



**ECONOMIC
DEVELOPMENT,
PLANNING AND
INTERNATIONAL
CO-OPERATION**



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INTRODUCTION

The contrasts of development

1. The problem of economic development is essentially that of rapidly assimilating the vast resources of modern technology in order to raise the living standards of the broad masses. Considerable difficulties stand in the way of solving this problem, both because of the magnitude of the process of transferring technology and because of the special circumstances in which the problem arises.

2. These circumstances offer very sharp points of contrast. Modern technology requires considerable capital, which can be accumulated without undue hardship in the more developed countries because of their high level of per capita income. This technology, built up gradually during the evolution of capitalism, has now to be absorbed by the Latin American countries with levels of per capita income and a capacity for capital formation much lower than those of the more advanced countries.

No such contrasts existed in the latter countries, at least not in the acute form in which they are found in the countries now in the course of development. When technology was being developed, innovations were translated into new forms of capital to the extent permitted by savings capacity. Naturally there can be no turning back of the clock to reproduce forms of capital that existed in the more advanced countries long ago, when their per capita income was comparable to that now prevailing in the Latin American countries. Nor does modern technology offer, except to a very small extent, alternative solutions that can be applied when capital is in short supply.

3. On the other hand, the Latin American countries are not making full use of their savings capacity. The high-income groups tend to follow patterns of consumption that became possible in the more advanced countries only after a long period of development. The existence of such patterns in conjunction with a low average per capita income is due to the fact that income distribution is heavily weighted in favour of the groups that hold a dominant position in the social scale.

Hence, the pattern of income distribution is one of the most serious obstacles to economic development; but it is also a source of social tensions, which lead to increasingly insistent demands for redistribution.

In the development of the more advanced countries, capital accumulation preceded income redistribution, which followed later as the political and trade union power of the masses became stronger. In Latin

America the problems of capital accumulation and income redistribution tend to arise at the same time.

Nevertheless, whatever action is taken to make more effective use of Latin America's savings potential, the low prevailing level of income sets limits that cannot be exceeded under the present institutional system.

The high rate of population growth

4. There are further points of contrast. The falling death rate seems to have been largely a social phenomenon in the historical development of the more advanced countries. It was a consequence of the steady improvement in living conditions; and this improvement also created — although not on the same scale — social conditions conducive to a drop in the birth rate.

In Latin America, on the other hand, the fall in the death rate is making itself felt long before those social conditions have been able to affect the birth rate. The fall in the death rate is a technical rather than a social development, due to the rapid absorption of techniques for the prevention and cure of disease.

There is no reason why raising living standards in Latin America should not bring about the same change of psychological outlook, conducive to a lower birth rate, as it did in its day in the more advanced countries. But this process takes time, and meanwhile the rate of population growth has reached an extraordinarily high level, much in excess of anything that occurred during the evolution of capitalism.

This is an extremely delicate problem, for it touches feelings that are rooted deep in Latin American life and cannot be dispelled by purely economic considerations.

The pressure of consumption and capital formation

5. Be that as it may, the rise in the rate of growth of the population makes it even more imperative to increase the investment coefficient. But there are strong forces working in the opposite direction. The technique of mass dissemination of information and ideas is propagated much more quickly than productive technique — another instance of the uneven process of permeation of technique that is a major factor in Latin America's economic development.

As regards consumption, this truth is evident in the tendency of countries that are developing to adopt the way of life of countries with a much higher income level. The broad masses of the population are by no means free from this tendency; on the contrary, it reveals itself with increasing clarity in both individual consumption and social consumption through State expenditure.

The dynamic value of the incessant emergence of new needs and new forms of consumption should not be ignored. It could become a strong

incentive to increased productivity and, in some cases, might counterbalance a certain inclination for the rate of personal activity to decline whenever income levels rise.

6. What should be done, therefore, is not to oppose the techniques for the dissemination of ideas and information but to enlist their co-operation in the service of economic development. With this in view, resolute efforts must be made to promote capital formation. If the broad masses of the Latin American population are easily induced to consume, this does not imply that they are incapable of shouldering the responsibilities of capital formation as well. This is a key point in economic development, since, if income redistribution is not accompanied by a predisposition towards popular capital formation, it will be impossible to bring about a steady improvement in the level of living of the lower-income groups.

The penetration of technology and structural changes

7. It is essential that as the assimilation of productive technology proceeds, it should spread to all internal activities in order to rectify one of the most notorious distortions caused by the unevenness with which technology penetrated in the early stages. It has not percolated from the centre to the periphery, as in a series of communicating vessels, in an even flow to all parts of the economy alike. Where natural resources were more abundant so that this was feasible, technique was directed almost entirely towards the development of exports and ancillary activities. It did not move towards the areas that were technically backward where, in fact, pre-capitalist techniques prevailed.

No external effort whatsoever was made to transform this unilateral development structure and to remedy these great technological discrepancies. On the contrary, they all became part of a characteristic concept of the natural order of the economy, according to which in the international division of labour the primary functions were relegated to the periphery.

8. Contemporary productive technology is currently seeping through into internal activities and this entails constant changes in the production structure, in which industrialization plays a dynamic and supremely important part. The resulting changes in internal activity and the concomitant wage increases are progressively strengthening the capacity of the countries on the periphery to retain the fruits of their technological progress in the export field. Without such wage increases, and except in special cases, these results tend to be transferred outwards, the intensity of this outward movement depending upon the degree of disparity in technology and productivity between export and internal activities.

9. The prevailing system of land tenure is one of the major impediments to the extension of technology, apart from its effects on income distribution. It is common knowledge that productivity is generally very low, particularly in the internal agricultural sector. But this evil

cannot be attacked by a mere redistribution of land, without reference to the over-all economic development problem. In actual fact, unless the rest of the economy grows at a satisfactory pace, it will be impossible to absorb the population that is displaced by technical advances in agriculture or to find an adequate outlet for the increase in agricultural production not intended for foreign markets.

10. The structural changes entailed by the penetration of technology cannot be confined to the internal market. To achieve maximum productivity, it is essential that production should become specialized and grow to a suitable scale. Truths as well known as these have been deprived of much of their meaning in Latin American development. The outdated mould of international trade has been preserved, in which every Latin American country focused its attention on the industrial centres and little reciprocal trade was carried on. Industry has thus developed inwards, neglecting opportunities for developing new exports, while agriculture has also tended to withdraw into itself, except in the case of most — but not all — traditional export commodities. Accordingly, the common market too is a *sine qua non* of technical progress, and the long and arduous advance towards this objective has already begun.

11. The problems of economic development are actually problems of transition: the transition of the Latin American countries to higher levels of production technology in which the entire labour force will have the opportunity to achieve levels of productivity approximating those in the more advanced countries. Hence, the changes cannot be limited to the economy. They have to embrace the individual himself and endow him with the necessary skills to manage and organize the new production techniques.

12. Economic development therefore calls for a conscious and resolute effort to influence the forces of the economy so as to bring about all the required structural changes in a systematic and far-sighted manner. This is to a large extent the duty of the State which thereby assumes new and difficult responsibilities. Generally, in the Latin American countries, the State is in no position to take on such responsibilities; no economic development policy can, however, be effectively formulated or executed unless the State develops its capacity to do so.

Significant changes in the policy of international co-operation

13. The new turn which the very idea of international co-operation is now taking is of decisive importance for development policy. When international finance contributed to the exploitation of peripheral resources only with a view to promoting the development of the centres, the unilateral penetration of technology into the primary producing countries was fully compatible with the maintenance of traditional structures. Indeed, the stability of such structures was conducive to the unilateral expansion of exports whatever the degree of political instability on the surface. International co-operation now tends to pursue a very different aim: to help the developing countries to increase their own rate of growth

and correct the substantial disparities in income distribution in order to improve the standard of living of the broad masses. Such bold aims cannot be achieved without the transformation of the existing structures.

14. International co-operation is thus taking on a new meaning consistent with the popular dimensions which economic development policy is assuming to an increasing degree — popular dimensions not only by virtue of the nature and scale of the aims pursued but also because of the new responsibilities which this co-operation involves.

If development policy requires the understanding of the ruling circles as to the inescapable need for structural changes, the exercise of the responsibilities referred to by the mass of the people has deep significance from both the economic and the political point of view.

Basically, the most important policy problem as regards development consists in mastering the art of achieving and constantly maintaining an adequate rate of investment financed from national savings. Savings must be increased at the expense of present consumption by the affluent groups and of increments in popular consumption, as per capita income rises. The stronger the determination to restrain such increments in popular consumption, the more necessary it will be to have recourse to measures of compulsory saving; and the wider the use made of compulsory saving, the more serious the danger of encroaching upon principles which are deeply rooted in the Latin American countries, irrespective of their political vicissitudes.

Hence the part — and it may well be a decisive one — to be played by international resources is to contribute to the rapid growth of per capita income, so that increased saving does not seriously jeopardize the chances of expanding popular consumption, since apart from its political effects, this might considerably weaken the incentive to raise productivity.

15. A policy of co-operation, however, would not alone suffice to cure Latin America's economic and social ills. If it consisted merely in sporadic bouts of action, dictated by the circumstances of the moment, it would be no more than a palliative. Nor could the most determined policy of structural reform forge ahead untrammelled by difficulties involving the institutional system itself, if international co-operation failed to fulfil the promise of recent events as regards its breadth of scope, and the course to be pursued.

Foreign and domestic private enterprise

16. Foreign private capital has an important part to play in all this; but the question should be approached in the light of a criterion different from certain nineteenth-century concepts whose influence is felt even today. Foreign private capital, besides making its immediate productive contribution, must be a powerful instrument for the diffusion of technology; that is, it must help to ensure that the latter is assimilated both by the technicians and by the entrepreneurs of the country into which

it flows, instead of remaining the exclusive prerogative of the foreign experts who introduce it. Once technology has thus been disseminated, these local entrepreneurs and technicians will be able, in the course of time, to emulate those of more highly-developed countries.

Unless an attempt is made to bring about this gradual and progressive technological levelling-up, in the broadest sense of the term, the steady advance of development will be impossible, since the patent differences in training levels and the inaccessibility of certain techniques to local personnel will breed discord. Development will be neither economically sound nor politically stable.

Herein lies the key to the solution of more than one problem, since lower standards of technology give rise to understandable inferiority complexes, whereas technological levelling-up, by strengthening the idea of equality of opportunity, will make a noteworthy contribution to the fruitful association of domestic and foreign elements in the wide field of private enterprise.

17. All this is of great importance for the efficacious operation of the system of private enterprise. The Latin American peoples are fundamentally endowed with a strong sense of personal initiative, which has developed to a remarkable extent where conditions have been favourable. The significance of this for development policy is profound. There is a huge private enterprise potential of which it has been impossible to take advantage because of the serious shortcomings of the educational system. The systematic training of the broad masses at all levels of technology could open up vast horizons for individual initiative by producing and promoting the social mobility of dynamic elements at present largely wasted. It will be no easy matter to tackle this problem in a continent where, in a good many cases, the countries have not yet been able to eradicate illiteracy. It also reflects a social complex which is unfavourable to economic development.

There can be no denying that herein, and in the strength of capital accumulation, are to be found two of the elements which are most important in the dynamics of other systems of development and which are reflected in high rates of growth. The deficiency of such elements in Latin America detracts from the efficacy which characterized the system of private enterprise based on the free interaction of the forces of the economy, when the capitalistic development of the more advanced countries was at its height.

There is something paradoxical in all this, since the endeavour to reproduce the outworn patterns of capitalistic development is precisely what is preventing the system of private enterprise from making the most of its potentialities.

CHAPTER I

THE REDISTRIBUTION OF INCOME AND THE ACCUMULATION OF CAPITAL

Disparities in distribution

1. As was the case during the economic and social evolution of the great industrial countries, the progressive improvement in the level of living of the people of Latin America depends essentially on the rate of growth of income and its proper redistribution. But there is a basic difference between the two cases, already referred to in the introduction to this paper: in the industrial countries the accumulation of capital essential to the growth of income took place prior to its redistribution whereas in Latin America the problems of accumulation and redistribution tend to arise simultaneously. Consequently the region is faced with a new situation, which cannot be dealt with purely on the basis of past experience.

A higher economic growth rate naturally calls for a speedier rate of accumulation. The present rate of investment is inadequate. This is attributed to the low average per capita income, and there are good grounds for advancing this argument, but it is not a complete explanation.

2. This low per capita income in fact covers great disparities in distribution, which, moreover, usually tend to increase rather than diminish with economic development.

No reliable data are available on income distribution or on the possibilities of increasing investment at the expense of the consumption of the higher-income groups, but one important consideration leads to the conclusion that this would not be enough to bring about a satisfactory rate of growth.

The question is one of increasing investment not merely in the form of specific capital goods, but also in the form of social investment in education, housing and health, which is usually very inadequate in Latin America. A major effort is needed in this respect, both to improve the immediate outlook for the broad masses and to help attain the great economic aim of increased productivity.

Combined use of national and international resources

3. In view of this need, it is essential for international resources to be made available on a greater scale than in the past, in order to increase the rate of growth. But the provision of such resources would not absolve Latin America from the obligation to reduce excessive consumption in order to promote economic and social investment.

This is a vitally important point; the provision of international resources must not be a mere palliative for the economic and social ills of Latin America. If it is not accompanied by measures for the effective use of national resources, it will be largely abortive from the standpoint of economic development.

The key to the problem is the proper combination of both types of resources. International resources cannot make up for the absence of a national endeavour to increase investment, nor can the intensification of such a national endeavour make up for the lack of a vigorous policy of international co-operation.

4. Such a combination would seem to be desirable from another standpoint: in addition to being a crying domestic need, the reduction of income distribution disparities also has some bearing on the policy of international co-operation, since it is hard to see how the provision of international resources could be on a sufficiently generous scale if decisive action is not taken against the excessive consumption of the high-income groups in Latin America.

Popular capital formation

5. The problem must be viewed from a dynamic standpoint. If the level of living of the bulk of the population is to be improved by redistributive measures, no static formula will do. The consumption of the higher-income groups must inevitably be restricted so that economic and social investment may be increased. But it is inconceivable that a redistribution policy could be applied for the purpose of directly and immediately raising popular levels of consumption, without some sacrifice of such investment. The end in view can only be progressively achieved as per capita income rises and its distribution is improved. And what is required to increase it is precisely the expansion of investment by means of the above-mentioned combination of resources.

Even so, the progressive redistribution of a growing income cannot bring about a parallel increase in popular consumption. The upward trend of the latter must be slower than that of income, so as to raise the rate of investment until the level necessary for the maintenance of a satisfactory rate of economic development is reached.

6. Herein lies the most difficult aspect of the problem, in which a new approach is more vital than in other cases: how to augment capital formation as the pattern of income distribution changes.

Without capital formation on the part of the broad masses, redistribution policy will have adverse effects on economic development. But although the saving of the higher income groups is inadequate at present, it is much greater in relation to income than that of the rest of the population. And the disparity would be still wider if tax incentives to saving on the part of these groups were provided.

Redistribution and development are needed at one and the same time. And it will be impossible to achieve this unless alongside the political and trade union power of the broad masses their economic power is developed, and with it their clearly-defined responsibility within the process of capital accumulation.

This is a matter not merely of propagating passive saving practices, but of stimulating active popular participation in capital investment and, in a wider sense, in the task of satisfying the demands of economic development.

Origin of major disparities and the problem of coping with them

7. Income redistribution has two facets. The first of these relates to the origin of the major existing disparities. The second comprises the disparities themselves. In former times, the major disparities in question derived largely from the land tenure system and from the rise in the value of land with the progress of the community. This problem still survives, in some cases in an intensified form. And other disparities due to different causes have gradually been superimposed on those of earlier date. These have their origin in over-protection of industry, practices designed to restrict competition and which also discourage technical progress, the regressive consequences of inflation, State intervention in the economic decisions of individuals, and other distortions of various kinds.

Consequently, the problem consists not only in redistributing income with a view to the progressive reduction of the disparities in question, but in striking at their very roots. Apart from their magnitude, there is a fundamental difference between the disparities resulting from arbitrary transfers of income and those deriving from the greater or lesser contribution of individuals to technical development and to the increasing efficacy of the production process. The former militate against economic development, whereas the latter are an expression of development itself.

8. As regards redistribution, in the course of history it has resulted from two forces, in addition to the economy's own momentum — the organization of the trade unions and taxation.

The power of the trade unions is increasing considerably in the Latin American countries. But in some of them it is not yet effective enough to ensure that wages are adjusted correlatively to the increase in productivity. What is more, it has not been possible to correct the adverse effects of investment-induced inflation. Here, in the last analysis, is to be found a very serious manifestation of the relative abundance of

under-productive manpower in primary activities, artisan industry and unskilled services. Its persistent pressure tends to preclude a rise in real remunerations.

But the reverse has occurred in some cases, where the trade unions have wielded their power in order to raise wages above the point warranted by productivity and the entrepreneurs' profits. The result has been the inflationary spiral, with all its pernicious and disturbing effects.

Incentives to capital formation

9. These circumstances partly determine the action of the State and place a greater responsibility upon it when the weakness of the trade unions leaves income distribution at the mercy of the free play of economic forces.

Through taxation the State may exercise a considerable influence over income distribution and capital formation. But, on the whole, it cannot be said to have made good use of its opportunities. In some cases, taxes have clearly come to form a high proportion of the economy's aggregate revenue, but only a relatively small part of the resources thus obtained is assigned to capital investment, the remainder being used to cover current expenditure in which social objectives are not always given the priority they deserve.

From another point of view, it is unusual for the high-income groups to contribute as fully as they should, either because the tax system is regressive or because tax evasion makes a mockery of taxation itself or of proper tax collection.

Furthermore, tax interests seem to have prevailed over economic considerations. Although investment is insufficient, the proportion of income that is consumed receives the same tax treatment as the proportion that is allotted to investment. Nevertheless, some reforms have been introduced with a view to stimulating investment and discouraging consumption on the part of the higher-income groups. This is an avenue which calls for thorough exploration.

It is undeniable that this tax differentiation tends to rectify disparities in consumption but not in the capital formation deriving therefrom. The inheritance tax is of course the ultimate corrective.

10. When the State, instead of taking this course, resorts to taxation in order to appropriate resources for investment, this does not mean that it is obliged to use the whole amount directly. The use of part of such resources for promoting private action through development institutions has proved to be effective in several countries. But no assistance has been forthcoming in this connexion from international sources except on a very small scale. None the less, Latin American private activity offers great opportunities for absorbing those resources through these or other suitable channels.

11. Apart from its immediate economic repercussions, this method

of contributing capital to Latin American private enterprise helps to raise the national saving coefficient. Elsewhere in this study reference is made to the fact that the periods allowed for amortizing international loans are frequently very short from a balance-of-payments point of view. But if this question is viewed from the angle of capital formation, amortization periods — for both national and international loans — should be much shorter than the period allowed for wear and tear or obsolescence of capital, since it thus becomes possible to save a larger proportion of the income generated by the investment of capital.

12. The loan of investment resources as a means of promoting the eventual formation of capital does not have to be confined to enterprises. It may also be extended to workers. This may turn out to be one of the most effective means of achieving popular capital formation and a question arises in this connexion which should be given some consideration. The use of credit for the purchase of durable consumer goods has been rapidly gaining ground in the Latin American countries. This is clearly a way to afford the broad masses of the population access to goods which it would be difficult for them to obtain in any other way. But this, in common with inflation, is a grave threat to saving practices. Perhaps such practices could be encouraged by credits for the purchase of securities by the workers themselves, either in the enterprises in which they work or in others. These possibilities should be explored and the organizations that finance development might play a very important part in this respect.

Loans for capital investment have so far been made direct to enterprises. A substantial part could be made indirectly, i.e., through loans to workers for the purchase of securities. Reference has just been made above to the need for international credit institutions to devote a large part of their operations in Latin America to encouraging incentive on the part of firms and concerns in the area. These operations could be co-ordinated, in one way or another, with the growing participation of workers in the capital formation process.

13. The Latin American countries regularly face a very serious problem of capital formation in their public services. The use of international assistance for the purchase of securities in these services could have very important repercussions on the accumulation of capital and on the management of the enterprise. The participation of the producers and users of such services could provide a new way out of the common dilemma of choosing between foreign ownership and management by the State.

14. The question now arises to what extent such incentives or incentives by way of taxation would be sufficient to raise the coefficient of national savings, or whether coercive savings measures will have to be used.

Under the existing institutional system the limits to compulsory savings are much narrower than in other types of economic-social organization, and it is natural that this should be so, since it constitutes one of the fundamental differences between them. In view of this limitation,

and the desire not to overstep the bounds, international financial assistance is inescapable.

This, in the final analysis, is the function of international assistance as part of a new approach to the policy of international co-operation: to reduce the coercive element in capital accumulation, or to do away with it altogether if this is possible, so long as spontaneous capital accumulation is not adequate to maintain a satisfactory rate of economic development. Once sufficient spontaneous capital accumulation has occurred, international financial assistance will no longer be inevitable, but may continue to be useful as an instrument for propagating new techniques or strengthening economic interdependence.

CHAPTER II

STRUCTURAL CHANGES IN THE ECONOMY AND FOREIGN TRADE

1. INDUSTRIALIZATION, ITS FLAWS AND SHORTCOMINGS

Discrepancies in demand and intensity of growth

1. The progressive industrialization of Latin America, as an essential step towards economic development, is based on a simple and well-known fact: as per capita income rises, the demand for industrial goods tends to grow faster than the demand for primary commodities. This is due to changing patterns of consumption and of production technology.

If the relatively heavier demand for industrial goods could be met from imports paid for with exports of primary commodities, without detriment to the price of the latter, the need for industrialization would not be inescapable. What happens, however, is that exports of primary commodities are subject in the rest of the world to the same disparity in the income-elasticity of demand and this disparity is usually accentuated by import restrictions on primary commodities.

This is the main reason why exports of primary commodities from Latin America have been relatively slow in expanding, although the trend is also partly attributable to certain deplorable mistakes in economic policy.

There is no sign that this tendency for exports of primary commodities to increase only slowly will change in the foreseeable future. Thus, if the rate of development of the Latin American countries is to be expedited, industrialization must be speeded up.

The scale of this structural transformation of the economy is in no way arbitrary. To achieve a given rate of economic growth higher than the growth rate of exports of primary commodities, the process of industrialization also has to reach a given magnitude in view of the intensity of demand for industrial goods.

All these tendencies can be expressed in quantitative terms, and it is necessary to do this so as to formulate the specific objectives of economic development policy.

The basic flaws in industrialization

2. Although the *volume* of industrial production is not arbitrary, its *composition* has proved to be so in Latin American experience. From this point of view, the process of industrialization suffers from three main flaws which have weakened its contribution to improving the standard of living. These are: (a) all industrialization activity is directed towards the domestic market; (b) the choice of industries to be established has been based more on circumstantial reasons than on considerations of economic yield; and (c) industrialization has failed to overcome the external vulnerability of the Latin American countries.

3. The excessive channelling of industry towards the domestic market is a result of the development policy pursued in the Latin American countries and of the lack of international incentives to exports of industrial goods from the region.

Development policies have been discriminatory as regards exports, Assistance has been given — through tariffs or other restrictions — to industrial production for internal consumption but not to industrial production for export. The production of many industrial goods has thus been developed at a cost far above the international level, when they could have been obtained with a much smaller cost differential in exchange for exports of other industrial products which might have been produced more profitably. The same could be said of new lines of primary commodities for export and even of traditional export commodities within certain relatively narrow limits.

It would not, however, have been enough to place production for export on an equal footing with production for the domestic market. In the larger centres, measures would have had to be adopted to facilitate imports of certain industrial goods from the developing countries, thereby giving these countries a greater capacity to import precisely those goods for which there is a greater difference in cost. In this way, a very useful division of labour would have developed in the industrial field, very different from the traditional pattern of trading primary commodities for industrial goods.

Until recently, no serious effort had been made to establish such a division of industrial activities among the countries of Latin America.

4. As regards the second flaw in industrialization — the frequent absence of considerations of economic yield — this is largely due to the lack of a far-sighted policy, which was naturally very difficult to establish at a time when the countries of Latin America had little experience in that respect. The process of industrialization has been neither continuous nor regular. Pressure of circumstance has provided a strong impetus, for example, in times of import difficulties due to a scarcity of foreign currency or to hostilities abroad.

On such occasions, restrictions were applied where they were easiest to introduce without upsetting the development of the internal economy, namely on imports of finished items, particularly consumer goods. Thus industries producing such goods sprang up. The easiest course of action,

however, is not always the most economic. In many instances the production of certain raw materials, intermediate industrial goods or capital goods would have resulted in a lower cost differential with respect to the international market than was the case with consumer goods.

5. The combination of the first two defects in the industrialization process leads to the third: failure to strengthen the structure of the Latin American economy so as to withstand external fluctuations and events. For want of a proper division of labour in industry — as also in agriculture — the policy of import substitution has had to go much further than would otherwise have been necessary; and as the preference in respect of import substitution fell on consumer goods, this trend either ended or is about to end in almost complete substitution as regards such goods in the more industrially advanced countries of Latin America. Imports are thus confined to the raw materials and intermediate goods essential for maintaining current economic activity, and also to capital goods.

This brought about a new kind of vulnerability resulting from the disappearance of the reducible margin of imports. When exports decline cyclically, inability to import essential goods has an unfavourable effect on the growth rate and even leads to a contraction of the economy.

Protection and the downward trend of the terms of trade

6. It has been stated above that industrialization is a *sine qua non* of development. In view of the considerable differences in technological levels and capital intensity as between peripheral industry and the major centres, the former usually has a much lower productivity, which is not offset by commensurately lower wages. Hence the need for customs protection or some other form of subsidy; in other words, a deliberate industrialization effort.

It is possible to conceive of spontaneous industrialization in the abstract. If wages were lower in proportion to the differences in productivity between peripheral industry and the big industrial centres, there would be no need for protection.¹ Nevertheless, this would mean a sizable loss in real income for the primary producing countries, since, except in special cases, the drop in wages would be accompanied by a deterioration in the external terms of trade.

The vital importance of this point justifies a brief digression. One of the dynamic functions of industry — and of the activities that develop in conjunction with it — is to absorb that part of the increment in the active population that is or may be rendered redundant as a result of technical progress, in primary production as well as in artisan industry

¹ The term "protection" is used here in its widest sense, that of any type of subsidy accorded to an activity.

and unskilled services. Protection allows industry to carry out this function of absorption at the prevailing or even a higher wage level.

Without protection, the increase in the active population would exert pressure on wages in primary production, and their consequent decline would stimulate exports. Except in special cases, the prices of exports would also drop, in view of the limitations of external demand.

In this abstract train of thought a decline may be imagined of such magnitude that wages would offset differences in productivity in relation to the big centres. The point of spontaneous industrialization would then have been reached, but at the expense of a deterioration in the external terms of trade.

Protection tends to counterbalance the depressive effects which the growth in the active population would otherwise have on wages in primary production and on the terms of trade. Thus, protection not only helps to ward off a decline in wages, but also enables wages to rise proportionately to the increase in productivity in primary activities.

Technical progress in these activities is not enough to raise wages. It is essential that the increment in the active population which is redundant in primary production should be absorbed into industry and other activities, thereby enabling primary activities to retain the advantage of their technical progress through a rise in wages. If this does not happen — and there are no measures of any other kind to prevent it from happening — the export activities transfer abroad all or part of the fruits of their increase in productivity, or go even farther in extreme cases.

7. This is the argument put forward in the present study. There is a tendency for the terms of trade to deteriorate, and deliberate non-spontaneous industrialization offsets this trend. The extent to which it is able to do so depends on the relative intensity of the industrialization process. If, despite industrialization, deterioration takes place, it is a clear indication that the process has not been intensive enough to check it.

The depressive effect on wages is not always manifested in deterioration of the terms of trade when there is technical progress. As stated before, special cases exist. In fact, if primary production comes up against natural obstacles to its expansion, or is deliberately restricted by entrepreneurs, wages do not rise nor do prices drop with technical progress. The only increases are in income from land and the profits of the entrepreneurs themselves. In this case, the retention in the country of the benefits of technical progress depends on whether production is in national hands or not. There are also cases in which the State acquires part of the benefit through taxation, or in which the same results are achieved through trade union action.

8. The foregoing statements on the increase in primary exports should not be interpreted in an over-simplified way. It is undoubtedly worth while for the Latin American countries to expand their primary exports, provided that certain limits set by the world market are not overstepped. Considerations of economic yield also enter into the picture.

The most economic solution would be to promote traditional exports

to the point at which the resulting increase in real income was not less than that achieved by employing the same factors of production in industry or in other primary activities for either the external or the domestic market. But there is no automatic solution and it is one of the most delicate aspects of economic development policy.

9. The deterioration of the terms of trade is one of the regressive effects of income distribution which derive from the precarious nature of economic development and justify a redistribution policy. But in this case the regressive effect operates in the external field and presents the policy of international co-operation with a serious problem.

2. ELIMINATING THE BASIC FLAWS IN INDUSTRIALIZATION

New exports

10. Eliminating the three basic flaws in the industrialization process referred to above calls for corrective measures of considerable scope which are not always within the reach of the Latin American countries and which merit a brief examination.

As stated above, industry has been directed exclusively towards import substitution to the detriment of exports, be they industrial products or new primary commodities. The common market provides a partial solution to this problem. The first step has already been taken with the establishment of the Latin American Free-Trade Area at Montevideo and the Central American customs union. The differential treatment that the member countries accord one another means in practice that the importing country is providing a subsidy for the exporting country. By encouraging exports, this will enable a gradual change to be made in the structure of production. The subsidy is reciprocal, and the essential aim of the negotiations is to ensure equivalence of benefits by means of readjustments effected in the light of the Montevideo Treaty's application.

This principle of reciprocity is of cardinal importance in enabling the member States to forge ahead with determination in reducing and gradually eliminating customs duties and other restrictions.

However, the readjustments entailed by the application of this principle cannot be undertaken at once. Some time must pass before any country that regularly exports more to the Area than it imports can correct the situation by expediting its liberalization measures. In the meantime, the deficit country will have to draw on its scanty monetary reserves to cover the excess of imports, and this may cause it to water down its own trade liberalization measures.

Hence the need to supplement the Montevideo Treaty by organizing a system of reciprocal credits financed by adequate international funds. This method, far from being incompatible with monetary convertibility, will help to make convertibility a reality. The lack of a credit system will make the road to the common market much longer and more arduous than it need be.

The development of industrial exports among the Latin American countries will help to reduce production costs and provide some industries with opportunities to export to the rest of the world. A policy of incentives and the co-operation of the large industrial countries could hasten the process.

Economic merits of the substitution policy

11. It was explained above that the substitution process has been directed especially towards the consumer industries, with the resultant distortion and inelasticity of imports. The gradual development of the common market will make it possible to embark on co-ordinated import substitution in respect of raw materials, intermediate products and capital goods from the rest of the world, and thus to import consumer goods. The same results could be obtained by developing new exports both within the common market and to the rest of the world. Apart from being a better economic proposition, this would mean that imports would become diversified again and recover the flexibility that they are now losing.

External vulnerability

12. Distortion of imports is exposing the Latin American countries to a new type of external vulnerability, formerly unknown to them. This vulnerability comes to the fore when exports fall and there are insufficient resources to cover the cost of the imports required by the level of economic growth attained.

The proper remedy is not to curtail income until imports fall to the level where they can be balanced by exports, but to readjust imports so that with a smaller volume it will still be possible to maintain the level of income and to continue to raise it.

But this presupposes a reducible margin of imports, and herein lies the crux of the matter. We have already seen that the progressive implementation of an import substitution policy steadily narrows the reducible margin of imports until it is insufficient for the proposed readjustment. Economic growth then either suffers a setback or its pace slackens, until the situation rights itself through import substitution and, whenever possible, the encouragement of new exports. In the meantime, these difficulties that beset the economy spur on the inflationary forces.

13. There is a positive lesson to be learned from this sequence of events. The source of the trouble is the failure to pursue a far-sighted policy that anticipates the requirements of economic development instead of merely attempting to meet them as they arise. It usually happens that when exports develop along satisfactory lines, with ample resources to absorb growing imports, there is no need for such measures as import substitution and the encouragement of exports.

There is no reason to expect that exports will fall as a result of pursuing

this policy. In reality, import substitution and the bolstering of new exports have to be carried on as a continuous and regular process so long as the discrepancies in external trade referred to earlier have not been corrected. If such a policy is applied, no increase in exports will be required to ensure an improvement in internal employment levels, nor will the latter fall when exports decline. Employment will also expand continuously and regularly at the rate of growth of the labour force, however exports may fluctuate.

14. Accordingly, the solution of the problem of external vulnerability is essentially of a structural and not an anti-cyclic nature. But, to be more effective, it needs the additional stimulus of certain anti-cyclic measures. To this end, attention should be given to ensuring that imports recover their flexibility, particularly in order to cope with fluctuations of exceptional magnitude. In addition, there are other conceivable anti-cyclic measures for taking full advantage of investment opportunities when exports grow and for promoting the regular development of internal investment. All this should not preclude any measures of international co-operation that might be taken to mitigate fluctuations in exports.

3. THE PERIPHERAL POSITION OF LATIN AMERICA IN INTERNATIONAL TRADE

Different meanings of substitution policy

15. Import substitution in respect of industrial goods in peripheral countries does not have the same significance as import substitution in respect of primary commodities in the industrial centres. There is a very important difference so far as the policy of international economic co-operation is concerned, and this derives from differences in the income-elasticity of demand for imports of primary commodities as compared with industrial goods, as already referred to above.

The demand for industrial goods tends to grow faster than the demand for primary commodities as per capita income rises. As a result, unless there is import substitution in respect of industrial items and unless new export lines are forthcoming, the countries exporting primary commodities, in order to maintain external equilibrium, will be forced to maintain a slower rate of growth than that in the industrial centres; and the greater the rate of population growth in the primary producing countries as compared with the industrial centres, the greater the effect of this trend will be.

But the primary objective of any international economic co-operation policy is that primary producing countries should grow faster than the industrial centres and thereby attenuate the great differences in per capita income between the two. Such an aim, which is far from being fulfilled, makes it essential to advance resolutely towards substitution in respect of new industrial lines.

Reflection will show that import substitution, if kept within certain

bounds, does not mean reducing imports below a level which can be met from exports. On the contrary, import substitution in respect of certain items is sometimes undertaken in order to leave room for larger imports of other goods required for economic development.

From another point of view; import substitution in respect of primary commodities in the industrial centres further accentuates the divergence between the volume of such imports and the demand for industrial goods in the peripheral countries. This places the latter countries in a quandary: either they must reduce their rate of growth to maintain external equilibrium or they must increase the scale of import substitution and create new export lines to maintain and expedite their rate of growth.

Import substitution therefore has a very different meaning according to whether it is achieved in the industrial centres or in the peripheral countries. In the latter it tends to correct the divergence of trends without affecting the volume of international trade; in the former it tends to aggravate the divergence and jeopardize international trade.

16. The need to correct the divergence limits the scope of the substitution policy which the peripheral countries can apply. If the limit is exceeded and imports fall below the capacity to import, the peripheral countries do harm to international trade too and compel the industrial centres to limit their own primary commodity imports in order to safeguard their external equilibrium.

Thus, so long as substitution policy is kept within these bounds, the efforts of the peripheral countries to protect their industrial production are in no way detrimental to the industrial centres. But measures to protect the primary production of the industrial centres are harmful to the peripheral countries.

The need to revise the traditional notion of reciprocity

17. The reduction or abolition of customs duties — or of other restrictive measures — likewise has a different meaning according to whether it is the industrial centres or the peripheral countries that are being considered. If the industrial centres apply such measures, primary commodity exports from the peripheral countries will grow, with a resulting expansion in their industrial imports, either at the same rate or, by taking advantage of the favourable situation, at a quickened pace. On the other hand, the reduction or abolition of duties on industrial imports by the peripheral countries will aggravate the divergent trends, without any possibility of an increase in the volume of such imports beyond the level allowed by primary commodity exports.

The fact is that the passive position of the peripheral countries prevents them from producing a favourable effect, through greater industrial imports, on the rate of growth of the industrial centres. And even if they were not thus prevented, the difference in income levels between the two groups would become more pronounced, thereby frustrating the main purpose of the policy of co-operation.

18. The time would therefore seem to have come to revise the traditional notion of reciprocity of customs concessions as between the industrial centres and the peripheral countries. So long as the divergent trends in external trade are not corrected, a peripheral country cannot be expected to make concessions similar to those granted by the industrial centres, for that would force a retreat in its import substitution policy. The point is not that the industrial centres should import more from the peripheral countries without the latter increasing their imports from them to an equivalent extent, but that, such an increase must take place only in respect of those imports which promote economic development and not of those which frustrate it by hindering industrialization.

Actually the imports that a peripheral country is interested in encouraging are not usually subject to protectionist duties, and hence no concession appears to be necessary to bring about an increase. But if concessions were made that affected existing industries and imports grew at the expense of those industries, imports favorable to economic development could not expand to the same extent and the tempo of development would slacken.

19. This aspect of the matter is of such vital importance that it is worth while dwelling on it even at the risk of being repetitious. A peripheral country subject to disparate trends in its external trade needs to forge ahead continuously with import substitution, and with the encouragement of new exports, in order to compensate for these trends. If exports to the industrial centres can be stepped up as a result of concessions granted by those centres, there will be less need for import substitution to maintain the same tempo of development, or the peripheral country can continue its substitution policy and use the growth of exports to hasten the pace of its development. But if import substitution falls behind — that is, if imports are increased to the detriment of existing industries — it will be unable to maintain the tempo of development. In the last analysis the peripheral country will have made a pointless sacrifice, since in any case it could not expand its imports beyond the level permitted by the increase in its exports.

There is a great difference between an increase in imports that encourages economic development and an increase that hinders it. It is essential to recognize this difference if the concept of reciprocity, in addition to being inspired by the basic interests of the industrial centres, is to meet the needs of peripheral development.

The responsibility of the peripheral countries

20. What has just been said does not mean that the entire initiative in this respect should lie with the industrial centres. On the contrary, the peripheral countries must also adopt a series of measures contributing to the effectiveness of this policy.

First, the substitution policy must be based on considerations of economic yield that have often been conspicuously absent in the decisions

taken by Latin American countries. Care must be taken that such considerations underlie progressive substitution policy, without precluding any adjustments that may gradually have to be made in existing activities.

Secondly, protectionist measures should be kept to reasonable proportions, so as to restore healthy external competition and obviate restrictive practices which weaken production efficiency, thereby slowing down the pace of economic development.

Lastly, the industrial centres must have some assurance that the concessions they grant will be accompanied by a corresponding increase in imports favourable to the economic development of the peripheral countries, and that substitution policy will go no farther than is required to correct disparities.

*The Latin American common market and trade with the
rest of the world*

21. The foregoing point is of great importance in view of the efforts now being made to establish a common market in Latin America. The fear is commonly expressed that the development of reciprocal trade among the countries of Latin America will weaken trade with the rest of the world.

There is no intrinsic reason why this policy should have such an effect. The composition of imports from the rest of the world will continue to change, and substitution in respect of those imports that are displaced by others can be effected at a higher economic yield in a much larger market than the small national markets where this process now takes place. Consequently substitution policy can be a joint undertaking. There are no grounds for supposing that it will be carried further than is necessary to ensure the dynamic balance of external trade with the rest of the world.

22. From another standpoint, encouragement by the industrial centres of imports from Latin America, both of primary commodities and of industrial goods, could be of great help in correcting external trade disequilibria and thus achieving dynamic equilibrium with a tempo of economic development far higher than that of recent years.

Once this aim has been attained, the traditional concept of reciprocal concessions can gradually recover its validity. But it should be remembered that the great differences in productivity between the industrial centres and Latin America require the maintenance of certain levels of protection, which are essential to a vigorous tempo of industrialization.

Thus it is understandable that the countries that have just set out on the road towards the common market, with the Montevideo Treaty, have restricted the market to themselves and to other Latin American countries that wish to accede. This does not mean that the common market is not compatible with a sizable expansion of trade with the rest of the world through more and more comprehensive reciprocal

concessions, as soon as dynamic external balance is assured. However, there cannot be a simultaneous movement in this direction because of the marked differences in the degree of development. The first impetus must come from the large industrial centres.

23. If the latter were gradually to open their markets to Latin American manufactures, the Latin American countries could begin to abolish their duties and restrictions, so that imports from the industrial countries could increase in proportion to the exports to them. Thus the industrial countries might manage to abolish duties completely while the Latin American countries continue to protect their industries.

But as industrial export activities demonstrated their capacity to absorb an increasing proportion of the human resources available with a high level of productivity, the area of protection might shrink progressively. It is true that the lowering or possible abolition of protective barriers in a growing number of industries in Latin America might be to the detriment of some. This problem would be offset by transferring factors of production to more efficient export industries.

However, it is not suggested that such a policy of liberalizing Latin America's imports from the large centres could be applied in the near future. It might require a very long time, as would, even in the most favourable circumstances, the technological assimilation and capital accumulation needed to provide an industrial structure strong enough not only to export increasing quantities of industrial goods, but to compete on equal terms with the products of the large centres in Latin America itself.

24. Now that the project of gradually establishing a Latin American common market is in its preliminary stage, it offers the large centres and the Latin American countries the opportunity of taking decisions of fundamental importance to world trade and to the tempo and nature of Latin America's economic development.

On these decisions depends the question whether development will be directed inwards to the Latin American common market, with whatever degree of external trade is permitted by the slow growth of exports, or whether it will be directed outwards, not in order to reproduce outworn patterns of international division of labour, but to develop new patterns that will make a powerful contribution to Latin American industrialization and at the same time spur on the progress of the industrial countries to yet higher levels of technology and productivity.

CHAPTER III

THE LAND AND ECONOMIC DEVELOPMENT

Marked inequalities in land tenure

1. The land tenure system prevailing in most of the Latin American countries is one of the most serious impediments to economic development. But the problem must not be looked at from one side only. Efficient use of the soil depends not only upon the reform of the land tenure system, but also upon the rate of economic growth itself. There is a close interdependence between the land and economic development.

2. The land tenure system is characterized by extreme inequality in the distribution of land and of the income accruing from it. Most of the productive land is in the hands of owners of large estates, relatively few in number, and the remainder is distributed among innumerable small and medium-sized holdings, that are usually too small to permit of rational farming.

Some of the large estates are, of course, farmed efficiently. But as a general rule, thanks to their very size, their owner draws a substantial income without troubling himself to improve the farming of his land or encourage his tenants or sharecroppers to do so. Moreover, he has only to wait, and the value of the land will increase by virtue of the growth of the population and the development of the economy. And this in itself helps to attract those whose object is not rational farm management, but a means of protecting themselves against inflation or of evading wholly or in part, the burden of progressive taxation.

The stronger this interest in the opportunistic investment possibilities of the land rather than in making the best use of its productive potential, the greater will be the disproportion between its value and its immediate yield. And this puts it almost out of reach of those who are best qualified to work it. Herein lies one of the reasons for the existence of minifundia. The existence of large estates, the excessively high price of land and the shortage of resources inevitably foster this phenomenon, as the pressure of population on the available land increases.

Land and population

3. The dissemination of modern production techniques is also very uneven. Progress has been made in respect of production for export in particular, but not as regards agricultural commodities in general. Low productivity continues to characterize production for domestic consumption. This is one of the most important strongholds of pre-capitalism. There is no other field in the Latin American economy in which the profundity and magnitude of the disequilibrium between labour and capital are more apparent. In Latin American agriculture, there is still a high proportion of the active population working on the land on a basis of scanty capital and very low productivity per capita and per unit of area.

4. This is a very broad generalization. The problem does not take the same form in all the countries of the region. There are countries or areas which were settled recently — during the second half of the nineteenth century — and in which the proportion of the active population in agriculture is relatively low, since the number of their inhabitants who went to work on the land was determined by the latter's productive capacity; while in other cases lands impoverished by centuries of cultivation are subjected to the ever-increasing pressure of a population which is multiplying at an exceptionally rapid rate. Thus the demographic factor so greatly complicates the problem of the inequalities in land tenure as to make it very difficult to solve in some cases.

Modern agricultural techniques and development

5. The *rate* and *pattern* of economic development strongly influence the use of the land. Its rate helps to determine domestic demand for agricultural commodities and the speed at which the population surplus is absorbed. Its pattern affects the incentives to agricultural production. And both factors set a limit to the introduction of modern farm techniques and to the expansion of production.

6. There are some branches of agricultural production in which demand has grown rapidly and has given the consequent impetus to technical progress. This has been true mainly of production for export and of import substitution activities. The farmer has surmounted the obstacles created by the land tenure system or has sought new land which he has worked on a basis of advanced and capital-intensive techniques. But in the remainder of the agricultural sector, which comprises most of the rural population, the situation has not been the same. Demand has grown more slowly here than the demand for other goods and services; and it has not been vigorous enough to overcome the difficulties confronting it.

To remedy this, State action to redistribute the land, disseminate techniques and furnish the necessary capital for their application was essential. Such action has not been taken on a scale proportionate to the magnitude of the problem. And even the relatively slow increase in demand referred to has often had to be satisfied by increasing imports or

reducing exports or their rate of growth, with the consequent aggravation of foreign trade disequilibria.

7. Thus, the limit to the introduction of up-to-date techniques is set not only by demand but also by the capacity of the rest of the economy to absorb the rural population surplus.

This same duality is also apparent in the case of technical progress, which tends, on the one hand, to increase the yield per unit of area and, on the other, to reduce the labour force required per unit of product. The logical limit to the advance of technology is set, in the one instance, by demand and, in the other, by the absorption capacity of the economy.

8. As regards the pattern of growth, a reminder must first be given of the unevenness in development policy which has had such adverse effects on agriculture, and which was analysed in chapter I. Production for import substitution purposes has been subsidized, and production for export has not.

In addition to its repercussions on demand, this discriminatory treatment has weakened the incentive to invest in agriculture and thus has retarded technical progress. And in some instances, its consequences have been combined with the depressive effects of overvaluation of the currency and price controls.

From another point of view, agriculture has also suffered when substitution policy — with or without due regard to economic expediency — has been brought to bear on production inputs, thus making costs heavier. It has been possible, by raising prices, to transfer this increase in the costs burden to the domestic consumer, but not to the external market, except when devaluation has afforded a temporary palliative for the maladjustment in question.

Redistribution of the land and surplus labour force

9. Redistribution of the land pursues the following two basic objectives: (a) to relieve social tensions by improving the distribution of property and income; and (b) to increase productivity by creating conditions favourable to the introduction of modern techniques.

Carried out on rational lines, redistribution alone may result in an improvement in productivity, since giving more land to those who have little by making use of land left idle or badly farmed offers immediate opportunities for an expansion of production. From this standpoint, it would seem essential to consider the position with respect to those latifundia which are efficiently operated. However well the land is worked, there is a dimensional limit beyond which productivity, instead of increasing, is liable to decrease. Within this limit, there would be no reason to divide up the land, since other efficacious means exist of redistributing the income it produces.

But this applies only to a few large estates, and these as a general rule are not common in agriculture for domestic consumption, where the prevalent type of farm is characterized by highly unsatisfactory techniques and waste of productive land.

10. It is here that the problem of technical improvements and population arises. The greater the extent to which modern techniques are introduced, the larger will be the population surplus that must be transferred from the land to other activities; and the bigger will be the share of land assigned by redistribution to each active person remaining in the agricultural sector. In the case of countries which, historically speaking, have only recently been settled, the problem is relatively simple, and within a few years the surplus in question may be productively absorbed by the economy if the rate of economic development is improved.

But the same is true of only a small proportion of Latin America's agricultural population. As regards the remainder, the existing surplus is striking in its proportions, despite the low prevailing level of technology. Technical progress would of course greatly reduce manpower requirements, even if production were to expand at a rapid rate.

This raises the most serious aspect of the whole question of redistribution. The active population at present redundant — and this is all the more true of that which technical progress would create — can only be employed very slowly and gradually in the manpower-absorbing activities, for the reasons which will be set forth in chapter IV. This applies to most of the Latin American countries, even if a highly satisfactory rate of economic development were successfully attained.

The foregoing assertion is valid from the standpoint of the economy as a whole; for as far as individual farms are concerned it may well happen, and often does, that the capital used to curtail manpower requirements generates a notable increase in profits. The situation described is yet another manifestation of the discrepancy between advanced technology and the lack of resources for its assimilation.

Thus everything goes to show that when the land is redistributed a larger number of workers will have to be left in agriculture than might be needed at more advanced stages of economic development. But due allowance will have to be made for the stages in question, through the farsighted incorporation of elements of flexibility in the programme.

11. This is a problem which agriculture cannot solve by itself. Capital is required in order to economize on labour in agriculture as in other activities; and it is also needed if that labour is to be absorbed without lowering the current productivity levels of the activities absorbing it. If sufficient capital for this latter purpose is lacking, it will have been worse than useless to expend capital on saving labour which is to be left without employment or at best employed unsatisfactorily. This problem is more thoroughly discussed in chapter IV.

In such cases, priority will have to be given, in agricultural research and in the dissemination of sound farm practices, to those techniques which increase the yield per unit of land, although in some cases the two types of technique are closely related.

Nor could this line of action be pursued without taking into account the growth of demand. Otherwise, the benefits deriving from technical progress would be lost to agriculture. It would not matter if this were to happen in the domestic market, provided always that producers retained

a sufficient margin to encourage further investment. But if the transfer were external, a situation unfavourable to development would recur.

In other words, the capital available for economic development and the proportion of the population that will have to remain on the land constitute decisive elements in determining the size of the holdings which will have to be formed by dividing up large estates or combining small ones, with due regard to ecological conditions. And this, of course, sets a limit to the application of labour-saving techniques.

The opening up of new land

12. In some cases new land can be opened up for farming, thus providing an outlet for part of the surplus population. This is generally a costly operation owing to the direct and infrastructural investment required. Whether it can be undertaken therefore depends on the amount of capital available.

In formulating plans for land reform this fact should be borne in mind. The settlement of new land is sometimes advocated in the case of badly-farmed latifundia that could be subdivided at much lower levels of real investment. This more economic solution is not incompatible with the opening up of new land to absorb excess population if the necessary capital is available to achieve this with a higher level of productivity than could be attained by the same factors of production in other branches of the economy.

Another possibility is to employ the surplus population in the rural areas themselves in investments that require a large amount of labour, either because of their nature or because they offer an alternative to other capital-intensive investments. But, except in special circumstances, such rural investment should be undertaken solely within an over-all investment programme and in its due order of priority. Otherwise, some of the meagre savings available might be wasted.

Land reform

13. Because of the different forms that the land problem assumes in the Latin American countries it is impossible to apply general formulae for land reform. For the same reason it is important to select the most suitable methods for each case.

In this connexion, a tax on the potential capacity of land without improvements might be efficacious when the introduction of improved techniques is not accompanied by a substantial labour surplus. In such cases, the tax might lead to the rational use of land or to its transfer to other hands.

But in most cases the tax would not be an adequate instrument of land reform, since it might lead to precisely those forms of technological improvement that would reduce costs by cutting down on labour. Conse-

quently, direct measures of redistribution are needed, without detriment to the eventual application of the tax to promote the more efficient farming of holdings, in accordance with the size of the lots into which the big estates have been split up or the small farms combined.

14. Sound measures for land reform have not produced the desired effect except to a very slight degree, as the subdivision was based on cash payments for the land acquired for this purpose by the State. The problem of land tenure will never be fully disposed of while the land still has to be paid for in this way, since resources will either not be available in sufficient volume or will be diverted from the direct investment and basic social capital investment required by the subdivided land.

Hence, it is essential to institute payments procedures which, while giving the new owners a breathing spell in which to develop their activities, would offer the previous owners the assurance that they would receive a proper price for their land without incurring the risk of monetary instability.

Another obstacle which has emerged in the course of events is the disproportionate price of the land in relation to its productive capacity, for the reasons given above. The tax might also play a useful part in this respect, to be followed by direct measures of land redistribution.

15. Land redistribution is not enough. The results it was expected to produce have been difficult to achieve when the State has merely redistributed the land and subsequently left the new owners to fend for themselves.

Land reform that is not accompanied by adequate technical improvements will fall short of its aims, if it does not end in total failure. For the introduction of modern techniques State action is indispensable, as regards both implementation and financing. Generally speaking, its intervention in both aspects has been deficient in the extreme. The resources allocated in the Latin American countries to agricultural research and extension services are usually small in comparison with those earmarked by the more industrialized countries for the same purposes. And this charge may also be levelled against State financing.

The introduction of up-to-date techniques, the improvement of the farmers' social conditions, and investment in the infrastructure demand substantial resources, apart from those required for the development of other sectors of the economy. This is yet another reason why a programme of land reform and technical improvement should be included within an over-all economic development plan.

CHAPTER IV

HUMAN RESOURCES, TECHNOLOGY AND SOCIAL MOBILITY

Technological penetration and shifts in the labour force

1. The increase in the active population is already showing the effects of the previous increase in population growth, and this fact will be even more noticeable in the years to come. Never before in the history of industrialization has such a phenomenon manifested itself so persistently; this is further evidence of the special nature of the development problems with which Latin America is faced.

The occupational structure of the active population will not be the same in the future as it is now. The changes which have for some time been taking place are bound to become more pronounced and the problem will grow more complex as well as more widespread.

2. Reference has already been made to these changes. As techniques permeate and average productivity and per capita income rise throughout the economy, the composition of demand changes. There is a relative decrease in the demand for agricultural items and primary commodities in general, and also for unskilled personal services, as the cost of such services mounts with the rising value of labour; there is a relative expansion in the demand for industrial products and skilled personal services, where technical progress makes it possible to improve quality and satisfy a greater variety of tastes.

In addition, some artisans move into industry, and the expansion of the market, combined with the growing domestic division of labour, results in a relative increase in employment in trade and transport. Lastly, an increase in the scope and complexity of State intervention is accompanied by an increase in employment in these activities.

Consequently, one of the dynamic tasks of industry, trade, transport and skilled services, and of the State, must be to absorb the active population displaced from primary production, unskilled services and artisan activities.

The relatively large scale of these shifts is due partly to the increase in productivity in all occupations and partly to the rapid expansion in the demand for goods and services.

Labour-economizing and labour-absorbing investments

3. Productivity naturally depends on the spread of technology by means of an increase in capital per worker and the capacity to handle and organize it. As explained elsewhere, in the more advanced countries technology is directed more and more towards economizing manpower; and this is the same technology which is available to countries in the course of development.

This causes very serious dislocations in Latin America, since absorbing a rapidly expanding labour force means assimilating a technology which in fact tends to economize manpower. Thus capital requirements greatly exceed the possibilities of capital accumulation in those countries.

The more productivity rises because of the saving in manpower resulting from the increase in investment per worker, the more pressing becomes the need for capital accumulation, both in order to give productive employment to the manpower thus saved and to provide employment for the continuous stream of those entering on productive activity.

In other words, the progressive adoption of the technology of the large countries, because it economizes manpower, also necessitates a faster rate of economic growth. If this rate is low, the maladjustments resulting from shifts in the labour force will be greater. People will be shifted from occupations that are turning away workers before the occupations that can be expected to absorb manpower are in a position to do so. This leads to a congestion or a surplus of unemployed or under-employed manpower which, in addition to representing a waste of factors of production, may understandably lead to social tensions.

4. However, it should be remembered that, if the rate of growth is slow, so is the assimilation of types of technology that economize manpower. This is a fact, though there is one important qualification to be made: even when the increase in investment is barely sufficient to meet the requirements of the growth in the labour force (without any increment in the average investment per worker), these maladjustments are likely to occur. The mere natural growth of capital and regular capital replacement do not leave conditions the same in the past, since more advanced types of machinery and equipment are adopted, with a consequent saving in manpower. This is intensified by the progressive training of the labour force. Thus, even when capital grows at the same rate as the labour force, part of the latter will be excluded from labour-absorbing activities.

Capital accumulation must have a much higher growth rate than the labour force if labour-absorbing activities are to play their full part in providing productive employment for all the overflow of extra manpower from the activities that are turning away labour.

Redundant manpower

5. The phenomenon of redundant manpower is not always apparent from unemployment figures. The surplus labour stays on in agriculture,

sharing work that could be done by fewer people for the same investment, or else migrates to the towns to offer unskilled and very poorly paid services.

The State is also affected by this pressure from the labour force that cannot be productively absorbed because capital is lacking. If, in an attempt to relieve the pressure, the Government creates employment that is not required by the expansion and improvement of the public services, capital accumulation is weakened through the greater proportion of private income that, through either taxation or inflation, is used to pay for the rise in government expenditure.

All this constitutes a problem that has not been properly clarified in Latin America; nor has due consideration been given to the tools needed to solve it. However, it is realized that no solution can be expected from the mere operation of private enterprise; this was possible during the evolution of capitalism in the more advanced countries because capital accumulation went hand in hand with technological development. The entrepreneur tends to use forms of capital which increase his returns by economizing manpower, but the effect of this on the economy as a whole is not his concern.

Balancing the two types of investment

6. Actually, to obviate these maladjustments deriving from shifts of the active population, what is needed is a suitable combination of capital investment leading to a saving in manpower, and the investment required to absorb both this manpower and its growth. The ratio between these two forms of investment is not arbitrary; it depends on the country's possibilities of development and the amount of capital available. However, there is a ratio of balance, and if investment that economizes in manpower exceeds its due proportion, the phenomenon of surplus manpower referred to above will occur.

If there is not enough capital to avoid this surplus, the development policy — and development planning — will have to cover matters that are now usually left to the free play of economic forces. In this case, it should be considered whether it will benefit the economy as a whole to invest considerable funds in replacing capital goods that still operate satisfactorily, merely because there are others available that are more productive in view of the saving in manpower involved; and also whether, in the case of new investments, those selected should be of the type that also result in a saving in manpower when the country does not have sufficient capital to absorb it elsewhere.

One of the main problems facing development policy is to find feasible solutions so as to avoid such waste of capital, and at the same time to devise suitable means of striking a balance between the two types of investment, either through the tax system or credit policy, or by other measures.

The dynamic elements

7. A low level of capital accumulation and a slow growth rate produce not only stresses of the kind just described, but also equally, if not more, important effects on social mobility and the emergence of dynamic elements.

Each generation has its dynamic elements, which usually place their distinctive stamp upon it, i.e. individuals who are destined to play a decisive part in economics, technology, scientific and cultural matters, politics and trade unionism. In economics and technology, their task will be to organize and direct enterprises, initiate action and assume risks and responsibilities. It is towards these persons that the drive for technological levelling-up, referred to elsewhere, should be directed.

Such individuals constitute dynamic elements not only because of their special gifts, but also because of their active role in promoting social mobility. A high rate of economic growth hastens this process, which in turn influences the growth rate. Hence strategic importance of these dynamic elements. An annual growth of per capita income of only 1 per cent, as is now the case, or of 3 per cent, means not only that the standard of living will be doubled within 70 years, or within less than 25; it also means something else of vital importance, namely that the higher of these two rates will permit the rapid absorption into economic activity of these dynamic elements, broadening their horizons, whereas a moderate rate means the waste of a great part of these forces and mounting tensions which, if they fail to find an adequate outlet in economic activity, will eventually discover some way of bursting out of the economic and social bonds that contain them.

Technical training

8. In addition to capital accumulation, a great drive is required to provide technical training for the broad masses, beginning at the primary education stage. The inadequacy of primary education in many Latin American countries is a clear proof that strong traces of the old social order still linger on in many places.

In earlier days, technological penetration was confined to export or auxiliary activities. There were no powerful economic motives to support the desire for better education, let alone technical training, since artisan activities and traditional forms of land tenure were the order of the day.

This problem is now receiving full recognition as is also the need to enforce the principle of equal access to technical training without, of course, neglecting cultural considerations. In practice no such equality exists, partly because of the obvious inadequacy of the funds devoted to public education, and partly because the few educational opportunities that exist are inaccessible to the working masses. This applies not just to higher technical education, but also to intermediate and even primary education, as witness the high rate of wastage in the schools.

Hence there is a tremendous waste of vital energies, partly due to the low average income of the population, which in turn contributes to keeping this income at a low level. Even so, there is no doubt that expenditure on education could be considerably increased, either by measures limiting military expenditure, as has been proposed, or by heavier taxation. There is also no doubt that subsidizing the education of the most gifted, a group which would include the dynamic forces referred to, would be one of the most economically profitable and socially significant investments that could be made.

9. There is also increasing recognition of the gap separating technical education and the requirements of economic development. The instruction given is often unrelated to the real needs of economic activity. Hence it is hardly surprising that there has been no general concern with the scope and emphasis of technical training in relation to the need to absorb the future increase in the active population. Since the occupational structure will not be what it is now, it is essential to make immediate changes in the nature and scope of technical education in the light of the foreseeable requirements for the coming years. This is one of the most important aspects of the planning task referred to in another chapter.

CHAPTER V

INFLATION¹

1. ITS DYNAMIC EFFECTS AND SOCIAL TENSIONS

1. The economic development of the Latin American countries is impeded by a number of structural obstacles which were briefly reviewed in preceding chapters. Foremost among them is the relatively slow rate at which exports are growing and their fluctuations. If income is to increase more rapidly and thus counteract the effect of that movement, constant changes must be made in the composition of imports and exports and in the structure of production. In the absence of an adequate policy to meet these development requirements, inflation deriving from credit conditions is apt to produce such structural changes through monetary devaluation with disturbing consequences, and it also increases investment to the extent that it forcibly expands savings.

But when inflation has dynamic effects of this kind, they are directly traceable to its regressive influence on income distribution and the consequent drop in consumption by the broad masses of the population. As the masses try to remedy its regressive effects through their political or trade union power, the inflationary spiral is unleashed; and however successfully they achieve their aim, thereby lessening the dynamic effects of inflation, the spiral produces increasingly acute social tensions, as well as the economic maladjustments that are an intrinsic part of inflation.

Furthermore, economic development is faced with other structural obstacles which are reflected in rising costs. The inflationary repercussions of cost increases often combine with those of credit inflation to give a fresh impetus to the spiral. The outcome is the same when costs increase as a result of certain types of social policy which, by not taking proper measures to attain the desired objectives, or by exaggerating such objectives, soon cause the advantages secured for the masses to be lost in the

¹ This chapter summarizes the ideas contained in the article: "Economic development or monetary stability: the false dilemma", *Economic Bulletin for Latin America*, vol. VI, No. 1, Santiago, Chile, March 1961, pp. 1 *et seq.*

inflationary spiral. Thus, inflation is not an effective and durable instrument by which to achieve economic development, still less the progressive redistribution of income.

2. The dynamic effects of inflation are reflected in demand and investment. Their characteristics should be briefly recapitulated here. The expansion in demand produced by inflationary investment tends to offset the decline in over-all income when exports drop and to accelerate the increase in over-all income when they rise, through more efficient utilization of existing production capacity and, in both cases, an expansion of that capacity when the imports required by over-all income exceed the limit imposed by exports, and external disequilibrium and monetary devaluation follow.

Devaluation tends to rectify this disequilibrium and to allow for overstepping of the limit, since it produces exactly those changes in the structure of production and the composition of imports and exports that are required for development purposes. It thus tends to lower the import coefficient sufficiently to enable the rate of growth of income to exceed that of exports.²

But other forces exist that tend to raise the coefficient. For instance, the rise in internal prices that precedes or accompanies devaluation has the same regressive effects on income distribution followed by changes in demand. The groups benefited usually increase their external purchasing power, thereby offsetting the favourable effect of devaluation on the coefficient of imports, and proportionately weakening the dynamic influence of inflationary demand. This explains the cases of under-utilization of productive capacity that are to be found when there is internal inflation.

The upward trend of the import coefficient may, of course, be checked by direct measures that divert demand towards internal activities, and thereby prevent any mitigation of the dynamic effects of inflationary demand. But such measures give still greater stimulus to the investment that meets the demand of the higher income groups.

3. Thus, the regressive effects of inflation lead to an expansion in investment, but consumption by the groups benefited often increases to a far greater degree, at the expense of consumption in the lower income groups. Thus the social cost of this increase in investment is high. Furthermore, part of the investment goes to satisfy the higher demand of the groups favoured by inflation.

As a result, any increase in the growth rate of average per capita income brought about by inflation does not lead to an equal improvement in the level of living of the masses, because of the way in which income is redistributed. However, it may be that in some cases the growth of

² Two degrees of devaluation should be distinguished, as explained in the article cited in footnote 1: that which corrects monetary over-valuation and the ensuing external imbalance, and the additional devaluation required for structural changes. The first is inevitable. The second is not a satisfactory alternative to direct measures of structural change. Apart from the fact that it involves a disruptive shift in the whole price and cost system, its influence is only transitory, since the more or less gradual adjustment in wages and salaries entails further devaluation or direct measures of structural change.

average income among the broad masses of the population in Latin America has been more vigorous than that induced by a policy of monetary stability alone. But this does not mean that inflation is recommended as an alternative to stability. Stability is not incompatible with development. What must be done is to combine it with a development policy which, in a non-inflationary way, would secure at least the same rate of growth without encouraging consumption in the higher income groups, or rather, would secure a higher rate by expanding capital investment at the expense of unduly high consumption, with the timely assistance of contributions from international sources.

4. There are countries in which the large proportion of the active population engaged in primary production, artisan industry and unskilled services maintains a constant pressure on wages and weakens the endeavours of the trade unions to combat the regressive effects of inflation. In such cases, the capital-forming effects of inflation may persist, even though the lines along which this capital formation is channelled run counter to the social aims of economic development. When, however, conditions are propitious for the strengthening of trade union power, or the masses exercise their political power in defence of their real wages, the capital-forming effects of inflation diminish or disappear. Some Latin American countries have already reached this stage and others are nearing it. Inflation then moves in a vicious circle, with the upswing of the spiral as wage adjustments are made to compensate for the rise in prices, followed by a new rise in prices under the impulse of the wage adjustments.

5. Let us now examine the structural obstacles to development. The first of these is the inflexibility of imports resulting from the slow growth of exports and the shortcomings — referred to elsewhere — of the industrialization process.

The cyclical decline in exports leads to external disequilibrium, because income growth requires imports which cannot be paid for out of exports. In the face of disequilibrium of this kind, immediate practical reasons call for reduced imports of finished consumer goods or their substitution and for continued or increased imports of raw materials and intermediate and capital goods. So long as there is a reducible margin of such goods, the problem is relatively simple. But as the margin begins to disappear, increasing difficulties will be encountered. There are countries in which the reducible margin is almost non-existent and any decline in exports will slow down or halt the rate of growth or even bring about a contraction in internal activity until such time as new types of import substitution or additional exports can be developed. Import substitution of this kind is usually more complex than for consumer goods, and some items require a considerable length of time for development. As to social dynamics, constant pressure for increases in wages is usually exerted. An increase in average per capita income through greater productivity will make it possible to meet this pressure by non-inflationary means. But if per capita income ceases to increase or even declines — and this is the situation under consideration — the pressure for wage increases may become frankly inflationary.

6. The goods resulting from import substitution are usually produced at higher cost than the imported article. Their production does, however, bring about an increase in per capita income in the labour force that is attracted to industry. The price rise that will result from import substitution will however, have unfavourable repercussions on those already employed in industry and on those remaining in occupations from which labour is becoming redundant. If the substitution process is gradual, the effect can be absorbed by increased productivity in the occupations concerned. Substitution usually occurs, however, during critical periods and at a rate exceeding the increase in productivity. It is therefore understandable that the affected groups should seek to protect their level of real income by claiming higher wages; and the increase if granted, gives fresh impetus to the inflationary spiral or can even set it in motion, if it is substantial enough.

If the substitution process comes about gradually and smoothly, cost increases may be absorbed by increases in the productivity of the affected groups. As, however, substitution occurs mainly when exports fall and after a period of relatively easy import conditions, its effects are usually concentrated in a short space of time and tend to be greater than any increases in productivity.

7. The spiral will gather further impetus if there is a relative increase in agricultural prices. Such an increase will be caused mainly by the fact that the land tenure system and the deficiencies of State action in technical and economic matters militate against improvements in agricultural productivity. The increase in demand caused by population growth and the substitution of agricultural imports will thus result in higher prices. The same effect is produced by a rise in the cost of inputs in the agricultural sector which had earlier been imported and were later produced internally.

8. Not all the cost increases which give impetus to the spiral are of structural origin. There are cost increases of other kinds, the main increase being seen in the method and scope of payment for social services : if contributions are not absorbed by increased productivity or earnings by entrepreneurs, they are bound to affect prices. In this way, the pattern of consumption of the mass of the population will undergo a change : their ordinary consumption will decline and their social consumption will increase, although not to the same extent, for a part of the differences will be absorbed by administration costs which are usually high. In addition, social benefits are generally distributed, not in relation to the needs of the various population groups, but in relation to their greater or lesser bargaining power.

9. Attempts are frequently made to attenuate the regressive effects of inflation by measures that suppress its consequences but aggravate existing structural maladjustment and create new ones. Thus, overvaluation of a currency will encourage imports and discourage exports; the fixing of arbitrary prices, particularly in so far as public service enterprises are concerned, will deprive such enterprises of the resources and incentives required to expand their productive capacity.

2. ANTI-INFLATIONARY POLICY AND DEVELOPMENT

10. The social tensions created by inflation and the weakening of its dynamic effects have made it essential to find means for combating it in some Latin American countries. In certain cases, anti-inflationary policy has brought with it a decline in the rate of development and in others has meant stagnation or even contraction of the economy.

These consequences are not necessarily inherent in an anti-inflationary policy; they are the result of the kind of measures adopted and failure to combine them to an adequate degree with other measures. Let us examine this question.

Inflation cannot be combated unless inflationary investments (or inflationary consumer expenditure) are eliminated. This has to be done gradually however, and must be accompanied by the development of investments for which there are genuine resources. Accordingly, the remedy is not to reduce the volume of investment — which is not excessive in any Latin American country — but to finance investment in a non-inflationary way and at the same time to alter its pattern so as to bring it more closely into line with the needs of economic development.

There are only two ways of ensuring that investments are backed by genuine resources: by increasing internal savings, particularly through tax measures designed either to stimulate savings and investment among the wealthier classes or to absorb a part of their resources for investment by the State, and by resorting to international assistance as an additional source of funds.

Such measures have usually been absent or inadequate in respect of anti-inflationary policy. Insufficient effort has been made to impose taxes and international assistance has usually been deferred to a second stage when it was possible to check the positive effects of the policy. These positive effects, however, depended specifically on international assistance being made available at once rather than later.

The result therefore has been a reduction in the volume of investment with the effects that might be expected on internal activity. Once the effects have occurred, it is much more difficult, if not virtually impossible, to adopt the tax measures which were needed earlier when conditions were more favourable.

11. It is true that the adverse effects on income of a reduction of investment have frequently made it possible to restore external equilibrium and even to accumulate surpluses. The problem, however, is not that of redressing the balance at the expense of growth but of pursuing and expediting development. This can only be achieved by investments which will allow for changes in the structure of the economy calculated to bring about import substitution and diversify and increase exports. Reducing investment with a view to achieving stability and equilibrium has usually prevented the required structural changes from occurring at the proper time and this has unnecessarily retarded economic recovery.

Even when steps are taken to bring about structural changes at the

proper time, however, an interval must necessarily elapse before dynamic equilibrium is restored. In the meantime, the only way to avoid internal contraction in the event of external disequilibrium coupled with the disappearance or inadequacy of the reducible margin of imports, is to obtain sufficient international assistance to cover not only the portion of the investments represented by imports of capital goods but also the domestic portion.

12. Although the purpose of all these measures is to obviate the adverse effects of credit restriction on inflationary investment, they are only sufficient to contain the price rises which such investments provoke. Action must also be taken to control wages, which are the other factor in the spiral. This is one of the most delicate and complicated aspects of anti-inflationary policy, particularly if it should happen that large-scale readjustments were made periodically. The problem is to establish the wage level so as to absorb part of the profits of undertakings or the immediate increases in productivity and to leave reasonable percentage for continued non-inflationary capital investment. The difficulties which this problem involves will increase if resort is had to corrective monetary devaluation and arbitrary price fixing is abolished.

13. The only way to cope with these difficulties is to see that the immediate consequences of anti-inflationary policy are shared by all social groups alike. In the experiments that have been carried out so far, this condition has seldom been fulfilled. The stabilization of wages has not been accompanied by measures to restrict the distribution of profits or by a satisfactory tax policy. And, in consequence, a wide flank has been laid open to criticism from the social standpoint.

14. In any event, such wage control measures cannot be applied for any length of time in face of the pressure for social improvement. Anti-inflationary policy can only be the starting-point for a development policy aimed at expediting the rate of economic growth.

Inflation may be checked by means of a combination of appropriate measures, but its recurrence will be very difficult to prevent unless a vigorous economic development policy is pursued. The savings shortage, the lack of internal measures to encourage saving and promote investment, and the inadequacy of the contribution represented by international resources, will continue to operate as active elements of inflationary credit expansion, which will also be resorted to as a means of offsetting the cyclical contraction of income when exports decline. All this calls for structural changes, which are likewise indispensable in order to prevent — or at least limit — those cost increments which produce inflationary effects. As the nature of these changes has been described in other chapters of the present study, all that need be dealt with here is the question of reforms aimed at strengthening the structure of the economy so as to reduce its vulnerability to external fluctuations, a point which was merely touched upon in chapter III because the appropriate place to discuss it is here.

3. THE EXTERNAL VULNERABILITY OF THE ECONOMY AND INFLATION

15. First and foremost it must be recalled that, if income is to increase beyond the limit set by traditional exports, import substitution must take place, with the attendant changes in the structure of production, in so far as new export lines cannot be developed.

If the expansion of exports were a regular process, import substitution would have to be effected steadily and persistently to allow the economy to develop. But this is not the case. The growth of exports is cyclical; during the rising phase of the cycle, income may increase at a relatively rapid rate without the need for import substitution, which becomes essential when exports decline and are insufficient to finance the imports necessitated by the income level that has been attained. The substitution process, however, takes time — sometimes a long time — and if the reducible margin of imports is exhausted, a diminution of income will be inevitable if no resources are available with which to cover the external disequilibrium.

Import substitution must be undertaken with due foresight before the situation has become critical. Its scope must be such that maximum internal economic activity can be maintained when exports sink to their lowest point, without the creation of external disequilibrium. If a disequilibrium is registered, the reason is that this lowest point in the level of exports is insufficient to finance the imports required for maximum economic activity. And in so far as it is impossible to expand the exports in question, the only way to achieve the desired end is to reduce the import coefficient by means of substitution.

16. If the substitution policy pursued is far-sighted enough, there is no reason why the cyclical growth of exports should affect internal activity. True, this growth will be accompanied by an increase in demand, but as internal activity is developing at its maximum level, the additional demand will immediately be deflected towards external markets, with the consequent expansion of imports.

From this point of view, exports could be divided into two parts — one fluctuating, and reflected, as has just been explained, in a similarly fluctuating demand for imports, and another whose growth is regular. It is the rate at which this growth takes place, in relation to the rate at which income rises, that will determine the scope of the substitution process.

The process in question will have to be carried out in such a way as to enable that part of exports whose growth is regular to cover at least those imports which are essential to the similarly regular growth of economic activity, i.e., imported raw materials, intermediate products and capital goods. This does not mean that non-essential current or durable consumer goods will not be regularly imported. This might be advisable for reasons of economic expediency such as have already been set forth in chapter III, care being taken to avoid a repetition of former errors. What is more, regular imports of these non-essential goods constitute a second reducible margin of which advantage could be taken if the cyclical export minimum dropped lower than had been anticipated.

Incidentally, if substitution policy has been based on the criterion of economic expediency, and has been implemented to the necessary extent, there is no reason whatever why non-essential or luxury goods should not be imported rather than produced domestically. If the aim is to restrict this type of consumption, recourse must be had to taxation on domestic production and imports alike.

17. As regards the fluctuating part of exports, it was stated above that, when internal activity reaches its peak, there will be a tendency for the demand generated by the cyclical growth of exports to be deflected abroad. If customs protection does no more than cover the difference in costs between domestic and foreign production, the increase in demand will easily outweigh the protectionist duty and will be diverted towards external markets. But if an excessive degree of protection is afforded, this ready safety-valve will not exist, and domestic production will be liable to expand in order to cope with the cyclical growth of demand. Were this to happen, an element of instability would once again be introduced into the internal economy, for when the fluctuating part of exports subsequently declined, demand for the goods concerned would contract. Furthermore, there would be a risk that substitution activities, when channelled in such directions, might not concentrate sufficiently on those other goods which are essential, with the result that external vulnerability could not be remedied.

18. In any case, a flexible import policy would be required, priority being given to the use of the tax instrument, not only in order alternately to increase and decrease import duties — according to the phases of the cycle — but also for the cyclical mobilization of investment resources.

This point calls for a little explanation. In the Latin American countries, the State effects a substantial proportion of investment, using tax revenue, as well as other resources. But in doing so, it has not usually taken account of anti-cyclical considerations. There would be two ways of employing the tax instrument for investment purposes within an anti-cyclical policy supplementary to the structural reforms suggested here. One possibility would be direct taxation on the cyclical increase in exports and the allocation of the resources thus obtained to imports of capital goods, either for the Government's own investments or, through official development agencies, for private enterprise. By this means, some proportion of the increment in demand would be appropriated and prevented from exerting pressure on internal activity, which, in turn, would not be affected when that part of the increment disappeared during the downward phase of the cycle. The second way would be to apply taxation not to exports but to the income accruing from internal activity; the part thus appropriated would also be used for capital goods imports, leaving a gap in internal demand which would be bridged with part of the growth of demand in the export sector. When exports entered upon their downward phase, the State would cease to import capital goods and would use the resources in question internally, this time to fill the gap which would be left by the export sector's demand. One of the most efficacious methods of doing this would be through internal investment designed to absorb cyclical unemployment in the export sector.

There are other supplementary anti-cyclical measures which could be adopted to render this policy more efficacious; but the foregoing general ideas will afford an understanding of what is proposed here and a starting-point for discussion of the problem.

19. It is superfluous to stress the importance of this point. The vulnerable structure of the Latin American economy makes it very difficult — if not impossible — to combat inflation when credit expansion becomes essential in order to offset economic contraction. The solution is outside the sphere of monetary policy, since it is of a structural nature, as shown above. And only if the structure of the economy is strengthened will it be possible to apply a sound monetary policy which will make monetary stability fully compatible with economic development.

CHAPTER VI

ECONOMIC FORCES AND DEVELOPMENT PLANNING

1. THE FREE PLAY OF ECONOMIC FORCES

The adverse effects of the uneven penetration of production techniques

1. Throughout this study, reference has constantly been made to the need for conscious and deliberate action to influence the forces of the economy in such a way as to ensure the attainment of certain economic and social aims. The free and unrestricted play of economic forces has adverse effects on economic and social development.

Care must, however, be taken not to draw erroneous conclusions from this thesis. The idea is not to stifle these natural forces — which have an enormous dynamic potential — but to establish, through State action, the conditions essential to their utilization for economic development.

In the foregoing chapters, a study has been made of what the adverse effects on development are. It would be as well to summarize them here in order to help clarify the theory of these phenomena, for without such clarification no effective influence can be brought to bear on the forces of the economy.

The free play of these forces has failed to bring about well-balanced technical penetration into all productive activities in the peripheral countries. Technical development has not flowed freely through the economic system as through a series of communicating vessels. Modern productive techniques have usually penetrated only where there were natural resources superior to those of the more advanced countries, as the purpose in such cases was to develop primary commodity exports and auxiliary activities of interest to the advanced countries. But the free play of economic forces has not spontaneously led to a process of industrialization in the peripheral countries nor to the introduction of modern techniques in internal activities which remained outside the orbit of international trade.

Bogus types of integration have thus developed between the centres and the peripheral countries, very different in nature from the types

of integration that have emerged among the industrial centres themselves in respect of trade in industrial goods. This has had a number of results which are important economically at both the international and the national level. At the international level, free and unrestricted competition has three types of effect.

2. First and foremost, the low level of productivity in internal activities, due to the fact that technological penetration has been slight and the consequent low wage levels prevailing in these sectors and extending to export activities, means that the increase in productivity in the latter tends to be transferred abroad. This phenomenon will manifest itself in the deterioration of relative wages as between the developing and the more advanced countries and in worsening terms of trade, unless the limitation of national resources checks this price trend by increasing the return from the land or unless the free play of forces enters the picture to oppose the trend.

3. From another standpoint, the difference in wage rates vis-à-vis the more advanced countries is not usually sufficient to outweigh differences in industrial productivity, hence the need to protect industry. It is possible to imagine spontaneous industrialization resulting from the free play of economic forces, so long as wages fall low enough to counterbalance differences in productivity; but this would be tantamount to aggravating the tendency towards a deterioration in the terms of trade and wages when the forces of the economy operate without restraint.

4. Lastly, the unilateral penetration of techniques into export activities has made the economy very vulnerable, and the longer the period between the beginning of primary production operations and the consumption of the final product in the rest of the world, the greater will be this vulnerability. Industrialization inwards at the expense of export possibilities, far from correcting this vulnerability to external fluctuations, may aggravate it greatly to the detriment of the use of productive resources.

Imbalance between technology and capital

5. The uneven penetration of modern technology has meant that it has failed to reach a considerable proportion of the active population. The problem of economic development consists essentially in creating suitable conditions for modern technology to be assimilated expeditiously. There are a number of obstacles in the way of this, among them the scarcity of capital in the face of advanced forms of technology which require enormous capital outlay. Given the impossibility of reverting to outdated patterns, the problem arises of distributing the scarce capital available so as to extract the maximum yield for the economy. The free play of economic forces does not provide an adequate solution to the problem, for the profit incentive frequently encourages capital investment and reinvestment which reduces costs at the expense of employment

without there being enough capital to remedy unemployment and maintain comparable productivity.

Given the discrepancy between capital requirements and the scarcity of available capital, the free play of economic forces does not ensure an adequate relationship between labour-saving investment and labour-absorbing investment. Hence there is capital wastage which has adverse effects on economic development.

Imbalance between national and foreign enterprise

6. The adverse effects of the free play of economic forces are not confined to things but extend also to people at the level of private enterprise. Foreign private enterprise clearly has technical and economic superiority over its national counterpart. The free play of economic forces will tend to give the former an advantage over the latter to the detriment of the efficient use of the human resources of the country concerned, not to speak of the tensions and antagonisms to which it gives rise.

All this leads to an important conclusion. The free play of economic forces functions correctly only when confined to one and the same level, both in technology and in the capital formation capacity required to apply the technology in practice.

If free competition is not confined to one and the same technical and economic level, the adverse effects on development are bound to make themselves felt, no matter whether the imbalance is between export activities and internal activities, between available technology and capital formation capacity, or between national private enterprise and foreign private enterprise.

Towards the attainment of international balance

7. Reflexion will, however, show that such internal imbalances are the result of international imbalances. The uneven penetration of production technology is an expression of this. In the developing countries, advanced techniques taken over from the large industrial centres exist side by side with pre-capitalist patterns. Until such time as these advanced techniques extend to the whole of the economy, the imbalances will produce effects unfavourable to economic development.

Although technology continues to improve steadily in the more advanced countries, it is conceivable that the less developed countries will in time manage to catch up, provided that a vigorous and enlightened development policy is pursued. The free play of economic forces may then have the same significance and the same effects in both groups of countries. It must not, however, be forgotten that in the more industrialized countries and under the private enterprise system, the free play of econo-

mic forces is no longer what it was in the period when capitalism was developing and will probably not continue to operate in the way it does today, for the most advanced countries also clearly intend to influence it consciously and deliberately, although in different ways from that which circumstances would counsel the developing countries to adopt.

8. Only by such deliberate action have the more advanced countries been able to achieve the progressive redistribution of income, for only a very small part of it was attributable to economic development itself. And only in this way will it be possible increasingly to attenuate the periodic fluctuations in the economy. Similarly, deliberate action is required to check and perhaps correct — at least in part — the phenomenal concentration of urban population which in those countries, as in Latin America, is an obvious outcome of the unrestrained play of economic forces.

A theory about transition

9. New phenomena need new interpretations and new ideas for practical action. The economic and social phenomena of the countries which are seeking to assimilate modern technique are very different from those characterizing the past and present development of the more advanced countries. As was said in the early part of this study, the phenomena are those associated with the transition from lower to higher stages of technique — a transition which will take a long time. Once this process is complete, the economy of Latin America may well display features similar to those of the more advanced countries. Latin American phenomena may then be interpreted in the light of common principles. But they cannot possibly be the same as those of to-day, because the more advanced countries will have become increasingly adept at mastering the economic forces, as has just been suggested.

This work of theoretical interpretation is already being carried out and must be pursued without delay if development policy is to be properly guided. It is not a matter of formulating a theory in isolation, separate from the over-all dynamic theory, but rather of making it include a valid explanation of the phenomena of transition.

Clearly, this is not an exclusive preserve of Latin American economists, for the phenomena of economic and social development, which are to be observed in different areas of the world to-day are very similar everywhere despite individual peculiarities and the effort to interpret them is proceeding very energetically in Latin America as it is in the advanced countries.

All this, combined with economic planning, opens up vast fields of creative activity, and it is to be hoped that the international agencies will be able to continue to play a more and more effective part in helping Governments to carry out economic development activities.

2. THE NEED FOR PLANNING AND FOR QUANTIFYING TARGETS AND RESOURCES

A plan to act on the economic forces

10. A development plan is a well co-ordinated group of forces whose aim is to expedite growth, or maintain it at the same rate if this is already high, to make it as steady as possible and to improve the distribution of income.

Thus planning means recognizing that the free play of economic forces does not solve development problems effectively. But it is not the only way of acting on such forces; it is possible to envisage a variety of measures for stimulating development and eliminating obstacles in its path without the quantification of targets and resources that a plan involves. In fact investment can be encouraged by discouraging consumption, attracting foreign private capital, obtaining plentiful international resources for certain specific projects, and making a number of structural changes. Such measures could even be taken as a co-ordinated whole. Would it be essential in such a case to quantify targets and resources?

The reply to this question depends on two fundamental considerations: on the one hand, the limited nature of the resources and, on the other, the time required for these structural changes and the accompanying capital investment.

The limit to resources

11. The limited nature of the resources raises a series of problems that need to be quantitatively analysed before they can be effectively dealt with :

- (a) Distribution of resources between consumption and investment;
- (b) Relationship between productive and social investment;
- (c) Balance between labour-economizing and labour-absorbing investment;
- (d) Distribution of State expenditure;
- (e) Contribution of international resources.

(a) Distribution of resources between consumption and investment

The starting point of a plan will be to raise the coefficient of investment. This would appear to be essential even when the rate of growth is satisfactory, in order to maintain that rate. The need is even greater in other cases — namely, the majority — where the rate is far from satisfactory.

This leads to the first major problem, which is how to reconcile the

aim of a rapid rise in the level of mass consumption with the aim of increasing the coefficient of investment. In other words, how far should present consumption, or an immediate increase in it, be sacrificed in order to obtain a much greater increase in future consumption ?

This question, which can be answered properly only if the data concerned are quantified, is of major significance, and will be even more significant in the future if, as is hoped, the share of the broad masses in income distribution improves steadily. It may be that measures taken to encourage savings in this group, as in the higher-income groups, will not automatically lead to the desired results. The State must then intervene in order to obtain the necessary additional savings, either by compulsory savings measures or by taxation; or its intervention might take the form of increased government participation in capital investment.

Thus the State obtains, by means of taxation, funds that may be devoted to government expenditure, and not necessarily to capital formation. Hence, a proper proportion between what is devoted to these two purposes is called for, because otherwise the Government would be exerting an unfavourable influence on the coefficient of investment and consequently frustrating the primary objective.

(b) The relationship between productive and social investment

Investment may be divided into two main categories: (i) that which contributes to increasing productivity; and (ii) that which is merely reflected in improved welfare and has only an indirect and limited relationship to the productivity of the labour force. The first type includes investment in machinery and equipment, technological research and technical training; and the second, investment in housing, sports grounds, etc. The second type, which may be called social investment, is as essential as the first, but its volume cannot exceed a certain proportion without seriously jeopardizing the growth of per capita income, which can be accomplished only by the first type of investment. Actually social investment is closer to consumer expenditure and may be regarded as a special category of such expenditure. Consequently, such investment must be governed by the plan's basic decisions as to how far the plan's objectives depend on restricting the growth of consumption.

(c) Balance between labour-economizing and labour-absorbing investment

After what has been explained in other parts of the present study, it is hardly necessary to stress the importance of this point. As there is no automatic solution to the problem of the proper relation between these two main categories of investment, this question must be tackled at the planning stage. However, it has not yet been given much study, and further progress is required with respect both to its theoretical analysis and to the information available, before any course of action is undertaken that would have the desired practical effect.

(d) *Distribution of State expenditure*

There is a strong and persistent trend on the part of State expenditure to mount, not only because the functions of government continue to expand, but also because of the actual redistributive pressure of income. This means that planning has to begin with the budget itself, as is already the case in a number of countries, This calls for a reorganization of the techniques of budgeting expenditure and investment, which at present are based solely on considerations of administrative or tax control. They need take account also of considerations of economic development, which are not, of course, incompatible with the other considerations.

For that purpose — and this applies to both investment and expenditure — economic and social objectives must be selected that usually require a number of years for their fulfilment. Once these objectives and their order of priority have been established, annual allocations can be made accordingly, and this will help to avoid the dispersion and waste of funds common in government activities owing to lack of planning.

(e) *The contribution of international resources*

The calculation of the over-all amount of international resources depends on the total amount of investment needed to reach a given investment target, and also on the extent to which it is decided to restrict consumption, or the increase in consumption, in order to obtain the necessary savings. But, in addition, the total contribution of international resources must be determined in order to estimate its effect on the balance of payments, so that the necessary measures can be taken in advance to permit transfer abroad of funds for servicing loans.

12. The foregoing brief account shows that shortage of resources is one of the two main justifications for quantification in development. This shortage means that decisions must be taken as to how far present consumption, or the increase in consumption, is to be restricted in the immediate future in order to reach the economic and social targets of the plan in the more distant future. And it also makes necessary a quantitative study of the scope of these targets and of the resources required for each of them, in relation to the resources available for the purpose.

Timely investment

13. Quantification is also essential in order to introduce the structural changes demanded by development and to make the relevant investment in good time.

If the interval between the decision to invest and the results were very short, the only justification for economic planning would be the shortage of resources. But the interval is long — sometimes too long — and if such decisions are not taken with due foresight, disequilibria or maladjustments occur which usually affect the development of the economy to a considerable extent.

In another chapter it is pointed out that the periodic disequilibrium in the balance of payments derives from the failure to make timely provision for certain structural changes in the composition of production — and for the corresponding investment — with a view to import substitution and the promotion of exports. Some activities have to be started well in advance, before the market offers the necessary incentive for starting them. For instance, while a raw material or intermediate product may be easily imported during the expanding phase of exports, only far-sighted action independent of the movement of prices will be able to provide the incentive required to attract private enterprise, or replace it by the State if it fails to respond.

The same may be said of basic investments — energy and transport — which generally require more time than the other productive activities, and where again the market cannot forecast the direction and intensity of future demand.

Similar foresight is called for in respect of technological research and technical training. If some thought is given to the time spent in research on genetics before definitive results can be obtained or the time required to train technicians and teachers and to put students through their studies, it will be realized that there is an undeniable need to make timely provision for capital investment of this kind, which probably yields the highest return of any in Latin America. But, in addition, such endeavours should be guided by the foreseeable requirements of economic development over a certain number of years. Hence the need for planning and also for quantification in this connexion.

14. The vital work of forecasting involved in economic planning, as well as making for timely decisions with respect to the future, is also valuable in the present. It provides, in fact, a yardstick by which to evaluate the measures that the State must continually take to solve current problems. Despite this aspect of their application, such measures usually have a bearing on the future, and only the existence of a plan with well-defined means of implementation and objectives will put the present and the future into their proper perspective. This applies, *inter alia*, to the anti-cyclic measures which are mentioned in another part of this study.

The technique, machinery and organization of planning

15. The technique of planning in a system of private enterprise is in its infancy, and the material it has to use is poor and inadequate. Nevertheless, enough progress has been made to place economic development policy on a sounder basis than before. This is evident from the experience of some Latin American countries with which ECLA has had the opportunity of collaborating. It has been possible to set growth targets and to quantify the investment required to attain them on the basis of different hypotheses; to establish the direction and scope of the structural changes involved in the attainment of such targets; to determine what adaptation

of the human resources will be required; and lastly, to ascertain the nature and magnitude of the international co-operation needed.

However precise its instruments — and they cannot be precise at Latin America's present stage of development — technology cannot entirely replace common sense deriving from familiarity with a country's things and people. But it does enable this common sense to come into play in an impartial analysis of the situation and its possible evolution, on the basis of alternative and clearly-defined hypotheses.

16. The lack of accurate statistics should not be allowed to stand in the way of the work of quantification that a plan needs in order to determine at least certain orders of magnitude, and there is no better incentive to remedying such shortcomings than to demonstrate the practical value of statistics in economic development, quite apart from their illustrative or scientific value.

17. Nevertheless, there is no reason to be content with the progress made either in this field or in the technique of planning; it may be substantial in comparison with the past situation, but it is still very meagre in relation to the magnitude of the problem. The technique of analysing past and present trends and of projecting their future course, on the basis of alternative hypotheses, needs to be perfected and a clearer understanding obtained of the facts on which it draws. Present knowledge of the technical coefficients of production, capital intensity and the absorption of manpower according to different technological patterns is somewhat shaky. It is therefore essential to study the experience of the more advanced countries in this respect and its possible application to other less developed areas. Lastly, to cut short this catalogue of needs more knowledge should be acquired about personnel inputs in relation to the whole range of technical requirements, and on the basis of alternative technological schemes, in order to find a solution to the vitally important problem of training the human potential.

18. But this is not all. A development plan requires machinery to put it into effect. The State already has such machinery, based on the expenditure and investment budget — of which brief mention has been made — and on the tax mechanism. But adjustments must be made so that these instruments, besides fulfilling their specific purposes, will work with maximum efficiency in development policy. The same applies to the administrative organization of the State. A planning organization cannot simply be superimposed upon it, nor can planning be merely a by-product of the State administration. It is essential to integrate the organization of planning in the administrative framework of the State, subject to such necessary modifications as are required.

19. These various activities have already been started, and as a result of the work being carried out in several Latin American countries — in which ECLA has been called upon to collaborate, together with United Nations Technical Assistance and FAO — these problems can be tackled from a more realistic point of view than would have been possible some time ago when the ground had first to be cleared for the establishment of a proper methodology. The time may now be ripe to compare notes

with other non-Latin American countries engaged on a similar task, in order to draw conclusions which may be useful as a guide for practical action.

All this comes within the sphere of planning technique and the pertinent policy decisions. As stated in chapter IV, these two aspects should be clearly distinguished. The technique of planning has to be neutral, but not the planning itself, since it involves taking decisions, and these have to be as rational as possible. However, the technique is not everything although a strictly scientific outlook and a neutral approach will undoubtedly be important factors in the progressive attainment of the requisite degree of rationality without which the task of consciously and deliberately influencing the economic forces can hardly hope to succeed.

CHAPTER VII

THE POLICY OF INTERNATIONAL CO-OPERATION

1. AT THE ECONOMIC LEVEL

The value of past experience

1. From the new course that the policy of international co-operation is following, it is plain that there is a determined desire to examine past experience and analyse the criticisms levelled at this policy in the last few years, while not overlooking its solid merits. The present chapter is intended as a contribution in this direction.

The criticisms relate to various aspects of both economic and technical co-operation. In the economic field, criticism is levelled at the inadequacy of international aid, the lack of a programme, the absence of any promotional sense, the undue importance attached to foreign private enterprise, the reluctance to cover local investment and the short credit terms.

The inadequacy of resources and their estimated aggregate volume

2. It is generally agreed that the international resources allocated to Latin America's economic development are inadequate and should be increased appreciably. Tentative estimates as to the amount needed have been made but they are merely rough approximations calculated by means of the averages for the input-output ratio, which have no very reliable statistical basis. Although these initial tentative speculations have proved useful, the time has come to make more precise estimates. The only way to do so is by obtaining a first-hand detailed knowledge of each country's main investment requirements in relation to the targets in a development plan. This has now been fully recognized, and it is to be hoped that concrete conclusions will be drawn without delay with respect to the amount of international assistance required over the next few years.

The reluctance to recognize the need for such aggregate estimates and to use them as a basis for an international investment programme may have been due to concern at being confronted with unduly high aggregate

estimates, either because the countries concerned fight shy of the necessary national savings effort or because the development targets proposed are too ambitious. But all this is avoidable, and must be avoided if the policy of co-operation is to succeed. One thing is certain — the amount of the international contributions, even at a cautious estimate, will have to be much higher than in the past.

It is possible, however, that if the estimates of the different countries are combined, the total amount will be far more than the international credit agencies see fit to grant. If so, the countries in process of development will have to lower their sights or else to take more energetic measures to restrict consumption and increase national saving. In any event, it is to the advantage of all concerned that this matter should be thoroughly examined.

Absence of promotional sense

3. It may well be that this concern with the amount of foreign aid has in many instances led to the adoption of a passive attitude. It was hoped that countries would submit projects, and it is common knowledge that they have not done so to the extent anticipated. One reason for this is the uncertainty as to whether the requisite resources would be granted. A country needs to be sure that, once the figure for aid has been agreed upon by the international credit institutions, it will be entitled to avail itself of the amount, provided that it submits specific projects and has been carrying out the plan which it has itself outlined and on which the commitment entered into by the credit institutions is based.

But there is no doubt that a more positive attitude would also greatly help to remedy matters. What is needed is a veritable promotion campaign to help Governments and private enterprise to study investment possibilities and prepare the relevant projects. One of the characteristics of economic under-development is the lack of proper administrative experience and organization for such a task, and international co-operation should begin precisely there.

In addition, international resources must be forthcoming at the right time. In some cases where this has not happened, it has made monetary stabilization policy extremely difficult to implement — as has already been seen — or it has helped to prolong certain critical situations unduly.

The stress on foreign private enterprise

4. According to the new concept of the policy of international economic co-operation, assistance in the form of foreign private capital should be appraised not only from the standpoint of its direct effects on the national product, but also with respect to its contribution to the transfer of technology through the training of local staff at all technical levels. Considerable progress has been made in this field. The old method by which the country concerned provided only natural resources and labour, and foreign private enterprise had a monopoly of technique and man-

agement, is largely disappearing, although it still has its strongholds. Otherwise, initiative from abroad is usually an effective means of training domestic skills.

However, close examination reveals that foreign private investment has by no means reached the level that might have been expected in Latin America. Furthermore, much of this investment continues to be concerned with the exploitation of natural resources and with public services rather than with industry or farming. Yet it must not be inferred that the solution of the problem lies mainly in encouraging investment in the last two types of activity. This would certainly alleviate the shortage of national savings, but it would undoubtedly give rise to other problems, and signs of these are not hard to find even now in some Latin American countries. The importance of this point justifies further consideration.

Encouraging Latin American enterprise

5. The technical and economic superiority of foreign private enterprise compared with its Latin American counterpart is not open to dispute, and neither is its importance in the transfer of technology. But this transfer operation is not enough; it is also necessary to encourage, in the country concerned, the training of entrepreneurs, of men to organize and manage production, with all the attendant responsibilities. If a marked increase were to take place in the influx of private foreign capital, such persons, nationals of the country by the mere fact that they have not the same background, would be unable to face the competition of their foreign counterparts either in existing fields of activity or in new branches.

There is no suggestion that the assistance of foreign private enterprise should be forsworn; far from it. But it should go hand in hand with measures to encourage the training and strengthening of domestic enterprise. In the absence of such measures, the unequal competition might well give rise to friction and antagonism which could easily take on a political complexion.

6. The measures that can be taken in this direction are various. The most obvious would be the establishment of a system of credits and technical assistance for domestic enterprises, so as to reduce and eventually eliminate the inequalities of capital and technology. There is a considerable potential demand for such action, especially if it is not made conditional upon the principle that only foreign capital may be used for imports of machinery and equipment (a principle that will be further discussed below), and if operations are adjusted to the methods current in the Latin American countries, which are sometimes different from those in other countries.

Although it is true that the Latin American countries are not in general ready for large-scale projects, it is equally true that there are a number of more modest — although none the less important — steps that they could take if such a system were organized. The rapidity and vigour with which imports of capital goods increase during a favourable

export phase is enough to demonstrate the fact that this potential demand exists and could increase enormously if a persistent effort were made to encourage it.

In most cases it would not be necessary to establish new credit institutions since use could be made of existing institutions, private or official, that are sufficiently reputable and responsible to undertake such a task without the need for detailed control exercised at the source of the funds.

7. In this context, it might also be useful to extend the practice followed in some countries whereby local capital is invited to associate with foreign private enterprise on equal terms, or even contributing a major share of the investment.

In other cases, very promising results have been obtained by provision of part of the capital from foreign sources, together with contracts for services to manage the industry during its first years, until domestic management skills are developed. There have also been strikingly successful examples of industries that originated as State enterprises and eventually passed under private domestic control, with respect both to the technical side and to ownership and management.

At a less ambitious level where considerable success could nevertheless be achieved with proper organization, there have been co-operative activities of a strictly technical nature, involving concessions of the right to use certain processes and the granting of assistance against payment of royalties.

State enterprise

8. Indubitably, if the promotion of the national spirit of enterprise in the Latin American countries were to become one of the cardinal principles of economic co-operation policy, this approach as well as others might be adopted to cope with the difficulty discussed above. Nor would it be surprising if such a development were to help to solve one of the problems which often give rise to concern — the question of State enterprise. The governing principle here has been to make international resources available for the establishment of government enterprises only if no private capital was forthcoming to assume responsibility for the services concerned. Actually, the trend in favour of State activity in respect of public utilities is of long standing in the Latin American countries, and springs from deep-rooted causes. In the days when foreign private enterprise pursued a policy of exclusiveness, State enterprise afforded the only means of developing the abilities of local personnel. Another reason for resorting to it was the wish to prevent over-concentration of economic power in the hands of private companies whose foreign background gave them a superiority in respect of capital and techniques with which only the State was capable of competing.

9. Thus, in the face of these two alternatives — foreign enterprise or domestic enterprise in the hands of the State — the foregoing considerations have frequently weighted the balance in favour of the second

although there has usually been little evidence of the State's administrative capacity. These, however, are not the only possibilities. The contribution of international resources might conceivably serve to encourage domestic private enterprise to undertake such activities especially in cases where there is a direct interest in making the service in question operate and expand satisfactorily so as to cope with a rapidly increasing demand. This applies, for example, to electricity services; credits granted to consumers and workers for the purchase of shares might be a way of reducing this problem to terms very different from those in which it presents itself today.

Financing of local investment expenditure

10. Another of the factors which have helped to limit the capacity to absorb international resources is the stipulation that they be used to cover only imports of capital goods and not the internal portion of the investments. The aim is very laudable — to encourage the national savings effort.

It is thus understandable that in the case of the State this limiting condition should lead to the reduction of expenditure or of its rate of expansion, or to an increase in taxation, or to the floating of internal loans to finance the Government's local investment. But it may well happen — and indeed it often does — that the product of these measures is not sufficient to cover the whole amount required. In such an event, insistence on the procedure referred to inevitably leads to the inflationary expansion of credit, unless the investment project is shelved altogether.

Similarly, in the field of private enterprise, there are cases where merely abstaining from the distribution of profits, or placing new issues of shares on the market, is enough to defray the local portion of investment expenditure. But in other instances this proves insufficient.

Consequently, desirable though it is to promote the greatest possible savings effort in each specific case, the serious drawbacks of the current procedure, especially when no active and well-organized stock market exists (as is the case in most countries), cannot be disregarded.

The stipulation under discussion here need not be taken as a principle based on solid theoretical grounds, but should rather be envisaged as a practical method of ensuring that savings possibilities are exploited to the fullest possible extent. Consequently, there is nothing to prevent its being applied with great flexibility.

11. Nevertheless, the value of its results is open to doubt. Even on the assumption that the practice were strictly applied, and that the whole of the local expenditure on projects submitted to the international credit institutions were financed with domestic resources, this would still not mean that all the savings possibilities referred to had been turned to account. It might well happen that the State would discontinue certain internal investments in order to comply with the foregoing requisite, and that while some entrepreneurs would earmark all their

profits for the same purpose, others who did not resort to international credit, would distribute them without using them for investment.

Hence it is clear that the problem could not be dealt with in terms of individual operations, but only by investigating all the savings possibilities of the economy as a whole and the measures whereby they could be efficaciously exploited. This undertaking — the determination of the volume of saving which could be obtained from internal sources — is one of the essential points in any plan as well as one of the decisive factors in its evaluation. On the same basis, the international credit institutions would, in turn, have to establish the amount of their contributions. This does not mean that the current practice of studying each specific savings possibility would have to be dispensed with, but that it could be applied with all the flexibility necessary to avert undesirable consequences. What is essential is that the plan as a whole should be steadily implemented. Otherwise, there would be grounds for reconsideration of the amount of international resources to be contributed, unless valid reasons could be adduced to justify the non-fulfilment of the internal effort programmed.

12. Rightly considered, what really matters is the achievement of the savings effort and not the relation of its volume to the amount of capital goods imported. The proportion of a country's aggregate investment represented by such external purchases depends not only upon the capacity to import, but also on the country's ability to produce capital goods itself. It is conceivable that the more economic procedure may be to manufacture capital goods at home and import consumer goods. Again, the country concerned may be able to produce capital goods and yet lack sufficient savings to cover their total value. In such an event, recourse to international contributions would be fully warranted.

Thus, there are two different aspects of the matter. One concerns the economic merits of the manufacture of capital goods as compared with the production of goods of other types, whether consumer goods or raw materials or intermediate products. The other consists in the relation between the internal capacity to save and the volume of investment. If these two aspects are confused, wrong decisions may be taken.

13. This last problem has no great practical significance at the present time, but may shortly acquire it if the advance towards the common market considerably stimulates — as seems likely — the production of machinery and equipment in certain countries. Were this to occur, the substantial reduction in the proportion of capital goods imported might force up the coefficient of local investment expenditure until it exceeded the domestic savings coefficient. There would then be no reason why international resources should not be used to cover the difference.

14. Misgivings are sometimes expressed at the possibility that if the international contribution were in the final instance allocated to finance imports of consumer goods, a large proportion of these might be non-essential or luxury items. Here too some elucidation is needed. The important point is that a country which is endeavouring to increase its

investment in order to expedite its development should restrict its consumption of such goods to the greatest extent possible, whether they are imported or domestically produced. The desirability of importing goods to satisfy the consumption thus restricted and producing capital goods at home, or vice versa, should be determined on grounds of economic expediency.

Credits for capital goods in the common market

15. The lack of international credit to finance internal investment expenditure has already given rise to situations in which a country has imported capital goods when they could have been domestically produced at comparable costs, for the simple reason that in the first case it could obtain plenty of credit, but not in the second. There are also Latin American countries which have been unable to export certain types of machinery and equipment, despite favourable conditions in respect of price and quality, because they are not in a position to grant sufficient credit.

Herein lies one of the most serious stumbling-blocks which will face the common market if the problem is not solved. In brief, if a country producing capital goods does not yet have enough savings to finance the whole of its own investment, it is idle to suppose that a system of export credits can be organized without additional external aid, unless by recourse to inflationary expedients which are better avoided.

16. This leads to another aspect of the question, namely, whether international contributions should benefit the countries exporting or those importing capital goods. This is another of the problems that could be satisfactorily solved under a development programme. Once the volume of the contribution had been established, the country concerned would have to be left at liberty to use the funds provided to purchase its imports of capital goods from the source that best suited its interest. The most-favoured-nation treatment granted one another by the members of the common market should suffice to encourage production and trade in respect of such goods without the need for credit incentives. If, however, the system is to operate satisfactorily, it would be desirable for the more advanced countries which grant export credits to draw upon their resources in order to contribute to this type of aggregate financing of the investment requirements of countries in process of development. Such a course of action, apart from simplifying the problem under discussion, would remove one of the most persistent obstacles to the full restoration of international multilateralism.

Credit periods

17. Another aspect of the prevailing system of export credits is the relatively short period for which they are granted. This has laid very heavy burdens on the balance of payments of certain countries and has involved the need for new credits to ease the strain. From the point of

view of individual operations, this policy of short-term credits is readily understandable; what is more, as was pointed out elsewhere, it usually signifies an incentive to enterprises to use their profits for expediting amortization, and thus helps to raise the domestic savings coefficient. But from the standpoint of a country as a whole, it is apt to create very disturbing situations, which militate against monetary stability itself.

Some means must therefore be found of reconciling the desirability of rapid amortization from the point of view of individual operations with an amortization system consonant with the possible development of a country's capacity to save, as well as with its ability to transfer its savings to amortization and imports of capital goods. Herein lies another of the advantages which only a plan can offer. A plan alone, with the structural reforms it aims to bring about, can enable savings and transfer possibilities to be gradually improved until the established target is attained.

2. AT THE TECHNICAL LEVEL

Technical assistance and development planning

18. International technical assistance has also been a source of widely varying experience of which advantage would have to be taken in the revision of the relevant policy. Such experience testifies to the full value of technical assistance for countries in process of development, and at the same time reveals basic flaws which must be eliminated. These shortcomings may be reduced to three main points: (a) technical assistance has not kept in close touch with the requirements of economic development; (b) since the form it has taken has been determined mainly by pressure of temporary circumstances, it has not been systematically planned with clearly-defined objectives; (c) resources have been inadequate.

19. The first point is closely related to the need for a development plan. Only by this means can real requirements in respect of technical assistance be ascertained and an order of priority established on the basis of their nature, their degree of urgency and the resources required to meet them. As long as no plan exists, all that can be expected is a more or less satisfactory succession of individual undertakings which often depend upon the diligence and the particular bent of the officials concerned — both at the national and at the international level — rather than on a precise analysis of requirements. It has become evident in practice that in such circumstances a considerable proportion of the resources used must inevitably be wasted.

Thus, the technical assistance rendered is dictated by immediate circumstances in a manner conducive to improvisation, or at least to decisions which are not prompted by definite aims whose fulfilment entails a systematic programme of work. There are three fields in which such systematic action is required, namely: (a) surveys of natural resources (b) technological research; (c) technical training of the human potential.

Research on natural resources

20. Making a survey of a country's natural resources is a costly operation which, if its object were the acquisition of purely scientific knowledge, would take a considerable time or require very substantial funds. Since funds are limited and time presses, it is advisable to organize research in terms of the requirements of a plan, and with due regard to the probable development of domestic and world demand for the resources in question. What is more, the problem arises in all the Latin American countries, and as it cannot be fully and simultaneously solved in each of them individually, a technical assistance programme covering the requirements of the region as a whole, and, here again, establishing a reasonable order of priorities, will need to be formulated.

Technological research

21. Technological research is concerned with ways of utilizing the above-mentioned resources and of adapting modern technology to the conditions prevailing in the Latin American countries. With respect to procedures for the utilization of natural resources, a series of problems arises on which, except for some fragmentary initial attempts, no systematic research has hitherto been conducted. The field of research is also wide, and could only be rationally approached on the basis of requirements clearly deriving from an economic development plan.

Naturally, this does not mean that the institutes of technological research should not at all times be ready to assist in an advisory capacity, on request, in the solution of immediate and *ad hoc* problems. But if they devote a major share of their energies to this work, they will do so at the expense of problems that should be tackled with foresight and in terms of the present and future requirements of a development plan.

22. As regards the other aspect — the application of modern technology with due regard to conditions in the Latin American countries — problems of productivity are increasingly becoming a motive of concern. Here too it is highly recommendable that the objectives pursued should be established in advance. To begin with, the possibilities of increasing productivity are considerable in all branches of economic activity in the Latin American countries. But it is not a matter of indifference whether this is achieved by economizing in manpower, or by saving on raw material or fuels, or by improving the yield of capital; the incidence on a country's economy differs widely from one case to another. First, therefore, it is necessary to determine the direction in which technological research should be channelled, in order to formulate a programme adapted to the requirements of the country concerned, instead of abandoning it to the vagaries of circumstance.

23. Apart from this, where the saving of capital is concerned — so important a consideration in the Latin American countries — the problem does not merely consist in improving the efficiency with which

the existing stock of capital is utilized; it is of much broader scope and virtually unexplored. It is, in fact, the problem of disequilibrium between modern technology and investment capacity to which reference has so often been made. Since it is impossible to revert to outmoded technological patterns, there are only two ways of approaching this difficulty: (a) research on new patterns which will enable capital rather than labour to be saved; (b) the appropriate selection or combination of available alternatives whereby this aim can be achieved. This is among the problems which, by their very nature, can only be studied at the international level.

The human potential

24. The technical training of the human potential, from skilled workers to technical experts, is of considerable importance, both because of the colossal magnitude of the problem and because such training must be adjusted to the structural changes in the economy. This whole question is a matter of increasing concern in Latin America and international technical assistance might be of great value in dealing with it. In this connexion, two points arise. The first is the help that might be given in defining the terms and the present and future dimensions of the problem, and the second, the best ways and means of solving it. In some cases, the necessary effort can be more satisfactorily organized at the national level; in others, by groups of countries or in Latin America as a whole.

Limitations of financial and human resources

25. The resources hitherto allocated by various organizations to technical assistance in Latin America have proved all too limited in relation to requirements and the necessary rate of progress. If the systematic programme of work outlined very briefly above is to be carried out on comprehensive lines, much more ample resources than those at present available will be needed, and the action of the organizations concerned will have to be co-ordinated to obviate dissipation of effort. But nothing can replace co-ordination at the national level, and for this only a clearly-defined order of priorities deriving from a development plan can provide a sound basis.

It is not merely financial but also human resources that are limited. The only solution is to train personnel, and train them quickly. Perhaps precisely because of the fortuitous and sporadic character of technical assistance, insufficient stress has been laid on this aspect, and the necessary effort to train Latin American experts has been neglected. This should be embarked upon without delay, both because knowledge of the environment is indispensable for the success of technical assistance activities, and because the experience thus accumulated becomes part of the heritage of the Latin American countries themselves, and may serve as a fountain-head for the wide dissemination of technology.

Technical assistance in economic planning

26. The work of planning itself calls for technical assistance. This is something relatively new, for while it is true that collective planning already has long years of experience behind it, the planning referred to relates to the system of private enterprise, which it endeavours to infuse with the maximum degree of dynamic validity. Certainly, the experience referred to is of considerable interest, but in order to tackle Latin America's problems under this head — and those of other countries in process of development — new trails must be blazed and new creative forces unleashed.

This is an aspect of the question to which increasing importance is being attached by international institutions, and now that the principle of planning is fully recognized in international co-operation policy, the way lies open for its more energetic implementation. In the preliminary phase already completed, groups of experts on programming techniques have been sent to some of the Latin American countries at their request, but it has been impossible to meet the needs of all those interested for want of financial and human resources. Even so, the experiment has been very successful and instructive, and may serve as a point of departure for an expanded and more systematic organization of this type of technical assistance.

27. From all that has been said in the foregoing pages, the following is the primary conclusion to be deduced: a development plan is the most satisfactory basis on which to establish international co-operation in both economic and the technical sphere. Upon this same basis, credit and technical assistance institutions can decide what form and amount of co-operation they consider appropriate. It would be desirable for this part of the work to be jointly carried out, within their respective areas, by both types of institution. After a study of the plan, each organization could decide upon the contribution it was prepared to make and the form that contribution would assume. Both in the economic and in the technical field, the contribution in question would have to be established for an adequate period, so that the national authorities could count on the availability of the resources approved, provided they submitted satisfactory specific projects, complying with the requisites which the Governments themselves had considered to be essential for the success of the plan.

Technical operation and political decisions

28. Here a clear line of demarcation must be drawn between two different aspects of the subject. It should be remembered that a development plan is not a purely technical operation, but involves highly significant political decisions. For these decisions the Governments alone are responsible, but there cannot be the slightest doubt that the technical work of elucidating problems and formulating alternative solutions may decisively affect them. Thus, for example, the national effort to raise the savings coefficient and reach programme targets can be achieved only

on the basis of certain internal measures — mainly fiscal — that represent political decisions as serious as those which, in another direction, might be involved in several countries in the reform of the land tenure system with a view to the attainment of agricultural production objectives.

In other words, the very dynamics of a plan must necessarily generate these and other problems; the process is logically inevitable. What is more, the measures adopted by Governments to solve them will afford the main yardstick by which to measure the value and efficacy of the plan, not merely from the domestic angle, but also from the point of view of international co-operation.

Fortunately, Latin America shows a clear awareness of the need to reform the economic and social structure in order to expedite development and reduce the disparities in income distribution. And unquestionably, those whose determination to launch such reforms induces them to assume grave political responsibilities will find lively encouragement in the new turn that international co-operation policy is now taking.

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