1	91.3		2.3	-8.3	-15.5	
Sugar, molasses and rum (1965)	80.3	78.2	77.6		-17.2	-2.7	-0.8	
Alcoholic beverages (1975)	134.8	140.0	138.3		-2.3	3.9	-1.2	
Non-alcoholic beverages (1974)	106.3	96.8	85.9		8.3	-8.9	-11.3	
Tobacco and tobacco products (1979)	122.7	118.5	131.0		0.2	-3.4	10.5	
Textiles and wearing apparel (1973)	101.0	92.9	67.6		-6.6	-8.0	-27.2	
Leather and leather products (1978)	135.8	174.3	162.6		5.2	28.4	-6.7	
Footwear (1970)	75.5	62.7	53.1		9.9	-17.0	-15.3	
Wood, wood and cork products (1977)	226.3	140.4	121.7		26.4	-38.0	-13.3	
Furniture and fixtures (1972)	83.5	64.3	49.2		-3.4	-23.0	-23.5	
Paper and paper products, printing and publishing (1975)	103.6	108.3	139.0		-20.9	4.5	28.3	
Petroleum refining (1970)	64.5	59.6	71.3		-15.0	-7.6	19.6	
Chemicals and chemical petroleum rubber and plastic products (1973)	120.9	128.2	115.5		-13.2	6.0	-9.9	
Non-metallic products (1972)	76.0	70.4	65.5		-5.6	-7.4	-7.0	
Metal and fabricated metal products, machinery and equipment (1973)	76.4	70.9	57.7		-21.5	-7.2	-18.6	
Other manufactures (1970)	69.7	72.1	89.9		-17.0	3.4	24.7	

Source: Jamaica, Department of Statistics. National Income and Product, 1979.

In the 1973/1976 period the sector's performance was also hampered by an appreciable fall in the real exchange rate. The steep rise in the costs of production at the prevailing (nominal) rate of exchange reduced the international competitiveness of Jamaica's manufactured exports, and this, in conjunction with the severe limits on the supply of imported inputs, occasioned the closure of a large number of firms that produced for the external market under a free trade zone-type of

arrangement. Between 1972 and 1976 the value of manufactured exports as a proportion of the value of total manufactured output dropped from 17% to 13.6%.

Finally, factory operations were prejudiced also by the migration of professional, technical and skilled manpower, industrial unrest, recurrent disruptions of basic services and, in 1976 and 1980, by the atmosphere surrounding the election campaigns.

Policy initiatives directed mainly or partly at halting the decline of this sector were focused almost exclusively on improving export performance. They included the successive devaluations of the Jamaican dollar between 1977 and 1979, which translated into a rise of almost 39% in the real exchange rate. This notable adjustment doubled the extent of the decline recorded between 1973 and 1976 and left the real exchange rate at its highest level since World War II. Also, the Government created the Certified Exporters Scheme, designed to ensure that producers geared to the export market, or those capable of meeting a specified level of exports, receive priority in the disbursement of foreign exchange for import needs. Finally, the Government obtained from the World Bank a sizeable loan to set up and finance an Export Development Fund (EDF). This revolving fund was used to cover the foreign exchange requirements of certified exporters. According to World Bank records, 80 firms, accounting for some 75% of the export volume of non-traditional exports, had made use of the EDF by December 1980. In addition to directly expediting the international transactions of exporters, the EDF also permitted firms to obtain better terms from overseas suppliers and from the Jamaican branches of foreign commercial banks.

In 1977 and 1978 exports of manufactures remained sluggish, but in 1979 the current value of manufactured exports climbed well over 32%. No comparable data for 1980 are yet available. However, it appears that little or no further growth took place.

(v) *Construction.* According to the preliminary figures on GDP, the value of construction output dwindled more than 20% in 1980. Selected indicators of construction activity are contained

Table 7

JAMAICA: INDICATORS OF MANUFACTURING ACTIVITY

	Thousand of metric tons			Growth rates		
	1978	1979	1980(a)	1978	1979	1980(b)
Production of selected manufactures						
Sugar	292	283	226	-1.0	-3.1	-14.7
Flour (wheat)	49	42	47	-10.0	-13.4	35.1
Animal feeds	21	203	169(c)	6.6	-3.8	-
Rum and alcohol (d)	17	18	18(e)	-5.1	7.1	6.1
Fertilizers	30	31	16(f)	38.5	4.4	21.1
Petroleum products (d)	1 173	1 371	982	1.6	16.9	-20.9
Textile fabrics (g)	9 330	5 944	2 986(f)	16.4	-36.3	15.9
Indicators of manufacturing production						
Electricity sales to industry by public utilities (h)	635	588	527	-	-7.3	-2.8
Industrial employment (i)	79	74	73	3.4	-6.9	-2.9

Source: Jamaica, Department of Statistics, *Production Statistics*, 1979, and *Statistical Digest*, January 1981.

(a) January to November.

(b) January-November 1980 with respect January-November 1979.

(c) January-October.

(d) Millions of litres.

(e) January-September.

(f) January-June.

(g) Thousands of metres.

(h) Millions of KWH.

(i) Thousands.

in table 8. As may be seen, the production of two of the main building materials, cement and steel, contracted by one-third and one-sixth, respectively, during the twelve months ending in November 1980. The marked drop-off in cement was caused by the recurrent shut-down of the kilns at the Cement Company because of the inability to obtain spare parts. The scarcity of cement in turn forced reductions in other firms that supply materials (e.g., concrete blocks and tiles) to the construction industry. The contraction of the domestic production of building components was aggravated further by the appreciable reduction in the supply of imported construction materials. As a result of the big drop in construction, employment in the sector was slashed by more than one-third (see again table 8).

The level of construction output had spurted ahead by almost 21% in 1970, as the last expansion of capacity in mining and tourism peaked. In 1971, however, the value of the sector's output rose less than 1%, and construction activity commenced what was to become a relentless contraction, notwithstanding a substantial increment in residential building in the middle of the decade. In 1980, the value of the construction GDP was a mere 40% of that recorded in 1971. After having dropped 15% between 1971 and 1973, when the rest of the economy expanded by over 14%, the persistent decrease in construction accounted for over 30% of the fall in the total product between 1973 and 1980.

While overall building activity systematically declined, housing completions rose from approximately 3 000 per year at the beginning of the 1970s to a high of 6 837 in 1977. In 1978, however, the total dropped to 4 876, and in 1979 4 940 units were built. No data for 1980 are yet available. Of the residences completed in the 1977/1979 period, 76% were constructed by the public sector.

In spite of the stepped-up effort in housing development in the 1970s, the pronounced shift in the age distribution of the population led to the doubling of the number of families formed as the decade progresses, so that the annual increment in the housing deficit registered a marked expansion.

Table 8

JAMAICA: INDICATORS OF CONSTRUCTION ACTIVITY

	1978	1979	1980(a)	Growth rate		
				1978	1979	1980(b)
Production of selected buildings materials						
Cement (c)	294	225	135	-11.7	-23.5	-33.5
Paint (d)	5 513	5 782	...	17.7	4.9	...
Steel (c)	14	10	8	37.9	-30.3	-16.2
Bagasse board (e)	6	60	...	-83.0	963.0	...
Employment (f)	33	32	24	-0.3	-3.0	-34.6

Source: Jamaica, National Planning Agency, Economic and Social Survey, 1979, and Statistical Digest, January 1980.

(a) January-November only.

(b) January-November 1980, compared to January-November 1979.

(c) Thousands of metric tons.

(d) Thousands of litres.

(e) Thousands of cm<sup>2</sup>.

(f) April of each year.

(vi) *Tourism*. Following the recuperation of the tourist industry in 1978 and the achievement of a record number of tourist arrivals in 1979, the total number of visitors through October 1980 was 6% less than in the corresponding period of the previous year (see table 9). The traditionally volatile short-stay (one or two nights) and cruise-ship segments of the market accounted for this

downturn as the first category dropped almost two-thirds and the second about one-sixth. On the other hand the number of long-stay visitors (three or more nights) showed a slight increase. Partly for this reason, but mainly due to a rise in average spending per tourist, estimated tourist expenditures climbed almost 31%. This development, however, largely reflected price inflation. Full-year data from the travel account of the balance of payments reveal an increment of slightly more than 1% in current US dollars, and a decrease of well over 18% in constant dollars.

The determinants of the recession in tourism in Jamaica in 1980 are broadly similar to those that led to the severe depression of 1976/1977. First, owing to the marked reduction in the growth of the developed market economies, particularly in the United States, where the product dipped 0.2%, and in Great Britain, where it declined 3%, and to the new rounds of fuel price hikes, tourism in the Caribbean as a whole fell about 2% in 1980. This negative panorama was further exacerbated by the upsurge in violence and disturbances associated with the continued deterioration of the economy and the election campaign in Jamaica, with the consequent effects on the image of the country as a destination for vacations. The 11% reduction in the real exchange rate of the Jamaican currency in terms of US dollars may also have influenced the decline in the number of tourists from Jamaica's principal market, although the country's price levels became highly competitive again following the huge exchange rate adjustments of the 1977/1979 period.

The total number of tourists increased somewhat more than 6% per annum in the 1960s in Jamaica. However, the number of long-stay visitors climbed well over 13% per annum, and by the second half of the decade the average hotel room occupancy rate surpassed 67%. In view of these and other developments, such as the rise of charters and group travel associated with the entry into service of the jumbo jets, and of the absence of convention-type hotels on the island, in the late 1960s the Government resolved to actively encourage a major enlargement of hotel capacity. For this purpose it obtained in 1968 the enactment of the Hotel Incentives Act. This initiative provided for the waiver of import duties on capital goods and exemption from taxes on profits for ten to fifteen years for the erection of hotels with 350 or more rooms. Also, the central government decided to make available government guarantees on loans raised to finance hotel projects.

Largely in response to these incentives, the total number of tourist rooms more than doubled between 1968 and 1973. In 1970, when hotel building activity attained its zenith, the room capacity was augmented by fully 22%, and while the rate of increase thereafter tailed-off progressively, additions were sufficient to lead to a rise of at least 10% in each of the following four years.

In the meantime, the growth of overnight tourism remained strong (10%), but was in no case sufficient to cover the massive expansion in hotel rooms. Consequently, between 1968 and 1973 the average room occupancy rate plunged from 66.8% to 48.1%, and when the number of tourists peaked in 1975, the occupancy rate was down to only 43.5%. In 1976, the occupancy rate tumbled to 32.2% in the wake of the drop of 18% in tourist arrivals and the completion of the final projects commenced under the Hotel Incentives Act. The bottom was reached the ensuing year, when the number of visitors contracted a further 18%. The fact that the occupancy rate only fell to 28.1% was due to the bankruptcies which had resulted in a 9% contraction in the supply of rooms. A greater cutback was avoided because the Government decided to take over and subsidize a number of facilities that otherwise would also have closed.<sup>11</sup>

Thus, the inordinate expansion of capacity in the late 1960s and early 1970s had already depressed the average occupancy rate below the breaking point prior to the severe 1976/1977 slump. Marginal operations—including many of the new projects—were flirting with bankruptcy before 1976.

The pronounced reductions in tourist arrivals in 1976 and again in 1977 would appear to be attributable primarily to the notable deterioration of the media image of Jamaica in the principal tourist markets. And as in 1980, this factor may be traced to the intensification of violence in Jamaica during the electoral campaign, and to the deterioration of Government-to-Government relations. But also of importance was the steady decline of the real exchange rate of the Jamaican

<sup>11</sup>The number of rooms decreased another 5% in 1978.

Table 9

## JAMAICA: INDICATORS OF TOURIST ACTIVITY

	1978	1979	1980(a)	Growth rates		
				1978	1979	1980(b)
Total visitors (c) (d)	533	594	457	37.9	11.4	-5.8
Long stay (e) (e)	370	401	334	45.3	8.3	2.3
Short stay (c) (f)	12	26	9	14.3	117.5	-63.7
Other (c) (g)	151	167	114	24.9	10.5	-15.7
Hotel room occupancy rate	40	48	46	38.4	20.0	0.4
Average length of stay (h)	9	9	9	-2.3	3.5	-8.3
Estimated expenditure (i)	148	194	215	41.8	31.1	30.6
Direct employment (j)	10 166	11 707	...	21.1	15.2	...

Source: Jamaica, National Planning Agency, *Economic and Social Survey*, 1979, and Bank of Jamaica, Research Department, *Statistical Digest*, January 1981.

(a) January-October only.

(b) January-October 1980, with respect to January-October 1979.

(c) Thousands.

(d) Excludes nationals residing abroad.

(e) Three or more nights.

(f) One or two nights.

(g) Includes cruise-ship passengers and members of the armed forces.

(h) Nights.

(i) Millions of current Jamaica dollars.

(j) In hotels, guest houses and cottages.

dollar in terms of US dollars between 1973 and 1976, because the United States provided around 80% of Jamaica's tourists at the time.

In spite of the 1976/1977 experience, and thanks to the remarkable rebound of 1978, the total number of tourists arriving in Jamaica in 1979 was 43% above the 1970 figure, or about half the growth rate recorded in the Caribbean as a whole. On the other hand, overnight visitors in 1979 were still slightly below the record 1974 level, and 1980 tourist expenditures, as measured in constant US dollars, were 12% less than in 1970 and 29% less than 1972, as the peak level was registered prior to the first devaluation of the Jamaica currency in 1973. Finally, in 1980 the occupancy rate remained excessively low (46%)

### (c) *Employment and unemployment*

Notwithstanding a high rate of economic growth and a modest rate of growth of the working-age population in the two decades ending in 1972, the relative and absolute levels of unemployment recorded very substantial increases in Jamaica. During the 1960-1972 period the asymmetry between the evolution of the product and the evolution of employment became increasingly pronounced: in fact, in the final years these two variables moved in opposite directions. Simultaneously, the steady stream of emigration of skilled technical and professional personnel, together with appreciable shifts in the structure of production, led to a growing shortage of skilled and managerial labour.

The disarticulation of the labour market from the expansion path of the economy and the marked division within the labour market between the unorganized unskilled segment and the highly organized, high wage one had a profound impact on the formation of both the short-term economic policy and the long-term development strategy of the Government elected in February 1972.

In 1960 the rate of unemployment in Jamaica stood at 13.0% (9.0% for males and 19.2% for females). In the 1960s total economic growth averaged 5.5% per annum, while per capita growth averaged 4.0%. After emigration, the average annual increase in the labour force attributable to the expansion of the working-age (15-64) population was a mere 0.4%. If it had not been for the massive net emigration which took place and affected principally those of working age, the growth



of the population aged 15 through 64 would have reached the figure of 3.6% per annum, or nine times greater than the actual rate. Part of this outflow was offset by a pronounced rise in the female labour force participation rate. But the overall annual increment of the labour force remained at the relatively low figure of 1.4%. A total of 94 500 individuals thus entered the labour force during the decade.

But high economic growth and low labour force growth was not accompanied by an improvement in the employment situation. Net job creation amounted to some 51 000, or less than 1.0% per year. As a result, the rate of unemployment climbed to 17.6%: 10.7% for males and 26.5% for females. The number of persons affected by unemployment rose by a total of 49%, or 4.6% per year.<sup>12</sup>

In the meantime, the high natural rate of growth of the population (3.1%), combined with the large-scale emigration of labour force members, led to a notable rise in the dependency ratio, which climbed between 1960 and 1970 from 834 to 1 065 (per 1 000 working-age inhabitants), and in 1970 children under 15 constituted 46% of the population. Moreover, the elevated vegetative growth of the population in the 1960s meant that the rate of growth of the labour force would accelerate appreciably in the 1970s, unless emigration were to register a systematic, proportionate increase. On the other hand, the pattern of the depletion of the labour force through emigration created a serious imbalance between experienced and inexperienced workers. The number of people of prime working age actually decreased between 1960 and 1970. Furthermore, the confluence of the population and emigration trends would exacerbate dramatically the proportion of this imbalance in the 1970s.

<sup>12</sup>The labour force data are from the Jamaica National Planning Agency, *Economic and Social Survey*, various years; and the World Bank.

Before proceeding further, account should be taken of the particular manner in which unemployment is officially defined in Jamaica. In this connexion, the National Planning Agency has observed: "In the Jamaican situation, unemployment levels include both active job-seekers as well as non-seekers, that is, persons who made no effort to find a job during the survey week but who indicate that they wanted work and were available to accept it. This approach has been judged to be more appropriate for the local context in view of the very high proportions of non-seekers among the unemployed, and because it is recognized that in situations of chronically high unemployment job-seeking activity is not a sufficient indicator of availability for work. In October 1979 about 41% of all unemployed males and 70% of all unemployed females were classified as non-seekers, while the highest levels of job-seekers were recorded in the urban parishes of Kingston and St. Andrew. Job-seeking activity is clearly related to personal judgements as to the likelihood of finding a job, as well as to the existence of formal agencies for securing employment. Whereas 29% of the unemployed labour force lived in the Kingston and St. Andrew area in October 1979, some 38% of all active job-seekers were found in those two parishes. It should be noted that the inclusion of non-seekers leads to a wider definition of unemployment than is used in many countries, and that it does serve to provide a higher estimate of the labour force and of the unemployed." (Jamaica, National Planning Agency, *Economic and Social Survey*, 1979, *op.cit.*, p. 162.)

Thus, while the rate of unemployment (and the labour force) as defined in Jamaica are not directly comparable with unemployment rates obtained under the conventional concepts, the Jamaican authorities consider that the broader definition of unemployment is the one most relevant to the characteristics of Jamaica's labour market.

If the unemployment and labour force data are modified to correspond to the most common usage, that is, if those who want to work but were not actively seeking work when interviewed are excluded from the labour force and from the unemployed, the rate of unemployment diminishes appreciably. In 1972, the first year for which it is possible to make this adjustment, the unemployment rate becomes 14.5% versus 22.9% according to the official definition. The large difference stems from the fact that 58% of the unemployed females and 14% of the unemployed males were not actively seeking work.

It is important to note that the proportion of unemployed who actively seek work does in fact decline as the rate of unemployment decreases. Thus in 1979, when unemployment officially reached 27.8%, around 70% of unemployed females and 41% of unemployed males did not actively look for work.

The 1960 census, from which the 1960 unemployment rate is taken, did not make a distinction between those who were or were not actively seeking work. It merely tabulated those who wanted to work. Consequently, the magnitude and direction of the trends in the 1960s remain identical under either concept of unemployment, unless the substantial rise in the labour force participation rate detected between the 1960 (population census) and 1968 (first labour force survey) data is attributed to the possibility that in 1960 non-seekers were excluded from the labour force. In the 1970s the situation is straightforward. The adjusted unemployment rate declines from 62.2% of the official unemployment rate (1972) to 47.2% (1979).

As these developments began to materialize, the limited capacity of the economy to generate a net gain in employment along the existing growth path simply vanished. Thus, while output expanded more than 26% between 1969 and 1972, total employment actually declined by 1%. This breakdown, together with the acceleration in the growth of the labour force despite an upturn in emigration gave rise to a 40% leap in the number of unemployed and the unemployment rate soared to 23.2% (see table 10). Male unemployment was 14.3% and female unemployment was 35.3%, which unemployment in the 14 to 24 age bracket was 40.9% (30.2% for males and 54.4% for females).

In addition to its direct consequences, the intensive increase in unemployment made for a deterioration in the already highly skewed distribution of income and created a climate in which crime and other social ills flourished.

On the face of it, the explanation of the inability of the economy to create enough jobs to meet even the minor increment of the labour force in the 1960/1972 period is straightforward: the growth of the product was concentrated in sectors in which the relative share of total employment is modest, the capital costs of job creation high, or the employment elasticity low. At the same time, the elasticity of employment in the sectors which account for the lion's share of jobs became negative. Suffice it to note here that the 150% expansion of bauxite mining and refining, which accounted for more than one-sixth of the rise in GDP and thus constituted the principal source of growth, generated a mere 3 500 jobs: sufficient to absorb just 3.7% of the new labour force entrants. On the other hand, employment in agriculture, which provided 41% of total employment in 1960, contracted by over 13%. The extent of the decrease surpassed by 4.6 times the total employment in mining in 1972.

On another level, the lack of correspondence between growth and employment was in large part attributable to the intensive exploitation of the country's abundant natural endowment in minerals and tourism: not only did these low-employment activities attract the largest part of economy-wide investment, but also their development depressed the level of relative profitability in the rest of the economy. In manufacturing this effect was largely offset by the array of policies adopted to foment industry. But agriculture was not compensated, under circumstances in which the profitability of the full utilization of the island's natural resources in agriculture was already in decline.

Employment and unemployment were also affected by the changing characteristics of the labour supply. The marked imbalance that developed in the labour force as a result of emigration in the 1950s and 1960s aggravated unemployment to the extent that: (i) the general level of employment was a function of the ratio of experienced workers to inexperienced workers; and (ii) it altered the relation between the overall supply of labour and the general level of wages and costs in the economy. Also relevant to the latter question were the repercussions of the creation of cases of high-wage employment (in mining) on the economy-wide wage structure. Large-scale rural to urban migration, for its part, led to a regional disequilibrium in the labour market, whereby unskilled labour was in short supply in agriculture, yet unemployed in the urban areas. Finally, it may be added that the long-run situation of high unemployment in Jamaica is partially rooted in sociological and demographic factors that have impinged on the conformation of an unusually high rate of labour force participation in relation to the working-age population.<sup>13</sup>

In the light of the grave situation and the dramatic implications of the impending surge in the growth of the labour force, the administration which assumed power in early 1972 placed a very high priority on the creation of jobs.

To this end a host of initiatives were undertaken: (i) first, and perhaps most important, was the reorientation of the growth strategy as a function of job creation: that is, as a function of the

<sup>13</sup>Approximately half the households in Jamaica are headed by females. This, coupled with the consistently high levels of emigration of labour force members in the past four decades, has led to an extraordinary rate of participation of women in the labour force. In 1979, for example, some 80% of the women of working age appear as labour force members, while over 47% of the total labour force is composed of females. (Jamaica, National Planning Agency, *Economic and Social Survey*, 1979, *op.cit.*)

Table 10

JAMAICA: EMPLOYMENT AND UNEMPLOYMENT  
(1969 = 100)

	1972	1973	1974	1975	1976	1977	1978	1979	1980(a)
Labour force	106.3	107.6	109.5	114.5	118.0	121.5	125.4	127.3	130.2
Employment	99.0	102.0	104.7	110.5	111.1	111.8	114.8	111.6	113.0
Agricultural (b)	86.9	86.7	96.8	97.4	104.8	104.8	110.4	99.7	...
Mining (c)	133.3	147.3	149.0	146.0	153.9	144.1	116.7	149.0	...
Manufacture	115.1	116.4	117.3	118.8	108.1	110.5	111.5	107.9	...
Construction	92.4	98.6	95.0	105.7	89.9	78.1	78.0	75.6	...
Transportation and communication (d)	118.0	121.0	121.0	144.1	143.8	134.9	133.8	133.8	...
Commerce	124.6	129.3	112.8	119.3	117.8	129.0	136.1	131.2	...
Public administration	123.6	140.7	138.9	180.0	194.5	203.5	198.8	201.2	...
Other	89.4	91.4	90.6	95.2	82.5	80.9	82.9	92.5	...
Unemployment	146.1	144.0	131.9	133.2	150.2	167.3	175.1	200.9	218.6
Rate of unemployment	23.2	21.9	21.2	20.5	22.4	24.2	24.5	27.8	29.5

Source: Jamaica, National Planning Agency, *Economic and Social Survey*, various years; and the World Bank.

(a) Estimates based on Statistics for the first half-year.

(b) Includes forestry and fishing.

(c) Includes quarrying and refining.

(d) Includes public utilities.

sectors capable of making the largest contribution to employment. Apart from long-term planning, this involved the implementation in 1972 of a set of policies known as Operation GROW, designed to stimulate growth and employment in agriculture; (ii) a package of measures designed to address the labour force imbalance on the one level, and the expected shift in labour demand, on the other. It consisted of training and literacy programmes and the establishment and upgrading of various social services in rural areas, including employment information offices; (iii) the creation of employment through public sector work programmes; and (iv) the implementation of an expansionary fiscal and monetary policy.

Between April 1972 and April 1975, the labour force increased at an annual average rate of 2.8%, against only 1.7% in the previous three-year period and a mere 1.4% in the 1960s. This radical upturn was a product not only of the expected bulge in the number of labour force entrants but also of a 60% plunge in net emigration. Nevertheless, the number of jobs created was not only sufficient to absorb this sudden influx, but even to effect important reductions in the number of individuals affected by unemployment. This was accomplished by augmenting employment 3.8% per year, providing a total of 82 000 new jobs in the three-year period. This figure may be compared with the 31 750 jobs added to the market in the twelve years ending in April 1972.

The outcome of the above trends was a decline in the rate of unemployment from 23.6% to 19.9% —the lowest rate recorded since 1969. Male unemployment dropped from 14.3% to 11.1%, and female unemployment from 33.2% to 31.2%.<sup>14</sup>

The turnaround in the employment situation mainly reflected the expansion of employment in the public sector, including public works projects, together with an appreciable rise in the number of jobs in agriculture. Indeed, employment continued to expand in the face of the downturn in output in 1974, and again in 1975 was almost solely a consequence of special public works programmes and increases in the regular public administration. The 44% enlargement in the labour force financed by the public sector between April 1974 and April 1975 was made possible by the enactment of the bauxite levy and the special tax on windfall gains in the sugar sector, which together led to a 62% leap in central government revenues in that fiscal year.

<sup>14</sup>If the size of the labour force had continued to grow at the same pace as in the 1969/1972 period, the overall rate of unemployment could have been reduced to 17.4%.

Contrary to expectations the economy did not recover quickly from the 1974/1975 recession. Employment continued to expand, but not enough to prevent the rate of unemployment from inching up over the course of the ensuing year. When output receded sharply between April and October of 1976, and the public sector was no longer in a position to offset the consequent loss of jobs, the rate of unemployment soared from 20.5% to 24.2% (see table 10).

The persistent decline of the product and the deterioration of public finances, was not, however, accompanied by a further aggravation of unemployment until the second half of 1978. In fact, by April of 1978 the rate of unemployment declined to 23% thanks to an appreciable expansion in agricultural employment.<sup>15</sup>

Unemployment rose sharply once again in the second half of 1978, and following a downturn in the first half of 1979 it climbed drastically to 31.1% in October of that year. In addition to the progressive contraction of the economy, the implementation in mid-1978 of highly restrictive monetary and income policies under the second IMF agreement conditioned the evolution of employment in this period. The exceptional upswing in unemployment in the second half of 1979 was largely a repercussion of the effects of flooding on agriculture, however.

Disastrous weather conditions in the second half of 1980 likewise propelled the rate of unemployment well beyond the proportion attributable to the reduction of output. Thus, while 27.9% of the labour force was without a job in April, 31.5% was in that position in October 1980.<sup>16</sup>

Statistics by age and sex are not available for 1980, but in October 1979 male unemployment reached 19.9% and female unemployment 43.5%. Over 34% of males and 63% of females aged 14 to 29 were unemployed.

When the then Prime Minister announced that the Government had resolved to discontinue negotiations for a new agreement with the IMF in March 1980, one of the main justifications he cited for this decision was that the additional budget cuts sought by the IMF would lead to a further 11 000 unemployed.

Between April 1972 and April 1980 employment increased 17.7%, while the product declined by a similar proportion. About one-half of the expansion in employment took place in agriculture, two-fifths in public administration, and the remainder in commerce. During this period the increase in overall employment averaged 1.8% per annum, against 0.45% between 1960 and 1972, when the product climbed over 90%.

### 3. The external sector

#### (a) *Introduction*

When the government decided to terminate the IMF talks in March 1980, the Bank of Jamaica possessed a mere US\$ 25 million in liquid reserves under circumstances in which the economy faced a projected current account deficit of some US\$ 390 million, or 13.5% of the GDP, if the anticipated contraction in the product were to be limited to 2.5%. This, however, implied a US\$ 300 million overall balance of payments deficit unless additional external finance were to materialize. Otherwise import volume would in fact have to be slashed by a larger proportion than planned, with the result that the decrease in output would be greater than originally contemplated.

<sup>15</sup>The rate of growth of the labour force also slowed at this time due to an upsurge in net emigration. But this type of development may have aggravated, rather than eased, the panorama, as was suggested in connexion with the discussion on the evolution of employment in the 1960s.

<sup>16</sup>Sectoral figures for October 1980 are not available. However, it may be noted that between April and October 1979 employment in agriculture dropped 14%. This decline appears to be wholly attributable to flood damage and disruption, inasmuch as the level of agricultural employment in April 1980 returned to the April 1979 level. In any case, the fall in agricultural employment in April-October 1979 accounted for 70% of the increase in unemployment in that period.

In spite of a decrease in export volume and an increase in import prices and interest rates beyond the dimensions projected, the country managed to avoid external insolvency and internal collapse through a combination of fortuitous circumstances: an unforeseen increment in official capital inflows; an emergency agreement with overseas commercial creditors; and an upturn in the foreign exchange earnings of the parallel economy. In fact, the overall balance of payments registered a surplus of some US\$ 83 million, after taking into account a US\$ 42 million reduction in outstanding obligations with the IMF. This was the first time since 1974 that a surplus had been achieved.

The current account deficit turned out to be US\$ 213 million (7.3% of the GDP), which was substantially more than in 1979, but markedly less than expected. The current value of exports of goods and services rose almost 24% thanks to a 34% hike in the unit price of merchandise exports. The increase in the current value of imports of goods and services was about the same and likewise reflected price behaviour. As a result, the deficit on the commercial account was somewhat smaller than in 1979, instead of the expected four-fold increase. On the other hand, payments of profits and interest rose more than anticipated, to US\$ 267 million, equivalent to fully 9.2% of the GDP.

The actual current account outcome translated into a reduction of US\$ 120 million in the originally identified gap in the overall balance of payments. This, together with unanticipated capital inflows from both formal and informal sources and an increase of US\$ 43 million in arrears, was responsible for the accumulation of US\$ 42 million in gross reserves. From another point of view, it may be observed that the increase in total foreign exchange inflows made it possible to keep the decline in import volume, and hence the decrease in the product, in the neighbourhood of the proportions planned for.

In the light of the failure to reach a new agreement with the IMF and the size of the projected payments gap, the actual performance of the external sector was remarkable. On the other hand, it continued to be mired in crisis: gross international reserves were still insufficient to cover a month's supply of imports of goods and services, while the renewed accumulation of arrears endangered the existence of the remaining sources of supplier credits.

The development and evolution of the crisis is outlined in table 11. The first signs of strain surfaced in the final months of 1972 and continued throughout 1973. The immediate cause was the steep downturn in private direct foreign investment, coupled with an acceleration in the growth of imports. The decrease in foreign investment in the bauxite sector was not accompanied by moderation in import growth because a mildly expansionary fiscal policy and a liberal monetary policy, together with a revaluation of the Jamaican dollar *vis-à-vis* the US dollar, stimulated the demand for imported consumer goods. In 1973 price rises, import controls, devaluation, and a slowdown in the growth of credit combined to reduce imports in real terms. But a decided worsening of the terms of trade led to a further deterioration in the balance of payments. As a result, by the end of that year gross international reserves were sufficient to cover only 1.5 months of imports, versus 3.4 months in 1971.

In 1974 the panorama improved substantially notwithstanding the dramatic increase in the value of imports, the tripling of interest payments on the foreign debt and the second successive downturn in earnings from tourism. In effect, the current value of merchandise exports leaped by more than 90% on the strength of an unprecedented rise in international prices. Simultaneously, the Government enacted the Bauxite Levy, which slashed the outflow of profits on foreign capital by two-thirds. As a result of the above developments, the current account deficit was reduced to 3.5% of the GDP, compared with 12.6% in 1973 and an average of 10.4% between 1969 and 1972. Private foreign investment continued to taper off and short-term capital flows turned highly negative, but long-term credits received by both the public and private sectors offset most of this difference. The overall capacity to import climbed 17%, but the increase in import volume was limited to 3%. Consequently, international reserves climbed almost 50%. But in terms of the prevailing cost and level of imports, the improvement in reserves was appreciably less (see again table 11).

In spite of further large gains in export prices the 1974 turnaround began to lose impetus the following year, as an intensification of the principal adverse trends was accompanied by a marked reduction in export volume.

In 1975 foreign direct investment became negative (as late as 1971 it had been equivalent to fully 11.3% of GDP), while payments of interest on the foreign debt doubled to almost US\$ 44 million, compared to a mere US\$ 8 million just two years earlier. Furthermore, the flight of capital, which first became apparent the previous year, assumed considerable proportions. Nevertheless, net capital inflows reached a new high in nominal terms, owing mainly to the loans contracted by the public sector. In the meantime, the deficit on the trade account quadrupled, primarily because of a 20% plunge in export volume, but also because of another substantial rise in import prices and the persistence of the recession in tourism. The pronounced contraction in export volume, it will be recalled, reflected the decision of the bauxite corporations to slash production in response to the Bauxite Levy.

Table 11  
JAMAICA: CAPACITY TO IMPORT, IMPORT VOLUME AND INTERNATIONAL RESERVES  
(1970 = 100)

	1972	1973	1974	1975	1976	1977	1978	1979	1980
Purchasing power of exports of goods and services	112.7	106.7	129.0	122.3	100.8	99.3	106.2	103.4	104.3
Purchasing power of net imports of capital (a)	72.9	80.3	74.4	98.6	38.8	(b)	(b)	10.1	21.5
Capacity to import	106.1	102.4	120.0	115.9	90.7	79.7	84.1	88.1	90.7
Import volume (c)	114.1	113.9	117.7	126.7	106.0	82.1	87.0	91.6	91.9
Gross international reserves (d)	97.8	59.2	75.4	52.7	15.8	18.8	20.1	20.9	27.5
Gross international reserves/imports (e)	2.4	1.5	1.8	1.2	0.4	0.6	0.6	0.6	0.8
Current account deficit/gross domestic product (f)	10.6	12.6	3.5	10.0	10.3	2.2	3.6	6.4	7.3

Source: CEPAL, on the basis of official data.

(a) Defined here in the difference between the global balance and the commercial balance plus the use made of IMF credit. (See the balance-of-payments data in table 15).

(b) Less than zero

(c) Goods and services.

(d) Deflated by the price index of imported goods and services.

(e) Months of imports of goods and services obtainable with the level of reserves and imports of each year.

(f) At the prevailing rate of exchange.

The deficit would have reached enormous proportions —or import volume would have had to be compressed— if it had not been for an additional 34% advance in export prices. Even so, however, the current account deficit rose from 3.5% to 10% of the GDP.

While relatively less than the record 1973 deficit and even somewhat smaller than the 1969/1972 average, the relation between the deficit and the structure of demand in 1975 was appreciably different from the one prevailing in the earlier period. Between the mid-1960s and early 1970s the large current account deficits were associated with high rates of both investment and savings, and this pattern reached its zenith when investment climbed to almost one-third and savings more than a quarter of the product in 1969 and 1970. Consumption was then around only 70% of output. Between 1970 and 1974, however, the investment coefficient tapered off, while consumption rose to about 78% of the product, and in 1975 consumption climbed to 82.5% of the product, while savings fell to less than 15%.

This shift in the allocation of income between consumption and savings is traceable to a substantial modification in the distribution of income in favour of wage earners, a surge in inflation to a rate well above nominal interest rates, and an expansionary fiscal policy.

One of its main effects was to maintain the demand for imports in spite of the evaporation of the large foreign investment inflows; that is to say, when investment declined, one of the factors that prevented the deficit on the current account from contracting was the stimulation of consumer demand for imports. On the other hand, it should be emphasized that 85% of the doubling of the current value of imports between 1971 and 1975 was accounted for by price inflation—at constant prices imports increased only 18%.<sup>17</sup>

In 1975 the capacity to import contracted slightly more than 3%, but the volume of imports rose close to 8%. As a result gross international reserves dropped 30% to a level sufficient to cover only somewhat more than one month of imports (see again table 11).

As 1976 unfolded, both the capacity to import and the payments position deteriorated steadily, and by the end of the year the authorities suspended foreign exchange transactions in order to avoid the total depletion of the gross reserves.

In 1976 the full effects of the international recession were thus finally manifested in Jamaica's external sector, as foreign demand for the country's principal exports, including tourism, contracted appreciably. The price of sugar, for instance, plunged 60%. At the same time, labour-management disputes and technical problems in the bauxite/alumina sector reduced the supply of mineral exports, while domestic strife aggravated the depression in tourism. As a result of these circumstances the value of the exports of goods and services declined by US\$ 166 million, or by more than 15%.

In the meantime, a 50% jump in interest payments on the external debt and a cut-off of private transfers on the one hand, and a more than 50% reduction in net short and long-term capital inflows on the other, pushed the net contribution of total capital flows to the capacity to import close to zero. However, this heavy blow was partially offset by the use of IMF credit under the petroleum and compensatory facilities and loans from other official sources.

The decline in exports and in capital flows translated into a drop of fully 22% in the overall capacity to import, and since the 17% reduction in import volume was somewhat less,<sup>18</sup> the global balance of payments suffered a record deficit of US\$ 187 million, equivalent to 6.3% of the GDP. The result was the virtual exhaustion of gross reserves: indeed, the net international reserves fell below zero. The current account deficit—10.3% of the GDP—was, on the other hand, similar to the one experienced in 1975. From this angle, the rundown of reserves appears as the counterpart of the paralyzation of commercial bank lending to Jamaica. In any case, the economy was squeezed between impending bankruptcy and an abrupt cutback in supply. The product decreased more than 6% and gross national income dropped almost 11%.

In the following year (1977) the precarious external payments situation improved considerably, thanks mainly to a remarkable 23% contraction in import volume, but also to a 15% increment in the current value of merchandise exports. The overall trade account in fact registered a surplus—the first one in the post World War II era. This performance, together with a partial recovery of private transfers, permitted reduction of the current account deficit to a level equivalent to 2.2% of the GDP. But the inflow of long and short-term capital once again decreased sharply, with the result that even this modest deficit entailed another, albeit small, deficit in the overall balance of payments. However, gross reserves rose slightly because of the use made of IMF credit.

The enormous reduction in imports—which clearly bore the brunt of the attack on the crisis—was accomplished through a combination of severe controls, an incomes policy, increased taxes and devaluation. And in the second half of the year the Government added to its arsenal a programme of fiscal and monetary restraint under a two-year US\$ 75 million stand-by agreement with the IMF. However, this accord was terminated in December and the scheduled US\$ 15 million

<sup>17</sup> In this connexion, it should be emphasized that these data are highly sensitive to the choice of the base year, which in this case is 1970, owing to the radical change in relative prices in 1974. If the prices prevailing in 1974 are used, the quantum of imports did not increase at all in this period.

<sup>18</sup> The volume of merchandise imports was actually compressed by 20.5%.

credit instalment cancelled when one of the performance criteria was not met. This setback also held up the disbursement of a large World Bank loan and a loan package negotiated with a group of commercial banks. The interruption of this agreement thus largely explains why the dramatic turnaround in the current account was not accompanied by any improvement in the capital account.

Most of the principal external aggregates evolved about the same in 1978 as they did in 1977. Thus, another surplus was achieved on the overall trade account, but once again the net movement of capital flows was negative, and the small current account deficit did not translate into a surplus on the overall balance of payments. In fact the deficit on the balance of payments widened. The small gain in gross reserves was made possible by the use of credit under a new agreement with the IMF.

On the other hand, for the first time since 1974 the capacity to import did not contract, thanks mainly to a major recuperation by tourism, but also to a modest recovery of mineral exports. The small increment in import capacity was matched by an expansion in import volume, following the enormous contraction of the previous three years.

In spite of a new downturn in the income terms of trade and an actual outflow of funds on the capital account, the country was able to augment import volume by an additional 5% in 1979 without depleting the gross reserves, thanks to a large infusion of IMF credit. But as had occurred with the first accord, the Government failed to comply with one of the performance criteria and the agreement was cancelled in December.

In early March 1980, the negotiations for an interim one-year agreement with the IMF were deadlocked over the question of the extent of further budgetary cutbacks and the effects of these on employment. At this juncture, the Government received a report from the Ministry of Finance indicating that by September at the latest the country would be unable to comply with the net international reserves performance test (the same one it had failed to pass in December). In the light of this, and owing to the further unemployment the new accord would entail, the Government resolved to break off the talks and call early elections. The alternative short-term economic programme it adopted rested on a crucial assumption: that the existence of a balance of payments gap would bring forth the necessary finance. And, in fact, the course of events did accommodate to Jamaica's external financing requirements, without the IMF agreement: the inflow of funds on the capital account was not only sufficient to finance a current account deficit equal to 7.3% of GDP—the largest since 1976—but also to cover the repayments to the IMF and attain a surplus on the overall balance of payments for the first time since 1974. Furthermore, the net inflow on the capital account turned out to be the largest, in constant terms, since 1975: over three times the level of 1977, and over five times the level of 1978. As already mentioned, 1979 saw a net outflow. After accounting for the movements of IMF credit, the net flow in 1980 was still one-third larger than in 1979, four-fifths larger than in 1978, and well over twice the 1977 one.

#### (b) *Merchandise trade*

(i) *Exports.* The improvement in the overall balance of payments in 1980 was in large part attributable to the performance of the bauxite sector. In effect, the total value of bauxite and alumina exports climbed over 29% (see table 12). While the volume of alumina exports climbed 15% to its highest level since 1974, the chief factor here was the 39% leap in international prices (see table 13).<sup>19</sup> The evolution of the other main traditional exports was not favourable. The value

<sup>19</sup>In this connexion it is of interest to note that bauxite is the mineral whose value has best stood up to the petroleum price onslaught. Between 1973 and 1980 the price of bauxite multiplied 3.5 times, while its relative international price rose almost four-fifths. It thus managed to retain about one-third of its value in terms of petroleum through 1980, with 1965 as the base year. If 1970 were chosen as the base, the deterioration is greater (over four-fifths). On the other hand, over the period 1974-1980 the price of bauxite in terms of petroleum did not decrease at all, in spite of the 1979/1980 round of petroleum price hikes. In the same period the price of tin in terms of petroleum declined close to one-third; and that of iron ore, over one-half.



of banana exports dwindled to US\$ 10 million (from US\$ 18 million in 1979), owing to the massive destruction of plantations by Hurricane Allen. For its part, the value of sugar exports expanded less than 1% notwithstanding the tripling of the international price of sugar and the 23% adjustment of the EEC price. As has occurred for the last several years, Jamaica was unable to fulfill its quota with the EEC in 1980 and for this reason could not take advantage of the sharp rise in the free market price, the shortfall in production in 1980 being provoked by poor weather.

Table 12

JAMAICA: EXPORT OF GOODS, FOB

	Millions of dollars			Percentage breakdown		Growth rates		
	1978	1979	1980	1970	1980	1978	1979	1980
<b>Total</b>	<b>795</b>	<b>815</b>	<b>992</b>	<b>100.0</b>	<b>100.0</b>	<b>7.6</b>	<b>2.5</b>	<b>21.7</b>
Main traditional exports	649	639	810	75.8	81.7	8.7	-1.5	26.8
Alumina	418	368	552	38.9	55.6	10.8	-12.0	50.0
Bauxita	171	214	201	26.7	20.3	6.8	25.1	-6.1
Sugar	60	57	57	10.2	5.8	-	-5.0	-
Other exports	146	176	182	24.2	18.3	12.1	20.5	3.4

Source: Bank of Jamaica, Report and Statement of Accounts, 1980; and Jamaica Department of Statistics. *External Trade*, 1979.

(ii) *Imports*. The value of imports (CIF) rose over 19% in 1980, or somewhat less than that of exports (see table 14). The sole cause of this movement was external inflation, inasmuch as the import quantum did not vary.<sup>20</sup> In this respect, the outstanding development was, of course, the jump of two-thirds in the international price of petroleum. In last year's *Survey* some of the effects of the oil price revolution on the Jamaican economy were explored. Suffice it to recall here that the economy is very energy-intensive, due primarily to the energy consumption of the bauxite sector, while at the same time 99% of the island's commercial energy supply comes from imported oil. The further marked increase in the price of oil was thus a heavy blow, particularly in the light of the severe constraints operating on the availability of foreign exchange in the economy. The increase in the oil bill accounted for 70% of the rise in the value of imports, and absorbed 41.5% of total imports in 1980, against only 22.8% just two years before.<sup>21</sup>

The substantially higher expenditures on food imports, for their part, were made necessary by the large reduction in agricultural production.

Together, the much enlarged outlays for energy and food resulted in a cutback in the nominal expenditure for other imports (see again table 14).

(iii) *The terms of trade*. In 1980 the terms of trade index, with 1970 as the base year, showed a gain of about 6%, and thus stood close to one-fourth higher than in 1970. On the other hand, it remained some 7% below the high registered in 1975 (see table 15).<sup>22</sup>

<sup>20</sup>The volume of merchandise imports in fact dropped 7%.

<sup>21</sup>Petroleum and petroleum products make up virtually the entire value of mineral fuel imports.

<sup>22</sup>As was discussed in connexion with the evolution of the import volume in the introduction to this section, the use of 1970 as the base year results in a distortion of the post-1973 situation in countries in which petroleum constitutes a relatively larger share of exports or imports. In the case of Jamaica the evolution of the terms of trade would appear much less favourable if the base year were chosen so as to take account of the dramatic shift in relative international prices in 1973/1974.

Table 13

JAMAICA: NOMINAL AND RELATIVE PRICES OF BAUXITE  
(1965 = 100)

Year	Nominal price	Relative price (a)	Price of bauxite/ price of petroleum
1966	112.6	107.1	112.6
1967	130.4	119.1	130.4
1968	133.7	116.8	136.8
1969	131.6	109.4	136.8
1970	131.6	103.2	134.7
1971	153.8	113.9	123.9
1972	165.5	115.9	115.8
1973	188.4	120.3	92.8
1974	223.3	123.7	30.4
1975	327.0	159.5	40.6
1976	364.2	159.3	42.1
1977	418.7	161.5	44.9
1978	429.9	145.2	45.0
1979	473.9	142.3	37.1
1980	659.8	178.8	30.6

Source: IMF, *International Financial Statistics*, various volumes.

(a) Nominal price deflated by world prices.

Table 14

JAMAICA: IMPORT OF GOODS, CIF

	Millions of Jamaica dollars			Percentage breakdown		Growth rates		
	1978	1979	1980	1970	1980	1978	1979	1980
<u>Total</u>	<u>865</u>	<u>1 003</u>	<u>1 196</u>	<u>100.0</u>	<u>100.0</u>	<u>10.4</u>	<u>16.0</u>	<u>19.3</u>
Food	169	130	192	17.2	16.1	26.1	-23.5	48.2
Mineral fuels	197	335	470	6.4	39.3	-12.2	70.3	40.2
Manufactured goods	222	221	205	26.1	17.2	29.9	-0.3	-7.1
Machinery and transport equipment	110	143	139	32.3	11.6	16.7	30.5	-2.9
Other	167	174	190	18.0	15.8	7.0	4.1	9.2

Source: Bank of Jamaica, *Report and Statement of Accounts*, 1980; and Jamaica, Department of Statistics, *External Trade*, 1979.

(c) *Services trade*

The modest surplus on trade in non-factor services was more than offset by the outflow in respect of profits and interest. Receipts from tourism stagnated in 1980, but other non-factor services showed a large expansion. In the meantime, remittances of profits climbed markedly, and exceeded US\$ 100 million for the first time since the enactment of the Bauxite Levy, while interest payments on the debt continued to rise at a fast pace. The sum of profits and interest payments equalled an unprecedented 9.2% of the GDP in 1980. On the other hand, private transfers remained buoyant as Jamaicans residing overseas responded to the distress caused by Hurricane Allen.

(d) *The current account position and its financing*

The outcome of the movements on merchandise and services trade was an overall current account deficit of US\$ 213 million, or 7.3% of the GDP (see table 16). This was the third successive

Table 15  
JAMAICA: MAIN FOREIGN TRADE INDICATORS

	1975	1976	1977	1978	1979	1980(a)
	<u>Annual growth rates</u>					
Exports of goods						
Value	7.5	-18.4	15.2	4.5	2.5	21.8
Volume	-19.5	-10.4	2.2	2.5	-4.9	-9.1
Unit value	33.6	-9.4	12.8	2.0	7.8	34.0
Imports of goods						
Value	19.5	-18.4	-15.8	12.5	17.7	20.2
Volume	5.2	-20.5	-20.5	4.8	5.9	-2.1
Unit value	13.6	2.6	6.0	7.3	11.1	29.5
Terms of trade	18.2	-11.6	6.4	-4.7	-2.9	6.4
	<u>Indexes (1970 = 100)</u>					
Terms of trade	134.4	118.8	126.5	120.5	117.0	124.4
Purchasing power of exports of goods	137.3	108.7	117.6	114.8	106.5	105.8
Purchasing power of exports of goods and services	122.3	100.8	99.3	106.2	103.4	104.3

Source: CEPAL, on the basis of official data.

(a) Preliminary figures.

year in which the current deficit increased both as a percentage of the product and in real terms, following its drastic reduction in 1977. But it remained modest in comparison to the ones sustained prior to 1977, when the average deficit equalled about 10% of the GDP.

Complete information on the breakdown of the financing of the deficit in 1980 is not yet available. However, provisional data of the Bank of Jamaica reveal that net public sector borrowing amounted to US\$ 120 million, or about 40% of the net inflow on the capital account. Precise figures on gross borrowing have yet to be published, but it may be mentioned that the Government raised well over US\$ 100 million from various OPEC nations. Of this amount, US\$ 50 million came from Libya, while US\$ 38 million represented advances under the Venezuelan petroleum loan facility.<sup>23</sup>

A significant proportion of the difference between the overall net movement of capital and the net borrowing of the public sector apparently originated from the parallel economy.<sup>24</sup>

For the first time since 1974, a surplus was registered on the overall balance of payments. One half of this was absorbed by the debt with the IMF, while the other half was used to augment the gross reserves. However, the increase in gross reserves may be viewed as being offset by an increment of virtually the same amount in arrears. In any event, the extent of the expansion of arrears was less than 40% of that originally anticipated.

#### (e) *External indebtedness*

Following an expansion of two-fifths between 1977 and 1979, the external debt outstanding rose by 7.5% to slightly more than US\$ 1 600 million in 1980,<sup>25</sup> but after allowing for the increase

<sup>23</sup>Bank of Jamaica, *Report and Statement of Accounts, 1980*, Kingston, 1981.

<sup>24</sup>Estimates of the size of the parallel economy vary widely, but there is general agreement that the foreign exchange it generates made an important contribution to financing the observed current account deficit. Strictly speaking, these foreign exchange inflows are payments for illicit exports. Hence, the current account deficit was in fact less than the recorded one by an amount equal to the value of these exports.

<sup>25</sup>Note that the external debt as defined in table 17 excludes public and State-guaranteed debt having a maturity of less than one year and private debt not guaranteed by the State. In 1980 the debt on these accounts totalled approximately US\$ 200 million.

Table 16

JAMAICA: BALANCE OF PAYMENTS  
(Millions of US dollars)

	1974	1975	1976	1977	1978	1979	1980(a)
Exports of goods and services	1 030	1 099	933	979	1 122	1 208	1 492
Goods FOB	752	808	660	760	795	815	992
Services (b)	278	291	273	219	327	393	500
Transport and insurance	60	74	77	69	100	114	150
Travel	133	129	106	72	147	195	198
Imports of goods and services	1 079	1 307	1 126	929	1 056	1 228	1 511
Goods FOB	811	970	791	667	750	883	1 061
Services (b)	268	337	335	262	306	345	450
Transport and insurance	162	193	171	148	182	203	300
Travel	21	52	59	12	10	11	10
Trade balance	-49	-208	-193	50	66	-20	-19
Profits and interest	-68	-103	-116	-138	-178	-203	-267
Profits	-47	-59	-50	-38	-92	-82	-115
Interest	-21	-44	-66	-100	-86	-121	-152
Unrequited private transfer payments	34	23	2	15	15	70	73
Balance on current account	-83	-288	-307	-73	-97	-153	-213
Unrequited official transfer payments	-9	5	4	5	10	10	9
Long-term capital	226	228	144	46	-32	-9	...
Direct investment	23	-2	-	-7	-27	-26	...
Portfolio investment	-1	-4	4	-	-	-	...
Other long-term capital	204	234	140	53	-5	17	...
Official sector (c)	107	154	129	48	172	71	...
Loans received	119	159	160	96	275	174	...
Amortization payments	-7	-4	-29	-47	-104	-111	...
Commercial banks (c)	-	-	-	-	-	-	...
Loans received	-	-	-	-	-	-	...
Amortization payments	-	-	-	-	-	-	...
Other sectors (c)	97	80	11	5	-177	-54	...
Loans received	89	115	57	33	-	-	...
Amortization payments	-14	-21	-29	-37	-177	-54	...
Basic balance	134	-55	-159	-22	-119	-152	...
Short-term capital	-49	95	9	56	40	1	...
Official sector	5	26	48	-9	-	-	...
Commercial banks	-12	2	5	-	5	3	...
Other sectors	-42	67	-44	65	35	-2	...
Errors and omissions	-15	-83	-34	-48	26	-15	287
Counterpart items (d)	-3	9	-3	2	-3	3	...
Global balance	67	-34	-187	-12	56	-163	83
Total variation in reserves (- sign indicates an increase)	-67	34	187	12	56	163	-83
Monetary gold	-	-	-	-	-	-	-
Special Drawing Rights	2	1	4	-16	12	5	1
IMF reserve position	-	-	-	-	-	-	-
Foreign exchange assets	-62	58	88	3	-19	-8	-41
Other assets	-7	-25	31	3	-	-	...
Use made of IMF credit	-	-	64	22	63	166	-42

Source: 1975-1979: International Monetary Fund, *Balance of Payments Yearbook*, (magnetic tape, March 1981); 1980: CEPAL, on the basis of official data.

- (a) Preliminary figures.
- (b) Services also include other official and private transactions, but exclude profits and interest.
- (c) In addition to loans received and amortization payments made, this entry includes net loans granted and other assets and liabilities.
- (d) Includes counterpart items in respect of monetization or demonetization of gold, allocation or settlement of Special Drawing Rights, and variations due to revaluation.

in gross reserves, the net position registered an increase of less than 5%.<sup>26</sup> Owing to the modest increment in money terms and to an acceleration in international inflation, the external debt decreased—for the first time in a decade—by 12% at constant prices. It also declined in relation to the product: from 62.4% to 55.3% at the prevailing rate of exchange, and from 53.4% to 48.1% at the real rate of exchange. This was also the first year since the 1960s in which the debt/product ratio fell.

Measured in terms of the exports of goods and services, the burden of debt service lessened for the second consecutive year, thanks to both the expansion of exports and to an interruption in the growth of debt payments. On the other hand, interest on the debt continued to absorb an even larger proportion of the GDP, due mainly to the persistent contraction of the product (see table 17).

Table 17

JAMAICA: INDICATORS OF EXTERNAL INDEBTEDNESS

	1970	1972	1973	1974	1975	1976	1977	1978	1979	1980(a)
Debt (b) (millions of US dollars)	129	210	354	528	706	965	1 052	1 236	1 495	1 607
Gross reserves (millions of US dollars)	139	160	127	190	126	32	48	59	63	105
Debt index (1970 = 100)										
Current prices	100	163	274	409	547	748	816	958	1 159	1 246
Constant prices	100	155	242	267	409	543	556	609	667	585
Debt/gross domestic product										
Prevailing rate of exchange	9.2	11.7	18.5	22.1	24.6	32.3	38.7	49.1	62.4	55.3
Real rate of exchange (c)	9.2	11.6	17.6	23.5	27.3	38.3	39.0	44.0	53.4	48.1
Debt service (percentages) (d)										
Exports (e)	0.5(f)	1.4	3.6	4.1	7.3	13.3	22.2	25.1	24.2	21.7
Gross domestic product (g)	0.4(f)	0.1	0.4	0.9	1.5	2.2	3.7	3.4	5.0	5.2
Debt sources										
Official lenders	41.0	37.1	36.2	29.9	27.8	41.9	45.6	53.8	66.8	68.9
International organizations	22.7	16.6	11.0	7.9	7.7	7.8	9.6	12.8	13.2	16.6
IMF	-	-	4.2	3.1	2.2	8.3	10.2	14.6	23.5	19.2
Governments	18.3	20.5	21.0	18.9	17.9	25.8	25.8	26.4	30.1	33.1
Private lenders	58.6	62.9	63.8	70.1	72.2	58.1	54.4	46.2	33.2	31.1
Debt uses										
Interest	56.5	23.0	10.6	16.2	24.0	20.7	43.1	24.0	23.6	68.6
Amortization	43.5	30.9	12.2	14.8	14.6	21.7	56.9	41.4	28.3	32.4
Investment	-	25.8	54.3	16.1	61.4	-	-	34.4	34.1	-
Consumption	-	20.3	22.9	52.9	-	57.6	-	0.2	14.0	-
Average rate of interest	...	8.3	8.3	9.7	9.5	7.7	6.4	6.8	7.7	...
Average maturity (h) (years)	...	9.4	12.8	15.9	11.5	14.3	15.2	17.6	17.7	12.2

Source: CEPAL, on the basis of data provided by the World Bank, IMF and the Bank of Jamaica.

(a) Preliminary figures.

(b) Disbursed public and State-guaranteed, private debt and use made of IMF credit.

(c) Trade weighted.

(d) From the balance of payments.

(e) Amortization and interest payments as a proportion of exports of goods and services.

(f) Receipts.

(g) Interest payments as a proportion of gross domestic product.

(h) On commitments of each year.

The main developments affecting the external debt situation in 1980 included the break-off of talks with the IMF, the conclusion of an emergency agreement with the country's commercial creditors, and an upturn in the flow of credits from official sources other than the IMF.

The March decision to terminate negotiations for a new accord with the IMF not only closed the door to the additional use of IMF credits, but entailed a reduction in the outstanding obligations with the Fund over the course of the year, and this accounted for the slowdown in the growth of the

<sup>26</sup>It should, however, be recalled that the increase in gross reserves in 1980 was achieved by allowing arrears to accumulate. The total of US\$ 120 million in arrears at year's end exceeded the holding of gross reserves.

external debt in 1980. Thus, whereas Jamaica received IMF credits totalling US\$ 73 million in 1978, and US\$ 171 million in 1979, it effected amortizations of US\$ 43 million on this account in 1980 (see table 18).

The Government managed, however, to augment net borrowing from other sources by an amount sufficient to cover repayments on its debt with the Fund and make up for most of the hypothetical inflow that would have been available had a new arrangement been reached with the Fund.<sup>27</sup>

Table 18

JAMAICA: USE OF IMF CREDIT (a)  
(Millions of US dollars)

	1975	1976	1977	1978	1979	1980
Credit tranche drawings, ordinary	-	-	23	25	16	7
Compensatory drawings	16	46	48	62	98	94
Buffer stock drawings	-	-	-	-	1	-
Extended facility, ordinary	-	-	-	55	102	87
Extended facility supplementary	-	-	-	-	103	99
Oil facility drawings	-	34	36	38	31	21
<b>Total</b>	<b>16</b>	<b>80</b>	<b>107</b>	<b>180</b>	<b>351</b>	<b>308</b>
Net yearly flow	-	64	27	73	171	-43

Source: International Monetary Fund, *International Financial Statistics*, Vol. 34, May 1981.

(a) Cumulative totals.

The principal factors involved here were the temporary scheme to refinance the public and State-guaranteed debt owed to foreign commercial banks, and an increase in loans from official lenders.

In mid-1979 the Government had negotiated an accord with the banks to postpone 87.5 % of the principal payments falling due between April 1979 and April 1981. The deferred sum was converted into a 3.5 year loan, with payment commencing in April 1982 but the existence of the agreement depended on Jamaica's compliance with the following conditions: (i) the amortization of the balance of the debt as it matured; (ii) the timely cancellation of interest charges on the entire debt; and (iii) the satisfaction of the quarterly performance criteria under the IMF agreement then in force, which was scheduled to last until April 1981. Consequently, the refinancing arrangement was placed in jeopardy when Jamaica failed the performance tests in December 1979, and the Government's decision to end negotiations for an interim agreement with the Fund in March was tantamount to the repudiation of the arrangement. Nevertheless, in April the Government persuaded the bankers' bargaining team (Steering Committee of Bankers) to allow the refinancing

<sup>27</sup>The use of the term "hypothetical" stems from the fact that the receipt of the full amount (US\$ 135 million) of the credit under the agreement being discussed in early 1980 with the IMF would have been contingent on the fulfillment of certain performance tests over the course of the year. However, as noted previously, the Ministry of Finance authorities were convinced that one or more of the tests would be failed by September at the latest. And in this connexion it should also be reemphasized that the magnitude of the net borrowing that actually materialized could have been less if an agreement had been concluded with the Fund. The bibliography on the IMF-Jamaica relationship in the period under review is lengthy. The principal sources consulted here include: Bank of Jamaica, *Report and Statement of Accounts* (especially 1978, 1979 and 1980); R.L. Bernal, "Transnational Commercial Banks, The International Monetary Fund and Capitalist Crisis in Jamaica 1972-1980" (paper presented at the Conference on Finance Capital and Dependence in the Transnational Phase: A Latin American Perspective, Instituto Latinoamericano de Estudios Transnacionales y Centro de Estudios Económicos y Sociales del Tercer Mundo, Mexico City, March 4-7 1980); N. Girvan, R.L. Bernal and W. Hughes "The IMF and the Third World: The case of Jamaica 1974-1980", *Development Dialogue*, 1980:2; G.R. Kincaid, "Fund aids Jamaica to restart its economic growth", *IMF Survey*, 22 December 1980, and "Conditionality and the use of Fund resources, Jamaica", *IMF, Finance and Development*, June 1981, Vol. 18, No. 2; People's National Party "The Way Forward. An Alternative Self-Reliance Economic Path Prepared by the People's National Party", Kingston, Mimeo, 1980.

scheme to remain in force, subject to monthly reviews and the payment of interest charges on deferred debt each month instead of every six months, and in September the Steering Committee agreed to the suspension of all debt amortization for the rest of the year. The deferred loans were rolled over on a monthly basis.

The previous and revised schemes permitted a reduction in principal payments totalling more than US\$ 62 million in comparison to the previous year. These temporary savings, together with the increase in loan receipts from official lenders, equalled over 90% of the IMF credits extended to Jamaica in 1979, and amounted to almost four times the repayments made to the Fund in 1980. On the other hand, the inflow of capital from formal sources did in fact fall short of the level the authorities sought, and given the rise in interest rates, turned out to be insufficient to cover the servicing of the debt in spite of the decrease in amortization (see again table 17). The injection of foreign exchange from informal sources more than offset this gap. In the case of central government finances, however, the shortfall placed the burden of the financing of the large fiscal deficit on the domestic banking system.

The evolution of various aspects of the external debt over the course of the 1970/1980 period is traced in table 17. As may be seen, in 1970 Jamaica was in an unusual position for a middle-income country: it was a net creditor with the rest of the world. This situation turned around in 1972, however, and between that year and 1976 the external debt multiplied 4.6 times in nominal terms (and 3.5 times at constant prices) while the gross international reserves plunged by four-fifths; the debt/GDP ratio climbed from 11.6% to 38.3% at the real rate of exchange; and amortization and interest payments as a share of exports leaped from 1.4% to 13.3%. Subsequently, the growth of the debt slowed markedly: it rose two-thirds between 1976 and 1980 in nominal terms and merely 8% at constant prices, while in the meantime holdings of gross reserves increased. However, the debt climbed from 38.3% to 48.1% as a proportion of the product, and interest on the debt absorbed more than 5% of the GDP in 1980, versus 2.2% in 1976 (and 0.1% in 1972).

In the first period, running from 1972 to 1975, the most important factor in the expansion of the debt was the stepped-up central government investment programme. Initially, this programme, as well as the decision to finance an important part of it through foreign borrowing, arose mainly as a response to the end of the investment cycle in the mining sector. Also of importance, however, was the expansion of social programmes on the one hand, and the attractive external debt terms available to the country, on the other. Subsequently, the progressive enlargement of the budget became a reaction to the generalized downturn in investment and in the overall level of activity. The appeal of financing a substantial proportion of the growing fiscal deficit from external sources was reinforced by the intensification of balance of payments problems. Thus, almost 53% of the increase in the external debt between 1972 and 1975 went to finance part of the capital expenditure programme of the central government. The other half of the growth of the debt was divided between financing diverse investment projects in the rest of the public sector and hotel expansion in the private sector.<sup>28</sup> While the foreign borrowing that took place in this period was thus channelled into investment, an analysis of the destination of the almost five-fold increase in the external debt from the perspective of the expenditure pattern of the economy as a whole reveals a different picture. As may be observed in table 17, the implied distribution of the increment in debt shows that around one-fifth of it went into consumption in 1972 and 1973, while in 1974 fully one-half of the total external loans received financed current consumption. On the other hand, in 1975 all net borrowing financed investment.<sup>29</sup>

<sup>28</sup>These private debts were guaranteed by the public sector under a programme implemented by the previous administration to encourage the expansion of capacity in tourism.

<sup>29</sup>The analysis of the uses of debt follows from the observations that interest and amortization have the first claims on loans receipts and that *ex-post*, net borrowing finances consumption to the extent that it exceeds the increase in investment (as occurred in 1972 through 1974).

The following year—one of profound crisis for the economy—marked the end of the period of rapid growth of the external debt and the beginning of the one in which the central government used foreign loans to help finance its current expenditures. For the 1976/1980 period as a whole, the accumulated current deficit exceeded total available foreign financing to the central government by 54.5%.<sup>30</sup> In only one year, 1978, were foreign loan receipts sufficient both to cover the gap on the current account and to finance an appreciable proportion of capital expenditures.

As far as the overall economy was concerned, the results were mixed. Thus, in 1976, when the GDP dropped by more than 6% and gross national income by almost 11%, over half of the large increment in the foreign debt was diverted to consumption. In 1977 the total net borrowing was in fact slightly less than the interest charge on the past debt. In 1978 and 1979, on the other hand, somewhat more than one-third of the much enlarged inflow was devoted to investment. In this connexion, it is interesting to juxtapose the reallocation of private expenditure in favour of investment in 1978 and especially in 1979, with the emphasis placed by the Government on the maintenance of current consumption, and to compare this pattern with the one that emerged in 1972/1974, when the increase in public investment was accompanied by the eventual diversion of an appreciable share of foreign loan receipts to consumption purposes in the private sector.

From the very outset commercial banks constitute the principal source of Jamaica's foreign borrowing, and by 1975 private lenders held over 72% of the country's outstanding foreign debt (see again table 17). This distribution of course raised the average rate of interest and shortened the maturity structure of the debt in comparison to one in which greater reliance is placed on official sources. Furthermore, it appears that the rate of growth of the external debt in the first half of the decade was so rapid that it exceeded the ability of the public sector to prepare projects fast enough to take advantage of the lower cost financing that otherwise could have been requested from official lenders. In any event, in what was both a reaction to the economic crisis and a factor which severely aggravated it, the foreign banks ceased all lending to Jamaica in 1976, and over the course of the ensuing four years their principal aim was the repatriation of their investments in the country.

In 1976 Jamaica applied for and received access to the IMF's oil facility and compensatory drawing scheme (available in order to deal with shortfalls in export earnings). All told, it obtained US\$ 64 million from the Fund that year (see table 18). These resources, together with the loans acquired from other official lenders (including US\$ 55 million from Trinidad and Tobago), temporarily counterbalanced the interruption of commercial bank lending. Nevertheless, by December of 1976 the deterioration in the external payments situation had reached the point where the authorities were forced to close the foreign exchange market in order to avoid the imminent exhaustion of liquid reserves. Following on-and-off negotiations with the IMF and the adoption of a series of measures to confront the economic crisis, the government and the IMF reached agreement in August on a two-year stand-by arrangement. Under this accord Jamaica would have access to US\$ 75 million, or 121% of its Fund quota (but only 1.4% of its GDP), over the course of a two-year period, provided it satisfied the performance criteria used to assess the progress of the stabilization programme to be adopted.<sup>31</sup> However, after just one disbursement this stand-by arrangement was suspended in December when Jamaica failed to meet the performance test relating to the net domestic assets of the Bank of Jamaica. Thus the country actually obtained a much smaller amount of IMF credit than in 1976, when the use of the compensatory and oil facilities in fact had not entailed any binding conditionality. Furthermore, this failure undermined a potential loan package with a group of commercial banks and postponed disbursements from a sizeable World Bank loan. Finally, the Government was unable to mobilize additional support of any magnitude from bilateral sources. In consequence, and despite the sacrifices

<sup>30</sup>The sum of ordinary and extraordinary foreign borrowing by the Government was slightly greater than the current deficit in the central government's budget. However, the extraordinary receipts (the IMF credits), were not directly available to fund the Government's budget deficits.

<sup>31</sup>The specific policies and performance tests adopted under this and ensuing agreements are described in the final section of this survey.



entailed in the reduction of the current account deficit from 10.3% to 2.2% of the GDP, only a marginal improvement in the overall balance of payments was obtained, since the total amount of borrowing was not quite sufficient to cover amortization and interest payments (see again table 17).

Following another prolonged round of strenuous bargaining a new agreement was put into place in May of the following year. This time Jamaica would have the option of purchasing SDR 200 million (then about US\$ 240 million) under a three-year Extended Fund Facilities (EFF). In exchange, the country's authorities were to adopt a package of drastic measures designed to turn the economy around. As usual, the release of credits would depend on the progress of the stabilization programme as measured by the results of the performance tests.

The yearly installment available under the EFF worked out at 3.2% of the GDP, or well over twice the proportion available in the previous agreement, but still much too modest an amount to restore the quantum of imports to the level obtaining prior to the balance of payments crisis, or even to the depressed volume of 1976.<sup>32</sup> Consequently, it was clear that an additional and very substantial sum of external resources was needed to arrest the contraction of output and facilitate the growth of exports, and considerable efforts, including in particular the EFF itself, were undertaken by the Government and the IMF to attract this support. Mainly as a result of these, the Caribbean Group for Co-operation in Economic Development was founded in June 1978. At this time Jamaica received loan pledges totalling about US\$ 54 million from donor countries and it also benefited from a US\$ 30 million programme loan from the World Bank. On the other hand, the response of the private international financial community was less than expected, as it was limited to the refinancing of 87.5% of the public and State-guaranteed debt. No new loans were obtained, and as a result net borrowing from this source was negative. The total response (exclusive of IMF credits) amounted to US\$ 107.4 million on a net basis in 1978. This was equivalent to 4.0% of the GDP, a somewhat greater proportion than the one absorbed by interest payments on the external debt.

In 1978 the balance of payments showed some improvement over 1977, in spite of a deterioration of the terms of trade and a sharp upturn in profit remittances, as it was possible to augment import volume by 6% and maintain the current account deficit at about the same modest level as in 1977, while decreasing arrears and increasing marginally the gross reserves. Notwithstanding this, and the satisfaction of the various performance criteria of the stabilization programme in both September and December, the economy continued to deteriorate, and indeed the rate of decline was in fact steeper than in 1977. Import volume needed to be raised much more, and in the absence of a dramatic turnaround in exports or the materialization of a massive foreign investment project, this meant that the country needed to obtain access to a much larger amount of external finance. But this was not to be the case.

Events in the first half of 1979 unfolded along a similar course. The quarterly performance tests were met, import volume rose moderately without leading to a reduction in reserves, and the economy continued to contract but at an even faster pace. In June the Government and the IMF agreed to modify various aspects of the stabilization programme in the light of the obtained and pending results. Simultaneously, Jamaica was able to benefit from a recent liberalization of the limits on the use of IMF credit. Thus, during the final two years of the EFF, Jamaica would be eligible to draw US\$ 340 million from the Fund instead of US\$ 160 million. In addition, US\$ 80 million was to be disbursed in the first two months. The level of financing in the June 1979 to June 1980 period would have been equivalent to 7.1% of the 1979 GDP.

Even this greatly expanded availability of IMF credit did not provide the full amount of support required to halt the decline of the economy, but it was hoped and expected that it would induce complementary flows from other sources. In particular, it was believed that the private

<sup>32</sup>Between June and December of 1978 the Fund provided an additional US\$ 14 million under the Compensatory Financing Facility. In 1978, Jamaica made use of US\$ 73 million in IMF credits, an amount equivalent to 2.9% of the GDP (see again table 18).

international financial community would reconsider its lending policy. These expectations were also based on Jamaica's observance of the performance criteria during the first year of the EFF. Finally, as it had done the year before, the IMF supported the Government's efforts to acquire additional external finance. The results were disappointing, however. Other official lenders stepped-up their lending, but the foreign banks elected to continue to withdraw their existing debt from the country. In June the previous refinancing agreement, with some minor alterations, was extended for the remainder of the EFF programme.<sup>33</sup> However, in September the banks rejected Jamaica's proposal to carry out a refinancing of its entire commercial debt and provide a new loan package of US\$ 200 million. This setback together with a series of new blows to the economy, including the severe floods, the new round of oil price hikes, an increase in interest rates and the paralyzation of bauxite mining for a lengthy period in the second half of the year, not only made unavoidable the continued disintegration of the economy, but paved the way for the failure of the performance tests in December and the cutting-off of the IMF resources.

(f) *Exchange rate regimes*

Table 19 shows various indexes of nominal and real exchange rates for the Jamaican dollar in the 1960-1980 period. The first is based on the United States dollar and United States prices; the second on the SDR and the price level of industrialized countries; and the third, on the currencies and prices of Jamaica's trade partners.<sup>34</sup>

Until 1970, all of the real exchange rate indexes moved in the same direction. Between 1960 and 1965 the Jamaican dollar became overvalued, especially in relation to the US dollar, owing to the faster pace of domestic inflation. On a trade-weighted basis the degree of overvaluation was less, and amounted to only 5% over the course of the five-year period. Subsequently, the real rate of exchange rose, and in 1968 soared well above 100 in each index. Here the principal factor was the devaluation of the English pound sterling, to which the Jamaican dollar was then linked by law. Between that year and 1970 the real exchange rate declined somewhat, but remained slightly undervalued. In 1971 there was a parting of ways between the US dollar index, on the one hand, and the SDR and trade-weighted indexes, on the other. Thus, the real exchange rate as measured in terms of US dollars and prices continued to drop, and in 1972 fell below 100, but measured in terms of SDRs and on a trade-weighted basis, it went in the opposite direction, and in 1972 it approached 120 on the SDR index and 102 on the trade-weighted one. These contrasting movements took place within the context of the international monetary crisis of 1971. Following the abandonment of the Bretton Woods Agreement and half a year of "controlled floating", the world's major currencies were realigned in the Smithsonian Agreement of December 1971. During this period of uncertainty in the international monetary system Jamaica moved to break the legal tie that bound its currency to the pound sterling, but elected to continue to link its dollar with the pound for the time being. As a result, the revaluation of the pound against the US dollar led to a proportionate revaluation of the Jamaican dollar with respect to the US dollar. This appreciation amounted to somewhat less than 2% in 1971 and somewhat more than 2% in 1972, and translated into a similar decline in the real exchange rate in 1971 and one of 3.5% in 1972, in terms of US dollars and prices. On a trade-weighted basis the nominal exchange rate of the Jamaican currency varied a mere 1% between 1970 and 1972, because its revaluation in terms of US dollars was virtually counterbalanced by its depreciation in relation to the currencies of other trade partners. In terms of the SDR, however, it experienced a considerable net depreciation. These results were accompanied by increases in the respective real exchange rates (see again table 19).

Against a background of growing stress in the balance of payments, and the marked instability of the pound sterling, in January 1973 the authorities decided to devalue the Jamaican

<sup>33</sup>In 1978 the banks had provided fresh loans to cover the amortization of 87.5% of the debt maturing that year, but in 1979 this was changed to deferment of the amortization of the same 87.5% of maturing loans, no new loans being provided.

<sup>34</sup>See the notes to table 19 for greater details.

Table 19

JAMAICA: EVOLUTION OF NOMINAL AND REAL EXCHANGE RATES  
(1960 =100)

Year	Jamaica dollars per									
	Nominal exchange rate indexes					Real exchange rate indexes (f)				
	US\$(a) (1)	SDR(b) (2)	EW(c) (3)	IW(d) (4)	TW(e) (5)	US\$(a) (6)	SDR(b) (7)	EW(c) (8)	IW(d) (9)	TW(e) (10)
1965	100.0	100.0	98.9	97.7	98.3	92.3	97.6	95.8	94.3	95.1
1966	100.0	100.0	98.8	97.7	98.3	93.2	98.7	97.2	95.5	96.4
1967	102.5	116.2	100.9	99.9	100.4	95.3	114.8	99.4	97.6	98.5
1968	116.7	116.2	110.6	109.3	110.0	106.8	112.4	106.9	104.8	105.9
1969	116.7	116.2	111.1	109.6	110.3	105.9	111.0	105.9	103.7	104.8
1970	116.7	116.2	111.5	110.2	110.9	102.1	106.7	102.9	100.1	101.5
1971	117.7	119.1	110.5	109.4	110.0	100.1	111.0	103.1	100.4	101.8
1972	117.0	129.5	109.8	109.5	109.7	96.6	119.6	103.3	101.0	102.2
1973	127.3	153.5	126.8	127.3	127.1	97.4	127.2	107.3	106.0	106.7
1974	127.3	155.8	126.2	126.1	126.2	86.8	117.4	96.3	94.7	95.5
1975	127.3	149.0	125.7	124.8	125.3	80.8	106.0	92.7	90.0	91.4
1976	127.3	147.9	120.1	119.0	119.6	78.0	103.4	87.1	84.3	85.7
1977	153.9	167.5	143.9	143.3	143.6	90.2	114.4	102.3	99.2	100.8
1978	208.6	313.8	198.4	202.8	200.6	97.4	176.1	113.8	112.9	113.4
1979	247.4	328.6	241.3	246.7	244.0	99.5	155.2	119.4	118.1	118.8
1980	249.5	318.1	258.7	261.9	260.3	89.8	125.4	118.6	115.7	117.2

(a) United States dollar.

(b) Special Drawing Right unit.

(c) Weighted by export shares, 1968/1972, as follows (in percentages): United States 46.3; Great Britain 25.1; Canada 10.6; Norway 9.4; Sweden 2.9; Trinidad and Tobago 1.4; Bahamas 1.2; Guyana 0.8; West Germany 0.6; Barbados 0.6; Netherlands 0.5; Japan 0.4; and Switzerland 0.2 (note that the remnant was allocated proportionately to the top five export markets.)

(d) Weighted by import shares, 1968/1972 as follows (in percentages): United States 43.6; Great Britain 22.4; Canada 9.1; Venezuela 5.3; West Germany 3.6; Japan 2.7; New Zealand 2.0; Australia 1.8; Trinidad and Tobago 1.7; France 1.6; Italy 1.4; Netherlands 1.3; Belgium 0.8; Hong Kong 0.8; Switzerland 0.7; Sweden 0.6; Norway 0.3; and Guyana 0.3 (note that the remnant was allocated proportionately to the top five import suppliers).

(e) Weighted by shares in overall trade. See (c) and (d) above.

(f) Nominal exchange rates (columns 1 through 5) divided by the relevant relative price indexes (i.e., Jamaica prices with respect to United States prices, etc.).

dollar with respect to all currencies and fix its new value in terms of US dollars. One month later a 10% devaluation of the US dollar was announced, and the Jamaican currency thus experienced a further devaluation *vis-à-vis* currencies other than the US dollar or ones pegged to the dollar.

These developments translated into increases in the nominal exchange rate of almost 14% in terms of US dollars, of 16% in the trade-weighted index, and of close to 19% in terms of SDRs. However, the real exchange rate *vis-à-vis* the US dollar rose less than 1%, remaining only slightly overvalued. On the other hand, in terms of both SDRs and the basket of currencies of the country's trade partners, the Jamaican dollar rose appreciably in 1973 —the fourth straight year in which both of these indexes recorded increases.

In 1973 the three indexes thus varied considerably: the US one equalled 97.4, the SDR one, 127.2, and the trade-weighted one, 106.7. This last index was made up of 107.3 on the export side and 106.0 on the import one.

Between early 1973 and mid-1977 the authorities elected to leave the Jamaican dollar fixed (at US\$ 0.909), in spite of a notable acceleration of domestic inflation relative to inflation in all of the country's principal export and import markets except Great Britain. Consequently, each of the real exchange rate indexes declined systematically, and by 1976 the Jamaican currency was seriously overvalued, both in terms of US dollars and on a trade-weighted basis. It remained slightly overvalued *vis-à-vis* the SDR, but the extent of the fall in the real exchange rate since 1973 was virtually the same in this case as in the others.

In April 1977 a dual exchange regime was introduced. The existing rate, now called the basic rate, was retained for transactions involving the Government, the bauxite sector, essential consumer goods and intermediate inputs. A devalued or "special rate" was applied to all others. As a result, the average real exchange rate *vis-à-vis* the US dollar was raised by almost 16%; *vis-à-vis* the SDR, by about 11%; and on a trade-weighted basis by a proportion approaching 18%.<sup>35</sup>

The currency remained overvalued (by an average of 10%) with respect to the US dollar, but the dual regime effectively eliminated the full extent of the overvaluation of the trade-weighted exchange rate. It remained, however, about 6% below the high registered in 1973. The degree of overvaluation with respect to the SDR returned to a level close to that prevailing in the early 1970s (see again table 19). In January 1978 the basic rate was devalued by 13.6% and the special rate by a further 5.2%. This devaluation followed the breakdown of the IMF Stand-by Arrangement in December, and constituted a prelude to the protracted negotiations for an Extended Fund Facility Agreement (EFF) in the first half of 1978. As part of the EFF accord that was finally concluded in May, Jamaica was to unify the basic and special exchange rates and undertake an immediate further devaluation of 25%. Moreover, the authorities agreed to devalue the currency an additional 15% over the course of the first year of the EFF programme. These devaluations were adopted at the insistence of the IMF. The Fund maintained that they were necessary in order to restore a competitive correspondance between domestic and international input and output prices and hence, to re-establish the balance between the supply of and demand for external resources. Furthermore, it was argued that the deterioration of the external payments situation and the reticence of the international financial community had reached such proportions that the measures to be taken should be immediate and drastic: hence the 25% devaluation. A restrictive incomes policy, deflation of the fiscal budget and curtailment of the growth of the money supply were also undertaken in order to ensure the effectiveness of the devaluation and to strike a balance between supply and demand in the economy as a whole. In this scenario, the expected increases in exports and capital inflows, together with the large injection of credit from the EFF, would permit an increase in import volume consistent with economic recovery and a surplus in the overall balance of payments.

In response to the questions that arise here, it should first be re-emphasized that the dual exchange regime had the effect of restoring the cost/price competitiveness of the economy in relation to its trade partners as a group. The additional devaluation in January 1978 measurably reinforced this situation. However, the Jamaican currency did remain overvalued in US dollars. From this angle, the May devaluation only appears appropriate insofar as the US dollar is concerned. On a trade-weighted basis, it was clearly excessive, as may be seen by reference to table 19.<sup>36</sup>

To the extent that the devaluation was in fact superfluous, it merely engendered inflation. Hence, the most relevant question are : Did the medicine lead to a cure? How did exports and the overall balance of payments evolve in the wake of the May and ensuing devaluations?

With regard to exports, the most germane concept is their net change, in constant prices. The sole available measure here is the foreign exchange budget of the Bank of Jamaica, because it is the only gauge of the amount of foreign exchange actually returned to the economy by sales abroad. On the other hand, its use does introduce a source of bias, inasmuch as not all of the foreign exchange circulating in the economy necessarily passes through the Bank of Jamaica.

An examination of the foreign exchange budget shows the following. Returns from merchandise exports declined over 7% in current prices between 1977 and 1978. In constant prices the decline was 9%. This decrease reflects the reduction in foreign exchange receipts from bauxite and alumina exports. The gross value of bauxite and alumina exports in fact rose, but the devaluation lowered the domestic costs of production in terms of foreign currency. Consequently, the bauxite

<sup>35</sup>These figures refer to the difference between annual averages for 1976 and 1977.

<sup>36</sup>The May and subsequent mini-devaluations, together with the depreciation of the US dollar *vis-à-vis* major currencies, translated into a leap in the real exchange index in SDRs of fully 54% (to 176) in 1978. In terms of the major markets of the world, Jamaica's goods and services thus became extremely undervalued.

companies returned less foreign exchange to the economy. On the other hand, the net receipts from tourism climbed over 36%. Nevertheless, the May and later devaluations were accompanied by an overall decline of 3.5% in the net receipts from the exports of goods and services in 1978. In 1979, the net returns from merchandise exports rose 3% in current prices but fell 3.4% in constant prices. However, the net receipts from the total exports of goods and services increased somewhat less than 5% thanks to the further 40% expansion in the return from tourism.

Between 1977 and 1979, the real exchange rate increased by 18% on a trade-weighted basis. The response of the export sector was an increment of 1% in the foreign exchange returned to the economy, at constant prices. The juxtaposition of these two figures does not necessarily imply that the exchange rate policy favoured by the IMF was a failure. On the other hand, it would appear to be much more problematic to argue that these figures suggest that it was a success.

Yet, it has been observed that while devaluation does not appear to help the trade balance, it does engender an improvement in the overall balance of payments.<sup>37</sup> It was indeed expected that the aggressive exchange rate policy would induce a return of capital flows to Jamaica. But this did not take place, as was discussed in the preceding section.

The poor response of exports and of the international financial community made it impossible to augment import volume by an amount sufficient to halt the contraction of the economy. The main effect of the devaluations, then, was to accelerate inflation.

The monthly devaluations of the Jamaican dollar were continued until May 1979. On a trade-weighted basis the real exchange rate index reached almost 119 in 1979, or the highest level in the post-war era. In 1980, this index declined about 1%.

#### 4. Prices and wages

##### (a) Prices

In 1980 the proportional increase in the average level of consumer prices declined for the second consecutive year; yet the rate of inflation intensified considerably. Thus, the average annual rise in price levels approached 26%, against 29% in 1979 and almost 35% in 1978. But the rate of inflation, as measured by the variation between the December consumer price indexes, climbed to 29.5%, versus about 20% in 1979 (see table 20). As occurred the previous year, the categories in which inflation was greatest in 1980 were food and beverages, and fuels. Food prices climbed by one-third in each of these years, mainly in response to the considerable production losses sustained in the wake of recurrent adverse weather conditions. Fuel prices soared 46% in 1979 and 41% in 1980, owing primarily to the increased cost of imported petroleum, but also to appreciable reductions in subsidies.

Price stability in Jamaica was interrupted in 1973, when the average increase of the consumer price index shot up to 20%, or more than four times the ones recently experienced. The outbreak of inflation was engendered by both external and internal factors. Thus, import prices rose well over 8% that year, following increments of less than 4% in 1971 and 1% in 1972. This increase, together with the involuntary and programmed devaluations of the Jamaican dollar, caused import prices in domestic currency to rise by almost 26%. This alone directly accounted for six-tenths of the increase of 20% in the general price level, given the share of imports in domestic supply. It likewise caused severe upward pressures on price formation in the rest of the economy. Between 1970 and 1972, in contrast, the domestic cost of imports had advanced a mere 3%, owing to the stability of import prices and the involuntary appreciation of the Jamaican currency. This played an important role in the stability of domestic prices in these years, especially in the light of the build-up of inflationary pressures of domestic origin. But the unintentional appreciation of the

<sup>37</sup>See, for example, M.A. Miles, "The Effects of Devaluation on the Trade Balance and the Balance of Payments: Some New Results", *Journal of Political Economy*, Vol. 87, No. 3, June, 1979, pp. 600-620.

currency, in conjunction with other factors, such as a brusque upturn in the expansion of domestic credit and the uncertainty caused by the disarray prevailing in the international monetary system, gave rise to growing strains on the balance of payments, in response to which, in January 1973, the authorities raised the exchange rate and fixed the Jamaican dollar in terms of US dollars. Subsequently, the currency was subjected to a further devaluation when the US dollar was devalued.

On the domestic side, an unusually large expansion in credit in 1972 eventually led to an upsurge in consumer spending and money supply growth. In that year, the price situation remained stable, partly because output and domestic supply rose markedly (9.8% and 11.3%, respectively) and more than gross national income, and partly because of a major decline in the net international reserves. In addition, the stabilizing effects of these developments were reinforced by the course of external prices and of the exchange rate. But in 1973 the environment underwent a radical change. Real interest rates began to decline about as fast as the domestic prices of imports began to rise. On the other hand, the rate of growth of output slowed abruptly, and for the year as a whole amounted to just over 1%. Agricultural output, in fact, dropped 6% and the production of food fell by close to 8%. Simultaneously, import volume was slashed in a move designed to stem the loss of international reserves. As a result, domestic supply did not increase at all.

In the meantime, the growth of credit was cut in half, while the net international reserves continued to shrink notwithstanding corrective measures. Moreover, virtually the entire amount of the increase in credit was spent. From another angle, the resulting upturn in the growth of the money supply in spite of the marked decline in the growth of factors of expansion appears as a lagged response to the bulge in credit in 1972.<sup>38</sup> In any event, the surge in the supply of money ran up against the stagnation in the supply of goods and services.

Finally, the abrupt inflation in prices provoked and escalation in wage demands from the highly-organized labour force, giving rise to a price-wage spiral which was not to run its course until 1977. In 1973, unit wage costs rose more than 14%, against 2% in 1972. However, compared to 1972, the major factor in this leap was not the increase in money wages, but the drop in labour productivity.

In the following year inflation intensified, soaring to more than 24%. Import prices shot up fully 35%, and almost two-thirds of the rise in consumer prices may be traced directly to this factor. Export prices climbed at an even faster pace, however, permitting the doubling of the net international reserves in spite of the much enlarged outlays for petroleum imports. As a result, the rate of growth of the money supply climbed to 27%, even though the expansion of credit was reduced for the second consecutive year. In addition, the large gain in the terms of trade allowed income to increase while output was contracting.

The pronounced heightening of inflation and inflationary pressures in the external sector was accompanied by mounting tensions on the domestic side. Output commenced its rapid downward trend in 1974, sliding by 4%, and the efforts to shore-up the balance of payments position and the large increases in import prices precluded an offsetting hike in the supply of imports, so that domestic supply tumbled by 3%. But the enactment of the Bauxite Levy, together with the notable improvement in the terms of trade led to a rise in gross national income of more than 8%.

This marked disproportion between the changes in supply and demand was accompanied by only a marginal increase in savings, as the increase in gross national income was transmitted throughout the economy via leaps of 60% in government spending and 50% in money wages and salaries. Consequently, it exerted a decided upward pressure on price levels.

Looking at the cost side, this extraordinary rise in wages, in conjunction with a substantial decline in labour productivity, translated into a 60% increase in unit wage costs.

<sup>38</sup>In 1972, the factors of expansion registered an increase of over 19%, due entirely to the 37% growth of credit. That year the money supply increased 10%, or about the same as the product. In 1973, the factors of expansion increased only 7%, with credit rising 18%, but the supply of money jumped almost 21%.

In the light of all these developments, it is rather remarkable that the rate of inflation was limited to 24%. Food output did recover in 1974, and also the rate of exchange declined, but it appears that it was price controls and subsidies which played the biggest role in mitigating the enormous and varied tensions to which the level of prices was subjected.

The following year witnessed a let-up in inflation, thanks primarily to the sizeable reduction in external price increases and a large rise in domestic supply, coupled with the stagnation of gross domestic income, but also to a further small decrease in the exchange rate. The increase in import prices dropped from 35% to 12.5%, involving a rise in the overall price level of somewhat more than 5%, versus 16% the year before. In the meantime, domestic supply climbed almost 9%, against an increment of only 1.4% in gross national income. This turnaround virtually offset the extent of the disequilibrium experienced in 1974. Finally, the exchange value of the Jamaican currency appreciated an additional 1%.

On the other hand, government spending and unit wage costs continued to expand very rapidly. In the case of the Government, however, the potential inflationary effects of the rapid growth of its expenditure in 1975 were in part counterbalanced by the major loss of international reserves and the contraction of income in the private sector. But the further 24% hike in nominal wages was not compensated by gains in labour productivity, which in fact dropped by 7%. The resultant one-third expansion in unit wage costs emerges as the major inflationary factor in 1975. Between 1973 and 1975, unit labour costs more than doubled.

In 1976 gross national income declined some 11%, while the liquid reserves were almost exhausted. The severe deflation of the economy, together with a steep decline in external inflation and an appreciation of the US dollar against other major currencies, permitted a reduction in the rate of inflation to 9.6%. The marked contraction of gross national income more than offset the fall of over 9% in domestic supply, due to a substantial deterioration in the terms of trade. At the same time, the increase in import prices was so small (3%) that the decrease in the exchange rate (5%) led to a decline in the cost of imports in domestic currency which implied a direct decrease of 1% in the overall price level. Furthermore, the virtual depletion of the international reserves kept the increase in the money supply to just 2% in spite of the doubling of credit to the Government. Consequently, the fact that the level of prices rose a further 10% must be attributed to the momentum of previous years, transmitted primarily via wages. In effect, unit wage costs climbed a further 23% in 1976.

Notwithstanding the considerable imbalance between the changes in supply (-7.3%) and demand (1.9%), an increase of 20% in the exchange rate, and a jump of 38% in the money supply, the rate of inflation drifted up less than two percentiles, to 11.4%, in 1977. Three factors moderated the effects of these pressures on the level of prices. Firstly, import prices rose less than 7%, while the output of food leaped 25%. But the most important countervailing force was the abrupt curtailment of wage inflation. After climbing 162% over the course of the previous three years unit wage costs rose less than 3% in 1977.

Domestic supply and gross national income evolved in a balanced fashion in 1978. Moreover, the output of food rose a further 20%. Import prices registered an average increment similar to that of the previous year. The growth of the money supply was pared back to less than 18%, a rate substantially below the one consistent with the magnitude of the expansion of nominal GDP, while the increase in nominal wages was limited to 12%.

Yet, inflation intensified drastically. The average annual change in prices soared to 35%, while the December 1978 consumer price index soared more than 49% above the December 1977 one, the principal determinant of this unprecedented rate of inflation being the 40% devaluation of the Jamaican dollar. To that shock was added the effects of the liberalization of pricing policy in most areas of the economy. In this respect, a share of the acceleration of inflation in 1978 was the counterpart of the past repression of price increases, and the bulge in money supply growth in 1977 may also have exerted an effect on prices in 1978. In any event, more than one-half of the jump in prices in 1978 may be traced directly to the devaluation.

In 1979 prices continued to advance at a rapid although somewhat slower pace. The exchange rate was on average almost 22% higher than in 1978, and this, together with an increase of almost 11% in import prices, explains six-tenths of the rise in domestic prices. Again, income declined more than domestic supply. However, in contrast to the enormous gains achieved in 1977/1978, food production dropped some 3%. Money supply growth was reduced to below 8%, or about half the expansion of the nominal GDP. The advance in unit wage costs, on the other hand, amounted to somewhat more than 20%.

In 1980 the average change in the level of prices eased somewhat further, but the rate of inflation picked up over the course of the year. The main determinant of this acceleration appears to have been the 23% escalation of import prices, although a host of other inflationary factors were present. Thus, the average exchange rate moved up a further 7% and, as occurred in 1979, food production contracted while price controls on food were liberalized. Moreover, the rate of growth of the money supply accelerated markedly to 35.5%, as the projections of the central government deficit and the supply of extraordinary foreign finance turned out to be way off target. Finally, wage demands and settlements rose appreciably subsequent to the breakdown of the IMF-Government EFF agreement.

Table 20

JAMAICA: EVOLUTION OF INTERNAL PRICES						
	1975	1976	1977	1978	1979	1980
	Variation between annual averages					
Total	17.5	9.7	11.2	34.8	29.1	26.9
Food and beverages	17.8	8.9	9.4	36.8	33.4	33.3(a)
	Change December-December					
Total	20.6	15.7	14.1	49.4	19.8	28.6
Food and beverages	19.8	15.5	12.3	54.1	24.5	33.7

Source: Jamaica, Department of Statistics, *Consumer Price Indices, Annual Review, 1978, 1979* and data supplied to CEPAL.

(a) January-November 1980 with respect to January-November 1979.

#### (b) *Wages*

Much has already been said about the evolution of wages, details of which appear in table 21. Sustained by a jump of almost 10% in labour productivity in the economy as a whole, real wages rose more than 7% in 1972, but virtually the entire amount of this gain was forfeited in the wake of the advent of inflation in 1973. Over the course of the ensuing three-year period, however, the labour force managed to obtain a one-third hike in real wages and salaries, notwithstanding systematic declines in output and labour productivity. Subsequently, real wages and salaries were forced to move in the same direction as output and productivity by devaluations and wage controls.

The outbreak of inflation in late 1972/early 1973 provoked an immediate escalation of wage demands, strikes and wage settlements. Real wages deteriorated only because two-year contracts were the norm: about half of the organized labour force did not have the option of negotiating that year. The contracts which were renewed involved wage increases ranging from about 25% in transportation, storage and communications, to over 50% in mining. In 1974 the average nominal increase reached an incredible 50%. In consequence, real wages soared by almost 19% even though the rate of inflation intensified. This enormous advance took place alongside a 4% drop in the gross domestic product and a decrease of well over 6% in total labour productivity, although the extent of the disproportion was tempered by the large expansion of gross national income. In fact, between 1971 and 1974 the 19.4% change in the index of real wages and salaries was not much greater than the 17% change in gross domestic income. But the gains in money wages and salaries



in both 1975 and 1976 continued to outdistance the (by then declining) rate of inflation in circumstances in which labour productivity continued to descend at a very fast pace. Furthermore, the gross domestic product did not rise in 1975 and fell sharply in 1976.

As a result of the divergence between the evolution of wages and of output, in 1976 real wages stood almost one-third above the 1973 level, while labour productivity was one-third below it. An interpretation of this marked contrast is beyond the scope of this survey, inasmuch as it would involve a lengthy discussion of the peculiar institutional characteristics of the Jamaican labour market and of the effects of the political change of 1972 on the Jamaica labour movement. In any case, this asymmetry evaporated in the 1977/1979 period.

Efforts to curtail the escalation of wage settlements beyond the variation in the cost of living got underway in August 1975. They were part of a package of corrective measures whose aim was to offset the effects of the international recession and the shift in the pattern of demand on the balance of payments and on growth.

In the absence of the sought-for agreement with the trade unions on an incomes policy, the Government established temporary guidelines for the private sector and commercially operated public enterprises which were to be in force from September 1975 to March 1976. For workers earning less than J\$ 7 000 per annum, real wages would be restored to the level prevailing in the last contract to expire before June 1973. For those earning between J\$ 7 000 and J\$ 12 000 per year, a ceiling equal to the highest increase obtained in the first group was established. For those earning between J\$ 12 000 and J\$ 16 000 per year, increases could not exceed one-half the highest increase received in the first group. All salaries above J\$ 16 000 were to be frozen. This moratorium applied to all types of emoluments.

Table 21

JAMAICA: NOMINAL AND REAL WAGES, EMPLOYMENT, LABOUR PRODUCTIVITY AND UNIT WAGE COSTS  
(1971 = 100)

	1972	1973	1974	1975	1976	1977	1978	1979	1980
Nominal wages and salaries (a)	112.2	126.1	189.2	233.7	269.0	275.1	308.6	365.3	-
Real wages and salaries	107.3	100.6	119.4	126.8	132.5	122.1	105.0	92.4	-
Employment	100.0	103.0	105.7	111.6	112.2	112.8	115.9	112.7	112.7
Labour productivity	109.8	107.9	101.0	94.2	87.8	87.4	84.5	83.2	80.3
Unit wage costs	102.2	116.9	187.3	248.2	306.2	314.8	365.1	439.1	-

Source: Jamaica, National Planning Agency, Economic and Social Survey, various years, and the World Bank.

(a) Between 1971 and 1973, based on the industrial wage index. Between 1973 and 1979, based on the median weekly income of income earners.

These guidelines were in fact highly restrictive, inasmuch as only a relatively small share of the labour force was then earning less in real terms than in June 1973. At the same time, they were designed to diminish the disparity between incomes. In this connexion, three other steps were taken: the implementation of a national minimum wage; the freezing of the rate of profits at a proportion equivalent to the average for the previous three years; and the limitation of dividends before taxes to 7% of net work for a period of one year.

Following a new round of negotiations between the Government and the trade unions the wage and salary guidelines were extended, with some modifications, for a one-year period beginning in March 1976. The changes and additions included the following. Wage and salary increases, where permissible, were restricted to a maximum of J\$ 10 per week, unless the amount required to restore real earnings to the June 1973 level was larger. Also, other exceptions were possible if certain stipulations concerning profitability, productivity and hardship were met. On the other hand, most allowances and fringe benefits were to remain at the levels existing at 1 September 1975. Finally, wages and salaries of employees of the central government and statutory boards were frozen.

Following its re-election, the Government instituted in January 1977 another set of policies to deal with the worsening economic crisis. With respect to wages and salaries, the existing guidelines were maintained, with several adjustments that had the effect of returning to the more restrictive features of the original guidelines, while retaining the more stringent aspects of the March 1976 ones. In addition, the moratorium on wage and salary hikes in the central government and statutory bodies was extended to 31 March 1978. The Government renewed its commitment to a restrictive incomes policy in April, when it introduced the dual exchange rate, and in July, when it entered into the standby agreement with the IMF.

There was a lag in the effectiveness of the successive guidelines in bringing the inflation of wages in the economy as a whole to a halt, but the size of wage settlements was compressed in 1975 and again in 1976,<sup>49</sup> and in 1977, when inflation accelerated once more and the average increase in money wages was limited to about 2%, real wages and salaries were cut by an average of almost 8%.

As part of the Extended Fund Facility (EFF) agreement of 1 May 1978, increases in wage contracts expiring after that date were limited to 15% per year, for a two-year period. This ceiling applied to all categories of emoluments, and to both the private and public sectors. The purpose of this restraint was to ensure that the simultaneous devaluation of the Jamaican dollar restored the real rate of exchange to the level prevailing in the early 1970s. In this respect it was more than successful. As regards the effect of the programme on wages, suffice it to note that the index of real wages and salaries plunged 14% in 1978.

For the second year of the EFF, the ceiling on wages and salaries was lowered to 10%, in conjunction with the suspension of the monthly devaluations. In contrast to the outcome in 1978, the variation in money wages in 1979 surpassed the limit. But the momentum of the inflationary process unleashed by the marked devaluation of the currency raised the average 1979 price level so far above the 1978 one that real wages were compressed a further 12%. At that point they were 30% below the 1976 high, and substantially lower than at the beginning of the decade. Another, albeit smaller, decline appears to have taken place in 1980.

## 5. Economic policy

### (a) *Introduction*

The Jamaican electorate opted for change in 1972, voting into power the party which had been in opposition since Independence in 1962. The priorities of the new administration were defined in large part in function of the factors which had prompted the election outcome. The burgeoning unemployment crisis, the deteriorating distribution of income, the lagging coverage and quality of social services, and the widening housing deficit were problem areas into which the new Government thus intended to channel a major share of public resources. Also, it was by then clearly appreciated that past demographic trends were on the verge of translating into a radical surge in the growth of the labour force. This of course greatly heightened the concern over the employment crisis and, together with the growing social tensions it was engendering, created a sense of urgency about dealing with it. As far as the longer term was concerned, it was recognized that the existing expansion path of the economy would have to be modified appreciably, inasmuch as it had proven incapable of generating enough jobs to satisfy even the very modest increment in the labour force registered over the previous decade. This, in conjunction with the multiple problems provoked by the massive rural to urban migration then taking place explains the prominence of agriculture in the Government's development plans. The long-term development programme was also conditioned by the need to face up to the impending decline in investment and in foreign capital inflows arising from the recent completion of a major investment cycle in

<sup>49</sup>As far as the central government was concerned, real wages and salaries—which had increased much less than those in the private sector—were slashed appreciably in 1976 and were left only slightly higher than in 1972.

mining and the approaching conclusion of one in tourism. Another important factor in the formation of development plans was the decision to seek greater autonomy from the course of events in the international economy. In this connexion, it was envisioned that the acquisition of assets in the foreign exchange earning sectors of the economy would play an important role.

The agenda thus included a set of difficult challenges, but the possibilities of success seemed to be reasonable. For more than a quarter of a century the international economy had grown year after year at a very fast pace without inflation and the Jamaican economy had behaved in exactly the same manner. Furthermore, the consistent expansion in the output of goods and services, together with a tradition of sound fiscal and monetary management, had placed the public sector in a position to finance a relatively ambitious capital investment programme without resorting to advances from the Central Bank. Over the course of the 1960s current savings financed about half of a capital expenditure programme that fluctuated around a figure equivalent to 6% of the GDP.<sup>40</sup> The other half was financed principally through bond issues on the highly developed local capital market. External capital markets, including multilateral development banks, had yet to be tapped on more than a token scale. Foreign reserves were then at an all-time high and in fact were greater than the external debt.

The confluence of pressing needs and propitious conditions thus impelled the country towards an experiment with a new set of policies. But the international environment was on the verge of a succession of crises that would pound the Jamaican and other small open economies throughout most of the decade. The monetary crisis had in fact already surfaced, although much more was still to come, while the petroleum and food crises were just around the corner. Soon to follow was the outbreak of international inflation and the subsequent recession. The end of the decade would be plagued by another round of petroleum price hikes and international stagflation. As it turned out, the times were not favourable for social experimentation in a small, fragile and highly vulnerable economy. Yet, for several years the attempt was made. By 1977, however, the principal focus of attention was on how to stop the economy from contracting, and by the end of 1980, when a new government was elected, the principal preoccupation was avoiding total economic collapse.

At the outset of its term in office in February 1972 the new administration implemented and expansionary fiscal policy and set about drawing up plans for a much enlarged capital expenditure programme.<sup>41</sup> Current expenditures were augmented and redirected in favour of social programmes, especially in the area of employment and low-income housing. The increase approached 27% in nominal terms and more than one-fifth in constant prices, and was the largest increase in any one year since Independence. Current receipts were very buoyant, owing primarily to the 10% expansion in output, but they were less than projected and thus not sufficient to prevent an appreciable deterioration in current savings. On the other hand, capital outlays were raised by much less than intended. Consequently, current savings still covered more than one-third of capital spending, while the overall deficit was smaller than planned. As in the past, domestic borrowing financed the lion's share of the deficit. The level of foreign borrowing was similar to that of the previous year.

The effects of the expansionary fiscal policy on output and employment met or even surpassed expectations. Perhaps the principal unintended effect was a marked upturn in imports and a deterioration in the balance of payments. The large expansion of government spending led to an upswing in bank liquidity and lending, and the resulting increase in consumer demand translated into a rise in the import bill beyond the extent implied by the growth of domestic output. This, together with a steep decline in foreign investment and the uncertainties over exchange rates, brought about a steady reduction in the international reserves. In response the

<sup>40</sup>These figures refer to the central government. For the public sector as a whole, savings averaged 5%, and investment 10%, of the product.

<sup>41</sup>Fiscal and monetary policy is described in the Bank of Jamaica's annual *Report and Statement of Accounts*. Unless indicated otherwise, the data in this section are from that source.

monetary authorities introduced some remedial measures in July, including higher interest rates, an increase in the statutory liquid assets ratio, and a reduction in discounts from the Central Bank. Subsequently, a ceiling on credit expansion was established. At that juncture (October) the commercial banks were almost fully lent-up, and interest rates were on the rise. On another front, a temporary ban on the importation of automobiles and of some other postponable imports was put into effect. Finally, in January, the authorities moved to relieve the growing stresses on the balance of payments by devaluing the currency and pegging it to the US dollar.

In 1973 government spending increased almost 25%, or somewhat less than in the previous year. However, in constant dollars the increment was only 4%, since the inflationary process had already commenced. Income rose by a somewhat smaller proportion. Consequently, savings declined for the second consecutive year as a proportion of the product (see table 22). Capital spending was hiked by about one-fifth, but again the size of the increase was less than planned. The overall deficit expanded by a quarter, and for the first time it was financed principally from foreign sources, in order to offset part of the gap left in the wake of the completion of the investment cycle in the bauxite industry. In this connexion the authorities took several additional steps, including arrangements for a major foreign investment project (in oil refining) and the negotiation of a standby agreement with the IMF.

Table 22  
JAMAICA: SOME FISCAL RATES  
(Percentages)

	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980(a)
Current revenue/gross domestic product	19.6	20.2	20.0	23.9	24.5	22.3	21.8	27.6	26.4	23.0
Direct taxes/current revenues	...	...	45.6	50.0	33.9	40.0	33.0	27.7	29.2	30.0
Bauxite levy/current revenues				16.4	19.5	13.2	16.9	25.8	20.8	25.1
Current expenditures/gross domestic product	15.9	17.9	19.6	22.7	24.1	28.4	27.9	30.5	30.3	27.8
Wages and salaries/current expenditures	...	...	28.7	28.1	28.0	25.6	27.4	24.5	25.6	25.7
Current transfers/current expenditures	...	...	41.8	46.5	44.6	44.6	43.7	43.5	37.9	37.5
Interest payments/current expenditures	...	...	9.1	11.9	10.6	12.6	16.0	18.6	24.6	24.0
Savings/gross domestic product	3.7	2.3	0.4	1.1	0.5	-6.1	-6.0	-2.8	-3.9	-3.9
Savings/gross domestic savings	33.2	25.5	3.6	13.7	5.9	307.1(b)	454.9(b)	-190.1	-107.3	...
Capital expenditures/gross domestic product	7.8	7.6	5.9	9.7	11.7	13.2	11.1	12.0	11.8	8.4
Capital formations/capital expenditures	...	...	47.1	44.7	46.4	35.4	37.9	32.2	30.9	38.2
Capital formations/net fixed investment	...	...	17.6	34.6	37.2	61.9	158.4	90.5	42.7	...
Total expenditures/gross domestic product	23.6	25.5	25.5	32.5	35.7	41.6	39.0	42.4	42.1	36.1
Fiscal deficit/gross domestic product	4.1	5.2	5.5	8.6	11.2	19.3	17.2	14.8	15.7	12.2
Domestic financing/gross domestic product	2.2	4.0	2.4	6.1	7.4	16.2	16.5	7.6	12.8	4.5
Banking system/domestic financing	...	...	43.6	32.8	59.3	73.9	46.6	47.4	57.3	57.9
Gross national debt/gross domestic product	...	26.7	27.0	30.4	33.1	41.0	60.5	75.4	77.5	76.6
Foreign debt/gross national debt	...	33.3	34.2	41.2	44.3	39.9	26.8	41.9	42.0	38.3

Source: Bank of Jamaica, Report of Statement of Accounts, various years, and the Work Bank.

(a) Budgeted amounts.

(b) Both central government and economy wide savings were negative.

Following some easing of tensions in the first half of the year, the international reserves began to dwindle rapidly from July onwards as a result of a shortfall in exports stemming from a deterioration in the terms of trade, a renewed upsurge in the growth of credit, and the belief that the currency would be devalued again. In response, the Government had resort to the IMF standby agreement. In addition interest rates and the liquid assets ratio were raised further. Moreover, in November the Central Bank was empowered to control quasi-bank operations that were affecting the money supply. Quasi-bank institutions had expanded their activities appreciably in the last few years, and it was their lending that had largely annulled the effects of the credit restraints applied to the commercial banks.

It was against this background that OPEC announced the enormous hike in the price of petroleum. At the time the Bank of Jamaica observed that: "The impact of this additional foreign exchange bill on a severely weakened reserve position was anticipated to be well nigh unmanageable".<sup>42</sup>

The year 1974 thus began on a note of impending crisis. An immediate and energetic response was forthcoming, however, as in January a comprehensive and far-reaching programme was introduced to deal with the crisis. First, the rise in the oil bill was anticipated by a special tax on petroleum products, while deliveries of gasoline were cut by 25%, with the savings to be exported.<sup>43</sup> Also a national energy conservation programme was outlined. On another front, existing restrictions on imports were tightened and amplified, with a view to releasing foreign exchange to cover part of the higher cost of petroleum imports. Most consumer goods were thus subjected to quotas and licensing. Exchange control regulations were also strengthened. Monetary policy was made more restrictive, in order to shift the structure of demand by reducing consumption in favour of savings and lowering the demand for imports. For this purpose, the entire range of interest rates was moved up, and new credit ceilings established. On the fiscal side, spending was to be held below budgeted amounts and reliance on bank financing reduced. Borrowing by statutory bodies and public enterprises would be pared back. The revenues that would not be received because of the reduction in imports were to be made up through special taxes on luxury consumption and on alcoholic beverages. Moreover, in a move to improve the management of the economy, a cabinet-level economic council with responsibility for the formulation of economic policy was established. Finally, several schemes to increase export earnings were formulated. In this connexion, it was expected that the upcoming contract negotiations with the bauxite companies would result in an increase in the share of mining sector earnings retained by the economy.

Following several months of inconclusive talks with the bauxite companies, the Government enacted the Bauxite Act, whereby a levy was assessed on bauxite extracted after January 1. That year (1974) the country received US\$ 116 million from the levy, or slightly less than the US\$ 123 million increase in the oil import bill. In addition, royalties were increased and arrangements made to acquire part ownership in the industry. In the interim the prices of Jamaica's exports were in the process of climbing to over 90% above the average prevailing in 1973.

Output had begun to lag in 1973, and with the set of policies implemented in January 1974 it actually began to decline. Simultaneously, inflation accelerated. Given the dramatic upturn in foreign exchange earnings and government revenues, on the one hand, and the interruption of growth on the other, the authorities not only resolved to loosen or lift most of the restrictive measures, including the reduction in petroleum supplies, but also to undertake a massive increase in spending. Thus, in the fiscal year beginning in May, current expenditures were boosted 45% and capital expenditures 100%. Even after allowing for inflation the increase in total expenditures still amounted to 28% in constant terms. The expansion in revenues was not much less spectacular, as it approached 20%. As a consequence, nominal savings tripled rising to 1% of the GDP, but the budget deficit climbed to an amount equivalent to 8.6% of the GDP, against 5.5% in 1973 (see

<sup>42</sup>Bank of Jamaica, *Report and Statement of Accounts*, 1973, Kingston, 1974, p. 6.

<sup>43</sup>The export plan concerned petroleum products refined in Jamaica.

again table 22). Most of the deficit was financed from domestic borrowing, but foreign borrowing was also important, and for the first time ever the Government relied on the Central Bank to cover more than a token share of its deficit.<sup>44</sup>

Instead of translating into an upturn in domestic output, however, the government spending programme and the relaxation of credit and other controls brought about a large expansion of imports. In January it was planned that imports would be limited to J\$ 645 million; in May this ceiling was raised to J\$ 725 million; and by December the final figure amounted to J\$ 851, versus J\$ 604 in 1973. Nevertheless, the overall balance of payments showed a surplus for the first time in two years, thanks to the Bauxite Levy and the improvement in the terms of trade, and reserves reached a new all time high.

On balance, the view that prevailed was that given the gravity of the crisis, the performance of the economy was very satisfactory.<sup>45</sup> Yet, in retrospect it now seems clear that an important opportunity was lost at this juncture. The timely and energetic measures to reduce the consumption of petroleum, together with the Bauxite Levy revenues and the windfall export gains, could have made it possible to confront the petroleum crisis with a less costly and more durable solution. Instead, the petroleum conservation measures were laid aside, the resources from the Bauxite Levy were diverted to uses other than the expansion of export capacity, and the unexpected export earnings were frittered away on consumer imports.

The evolution of the economy in the first half of 1975 turned in mixed results. The balance of payments showed a small surplus, in spite of the steep decline in mining and a recession in tourism, thanks to the continued buoyancy of the prices of Jamaica's exports. On the other hand, output continued to lag as the prolonged depression of private investment and the marked reduction in mining and tourism offset gains in other sectors. But the decline in the rate of unemployment persisted, and in April it fell below 20% of the labour force for the first time since the late 1960s. The deceleration in the rate of inflation also was sustained in spite of enormous wage settlements. This was the context when the Government decided to introduce another sizeable increase in spending with the fiscal year beginning in April. Overall expenditures were slated to expand 28%, or about 10% in real terms. On the other hand, revenues were projected to rise even more, with the result that in constant prices and as a share of the product the deficit would be about the same as in 1974. In short, the 1975 budget represented a continuation of the policies adopted in May of the previous year, whereby aggressive fiscal measures and a greatly expanded public investment programme (including the acquisition of assets in the private sector) were directed at offsetting the decline in private sector investment and reflating the economy so that unemployment would continue to fall, while the preoccupation with the external sector and prices was relegated to a secondary plane. In this approach, the public sector would need to rely on the domestic capital market for a much larger amount of support than had hitherto been the case. But it was felt that this would not lead to any significant dislocations, inasmuch as private sector

<sup>44</sup>That year net domestic borrowing by the entire public sector amounted to 2.9% of GDP (overall public sector savings were much higher than central government savings). According to a World Bank study, the public sector could borrow a sum equivalent to almost 4% of GDP from the domestic financial system without creating notable inflationary pressures or an inadequacy in the supply of credit available for the private sector.

<sup>45</sup>In the Bank of Jamaica's words: "The year 1974, which at the beginning threatened to be one of the most disruptive for the Jamaican economy, ended with a fair degree of stability as a result of the economic policies adopted by the authorities. The serious payments problem posed by the increase in oil prices was offset by increased earnings from the bauxite industry following the imposition of the new levy. In light of the fact that many other countries, developed and developing, had to contend with massive problems of recession, unemployment, inflation and balance of payments deficits, the performance of the Jamaican economy in 1974 was creditable. Modest economic growth was achieved, the rate of inflation showed some indication of slowing down in the last quarter, some progress was reported in the area of unemployment, while the balance of payments recorded an overall surplus of some J\$ 54 million.

Unlike 1974, therefore, 1975 began with a more relaxed atmosphere. The crisis of the previous year had been defused and there was general expectation that the gains recorded in 1974 would be consolidated, if not expanded. To this end there was a further relaxation in monetary policy by the reduction of the Bank Rate in February 1975 as a continuation of the policy of gradual reflation begun in late 1974". Bank of Jamaica, *Report and Statement of Accounts*, 1975, Kingston, 1976, p. 1. Note that subsequent revisions of the national accounts indicated a decline in GDP in 1974.

investment demand was waning. Should unintended secondary effects of this or other aspects of the expansion of the public sector arise, they would be handled by controls.

As it turned out, expenditure rose more, and revenue less, than envisioned, not only because output failed to respond to the stimulus of government spending, but also due to the repercussions of the international recession, unanticipated wage hikes, and the unplanned takeover of failing businesses (mainly in tourism). Thus, the fiscal deficit climbed to 11.2% of GDP, against a projected figure of 8.8%. Consequently, net domestic financing equal to more than 7% of GDP was required, and the Bank of Jamaica was called on to provide over-two-fifths of that amount (see again table 22).

While the large budgetary deficit did not have much effect on output, nor for that matter on private sector access to domestic credit, it translated into an immediate surge in imports and, together with the stagnation of exports, led to a marked deterioration of the current account. In the interim the flight of capital had begun to accelerate, and when the Government announced in July that it would be taking steps to shore up the balance of payments, an unprecedented outflow of foreign exchange took place, in the belief that the currency was to be devalued. In August and October a series of remedial measures were taken. The deterioration in the external payments situation was to be halted by restraining the escalation in wages and in prices (through an incomes policy and price controls) and encouraging savings (via changes in the tax laws, and the establishment of a National Housing Trust to be financed from mandatory employer and employee contributions). But these measures proved insufficient to stem the loss of reserves, and in February 1976 a set of more restrictive and wider-ranging policies was announced. In the area of monetary policy, interest rates and liquidity ratios were raised, and Central Bank lending to commercial banks was reduced. Also, commercial banks were to cut back on consumer credit. On the fiscal side, a tax package designed to curb consumption and raise revenues totalling 3% of GDP was introduced, while the temporary wage guidelines were beefed-up and extended for an additional period of one year. Furthermore, direct controls were to ensure that imports were slashed by one-fifth. Simultaneously, arrangements were made for loans for balance of payments support from foreign commercial banks, while an application for access to the IMF's Oil Facility was presented.

During the course of the year the economy was subject to a series of setbacks that prevented the stabilization of the external sector in spite of the fact that imports were reduced by the intended proportion. Prominent here were the fall in export prices, the further reduction in mineral exports, the cessation of foreign commercial bank lending, bad weather, and the virtual paralyzation of tourism. In addition the general expectation for a devaluation of the currency persisted throughout the year. In the meantime the severe contraction in import volume led to a big drop in production, and unemployment rose from 20.5% to 24.2% of the labour force between April and October. In the circumstances the Government's finances threatened to spiral out of control. Revenues declined, while expenditures climbed by one-fourth. As a result, a current deficit equal to 6.1% of GDP was sustained, and the overall fiscal deficit soared to 19.3% of GDP. To cover this enormous gap, domestic resources equal to 16% of GDP had to be mobilized. The lion's share was provided by the Bank of Jamaica. This massive increase in credit to the Government did not lead to inflation, however, as it was offset by a major loss of reserves, and the money supply rose only 2% in nominal terms. In fact, without the enormous creation of credit that the deficit implied, the money supply would have contracted systematically.

One week after the December elections, in which the Government was returned to office with a much larger majority than in 1972, the foreign exchange market had to be closed to prevent the exhaustion of liquid reserves. Towards the end of January (1977) exchange operations were resumed under a new set of controls, and at that time additional policy initiatives were taken to deal with the balance of payments crisis and get the fiscal budget under control. The import bill was to be reduced by a further 30%, while all other exchange outflows were limited to authorized transactions. To ensure compliance with these directives the Bank of Jamaica began to monitor

and control all foreign exchange flows in the economy. Consumption taxes were again increased appreciably, and the wage guidelines were made more stringent.

In April a fresh set of measures, including a dual exchange rate, a cut in government expenditure and a halt to deficit financing by the Bank of Jamaica, were announced. Also, an Emergency Production Plan was formulated, geared to boost the output of essential consumer goods and exports. Finally, the Government decided to negotiate a standby arrangement with the IMF, and in August a two-year US\$ 75 million programme was hammered out. In return for this balance of payments support the Jamaican authorities agreed to pursue a programme similar to the one already in place, but with more restraint in fiscal and monetary matters. The fiscal deficit was to be sliced in half instead of by one-third, and government domestic borrowing reduced even further. Also, targets for improvement in the external sector were established. Progress would be checked on a quarterly basis by performance tests relating to net foreign reserves and net domestic assets of the Bank of Jamaica, net banking system credit to the public sector, outstanding arrears, and foreign borrowing.

There was considerable improvement in the economy in 1977. The three-year decline in the product was halted, although no growth was recorded. Particularly, encouraging was the large gain in agricultural output and the marked increase in the production of food. For its part, gross national income actually increased 2%, by virtue of an improvement in the terms of trade. Also, the rate of unemployment stabilized, while inflation did not accelerate very much, notwithstanding the large devaluation. Important, in this regard, was the complete curtailment of wage inflation, while a reduction in the government deficit and in the creation of credit eased the pressures on both the level of prices and on the balance of payments. In this latter connexion the first trade surplus of the post-war era was recorded, and this made it possible to trim the current account deficit from more than 10% of GDP to just over 2%, in spite of a marked accentuation of the depression in tourism.

On the other hand, the capital account refused to respond to the stabilization programme, and partly for this reason, but also due to a shortfall in central government revenues, the net domestic assets of the Bank of Jamaica exceeded somewhat (by 2.5%) the permissible level on the day the performance tests were scheduled to be applied. Consequently, the standby arrangement was suspended, and Jamaica was prevented from drawing the second credit installment. Instead of renegotiating this accord, however, the authorities decided to seek access to the Extended Fund Facility (EFF). In January the dual exchange rate was devalued by an average of 10%, and negotiations over the characteristics of the stabilization programme that would be adopted in connexion with the EFF got underway. However, a mutually satisfactory accord proved difficult to reach, as there was much disagreement over the question of the need for further devaluation, and over the appropriate relation between exchange rate adjustments and incomes policy. Finally, faced with growing shortages, large external debt amortizations and a deteriorating social climate, in May the Jamaican authorities agreed to the IMF stabilization programme.

In exchange for access to US\$ 240 million from the EFF, the Government agreed to implement what amounted to a new economic policy. The market and the private sector were now to be relied on to turn the economy around. Thus, the maze of controls that had been erected in response to the various successive crises was to be phased out, the size of the public sector was to be reduced, and every effort was to be made to regain the confidence of, and stimulate output in, the private sector. Simultaneously, a drastic deflation of consumption was programmed, and the resources thereby released were to be channelled into the external sector via a realignment of relative prices.

The main policy measures involved the devaluations; the restriction on wage increases; reductions in the current and overall government budget deficit; and the dismantling of controls on prices and transactions. Targets for the principal macro-variables were fixed, and a set of quarterly performance tests were designed to monitor the progress towards these objectives. As usual, the targets were not binding, but the breach of a performance test implied the immediate suspension of the agreement. The tests and the results turned in by the economy are shown in table 23.



Table 23

JAMAICA: EFF PERFORMANCE TESTS AND RESULTS  
(Millions of Jamaica dollars)

	1978				1979			
	I	II	III	IV	I	II	III	IV
1. Net foreign assets of								
Bank of Jamaica (a)								
Ceiling		-335.0	-300.0	-300.0		-425.0	-425.0	-370.0
Actual	-317.0	-318.3	-279.0	-289.5	-319.1	-381.6	-419.6	-496.7
2. Net domestic assets of								
Bank of Jamaica								
Ceiling		440.0	445.0	480.0		900.0	925.0	940.0
Actual	403.0	405.2	393.6	424.6	708.2	866.9	924.5	1 064.1
3. Net banking system credit to the public sector								
Ceiling		930.0	1 010.0	1 110.0		1 070.0	1 105.0	1 125.0
Actual	841.0	856.8	887.0	1 021.5	992.4	1 059.1	1 072.2	1 265.0
4. Outstanding arrears								
Ceiling		80.0	60.0	40.0				
Actual	82.0	79.2	48.8	30.4				
5. Foreign borrowing								
Ceiling (1 to 5 year loans)						60.0	60.0	60.0
Actual						0.9	4.5	12.9
Ceiling (1-12 year loans)						110.0	110.0	110.0
Actual						0.1	21.2	41.1

Source: Bank of Jamaica, Report and Statement of Accounts, 1978 and 1979.

(a) Including outstanding arrears.

The net foreign assets test measures the evolution of the balance of payments. The net domestic assets test gauges the central government's use of Central Bank credit. The test concerning net banking system credit to the public sector is meant to check the adequacy of credit to the private sector. At the same time all of these tests imply constraints on policy. Finally, the original EFF agreement also included a timetable for clearing up outstanding arrears. For the second year of the programme no specific requirements in this regard were included, although arrears continued to affect the net international reserves test. On the other hand, certain limits on foreign borrowing were added.

During the course of the first year of the programme all of the performance tests were met, although in the case of net foreign assets compliance sometimes required the curtailment of exchange outflows. Adjustments in the area of wages, profitability, relative prices, consumption, the real rate of exchange and administrative controls also proceeded more or less according to plan. On the other hand, there was some slippage in the fiscal targets, as revenues failed to increase by the projected amount. The most important setbacks, however, had to do with the evolution of output and the balance of payments. Thus, after showing no growth in 1977, the GDP declined 0.4% in 1978 and over 4% in 1979, as private sector investment, exports and the capital account of the balance of payments failed to respond as expected. The approximate equilibrium established in the balance of payments in 1977 was maintained in 1978 and 1979 only by the temporary expedients of continuing to repress imports and using IMF credit. Indeed, at the existing level of foreign exchange inflows the maintenance of equilibrium in the external sector made the decline of output virtually inevitable. On the other hand, the devaluations, relaxation of price controls and reduction of subsidies sent the level of prices spiralling upwards.

In the light of the persistence of the severe foreign exchange constraint, and taking advantage of a recent liberalization of the ceilings on the use of Fund resources, the IMF augmented its support to Jamaica to US\$ 340 million in the final two years of the stabilization programme. At the same

time, the targets, performance tests and policies were modified. The monthly devaluation of the exchange rate was ended, but the limit on wage increases was lowered from 15% to 10%, and more restrictive monetary policies were adopted. On the other hand, the fiscal targets were liberalized somewhat. On another front, the Government agreed to forge a "social contract" with business and labour, whereby maximum co-operation and consensus on crucial economic and social matters would be sought. Also, negotiations on the question of the modification of the Bauxite Levy and the foreign debt were commenced.

These initiatives met with some success. In particular, the dispute between the government and the bauxite companies over the levy apparently was resolved. But talks with the foreign commercial banks failed. That setback, together with escalating oil prices and interest rates, on the one hand, and an unexpected decline in exports stemming from flood damage in agriculture and a strike-related shutdown of mining operations on the other, made it impossible to satisfy the December 1979 net foreign assets test (see again table 23). Simultaneously, the evolution of the fiscal variables was straying way off target, partly because the anticipated upturn in economic activity refused to materialize and government revenues consequently fell short of the anticipated level, and partly because spending overshot budgeted amounts in the wake of the floods, the increase in interest payments and unexpected wage increases. As a result of this and the inability to acquire the hoped-for amounts of foreign financing, the Government absorbed a much greater amount of domestic resources than planned, and the permitted levels of net banking system credit to the public sector and of the net domestic assets of the Bank of Jamaica thus also were surpassed (see again table 23).

The failure of the foreign assets test triggered the suspension of the EFF accord. Notwithstanding the drastic measures of the stabilization plan and the unprecedented levels of IMF credit, it had proven impossible to overcome the foreign exchange constraint. The choice facing the authorities was to either implement more severe deflationary policies or lose access to IMF resources.

#### (b) *Fiscal and monetary policies in 1980*

In early February the then Prime Minister announced to the country that elections were to be held towards the end of 1980, or well over a year ahead of schedule. The purpose of calling early elections was to resolve as soon as possible basic questions concerning the future course of the nation, in the light of the failure of the IMF stabilization plan to lead to a recuperation of economic activity, of the suspension of access to the EFF and the inability to reach a new understanding with the IMF, and of the spreading breakdown of social order. In late March the cabinet, acting on the recommendation of the executive committee of the governing party, resolved to end negotiations with the IMF, and at the same time an alternative economic programme was outlined to the public.

As early as the previous September it had been clear that the December performance tests would not be met. Consequently the Jamaican authorities and IMF officials had entered into discussions over what steps would have to be taken to move the targeted variables back towards the established paths, and to secure a waiver from the December performance tests so that the agreement and scheduled credit drawing would not be interrupted. Also, the possibility of augmenting the amount of credit to offset the unanticipated exchange outflows was considered. Simultaneously, however, there was a growing consensus in the governing party that substantial costs but no benefits were being incurred under the IMF programme.

By December, agreement on such questions as the reorganization of the central government and of public enterprises was reached, but the size of the budgetary cutbacks continued to be disputed. Eventually, the Jamaican authorities decided to seek instead a one-year interim standby agreement, in connexion with the decision to hold elections before the end of the year. In the meantime an alternative economic programme was drawn up. And when the Minister of Finance determined that the performance test figures sought by the IMF under the interim accord would be violated by September at the latest, the Government resolved to follow an economic programme that excluded the IMF.

Table 24

## JAMAICA: CENTRAL GOVERNMENT INCOME AND EXPENDITURE

	Fiscal year (a)				Growth rates			
	1978	1979	1980(b)	1980(c)	1978	1979	1980	1980(d)
1. Current revenue (e)	1 037	1 118	1 241	745	59.0	7.8	11.0	-2.3
Tax revenue	737	823	886	...	51.1	11.7	7.7	...
Non-tax revenue	30	61	40	...	-21.2	103.3	-34.4	...
Transfers from capital	268	233	312	...	143.6	-13.1	33.9	...
Development Fund (f)								
2. Current expenditure	1 143	1 283	1 438	1 088	37.2	12.2	12.1	15.8
Wages	280	328	363	...	22.8	17.1	10.7	...
Goods and services	154	152	170	...	35.8	-9.3	11.8	...
Interest payments	212	315	345	...	59.6	48.6	9.5	...
Current transfers	497	487	561	...	38.5	-2.0	15.2	...
3. Savings on current account (1-2)	-106	-165	-198	-343				
4. Capital expenditure	451	499	434	371(g)	35.7	10.6	-13.0	-8.2
Capital formation	146	154	166	...	15.4	5.5	7.8	...
Other	305	345	268	...	48.1	13.1	22.3	...
5. Total expenditure (2+4)	1 594	1 782	1 872	1 459(g)	36.8	11.8	5.0	8.6
6. Fiscal deficit (1-6)	-557	-664	-631	-641(h)				
7. Financing								
Domestic financing (net)	287	541	233	523	-41.7	88.5	-56.9	17.3
Banking system	136	310	135	419	-40.8	127.9	-56.5	12.5
Non-bank	151	231	98	104	-42.6	53.0	-57.6	41.7
Foreign financing (net)	270	122	398	122	1 179.1	-54.8	226.2	336.8
Other	-	-	-	4				

Source: Bank of Jamaica, Report and Statement of Accounts, 1980, and the World Bank.

(a) The fiscal year covers the period April to March. Thus the fiscal year 1978/1979 is shown under 1978, and so on.

(b) Budget estimates.

(c) Provisional outturn, April to December.

(d) April-December 1980 compared to April-December 1979.

(e) Includes capital revenues.

(f) Bauxite levy.

(g) Includes amortizations.

(h) Excludes amortizations.

This alternative economic programme consisted of two parts. One dealt with the long-run strategy of economic development, and the other with the short-term policies designed to contain the expected deterioration of the economy within tolerable limits, while the election issues were resolved.

The main goals of the short-term programme were to minimize the decline of output and employment without accelerating the rate of inflation, and to ensure adequate supplies of essential consumer goods. Targets were set for the product (-2.5%) and inflation (20%, or the same as in 1979), and the required performance levels in the balance of payments, public finance and money supply were identified. Above all, the viability of the programme hinged on mobilizing a supply of foreign exchange sufficient to plug the gap left in the wake of the breakdown of the IMF accord. Otherwise, imports would have to be slashed and the decline in output thus would be greater, while the burden of financing the government deficit would be shifted to the domestic banking system. The latter would lead either to an excessive creation of credit and hence additional inflationary pressures, or an inadequate supply of credit to the private sector, and hence an additional reduction in output. Alternatively, government spending could be reduced, but this also would entail a further contraction in the product and in employment.

In the circumstances, every effort was made to minimize the outflow and maximize the inflow of foreign exchange. Exchange controls were strengthened and the sources and uses of foreign exchange monitored on a continuous basis. An emergency external debt deferral operation with the commercial banks was arranged, and emergency measures, such as the plan to increase payments arrears by over US\$ 100 million, were implemented. Finally, the Government sought extraordinary financing from bilateral sources.

In the area of fiscal policy, expenditures were to be increased by an amount consistent with the maintenance of existing levels of employment and the targeted increase in nominal GDP. The current account deficit would thus be similar to that of the previous year, but the overall deficit would be reduced from 16% to 12% of GDP. Since only minor increases in taxes were contemplated, this entailed reducing capital expenditure to keep the rise in overall spending below the expected rate of inflation. It was hoped that about two-thirds of the finance needed to cover the fiscal deficit would be provided by external sources (see again table 22).

Monetary policy was designed to dampen inflationary pressures, ease the strains on the balance of payments, and provide an expansion in credit sufficient to finance the planned level of economic activity. In January the bank rate, prime lending rate and savings deposit rates were all raised, although they remained appreciably below the rate of inflation. In February, a Deposit Scheme for Payments Arrears was established to mop up excess liquidity arising from the demand for foreign exchange that could not be met on a current basis, and to ensure an orderly liquidation of accumulated arrears as foreign exchange became available. Such a scheme had been used in connexion with the EFF programme in 1978, but this time interest would be paid on the deposits. In March, ceilings on consumer credit equal to the amounts outstanding on 31 December 1979, were established. Finally, the voluntary 40% liquid assets ratio for commercial banks that was introduced in 1979 on a temporary basis was extended through 1980.

Fiscal and monetary measures were reinforced by an incomes policy and price controls. The 10% lid on wage increases introduced at the start of the second year of the EFF programme was retained, while price controls were amplified and rigorously administered.

The fiscal accounts for the April-December segment of the 1980/1981 fiscal year are shown in table 24. As may be seen, significant variations occurred in relation both to the comparable period of the previous year and to the budgeted amounts. Current revenue was about 2% below the 1979 intake, and over 19% below the corresponding budget estimates. Current expenditures exceeded the 1979 ones (by 16%), but were virtually the same as planned. The resulting deficit on the current account was almost twice that of 1979 and two-thirds more than that envisioned for the entire fiscal year. Capital expenditure, on the other hand, was held below both the 1979 level and the planned level. In the latter case, the cutback amounted to one-fourth. Nevertheless, the overall deficit for the April-December period was already larger than projected for the entire fiscal year. This, together with the failure to mobilize foreign financing of the magnitude hoped for, led to much greater reliance on the domestic banking system, and especially on the Bank of Jamaica, than had been intended.<sup>46</sup> Net borrowing from the domestic banking system between April and December was equivalent to over 8% of the GDP for 1980 as a whole. Consequently, as the year progressed the monetary targets had to be modified. The decision taken was to accommodate both the public and private sector demand for credit and thus maintain the output and employment targets, while sacrificing the inflation one. In this manner the expansion of domestic credit reached over 34%, or much more than originally intended: that is to say, much more than would have been consistent with the projected levels of output and inflation.<sup>47</sup> As a result, the increase in the money supply approached 36%, notwithstanding a further appreciable deterioration in the net international reserves and a major increase in savings and time deposits (see table 25). The actual rate of growth of money was about four-fifths greater than planned, and this was probably a major factor in the acceleration of the rate of inflation over the course of the year.

<sup>46</sup>While the foreign exchange gap in the balance of payments was closed only a small proportion of the offsetting inflow was available to the central government.

<sup>47</sup>In this connexion, it should also be noted that the commercial banks exceeded the credit ceilings by an appreciable margin.

Table 25

## JAMAICA: MONETARY BALANCE

	Balance at end of:				Growth rates		
	(millions of Jamaica dollars)				1978	1979	1980
	1977	1978	1979	1980			
1. Money	494	581	625	847	17.6	7.6	35.5
Currency outside banks	182	173	220	260	-4.9	27.2	18.1
Demand deposits	292	397	410	457	36.0	3.3	11.5
2. Factors of expansion	1 122	1 106	1 251	1 831	-1.4	13.1	46.4
Foreign assets (net)	-246	-626	-845	-983	-	-	-
Domestic credit	1 368	1 732	2 096	2 814	26.6	21.0	34.3
Government (net)	691	914	1 128	1 619	32.3	23.4	43.5
Official entities	117	130	161	223	11.1	23.8	38.5
Private sector	560	688	807	972	22.9	17.3	20.4
3. Factors of absorption	628	525	626	984	-16.4	19.2	57.2
Quasi-money (savings and time deposits)	570	665	793	996	16.7	19.2	25.6
Other items (net)	58	-140	-167	-12	-	-	-

Source: International Monetary Fund, *International Financial Statistics*, Vol. 34, No. 9, September 1981.

Measured against the initial targets, the performance of the economy was rather disappointing. Yet, given the yawning foreign exchange gap, the very adverse weather conditions, and the extremely turbulent social climate that developed in anticipation of the election results, the performance was creditable. In any event, it was about the same as was turned in under the IMF stabilization plan.

In the October elections the governing party was defeated, and the new administration indicated that a fresh agreement with the IMF would be a principal component of its plan for economic recuperation.



DEVELOPMENT AND EQUITY

- The challenge of the 1980s -

Enrique V. Iglesias \*/

This article reproduces, with a few changes the Report which the author presented to the nineteenth session of CEPAL in his capacity as Executive Secretary of the Commission.

In the first part, he describes some of the main features of the international situation and the regional scene at the beginning of the 1980s. With regard to the international situation, he stresses the dangers of the protectionism that is reappearing in the industrialized economies; with respect to the regional scene, he stresses the inconsistency between the expanding and increasingly diversified base of production and the continuation of unresolved distribution problems and social inadequacies.

In the second part, he takes up two key concepts in the CEPAL theory of development--the centreperiphery system and industrialization--and uses them as guidelines for dealing with the problems of the present and the future. In so doing, he does not seek to make a retrospective eulogy of those concepts, but rather to use them to interpret some of the pressing economic problems of the region.

In the third part, he outlines the strategic problems of the coming years which, in his view, are those pertaining to international trade, external financing, the energy transition and food security.

In his final observations, he summarizes his vision: whilst it is very important to solve the external problems, it is on the domestic front that the groundwork for the region's development must be laid. On this front, he draws attention to three challenges: the reconciliation of economic and social efficiency, the modernization of private enterprise and of the State, and the bringing of all national policies into line with the criterion of integral development.

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\*/ Executive Secretary of CEPAL.

PROBLEMS AND ORIENTATIONS OF DEVELOPMENT

CEPAL, Economic Projections Centre

At its nineteenth session, held in Montevideo in May 1981, the CEPAL Secretariat submitted a report entitled "Latin American Development in the 1980s", for the main purpose of collaborating with the governments of the region in the preparation of a regional programme of action in relation to the new International Development Strategy.

This article is a slightly modified version of the first two chapters of this report, aimed at the study of two major areas of Latin American development. Firstly, it deals with economic and social trends, focusing its attention on the problems of economic growth, income distribution, poverty, unemployment, energy problems and problems of the external sector, and concluding that it is essential to give a new orientation to development strategies and policies. Secondly, the article considers the main elements of this new orientation, indicating certain objectives which Latin America should set itself in the next decade, especially in the economic field. These include in particular the stepping up of economic growth, the equitable distribution of income and the elimination of extreme poverty, the control of inflation, the transformation of the structure of external economic relations and the stimulation of the participation of the population in development.

The article recognizes the diversity of national situations and stresses the need to take them into consideration in concrete strategies, but it also points out that these general objectives are very useful for guiding the progress of the particular processes towards the common goal of development.



CONSUMPTION IN THE NEW LATIN AMERICAN MODELS

Carlos Filgueira \*/

The main objective of this article is to study the role played by consumption in the economic and political strategies followed in recent years in the countries of the Southern Cone of Latin America. The author places at the centre of this analysis an apparent paradox whose significance he seeks to discover: on the one hand, these societies display a considerable increase in the consumption of durable goods and other "sophisticated" articles, primarily acquired through imports, and this is usually presented as a manifestation of the success of such strategies, but on the other hand, the same societies also display both growing inequality in the distribution of wealth and income and a deterioration in the degree of coverage of the basic needs of the poorest strata.

In order to elucidate this paradox, the author begins with a critical analysis of the significance which consumption usually has in economic theory and emphasises the need to take into account its sociological aspects which makes it an important interface between the two disciplines. He goes on to explore the statistical information available in order to describe the patterns of concentration and dissemination of the consumption of durable goods, especially in the case of Chile, and finally gives a summary of his main conclusions. Among the latter he suggests that the new and sometimes paradoxical patterns of consumption adopted by the various social strata in these societies can only be understood within the context of global tendencies furthering the creation of forms of social organization in which the relative absence of other accepted manners of personal realization and social participation given 'modern' consumption a central role in both personal life and in the principles of social integration.

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\*/ CEPAL Consultant and Director of the Uruguayan Centre for Information and Studies (CIESU).

SOME REFLECTIONS ON SOUTH-EAST ASIAN EXPORT INDUSTRIALIZATION

Fernando Fajnzylber \*/

The succesful export strategies of some South-East Asian countries have been raised in certain Latin American circles to the level of veritable paradigms and it is held that our region should imitate these processes in order to achieve high rates of growth of production, employment, productivity and even real remuneration. For this reason, it is of particular interest to analyse the policies, institutional machinery, and domestic and international social and political conditions within the framework of which these cases have taken place.

The present article analyses some aspects of these processes which show the complexity, richness and heterogeneity that characterize them and which make it clear that the lessons that can be drawn from them while richer and more valuable than those deriving from the 'popular' version generally disseminated in Latin America, do not permit their imitative application in this region.

After the Introduction, section II of the article gives a brief description of the main economic parameters of the four countries in question--South Korea, Taiwan, Hong Kong and Singapore. Section III examines the relationship between the export and industrialization policies, section IV raises some aspects of protectionist and import substitution policy, section V analyses the role which the State has played in these strategies, and the last section of the article sets these examples against the international context in which they have occurred.

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\*/ UNIDO Industrial Adviser in Mexico.

THE DEVELOPMENT STRATEGY AND EMPLOYMENT IN THE 1980s

Víctor E. Tokman \*/

The productive absorption of the labour force has always been one of CEPAL's top priorities, not only because it indicates a rise in the level of productivity but also because it serves as a basis for a more equitable distribution of the benefits of development.

The author analyses this subject in depth, stressing the persistence of a high level of underutilization of the labour force in the region as a whole--as expressed in high unemployment and underemployment indexes--despite the considerable absorption capacity shown by high-productivity urban activities. If the region wants to reach a level of utilization equal to that of the industrialized economies within the next twenty years, the growth rate will have to be 8.3% annually and will also have to be supported by public policies directed towards productive absorption.

Given these requirements, the article emphasizes the need to carry out action directly oriented towards achieving an increase in the productive absorption of the labour force, as historical experience shows, that this problem will not be solved spontaneously, nor is such absorption merely a subproduct of economic growth.

In the final part, the author examines some of the repercussions which the new strategies applied in the region--oriented towards greater external openness--have had on employment, especially in industry. He admits that this sector of production must increase its efficiency and competitiveness, but he also stresses the important role it has played in the absorption of the labour force and consequently in the latter's living conditions. New strategies should always take into account their consequences for employment and the standard of living of the population.

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\*/ Director of the Regional Employment Programme for Latin America and the Caribbean (PREALC).

THE CONCEPT OF INTEGRATION

Isaac Cohen Orantes \*/

The concept of integration dates back a long time, although it has been used as an economic term only since the Second World War, when it was used to explain one of the objectives of the programmes for the reconstruction of Europe. Since its distant origins, its meaning has changed according to circumstances, which justifies an exploration of its various meanings in order to give them a sense appropriate to the present circumstances.

This article does not have a merely semantic purpose, however, as it attempts to shed light on the term by adapting it to reality as far as possible, in order to derive from it more viable integrationist measures. In other words, it is an attempt to define integration so as to identify concrete measures capable of being adopted and carried out. This does not mean, of course, that a simple clarification of the concept of integration is enough to overcome the difficulties involved in the process. This approach does, however, recognize that overcoming these difficulties requires, inter alia, the development of a suitable definition.

The study is divided into two parts. The first is a review of the definitions of integration most frequently used at present, in order to define their common features and some of their disadvantages; the second part offers an alternative definition and analyses its components some of its advantages.

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\*/ Staff member of the CEPAL Office in Mexico City.

DIALOGUE ON FRIEDMAN AND HAYEK

- From the standpoint of the periphery -

Raúl Prebisch \*/

In all his recent writings, the author has maintained that neoclassical thinking is not only incapable of explaining the structure and operation of capitalism in the periphery, but has a misleading influence on economic policy decisions. In the present article he reverts to these ideas, formulating them as if they came up in the course of a dialogue carried out with followers of the two leading contemporary mentors of the thinking in question; thus he is able to present his points of view with the fluid simplicity in which strictly academic essays are often lacking.

In his opinion, the root cause of the incapacity of neoclassical thinking to interpret peripheral capitalism lies above all in its failure to take into consideration the economic surplus, which is the hub of this system's basic characteristics. It disregards the structural heterogeneity which possibilitates the existence of the surplus; it bypasses the structure and dynamics of power which explain how the surplus is appropriated and shared out; it shuts its eyes to the monetary mechanism of production which allows the surplus to be retained by the upper strata; and it underestimates the waste involved in the ways in which the surplus is currently used.

This shortsighted interpretation of the economic process predisposes neoclassical thinking to propose policy measures which do not succeed in promoting the development of the periphery; which increase and consolidate social inequality and which necessitate the establishment of authoritarian régimes, diametrically at variance with the ideas of democratic liberalism. The necessary transformation of peripheral capitalism, which the author propounds, must preserve the values and institutions of democracy and at the same time ensure vigorous economic development and equitable distribution of its fruits.

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\*/ Director of the CEPAL Review.

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