

# CEPAL

## Review

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## Review

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## An economic policy for development

Norberto González\*

This article seeks to make a contribution to the conceptual review of economic policy design and implementation in Latin America. To this end, the author addresses three topics. The first section is devoted to a brief analysis of a number of the factors behind the challenges now being faced, some of which were already in existence prior to the present crisis and some of which have emerged or grown more serious since it began.

The second section is given over to an examination of the orthodox economic policy option as regards the adjustment and the fight against inflation. In the course of this analysis, the author discusses the conceptual postulates of this approach, the policy recommendations made by its advocates and the experiences to which its implementation has given rise.

In the third section, the author deals with some of the currently controversial issues associated with the question of how to manage economic policies so as to bring about structural change. In this connection, he discusses both the conventional or orthodox position and other approaches which might serve as a basis for a different option oriented towards achieving a more dynamic and socially more just form of development.

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## Introduction

As economic policy-makers in Latin America and the Caribbean strive to reconcile the need for a recovery and for economic and social development with the adjustment of the region's economies and the control of inflation, they are faced with challenges of a much broader scope than those encountered for many decades. Hence the need for a thorough review of the conceptual foundations for the design and implementation of these economic policies. In so doing, it is necessary to bear in mind the power relations which serve as their backdrop since, by virtue of their presence, the processes of adjustment and of controlling inflation are not purely technical or economic problems, but social and political issues as well.

This article is intended as a contribution to such a conceptual review. To that end, I will touch upon three topics. In the first section I will comment briefly on a number of the factors underlying the challenges now being faced, some of which were already present before the current crisis and some of which have appeared or grown more serious since it began.

In the second section I will examine the orthodox economic policy option for achieving an adjustment and fighting inflation on the basis of its conceptual postulates, the policy recommendations made by its advocates, and the experiences to which its implementation has given rise. These experiences have varied quite markedly. In some cases, such as in the countries of the Southern Cone around the year 1980, the application of this option was more systematic and adhered relatively closely to its conceptual postulates. In other cases, its implementation has been partial or sporadic. For the sake of brevity, I will not go into these cases in detail. For the same reason, rather than presenting a comprehensive analysis of the orthodox approach in relation to adjustment and stabilization policies, I will focus on those characteristics of this approach which, in my opinion, largely account for the recessionary effects of the policies based on such recommendations.

In the third section I will deal with some of the currently controversial topics associated

with the question of how to manage economic policy so as to bring about structural change. In this connection, I will refer both to the conventional or orthodox position and to other

approaches which might serve as a basis for a different option oriented towards the achievement of a more dynamic and a socially more just type of development.

## I

### The crisis and economic policy

#### 1. *The challenges*

Even before the onset of the crisis, the task of managing the balance of payments and maintaining a reasonable fiscal and monetary balance was quite complex, if this were to be done in a way which would permit growth and through-going economic and social changes to be achieved in the countries of the region. This complexity stemmed from the particular pattern of development which characterized the region over a period of 50 years, a pattern that combined considerable progress in certain aspects with structural flaws in others. A few examples will illustrate this point.

After the great 1930 world crisis, a process of industrialization and agricultural modernization took place in the region. However, backward manufacturing sectors continued to exist, as did an agricultural peasantry whose productivity was very low, and these circumstances placed constraints on supply which were conducive to inflationary processes.

Some degree of export diversification had been achieved, but it was a limited one, and there continued to be a sharp asymmetry in foreign trade between the structure of exports and that of imports. The region's economies were heavily dependent on other countries for technology and were highly vulnerable to fluctuations in the international economy. This gave rise to a systematic tendency towards balance-of-payments deficits and external bottlenecks.

The conflict over income distribution sharpened as the development process continued. The high-income strata of the population acquired luxury goods in what amounted to a premature imitation of the consumption patterns of developed countries, thereby hampering

efforts to achieve the levels of saving and productive investment necessary for growth while, at the same time, meeting the needs of the poorer segments of the population. The emergence of middle-income strata, although undoubtedly an economic and social step forward, also generated aspirations to a better standard of living which outstripped the possibilities opened up by the region's economic growth, and this created additional social and economic tensions.

The urbanization process gave these sectors an even greater voice. It was thus no easy task to align the level of consumption of the whole of the population with the total amount of goods available, and this difficulty gave rise to persistent pressure from the excess of demand over supply and to a dispute among social sectors concerning the distribution of income.

Meanwhile, the public sector's responsibilities in connection with the economic and social development process had been growing and, as a result, its expenditures had been increasing steadily. Its income, however, had not been rising at the same pace owing to the resistance put up by those sectors which were called upon to shoulder the greater part of the increase in tax payments. The outcome was a mounting —and inflationary— fiscal deficit.

This combination of progress and shortcomings in the economic and social structure gave rise to short-term imbalances and tensions in two different ways. Firstly, it made it difficult to carry forward the process of economic and social development while at the same time maintaining fiscal, monetary and balance-of-payments equilibria. Secondly, it generated the sort of price and wage spiral typical of inflationary processes.

These problems, which already existed prior to 1981, are still with us, but they have grown even more serious since the beginning of the crisis and have assumed truly dramatic proportions. In addition, some new factors of major significance have emerged. One such factor that is particularly deserving of attention is the payment of interest on the external debt, which constitutes an unprecedented burden on both the balance of payments and the fiscal sector. As regards the balance of payments, the interest on the external debt represents around 35% of exports, a proportion which is not compatible with a normal management of the external sector in the countries of the region. Even after deducting net capital inflows (which have, moreover, diminished due to the reluctance of private banks and international public financial agencies to lend to the region), the net transfer of resources out of the region still amounts to approximately one-fourth of its exports. Given the slow growth—or even decrease—of exports, in order to make these transfers the countries have had to drastically cut back their imports, thereby exacerbating the external bottlenecks to which they are subject, as well as the internal imbalances between supply and demand in terms of the availability of goods and consumers' aspirations.

As for the fiscal sector, since it is responsible for paying a portion of the interest on the external debt equivalent to around 4% of the product, it has become virtually impossible for this sector to balance its accounts. In order to do so, it would have to generate income far in excess of its expenditures on consumption and investment and this, in turn, would entail an even greater sacrifice as regards the wages of public employees and the expenditures necessary for economic and social development than those already made in recent years.

The consequences of the crisis have been even greater than they might otherwise have been because it has taken place over a much shorter time span than would be needed in order to change the countries' economic and social structures and to raise their exports and fiscal income.

Bearing these facts in mind, it becomes easier to account for the very rapid acceleration of inflation seen in Latin America in recent years

and for the difficulties encountered by the countries in their attempts to carry out an adjustment and to manage inflation. The countries' and governments' scope of action has been so greatly reduced that it is virtually impossible for them to achieve sustained growth, an external equilibrium and the control of inflation all at the same time.

This has been going on for six years now, and the situation shows signs of continuing for quite some time into the future, with no indication of when any substantial improvement may be expected. This is not a temporary problem. The countries of the region find themselves forced into a behaviour pattern that entails structural features of stagnation, marked economic instability and mounting social tensions, which are difficult to reconcile with political stability and the consolidation of democratic processes. The countries of the region are caught up in a vicious circle whereby their limited capacity for action hampers growth, and their lack of growth hinders them from expanding their manoeuvring room.

## *2. What is needed in order to broaden the options*

During the past few years, an effort has been made in various countries of the region to construct an economic policy option based on an approach which would incorporate elements of economic reactivation, economic and social development and, particularly, structural change in such a way that all these processes would be compatible with the adjustment and the control of inflation. Although some countries in the region have experimented with combining long- and short-term objectives and have obtained interesting results, this is far from being enough.

One of the preconditions for this option is a major reduction in the net external transfers represented by interest payments on the external debt, which, as mentioned earlier, take their toll on both the balance of payments and the fiscal sector. If this is not done, the countries will have to continue generating large surpluses of exports over imports and of fiscal revenue over fiscal expenditure on consumption and investment. Under such conditions, the possibility of creating a different economic policy option

either becomes quite remote or ceases to exist entirely, no matter how effective the design and management of such a policy might be.

Even assuming that a substantial decrease in net external transfers were to be achieved, the countries would still be faced with the task of defining an economic policy orientation different from that suggested by the orthodox school of thought. It is important to grasp the fact that, although this task is not an easy one, it is possible and should be undertaken—resolutely and with a sense of urgency—by building upon the progress and experiences of recent years. It is imperative that the economic discipline required to keep inflation within acceptable bounds should be maintained in order to prevent an economic disarticulation such as that seen in processes of hyperinflation. However, controlling inflation in the countries of the region, which has gradually given rise to types of social behaviour that lead to expectations of instability, is a complicated undertaking. These economies

must also be modernized and must undergo a structural change so that they may become more efficient and competitive and so that both economic effort and its fruits may be distributed more equitably.

Genuine progress towards long-term economic and social development objectives is not a by-product of policies whose chief aim is to prevent price increases and permit the payment of the interest owed on the debt. Instead, the transformation of the economic and social structure, the creation of more equitable and participatory societies, a frontal attack on underemployment and poverty, the improvement of the living standards of middle-income sectors and the achievement of a faster rate of growth should carry a high priority in the management of economic policies and in the approach taken to the payment of interest on the external debt.

Thus, the challenge before us is a very great one, and a great deal of realism and imagination will be required in order to meet it successfully.

## II

### The orthodox approach to the adjustment and to controlling inflation

#### 1. *Some basic characteristics of the orthodox approach*

First of all, the orthodox approach places the whole of its emphasis on the management of demand. According to this focus, adjustment and stabilization policies are primarily aimed at rectifying imbalances caused by excess demand—generated mainly by the public sector—which produces a deficit on the current account of the balance of payments, speeds up inflation, and distorts the relative prices of internationally tradeable and non-tradeable goods. It ascribes little importance to the fact that these problems may not be caused by the excess demand of the public sector, but instead by the private sector, by cost-push factors (coming from outside the country or stemming from an internal conflict over income distribution), or by a reduction in supply resulting, for example, from the deterioration of the terms of trade, from higher interest

payments on the debt or from a slump in agricultural output due to adverse weather conditions. Consequently, the policies designed in accordance with this approach may not attack the true causes of these problems and may thus produce negative effects unnecessarily.

Secondly, this approach relies almost exclusively on aggregate instruments for achieving an adjustment and stabilization. Hence, in seeking to lower demand, consideration is not given to the differences in the importance of various types of public and private expenditure on consumption and investment. Some government outlays, such as excessive military spending, may be cut without having a detrimental effect on economic and social development. The same may be said of the private consumption of luxury items. On the other hand, public or private expenditure on education, health, support for important production activities, the promotion of non-traditional exports, or consumption by

lower-income strata are of a high priority and should be defended to the utmost when it comes to reducing overall demand.

Thirdly, at least as applied in the region, this approach has not taken into account the fact that policies of adjustment and of inflation management are not one and the same. Some policy measures which are good for the adjustment may be bad for the fight against inflation, and vice versa. For example, a currency devaluation reduces imports and increases exports, thereby improving the trade balance, but at the same time may intensify the inflationary process. Since the onset of the crisis in the region, relatively more attention has perhaps been paid to the adjustment than to inflation, and this may help to account for the sharp and widespread deterioration seen in the stability of domestic prices.

Fourthly, this approach strives to carry out the adjustment quickly, using short-term measures, without taking either the time or the steps needed in order to make structural reforms in the economy, raise fiscal revenues, and increase and diversify exports. The adjustment therefore tends to be a recessionary one involving a drastic reduction in consumption and investment. Fifthly, an attempt has been made to apply these policies in a large number of countries at the same time, without taking into account the fact that their simultaneous implementation has a more widespread effect on the world economy. I will come back to this point later on.

Finally, the same or very similar versions of these policies are recommended for all the countries, despite the fact that the prevailing circumstances usually vary considerably from one country to the next. These policies have not been made flexible enough so that they might be tailored to the quite distinct circumstances and characteristics of each one of the various countries and to the particular stage each has reached in its history.

## *2. Experiences with the application of the orthodox approach*

The choice of which approach to take to the adjustment and to the fight against inflation, as well as its form of implementation, depends on the amount of power held by different social

groups. It should therefore come as no surprise that the burden of this effort may be unequally distributed. The more influential sectors will attempt to see to it (and they will succeed in doing so) that the measures taken will be such as to protect them in so far as possible from the adverse consequences of these processes. Hence, the effort demanded of the weaker social groups will be disproportionately great.

In those cases in which the orthodox approach has been put into practice it has succeeded in ensuring that the interest on the debt has indeed been paid, but it has not diminished the relative debt burden being shouldered by these countries' economies. Inflation has been reduced, but has later often increased once again. Furthermore, the characteristics mentioned earlier have largely been responsible for the recessionary results of these orthodox policies.

The reduction of demand has been pursued by means of cuts in the fiscal deficit (primarily made by decreasing expenditure on consumption and investment) and the tightening of credit. Attempts have also been made on the basis of this approach to lower production costs and correct relative prices through wage controls and currency devaluations.

Thus, there has been a failure to take into account the fact that—unlike the situation in the past—ever since the beginning of the debt crisis, the interest payments made on the external debt have been the cause of a very large part of the fiscal deficit, of the struggle over income distribution and of the balance-of-payments deficit on current account.

Hence, the concrete facts are that the cuts made in fiscal expenditures on consumption and investment and the reduction in domestic demand required in order to generate the trade balance needed to offset the countries' interest payments have been of an unprecedented magnitude and have not attacked one of the main roots of the problem, i.e., reducing the enormous outlays made in the form of interest payments on the debt.

The reduction of demand alone will not enable the developing countries to adapt to changes in the international context such as the slowness of the world economy's growth, the decline of commodity prices, the increased protectionism

of the developed countries and the high level in real terms of international interest rates.

These policies are capable of doing no more than temporarily fending off some of the symptoms of the increase in the developing countries' external debt and of the crisis in their economies. They do so, however, in a way which causes these same policies to become unstable over the medium term, as demonstrated by the experiences of many Latin American and Caribbean countries during the past few years. The burden of the adjustment cannot be shouldered only by the developing debtor countries without creating tensions which will adversely affect the continuity of such policies.

Due to their lack of differentiation and selectivity, these orthodox policies frequently produce results which are just the opposite of those desired. Non-essential expenditures are continued and even increased (e.g., military spending and expenditures on luxury consumer goods), while the bulk of the reduction is made in the living standards of low-income sectors and in expenditures on consumption and investment which are essential to economic and social development.

In those cases where inflationary processes are nearing the point of hyperinflation, shock policies may be appropriate. Structural economic changes, however, are quite a different case altogether; in such situations, shock treatments are counterproductive.

In addition, unlike what occurred in the past, when this approach was applied in just a few countries at the same time, in recent years and especially since the crisis began, it has been implemented simultaneously in a large number of developing countries whose exports are heavily concentrated in a limited number of commodities or traditional manufactures. This constitutes an additional cause for concern inasmuch as, if many countries reduce their imports and increase their exports of similar products simultaneously, this will tend to depress the international economy, push down export prices and heighten the protectionism of the developed countries.

In those instances where the orthodox approach has been implemented in the region, the drastic reduction in demand—made without selecting or prioritizing the expenditures to be

cut back—has resulted in a sharp deterioration in the living standards of wage-earners and other low-income groups and has thereby exacerbated social inequalities, as well as causing a steep drop in investment. Consequently, these economies are not growing and their production capacity is not being modernized. The increases in output which have been achieved in some years have constituted no more than a partial recovery from previous declines rather than representing any actual expansion of their production capacity. Since other countries in the world, including other developing nations, are making new investments and are constantly modernizing their production capacity and adapting it to the new technologies which are gaining sway in the world economy, the region's relative level of competitiveness is rapidly declining and this, in turn, gives rise to further devaluations and additional inflationary pressures. The region's economies are thus becoming structurally stagnant and its societies are becoming less and less equitable. Moreover, since the drastic nature and rapid pace of the reduction being made in fiscal expenditure render it impossible to programme, the State is losing its capacity for action and its ability to meet economic and social development needs.

Furthermore, in some countries which have implemented the orthodox approach, economic power has been concentrated in the hands of a few and in some cases has been used in a highly speculative manner and in the pursuance of objectives which, to a great degree, are aimed at transferring existing assets from one owner to another rather than augmenting production capacity.

### *3. The structural adjustment according to the conventional approach*

A number of the basic structural guidelines followed by the orthodox approaches to the adjustment and to the fight against inflation used to be, to a certain extent, implicit. In recent years, however, they have been stated more explicitly in the terms and conditions generally laid down by international lending agencies and the positions adopted by developed countries in international negotiations such as the Uruguay Round of GATT.



This conventional or orthodox approach to the structural adjustment involves three main points:

a) The liberalization and opening up of the economies to the outside world in respect of both trade in goods and services and foreign investment.

b) The predominant role assigned to market forces, which are allowed to operate freely or with the least possible interference, and to the price system as the mechanism for resource allocation, along with the reduction of the State's role in directing the economy to a minimum.

c) The privatization of public enterprises and of activities formerly conducted by the public

sector as such or by its decentralized units, coupled with a reorganization of public enterprises aimed at ensuring that they will operate on the basis of criteria which are either identical or very similar to those used by private enterprises.

These three elements are closely interrelated and together constitute what has been termed a "neo-liberal" concept of development. I will discuss these elements as a group in the final section of this article, as well as suggesting some alternatives to them which I believe are better suited to the actual conditions in the region and provide a sounder basis for guiding its development strategies and policies.

### III

## Towards an economic policy for development

#### 1. *Two ways of opening up the region's economies*

The concept of opening up the region's economies to the rest of the world can be interpreted in two different ways, which, although interrelated, have different implications. On the one hand, the opening up of an economy may involve an emphasis on the export of new goods and services and on the winning of new markets. On the other hand, it can be interpreted as the dismantling of existing protectionist barriers in order to allow the unrestricted, or less restricted, entry of goods or services produced by other countries into the domestic market where they can compete with locally-produced goods or services; in this second sense, the opening up of an economy usually also involves the unrestricted movement of finance or of direct foreign investment.

As regards the movement of goods and services, the first interpretation is perfectly compatible with, and complementary to, the most intensive possible utilization of the domestic and regional markets of Latin America and the Caribbean. The second interpretation, entailing the total or partial dismantlement of protectionist barriers, may or may not be compatible with

the internal development of economic activities, depending on whether or not it is a measured process which takes two requirements into consideration. The first of these is that a reasonable amount of time must be allowed for the strengthening of national economic activities before they are subjected to competition from products of more developed countries. The second is that consideration must be given to how much protection other countries, particularly the developed nations, provide for their own activities so that the degree to which the economy in question will be opened up may be determined in relation to whether or not other countries place increasing obstacles in the way of the entry of its products into their markets and whether or not they subsidize their exports of similar goods.

History shows that all the industrially developed countries except England (which had the advantage of being the first) started out by protecting their local economic activities from foreign products. Even countries already at a quite high level of industrialization have provided support and protection for new sectors in order to overcome their relative disadvantage *vis-a-vis* countries which had a headstart. It is therefore both sensible and necessary to apply foreign trade restrictions in order to achieve technologi-

cal progress through the incorporation of more advanced production activities.

On the other hand, as national industries acquire experience and maturity, they need to be subjected to an increasing degree of external competition so that they will be spurred on to greater competitiveness and efficiency. Thus, protection should be gradually reduced over time. Nevertheless, this reduction must also be a measured process which takes into account the level of openness or protectionism of other countries in the world and the extent to which they subsidize their exports.

In parallel with this, appropriate protection, promotion and support need to be provided in order to stimulate other sectors whose development plays a functional role in each stage in the evolution of these economies so that the process of technological progress and dissemination may reach increasingly higher levels of complexity.

The reduction of protection and promotion in given production sectors should therefore be gradual rather than abrupt, as it has sometimes been when orthodox concepts have been applied in the region. In these instances, the protective structure was dismantled quite swiftly on a very widespread and relatively unselective basis and was also, in some cases, coupled with an overvaluation of the local currency in an attempt to help lower inflation. The excesses committed under this doctrine when attempts have been made to apply a very low and uniform level of protection to all sectors have been based on the mistaken idea that the industrialization process must be spontaneous and have resulted in major setbacks in the industrial and technological development of the economies concerned.

We live in a world of imperfect competition, in which all countries, and particularly the developed nations, erect substantial tariff and non-tariff barriers and subsidize their exports. The protectionism of the developed countries has been a persistent and significant phenomenon ever since the great worldwide crisis of 1930. The reduction in protectionism achieved through the series of GATT negotiations has primarily been in relation to goods which the industrialized countries trade among themselves, while a much smaller decrease has been made in the protectionism applying to the manufactures and semi-manufactures exported

by the Latin American countries. Moreover, the protectionism of the developed countries *vis-à-vis* these goods has been on the rise since the 1970s and has come to include a growing number of products. Restrictions tend to be placed on the exports of developing countries in precisely those sectors in which they are managing to become competitive in the developed countries' markets, due to the demands for protection made by producers in those countries. There are many well-known cases of protectionism and subsidization by developed countries in respect of activities in the agricultural sector, the textile industry, automobile production, electronics and iron and steel, to name but a few. It is important to underscore the fact that the developed countries' attitude towards the protection and promotion of economic activities has been a dualistic and changeable one. During certain periods they have strongly favoured the opening up and liberalization of those sectors in which they have had a competitive advantage over the developing world. However, they have applied heavy restrictions (and, moreover, continue to do so and even to increase such restraints) in those sectors and time periods in which they have been at a competitive disadvantage.

Thus, while the developed countries try to convince the developing countries of the virtues of conventional economic doctrines, they themselves generally choose whether or not to use these same approaches according to the specific requirements of each given situation. Sometimes they opt for free trade and sometimes for protectionism. The developing countries of the region should therefore take this into account and avoid doctrinary excesses.

One of the topics which has been much discussed in recent years in connection with the opening up of economies has been that of service activities. Some of these are high technology sectors whose development is closely tied to overall economic development and which are becoming of increasing importance for goods-producing sectors as well. Certain sectors related to technology, information sciences, banking and marketing are of great importance not only because of the direct contribution they can make to overall development, but also because the goods-producing sectors must rely upon them in order to achieve an adequate level of efficiency.

This topic is currently being actively discussed at the international level. In my view, an approach much like that applied to goods-producing sectors needs to be implemented in these service sectors so that they will receive the protection and support which will permit rapid progress to be made in activities of such great overall significance. In so doing, however, care must be taken to ensure that the support required by these activities does not result in an excessive increase in the costs of other products for which they provide inputs.

The international market's price structure is useful as a basic point of reference for the behaviour of the various economic sectors and as a tool for economic decision-making and for the management of the development process. Exaggerated and unnecessary distortions of domestic prices, especially when maintained for an indefinite period of time, cause the economy to lose its point of reference, promote inefficiency and reduce the incentives for improving competitiveness so as to bring it up to international standards. On the other hand, however, in many cases developing countries need to adopt a long-term view which takes in the dynamics and external factors involved and, on the basis of this perspective, modify the domestic prices of certain sectors or goods, moving them away from international levels, so that new production sectors may be developed. The use of economic policy tools, the exchange rate, protective tariff and non-tariff measures, export promotion mechanisms, taxes, subsidies and credit, as well as direct action when necessary, are all forms of State action which should be used to promote and guide overall development, with emphasis on priority activities.

## *2. Planning and the economic role of the State*

Planning must play a leading role in guiding economic policy. The setting of priorities and the effective implementation of an economic and social development strategy should be basic components of economic management. Short-term factors need to be managed with a view to the direction in which the economy should move in order to reach its medium- and long-term goals. Concern for the real economy needs to be

reintroduced into short-term management, and the countries need to put aside the predominantly financial approach and the aggregate tools of economic policy which have become prevalent in many of them as a consequence of the crisis and the use of orthodox policies. A type of planning directed towards these aims should play a concrete part in decisions concerning which expenditures should be reduced and which expenditures should be increased, what economic and social projects should be carried forward, and what are the most suitable policy tools for promoting industrial, agricultural, technological and social development. The need for a genuine and effective use of planning is an important one because formulations of general medium- and long-term goals and guidelines are only useful if they are put into practice by means of an appropriate set of implementational tools.

As regards the role of the State in the economy, an animated discussion is now going on in the region as to what size it should be, what types of functions it should perform and what are the most effective ways for it to do so. In recent years a number of groups both inside and outside the region have strongly advocated a reduction in the size of the State and the privatization of activities which have until now been carried out by State enterprises, decentralized units or the central government administration itself.

Stating this problem in terms of what size the State and its enterprises should be is, in my view, a mistaken approach. Instead, the discussion should focus on what functions the State needs to perform, directly and indirectly, and what is the most efficient way for it to do so. On the basis of such an analysis, a decision could then be taken as to which elements should be privatized and which should be maintained within or incorporated into the sphere of direct State action. The outcome might well be that the State should be smaller, the same size or larger than at present. Another result would be the formulation of definite guidelines concerning the way in which to modernize it and to make it more effective.

There have been many instances in the past when the State has taken on too large a number of activities or when too large a portion of the labour force has been employed by the government or public enterprises. In some cases this

incorporation of enterprises or functions has come about in response to crisis situations in private enterprises or economic activities that have been resolved through their absorption by the public sector, which has thus taken on problems and responsibilities normally outside its purview. One such case occurred as a result of a hasty opening and liberalization of the economy, which placed private enterprises operating in the local market in serious difficulties and, without giving them the time or support they needed to become more efficient, presented them with the option of going out of business unnecessarily or being taken over by the State. It is quite easy to find examples of enterprises now in the public sphere which were incorporated into it when they were on the point of going bankrupt.

It is therefore clear that there are situations in which it is best to reduce the size or privatize certain functions and to seek to increase the efficiency of the operations of the public sector and its enterprises.

However, it is equally clear that there are extremely important direct functions of production or consumption and investment expenditure which the State and public enterprises should continue to perform in order, among other things, to carry out activities that are essential to development and to ensure that external savings will complement domestic savings rather than taking their place. Furthermore, in some countries of the region, public enterprises have played an important role in establishing a balance with transnational corporations, especially in situations where local private enterprise is not yet strong enough to function as a major independent force. Dealing with foreign enterprises is useful, not only because of the financial contribution they may make, but also because of the important role they play in incorporating new technologies into the economy and in opening up external markets to non-traditional exports. At the same time, however, direct foreign investment must conform to the development needs of each country, the need for an increasing endogenous capability for creating technologies and the Latin American countries' need to maintain control over the basic workings of their economies and to conserve an essential measure of decision-making autonomy in regard to their economic and social

development. The public sector as such, as well as State enterprises, have a highly important part to play in all of this. A reasonable degree of articulation must therefore be achieved among the roles of the State and of State enterprise, foreign enterprise, and private national or regional enterprise. Otherwise, in the absence of an appropriate public-sector policy, foreign investment may simply become a substitute for domestic investment, rather than complementing it.

### *3. The complementarity of exports and import substitution*

Another point in connection with development strategies which warrants discussion is the complementarity that ought to exist between a reasonably efficient form of import substitution and the exportation of non-traditional goods. In the debate of economic matters within the region, these two courses of action have often been presented as if they were opposed to one another rather than as complementary activities. It has been said that the possibilities of import substitution have been exhausted and that engaging in it greatly reduces the possibilities of promoting exports and winning over external markets.

While it is true that in some cases the authorities have waited too long before combining policies for promoting non-traditional exports with import substitution and that protectionist barriers have been too great and have been maintained longer than they should have been, this does not mean, in my opinion, that the import substitution process should be discarded.

When all is said and done, the term "import substitution" signifies the development of new sectors which are essential to the incorporation and dissemination of technology. From this standpoint, the possibilities of import substitution have not been exhausted, nor will they be, at least not for a long time. The incorporation of new and more advanced sectors is important not only because they can make a direct contribution to the level of economic activity, but also because the continuation of technical progress in the entire economy hinges upon them.

Furthermore, it is perfectly possible to manage economic policy tools in such a way that import substitution and export promotion will be both compatible and mutually complemen-

tary. If the use of these tools is differentiated according to the stage of development of each of the various economic sectors and if the levels of protection and export promotion are co-ordinated both between and within sectors, then a strategy combining substitution and exportation can be developed which will serve to promote and expedite structural changes in the economies and societies of the region.

In short, the artificial dichotomy between import substitution and exportation, between the State and the private sector, and between planning and the market must be laid to rest as soon as possible in the region. When these elements are presented as if they were mutually exclusive alternatives, or when an attempt is

made to discuss in the abstract, how important each should be, then these subjects come to be treated as issues of economic doctrine rather than as the object of realistic analyses. If, however, the discussion is based on the assumption that the State and the private sector, planning and the market, import substitution and exports all have essential functions to fulfil in economies such as those found in most of the Latin American countries, then the right question to ask—and to answer—is what type of functions each needs to perform and, above all, how these functions should be co-ordinated so that, together, these elements will operate as they must in order to bring about changes in the economic and social structures of the countries of the region.

## Conclusion

In this article I have focused on the subjects of economic policy management, the opening of economies to the rest of the world, and the role of the State and of the private sector so that I might examine these topics with some degree of specificity. This has meant, however, that I have had to pass over other subjects which are equally vital to the region's development, despite the fact that they should occupy a position of central importance among the region's concerns and activities. These include production-sector strategies; policies on technology; international economic, trade and financial relations and the region's position in the world economy; the strategies and policies required in order to bring about a transformation of the social structure; broader participation and greater equity in the development of the region; and co-operation within the region and with the rest of the developing world. These subjects have, however, been analysed on repeated occasions by ECLAC, and the author therefore refers the reader to these studies.

In conclusion, I would like to return briefly to the subject of the external debt in order to stress the need for changing the way in which this issue is addressed so that an effective and stable reduction may be achieved in the net external transfers and interest payments that must be

made by the public sector. The object of such a reduction would be to allow the countries to pursue adjustment policies and their fight against inflation under substantially different conditions than those now prevailing and to make these objectives more viable and more compatible with the countries' economic and social development. Such development, hitherto postponed, has clearly become not only imperative but urgent as well.

The burden of the adjustment cannot be shouldered by the debtor countries alone but instead must be properly distributed between creditors and debtors, between developed and developing countries. Furthermore, the countries of the region, for their part, need to achieve a more equitable distribution of the effort required to bring about structural change and to control inflation, as well as of the fruits of this effort.

Only in this way can the countries attain a socially enlightened form of development, greater decision-making autonomy and the consolidation of democracy, which, in addition to its intrinsic value as a fundamental political objective, is also necessary in order to arrive at the social consensus that is, in turn, essential if a sustained development process is to be achieved.