THE PUBLIC SECTOR INVESTMENT PROCESS

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NOTES ON THE INVESTMENT PROCESS

I. THE INVESTMENT PROCESS IN MIXED ECONOMIES

1. In a mixed economy, the investment process is a result of the actions taken by a large number of public and private agents, both national and foreign. These agents utilize human, material and financial resources and information as a means of transforming ideas (which have been developed in response to a need or opportunity) into feasible solutions that take the form of investment projects. Thus, for example, a problem or need relating to energy, irrigation, storage or agricultural techniques may, if the investment process is functioning normally, give rise to projects concerning electrification, irrigation, warehouses, experimental stations or demonstration centers. Similarly, the existence of a renewable natural resource, if it can be developed, may give rise to a settlement project or to land-incorporation project.

2. The investment process is neither unique nor is it continuous. It rather is the result of the integration of many different, parallel processes which are often marked by sharp internal discontinuities; these processes are directed by numerous independent decision units each of which is in charge of some part of their development; the units frequently use different criteria when taking decisions. Nevertheless, even in the absence of any formal planning system, the investment process is not, strictly speaking, a spontaneous one. A variety of public policies and activities influence this process or guide it in one direction or another. Exchange rate, fiscal and monetary policies are some of the elements which provide such guidance.

3. Frequently, the investment process functions on an inorganic, inefficient and expensive basis uses a great deal of resources in proportion to the investment which is made; involves a duplication of effort by two or more decision making units in
their search for solutions to common problems, while other important areas are ignored; the criteria utilized in selecting and assessing projects differ from national objectives and strategies; unnecessary discontinuities and suspensions of activity occur which result in wasted time and resources; the contacts, links and sequences which would make it possible to improve the implementation of complementary projects are not established; and no effort is made to co-ordinate or align different investment initiatives.

4. The shortcomings exhibited by the investment process as a whole manifest in similar ways in its various components. Thus, in the case of public investment, government agencies often display striking differences from one another in so far as their project design, formulation and implementation capabilities are concerned. For example, public works and electric power agencies usually take an active and appropriate part in the investment process; on the other hand, agencies concerned with the agroindustrial sector, support services for agricultural production activities, or social infrastructure frequently lack teams which can meet their project needs.

5. Public intervention through the planning process has been a more or less generalized response to the above issues. In essence, planning in a mixed economy is basically an attempt to place government decision making in a more systematic and coherent framework that would normally be achieved through the piecemeal treatment of public polities. Regarding the investment process the issue of policy coordination is enhanced due to the time dimension that is involved. However, the exploration of a pragmatic approach to coordination among economic agents through a system that combines plan and market should not only point to both its need and possible advantages, but must also confront the record of developing countries' experience with planning in
earlier periods, and the emerging conditions of complexity and uncertainty in the economic environment.

6. Since the 1950s governments in most developing countries have taken an activist role in promoting development - setting macro-economic policies, investing to build infrastructure, expand basic services and engaging - through public enterprises - in directly productive activities. Some form of national economic planning to guide the rise of the country's investment resources has been considered an essential part of the development effort.

7. The establishment of planning agencies for formulating comprehensive development strategy represented an important institutional departure. These agencies were intended to provide medium- and long-term perspectives on development, supplementing the short-run preoccupations that had dominated the approach of economic and finance ministries. While the products of planning agencies - the plans themselves - have frequently been ignored, the process of planning has been useful. It has provided a forum for bringing together different government agencies and different societal groups to think about national development. Also, it has helped politicians to mobilize public support for development programs.

8. In spite of its positive contributions to the development process and to the coordination of public policies, several factors underlie the limited success of plans. At root there is an inherent weakness in the "blue print" approach adopted by most planning agencies, since available analytical techniques are just not able to cope with the complexity of economic and social change and to produce plans that are up-to-date, relevant and comprehensive. As a common practice targets were set for variables which could not be controlled nor even predicted, expectations on economic behavior had more to do with faith than
analysis, there has been lack of clarity regarding key instruments and actors, and even a failure by governments themselves to accept the discipline of the plans formulated in their behalf. Consequently, the plans have been secondary rather than primary, passive rather than active, and on paper rather than in the field of real politics.

9. More recently, there has been a shift in many development countries towards concentrating their efforts on a more selective, flexible and pragmatic approach to planning and coordination of public policies.

10. This shift in approach has good reasons derived from a sound evaluation of the actual methodology and achievements of planning, but it has also been induced by the turbulence that has characterized the international economy from the 1970s on, and by its most likely future developments. In fact, during the 1970s the developing countries' capacity to manage their economy was tested to the limit. Energy prices surged twice, inflation rose to new peaks and then came down sharply, exchange rates fluctuated widely, and international interest rates were higher for longer than at any time in history. Growth rates in the industrial countries slumped as they faced the most protracted recession in fifty years.

11. International trade, financial flows and technological change form the primary economic links between industrial and developing countries. Recent trends in these three areas have resulted in cumulative uncertainty that poses extremely difficult challenges to both the direction of feasible long-term development strategy, and short- and medium-term economic management.

12. The volume of international trade has shown sharp variations complemented by profound changes in major trading
flows, and a new wave of protectionism has arisen affecting developing countries' exports and terms of trade.

13. International finance in periods of volatile change plays a dual role; on the one hand, it might help countries adjust to external shocks as happened during the 1974-75 recession; on the other hand, it could be an additional channel for the transmission of external shocks, as in the 1981-83 recession. There are increasingly justified doubts on the sustainability of a continuous and massive transfer of resources from developing to industrial countries as a consequence of the roll-over of the cumulated debt.

14. Finally, the sharp changes in production patterns occurring in response to technological innovations and the "services revolution" underway are affecting significantly the traditional comparative advantages for developing countries.

15. The problems of managing in a hostile environment are thus superimposed on the "normal" problems of development and economic management.

II. PLANNING AND COORDINATION OF PUBLIC POLICIES

16. The need for developing countries to adjust to the complexity and interdependence of the modern international economy has caused them to focus even greater attention on managing the national economy. Instead of constructing elaborate models for comprehensive planning, governments are concentrating more of their efforts on the two primary means within their control for guiding the growth process: a sound public sector investment program - that allocates scarce resources to high-priority public needs - and a macroeconomic policy framework that attempts to provide the right signals to both public and private entities.
17. The macroeconomic policy framework is composed of a series of interlocking policies that affect all aspects of economic life and call for strong coordinating mechanisms in the public sector. The key elements are fiscal, monetary, exchange rate, wage and trade policies. They combine in determining the rate and pattern of capital accumulation and resource utilization, and the pace of economic activity and growth as well as the maintenance of external (balance of payments) and internal (domestic inflation) equilibria. Experience has shown the importance of a pragmatic and flexible framework so as to allow for the "administration of trade-offs" among potentially conflicting objectives such as to provide adequate incentives for longer-term growth, to attain objectives of equity and social advance, and to permit the economy to adjust to external disturbances.

18. The other major area of policy concern is investment planning, since the character of development, its direction and pace, and the way people share in its benefits are largely determined by how a country manages its investment resources. This comprised analysis and decisions at the national level, where projects are aggregated into a national investment plan that fits into the macroeconomic policy framework just mentioned; at the sector level, where sector investment strategies and priorities, along with supporting policies, are elaborated; and at the project level, where specific projects are identified, prepared and implemented.

19. Both areas of policy concern - the macropolicy framework and investment programming - are strongly complementary. If stress is laid on the macro level only, growth is conceived as a rather mechanical phenomenon, and the important aspect of real resource mobilization tends to get overlooked.

20. Prior to the economic crisis, investment programming was often visualized as the mobilization of the development effort by
rising the level of public investment. Financially this effort might be limited by the public sector's capacity to implement on the expenditure side of the budget, or by the limited capacity to generate revenues of external finance. The underlying objective was to ease those constrains so as to expand the investment program.

21. The typical situation is viewed in a quite different perspective nowadays. The economy is constrained by excessive pressure on macroeconomic resource availability, as manifested in acute external payments difficulties, budgetary imbalances, undue monetary expansion and domestic inflation. The context for public investment, therefore, is likely to be dominated by the short-term pressure for stabilization and the medium-term structural adjustment requirement, rather than by the long term need for structural transformation.

22. The integration of the allocation/mobilization dimensions of the development process and the macro and micro levels has strong requirements both in terms of the analytical framework for policy design, and in terms of policy coordination among central government, line ministries and autonomous and decentralized agencies.

III. THE PUBLIC SECTOR INVESTMENT PROGRAM PSIP

23. Within the PSIP process itself one of the key problems is the proper relationship between the individual project and the overall development strategy. The attempt to completely separate projects from plans is misconceived because of the important parameter values that are thereby left unresolved; in other words there is a positive need for a downward flow of information. On the other hand more precise estimated for the PSIP can only be built up from details of on-going projects and prefeasibility.
FIGURE 1
PSIP and Individual Projects

Note: Adapted from ILPES, "La Planificación del Desarrollo Agropecuario", Siglo XXI, 1977.
studies of planned projects; that is there is also a need for an upward flow of information (see Figure 1).

24. In the past there has been a certain amount of somewhat sterile argument among planners as to the relative merits of planning from the top down as opposed to from the bottom up. The former refers to the prior determination of the macroeconomic plan and the derivation of projects (i.e. investment requirements) therefrom; while the latter terms refers to the identification of feasible projects and the building up of an aggregate plan from these elements. In practice, of course, the process is inevitably a circular one, involving both these steps.

25. A somewhat idealized methodology to build up a PSIP is usually presented as follows. The first step is preparation of macroeconomic forecasts to provide a framework for making decisions, included those about feasible growth patterns on the economy, after assumptions about proposed tax and other revenue policies, the growth of recurrent expenditures and similar factors are incorporated, this framework also supplies a basis for estimating the financial resources, both domestic and external, likely to be available for public investment in a given year. This is followed by identification of major investment programs by problem-areas (sectors) including the assignment of preliminary priorities among them consistent with the overall development strategy.

26. The second step involves a survey of on-going and identified projects as well as an evaluation of its potential to produce the desired results. The final step consists of the identification of new project ideas to close the gap between investment requirements and on-going and identified projects by problems areas subject to the resource constraints (see Figure 2). Drawing up the PSIP requires several rounds of iteration, that
FIGURE 2

PSIP Formulation Process

Note: Adapted from ILPES, "La Planificación del Desarrollo Agropecuario", Siglo XXI, 1977.
is, feedback from one step to another to obtain a satisfactory fit among the variables.

27. The purpose of the PSIP formulation process is to obtain, efficiently and economically, a sufficient number of projects whose quality, diversity and timeframe are such that they will help to put a given development strategy into effect. In this connection, the idea of "quality" involves two elements: first, it relates to the methods of project formulation and assessment which are used; secondly, it relates to project characteristics which will contribute to the achievement of the objectives that are pursued. The projects should be varied enough to cover, as comprehensively as possible, those activities which would play an important part in achieving the objectives that have been set. The term "quantity" is clear: it refers to the availability of a sufficient number of projects to meet the needs arising out of the development strategy. Finally, projects must be available when they are required by the proposed development process. In other words, a project of the necessary quality may not be very useful if it will take so long to complete that its goals cannot be achieved within the required time period.

A. The Committed Resources Issues

28. The abstract presentation of the above circular procedure tends to underestimate the difficulties in practice which clearly place serious constraints on the freedom to achieve an optimal result. In the normal course of events, major projects will have a long gestation period, and thus for anyone (say five-year) planning period, much of the capital funds will have been committed by decisions made during the previous planning period, or even the one before that. In consequence, it would not be unusual for the uncommitted budget to be less than one third the total at anyone point in time. Thus when the most pressing new projects are added, the public investment budget may be somewhat
inflexible, and the aggregate plan has to be pragmatically adjusted to it. As a result there is often a need to overcome inconsistencies between the projects and the budget on the one hand, and the projects and the plan on the other.

29. There are strong reasons for giving priority to the completion of on-going projects, since the sunk costs usually mean a high return on the additional investment needed for completion. Also there is a need to using and safeguarding existing capital stock by proper operation and maintenance. An insufficient provision of recurrent resources for maintenance and repair would only make investment for rehabilitation the leading spending activity at a future time.

30. Due to the serious consequences of neglecting on-going projects and disregarding maintenance and repair costs for completed projects, it is necessary to adopt a systematic approach to deciding how much funding can be devoted to new projects in a given budget year. A technique that has proven useful is to calculate the funding needs of on-going and completed projects, explicitly including operation and maintenance needs, in order to determine the free public sector resources remaining for new projects.

B. The Large Scale Project Issue

31. A second qualification refers to the problems associated with large scale projects that preempt the development budget over several years. At times, they do not show specially attractive rates of return, but nonetheless they find their way into the PSIP.

32. A more rigorous application of economic criteria would make a major contribution to the better use of resources by pointing out the need to abandon, scale down or postpone projects with low
economic returns. For these purposes strengthening the capacity to appraise projects is still essential.

33. However, it is not all that clear that the pledge to increase this capacity has been as fruitful as it would have been hoped. One of the possible reasons is that the requirements for systematic project evaluation place demands on weak administrations beyond their capacity. Another reason could be that political and administrative interest find it advantageous to by-pass an organized project evaluation process.

33. This would suggest as a complementary course of action to analyze with some insight the sources of weakness of the existing evaluation system, and not only fall back on reiterating the virtues of economic analysis and the need to strengthen evaluation capacity.

C. The Organizational Issue

35. A third major qualification is related to the organizational and administrative arrangement of the process. As argued before, project generation is a highly decentralized process, even if its locus is restricted to the public sector. This has three main implications:

   a) There is a multiplicity of decision units sponsoring different projects.

   b) The behavior of these units is oriented by its own interest and particular rationality.

   c) The power at the disposal of each unit to push through its own initiatives varies significantly among them both in technical and political grounds.

30. Thus the process of building up a consolidated PSIP involves a good deal of bargaining and it is not just a matter of
technical judgement. Normally, the background of this bargaining process is conditioned by differences in:

- the statement of objectives which rationalizes a more subtle process of social and bureaucratic goals being pursued;

- the time frame derived from the type of activity each agency is mainly involved with (i.e.: long-term electric power programs vs. short- and medium-term rural works programs);

- the estimates of resource availability which in an uncertain world, may also involve different attitudes towards risks of under- or over-targeting expenditure programs.

37. The complex process whereby political choices are adopted can be made more rational and efficient by improved analysis, but it cannot be replaced by a pure technical calculus. The minimum which might be expected is that public sector spending is presented with sufficient clarity, and its level and disposition be reasonably transparent. However, information in this context is highly valuable and therefore there are strong incentives to withhold it; this, in turn, makes more imperfect the consolidation process.

38. In spite of these constraints there is a need for giving coherence to the investment ideas and hopefully make them consistent with both the overall development strategy and ex-ante resource availability. The first task is normally undertaken by the planning agency, but most of the time it ends up in a list of projects as a means of avoiding implicit conflicts to develop.

39. Finance ministries have the responsibility of ensuring ex-post balance between planned expenditures and resource availability. To cope with budgetary shortages and uncertainties they normally resort to two main mechanisms. On the one hand, they tend to release money only on a monthly or quarterly basis.
This makes it difficult for other ministries and project managers to plan their operations even a year ahead. On the other hand they also resort to across-the-board cuts, which hit high priority projects as hard as any others.

40. Thus an important priority is to explore the possibilities of making the PSIP preparation process as explicit and systematic as possible in order to discover the choices to be made and their implications for financial management over several years. In this case the PSIP document might progress from a list of projects to a useful planning tool, consistent with reasonable estimates of available resources.

D. The Flexibility Issue

41. A fourth major qualification arises in relation to possible ways in dealing with the consequences of economic uncertainty and the resulting fluctuations in the budgetary situation. Experience during the 1970s has shown that even the most carefully designed policies and investment programs can be confounded by sudden changes. To minimize this damage, it has proven useful to identify a core investment program that includes all strategic projects and has priority for funding in case of budget cuts.

42. Even with much provision, governments need to revise their macroeconomic framework periodically and to phase the multiyear investment program for implementation in the form of annual programs that could be integrated with the annual budget. A useful procedure is to update the macroeconomic framework at the time each annual program is prepared, and to revise and extend the PSIP by one more year, thereby making it a rolling plan. For most a three to five year horizon is the longest that is practicable, with programs rolled over each year.
43. For the procedure to be successful, an effective system must be established for monitoring physical and financial implementation of the investment program so that the annual revisions can be based on reliable and up-to-date information. The PSIP, or its main projects, may have to be revised even more frequently (i.e.: quarterly) if the economic environment changes sharply. Critical stages of the process are likely to involve decision making under pressure in which strong judgments have to be made on the basis of highly summary data. Thus resource allocation will be enhanced if there is an effective information system to summarize and present data in these final decision stages.

44. A complementary line of advance relates to project design and evaluation to take into account macroeconomic uncertainties. Explicit consideration of the implications of possible changes in resource availability during the implementation of the project might lead to different project design (with more built-in flexibility), to different project choices, and to more effective contingency planning at the project level. In project design one specific characteristic to be assessed is the degree to which it is either divisible or can be postponed without increasing excessively its costs.

45. The flexibility issue is most important in connection with long gestation period projects. There are two reasons why budgets cuts will favor postponement of these projects. On the one hand, resource scarcity increases the opportunity cost of capital, which in turn should be translated into an increase in the discount rate, favoring immediate as compared to future benefits and thus tilting the balance against longer gestation period projects. On the other hand, previsible resource shortage will favor budgetary flexibility as an end in itself decreasing the interest for projects involving multiperiod budgetary commitments.
46. However, on the real side of the economy the postponement of a long gestation indivisible investment (i.e.: a dam) may create bottlenecks of high cost beginning at the date it was initially scheduled for completion. In these circumstances the long gestation, indivisible and strategic character of the project may provide a rationale for inclusion in the core investment program to avoid being affected by short-term difficulties.

E. The Small-Open Economy Issue

47. A final consideration is particularly applicable to small-open economies and relates to the initiative and funding of major investment decisions. There are two features characterizing small-open economies which are particularly relevant to the discussion.

48. First, the fact that the economic structure of a small-open economy resembles more an aggregation of individual economic activities than a fairly reasonable integrated system (i.e. the matrix of intermediate demand in an input-output table will be sparsely covered with non-zero figures). Additionally, most if not all the individual major economic activities are outward-looking either due to the high incidence of foreign decision making, or because of considerations relating to markets, technology and factors of production.

49. Second, the rhythm and intensity of the capital accumulation process will heavily depend on outside occurring events and decisions. If a distinction is drawn between national-space and economic-space, most of these activities will be a part of a much larger decision making economic space. Therefore, the local portion of the global economic activity will derive its rationality from this much larger decision space. Since each local economic activity will be inscribed in different economic
spaces, the national economy will be the locus of a series of non-articulated small parts of various large economic spaces.

50. Consequently, the likelihood of a lack of coordination and even synchronies in their relative development is very high, and it is a fundamental question for national governments to address, even though the room for maneuver might be rather small.

51. There are a number of ways by which this issue will be constraining the PSIP formulation process. For one thing, there is the important requirement of making externally generated initiatives consistent with government strategy and policies. Second, some projects financed by donors will require local co-financing of capital costs. Third, normally there will be recurrent costs implications on the fiscal budget of projects financed by donors or foreign sources. Fourth, some investment decisions will be external initiatives but will demand complementary public investment projects (i.e. tourism facilities and road or transportation improvements). Last, aid funds are allocated and complementary local funding compromised in a negotiation which usually looks at the projects on the table in a sound fashion, but which fails to consider their priority against alternatives not introduced in the particular negotiation.

52. Thus a big effort might be needed in order to coordinate all these initiatives, and to develop the bargaining power of the government vis-a-vis external decision making agents and donors, and in general regarding international or bilateral technical and financial assistance. Certainly, a sound and pragmatic development strategy and well-organized procedures for dealing.

53. Taken together the preceding five qualifications show some of the main complexities of building up a PSIP, and of making it a selective, flexible and pragmatic instrument of public policy.
In principle, there are some alternative procedures for making the available projects more compatible with the requirements of the development strategy. One option would be to increase its quantity since the availability of a large number of projects could maximize the possibility of identifying those which are needed in order to implement the development strategy. A second option would be to reconcile the medium-term goals of the development strategy with the supply of available projects, which would be formulated on a more or less spontaneous basis by line ministries and government agencies. The surveys on expected investments carried out by planners are an example of this type of procedure. The third option would be to use a procedure for translating the goals of the development strategy into a series of projects. Finally, a procedure could be designed which would work in parallel and on an iterative basis. This procedure would stress the importance of beginning to generate projects at the very earliest stages in the design of the development strategy, specially if the case of projects requiring a long gestation period. Each of these options, along with their advantages and disadvantages, are detailed in Table 1.

IV. THE INTERFACE OF PUBLIC AND PRIVATE SECTORS

54. A final issue relates to the interface of public and private sectors in a mixed economy. The relationships among participants from both sectors have become less and less anonymous in the modern economy, and bargaining has grown in importance. From a public viewpoint it must be recognized that key policy instruments work through the market.

55. The experience from mixed economies permits to identify three types of interrelation between public policies and the market:
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a) \textbf{Counter market} that are mainly interventions aiming to
distribution, cutting of profits, rules for
localization, environmental restriction, workers'
protection, etc.

b) \textbf{Pro-market} which are interventions directed to restore
a more ideal market (i.e. anti-trust legislation). At
times there is a more advanced form of this, namely to
speed up the process of the market forces without
affecting its direction (i.e. government research
subsidies).

c) Management of activities in the public sector, hence
\textit{outside the market} and, in principle, under political
control.

56. There is no way to neatly group various policies into one or
the other category: in monetary policy, for instance, (a) and (b)
tend to appear in some mixture, and in fiscal policy all three.
Counter-market interventions are often legitimized by claiming
that they are really pro-market in the longer run. On the other
hand, it is quite frequent that agents who support in principle
an ideal, free market argue for counter-market interventions in
favor of special interests.

57. Most of these issues belong more properly to the realm of
institutional regulations and the design of the macropolicy
framework, and the questions posed are indeed problematic and
controversial. However, some final considerations are in order
regarding the role of the public sector in stimulating and
influencing the overall investment process consciously. There
are three topics that deserve some discussion:

a) Identification of those areas of the investment
process which may be subject to public action.

b) Selection and advisability of direct or indirect
action.

c) Definition of the intensiveness, extent and scope of
public action.
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<th>Options</th>
<th>Advantages</th>
<th>Disadvantages</th>
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<tr>
<td>a) Increase in the number of</td>
<td>The simplicity of the system</td>
<td>The high cost associated with the large number of projects needed to ensure the</td>
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<td>projects</td>
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<td>required quantity, quality, variety and timing</td>
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<td>The after-effects of this cost: the need for a large amount of information and</td>
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<td>a large number of skilled personnel, which is not always available</td>
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<td>The impossibility of always attaining the quality, diversity and timing</td>
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<td>required by the development process</td>
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<td>b) Limitation of goals so that</td>
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<td>An over-limitation of the &quot;goals&quot; of the plan which in the best of cases, would</td>
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<td>they will be in keeping with</td>
<td>this basis</td>
<td>thus become no more than a means of organizing an &quot;spontaneous&quot; development</td>
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<td>spontaneous project generation</td>
<td>The simplicity of the project formulation system</td>
<td>process</td>
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<td>capabilities</td>
<td>The reduction of the &quot;death rate&quot; of spontaneous</td>
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<td>projects</td>
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<td>c) Sequential procedure</td>
<td>Economy in the project formulation process</td>
<td>In most cases, the impossibility of holding to the timetable for expected</td>
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<td>Coverage of quality, quantity and diversity</td>
<td>results due to the lead-time required by the projects</td>
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<td>The possibility of lowering the costs involved in</td>
<td>The relative complexity of the system planning/projects</td>
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<td>procedure</td>
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<td>diversity and -most importantly- timing as</td>
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Note: Adapted from ILPES, "La Planificación del Desarrollo Agropecuario", Siglo XX, 1977.
58. In order to identify possible areas of action it is useful to refer to a functional diagram of the transformation process as a black-box: certain inputs enter this unit, are processed within it, and emerge in the form of outputs. Thus, in the case of the investment process, the inputs are problem situations and ideas for projects, while the outputs are projects which represent the best technically- and economically-feasible solutions. Human, material, financial and information resources are required in order to bring about this transformation (see Figure 3).

59. The government can take action which will have an effect on the existing problem situations and project ideas. Indeed, one of the tasks of public policy is the systematic identification of the main problem-situations and of the project ideas which, with time, could resolve them.

60. An adequate flow of project ideas is needed, but it is not sufficient to ensure a suitable generation of projects within the investment process. It is also necessary for the process of transforming these ideas to have an appropriate structure and mode of operation. The following complementary options are available as regards action in this connection:

- to influence the design of the process;
- to regulate the supply of the resources to be utilized;
- to take action on information fed into the process;
- to participate in or influence its management; and
- to refine the criteria used in the decision making process.

In this way, public policy can reinforce, modify, encourage or discourage some of the participants in the investment process. In addition, the government can also alter the quantity and quality of the human, financial and material resources which itself allocates for activities linked to the investment process and can have an influence on many of the resources utilized by the private sector. (For example, it can train personnel.
FIGURE 3
Action Areas in the Investment Process

Note: Adapted from ILDES, "La Planificación del Desarrollo Agropecuario", Siglo XXI, 1977.
develop and disseminate new methodologies, obtain loans and technical advisory services from abroad, endorse requests made by the private sector, etc.).

61. In so far as the various forms of public action are concerned, it is helpful to distinguish between direct and indirect action affecting the investment process. Indirect action is design to bring about the required changes in the structure and mode of operation of the investment process through the use of generic incentives and sanctions. For example, the government can offer technical and financial assistance to agencies, enterprises or consultancy firms which identify and formulate projects; it can grant tax exemptions for the resources used in the preparation of projects; it can train or encourage the training of the human resources required by the investment process; it can improve the available information as regards pre-investment; etc.

62. Direct action is designed to alter the structure and mode of operation of the investment process by means of specific measures. The following examples illustrate various forms of direct action:

- The identification of problem situations and the subsequent generation of project ideas (using its own technical resources for this purpose) and the placement of the results at the disposal of agents which will be responsible for their subsequent formulation and implementation.

- The proposal or modification of legal and technical regulations which influence the way in which the investment process operates and the establishment of new guidelines or criteria for the assessment of given projects.
... Action affecting various decision-making components of the investment process, which would involve the issuance of orders to centralized entities and of instructions to directors who represent the government in autonomous decentralized agencies or in public enterprises, directing them to initiate or speed up some projects or to postpone others.

- The conclusion of agreements with public entities or with private sector organizations having similar purposes.

It is, therefore, necessary to design a specific mode of action which is suited to the characteristics of the area of the investment process in which action is to be taken. This modality may range from an imperative action to a merely indicative one, depending upon the characteristics of the decision making units in question, and the magnitude and speed of the change which is to be brought about.

63. In addition to selecting the areas of the investment process which are to be the special concern of the public sector, and to weighing the relative proportions of direct and indirect action to be taken in each, decisions must be made in relation to the intensiveness, extent and scope of the role to be played by the public sector. Figure 4 illustrates one hypothesis concerning the possible results of an increasing public intervention on the investment process. Beginning from zero, the public sector could begin to take action in a few projects and could then gradually expand its influence. The effects of such public action would not have any tangible results as regards the investment process in the beginning; only after a "critical number" of projects had been reached would the first positive effects be seen. If the scope of action remains below this threshold level it may be insufficient. From this point onwards, any increase in the number of projects subject to such action could have increasingly positive effects. If it continues to
INTERVENTION IN THE INVESTMENT PROCESS

RELATIVE LEVELS

Note: Adapted from ILDES, "La Planificación del Desarrollo Agropecuario", Siglo XXI, 1977.
grows, however, it is quite likely that a point will be reached where this type of action will become less flexible and less effective and may begin to hinder the investment process, thus ushering in a phase of decreasing returns. The illustration of this hypothesis shows the benefits in terms of quality, quantity and timing vis-a-vis the costs of direct action. It is thus possible to determine a range of public action which would avoid the unproductive efforts associated with a very limited scope of action as well as the paralysing effects of excessive intervention.

64. Even a more interventionist approach should be selective in scope, and in practice the analysis of the impact of policy will always be partial. After all the issue addressed is planning in mixed economies, in which the bulk of economic activity continues to be coordinated through the market and much of the detail is of no great concern to government.

65. The important point in this connection, however, is to distinguish two quite different meanings of planning. On the one hand, the orderly and systematic formulation and monitoring of a course of action; on the other hand, decisive or effective intervention. In this sense, a useful distinction can be made in describing government economic work as between routine and strategic planning.

66. Routine planning involves the systematic application of economic and administrative logics to the detailed day to day decision of government. Planning in this sense should be built into the decision making structure at the appropriate levels, with the necessary data support systems and established criteria.

67. However, there is also a need for the government to make strategic choices both in relation to macro-economic policy, and in pushing for those changes in institutions and the policy
regime which it consider to be key elements to fulfill its political mandate. In this sense, strategic planning is addressed to a relatively narrow range of tasks to be put to the attention of top decision makers.

68. The implication in terms of institutional structures is that two types of planning capacity are required. In the line ministries, public agencies and the finance ministry there is a need for a working capacity to plan and monitor the implementation of detailed projects and programs; that is a routine planning and management capacity. There is also a need, at the center of the political system, for a staff capacity to identify the priority areas for analysis, and to advise the top political authorities regarding strategic actions and choices.