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CONTENTS

Part One

WORLD INFLATION AND LATIN AMERICA

Chapter	*Page*
I. INFLATION IN THE DEVELOPED COUNTRIES: CRITICAL POSITION IN RESPECT OF DIAGNOSES, THERAPEUTICS AND PROSPECTS	3
A. The crisis of diagnoses	4
1. The structural background	5
2. The mechanisms of dissemination	8
3. The conjunctural elements	10
B. The crisis of corrective measures	11
1. The original success but recent impotence of the Keynesian approach	11
2. Monetary orthodoxy (or heterodoxy)	12
C. The crisis of prospects	13
II. LATIN AMERICA AND "IMPORTED INFLATION"	15
A. Structural characteristics and vulnerability vis-à-vis imported inflation	16
B. Channels of transmission of imported inflation	17
1. Indirect internal propagation: general channels	19
2. The fiscal channel	21
3. Prices and wages and salaries	22
C. Economic policy options and instruments	24
D. Prospects and queries	25
III. RECENT INFLATION IN SIX LATIN AMERICAN COUNTRIES	27
1. *Bolivia*	27
A. Introductory note	27
B. Background to the nature and evolution of the economy	27
1. The general context	27
2. Main features of the evolution of the economy	29
C. The inflationary process in Bolivia	37
1. Perspective of periods and phases	37
2. Over-all view	38
D. Inflation and economic policy	48
1. The frame of reference	48
2. The main measures adopted	49
2. *Brazil*	52
A. Introductory note	52
B. Outstanding features of the evolution of the Brazilian economy	53
1. Evolution of the gross domestic product and its components	53
2. The bases for growth	54
C. Main features of anti-inflationary policy	61
1. The crash policy, 1964–1966	62
2. Growth with relative stability. The gradualist policy applied in 1967–1973	64
D. The recrudescence of inflation (1974)	76

Page

3. *Colombia* 83
A. Introductory note 83
B. Main features of the trend of the Colombian economy 83
1. Growth trends 83
2. The external sector 86
C. The recent inflationary process 91
1. Background 91
2. Factors which influenced the acceleration of the inflationary process . 93
D. Main features of anti-inflationary policy 101
1. General remarks 101
2. Stabilization measures 101

4. *Costa Rica* 108
A. Introductory note 108
B. Recent economic trends 108
1. The external sector 108
2. The evolution of total supply and demand 114
3. The product and its sectoral structure 118
C. Appearance and acceleration of inflation 120
1. The general context 121
2. Indicators of levels of inflation 121
3. Disparities in price increases 122
D. The phases of inflation 124
1. Inflation in 1970-1971 124
2. Inflation during the period 1972-1973 127
3. Inflation in 1974 130
4. The peculiarity of inflation in Costa Rica 131
E. Inflation and main economic policy measures 131
1. Public sector financing policy 131
2. Private sector financing 133
3. Foreign exchange policy 134
4. Prices and wages policy 135

5. *Ecuador* 137
A. Introductory note 137
B. Salient features of economic trends in Ecuador 137
1. Growth trends 138
2. The external sector 141
C. The recent inflationary process 145
1. Background 145
2. Factors which influenced the speeding up of inflation 146
D. Principal aspects of anti-inflationary policy 154
1. Background 154
2. Basic policies 155
3. Complementary policies 156

6. *Uruguay* 158
A. Introductory note 158
B. Longer-term prospects: stagnation and inflation 159
1. Background 159
2. Origins of inflation: structural factors and propagating mechanisms . . 162
3. Stabilization efforts up to 1971 164
C. The period 1972-1974: reactivation of the movement of prices and imported inflation 168
1. The general setting 168
2. Internal factors of inflation 171
3. Imported inflation 172
4. Additional aspects of anti-inflationary policy 175

Part Two

THE LATIN AMERICAN ECONOMY IN 1974

Chapter	*Page*
I. GENERAL TRENDS	177
1. An over-all appraisal	177
2. Economic growth in 1974	178
3. The persistence and extensiveness of the inflationary process	180
4. The external sector	182
(*a*) Latin American trade	182
(*b*) The Latin American balance of payments in 1974	187
(*c*) Inter-Latin American trade	191
II. THE ECONOMIC SITUATION BY COUNTRIES	195
Argentina	195
Barbados	209
Bolivia	212
Brazil	218
Colombia	223
Costa Rica	229
Chile	235
Ecuador	248
El Salvador	253
Guatemala	258
Guyana	264
Haiti	267
Honduras	270
Jamaica	275
Mexico	278
Nicaragua	291
Panama	297
Paraguay	303
Peru	308
Dominican Republic	319
Trinidad and Tobago	324
Uruguay	327
Venezuela	331

NOTES AND EXPLANATION OF SYMBOLS

The following symbols have been used throughout this Survey:

Three dots (...) in the tables indicate that data are not available or are not separately reported.

A dash (–) indicates that the amount is nil or negligible.

A minus sign (–) before a figure in a table indicates a deficit or decrease, unless otherwise indicated.

A plus sign (+) indicates an increase.

A full stop (.) is used to indicate decimals.

A slash (/) indicates a crop year or fiscal year, e.g., 1969/1970.

Use of a hyphen (-) between dates representing years, e.g., 1960-1970, normally signifies an annual average for the calendar years involved, including the beginning and the end years; growth rates refer to the cumulative annual rates for the whole period, including the beginning and the end years.

References to "tons" indicates metric tons, and to "dollars" United States dollars, unless otherwise stated.

Figures and percentages in tables do not necessarily add up to the totals, because of rounding.

Part One

WORLD INFLATION AND LATIN AMERICA

The object of this part of the *Economic Survey* for 1974 is to analyse some main aspects of world inflation, especially in relation to the industrialized countries and Latin America.

The importance and topicality of this subject are too evident to make any justification of its examination necessary. All over the world, peoples and Governments are concerned at rising prices and at the economic and social consequences of inflation. This concern is felt even in the socialist areas of the world, although perhaps only in regard to inflationary pressures that may be transmitted from the exterior. Table 1 illustrates the spread or, as we have called it, the "internationalization" of rising prices and the growing intensity of this phenomenon in the period 1973-1974, although as we shall see there are some interesting exceptions, especially in the case of certain African countries.[1]

Another feature of this state of affairs, which is unusual for many reasons, is that the problem under discussion goes hand in hand with another which is perhaps even more important: the loss of impetus and perhaps even the contraction of the central economies, which, like inflation, is threatening to extend its effects to the rest of the countries that are linked with and dependent on the central countries in various ways. Furthermore, it is well known that the relative significance of each of these questions tends to change with the passage of time. Thus, for example, whereas in mid-1974 it seemed clear that inflation was considered the outstanding peril,[2] towards the end of the first quarter of 1975 (i.e., the date of preparation of the present document) the main danger was economic stagnation and unemployment.

Both these factors are intimately connected, and a full analysis of the present situation would involve going into both of them in depth simultaneously. Unfortunately, this is outside the scope of the present study, although it may be recalled that in the *Economic Survey* for 1971 some hypotheses were considered regarding the weakening of the forces of expansion in the industrialized market economies.

We will therefore limit ourselves to discussing inflation, although without forgetting that inflation must be located—especially in the present situation—within a much broader context than that formed by the variables which are usually dealt with or combined in specific studies on this matter.

In chapter I we will consider the picture presented by the central economies, concentrating our discussion on the obvious and generally recognized crisis of diagnoses, corrective measures and prospects which affects thinking and action on inflation.

In chapter II we will deal with the impact on Latin America of the so-called "imported inflation" of recent years, describing its various aspects, the particular form they take in certain countries, and the main lines of existing or possible policies.

Chapter II is actually based on the observations made in the analysis of six specific countries (Costa Rica, Colombia, Ecuador, Brazil, Bolivia and Uruguay), which make up the third and last section of Part One of the present *Survey*.

[1] Leaving aside the problems connected with statistical criteria and coverage, it may be assumed that the seriousness of the repercussions of external inflation will depend basically on (*a*) the size of the sector which operates on a relative or absolute subsistence basis; (*b*) the degree of openness of the economy towards the exterior; (*c*) the structure of exports and imports; and (*d*) the internal policies applied to absorb or cushion price rises. This subject will be dealt with further in chapter II.

[2] At the Meeting of Governors of IMF and IBRD, the Managing Director of IMF stated that "inflation is the top economic problem all over the world". Press Release No. 3, 30 September 1974.

Table 1. Acceleration of the inflationary process
(Annual rates of variation of consumer price indexes, as between annual averages)

	1965-1970	*1972*	*1973*	*1974*
Developed countries				
Japan	5.5	4.8	11.7	22.7
Italy	3.0	5.7	10.8	19.1
United Kingdom	4.6	7.1	9.2	16.0
United States	4.3	3.3	6.2	11.0
Norway	4.9	7.2	7.5	9.4
Netherlands	5.0	7.8	8.0	9.7
Federal Republic of Germany	2.4	5.5	6.9	7.0
Developing countries				
Asia:				
India	6.8	5.8	17.4	27.3
Indonesia	...	6.7	31.5	40.4
Philippines	6.0	10.3	11.0	34.4
Thailand	2.6	4.0	11.7	23.3
Iran	1.4	6.5	9.8	14.0
Africa:				
Ghana	3.4	13.5	10.2	23.2
Burundi	2.3	3.6	6.0	15.9
Kenya	1.8	5.7	9.3	17.8
Zaire	24.6	15.5	16.0	29.5
Nigeria	5.6	2.8	6.0	17.1
Zambia	6.2	5.4	6.4	9.2
Morocco	0.6	3.7	4.1	14.4
Latin America				
Long-standing inflation:				
Chile	26.0	79.0	351.6	504.7
Uruguay	59.9	76.5	97.0	77.2
Brazil	29.0	16.7	10.9	27.2
Argentina	19.3	57.8	61.5	23.5
Irregular inflation:				
Bolivia	5.9	6.5	31.6	62.8
Colombia	10.0	14.3	22.8	24.4
Ecuador	4.7	7.9	13.0	23.3
Peru	9.8	6.9	9.5	16.8
Recent inflation:				
Guatemala	1.5	0.6	13.8	16.9
El Salvador	1.1	1.5	6.4	16.8
Paraguay	1.3	9.2	12.7	25.2
Mexico	3.5	5.0	11.3	23.0
Honduras	1.7	3.7	6.0	13.8
Dominican Republic	1.2	7.9	15.1	13.1
Costa Rica	2.5	4.7	15.2	30.1
Caribbean countries:				
Barbados	4.1	11.8	16.9	38.9
Guyana	2.6	5.0	7.5	17.2
Jamaica	5.3	5.8	19.9	26.4
Trinidad and Tobago	3.9	9.3	14.8	22.1

SOURCES: IMF, *International Financial Statistics*; United Nations, *Monthly Bulletin of Statistics*.

Chapter I

INFLATION IN THE DEVELOPED COUNTRIES: CRITICAL POSITION IN RESPECT OF DIAGNOSES, THERAPEUTICS AND PROSPECTS

In starting this examination, it is desirable to keep two significant aspects in mind: firstly, that the upsurge of inflation in the last two years has roots which go back through almost the entire post-war period, and secondly, that the motive force behind the process, contrary to what is often believed or stated, is located in the industrialized economies.

With regard to the first point, it is well known that the industrialized countries have been showing a persistent tendency towards rising prices, which first became noticeable in the 1960s with an average annual rate of increase of 3.4 per cent and speeded up markedly in the first years of the present decade (7 per cent in 1972, around 12 per cent in 1973, and over 15 per cent in 1974 with respect to the previous year).[3]

From this point of view, the generalized and active inflation of the present time must be viewed as a result of or perhaps a qualitative change in a process which had been taking place and building up reactions and expectations for a long time past. This observation is important for the examination of the various diagnoses, as we shall see later.[4]

As regards the second aspect, i.e., that of the predominant influence of the central economies, it should be clearly understood from the beginning that this does not mean that this influence explains or acts as the determining factor in every case, or, above all, every degree of inflation in the peripheral countries. This is too obvious to require further discussion.

It is justifiable, however, to hold that the "world tendency" towards the resurgence of inflation originated in the leading industrialized countries. Correspondingly, it would be superfluous to point out that the cases of inflation in the peripheral countries, even in such outstanding cases as certain Latin American countries, have had little or no influence in this general trend.[5]

In order to provide more concrete proof of this assumption, all that is necessary is to bear in mind what was stated by the President of the World Bank regarding the increase in the prices of exports of industrial goods: "There has, of course, been a significant acceleration in the rate of inflation in the developed nations. It began before the rise in the prices of petroleum and other primary commodities, and it is only partially explained by them. International prices, which had risen only 6 per cent in the decade prior to 1968—less than 1 per cent per year—have risen at an annual rate of nearly 10 per cent in the five years since."[6]

This aspect of the problem is worthy of emphasis, because it is obvious that the importance within the over-all picture of the increase in the prices of primary commodities in general and

[3] See the statement made by Mr. H. J. Witteveen, Managing Director of the International Monetary Fund, before the American Economic Association in San Francisco on 28 December 1974. The figure for 1974 is taken from OECD, *Economic Outlook*, No. 16, December 1974.

[4] The evolution of the rate of inflation and its relationship with the growth rate are reflected in the economic terms used to describe the phenomenon in the English-speaking industrialized countries, where a distinction is drawn between creeping inflation, trotting inflation, stagflation and slumpflation. Of all the main countries of OECD, in 1974 only Canada and France showed what could be called growthflation, and even in those two cases the rates of inflation were higher and the growth rates lower than in previous years.

[5] "It seems beyond question that controlling world inflation is conditional upon controlling inflation in the industrialized countries. Any change in monetary parities and any programme of domestic monetary stabilization in the main industrial countries can exert an influence on the flows of finance at the world level." (Denis C. Lambert, "*Structuralisme et monétarisme. Les inflations oubliées d'Amérique du Sud*", *Economie Appliquée*, 1974, No. 1.)

[6] Statement by Mr. R. McNamara at the Meeting of the Boards of Governors of IMF and IBRD, 30 September 1974.

petroleum in particular has come to be exaggerated.[7]

Following this line of thought, it is reasonable to assume that the intensification and wider spread of inflationary pressures will bring about still greater disturbances in the economies of the peripheral countries, while at the same time they will find it more difficult to take defensive measures against these problems. The first reason for this is that the considerable changes in their levels and systems of prices will not be accompanied, in general, by the elaborate compensatory machinery which gives various degrees of protection to those affected by these changes in the industrialized countries. It is sufficient, for example, to think of the many protective arrangements in the central countries which look after the level of wages and the situation of those who may lose their jobs. Unemployment insurance and allowances are an example of this.

The second reason is that inflation itself is either a new problem for many of the peripheral countries, or else it is a very long-standing problem, at various levels of latency, which releases vigorous and deep-rooted forces and propensities as soon as there is some change in the equilibrium. It may be noted in passing that even the oil-exporting countries, which are obviously in a more favourable position than the others, are facing very complex problems as regards the manner of managing their very large amounts of foreign exchange in such a way as to avoid releasing uncontrollable pressures on price levels (some of these difficulties, as they affect Ecuador and to a lesser extent Bolivia, will be dealt with below).

All the foregoing leaves aside another question of vital importance: the fact that this time, in the great majority of the countries, the spread of inflationary pressures is not accompanied by any reflex effects—through trade and financial flows—tending to give a boost to the economies of the central countries. On the contrary, the shadow of stagflation is looming over the peripheral countries.

It is hardly surprising, then that the developing countries view with apprehension the picture which has emerged in the developed market economy countries as a whole.

A. THE CRISIS OF DIAGNOSES

The very special nature of the phenomenon of inflation in recent years has severely challenged traditional approaches to this matter, both as regards the diagnosis of inflation and its causes and as regards the corrective measures to be applied.

With regard to the first element, perhaps the most striking feature is what Professor Paul Samuelson has called the crisis of monistic explanations, i.e., the search and preference for a single dominant or responsible cause. In actual fact, however, "the explanation of the varied pattern of ongoing experience calls for a bold combination of causations".[8] Moreover, it is usual to refer to a wide variety of causes of very different nature and importance which cannot be combined into an integrated and coherent explanation of the phenomenon.

The problem, then, is to disentangle, arrange and organize the mass of factors which simultaneously, successively or in turn have been giving the inflationary process its body and rhythm.

There is no need to stress the magnitude of this task and the caution with which it must be approached. It may well be, however, that Latin America's long and rich experience in this matter will enable it to make a contribution to this process, especially as it has been accompanied by an active intellectual discussion which continues to take place.

Indeed, there are numerous references to Latin America in the analysis of this question in the central countries.[9] What was sometimes considered previously with some disdain as an eccentricity of the region or of a few countries in it, due basically to their indisciplined monetary and fiscal policies, has now come to hold particular interest because of the internationalization of the phenom-

[7] An illustration of the contrast of views on this matter is provided by the statements of the delegates of the United States and Iran at the Meeting of Governors of IMF and IBRD. Thus, the United States Secretary of the Treasury said: "Our current inflation developed from a combination of factors: in addition to pressures emanating from cartel pricing practices in oil, we have suffered from misfortune—including bad weather affecting crops around the world; bad timing—in the cyclical convergence of a world-wide boom, and bad policies—reflected in years of excessive government spending and monetary expansion", while the representative of Iran said that "the record shows that the inflationary spiral was spearheaded by the rapid rise in the prices of industrial products long before the increase in the price of oil . . . it is interesting to note that even at its present price the possible share of oil in this year's rate of inflation in the industrial countries, now estimated to reach about 14 per cent, is no more than an average of 1.5 per cent."

[8] See "Worldwide stagflation", *Morgan Guaranty Survey*, New York, June 1974.

[9] See, for example, the following statement in an important and much discussed article by Peter Wiles, "Cost, inflation and the state of economic theory", *The Economic Journal*, June 1973: "The presentation of very large wage demands that are absolutely certain to raise product prices and may perfectly well leapfrog each other forever is both quite new and universal in the capitalist world. Like hijacking and student power it originated in Latin America." See also Denis C. Lambert, "*Les inflations oubliées d'Amérique du Sud*", op. cit.

enon and the newly rediscovered complexity of its origins and processes.

From the point of view of the investigation of the Latin American situation, it is easy to distinguish right from the start a set of economic, social and institutional elements which form the foundation of the problem, the Procrustean bed in which pro-inflationary tendencies germinate and thrive with greater or lesser vigour depending on circumstances and policies. In short, it was the structural factors which the regional debate on this matter took up and considered with particular attention.

It would be a long and perhaps pedantic business to mention the many social scientists who have been stressing the significance of these aspects for some time past in the central countries, although it cannot be said that so far they have found much of an echo at the ruling levels and in academic circles.[10] This inclination, of course, is not limited to authors with more or less similar views. Professor Paul Samuelson, who thinks along quite different lines, stresses in an article already referred to of the "deep rooted structural changes here and abroad that have created a new bias towards inflation".

Obviously, the basic elements of different types which set their stamp on or feed the inflationary potential are not the same in the industrialized economies as in Latin America and other parts of the peripheral area. Neither the rigidity of agricultural structures, which is characteristic of some Latin American countries, nor the vulnerability of depending almost exclusively on a single primary commodity export, which is something that affects most of the countries of the region, are among the aspects that are of major concern to the central countries. At the same time, however, as we shall see, there are some aspects which are familiar to any Latin American country, and especially those with a long tradition of inflation.

Clearly, the methodological differentiation of the outstanding factors or levels in the diagnosis of inflation does not involve groups of relatively independent phenomena, and still less is there any unilateral type of causation among the components. On the contrary, the actual process involves the simultaneous and combined action of each group of elements and each single element, with their presence and importance depending on the characteristics of each country and each particular situation.

As the long-standing inflationary way of life of quite a number of Latin American countries shows, the basic structural or institutional factors, and even the mechanism of dissemination, are relegated to a temporarily secondary place in the phases of resurgence of the inflationary process, and the emphasis consequently shifts to the more immediate connexion and pressures, such as the prices-wages race. As the experience of the region also shows, however, the proper control of the process, even within a scheme of tolerated and manipulated inflation, calls for parallel action on the various different planes. From this point of view, as we shall see later, the Brazilian experience is of particular interest, and it has frequently received the attention of the central countries who are facing the difficult problem of how to overcome or live with inflationary processes. This brings us to the following topic.

1. *The structural background*

Subject to the risk involved in making any kind of classification, and without pretending that the classification is complete or implies any order of priority, certain factors or groups of factors of outstanding importance can be identified from the examinations made in the central countries.

Firstly, there are three elements which can be taken together for the purposes of the analysis and in the interests of brevity. These are the passage of an extraordinary long period of dynamic growth (by past standards), which has taken place in conditions of virtual full employment and on the basis of growing concentration and organization of the key social groups, including of course the State. Together with and above these facts is a definition of economic policy (and policy in general) which is unequivocally committed to the first two features—growth and full employment. We shall return to this aspect later.

Before going any further, it is essential to emphasize the differences between this picture and the image and reality of what may be called "nineteenth century capitalism". While this was undoubtedly dynamic over a long term, one of its primary characteristics was its cyclic irregularity. With the passage of time it was evident that the labour force became more fully employed and its income rose, but waves of unemployment, sometimes on a massive scale, and a stubborn residue of unemployment remained an indisputable feature of this system. Finally, taking into account all the variations of individual cases and situations, as well as the emerging trends, there was the system of free or imperfect competition, i.e., of the "open market" for labour and the lack

[10] Among them, however, mention may be made of J. K. Galbraith in the United States, *Economics and the Public Purpose* (Boston, Houghton Mifflin, 1973); F. Perroux and his followers in France, "*L'inflation des années 60*", *Economie Appliquée*, No. 2, 1971; and Gunnar Myrdal in Sweden, "*Against the Stream: Critical Essays on Economics*" (New York, Pantheon Books), 1973.

of organization or incipient organization of the wage-earners. All this took place under a relatively weak State which limited its activities to maintaining law and order, palliating the most dramatic hardship situations, and defending and promoting national interests.

It should be noted that the negative sides of this contradictory reality were vital ingredients of its functioning and expansion. In other words, the periodic crises, the rises in unemployment, and the bankruptcy and failure of enterprises at periods of depression and low prices were, as has been pointed out more than once, the harsh but, it was felt, necessary means for "clearing the decks" of the system and making way for its next growth cycle. Government intervention, of course, was conspicuous by its absence, and it was even considered undesirable, since it was felt that it could hamper the operation of the laws of the market.

To a considerable extent, as we have already seen, this "world of yesterday" had little or nothing to do with the reality which took shape and became consolidated in the war and post-war years in the central economies, although a purist could argue that the essential nature of the system of private property, profit and the market has not been changed. However, the implications of this change for the problem under discussion here are obvious. Each of the new elements referred to above contains inflationary possibilities, and the combination of them obviously strengthens this predisposition.

(a) *Growth and inflationary potential*

By its very nature, a prolonged period of expansion—even with brief, scattered and local pauses like the contractions referred to earlier—implicitly contains such a potential and calls for constant changes—in some cases of considerable extent—in the structure of production in keeping with variations in levels of income and patterns of demand or spending. The "signals" from the market and profitability, on the one hand, and public initiatives on the other, are hypothetically responsible for channelling and redistributing resources with the objective of structural readaptation, but any fault in the timing, objective or magnitude of the allocations will result in imbalances of varying importance and duration which usually manifest themselves in the form of partial or general rises in prices if there is a suitable mechanism and suitable conditions for its transmission.[11]

From another point of view, the problem is also related to the eventual tendency to rising costs in every process of lasting expansion. This may be due to various causes, such as the higher marginal cost of the factors used (for example, raw materials coming from deposits of lower content or further away), a higher density of investment per unit produced (which could be counteracted or aggravated by the prices of capital goods), or a number of other elements (scarcity of labour, higher taxes, high interest rates, etc.). This aspect is summed up in the diagnosis on overheating of the economy.

Although there have been many references to this point based on many specific cases and situations, the truth is that—especially as regards the United States—the available evidence does not seem to confirm that the expansion of the central system has run into real limits that make it difficult to achieve further progress without abnormal inflationary pressures. For the United States, however, the margin between the "potential product" and the product actually achieved grew considerably narrower between mid-1972 and the beginning of 1973, after having been quite wide between 1969 and the beginning of 1972.[12]

In other words, the key inflationary element may not have been excessive over-all and generalized demand on the available resources, but rather the inter- and intra-sectoral imbalances deriving from rapid growth and the postponement or total absence of decisions aimed at anticipating or remedying these problems.

Lastly, this aspect of sustained growth and its relationship with inflation can also be viewed in connexion with a characteristic of modern economies in which there are interesting similarities between the market economies and the socialist or centrally-planned economies. Furthermore, it may be noted that it is connected with one of the main lines of analysis of ECLA.

Thus, in contradiction of assumptions which were deeply rooted in academic circles up to the 1930s, the dissemination of the benefits of technical progress deriving from a period of dynamic and lasting growth has taken place principally through the increase in income and not through the reduction of prices.

[11] In this connexion, the following appraisal of the difficulties anticipated in reactivating the growth of the OECD countries is of interest: "Important sectoral differences have arisen, with capacity still strained until recently in some industries (steel, coal, chemicals) but with large slack developing in others (automobiles, textiles, house building, tourism). The unused capacity partly reflects weakness of aggregate demand but is probably also, in part, the result of recent large changes in relative prices. It is not yet clear, given the coexistence of bottlenecks and of slack which may partly be structural, how far the rate and pattern of future expansion both in the short- and medium-term will need to be modified." OECD, *Economic Outlook*, December 1974.

[12] See First National City Bank, *Monthly Economic Letter*, November 1974.

This point calls for some clarification. It is beyond any doubt, of course, that the technical advances and mass production achieved in certain lines (automobiles and television sets, for example) was generally followed in the central countries in the past by appreciable reduction in prices. This was a precondition for their generalized dissemination, quite apart from another fact of primary importance: namely, that the *average* levels of income should make such goods accessible to the majority of the population.

It is none the less evident, however, that once this stage of the opening and widening of the market was completed, the prices of the products of the industrial society did not continue to go down in keeping with the growing "physical" or real productivity (brought about by improvements in technology and economies of scale). The reason for this is very simple, and has been set forth in analyses based on the most diverse doctrines: what happened was that there was preferential and sometimes total appropriation of the benefits of technical progress by those participating in it or controlling the increases in productivity.[13]

In principle, and in itself, this closed or preferential appropriation of the benefits of increased productivity would appear not to have any great influence on inflationary pressures except when it does not permit trends towards lower prices to come into effect. The truth is, however, that it is necessary to take into account the incidence of the relative improvements of income over other groups and the reactions of these latter groups aimed at eliminating or decreasing the gap thus opened. In other words, what we are faced with is the old "demonstration effect", but this time in the domestic conditions of the industrialized countries. In order to go deeper into this matter and into its projections it is necessary to bear in mind the changes which have taken place in the negotiating power of the social groups. This we will do below.

(b) *Full employment and "oligopolization"*

It is hardly necessary to stress the influence of a situation of virtual full employment on the inflationary phenomenon. Many, of course, have pointed to this as the main element in tendencies towards price rises, because of the strengthening of the negotiating capacity of wage earners in situations of very low unemployment. The often-mentioned "Phillips curve" related the movements of wages to levels of employment and made it clear that, at least in British experience, increases in the former had depended mainly on the state of the latter, i.e., wages tended to rise in accordance with improvements in the employment situation. This seemed to justify a very widespread and generally accepted hypothesis.[14]

At all events, this element must be appraised in conjunction with the third factor referred to at the beginning of this section, namely, the increasing concentration and organization of the key social groups. Once again, it would be superfluous to refer to or quote the abundant literature on this matter, which goes all the way back to the writers who anticipated the tendencies towards entrepreneurial concentration and the disappearance of the atomistic structure which predominated for much of the last century and perhaps even up to the great depression. Obviously, of course, these writers did not foresee or include in their analysis the implications of the agglutination and parallel development of the trade associations and the State apparatus.

What we are dealing with is a phenomenon which is just as inevitable as it is irreversible, which has continued unchecked in spite of legislation and other expedients, and which, we may add, is still obscured by the insistence on viewing it through the eyes of the old monopoly theory instead of considering it as a structural reality of the modern industrial economy.

The combination of full employment and of the so-called "oligopolization" of large sectors where the State is an interested party as well as an uncertain arbiter introduces another markedly inflationary bias or propensity.[15]

The most recent experience (first quarter of 1975)—above all in the United States, where there has simultaneously been an unusually high level of unemployment and a serious contraction in production activities—is an eloquent testimony to

[13] The international response to this phenomenon is the retention by the central economies of the gains made through increased productivity, which operates through changes in the terms of trade. Among recent work by ECLA on this matter, see Part One of the *Economic Survey of Latin America, 1973* (E/CN.12/974).

[14] Recent experience has cast some doubts on this relationship, although from another aspect: i.e., that increases in levels of unemployment do not necessarily signify a drop in the rates of remuneration of the employed population.

[15] Analysing this matter, G. Myrdal noted the following: "The entire system of organizations in a society is in all countries grossly biased [in favour of inflation], and this becomes increasingly important as organizations are also becoming stronger. People are becoming organized as income earners of various sorts or as profit takers, while organizations defending the general and common interest of all as consumers are weak in all countries. The interests of salary-earning employees and of profit-earning employers are not always conflicting. While within an ongoing inflation development the former rationally have to count on higher costs of living and to press for higher wages, the latter can in the same way often count on higher prices for their products or services." (See *Against the stream*, op. cit.)

the considerable resistance to a drop in remunerations and, to a lesser extent, in prices, brought about by the institutional conditions referred to.

Taking the foregoing realities as a whole, a hypothesis has also arisen regarding the "functionality" of inflation as a means of smoothing down antagonisms and achieving certain cardinal objectives for the economic system. On the one hand, the increase in income achieved by certain groups reduces their pressures to reach or recover certain given levels, but on the other hand, the increase in prices soon reduces the real significance of these apparent gains.

This is not all, however. To the extent that more or less generalized increases in remunerations exceed the increases in productivity and diminish the resources needed by enterprises for their renewal and/or expansion, the increases in prices have the effect of making good this deficiency by, for example, redistributing income in favour of the enterprises.

From this point of view, inflation could be considered not as an abnormal phenomenon, but rather as a mechanism that helps modern market economies to function. Naturally, this analysis does not deny that the process also involves serious disturbances in the progress of the system, which have been adequately dealt with in the literature on this problem.

(c) *The internationalization of the processes*

The second group of basic elements in the inflationary tendency seems to be linked to the process of world economic integration and particularly to the process of integration between the central countries. We will not enlarge on this general aspect, since its characteristics and tendencies were fully presented in the *Economic Survey* for 1971.

The last few years have of course witnessed an extraordinary acceleration in this integration process, and a considerable degree of synchronization has now been established in the behaviour of the central economies. In the past, it was frequent for their growth rates and domestic price movements to show significant differences. Thus, more than once the effect of a reduction in the growth rate of the United States, for example, was counteracted to some degree by continued expansion of the European area or Japan, and although prices tended to rise, there were also considerable differences which moderated this long-term trend.

It will readily be understood that the new situation involves an obvious possibility of the intensification and multiplication of any tendency towards inflation or deflation, expansion or depression. Moreover, as has been stated on a number of occasions, it makes it more unlikely that isolated action at the national level can succeed.[16] Indeed, it could be maintained that such action is actually undesirable in view of the possibility that arbitrary measures designed to isolate specific economies from general difficulties may actually help to aggravate the situation of other countries and finally that of the world economy in general. The experience of the 1930s provides typical examples of this.

2. *The mechanisms of dissemination*

In the Latin American inflationary situation, the machinery and decisions of the fiscal, monetary and foreign trade areas have constituted, so to speak, the second line of elements which effect the rise in prices. More specifically they have generally been considered as "propagating factors".

This is not the place to go again over the foundations of this general hypothesis, which has been opposed and criticized in favour of other interpretations. It is sufficient to repeat two considerations which are of basic importance for the discussion. The first is that obviously the measures taken in one of those fields or in a combination of them can be identified as visible agents of inflationary imbalance (and price rises). The second is that only rarely can they be considered as really independent or as true sources of the expansive effect. There is nearly always a more distant reason which is responsible for or encourages the decision on one or all of these fronts. We shall return to this point later.

As regards the possible influence of fiscal and monetary policies on the impulsion of the inflationary process, the industrialized economies are too varied in their characteristics and in time to enable any generalization to be made. The most

[16] Consider this view of the matter: "The worldwide character of recent price and wage advances has inevitably focused attention on inflation as an international phenomenon. The authorities in the industrial countries have found internal stability threatened by inflationary forces from abroad. Increasingly, international factors: the expansion in world trade and investment flows, the official efforts in recent decades to eliminate restrictions on private current-account and capital transactions, the growth of multinational corporations and the development of international banking facilities ... have limited the effectiveness of national programmes to protect the internal economy from external disturbances ... In this environment, it no longer seems to make sense to view inflation merely as a collection of individual national phenomena." (Samuel Katz, "Imported inflation and the balance of payments", *The Bulletin*, New York University, Nos. 91-92, October 1973.)

that can be done is to make general appraisals like the following:

> "... The 1972-1973 upsurge of global demand was marked by failures or miscalculations in the conduct of monetary and fiscal policies. In relation to the buoyancy of private demand that materialized during the boom period, fiscal policies proved insufficiently restrictive in a number of instances, and rates of monetary and credit expansion permitted by prevailing monetary policies would have to be characterized as excessive from the standpoint of controlling inflation. However, since broadly parallel judgements are applicable also to the boom phases of other major post-war business cycles, it cannot be taken as a certainty that laxity of monetary and fiscal policies contributed more to the excesses of the latest boom than it did to those of previous upswings."[17]

There can be little doubt that this cautious appraisal of the role of the fiscal and monetary mechanisms would not be shared by the defenders of the thesis that this is precisely where the basic impulses for inflationary pressure are to be found. It is clear, however, that the experience of recent years, even in Latin America, has reduced the degree of emphasis of former positions.[18] Thus, recent discussions show a subtle shift of judgement regarding the role of monetary expansion. Whereas in previous explanations this factor was given as the primary cause of inflation, in more recent discussions it is held that it would merely be decisive in making possible the continuance of the phenomenon, which is an obvious reflection, but which fails to shed light on all the antecedents and consequences implicit in such a statement.

From this point of view, it is true to say that the alternative criteria have become considerably more realistic than in the past. At all events, whatever the extreme criteria regarding this matter, it seems clear that while the "independent" or original gravitation of monetary and fiscal action is neither certain nor demonstrable, it is not reasonable either to think that these factors have responded to or permitted, as some would say, the manifestation of the underlying forces favouring expansion on these two planes.[19]

(a) *Transmission via the foreign trade deficit*

There remains to be considered the influence of the action taken in the foreign trade area, which must be appraised in the light of what we said before about the internalization of the problem of inflation.

There are many elements to be considered in regard to this question, but in the interests of brevity we will concentrate on the aspect which was emphasized most strongly in the debate, namely, the possible impact of the United States balance-of-payments deficit.

While the incidence of this phenomenon on international monetary equilibrium cannot be ignored or underestimated, there is some doubt as to whether it has really been a decisive factor in the inflationary tendencies of the central economies and the world as a whole.[20]

In reality, the available figures do not confirm this assumption. Up to at least 1973 the ratio between the availability of international reserves and the magnitude of world trade--which is one of the generally employed indexes--went down compared with the situation in 1960 and 1965. In contrast, because of the rise in the prices of primary commodities and particularly oil, the reserves of the developing countries showed greater relative growth, and this, although it was undoubtedly an important factor in internal inflation, certainly did not carry much weight at the world level.

It is true, however, that one of the outstanding phenomena of recent years has been the increase in the amount of monetary assets in private hands: Eurodollars, for example. From this point of view

[17] IMF, *Annual Report, 1974*. Regarding the United States, which is the country most often quoted in this respect, it is also worth considering the opinion of the November 1974 *Monthly Economic Letter* of the First National City Bank, which states that government spending advances have been modest over the past two years and monetary policy has been restrictive as the authorities have refused to validate double-digit inflation by allowing the money supply to grow fast enough to accommodate both the inflation and a rise in real output.

[18] The prudence of present appraisals is to be contrasted with the tone of the recommendations which used to be made in the 1950s and the beginning of the 1960s regarding stabilization policies in Latin America.

[19] Professor Gottfried Haberler, in a recent article entitled "Inflation as a world-wide phenomenon: an overview", *Review of World Economics*, vol. 110, book 2, 1974, sums up the question very frankly in the following words: "... In my opinion it is evident that government finances (big budget deficits) and the pressures of the trade associations often exercise strong and sometimes irresistible political pressure on the monetary authorities to increase the supply of money either actively or permissively." He adds in a foot-note "H. G. Johnson calls this reproachfully and even contemptuously a political or sociological theory of inflation. Whatever you call it, it is a fact of life that cannot be ignored."

[20] H. G. Johnson, for example, sees long-standing inflation as "a world-wide phenomenon associated with excessively rapid growth of the monetary base of the international monetary system in the specific form of a rapid growth of foreign official holdings of dollars" ("Secular inflation and the international monetary system", *Journal of Money, Credit and Banking*, February 1973).

also, however, the figures do not back up the hypothesis of excessive international liquidity, and as an IMF document has stated:

> "World imports during the period examined [1954-1972] have grown more rapidly than world reserves, and the global ratio of reserves to imports has declined steadily from 1954 to 1970. The inclusion of private holdings does not modify this finding, although the downward trend becomes more stable."[21]

On the other hand, in connexion with the problem under consideration, it should be recalled that the two countries which accumulated most reserves of dollars, i.e., the Federal Republic of Germany and Japan, were among those which had most success in controlling their inflationary pressures (see table 1). The rise in prices in Japan since 1973 is due to the rise in the prices of commodities and oil. Likewise, insufficient attention has often been paid to the possible deflationary effect in the United States of that country's balances accumulated abroad, with the consequent substantial increase in its imports.

These and other facts go to prove the significance, as far as price rises are concerned, of domestic policies and of the factors which determine them.

There can be no doubt, however, that one of the primary consequences of the United States deficits was of decisive importance in the resurgence of inflation. We refer to the devaluations of the dollar from 1971 onwards. At the level of the international economy, these devaluations had repercussions which were substantially similar to those of changes in the exchange rate in countries affected by inflation, especially where such changes had been held up longer than was advisable and resulted in more violent price changes.

This does not, of course, refer only to the direct repercussions, but also to the transmitted impact of these devaluations on inflationary expectations.

(b) *An inflationary mentality?*

The last factor to be mentioned among the elements producing inflation is of a subjective nature, but it is none the less important, particularly at a time like the present. We refer to the dissemination and establishment of inflationary expectations.

In this matter, to which growing attention is being given, the anticipated price rise and the "inflationary psychology" take the form of a variety of expedients which, while trying to avoid the distortions and ill-effects of the process, can in fact actually make it deeper rooted and more intensive. In the words of a noted monetary authority:

> "As a result, we have shorter trade union contracts, linking of wages and social security benefits to the cost of living, flexible rules about interest rates, modifications in accounting practices, and other systems whereby price increases are passed on more rapidly than would be possible in other circumstances."[22]

3. *The conjunctural elements*

One of the clearest facts in the period 1973-1974 is the appearance on the scene of certain far-reaching conjunctural changes which exert a powerful effect on a situation where there is already a tendency towards the acceleration of inflation and which release pressures that were either latent or only weakly kept in check. In the analyses of the process which OECD has been carrying out,[23] it is shown that there is a regular sequence of impulses promoting price rises.

The first stage in the period in question can be located approximately between mid-1972 and October 1973, and is characterized by "a sharp rise in the price of most primary commodities relative to the general price level of all other goods, brought about by the emergence of a marked imbalance between final demand and current supplies". It will be recalled, for example, that the failure of the harvests in 1972 in some producer countries had particularly marked repercussions on the price of food-stuffs and hence on the wholesale and retail price indexes. It may be noted in passing that, generally speaking, it was developed countries—above all the Unived States and Canada—which were most favoured by this situation, although this does not mean that they did not suffer from the inflationary effects also.

The second dividing point is from October 1973 onwards, as a result of the Middle East War, the initial effect of which, according to the OECD study referred to, was to add a new element of uncertainty to the world situation, followed by physical shortages of oil arising from the embargo and from hoarding, plus substantial increases in oil prices.

While, from the point of view of the central countries, these two "moments" take the form of influences originating abroad, the third point corresponds to the internalization of the impacts

[21] See "Total international liquidity: economic devaluation and policy implications", IMF document EBD/72/196, 1972.

[22] Statement by the Managing Director of the International Monetary Fund, 28 December 1974, op. cit.

[23] See, *inter alia,* OECD "Aspects of world inflation", *Economic Outlook*, No. 15, July 1974.

and the predominance of domestic impulses. The fundamental aspect is probably the reaction of workers to prior considerable increases in prices. Thus ... "throughout 1973 ... a general acceleration in the rate of growth of wages took place in most OECD member countries and currently wages are going up extremely rapidly, although often not as rapidly as prices".[24] In other words, the centre of attention has now become the well known prices-wages spiral, which is a basic factor in the phases of acceleration of inflation.

B. THE CRISIS OF CORRECTIVE MEASURES

While it is beyond doubt that there is considerable confusion in the industrialized economies as regards the diagnosis of the resurgence of inflation, the situation is even worse when it comes to discussing ways to combat inflation.

The discussions show that the majority of those concerned are fully aware that times have changed and that old formulas are no longer suitable, but there is a marked shortage of opinions on how to deal with the new situation, and the suggestions that have been made are either subject to many criticisms or else raise fresh queries, perhaps of even greater scope, which introduce variables that clearly go outside the limits of the problem of inflation in the strict sense.

1. *The original success but recent impotence of the Keynesian approach*

The first aspect to be borne in mind is the general disenchantment with the policies that have governed—with various degrees of vigour and efficiency—the development of the central countries in the post-war era, i.e., the policies inspired by the Keynesian school. This involves two questions which are different but not contradictory.

On the one hand, there is no doubt that the policies which are generally called Keynesian, and which are based on the maintenance of effective over-all demand and full employment, mainly through government initiatives, have had considerable success in achieving their ends. The vigour and consistency of the growth during the period in question, the low rates of unemployment, and the steady rise in the standard of living (leaving aside any reservations regarding the "quality of life"), are an indisputable proof of this assertion.

Of course they are not the only explanation and cause of it. Among the other reasons, paradoxically enough, we should not forget the challenge and stimulus provided to the market economies by the expansion and the sustained development of a competitive area made up of the socialist or centrally-planned economies. Taking into account such factors as this only goes to corroborate, however, the fact that the policies in question were capable of coping with such challenges.

As far as inflation is concerned, the truth is that the Keynesian philosophy did not contemplate any special corrective measures, either because one of its principal hypotheses was that the system had a persistent tendency towards under-utilization of resources, including labour, or because the problem was not very serious during most of the post-war period. When this second aspect changes, attempts were made—above all in Northern Europe and to a lesser extent and with little success in Great Britain—to introduce or intensify the so-called "income policies" designed to discipline and guide movements of prices and wages. At all events, however, as already stated, in the last few years the operational efficiency and interpretative and regulative validity of the Keynesian heritage have been deteriorating.[25] Up to about the middle of the last decade, the prevailing Keynesian policies fluctuated between expansive and restrictive versions of the basic orientation. As soon as the growth rate slackened and the employment situation was endangered, the time came to take off the monetary or fiscal brakes so as to inject new impulses into the system. In contrast, when signs of "overheating" appeared and prices tended to rise, the rudder was swung to the other side, more through monetary discipline than reduction of fiscal expenditure, which is much more difficult to apply in the short term for very well-known reasons.

This operation had to take into account a third element, namely, the balancing of external accounts. Very fast expansion—at least in the conditions in which it was taking place—not only had repercussions on prices, but also manifested itself in growing balance-of-payments deficits.

There can be no doubt that this analysis is mainly valid for the United States and Great Britain, since several European countries have managed to face up to this dilemma much better,

[24] See "Aspects of world inflation", op. cit.

[25] In some ways this assertion corroborates that made by the Secretary of the Treasury of the United States when he set out the essence of the new situation very concisely in his statement in September 1974 at the Meeting of Governors of IMF and IBRD: " ... It is clear that most countries are no longer dealing with the familiar trade-off of the past, balancing a little more or less inflation against a little more or less growth and employment. We are confronted with the threat of inflationary forces so strong and so persistent that they could jeopardize not only the prosperity but even the stability of our societies."

both because they took into account the institutional factors of the problem and because there was greater continuity in the policies followed.[26]

Be that as it may, what is certain is that towards the end of the 1960s the compensatory effect of the systoles and diastoles of the system entered a period of decreasing returns and, in some cases, virtual impotence. If expansive instruments were used, then it was more likely that these would increase the rise in prices rather than impart greater dynamism to production. On the other hand, if restrictive instruments were put into effect, there was a clear possibility that the sluggishness of the system would be made worse and unemployment would rise, without this bringing any kind of commensurate relief as regards the rising price tendency.

In the presence of this dilemma, there are some main criteria regarding the action to be followed.

On the one hand, of course, there are the various different versions of the basic Keynesian doctrine, which has still not been replaced. Up to the end of 1974 the predominant voice was that of the supporters of resolute deflationary action, although the events in the United States, where the supporters of this line have significant influence, have cast doubts on the viability of such a policy in the present conditions of marked stagnation, rising unemployment and little relative effect on prices and wages.

Those who favour a turn in the opposite direction, i.e., towards economic reactivation, have in their favour the existing data and the lack of prospects of the present situation and policies, but obviously they cannot give any guarantee that the traditional remedies will give the desired effect and not prove to be simply another stage in the so-called "stop and go" policies, whereby they could merely amount to another impulse to inflation instead of bringing about the redynamization of the economy.

Leaving aside their differences, however, and the fact that the time factor is very important in the decisions to be adopted, there is a common conviction that the choice between inflation, growth and full employment must not imply any substantial sacrifice on the part of either of the two terms of the problem.

2. *Monetary orthodoxy (or heterodoxy)*

A second current which is doubtless less important than the foregoing ones but is of significant importance in certain academic circles is the so-called monetarist current. Although, at the present moment and in the corrective measures applied, it is close to the restrictive variety of the Keynesian doctrine, it calls for separate comments. The relative ineffectiveness of the approach previously in fashion has given the monetarist approach more currency, although it has still not been taken up in any central countries by the ruling circles. For this reason, rather than considering it an example of orthodox thinking, it should rather be considered as one of the current heterodoxies.

The monetarist criteria extend in various dimensions. On the most general level there is the contention that the economic system, if left to the free play of market forces and backed by a suitable but unspecified monetary policy,[27] would have achieved better results than the Keynesian orientations, and would have done so without inflationary tendencies.[28] We are unable to go here into a lengthy discussion of this point of view, but it is enough to point out that it does not take account of the past evolution of the system, the characteristics of which are recalled in previous pages, for it would be difficult to find any proof that the pre-war economy, which was free of all Keynesian interference, was "inherently stable" (see footnote 28).

[26] Referring to this first aspect, the OECD publication, *Economic Outlook*, No. 16 (December 1974) points out the following:

> "A number of smaller countries believe that they have, very usefully, supplemented overall demand management by a variety of policies ranging from partial measures like wage indexation or price controls to comprehensive price and incomes policies, with cases of close co-ordination of fiscal and incomes policies being of particular interest. There is evidence that such a "multi-policy approach" has often helped in combining steady and relatively fast growth with comparatively low price increases, and the countries practising it have felt able to react to the oil crisis in somewhat similar manner, reducing the depressive impact on real demand of the oil price increase while limiting the propagation of its inflationary influence through the wage-price spiral."

Time Magazine (14 February 1975) says: "With regard to the problem of the continuity of policy, it should be recalled that in the last four years the United States has in practice had nine different policies for facing the problems of inflation and growth."

[27] One of the basic proposals is that the supply of money should grow at a regular rate in keeping with the real increase in the product, so as not to introduce any disturbances of an inflationary or deflationary tendency.

[28] According to H. G. Johnson, who is one of the best-known spokesmen of this current, "In a sense the crux of the issue prevailing between Keynesians and monetarists is that while the Keynesian position maintains that the real economy is highly unstable and that the monetary management has both little relevance and little control over it, the monetarist position on the contrary is that the real economy is inherently stable, but can be destabilized by monetary developments, which therefore need to be controlled as far as possible by intelligent monetary policy." See *Inflation and the Monetarist Controversy*, North-Holland Publishing Company, Amsterdam, 1972.

On the other hand, and at a more concrete level, there is the criticism that policies inspired by Keynesian doctrines have generally intensified the tendencies in expansion or contraction phases rather than moderating them. Once again, as in the case of the continuity of policies, this reservation does seem to be quite valid as far as the experience of the United States and Great Britain in recent years is concerned.

But doubtless the most controversial aspect of the monetarist position is its characterization of the control of the supply of money as the main anti-inflation tool. In other words, for followers of this doctrine, price discipline can only be obtained if the supply of money is managed so energetically and parsimoniously as to obviate or make impossible a rise in prices.[29]

Although exceptions to this principle could be pointed out, above all as regards relatively short periods, its hypothetical validity can be accepted if (and this is a fundamental condition) the monetary authority is in one of the following two extreme positions: (*a*) it has absolute power to establish the amount of the increase in the supply of money, or (*b*) it has the complete backing of the authorities and is in a position to discipline and manage all the pressures that are exerted on it. It does not seem that anyone could advocate the first possibility in the light of the conditions of modern society. There therefore remains only the second one.

Taken in the abstract, there is no reason to reject it as a totally unrealistic proposition. If it is taken as a base, however, it will be found as one goes deeper into its significance and implications that the problem shifts from the strictly monetary sphere to other fields or variables outside that sphere.

Thus, when we have to admit the patent fact that the central banks do not have independent and complete control over the supply of money it becomes evident that their decisions are subject to the manner and the degree of success with which the many sources that originate the demand for means of payment are managed. Thus, the dominating factor will be the general spectrum of economic policy and the variety of elements which go to make it up. Essentially then, the decisions of the monetary authority simply give sanction to a reality which is substantially generated and formed outside its orbit, although this should not lead us to forget its important role as a "propagation mechanism" for various types of tendencies or as a key element in the allocation of resources in market economy.

If we contrast these observations with the experience of the central economies, it is easy to see that the monetarist view has come into collision with or had to accommodate itself to basic common circumstances such as the commitment to sustained growth and full employment, the strength and balance of the great social groups, the expansion of military and social security expenses, etc. In the final analysis these are the factors which have established the general spectrum of economic policy within which the monetary authorities must operate.[30]

C. THE CRISIS OF PROSPECTS

The forecasts of the central countries regarding the course of inflation in 1975 are very cautious and subject to all kinds of reservations.

Following the examination to which reference was made when we were dealing with conjunctural factors, it can be assumed that pressures originating in the exterior—mainly increases in the cost of primary commodities—will lose some importance, while endogenous elements will gain it, especially through wage claims aimed at recovering previous levels of real income.[31] Thus, while it is

[29] A sign of the times is that the dispute between supporters of shock treatment for stopping inflation and the "gradualists" has lost all significance. Today, it can be said, everyone is a gradualist, except the ultra-monetarists.

[30] Analysing the ups and downs of the monetarist position, H. G. Johnson made this very pertinent comment:

> "... the real motive force behind the rise of 'monetarism' (the quantity theory approach) in popular thinking in recent years has been the failure of the alternative Keynesian approach to deal effectively with the problem of inflation in concrete economic policy-making terms... the triumph of monetarism has been short lived in both countries [the United States and Great Britain], and the quantity-theoretic approach is again in popular eclipse, partly because in the euphoria of belated popular recognition the monetarists vastly exaggerated the potency—a different matter from the necessity—of monetary restraint as a means of stopping inflation once inflation is well under way, in terms of both the amount and the duration of the unemployment required to change inflationary expectations and therefore wage and price determination behaviour... when the chips are down the political process attaches a relatively low cost to inflation and a relatively high cost to heavy unemployment." See *Inflation and the Monetarist Controversy*, op. cit.

[31] In appraising this phenomenon, the most recent issue of *Economic Outlook* (December 1974), op. cit., stated the following: "By the middle of this year, 'wage claims' (in manufacturing) were approaching 20 per cent at an annual rate in the OECD area as a whole, though with considerable divergence between countries. To the extent that those claims are realised, manufactured goods prices will be under considerable pressure that could only partly be alleviated by a shift away from profits, a rise in productivity or a fall in imported input prices."

anticipated that the rise in the prices of industrial goods will continue at an indeterminate rate varying with the individual countries, the surest and most immediate relief from inflationary impulses will come from steadier and perhaps even lower prices for raw materials.

Various sources seem to confirm these forecasts. In one of them, for example, an analysis was made of the evolution of prices of various groups of goods in the United States during the whole of 1974.[32] If we take only the cases of raw materials and producer finished goods, then we see that whereas the prices of the latter continued to rise during 1974 (albeit slower than in 1973), the price levels of primary commodities began to show reductions from the middle of the year onwards, and by December had fallen by 5.8 per cent.

It is therefore easy to understand the reflection made by the spokesman for most of the Latin American countries at a meeting held at the end of last year: "The anti-inflationary measures of the industrialized countries are having more effect on the prices of primary commodities than on their own manufactures, whose upward tendency shows no sign of slackening".[33]

This imbalance which is so disturbing for the peripheral economies must be viewed in conjunction with another negative fact: that most observers are more optimistic regarding the possibility of containing or moderating the acceleration in price rises than in reactivating the economy within a short period or even in the next two or three years, which is the time given in some official estimates for the United States. In fact it is assumed that the first will be facilitated by the second, i.e., that a contraction, even though it may be quite relative compared with the growth rates of the previous period, will favour restriction of price rises.

Viewing the matter closely and in direct relation to the subject of this document, one unknown quantity is whether the great industrial economies will succeed in obviating inflationary pressures to a significant extent (returning, for example, to inflation rates similar to those of the early 1960s), or if they will have to resign themselves to merely stopping the present spiral and henceforth learning to live with inflation rates of around 10 per cent per year.

The forecasts are situated between these reference points, because in actual fact very few persons fear that the phenomenon will really get out of hand.[34] Whatever the situation which finally emerges, it seems certain that it will differ substantially from previous conditions. It will therefore be all the more necessary to renew conceptual frameworks, to start using other instruments, or to substantially modify the operation of traditional instruments.

Moreover, it is still difficult to gauge the significance that these changes will have for the developing countries. So far, these countries have only experienced the first effects of world inflation. The analysis of some of these countries may help to give a clearer picture of the new problems which are emerging, and this is the subject of the next chapter.

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[32] See First National City Bank, *Monthly Economic Letter*, New York, February 1975.

[33] Statement by the President of the Bank of Nicaragua, R. Incer Barquero, speaking on behalf of a large number of Latin American countries at the Meeting of Governors of the International Monetary Fund and the World Bank, 30 September 1974.

[34] Professor Paul Samuelson makes the following comment on the prospects which have opened up:

> "... it seems only realistic to perceive the outlook for the mixed economies not only as an outlook for stable prices but rather for a series of compromises which will make for creeping or trotting inflation. The problem is how to keep the creep or trot from accelerating. This includes the challenge of finding new macroeconomic policies beyond conventional fiscal and monetary policies that will enable a happier compromise between the evils of unemployment and of price inflation". See "World stagflation", op. cit.

Chapter II

LATIN AMERICA AND "IMPORTED INFLATION"

In order to examine "imported inflation" in Latin America, it is first of all essential to clarify some points so as to prevent any misunderstanding. Of course, there will always be those who recall with some irony that the inflationary situations prevailing in several countries of the region and in different and sometimes fairly long periods were not precisely "imported", but were mainly due to various internal factors and trends that are amply discussed in the bibliography on the subject. What is more—as noted in the preceding chapter—it is not unusual to find in the analyses of the recent inflation affecting the central economies references to the "Latin Americanization" of their process of rising prices.

There is no reason to differ outright with that point of view. As will be seen later in the country studies, care has been taken to bring out the inflationary history of some countries, as well as the structural and other characteristics affecting this question and the form currently taken by the process. Among them, incidentally, are those of the external sector, its structure and fluctuations, which existed or played a decisive part in many outbreaks of phases of inflation.

It is also clear, however, that these factors have never had such a predominant, widespread and intensive effect on the acceleration of prices as in the present situation.[35] Moreover, coming to accentuate the original nature of the process, this time it is the reflection of a considerable expansion of trade and, in particular, a sudden substantial increase in export and import prices.

The following analysis deals with the most significant aspects of the country studies included in chapter III, and focuses on 1973 and 1974 which are the most representative years of imported inflation. Needless to say—it has already been pointed out in other parts of this study—this whole picture may prove circumstantial or transitory in the light of the new prospects for the international economy.

The country studies reveal widely differing situations. Sometimes, as in Bolivia and Costa Rica, the renewed acceleration of price increases is taking place after periods of marked stability, although in both cases the external pressure was superimposed on other pressures that had been activated locally. In other countries—Brazil and Colombia, for example—the disequilibria broke out in a context of a precarious control and moderate and, in the former country, declining rates of inflation. Ecuador, to a greater extent than Bolivia, presents the peculiar case of an economy in which petroleum exports raise the problem—not now *sui generis*—of a qualitative change in the magnitude of the foreign exchange surpluses which must be absorbed. Lastly, there is Uruguay, where imported inflation is linked with domestic inflation which in previous years led to substantial price increases.

In this spectrum of contrasting circumstances, consideration must be given to the basic data on past trends and on the socio-economic structures which are exposed to the vicissitudes of the international situation, and to long-term or contingency economic policy directives.

In Brazil, for example, the challenges of the new situation are present in the context of vigorous growth, relative flexibility of the production system, an increasing openness and dependence with respect to the external variables—albeit offset by a not insignificant freedom of manoeuvre in that respect—and an explicit, continuing and pragmatic over-all economic policy, whatever reservations may be made regarding its content and weaknesses. On a different and certainly more restricted plane, this model could be applicable to Colombia, although its domestic market is not so large nor its production structure so diversified as Brazil's, and its policy has experienced more variations, besides being considered in a more limited context.

Ecuador and Bolivia have some structural features in common which are observable in their

[35] Even in countries like Chile and Uruguay, where internal circumstances were the main cause of the recent high rates of inflation, the external impact has played an important part in the trends and fluctuations of the phenomenon.

past evolution and are more clearly visualized in a situation such as that which has recently arisen. Without going into details, which are given later in the country studies, these features point to the difficulty of absorbing expansionist waves (particularly of the magnitude of Ecuador's) when they are projected on extremely heterogeneous production profiles in which a major part of the population belongs to the primitive stratum. It is unlikely that this stratum will be able to react to substantial increases in demand, but it does seem more sensitive in the way of adjusting its prices if for any external reason the prices of its imported inputs and food-stuffs rise.

Moreover, in both cases it is difficult to frame suitable policies, either because for Ecuador it is a new problem, in both quantitative and qualitative terms, with respect to the utilization of foreign exchange, or because, in Bolivia's case, the policies adopted in the face of the same problem but at a different level have followed certain basic principles which have not been successful in taking advantage of the potential of the external sector's vigorous growth.

The situations in Costa Rica and Uruguay differ in many respects. They are, however, alike in others which have a significant influence on the issue reviewed here, such as the fact that they are favoured less than others by the international trade situation.

Important differences are also observable, however, such as the relative novelty of the inflationary problem in Costa Rica, in contrast with its duration and severity in Uruguay. This and other more basic factors are the reason for the different content and scope of the policies adopted.

In the following pages an over-all analysis is attempted of the countries selected on the basis of two main questions: the pattern and symptoms of the incidence of imported inflation, and the guiding principles and options of the policies or measures devised to combat it.

A. Structural characteristics and vulnerability vis-à-vis imported inflation

While admittedly inflationary pressures in recent years in the majority of cases mainly originated abroad, it is none the less true that their incidence has depended on a number of factors which have given them greater or lesser force. What it really amounts to is the interaction of many influences, including the external situation, which is the main variable, the particular features of each economy and–last but also highly important–the decisions adopted to contend with the situation. On this interaction will depend the manner and degree in which the inflationary impact is transmitted, imported, multiplied or attenuated, all within a dynamic process of successive actions and reactions.

Among the key factors to be considered in this analysis is, first and foremost, the degree of openness of the economy, i.e., the degree to which it is integrated in world trade and the financial flows.

From this standpoint, there are a number of important points to consider. To begin with, most of the Latin American countries have fairly low coefficients of openness compared with some European countries, such as Belgium, the Netherlands and Norway, whose trade flows represent proportions of over 40 per cent. There are marked differences, however, between the larger and the smaller countries, as also happens in the case of the industrialized countries.[36] Table 2 shows that Brazil's share is very low compared with that of Costa Rica, which is a typical example of an open economy. This merely confirms the well-known assumption that the development of foreign trade and consequent possibilities of specialization acquire more importance in the smaller countries with a smaller market and range of resources.

It seems clear, however, that the developments under review have resulted in a fairly widespread and appreciable enhancement of external relations. This is true of four of the six countries studied (see table 2). As regards Colombia and Uruguay, which have not followed that trend, some special situations affecting them must be taken into account. For example, the unfavourable trend in

Table 2. Latin America: average exports and imports of goods and services as a percentage of the gross national product at current prices in selected countries

	1960-1962	*1973*	*Percentage variation*
Bolivia . . .	20.2	29.7	47.0
Brazil	7.7	8.9	15.6
Colombia . .	14.5	14.2	−2.1
Costa Rica . .	24.1	34.2	41.9
Ecuador . . .	18.3	24.1	31.7
Uruguay . . .	14.0[a]	13.6	−2.9

SOURCE: IMF, *International Financial Statistics*, October 1967 and March 1975.

[a] 1961-1962.

[36] The coefficients of France (15.6 per cent), Japan (10.7 per cent) and the United States (5.9 per cent) contrast strongly with the Netherlands coefficient of nearly 50 per cent (figures for the years 1968–1970, in OECD, "The international transmission of inflation", *Economic Outlook*, op. cit.).

Colombia's traditional exports in the middle years of the past decade reduced the above share. Therefore, the 1973 figure indicates a recovery as a result of the vigorous growth of new exportable commodities. The situation in Uruguay, which contradicts the aforementioned assumption regarding small countries, is a sign of the external sector's inability to expand from which it has long been suffering, and which is one of the crucial factors of its present stagnation.

This question, however, is linked not only with the qualitative representation of external transactions, but also—to a considerable degree—with their structure, particularly the composition of exports and imports, an aspect which is dealt with in detail later in this study. Here attention is drawn merely to some important facets in the light of recent experience. It is unnecessary, of course, to stress the decisive significance of being a net oil importer or exporter. In each case, the repercussions, apart from being considerable, will show a very different sign in the trend of prices, balance-of-payments position and monetary implications. In the equally disparate case of countries with exportable agricultural surpluses and those importing food-stuffs, the external situation has a very different impact on each of these groups and the problems that arise are also very different.

As the structural counterpart of the situation as regards the level and quality of openness of the economy, consideration might be given to the representation in the various countries of the subsistence sector—partly or completely outside the money market—which in differing degrees would not be greatly affected by inflation associated with the external sector, nor would it influence the reproduction and spread of this phenomenon locally.

In this respect, reference has been made above to Ecuador and Bolivia, which seem to be the most relevant cases for this discussion. In any case, it would not do to exaggerate the significance of this aspect of the situation in Latin America, although it may be more worthy of consideration in countries or areas with a more typically dual structure and with few links with other countries owing to their very state of underdevelopment. This subject is dealt with more fully in the studies on these two countries.

In addition to these structural characteristics, the impact of imported inflation will largely depend on the policies adopted to combat it, a matter which is examined later in this study. It can be stated in advance that the freedom of manoeuvre and the possibilities and choice of action will be decisively conditioned by those structural characteristics and by institutional and socio-political elements which are well known.

B. CHANNELS OF TRANSMISSION OF IMPORTED INFLATION

Against a backdrop of the foregoing circumstances, the various ways and forms in which external inflationary pressures are disseminated should be identified. The 1973 *Economic Survey* includes a preliminary study of the question, and other attempts at analysing it have been made since, as inflation took root and spread. They include a special study by the OECD,[37] which endeavours to classify the channels of transmission of the process, identifying the factors which are seen to stimulate it in the industrialized countries represented by that organization.[38] A different system is adopted here, which naturally has some elements in common with the aforementioned system, but seems better suited to the circumstances in Latin America. A distinction is made between direct influences and indirect influences, and, among the latter, between those constituting the initial spur to the propagation of inflation and those deriving from such influences.

The most obvious of the direct channels is the rise in import prices. As will be seen in table 3, substantial increases were recorded in 1973 and 1974 in all the countries considered, especially in the latter year. The variations in 1974 range from 22.8 per cent in Bolivia to 57.5 per cent in Brazil.

Unfortunately, the available data are unreliable and usually underestimates of the actual magnitude of the adjustments. There are better classified data for Brazil, which show much sharper contrasts between the trends of prices and quantities in the case of some major groups of products. Table 4 reflects the situation in the first six months of 1973 and 1974.

There is, in fact, a marked disparity between the trends of prices and of the volume of imports (see table 3). Some countries recorded substantial increases in both. In the majority, prices increased much more than the volume. Basically, these disparities are in keeping with the developments in 1974 as regards oil prices (see in table 3 the price increases particularly affecting Brazil, Costa Rica and Uruguay).

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[37] "The international transmission of inflation", *Economic Outlook*, July 1973.

[38] These factors are grouped as follows: (*a*) price-effects, whether of competitive or non-competitive imports, or of exports that follow the trend of prices; (*b*) demand-effects, deriving from the increase in exports and the improvement in the external current account, which results in excessive demand in a period of full employment; (*c*) liquidity-effects of the balance of payments on monetary conditions, and hence on domestic demand and prices; (*d*) other links, such as those between multinational enterprises and trade union organizations, international inflationary expectations and demonstration-effects.

Table 3. Latin America: indexes of prices and volume of imports in selected countries
(1970 = 100)

Country	Price index				Index of volume			
	1973	1974	Percentage variation		1973	1974	Percentage variation	
			1973	1974			1973	1974
Bolivia	127	156	17.6	22.8	117	150	8.3	28.2
Brazil	134	211	19.6	57.5	177	232	18.0	31.1
Colombia	130	158	18.2	21.5	98	112	6.3	14.0
Costa Rica	128	168	15.3	31.3	109	126	2.8	15.6
Ecuador	128	166	16.4	29.7	144	186	15.2	29.2
Uruguay	133	208	19.8	56.4	92	99	15.9	7.6

SOURCE: ECLA, on the basis of official statistics.

Table 4. Brazil: variations in the value and volume of imports
(First half of 1973 and 1974)

	Percentage increase in value	Percentage increase in volume
Basic commodities	225	4.3
Processed products	93.8	71.9
Total	*122.5*	*14.7*

SOURCE: *Conjuntura Econômica*, October 1974. See table 64 in the study on inflation in Brazil.

These ratios raise some queries regarding the inflationary impact of the larger volume of imports. From one point of view, the bigger inflow of foreign goods might be considered to act as a restraint on price increases, because of its contribution to total supply and, in particular, towards eliminating partial disequilibria within total supply in the face of changes in demand. From a different standpoint, however, opposite repercussions are observable for two main reasons: first, the increases in the volume of imports, to the extent that they increase the share of foreign goods in total supply, extend the area of impact of the rise in external prices; secondly, a varying proportion of the increase in imports may have gone towards increasing the reserves or stocks of private or public enterprises as a safeguard against an uncertain situation, which would cancel out part of their possible contribution to actual supply.

It is not easy to clarify this point without careful research. At all events, it seems that the effect of the increases in the volume of imports remains contradictory, although the increases in import prices certainly is not.

The second and more complex direct channel of transmission of external pressures is that set in motion by export trends. Table 5 shows the trend of exports in terms of prices and volume. Here the increase in prices is considerably larger in all the countries studied, particularly in 1974. Obviously, the disparity is greatest in the case of the two oil-exporting countries (Bolivia and Ecuador), which reduced their volume of exports.

Table 5. Latin America: indexes of prices and volume of exports for selected countries
(1970 = 100)

Country	Price index				Index of volume			
	1973	1974	Percentage variation		1973	1974	Percentage variation	
			1973	1974			1973	1974
Bolivia	116	245	33.3	111.2	121	117	1.7	−3.3
Brazil	166	214	37.2	28.9	136	136	13.3	0.0
Colombia	125	145	27.6	16.0	136	149	9.2	9.8
Costa Rica	120	143	20.0	19.2	122	129	2.5	5.7
Ecuador	138	329	38.0	138.4	178	164	28.6	−7.8
Uruguay	190	204	45.0	7.4	77	81	−6.8	5.5

SOURCE: ECLA, on the basis of official statistics.

Table 6. Latin America: price indexes of selected export commodities
(*1970 = 100*)

	1965	*1971*	*1972*	*1973*	*1974*
Wheat	102	107	119	135	329
Maize	108	112	115	167	306
Rice	92	114	104	141	571
Beef	108	149	180	243	272
Sugar	57	120	198	256	1,300
Coffee	91	78	96	117	121
Bananas	116	108	112	113	140
Cotton fibre	109	134	147	168	206

SOURCE: ECLA, on the basis of official statistics.

As regards the transmission of inflationary pressures through exports, it is useful to distinguish those products which are mainly or, in some cases, wholly exported from those which in a fairly considerable proportion are absorbed by the domestic market.

It seems clear that the transmission of price increases is much more direct and widespread in the case of the second group of exports. Note, for example, the countries producing basic food-stuffs: wheat, meat or rice. Irrespective of what a prices policy can–and in practice actually does–accomplish, as will be noted in the country studies included in this *Survey*, there is no doubt that an immediate link is established between the two spheres, transferring the external increases to prices on the domestic market. Table 6 shows the price trends of some important items in the two categories described.

In the case of the former group of exports, in contrast, the impact of improved prices is felt indirectly and with some delay through government income and expenditure or through the effects on the demand of those benefiting from the export business. This is generally the case with respect to exports of basic and industrial inputs, such as petroleum itself and mining products. Naturally, products of the two types may be found in some countries. Brazil, for example, is an important exporter of agricultural commodities as well as of iron ore.

1. *Indirect internal propagation: general channels*

As regards the indirect effects, attention must be centred first on three areas which act as amplifiers (or dampers) of imported inflation: (*a*) foreign trade; (*b*) the monetary field; and (*c*) the fiscal area.

In foreign trade, under other conditions, the foreign exchange rate and its devaluations were a major factor in raising domestic prices as a result of the rise in the cost of imports and related effects. In the recent situation, matters have taken a different course and this instrument may be said to have had an essentially moderating effect on imported inflation. This assumption applies to three countries in particular–Costa Rica, Ecuador and Bolivia–which have kept their exchange rates stable, in spite of the appreciable increase in domestic prices and, consequently, the actual depreciation of their currencies. By this and other methods, such as tariff reductions and subsidies, the impact of the higher import costs was softened.

The situation is quite different in other countries which, in keeping with their own special characteristics, have followed the system of mini-devaluations. These have permitted the price increases of imported products to filter through to the domestic market. Even in this case, however, the adjustments in the exchange rate generally lagged behind the increase in the price index, as will be seen in the country studies, particularly in the case of Brazil in 1973. This subject is referred to again later in discussing economic policy guidelines vis-à-vis imported inflation.

The lesser importance of the exchange rate channel in the recent situation is counterbalanced by the considerable importance acquired by another element which had been of little significance in past inflationary experiences: the movements of foreign exchange reserves and their relationship with monetary expansion.

Table 7 shows that in three countries there were substantial increases in these resources in 1973: 64.3 per cent in Colombia, 53.4 per cent in Brazil, and 68.5 per cent in Ecuador. The increase was more moderate in Uruguay (17.2 per cent), and in Bolivia there was a big jump the following year (164.2 per cent). In 1974, however, except in the case of the oil-exporting countries, they all recorded a drop in their reserves.

These changes had an evident impact on the growth of the means of payment in several countries in different years (see table 8). In

Table 7. Latin America: international reserves in selected countries
(Millions of dollars, at the end of each period)

Country	1970	1973	1974	Percentage variation	
				1973	1974
Bolivia	45.5	72.1	190.5	20.8	164.2
Brazil	1,187.0	6,417.0	5,252.0	53.4	−18.2
Colombia	206.0	534.0	449.0	64.3	−15.9
Costa Rica	16.3	42.4	38.1	7.7	−10.1
Ecuador	83.0	241.0	349.9	68.5	45.2
Uruguay	175.0	232.0	217.0	17.2	−6.5

SOURCE: IMF, *International Financial Statistics*, May 1975.

Table 8. Latin America: increase in the money supply in selected countries
(Percentages)

Country	1971	1972	1973	1974
Bolivia	15.2	25.2	34.3	43.4
Brazil	31.3	38.9	48.0	34.8
Colombia	11.9	27.1	30.7	20.0
Costa Rica	28.8	14.2	24.1	19.2
Ecuador	11.4	21.6	30.7	36.5
Uruguay	51.1	52.1	74.5	62.2

SOURCE: IMF, *International Financial Statistics*, May 1975.

Ecuador and Bolivia, for example, the expansion of monetary resources was basically due to the purchase of reserves by the Central Bank. As regards Colombia and Brazil, the violent expansion of reserves in 1973 would account for about one third of the increase in monetary resources in the former, and approximately one quarter in the latter.[39] In 1974, in contrast, the drop in reserves experienced by the four non-oil-exporting countries helped to curb the increase in the money supply (see table 9).

Although the fluctuations in international reserves and their monetary projections follow a fairly regular pattern in keeping with the structure of the external sector, the same cannot be said for the movements of domestic credit, whose contribution to the money supply and its internal composition varies considerably between one country and another (see table 9).

In Ecuador, for example, the striking feature is the contrast between the increases in this monetary source and the fluctuations in foreign exchange reserves. The rates of expansion are fairly moderate and only the private sector benefited from the increase in credit. Conversely, taking advantage of the oil boom, public credit became independent of the Central Bank and even reduced its debts. A similar process is apparent in Bolivia, although the expansion of credit was only slowed up in 1974, also at the expense of the public sector and with fairly high growth rates for the private sector.

In Brazil, the increases in credit in the years considered were fairly uniform, except in the case of the public sector, which shows a negative sign in 1972 and 1974. It should be borne in mind, however, that the financial market constitutes an important alternative source of funds for the Government.

In Costa Rica there was an appreciable rise in the rates of increase in domestic credit between 1973 and 1974, especially as regards the public sector. This, however, was not reflected in a bigger increase in the money supply (see table 8), no doubt as a result of the restrictive effect of the drop in foreign exchange reserves (see table 7).

The figures for Uruguay are evidence of the serious inflation experienced by that country in recent years. Although admittedly the rate of increase in the money supply decreased somewhat in 1974 (see table 8), this was due to the movement of reserves rather than to the development of credit, since the latter rose

[39] See the country studies for a more detailed analysis of these questions.

Table 9. Latin America: variations in domestic credit in selected countries

	Percentage variation			
	1971	*1972*	*1973*	*1974*[a]
Bolivia	21.2	28.2	31.2	8.5[b]
To the public sector	18.4	21.2	4.1	--39.4
To the private sector	25.9	39.2	68.1	60.0
Brazil	41.4	31.9	46.6	44.8[c]
To the public sector	12.2	−42.4	22.4	−27.6
To the private sector	48.0	44.6	48.2	48.9
Colombia	18.4	17.4	18.8	...
To the public sector	32.0	7.0	12.1	
To the private sector	15.4	20.0	20.4	
Costa Rica	34.1	17.5	10.2	50.3
To the public sector	37.6	42.2	1.0	44.7
To the private sector	33.5	12.9	12.3	51.5
Ecuador	11.6	3.5	–	20.9
To the public sector	16.8	−18.5	−88.4	–[d]
To the private sector	10.0	10.3	20.5	39.0
Uruguay	66.5	94.0	51.3	86.0
To the public sector	109.4	80.7	9.8	67.0
To the private sector	56.0	98.3	63.6	94.0

SOURCE: IMF, *International Financial Statistics*, May 1975.
[a] Preliminary estimates.
[b] The source of the 1974 figures is the Central Bank of Bolivia.
[c] Variation up to November.
[d] A negative balance was recorded again.

appreciably, particularly in support of the private sector (see table 9).

It might be interesting to compare the relationship between the increases in the money supply and the rise in prices; these variables are usually compared in search of some causal relationship. Table 10 presents the respective figures for the six countries considered. It is easy to see that only in Bolivia and Ecuador is there a certain parallel relationship between the two indicators. In the other countries the connexion is much more erratic. For example, in Brazil, a considerable expansion of the means of payment in 1973 was accompanied by a substantially lower rise in the price index, in contrast with 1974 when these indicators showed similar increases.

Thorough research would be required to determine the reasons underlying these trends and disparities, and some light is shed on the subject by the country studies which form part of this *Survey*. Suffice it to say here that the figures reveal scant grounds for an over-simplified or quantitative approach to the relations between monetary expansion and price increases.

2. *The fiscal channel*

The repercussions of imported inflation on the fiscal area seem to have been less severe than the classic impact of situations of crisis or restraint in the external sector. The obvious exceptions are Ecuador and Bolivia, where the Governments are the main internal beneficiaries of the petroleum export boom. It also seems clear, however, that the repercussions on prices have everywhere affected the public finances, through increases in current or capital expenditure or in spending on imports or domestic goods and services. It is equally true that in the countries enjoying an increase in fiscal revenue, the inevitable tendency towards a parallel increase in public spending involves redoubled pressures on the availability and flexibility of production resources, in addition to which it is much more difficult to endeavour to raise domestic taxes, either for anti-inflationary purposes or in order to obtain the domestic saving counterpart of the bigger investments being made or in view. Paradoxically enough, the boom resulting from the foreign trade situation is not a favourable atmosphere for pursuing those aims, although the objective conditions make them more feasible than at any other time.

Table 11 shows the trends of and relationships between the growth of total expenditure and current income in the countries considered. Since the figures represent nominal values, they tend to overestimate the actual growth, but it is none the less true that the changes between 1974 and 1973

Table 10. Latin America: comparison between increases in the money supply and in the consumer price index in the six countries considered

	1973	*1974*
Bolivia		
Increase in money supply	34.3	43.4
Increase in consumer price index	34.9	38.8
Brazil		
Increase in money supply	48.0	34.8
Increase in consumer price index	13.6	34.6
Colombia		
Increase in money supply	30.7	20.0
Increase in wholesale price index	25.1	26.9
Costa Rica		
Increase in money supply	24.1	19.2
Increase in consumer price index	26.4	38.2
Ecuador		
Increase in money supply	30.7	36.5
Increase in consumer price index	20.5	21.2
Uruguay		
Increase in money supply	74.5	62.2
Increase in consumer price index	77.7	107.3

SOURCE: ECLA, on the basis of official statistics.

without exception exceed the rise in prices, sometimes by a considerable amount (see, for purposes of comparison, table 12). This comes on top of what are also significant increases if the situation in 1973 is compared with that of the base year (1970).

It will be noted, moreover, that the expansion of total expenditure in 1974 over 1973 was accompanied fairly flexibly by current income. Except in Uruguay, the latter rose at a higher rate than the former. Furthermore, as regards Ecuador, the growth of income compared with expenditure has been considerable between 1970 and 1974, which is not surprising in view of the impact of the inflows obtained from the development of petroleum.

It should be borne in mind that the evident benefits deriving from petroleum exports have also meant that the fiscal system of the countries thus favoured have become overwhelmingly more dependent on this activity.

3. *Prices and wages and salaries*

In the wave of pressures and impulses set in motion by imported inflation, another element may be distinguished: the movements or responses of domestic prices and income to the changes analysed above. As regards the above pressures, the direct impact of the rise in import and export prices has already been discussed. It was also stated that in the case of export commodities of which a significant proportion is consumed locally, the impulse is immediately transmitted to the share destined for the domestic market.

Undoubtedly, however, the process of dissemination and possible multiplication of the direct effect only starts here. It is recognized that there is a sympathetic association of changes in prices, which operates and is manifested in many different ways. A rise in the price of the products concerned—whether imports or exports—will trigger increases in the prices of substitutes or competitive products. Spending the additional income—even if with the object of increasing the exploited area or the quantities produced—will in some degree affect the availability of resources and, consequently, their prices. Efforts to use land or materials for activities yielding the highest returns have often resulted in the reduction or insufficient growth of other lines of production, with the resulting price-effects. The reactions are thus linked together and extend indefinitely, compelling the Governments to adopt different measures.

Without going too deeply into this well-known aspect, it is useful to note the asymmetry of this phenomenon, which is of key importance in discussing the behaviour and role of the movements of income.

Table 11. Latin America: evolution of current income and fiscal expenditure in the countries considered
(Percentage annual variation)

	Variation 1970-1973	*1974 (over the same period in 1973)*
Bolivia		
(Central government)		
Current income	32.1	106.7
Total expenditure	32.1	92.4
Brazil		
(Federal government)		
Current income	40.2	41.0 (January-October)
Total expenditure	38.1	33.5 (January-October)
Colombia		
(National government)		
Current income	18.8	29.5
Total expenditure	19.5	25.4
Costa Rica		
(Central government)		
Current income	16.2	32.5 (January-September)
Total expenditure	35.0	16.3 (January-September)
Ecuador		
(Central government)		
Current income	29.6	86.7
Total expenditure	16.4	79.8
Uruguay		
(Central government)		
Current income	64.7	63.7
Total expenditure	64.6	80.8

SOURCE: ECLA, on the basis of official statistics.

Table 12. Latin America: variations in the consumer price index
(Percentage annual variation)

		Variation December 1973	*Variation 1974*[c]
		1970	*December 1973*
Bolivia	General index	20.8	38.8 (December)
(La Paz)	Food index	24.0	44.7 (December)
Brazil	General index	18.6	30.9 (November)
(Guanabara)	Food index	21.1	38.5 (November)
Colombia	General index	17.3	16.3 (August)
(Bogotá)	Food index[b]	20.5	18.7 (August)
Costa Rica[a]	General index	12.3	26.0 (June)
	Food index[b]	12.2	20.4 (June)
Ecuador	General index	13.1	21.8 (November)
(Quito)	Food index	17.2	30.1 (November)
Uruguay	General index	72.6	50.7 (August)
(Montevideo)	Food index	80.7	45.4 (August)

SOURCE: United Nations, *Monthly Bulletin of Statistics*, February 1975.
[a] Wholesale prices.
[b] Weighted average for food of animal and vegetable origin, and for beverages and other items.
[c] The last month considered is given in brackets.

Another glance at table 1 of this first part of the *Survey* will show the rates of increase in the price index of the countries under review. Going a step further, table 12 has been prepared in which the general rise is compared with the increases in food-stuffs between December 1973 and the last month of 1974 for which data were available at the time of writing this study.

It will be seen that at the end of 1973—compared with the base year (1970)—in all the countries except Costa Rica the increase in food prices was bigger than that recorded for the over-all index. This disparity is again evident from a comparison of the changes between 1974 and 1973, although Uruguay and Costa Rica do not follow the prevailing pattern, which is more strongly marked in the cases of Brazil and Ecuador. Naturally, this ratio underestimates the actual difference between the two figures, because the over-all index includes the index recorded for food-stuffs.

Moreover, there are well-known inadequacies in coverage and procedures which tend to have the same effect, especially in periods of substantial increases, which make it more difficult to control prices and widen the gap between official prices and actual market prices.

The acceleration of price increases and the asymmetry of these movements have obvious and only too well-known implications in terms of income trends. The more than proportional increase in food prices and the various obstacles preventing or delaying adjustments in the income of large groups of wage-earners encourage the trend towards a regressive income distribution which is in any case a result of any acceleration of the inflationary process.

At least in the countries under review—and for different reasons in each—no great propagating or multiplier effect appears to have been exercised by the pressure of wage-earners to regain former levels of real income, which in the previous chapter was seen to be a very significant factor in the present situation of the central economies. However, the country studies show that in several countries measures have been taken to counteract such deterioration or wage and salary adjustments have been accorded, especially to urban workers. In this respect, it is pointed out that the acceleration of price increases in Brazil led to a change in the approach which had long been in force regarding the movement of wages and salaries.

C. Economic policy options and instruments

It is not possible to review the wide range of positions and instruments which have been adopted by the countries considered in dealing with imported inflation, and which are discussed later in the respective studies. It might, however, be useful to present the problem here in broad terms.

These countries, of course, like the rest of the countries of Latin America, have had to choose between two clear-cut possibilities. First, to accept the rise in external prices and to adjust their domestic prices and price system accordingly, with all the possible drawbacks and advantages involved. This is what some have called the "internalization" of world inflation, which would lead to the search for a new balance at a different level. The other choice would be as far as possible to shut themselves off from the tide of rising external prices in order to curb price increases; but this would also mean, to a considerable degree, maintaining the relation between prices or the price system existing before the situation developed.

Of course, this is merely a hypothetical option. In practice, no country has been or would be able to take either of these opposite courses to extremes.[40] What is observable, however, is a tendency in the one or the other direction. This tendency, moreover, depends more on particular and objective circumstances than on the arbitrary or subjective decisions of policy-makers.

The dilemma in the case of a Caribbean country was presented clearly at a recent meeting:

> "Much of the inflation is imported. The prices of basic food which we have to import—flour, rice, meat, animal feeds and textiles—have risen very sharply and continue their uninterrupted rise. To cushion the effect of all these price increases would be very costly; it would further reduce the amount of money available for developmental purposes. Not to cushion it would lead to the inevitable demands for high wage increases which will affect our competitive position, and will further add to inflationary pressure. Our dilemma is similar to that faced by many small countries with open economies and an undiversified production structure. The Government has chosen the middle way; it is to keep stable the prices of certain key goods such as flour, rice and internal transportation by means of direct subsidies; and to use other devices, including credit and monetary policy, fiscal concessions to industry, and an improvement in guaranteed

[40] In the European discussion of the matter (see *Economic Outlook*, July 1974, op. cit.) it is clear that the option of shutting themselves off from imported inflation is utterly impracticable for the more open economies. Moreover, experience has shown it to be inadvisable even for the more important economies, though they certainly have more radius of action in the matter.

prices for local farm production to control price increases originating within the domestic economy."[41]

This eclectic approach to the problem seems to have been followed by most of the countries studied. However, some countries–Ecuador, for example, which has had an extraordinary amount of fiscal resources–have had more recourse to instruments such as subsidies and tariff reductions in moderating the rise in price of essential imports. Furthermore, to keep the parity of the sucre fixed in the face of a significant increase in domestic prices has in fact meant a revaluation of the exchange rate. This did not, however, jeopardize its basic export commodity (petroleum) or its foreign exchange reserves, although the latter grew less in 1974 than in 1973 (see table 7).

Other countries, in contrast, either for lack of the same possibilities or in keeping with the policy adopted, or a combination of the two, have let the level and system of prices adapt to the changes in the external situation.

From a different standpoint, two other types or forms of action in dealing with imported inflation may be distinguished in the national experiences reviewed here, as also in the rest of the countries. On the one hand are the countries in which the measures and instruments applied have been placed within or have derived from an over-all economic policy framework. On the other hand are the countries which have adopted a number of *ad hoc* decisions of which the guiding principle may have been to curb the rising prices and mitigate the social and economic impact of the situation.

Neither can a rigid or complete division be established here, but it is clear that Brazil, for example, is a conspicuous illustration of the first approach. Not only is it possible to observe a clearly-defined anti-inflationary strategy, which has been implemented for nearly a decade, but this strategy has formed part of an over-all approach to development. In fact, it would not be possible to understand the former without having in view the latter, and to a certain extent it might be maintained that the management of the inflation variable has had outstanding significance in the framing and handling of development policy.

Contradicting what has sometimes been maintained in certain circles outside Brazil, those general and specific frameworks do not seem to have involved unvarying or dogmatic commitments through specific instruments and actions. Quite the contrary. As pointed out by some of the foremost leaders of that experience. the basic definitions have gone hand in hand with a considerable dose of pragmatism.[42] Thus there has been no reluctance to alter rules or prime directives of the policy being implemented, when circumstances have dictated a different course. Reference was made above to the criteria with respect to wage increases. It is also useful to recall the moderation involved in the practice of mini-devaluations when external pressures on prices were intensified in 1973, or the abandonment of the adjustability clause in the new Treasury bills.

At the other end of the scale, logically enough, as regards the definition or scope of policies, are those countries which have had less experience in the ups and downs of inflation, or which have had to face substantially novel situations. Costa Rica and Ecuador are clear examples of these two situations. In Uruguay and Bolivia, to a certain degree, the measures against inflation have been conditioned by an over-all policy, although this may not, of course, have the radius of the Brazilian policy. Lastly, and at a different level, it is possible that Colombia's policy is closer to that of Brazil, at least as regards the expeditious and practical nature of many of its provisions.

D. PROSPECTS AND QUERIES

At the beginning of 1975, it may already be anticipated without too much risk of error that the conditions prevailing in the dynamic and complex period 1973-1974 are likely to be appreciably modified. As noted in chapter I, the price curve of basic materials is definitely pointing downwards. This trend also includes petroleum, if account is taken of its terms of trade, i.e., vis-à-vis the rise in industrial prices. Although the majority assume that these prices will remain at fairly high levels compared with those recorded at the end or in the middle of the 1960s, nobody can hazard specific forecasts, since a decisive factor in this connexion is the recovery by the central economies of their dynamic impetus.

In any case, from the Latin American standpoint and with the relative exception of the oil-exporting countries, one all-important aspect of imported inflation, which is precisely the advantageous one, has come to an end, since the expansion and rise in the prices of exports has halted, while prices of imports continue to rise.

This change in the external picture has an

[41] See the statement by Mr. V. C. McIntyre, representative of Trinidad and Tobago, in OAS, in the final report of the Sub-Committee of CEPCIES on Trinidad and Tobago, September 1974.

[42] See M. H. Simonsen, *Inflaçao: Gradualismo versus tratamento de choque* (Apec Editora, Río de Janeiro, 1970); and M. H. Simonsen and R. de Oliveira Campos, *A nova economia brasileira* (Libraria José Olympio Editora, Río de Janeiro, 1974).

evident impact on the inflationary prospects of the Latin American countries, apart, of course, from its more general implications which are also a source of concern.

This means that the effect of the rise in import prices will continue to be felt, in addition to the internal pressures set in motion by the current situation. Furthermore, the possible slowing-up of the inflationary process, as a result of the slackening in the rise of export prices and the channelling of some export commodities to the domestic market, would also mean a deterioration in the balance of payments and in the situation of important sectors of production.

Accordingly, it would not be surprising if in some countries a situation arose which was somewhat similar to the stagnation combined with inflation (stagflation) affecting the central economies. The rise in import prices and the cumulative internal pressures would act as a fillip to inflation, while the weakening of exports and the consequent probable decline in the capacity to import would jeopardize opportunities of growth.

Be that as it may, a new stage seems to be opening up after the fleeting but violent impact of imported inflation, which will once again put the countries' economic policies to the test. No doubt it will not be easy to adapt them in order to contend successfully with a situation which may be more like those confronted in earlier periods.

Chapter III

RECENT INFLATION IN SIX LATIN AMERICAN COUNTRIES

The following review of inflation in six Latin American countries devotes particular attention to events in the years 1973 and 1974, which have been the most affected by international price trends. However, an attempt has been made to present a retrospective view of the phenomenon, especially in those countries in which its roots go fairly far back.

It was not a simple matter to select the countries. Two criteria predominated here. First, to show cases that differed as regards the impact of the external situation, which has depended basically on the consumption of exports and imports. Thus, side by side with the oil-exporting economies there are others in which the increases in import prices have been more significant than the export boom. Secondly, the idea was to present cases of countries in which inflation had not been very serious until the present situation, together with others in which it has been an important factor of past trends.

It should be borne in mind that the general picture and the specific situations presented in this study underwent appreciable changes at the end of 1974, as a result of the new circumstances of the world economy, particularly the central countries. It will therefore shortly be necessary to revise observations and even analytical categories which may have been useful in dealing with this transitory situation, but which may not be so in grasping what is happening now.

1. BOLIVIA

A. INTRODUCTORY NOTE

The recent inflation in Bolivia is of particular interest, in that its course would appear to be strongly influenced by the interplay of factors of different types, which give it a very special character as far as its origins and the final form it takes are concerned.

The situation, moreover, is one of an inflationary cycle preceded by a long period of stability, and this undoubtedly provides a further factor of interest. The contrast between the stability and of the period 1959-1971 and the inflation which appeared in 1972 shows just how decisive structural aspects are in Bolivian development.

Perhaps the main interest of the present case, however, is the simultaneous existence of a wave of prosperity in the external sector which reached heights unknown previously, and an inflationary process whose origins are deeply rooted in the country's productive system, this process being set off by the increase in the liquidity of the economy and then resurging under the impetus of international inflation. The extent to which inflation has affected the taking of decisions, which would otherwise have been more far-reaching, makes the study of this process a matter of high priority.

The present document only attempts to identify the most significant facts and the basic elements of inflation in Bolivia. Further clarification and more exact appreciations would require intensive work on the spot, which is outside the scope of this first attempt.

B. BACKGROUND TO THE NATURE AND EVOLUTION OF THE BOLIVIAN ECONOMY

1. *The general context*

The evolution of the Bolivian economy in the past 15 years has been marked by modest rates of economic growth. The main macroeconomic indicators show fairly moderate growth rates, the variations in which, generally speaking, do not take the form of downward or upward movements of any great importance. The more substantial variations were restricted to centres of activity whose influence was only secondary in the general economic situation. The moderate growth rates

mainly benefited certain urban groups linked with such services sectors as trade and banking, with some forms of processing such as ore-smelting, with certain manufacturing industries, and with construction activities. The mass of the population of Bolivia, who depend on agriculture for a living, made no major progress in their standard of living.

With its plentiful natural resources and fairly low level of economic activity Bolivia should be able to achieve rather more ambitious margins of growth than those which actually materialized, i.e., the growth potential of the economy should be well above the moderate growth rate which it has shown in the past.

It should be mentioned that, during the period referred to, various development strategies and policies were tried out in different external and internal economic situations, but they did not achieve the changes which they were intended to bring about. The conduct of economic activity, generally speaking, has found obstacles of different types, among which may be mentioned the lack of coherence in the structure of the economy.

The following description of the over-all economy and the interpretation of inflation in Bolivia in recent years call for the identification of a group of basic shortcomings in the economic system which seriously restrict the process of production and distribution in the country's economy.

The marked structural heterogeneity which characterizes the production function is one of the basic explanations why Bolivia is a relatively less developed country. By way of illustration, mining and petroleum must be compared with agriculture and even with incipient industry in Bolivia. The differences in productivity are exceptionally great, and, as already stated, this means an acute lack of interrelation between the sectors of production.[43] The absence of a lively manufacturing sector has caused the emergence of enclaves of exports of raw materials severed from the domestic process of production, while on the other hand a large part of the agricultural sector is functioning on the basis of archaic technology, with uneconomic scales of production and with no clear idea of how to plan the allocation of resources, markets and prices. In other countries, industry is the sector which plays an integrating role, but the volume of Bolivia's industrial output and the type of products manufactured show that this sector does not succeed in carrying out this role.

In addition to the lack of integration of the sectors of production, which is in itself a serious problem, there are other manifestations of structural heterogeneity, such as the existence of large geo-economic areas which are potentially very rich but are not linked with the producer and consumer centres of most importance in the country. On the other hand, structural heterogeneity is also manifested in the coexistence of several different cultural patterns in which different races, languages, customs, etc., constitute considerable obstacles to a more harmonious and integrated functioning of the socio-economic system. These structural features in turn are the cause of considerable disparities between the urban centres and the rural areas, and between the strata which make up each of these categories. On one side are the country dwellers, who form the majority of the population but have no real purchasing power as regards industrial products; on the other are the high- and middle-income urban groups whose demand constitutes an incentive only to small-scale industries which respond to their particular spending patterns. In the circumstances, it would be difficult to arrive at a rapid process of industrialization which would integrate the different sectors of production. The narrowness of the consumer market, resulting mainly from the low productivity of a large part of the agricultural sector, is a structural obstacle to any attempt at industrialization.

In view of the importance of the agricultural sector in the Bolivian economy, and in particular in the interpretation of inflation, some additional observations from the point of view of the heterogeneity of productivity would appear to be in order. The levels of production and the growth rates which will be given for the agricultural sector in the analysis of the over-all economy are an aggregate of *altiplano* and valley output, where chronic stagnation exists, and of the output of the eastern plains where products like cotton, sugar cane, soybean, etc., have excellent external markets, employ more advanced technologies and record fairly high indexes of output and productivity. If agriculture as a whole shows an inadequate rate of growth, how much more drastic such a qualification could be if it only referred to the agriculture of the *altiplano* and valleys in which the majority of the rural population works. These disparities should be borne in mind in the description and analysis of the performance of the main sectors of the economy given below.

This summary enumeration of the main structural shortcomings suffices to weigh their importance in the economic process in Bolivia in their true context. The disequilibria described are, in fact, the principal source of a series of problems affecting the economy, and of course lie at the

[43] According to ECLA estimates and the *Memoria del Banco Central de Bolivia*, 1973, the product per employed person in 1973, in terms of Bolivian pesos at 1970 prices, is 1,500 in agriculture, 9,400 in manufacturing and 33,200 in mining and petroleum.

root of a group of conjunctural disequilibria which in their turn are manifested in the form of inflationary pressures.

2. *Main features of the evolution of the economy*

A study of inflation in Bolivia requires the identification of the main macroeconomic phenomena which characterized the recent evolution of the country's economy. The performance of some variables was a direct determining factor of inflation in Bolivia; the disequilibria which separated the physical area of the economy from its financial counterpart resulted in the unbottling of strong pressures on prices. This section therefore endeavours to select the aspects of Bolivia's economic evolution most closely linked with the phenomenon of inflation. In this context it is useful to compare the main variables in 1972 and 1973 (1972 was the year of the initial impetus and 1973 saw the aggravation of inflation) with their performance during the period 1970-1971, and in some cases with the last five years of the 1960s, as a basis for reference.

Of particular importance is the analysis of the main movements of the external sector, the structure of over-all supply and demand and the evolution of the product in the major sectors of activity. The main features of the over-all evolution of the Bolivian economy will be described in terms of these aspects taken in the same order.

(a) *The external sector*

The very considerable variations experienced by the external sector came to constitute the most important phenomenon of what has elapsed of the present decade. Their repercussions on the production function, income distribution and particularly on the future growth potential of the economy, confers particular importance on them, especially if it is recalled that tremendous importance in respect of the country's state of underdevelopment was attributed to the traditional bottlenecks in this sector. The events of recent years meant a change of some consideration in the scales of operation of external trade; in a brief period of two years, the current values of international transactions more than doubled. This is not just a matter of significant increases, but more than anything else of a situation different from that of the recent past in quantitative and qualitative terms, as is obvious from the description given below.

(i) *The performance of exports.* The current value of exports of goods showed an extraordinary increase. A comparison of the annual averages for the period 1965-1969 and those for the three-year period 1971-1973 shows a growth of 62 per cent, reflecting a clearly defined trend despite the decline in the value of exports in 1971 (see table 13). The growth rates of 1973 and 1974 are noteworthy; they showed an unprecedented increase when the CIF value of exports of goods amounted to 337 million dollars in 1973 and around 680 million dollars in 1974. These levels imply annual growth rates of 40 per cent in 1973 and 104 per cent in 1974, and show how the value of exports tripled within the space of two years.

Important changes may also be observed in the structure of exports of goods. While during the

Table 13. Bolivia: evolution of exports of goods
(Values in millions of dollars at current prices)

Products	*1965*	*Average 1965-1969*	*Average 1971-1973*	*1970*	*1971*	*1972*	*1973*	*1974*
Tin	93.0	94.4	116.5	101.9	105.9	113.5	130.0	229.4
Copper	3.5	6.9	10.2	12.5	8.3	8.8	13.4	16.0
Lead	5.7	5.8	6.7	7.8	5.9	5.8	8.3	11.5
Zinc	4.2	4.9	18.8	14.3	15.3	15.4	25.7	36.8
Bismuth	1.4	1.9	4.3	8.0	5.8	2.6	4.4	12.7
Tungsten	2.2	7.2	11.6	17.6	13.6	10.3	11.0	20.3
Antimony	5.9	6.9	11.8	31.0	9.0	9.1	17.2	29.1
Sulphur	0.2	1.2	0.6	0.5	0.3	0.5	1.1	1.0
Silver	5.3	8.1	9.5	10.5	8.3	7.6	12.6	86.8
Gold	2.9	1.6	0.5	0.5	0.3	0.6	...	...
Crude oil	0.7	15.7	34.8	13.2	23.9	31.7	48.9	160.8
Natural gas	–	–	14.0[a]			9.9	18.1	24.2
Cotton fibre	–	–	7.0	3.0	3.8	7.6	9.7	21.3
Coffee	–	–	4.4	3.8	2.6	4.7	5.9	3.9
Sugar	–	–	6.4[a]			0.4	12.4	16.9
Timber	–	–	5.7[a]			3.7	7.7	10.4
Total	*128.9*	*162.9*	*264.4*	*225.6*	*215.9*	*240.4*	*336.8*	*621.1*

SOURCE: ECLA estimates based on official data.

[a] 1972-1973.

Table 14. Bolivia: percentage structure of exports of goods

Products	1975	Average 1965-1969	Average 1971-1973	1970	1971	1972	1973	1974
Tin	72.1	57.9	44.1	45.2	49.1	47.2	38.6	36.9
Copper	2.7	4.2	3.9	5.5	3.8	3.7	4.0	2.7
Lead	4.4	3.6	2.5	3.5	2.7	2.4	2.5	1.9
Zinc	3.3	3.0	7.1	6.3	7.1	6.4	7.6	5.9
Bismuth	1.1	1.2	1.6	3.5	2.7	1.1	1.3	2.0
Tungsten	1.7	4.4	4.4	7.8	6.3	4.3	3.3	3.3
Antimony	4.6	4.2	4.5	13.7	4.2	3.8	5.1	4.7
Sulphur	0.2	0.7	0.2	0.2	0.1	0.2	0.3	0.2
Silver	4.1	5.0	3.6	4.7	3.8	3.2	3.7	4.3
Gold	2.2	1.0	0.2	0.2	0.1	0.2	...	...
Crude oil	0.5	9.6	13.2	5.9	11.1	13.2	14.5	25.9
Natural gas	–	–	5.3[a]	–	–	4.1	5.4	3.9
Cotton fibre	–	–	2.6	1.3	1.8	3.2	2.9	3.4
Coffee	–	–	1.7	1.7	1.2	2.0	1.8	0.6
Sugar	–	–	2.4[a]	–	–	0.2	3.7	2.7
Timber	–	–	2.2[a]	–	–	1.5	2.3	1.6
Total	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*

SOURCE: Table 12.

[a] Average 1972-1973.

five-year period 1965-1969, tin, which at the time was the only really important export item, accounted for 58 per cent of the total values of exports, in 1974 it accounted for only 37 per cent. On the other hand, most of the other exports of minerals, particularly oil, increased their share (see table 14).

During the first years of the 1970s a stage of diversification began in exports. A comparison of the structure existing during the last decade with that of 1974 speaks for itself. Products like oil, natural gas, sugar and cotton reached fairly high levels. This has made it possible to rise above Bolivia's traditional one-export system which in the past made the country extremely vulnerable to fluctuations in tin prices. Although the present export base is largely concentrated in a limited number of items, it represents a definite strengthening of external trade, especially if the increase in the prices of primary products is taken into account.

It should, however, be pointed out that the above-mentioned diversification exclusively involves primary products with a minimum of industrial processing. This constitutes a basic feature in the interpretation of the entire economic process, and particularly in the analysis of inflation. The export centres are severed from the rest of the economy, thus determining the alarming disparities in productivity indicated above. This is the root of one of the difficulties which prevents Bolivia from taking full advantage of the bonanza in its external sector in the last two years.

The accelerated increase in the value of exports in 1973-1974, and the variations in their structure, were determined to a large extent by the changes in international prices.

Table 15 gives the price and quantum factors which determined the increase in the current value of exports. It may be observed that in 1971 and 1972 export prices were much lower than 1970, while the considerable increase in the export quantum cushioned the adverse effect of the decline in these prices. The situation was reversed in 1973 and 1974; the export quantum increased by 2 per cent in 1973 and decreased by 3.3 per cent in 1974, compared with an annual growth in prices of 33 per cent in 1973 and 111 per cent in 1974. These uneven variations in volume and value should be noted since they will be useful in the analysis of inflation.

(ii) *Evolution of imports.* The current value of imports increased steadily during the three-year period 1971-1973, with an annual increase of 8 per cent in 1971 and 1972 and 28 per cent in 1973 (see table 16). A comparison of the annual average for the period 1966-1970 with that of the

Table 15. Bolivia: indices of prices, quantum and value of exports
(*1970 = 100*)

	1971	1972	1973	1974
Price index	84	87	116	245
Quantum index	111	119	121	117
Value index	93	104	140	287

SOURCE: ECLA estimates based on official statistics on exports of goods in terms of FOB values.

Table 16. Bolivia: structure of imports of goods
(Millions of dollars at current prices)

	1970	*Percentage of total*	*1971*	*Percentage of total*	*1972*	*Percentage of total*	*1973*[a]	*Percentage of total*
1. *Consumer goods*	*32.3*	*20.3*	*34.2*	*21.5*	*34.6*	*20.1*	*65.2*	*25.5*
(*a*) Non-durable consumer goods	22.5	14.1	24.7	15.5	26.5	15.4	39.6	15.5
(*b*) Consumer durables	9.8	6.2	9.5	6.0	8.1	4.7	25.6	10.0
2. *Raw materials and intermediate products*	*59.9*	*37.6*	*53.4*	*33.6*	*51.0*	*29.6*	*69.3*	*27.1*
(*a*) Fuels and related products	1.1	0.7	1.2	0.8	1.7	1.0	2.2	0.9
(*b*) Raw materials and intermediate goods for agriculture	2.4	1.5	2.0	1.3	2.1	1.2	2.6	1.0
(*c*) Raw materials and intermediate goods for industry	56.4	35.4	50.2	31.5	47.2	27.4	64.5	25.2
3. *Capital goods*	*66.2*	*41.6*	*71.3*	*44.8*	*84.6*	*49.1*	*119.0*	*46.4*
(*a*) Construction materials	8.8	5.5	15.4	9.7	14.5	8.4	29.0	11.4
(*b*) Capital goods for agriculture	3.2	2.0	3.0	1.9	4.1	2.4	6.0	2.3
(*c*) Capital goods for industry	26.4	16.6	31.3	19.7	31.5	18.3	49.0	19.2
(*d*) Transport equipment	27.8	17.5	21.4	13.5	34.5	20.0	35.0	13.7
4. *Miscellaneous*	*0.8*	*0.5*	*0.2*	*0.1*	*2.2*	*1.2*	*2.0*	*0.8*
Total CIF value	*159.2*	*100.0*	*158.9*	*100.0*	*172.4*	*100.0*	*255.5*	*100.0*
Adjustments[b]	–		9.1		13.0		–	
Total CIF value adjusted	159.2		168.0		185.4		255.5	
Deduction for freight, insurance and other costs	−24.0		−25.2		−32.2		−48.1	
Addition for contraband	31.0		38.6		42.6		42.1	
Total FOB value	*166.2*		*181.4*		*195.7*		*249.5*	

SOURCE: *Boletín Estadístico del Banco Central de Bolivia*, June 1974.

[a] Estimates of the Central Bank of Bolivia.

[b] Including imports of wheat flour and other products.

three-year period 1971-1973 also shows a steady upward trend. To judge by the rates of increase, however, growth became more pronounced as from 1973. Preliminary estimates for 1974 place the current value of imports of goods at a level bordering on 370 million dollars, which would imply a growth rate of around 57 per cent compared with 1973. The result of these increases was that the current value of imports of goods doubled in the space of two years.

From the point of view of the structure of imports, it is noteworthy that the share of capital goods does not show a more definite upswing. On the contrary, imports of consumer goods increased considerably in 1973, and their share of the total rose by over 25 per cent. Preliminary estimates for 1974 indicate higher rates of growth, especially of consumer durables, which, as is obvious, are destined for a small sector of the population. The dynamism of imports of consumer goods, to the detriment of imports of capital goods and intermediate products, brings to light a basic problem in the growth of the Bolivian economy. The relaxation of external restrictions took a rapid and easy route to spending in the form of imports of consumer goods, implying an allocation of resources which was not in keeping with the priorities assigned by the Government to purely productive activities. In addition, imports of capital goods for agriculture, the economy's major sector, were worth only 6 million dollars in 1973, which represented 2.3 per cent of total imports (see table 16). The policy of allocating resources, particularly for imports, has very important effects on inflation in Bolivia. Equally important in this context is the estimated amount of smuggling, which would certainly increase if this estimate, instead of being based on foreign currency sales, were also to take into account illegal two-way operations,[44] which, being illegal, do not necessarily imply any purchase of foreign currency.

The variations in the current value and in the structure of imports, may be explained by variations in prices and in quanta. Table 17 shows the respective indicators. The rising trend of import prices showed a sharp acceleration: 2 per cent in 1971, 6 per cent in 1972, 18 per cent in 1973 and 23 per cent in 1974.

The import quantum also grew at increased rates. Of particular importance is the 1973 rate, which exceeded by 8 per cent the volume of the previous year's imports, and the 1974 rate which

[44] Earnings from illegal exports make it possible to finance external purchases of goods which in turn are smuggled into the country. This traffic does not necessarily assume any purchase of foreign exchange from the Central Bank.

Table 17. Bolivia: indices of prices, quantum and value of imports
(1970 = 100)

	1971	*1972*	*1973*	*1974*
Price index . .	102	108	127	156
Quantum index .	106	108	117	150
Value index . .	108	117	149	234

SOURCE: ECLA, on the basis of official statistics.

resulted in an increase of 28 per cent (see table 17). Although these increases are considerable, export prices rose so much that the trade balance showed a surplus in 1974 and paved the way for large-scale increases in international reserves, as will be seen below.

Estimates of the structure of imports in 1974 are still not available. Data of this type will be useful for evaluating to what extent the disappearance of the external bottleneck meant that advantage had been taken of this favourable economic situation. Of particular importance is the performance of imports in analysing the imported inflation which afflicted Bolivia as from 1973.

(iii) *The balance of payments.* As noted above the real boom in Bolivia's external situation only began at the end of 1973. Up till then, the trade balance showed a continuing deficit. A comparison of the average deficits for the period 1966-1970 with those for the three-year period 1971-1973 shows that they increased to a fairly considerable extent (see table 18). It should be noted, however, that the deficit, particularly in 1973, was not actually due to external trade difficulties, as was the case traditionally. The traditional deficits were to be explained by the slow growth of exports which did not allow foreign exchange requirements to be met. The situation in 1972 and particularly in 1973 was quite different: despite an appreciable increase in exports, imports outstripped them. In each case, therefore the trade deficit had different implications.

The heavy current account deficits are accounted for not only by the trade deficits; the sums corresponding to payments of profits and interest on foreign capital were also considerable (see table 18). These items actually accounted for nearly 50 per cent of the current account deficit in the period 1966-1970, and around 40 per cent in the three-year period 1971-1973. It is to be noted that in 1971 these payments on foreign capital were more than the current account deficit.

In the three-year period 1971-1973 the current account showed a considerable deficit, i.e., an average of over 50 million dollars, or more than 20 per cent of the total value of exports, In 1973 it exceeded 54 million dollars, although exports

Table 18. Bolivia: balance of payments
(Millions of dollars at current prices)

	Average 1966-1970	*1970*	*1971*	*1972*	*1973*	*1974*	*Average 1971-1973*
Current account							
Exports of goods and services	176.5	210.3	198.3	224.4	298.5	591.5	240.4
Goods FOB	163.9	195.7	181.9	203.0	273.3	560.0	219.4
Services	12.5	14.6	16.4	21.4	25.2	31.5	21.0
Imports of goods and services	199.2	210.7	227.5	260.5	334.4	503.9	274.1
Goods FOB	158.3	166.2	181.4	195.7	252.8	390.0	210.0
Services	40.8	44.5	46.1	64.8	81.6	113.9	64.1
Net external investment income	−19.5	−25.0	−17.0	−21.6	−23.2	−21.1	−20.6
Profits	−13.1	−17.0	−8.4	−6.0	−6.5	−8.1	−7.0
Interest	−6.4	−8.0	−8.6	−15.6	−16.7	−13.0	−13.6
Net private transfer payments	1.0	1.5	2.1	4.9	4.9	5.0	4.0
Balance on current account	−41.2	−23.9	−44.1	−52.8	−54.2	71.6	−50.4
Capital account							
Net external financing ($a + b + c + d + e$)	41.2	23.9	44.1	52.8	54.2	−71.6	50.4
(*a*) Net external non-compensatory capital	49.1	41.7	67.7	104.2	55.4	82.5	75.8
Direct investment	−11.6	−75.9	1.9	−10.5	4.7	1.3	−1.3
Long- and medium-term loans	66.0	131.2	82.6	140.4	81.6	148.3	101.5
Amortization payments	−16.7	−20.4	−22.0	−30.7	−48.5	−62.2	−33.7
Short-term liabilities	1.9	4.4	0.2	−3.6	6.9	−10.9	1.2
Official transfer payments	9.5	2.4	5.0	8.6	10.7	6.0	8.1
(*b*) Domestic non-compensatory capital or assets	−2.7	−6.1	1.7	−17.0	−0.4	−27.3	−5.2
(*c*) Errors and omissions	−6.1	−13.0	−31.6	−33.7	−7.1	−7.1	−24.1
(*d*) Allocation of SDRs	1.0	4.9	4.0	4.2	–	–	2.7
(*e*) Net compensatory financing (increase −)	−0.2	−3.6	2.3	−4.9	6.3	−119.7	1.2

SOURCE: ECLA, on the basis of official statistics.

showed a growth rate of more than 33 per cent.

The financing of these current account deficits meant that debts were incurred abroad; these reached appreciable amounts in the various years of the present decade (see table 18). This process in turn generated amortization payments and interests which then in the course of time brought pressure to bear on the external trade balance. The 1972 debt is noteworthy; it exceeded 140 million dollars, and nearly tripled the current account deficit.

Direct investment did not reach levels of importance. The disinvestment to be observed in 1970 corresponded to the nationalization of the assets of the Gulf Oil Company. The item errors and omissions, particularly in 1971 and 1972, reached considerable proportions; this balancing item summed up the lack of accurate results in other items, particularly the estimates on smuggling commented on above.

Balance-of-payments estimates for 1974 give a current account surplus of 72 million dollars, and also an increase in international reserves of approximately 120 million dollars, which is largely attributable to the external medium- and long-term loans obtained (148 million dollars). The resurgence of inflation during this period is closely associated with these movements, among other reasons because of the increase in liquidity which gave rise to the accumulation of reserves as will be seen below.

The evolution of prices and quantities of exports and imports during the period 1971-1974 resulted in an adverse effect, amounting to considerable sums, on the terms of trade. As may be seen in table 19, the main indicators resulting from these developments reveal situations which had clearly degenerated in comparison with 1970.[45]

The upsurge in 1974 export prices resulted in a positive terms-of-trade effect but did not represent a full recoupment, despite the fact that forecasts for 1975 anticipate considerable increases in import prices.

[45] In order to interpret these indicators it should be recalled that 1970 was a period of a certain upsurge in the export prices of mineral products. On the other hand, it should be noted that in the calculation of the export price index, the structure of exports corresponds to 1973; the share of petroleum increased significantly in 1974 thus changing the structure.

Table 19. Bolivia: external trade indicators
(Millions of dollars at 1970 prices)

	1971	*1972*	*1973*	*1974*
Export quantum	232.1	255.6	264.5	254.5
Purchasing power of exports	194.4	207.8	235.0	400.0
Terms-of-trade effect	−37.7	−47.8	−29.5	145.5
Index of the terms of trade (1970 = 100)	82	81	91	157.1

SOURCE: ECLA, on the basis of official data.

Table 20. Bolivia: total supply and demand

	Millions of pesos 1970	*Annual growth rate*						
		1965-1970	*1970-1974*	*1970*	*1971*	*1972*	*1973*	*1974*[a]
Total supply	*14,604*	*5.9*	*6.4*	*3.1*	*4.2*	*6.4*	*6.1*	*8.8*
Gross domestic product (at market prices)	12,080	6.3	5.2	5.2	3.8	6.0	5.4	5.7
Imports	2,524	3.9	11.2	−6.1	5.8	8.1	9.2	22.6
Total demand	*14,604*	*5.9*	*6.4*	*3.1*	*4.2*	*6.4*	*6.1*	*8.8*
Exports	2,504	8.6	4.7	−3.5	10.4	10.1	3.5	−4.4
Gross domestic investment	1,880	5.3	7.2	2.2	−0.7	−11.2	27.6	18.0
Gross fixed investment	1,666	5.9	...	0.3	8.8	−17.8	...	...
Public	1,053	15.2	...	13.8	...	...	...	...
Private	613	−2.9	...	−16.7	...	...	...	...
Total consumption	10,220	5.4	6.9	5.0	3.5	5.0	3.7	10.5
General Government	1,351	6.9	10.3	17.0	−7.3	14.0	5.4	10.0
Private	8,869	5.2	6.3	3.4	5.2	3.5	3.4	10.6

SOURCE: ECLA, on the basis of official statistics.

[a] Preliminary figures.

(b) *Over-all supply and demand*

The performance of supply showed no appreciable change if the period 1970-1974 is compared with the period 1965-1970. The annual rates of growth were 6.4 per cent and 5.9 per cent respectively (see table 20). It should be mentioned that in 1972, 1973 and 1974 supply grew at rather faster rates than in 1970 and 1971.

The drop in the growth rate of the product recorded in the period 1970-1974 when the average annual rate was 5.2 per cent, compared with 1965-1970, when the average annual rate was 6.3 per cent, was offset by increases in imports, the growth rate of which increased from an annual 3.9 per cent to 11.2 per cent between the two periods. During the period 1970-1974, the product showed considerable fluctuations, while imports grew at an increasing pace (see table 20).

No major changes are to be seen in the structure of supply. The import coefficient, which dropped from 23.5 per cent in 1965 to 22.1 per cent during the period 1969-1970 and to 21.9 per cent in the three-year period 1971-1973, reversed its trend in 1974, rising to 26.3 per cent. The low level of the imports in 1970 should be taken into account to give an idea of the real scope of the variations in rate and relative share (see table 21).

As regards total demand, the sharp fluctuations of its main components are particularly striking. Exports increased by over 10 per cent in some years and dropped significantly in others. The average rate of 4.7 per cent for the period 1970-1974 was appreciably lower than the rate for the years 1965-1970 (see table 20).

In line with these movements, the export coefficient also fluctuated between a maximum of 22.8 per cent in 1972 and a minimum of 20.5 per cent in 1974.

Gross domestic investment fluctuated somewhat erratically with disinvestments in 1971 and particularly in 1972, and rates of increase of 27.6 per cent in 1973 and 18 per cent in 1974. Capital formation decreased noticeably in the years 1971 and 1972, but started to recover vigorously as from 1973 (see table 7). In line with the above trends, the investment coefficient declined up to 1973 in comparison with the figures for the second half of the 1960s, and rose sharply in 1974 (see table 21).

Total consumption showed an increasing trend over the periods compared. There were, however, fluctuations of some consideration between the years 1970 and 1974. In 1971 the growth rate was 3.5 per cent and 1973 it was 5 per cent, contrasting with growth rates recorded for 1972 and 1974 which were 8.6 and 10.5 per cent, respectively. These fluctuations may be explained in the main by variations in government consumption: a decrease of 7.3 per cent in 1971 vis-à-vis an increase of 28 per cent in 1972 (see table 20).

Of some note is the growth of private consumption which reached an annual rate of 6.3 per cent in the period 1970-1974 and only 3.5 per cent in 1973. Rates of this order, which are the result of taking the average consumption of sectors and population centres with very different purchasing power, mask particularly delicate situations for those strata whose incomes are close to the critical poverty level. Total consumption showed no significant changes in its share of over-all demand in recent years; though private consumption showed a decline in 1973, its relative importance was balanced by the increases in

Table 21. Bolivia: structure of total supply and demand[a]
(Percentages)

	1965	*Average 1969-1970*	*1970*	*1971*	*1972*	*1973*	*1974*	*Average 1971-1974*
Total supply	*123.5*	*122.1*	*120.9*	*121.3*	*121.7*	*122.5*	*126.3*	*122.9*
Gross domestic product	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Imports	23.5	22.1	20.9	21.3	21.7	22.5	26.3	22.9
Total demand	*123.5*	*122.1*	*120.9*	*121.3*	*121.7*	*122.5*	*126.3*	*122.9*
Exports	18.7	21.6	20.7	22.0	22.8	22.5	20.5	21.9
Gross domestic investment	16.4	15.8	15.6	14.9	12.5	15.0	18.8	15.3
Gross fixed investment	14.1	14.1	13.8	14.5	11.2	...	...	
Public	8.2	8.4	8.7	...	...	...	...	
Private	5.9	5.7	5.1	...	...	...	...	
Total consumption	88.4	84.7	84.6	84.4	86.4	85.0	87.1	85.7
General Government	10.9	10.6	11.2	10.0	12.1	12.1	12.6	11.7
Private	77.5	74.1	73.4	74.4	74.3	72.9	74.5	74.0

SOURCES: Table 20 and ECLA estimates.

[a] 1970 prices.

government consumption; in 1974, however, it increased noticeably (see table 21).

(c) *The evolution of the product by sectors*

The growth rates of the sectoral product during the period 1970-1974 are, generally speaking, lower than those of the period 1965-1970 (see table 22). Of particular importance is the decline in the growth of the mining product, the rate of which dropped from 11 per cent to 4 per cent between the two periods referred to, and that of industry, which during the first-mentioned period increased at an annual rate of 6.4 per cent, and during the period 1970-1974 at a rate of 5.5 per cent.

Although the agricultural product had a higher rate of growth (2.8 per cent during the period 1970-1974 compared with an annual 0.2 per cent during the period 1965-1970), its rates of growth have generally been rather lower than that of the population. Since this sector is the most important in the country's economy, its lack of dynamism severely affects over-all growth and as will be seen below, constitutes one of the deepest-rooted causes of inflation in Bolivia.

Among the goods-producing sectors the only activity which showed some dynamism was the construction sector, which increased its growth rate from 1.8 per cent during the period 1965-1970 to 8.3 per cent in 1970-1974.

In the basic services sector it should be mentioned that the electricity, gas, water and sanitary services sector showed a high rate of growth compared with those of other sectors of the economy during the period 1970-1974, although it was appreciably lower than in the period 1965-1970. The transport and communications sector, which is of vital importance in view of the geography of Bolivia, was another activity whose growth rate decreased, although there was some degree of recovery from 1972 onwards (see table 22).

The loss of dynamism spread to all the services sectors between the periods compared. The annual growth rate for these as a whole was 8.6 per cent during the period 1965-1970, and only 6 per cent between the years 1970 and 1974. As may be observed, in 1972, 1973 and 1974 the growth rates of the majority of these activities were higher than those of 1971.

The trend of the different sectors of the economy was towards a fairly generalized loss of dynamism which no doubt constituted fertile ground for the growth of inflation in Bolivia.

Reference was made above to the structural factors which slow down development and feed the roots of the inflationary process. It is useful here to analyse in detail the structure of the gross product, which clearly illustrates the lack of integration in the Bolivian economy (see table 23). One of the most striking facts is the small share of the industrial sector. Its contribution to the product does not exceed 13 per cent, and has remained unchanged since 1965. This marked stability in the share of a sector called upon to integrate and reactivate the economy indicates the existence of very deep-seated and complex problems.

As a result of its slow growth, the agricultural sector showed a decrease in its contribution to the

Table 22. Bolivia: gross domestic product at factor cost, by sectors of economic activity

	Millions of pesos 1970	*Annual growth rate*						
		1965-1970	*1970-1974*	*1970*	*1971*	*1972*	*1973*	*1974*
Agriculture	1,901	0.2	2.8	4.4	4.0	2.0	2.1	3.5
Mining	1,670	11.0	4.0	5.2	4.2	9.1	3.0	–
Manufacturing	1,446	6.4	5.5	5.4	2.8	6.7	6.5	6.0
Construction	507	1.8	8.3	−3.7	4.1	8.0	7.2	14.0
Subtotal goods	*5,524*	*4.7*	*4.5*	*4.1*	*3.8*	*5.9*	*4.0*	*4.2*
Electricity, gas, water and sanitary services	218	11.1	7.8	7.4	6.9	8.8	9.6	6.1
Transport and communications	996	5.6	4.8	2.6	3.3	4.8	5.0	6.0
Subtotal basic services	*1,214*	*6.5*	*5.3*	*3.4*	*4.0*	*5.5*	*5.9*	*6.0*
Commerce and finance	1,265	7.1	6.0	1.6	1.9	6.4	7.0	9.0
Ownership of dwellings	978	9.3	6.7	10.7	4.3	10.5	6.0	6.0
Government	1,021	7.0	5.8	8.5	6.3	3.6	8.2	5.0
Miscellaneous services	1,232	11.2	5.5	10.8	4.3	4.9	4.8	8.0
Subtotal other services	*4,496*	*8.6*	*6.0*	*7.5*	*4.1*	*6.2*	*6.5*	*7.1*
Total	*11,234*	*6.3*	*5.2*	*5.2*	*3.8*	*6.0*	*5.4*	*5.7*

SOURCE: ECLA, on the basis of official statistics.

Table 23. Bolivia: structure of the gross domestic product by sector of economic activity[a]
(*Percentages*)

	1965	*Average 1966-1970*	*1970*	*1971*	*1972*	*1973*	*1974*	*Average 1971-1974*
Agriculture	22.8	19.0	16.9	17.0	16.3	15.8	15.8	16.2
Mining	12.0	14.6	14.9	14.9	15.3	15.0	12.6	14.5
Manufacturing	12.8	12.9	12.9	12.8	12.8	13.0	13.0	12.9
Construction	5.6	4.5	4.5	4.5	4.6	4.7	4.7	4.6
Subtotal goods	*53.2*	*51.1*	*49.2*	*49.1*	*49.1*	*48.5*	*46.2*	*48.2*
Electricity, gas, water and sanitary services	1.6	1.9	1.9	2.0	2.0	2.1	2.1	2.1
Transport and communications	9.2	8.9	8.9	8.8	8.7	8.7	8.9	8.8
Subtotal basic services	*10.7*	*10.8*	*10.8*	*10.8*	*10.8*	*10.8*	*11.0*	*10.9*
Commerce and finance	10.9	11.4	11.3	11.1	11.1	11.3	12.8	11.6
Ownership of dwellings	7.6	8.0	8.7	8.7	9.1	9.2	8.3	8.8
Government	8.8	8.9	9.1	9.3	9.1	9.3	10.6	9.6
Miscellaneous services	8.8	9.8	11.0	11.0	10.9	10.8	11.0	10.9
Subtotal other services	*36.1*	*38.1*	*40.0*	*40.1*	*40.2*	*40.6*	*42.8*	*40.1*
Total	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*

SOURCE: Table 22.
[a] The absolute values which gave rise to these percentages are expressed in pesos at 1970 prices.

product: 22.8 per cent in 1965, 19 per cent on average in the five-year period 1966-1970, and 15.8 per cent in 1974. These coefficients and the obstacles of a structural nature which affect the agricultural sector, make further analyses unnecessary in order once again to point out that it is here that the root of a great part of the country's underdevelopment is to be found, and that it constitutes the main source of disequilibria which take the form of inflationary pressures.

The mining sector slightly increased its share in the first three years of the present decade; in 1974 it decreased significantly. The construction sector showed no appreciable changes. The goods-producing sectors as a whole had a smaller share during the period 1971-1974 (48.2 per cent) than during the period 1966-1970 (51.1 per cent). The sectors producing basic services did not undergo any changes, while the share of tertiary activities, which are less important to the country's development, increased.

For the purposes of the description of inflation begun in the next chapter, and with a view to placing in order of importance the problems of the functioning of economic activity in Bolivia, it should be pointed out that, as has been already suggested, the virtual standstill of the agricultural sector and the slow tempo of economic activity in the industrial sector are the most far-reaching problems, to the extent of preventing any real advantage being taken of the dynamism of the external sector; the description of the recrudescence of inflation in Bolivia will come back to this point.

C. THE INFLATIONARY PROCESS IN BOLIVIA

1. *Perspective of periods and phases*

In order to study the current inflationary cycle in Bolivia which started in mid-1972, some data which help to interpret this process must be taken into account.

During the whole of the 1960s and up to the middle of 1972, domestic price trends were exceedingly stable. This long period of stability was directly attributable to the agents of the economic process, although it was preceded by a period of acute inflation and chronic shortages in the years 1953-1958. In other words, between 1950 and 1972 Bolivia had experienced completely opposite phenomena: great stability and runaway inflation. The behaviour of consumers and producers, of entrepreneurs and wage-earners, from October 1972 onwards is accounted for by such contrasting experiences. It is necessary to assess the true dimension of this type of eminently qualitative factor in attempting to explain inflation in recent years, which clearly had some very special features.

The existence of such pronounced cycles of stability and inflation would seem to be linked with a special form of operation of socio-economic activity within the context of marked structural heterogeneity, as noted above. In fact, structural heterogeneity is a key factor in analysing both types of situations: stability and inflation. The external, internal or combined situations of disequilibria are reflected in pressures on prices rather

than in correlative structural changes, precisely because of the production apparatus' limited capacity to respond and, in particular, the inflexible nature of agricultural supply, which undoubtedly constitutes the essence of structural heterogeneity in the economic sphere. The two attempts made to reactivate the economy through public expenditure (in 1952 and 1972) resulted for this reason in acute inflation.

Conversely, the long period of stability starting in 1959 and ending in 1972 was basically the outcome of the structural heterogeneity itself and of the socio-political controls on pressure groups, although at the expense of little change in the basic economic structure and the attainment of fairly mediocre rates of growth. With these sacrifices and such an expedient, it was not difficult in the circumstances to control price levels throughout most of the period concerned. Contrary to what happens in more industrialized countries, the lack of coordination in the economic system prevents the disequilibria occurring separately in the various activities from spreading too easily to the rest of the system, which, paradoxically enough, is an advantage if the objectives are confined to the achievement of stability. Accordingly, in the period 1969-1971 when attempts were made to attain other additional objectives, the maintenance of price levels entailed a much stricter management of the whole financial system, limiting the possibilities of greater economic growth.

Although the recent inflation in Bolivia differs in nature from previous inflationary cycles, the explanation for it is again mainly the uncoordinated type of structure which, as well as being the basic factor of inflation, is propitious ground for the spread, in both scope and depth, of another type of internal and external disequilibria in economic activity, as will be seen below.

The kind of perspective suitable for a study of this inflationary process requires, however, that stress be laid on the following questions which have already been described in the development of the over-all economy: the problems facing the agricultural sector, the backward state of industry and external sector trends.

It will be recalled that agriculture is the main productive activity of the Bolivian economy, its contribution to the product—while showing significant reductions in recent years—still represents annual proportions of around 16 per cent, and about two thirds of the labour force is engaged in agricultural activities. It is easy to see the effect of its virtual stagnation on price trends; the type of goods this sector produces is closely associated with basic food consumption.

It must be borne in mind that industry is of little importance as a productive activity and that the composition of manufacturing output mainly responds to demand from the higher-income strata. Processing methods are fairly primitive and growth is achieved at the expense of heavy dependence on imports of raw materials.

The evolution of the external sector in recent years is another crucial factor in interpreting Bolivia's inflation. As was also shown in the previous section, the extraordinary increase in price of most export and import items led to an external relations situation which, as will shortly be seen, had a direct and indirect incidence on the inflationary process.

2. *Over-all view*[46]

As stated previously, following a long period of stability, a new inflationary cycle was initiated in Bolivia in the middle of 1972. Table 24 shows the contrast between the price increases in both periods. It will be noted that in 1972 the rate of price variations showed an increase over the previous three-year period, although being comparisons of annual averages, the prices still did not reflect the proportions they were likely to reach after the phenomenon itself. In 1973 the rate was already significant and in 1974 it was double the 1973 rate. The figures in table 25 show more precisely that the start of the recent inflation was in the second half of 1972, and more clearly reflect the acceleration process. Prices rose during that period by 23.3 per cent in contrast with the small increases in the index for previous six-month periods. The six-monthly variations from June 1973 onwards clearly show the inflationary spiral. During the second half of 1974, however, the rise in prices fell off considerably.

Although the price increases leave no room for doubt regarding the virulence of the inflation, the significant changes in the price system, in their turn, constitute another peculiar feature of the phenomenon. The price trends of the various

[46] It is difficult to classify an inflationary process on the basis of only one price index which, moreover, is clearly inadequate as an indicator of inflation. The more so if an attempt is made to interpret a process that is more complex than previous inflationary cycles, the full effects of which have still to be felt. To analyse a past phenomenon, of which the complete cycle of development and effects are known, is very different from analysing one which has just started, of which only the broadest effects are known in the light of such scant information. Therefore, the various quantitative assessments made in this study must be taken only as rough figures which are not as accurate as might have been desired. It is not possible to elucidate a number of phenomena, particularly those related to the differences between producer, wholesale and consumer prices, which reflect decisive instances in an inflationary process.

Table 24. Bolivia: consumer price index
(1966 = 100)

Year	General index	Annual variation	Food	Annual variation	Housing	Annual variation	Clothing	Annual variation	Miscellaneous	Annual variation
1963 . .	82.5	–	86.6	–	75.8	–	77.8	–	93.9	–
1964 . .	90.9	10.2	88.9	2.7	90.8	19.8	94.2	21.1	94.5	0.6
1965 . .	93.5	2.9	91.6	3.0	92.6	2.0	97.3	3.3	96.5	2.1
1966 . .	100.0	7.0	100.0	9.1	100.0	8.0	100.0	2.8	100.0	3.6
1967 . .	111.2	11.2	116.1	16.1	112.3	12.3	100.4	0.4	102.1	2.1
1968 . .	117.3	5.5	124.7	7.4	118.0	5.1	102.2	1.8	103.8	1.7
1969 . .	119.9	2.2	127.3	2.1	120.5	2.1	105.3	3.0	105.9	2.0
1970 . .	124.5	3.8	133.1	4.6	125.2	3.9	109.2	3.7	107.0	1.0
1971 . .	129.1	3.7	138.4	4.0	130.7	4.4	114.3	4.7	107.6	0.6
1972 . .	137.5	6.5	147.2	6.4	138.1	5.7	124.6	9.0	113.8	5.8
1973 . .	180.8	31.5	198.6	34.9	158.6	14.8	172.8	38.7	147.5	29.6
1974 . .	294.3	62.8	360.9	81.7	193.7	22.1	252.5	46.1	199.7	35.4

SOURCE: National Institute of Statistics.

Table 25. Bolivia: consumer price index
(1966 = 100)

Period	General index	Half-yearly variation	Food	Half-yearly variation	Housing	Half-yearly variation	Clothing	Half-yearly variation	Miscellaneous	Half-yearly variation
December 1970 .	127.6	–	137.0	–	128.0	–	112.2	–	107.2	–
June 1971 .	128.2	0.4	136.7	−0.2	131.1	2.4	113.7	1.3	107.9	0.6
December 1971 .	131.8	2.8	141.6	3.6	133.5	1.8	117.3	3.2	107.9	0.0
June 1972 .	132.1	0.2	140.2	−0.9	136.7	2.4	119.4	1.8	109.9	1.9
December 1972 .	162.9	23.3	175.9	25.5	151.6	10.9	152.5	27.7	137.5	25.1
June 1973 .	169.4	4.0	180.8	2.8	158.4	4.5	162.6	6.6	146.1	6.3
December 1973 .	219.5	29.6	254.7	40.9	172.1	8.6	202.1	24.3	159.2	9.0
June 1974 .	302.6	37.9	378.1	48.4	187.6	9.0	248.2	22.8	202.0	26.9
December 1974 .	305.0	0.7	368.6	−2.5	205.6	9.6	274.8	10.7	208.6	3.3

SOURCE: National Institute of Statistics.

components of the index show considerable disparities. Whereas food prices rose by 98.6 per cent between the base period and 1973, the increases in housing and miscellaneous items were 58.6 and 47.5 per cent, respectively, over the same period, and in clothing 72.8 per cent (see table 24). Although these variations reflect considerable changes in the price system, it must be borne in mind that they are the result of comparing averages for groups of products. The disparities in price variations for the individual products are much greater.

The changes in the price system became more pronounced from 1973 onwards, as may be noted from the six-monthly variations in the different components of the index (see table 25). The increases in food prices in the second half of 1973 and the first half of 1974 are twice those for clothing and five times those for housing. Although the second half of 1974 marked a decrease in food prices compared with rises for the other components, this failed to offset the changes in relative prices which took place in earlier periods. In view of the size of the variations in

relative prices, there is reason to think that the indicator used (the only one available) does not faithfully reflect the real variation, or that the market mechanisms, which are generally sensitive to this type of phenomenon, are not operating as efficiently as is usually believed, since price controls have gradually lost ground to the laws of supply and demand. This is a situation which merits a direct and thorough investigation since, however serious the limitations of the index, it does convey an idea of situations connected with the functioning of economic activity, particularly its structural rigidity, which would enable progress to be made in diagnosing Bolivia's inflation.

The above-mentioned changes in the price system and the rise in prices indicate the depth and complexity of Bolivia's inflationary process and its recent acceleration. The Government's efforts to control it have not so far produced the desired results. Note the progressively higher six-monthly rates of increase in prices: 30 per cent in the second half of 1973 and 38 per cent in the first half of 1974. The increase between June 1973 and June 1974 was 79 per cent (see table 25). The slowing down of the inflationary process observed in the second half of 1974 is an encouraging sign. Nevertheless, it will be necessary to verify in terms of price movements in 1975 whether inflation has really been controlled or whether it is merely a fleeting period of stability.

The following is an attempt to describe the development of this process and to identify the inflationary factors and the mechanisms reproducing the price increases. For this purpose, two phases in the last cycle of Bolivia's inflation may be distinguished. The first, covering 1972 and the early months of 1973, and the second, comprising the second half of 1973 up to the present (they can both be clearly identified in table 25. As will be seen later, each of these phases developed in a different context: the first responded to essentially internal factors, and the second to inflationary stimuli from abroad as well. It is worthwhile to emphasize, however, that in both these phases structural factors were an underlying constant, added to which was a different type of factor. In the first phase, the economic structure could not withstand the internal situations of disequilibrium and the interpretation of inflation is clear. The second phase, on the other hand, represents a complex inflationary situation in which the phenomenon operates with all its ingredients, i.e., situations of disequilibrium, structural rigidity and imported inflation, acting upon and simultaneously and mutually influencing one another.

(a) *First phase of inflation*

The first phase of the recent inflationary process derived primarily from internal factors: a sudden monetary expansion which, because of the serious structural problems confronting the country, was not accompanied by a similar growth in the real supply of goods and services. The Government's attempts to reactivate the economy and achieve more accelerated growth by increasing public expenditure and granting the private sector exceptionally favourable credit facilities caused disequilibria which unleashed a new inflationary process.

By the middle of 1972 a series of financial pressures clearly pointed to an upswing of domestic prices. The liquidity which had been injected into the system did not result in a parallel increase in the real supply of goods and services. The first symptom of this disequilibrium was the steady decline in international reserves caused mainly by essentially speculative operations and only secondarily by larger imports of goods that would really cover domestic needs. The monetary pressure to which the economy was subjected made it clear that a change in the value of the dollar was to be expected shortly. In fact, purchases of foreign exchange by the private sector in August, September and October 1972 were 31.4 per cent higher than those effected in the same months of 1971.[47]

In the face of the imminent exhaustion of international reserves at the end of October 1972, exchange parity was raised from 11.88 to 20 Bolivian pesos to the dollar. This devaluation is an important milestone in the first phase of the inflationary process. To understand it better, and in view of the considerable effect of this measure on the subsequent course of inflation, it is useful to review the main financial movements which took place in the months prior to devaluation. Table 26 shows the main components of the monetary balance and their variations over the period concerned. Monetary resources increased by 24.3 per cent during this period, as a result of increments of 20.4 and 53.5 per cent in money and quasi-money, respectively, which from a quantitative standpoint are the most important items. Counterpart funds[48] dropped by 30 per cent and other items showed an increase of 20 per cent (see table 26). The 24.3 per cent rise in total liquidity was due to an increase of 31.7 per cent in domestic credit. The private sector increased its credit by 44.2 per cent, and the public sector by 23.3 per cent, both rates being substantially higher than the previous annual increases.

Although the sharp reduction in international reserves, which was more acute in October 1972, acted as a factor of contraction, their small share

[47] Banco Central de Bolivia, *Memoria.*

[48] National currency counterpart funds for United States government credits.

Table 26. Bolivia: monetary balance

	September 1971	*Structure (percentages)*	*September 1972*	*Structure (percentages)*	*Percentage variation*
	Balances at end of each period in millions of pesos				
Structure of monetary resources					
(total liquidity)	*2,473.3*	*100.0*	*3,074.2*	*100.0*	*24.3*
Money (means of payment)	1,567.6	63.4	1,888.0	61.4	20.4
Quasi-money	437.4	17.7	671.4	21.8	53.5
Counterpart funds	93.7	3.8	65.4	2.2	−30.3
Other items (net)	374.6	15.1	449.4	14.6	20.0
Factors of expansion and contraction	2,473.2	100.0	3,074.6	100.0	24.3
International reserves	181.8	7.4	57.4	1.9	−68.4
Credit	2,291.4	92.6	3,017.2	98.1	31.7
(*a*) To the Government	1,376.5	55.7	1,697.6	55.2	23.3
(*b*) To the private sector	914.9	36.9	1,319.6	42.9	44.2

SOURCE: IMF, *International Financial Statistics*, November 1974.

in the total caused the financial picture to change only marginally. These sequences in the financial movements necessarily led to one of two crucial options: exchange control or devaluation. The seriousness of the financial situation and the important part played by the private sector in the adoption of decisions resulted in a modification of the exchange rate.

A 68 per cent devaluation of Bolivia's currency was bound to have a tremendous impact on the performance of the country's economic activity, which is heavily dependent on imported supplies. If, moreover, it is recalled that the exchange rate had not been altered since 1959 and that prices, in general, had been very stable, it will be understood that the effects of such a measure caused an upheaval in the whole economic and financial apparatus. As a result of this decision, domestic prices suffered violent increases, which must also be ascribed to subjective motivations in an atmosphere hypersensitized by the memory of the inflationary cycle in the 1950s which had had serious repercussions on the population's standard of living. In the eyes of producers and consumers, devaluation destroyed the principal symbol of confidence in the financial management. Keeping the exchange rate unchanged for 13 years had come to represent a general indicator of stability, even for sectors unrelated to the financial markets, far greater qualities being ascribed to it than it really merited. Such a drastic change seriously altered the behaviour of the agents of the economic process, which accounts for that initial period of upswing in prices.

The group of economic policy measures adopted simultaneously with the change in parity, particularly wage controls, and the lessening of the initial pressures tended to moderate the rise in prices. The consumer price index recorded an increase of 24 per cent in the month following devaluation, whereas in the first few days the increases were over 50 per cent and some as high as 100 per cent.[49]

External aid and contingency credit from the International Monetary Fund, which were granted simultaneously with the devaluation, strengthened the reserves position. At the same time, the new single and fixed parity and the elimination of controls on the unlimited purchase of foreign exchange were an attempt to re-establish general confidence, which had effects only in the short term. Thus, the price index showed a small increase in the first half of 1973.

The monetary balance at the end of 1972 compared with that for 1971 reflected more clearly, on the one hand, the sharp increases in over-all liquidity and on the other, the strengthening of reserves owing to the above-mentioned credit. In 1972, monetary resources rose by 43.1 per cent as a result of increases in all their components, including counterpart funds which went up at a rate of 310.8 per cent (see table 27). The extraordinary increase in total liquidity was due to the expansion of credit that year to both the public and the private sector, at rates of 21.2 and 39.2 per cent respectively, which are significantly higher than in previous years. Similarly, there was a considerable expansion of national currency due to the increase of 198.1 per cent in international reserves, whose share among the factors of expansion rose from 8.8 per cent in 1971 to 18.2 per cent in 1972 (see table 27).

It is useful now to examine the reasons why the monetary expansion reached these proportions.

[49] It will be recalled that the increases shown by this index are underestimates of the real variations over the short term.

Table 27. Bolivia: monetary balance

	1969	Rate	1970	Rate	1971	Rate	1972	Rate
	Balances at end of each period in millions of pesos							
Structure of monetary resources								
(total liquidity)	*2,002.2*	*5.2*	*2,363.4*	*18.0*	*2,751.5*	*16.4*	*3,937.5*	*43.1*
Money (means of payment)	1,361.2	5.8	1,532.3	12.6	1,765.6	15.2	2,210.1	25.2
Quasi-money	305.9	35.7	382.1	24.9	493.1	29.0	634.2	28.6
Counterpart funds	120.8	−42.7	146.9	21.6	116.0	−21.0	476.5	310.8
Other items (net)	214.3	19.3	302.1	41.0	376.8	24.7	616.7	63.7
Factors of expansion and contraction	*2,002.2*	*5.2*	*2,363.4*	*18.0*	*2,751.4*	*16.4*	*3,937.5*	*43.1*
International reserves	237.7	8.8	292.6	23.1	241.0	−17.6	718.4	198.1
Credits	1,764.5	4.7	2,070.8	17.4	2,510.4	21.2	3,219.1	28.2
(*a*) To the Government	1,125.5	0.9	1,294.5	15.0	1,532.9	18.4	1,858.1	21.2
(*b*) To the private sector	639.0	12.1	776.3	21.5	977.5	25.9	1,361.0	39.2
			Structure (percentages)					
Factors of expansion and contraction	*100.0*		*100.0*		*100.0*		*100.0*	
International reserves	11.9		12.4		8.8		18.2	
Credit	88.1		87.6		91.2		81.8	
Credit	*100.0*		*100.0*		*100.0*		*100.0*	
(*a*) To the Government	63.8		62.5		61.1		57.7	
(*b*) To the private sector	36.2		37.5		38.9		42.3	

SOURCE: IMF, *International Financial Statistics*, November 1974.

The first was the increasing deficit in the fiscal budget, of which the main source of financing was currency issues by the Central Bank; the second was the pressure brought to bear by the private sector to obtain bank financing, which was granted by virtue of the development policy that anticipated a vigorous production response from this sector.

Table 28 shows the variations in the items which gave rise to these deficits in the 1972 fiscal year. Budget income rose by 18.7 per cent, and expenditure by 29.9 per cent. A noteworthy fact is the small growth of tax collections and the significant increase in personal services, materials and supplies, and in fixed and financial assets. This uneven growth of income and expenditure resulted in a deficit amounting to 32.2 per cent of total income in 1972, which meant an 84 per cent increase over the 1971 deficit. About 93 per cent of this deficit was financed with credit from the Central Bank, or, in effect, through currency issues. It will be noted that the deficit relates only to the current account of the fiscal budget; the total deficit, which includes the capital account, was double that, amounting to 928 million Bolivian pesos, or 67 per cent higher than in 1971.[50]

The increase in credit to the private sector referred to above was the other factor with distinctly inflationary repercussions. A growth of 39.2 per cent in this variable was bound to create short-term inflationary pressures, particularly if it had no direct or immediate counterpart in the way of bigger imports or domestic production.

If the increases in total liquidity, especially those deriving from the expansion of credit, are compared with the real trend of economic activity, particularly the supply of goods, it is not surprising that the system itself should have found its own natural corrective mechanisms, first in the reduction of reserves (up to October 1972) and then in drastic changes in the system and level of prices. In fact, in the face of a 43 per cent increase in total liquidity in 1972, the product grew by 6 per cent in real terms and imports by 8.1 per cent, which represents an increase of only 6.4 per cent in supply (see table 20). Such disparities inevitably provided fertile ground for definite inflation.

(b) *Acceleration of inflation*

The middle of 1973 marked another point of inflexion in Bolivia's inflation, since the consumer price index rose by 29.6 per cent in the second half of the year. The acceleration of inflation continued unabated, with the same index showing price increases of 37.9 per cent in the first half of 1974 (see table 25).

In this second phase of the recent inflation in Bolivia, the inflationary pressures deriving from the growing liquidity in the economy are still active, but in addition there are appreciable

[50] CIAP Sub-Committee on Bolivia, *El esfuerzo interno y las necesidades de financiamiento externo para el desarrollo de Bolivia*, 1974, table II-11.

Table 28. Bolivia: budgetary operations
(Millions of pesos)

	1970	*1971*	*1972*	*Percentage variation 1972*
Income	*1,070.2*	*1,120.4*	*1,330.0*	*18.7*
Internal revenue	399.3	511.7	565.3	10.5
Customs revenue	418.0	377.1	418.2	10.9
Revenue from medium- and small-scale mining	174.2	47.5	43.1	−9.3
Revenue from petroleum production	2.7	53.5	68.9	28.8
Other income	76.0	130.6	234.5	79.6
Expenditure	*1,248.7*	*1,353.4*	*1,758.7*	*29.9*
Personal services	675.1	832.0	1,009.5	21.3
Non-personal services, materials and supplies	157.2	152.7	224.4	47.0
Fixed and financial assets	16.9	6.7	19.0	183.6
Public debt	169.5	192.4	293.5	52.5
Current and capital transfers	227.5	160.9	174.8	8.6
Other expenditure	2.5	8.7	37.5	331.0
Deficit	178.5	233.0	428.7	84.0
Financing				
External credit	17.9	18.5	28.4	53.5
Central Bank credit	155.5	220.0	398.0	80.9
Balance of previous period	17.6	12.5	18.1	44.7
Balance at end of period	12.5	18.0	15.8	−12.2

SOURCE: Ministry of Finance, Office of the Under-Secretary of Financial Administration.

external inflationary pressures which find a propitious field for reproducing themselves locally. These two influences are examined below.

From the standpoint of total liquidity in the economy, it will be noted that its most important components—money and quasi-money—increased by 34.3 and 27.2 per cent respectively in 1973, maintaining their accelerated rate of growth. In contrast, counterpart funds and other items decreased appreciably, but, because of their smaller share in the total, they failed to counteract the expansion of money and quasi-money (see table 29). Therefore, monetary resources grew by 13.1 per cent in 1973. In view of this apparently low rate, which is below that of previous periods, two warnings are necessary. First, it represents an increase over a reference period in which there was already exceptional liquidity. It is not easy to determine how far the increased liquidity observed at the end of 1972 was absorbed by the economic system, in particular by prices, in the first few months of 1973. It will be recalled that prices rose by only 4 per cent in the first half of that year. Furthermore, the 13.1 per cent increase in monetary resources was the result of a combination of the growth of components with a greater degree of liquidity (money and quasi-money) and reductions in those with a lesser degree of liquidity (counterpart funds and other items) (see table 29).

In 1974, total liquidity once again increased appreciably. It will be noted that monetary resources rose by 45.7 per cent in this period as a result of significant increases in all their components (see table 29).

Monetary expansion in 1973 was mainly due to the expansion of credit, which reached the rate of 31.2 per cent, exceeding the rates in previous years. What stands out once again is the extraordinary increase in credit to the private sector (68 per cent), while credit to the Government rose by only 4.1 per cent. The sharp drop in international reserves to one third of their value over the period of one year acted as an important factor of contraction. In fact, this decrease meant the sterilization of about 500 million pesos, which represented 67 per cent of the increase in money in 1973 (see table 29).

The factors of expansion and contraction followed opposite trends in 1974. Reserves quadrupled, while credit dropped by 2.5 per cent over the year, as a result of a decrease of about 76 per cent in credit to the Government and the continued increase at a rate of over 59 per cent in credit to the private sector.

Monetary expansion in this second phase of inflation in Bolivia was mainly attributable, as stated previously, to the extraordinary expansion of credit to the private sector. The Government's

Table 29. Bolivia: monetary balance

	1972	*Rate*	*1973*	*Rate*	*1974*	*Rate*
	Balances at end of each period in millions of pesos					
Structure of monetary resources						
(total liquidity)	*3,937.5*	*43.1*	*4,452.0*	*13.1*	*6,486.0*	*45.7*
Money (means of payment)	2,210.1	25.2	2,968.9	34.3	4,257.0	43.4
Quasi-money	634.2	28.6	806.9	27.2	1,192.0	47.7
Counterpart funds	476.5	310.8	95.0	−80.0	318.0	234.7
Other items (net)	616.7	63.7	581.2	−5.8	719.0	23.8
Factors of expansion and contraction	*3,937.5*	*43.1*	*4,452.0*	*13.1*	*6,486.0*	*45.7*
International reserves	718.4	198.1	228.7	−68.2	2.368.0	935.4
Credits	3,219.1	28.2	4,223.3	31.2	4,118.0	−2.5
(*a*) To the Government	1,858.1	21.2	1,934.9	4.1	465.0	−76.0
(*b*) To the private sector	1,361.0	39.2	2,288.4	68.1	3,653.0	59.6
			Structure (percentages)			
Factors of expansion and contraction	*100.0*		*100.0*		*100.0*	
International reserves	18.2		5.1		36.5	
Credits	81.8		94.9		63.5	
Credits	*100.0*		*100.0*		*100.0*	
(*a*) To the Government	57.7		45.8		11.3	
(*b*) To the private sector	42.3		54.2		88.7	

SOURCE: IMF, International Financial Statistics, November 1974.

development policy has openly supported private entrepreneurial activity. In this respect, it is highly illuminating to compare the amount and proportion of credit assigned to the private sector at the end of 1971 with the position at the end of 1974. Whereas in 1971 it amounted to 977.5 million pesos, or 38.9 per cent of total credit, in December 1974 it had risen to 3,653 million pesos and its share was 88.7 per cent of the total; conversely, the Government share of total credit decreased considerably (see tables 27 and 29). No more data are required to conclude that the monetary expansion was mainly in favour of the private sector. The increases in credit which successively benefited private activity already as from the end of 1971 were so accelerated that they could not but have repercussions in terms of inflation. The trend of this variable is a clear expression of the Government's development policy, which assigned to private enterprise the leading role in the country's production process.

The financial behaviour of the Treasury was another exacerbating factor of the inflationary process.

Table 30 summarizes the fiscal position. Current income rose by 85.7 per cent and expenditure by only 57.3 per cent. The increase in income is basically due to the high prices of export commodities (particularly mining products, petroleum and gas), which meant exceptional increases in production royalties and export taxes. The smaller increase in expenditure is largely attributable to the wages policy under which only moderate wage and salary adjustments were granted. It will be noted that the increase in personal services was only 31.9 per cent and that, if the recruitment of new government officials is subtracted from this, the increase in wages and salaries was considerably lower, while in the same year consumer prices went up by 35 per cent. In spite of this austerity in connexion with wages and salaries and the higher tax revenue obtained, it was not possible to avoid a deficit in the fiscal budget. The current account deficit was 413 million pesos in 1973 (17 per cent of the total fiscal revenue for that year). Although lower than in the previous financial year, it continued to represent one of the important reasons for currency issues, with their sequel in terms of inflation.

It should be noted, however, that it was not only the fiscal deficit and its financing by means of currency issues that spurred on inflationary pressures. An increase of 57.3 per cent in expenditure in so rigid a structure as that of the Bolivian economy also caused disequilibria between supply and demand and, therefore, exerted pressures on prices. It will be noted that the considerable increase in income which made such a growth of expenditure possible is mainly attributable to royalties in respect of exports of mining products, petroleum and gas, the export prices of which had soared. This fact was particularly important because the increase in fiscal revenue did not lead to a contraction in spending power in the econ-

Table 30. Bolivia: budgetary operations
(Millions of pesos)

	1972	*1973*	*Percentage variation 1973*	*1974*	*Percentage variation 1974*
Income	*1,330.0*	*2,469.4*	*85.7*	*5,104.3*	*106.7*
Internal revenue	565.3	905.7	36.1	1,299.1	43.4
Customs revenue	418.2	517.4	23.7	947.3	83.1
Mining revenue	43.1	190.7	342.5	903.3	373.7
Revenue from gas and petroleum	68.9	278.6	304.4	883.3	217.0
Other income	234.5	577.0	204.2	1,071.3	85.7
Expenditure	*1,758.7*	*2,882.0*	*57.3*	*5,544.8*	*92.4*
Personal services	1,009.5	1,332.2	31.9	2,313.7	73.7
Non-personal services, materials and supplies	224.4	386.9	61.3	553.5	43.1
Fixed and financial assets	19.0	119.9	497.8	101.9	−15.0
Public debt	293.5	433.4	40.5	679.1	56.7
Current and capital transfers	174.8	549.5	171.1	1,575.1	186.6
Other expenditure	37.5	60.1	97.0	321.5	434.9
Deficit	*428.7*	*412.6*	*−30.5*	*440.5*	*6.7*
Financing					
External credit	28.4	31.0	9.2	...	–
Central Bank credit	398.0	498.7	25.3	...	–
Balance of previous period	18.1	15.8	12.7	132.9	–
Balance at end of period	15.8	132.9	741.1	...	–

SOURCES: Ministry of Finance, Office of the Under-Secretary of Financial Administration; Banco Central de Bolivia, *Boletín estadístico*, December 1974.

omic system, but rather to increases in liquidity through the purchase of foreign exchange from exporting concerns.

In the light of the economic situation in the first nine months of 1973, the prospects for the final balance were decidedly gloomy. In October of that year the current account deficit was estimated at 960 million pesos (then 40 per cent of estimated income), which was over three times the deficit actually shown at the end of the year. The prices of export commodities distinctly benefited the public finances, which would otherwise have had to face pressing problems.

Be that as it may, the inflationary process was strongly influenced by the difficult situation in the earlier months. The monetary balances recorded at the end of the year, which underwent significant changes in the last quarter, conceal intermediate situations which it is useful to consider because they determined domestic price trends. Suffice it to say that Central Bank credit to the Government at the end of September 1973 was 18 per cent higher than at the end of 1972, and three months later it was only 4.1 per cent over the same figure. The change in the fiscal situation in those last three months obviously mitigated the quantitative impact of the liquidity recorded previously, but the motivations, both objective and subjective, of the agents of the economic process were more influenced by the expansionist situation in the first part of the year than by the balances at the end.

As in the first phase of inflation, the extraordinary liquidity experienced by economic activity could scarcely be absorbed without drastic changes in the system and increases in prices. If indexes of monetary expansion in that period are compared with the indicators of the real increase in the supply of goods, it will be seen that the real product grew by 5.2 per cent in 1973, the agricultural product by 2.1 per cent and imports by 9.2 per cent, resulting in a 6.1 per cent increase in total supply. Although this is not a really strict comparison in view of the nature of the physical and financial variables considered, it has sufficient value to show that the two spheres failed to operate in a synchronized manner and their adjustment would necessarily involve an increase in prices.

The acceleration of inflation was closely associated with what has been called imported inflation. Since this factor has only recently made its appearance on the inflationary scene and has particular features which need to be identified, it is dealt with in a separate section.

(c) *The incidence of imported inflation*

With the purpose of clearly identifying the exogeneous factors stimulating inflation in Bolivia,

a study is made of both their nature and their mode of action.

The dynamic impetus of international prices as from mid-1975 had distinctly favourable effects for Bolivia. The high prices of export items alleviated the pressures on the balance of payments and enabled imports to be increased so as to cover the needs which the slow growth of supply of agricultural commodities was unable to satisfy. Concurrently with these benefits, world inflation was transmitted through various mechanisms to the domestic scene with unfavourable results.

(i) *Import prices.* The first direct impact made itself felt through the higher prices of imports of goods and the higher cost of freight and insurance. As noted above, the import price index went up 17.6 per cent in 1973 and 23 per cent in 1974. The increases were bigger in the case of machinery, equipment and spare parts in general, which make up almost half of Bolivia's imports. The new prices of these products indicate price increases well above the rates already mentioned. The effects of these increases, combined with those produced by the devaluation of the exchange rate, represented severe inflationary pressures on production costs in national currency.

In view of the dependence on imported supplies which is a feature of the Bolivian economy, this exogenous impact spread rapidly inside the country. It is not easy to determine to what extent inflation may be ascribed to each of the various factors involved. The interaction of some and the essentially qualitative nature of others make an accurate breakdown somewhat difficult. However, an increase in import prices of the magnitude reached in 1973 and 1974 is justification for assigning to this aspect of inflation tremendously important quantitative and qualitative effects in terms of the phenomenon itself, particularly the acceleration which took place between mid-1973 and mid-1974.

(ii) *Enlargement of the imported base.* In view of the exceptional increase in the volume of foreign trade operations, imported inflation was not only transferred through prices; the increase in volume means an enlargement of the imported base, which offers a wider opportunity for the importation of foreign inflation. From this point of view, the appreciable increase in the import coefficient favours the transfer of external inflationary pressures. This dual effect is, however, partly offset by the bigger supply of goods resulting from the real increase in imports. To determine how far this fact moderates the exogenous pressures would require a detailed knowledge of the structure of demand by income strata and of the composition of imports.

In this respect, too, the change in the scale of Bolivia's foreign trade fostered the spread of imported inflation. A considerable and rapid increase in foreign trade activities, particularly imports, came up against a basic infrastructure which had not grown, and could not grow, at the same rate. The increases in demand associated with this type of activity were naturally an additional source of price increases.

(iii) *Export prices.* In addition to the higher cost of imports, world inflation had adverse effects of a different type on pricing. The excellent prices of commodities such as meat, sugar and flour prevailing on the external markets caused exports to soar at the expense of covering domestic needs. There were periods in which these movements led to acute local shortages, with the natural repercussions on prices. In the middle of 1973, the Bolivian economy began to feel this new impact of external inflation. Paradoxically enough, a situation of excellent export prices had negative internal effects. In the face of foreign markets to which access was difficult in the past, a policy of export promotion and incentives had been developed, which combined with the new foreign trade conditions to obtain large export flows. Not only did this situation, as stated previously, upset the balance between domestic supply and demand, which in itself exerted pressure on domestic prices, but the excellent external market conditions strengthened the position of the exporter groups. Within a general policy of promoting private enterprise, it was not easy to direct entrepreneurial decisions against the market forces. For this among other reasons, the domestic prices of these types of commodities, which have both domestic and external markets, were adjusted.

Among the negative effects of external inflation, mention cannot but be made of the proliferation of illegal export and marketing activities. Although it was impossible to assess the volume of these operations with any accuracy, data obtained from various official sources indicate a considerable scale of illegal trade, including contraband in gasoline.[51] The increase in these activities not only meant large transfers of physical resources abroad without any kind of fiscal control, but it fostered imports of essentially luxury goods, also in the form of contraband, with all their pernicious effects. The unrestricted freedom of exchange certainly helped such activities, which in some departments reached very high levels. Contraband had been a big problem for many years, so that it can well be imagined how much more serious it became after it had increased so alarmingly, to the extent that at times it was the focal point of the Government's concern. This was

[51] Estimates of the Office of the Under-Secretary of Financial Administration, Ministry of Finance.

yet another way in which imported inflation passed into the Bolivian economy, obviously with worse consequences than through the legal flows.

The steady growth of legal or illegal exports meant a considerable concentration of income in the hands of the groups associated with those activities. The sequel of negative effects does not stop there, however. The surpluses accumulated by the exporter sectors boosted their internal and external purchasing power. Prompted by the urgent need to take advantage of the external situation, they stepped up their purchases of inputs, freight and other services, and the behaviour of their suppliers, conscious of the extraordinarily high profit margins obtainable from exports, brough additional pressures to bear on prices.

(iv) *Accumulation of reserves.* Another phenomenon which clearly had some influence on the recent inflationary process, especially its acceleration, was the exceptionally rapid growth of international reserves. In view of the foreign exchange policy in force in Bolivia, the expansion of exports and the consequent accumulation of reserves resulted in national currency issues which significantly increased the liquidity in economic activity (see table 29). It will be remembered that the increases in money and quasi-money in the first half of 1974 were 22.6 and 22.5 per cent, respectively. The expansion of total liquidity was 26.7 per cent over the same period, one of the main causes being the increase in reserves, which in June 1974 stood at nearly eight times the end-1973 figure. A violent change is noted in the ratio of credit to reserves as a factor of expansion. At the end of 1973 this ratio was 19 to 1, and six months later it was only 2 to 1. Such variations over so short a time can scarcely be harmless in terms of prices. The larger currency issues, albeit motivated by increases in reserves, had inflationary effects. Although the bigger supply of foreign exchange, as already stated, makes for more imports which increase total supply, there is generally a period in which the actual entry of imported products lags behind the increase in liquidity, and degrees of variable incompatibility between the structure of the additional demand and the composition of the new imports. Similarly, the lead time of the investments militates against the achievement of basic equilibria in the economic system. These maladjustments are clearly observable in the second phase of inflation in Bolivia. The price increases in the first half of 1974 took place in a context of a considerable accumulation of reserves, large-scale investment and imports at ever-increasing prices.

(v) *Inflationary expectations.* Lastly, in thus identifying the inflationary factors associated with the pressures from the external sector, mention must be made of the fact that inflationary expectations played a highly important role. In pricing, profit margins were usually calculated on the basis of replacement costs which more than safeguarded future increases in prices. Similarly, as regards consumers, the expectations of price increases meant the accumulation of stocks and little resistance to the usual speculations in openly inflationary processes. For the one reason or the other, prices soared.

The most important entrepreneurial decision-making centres in Bolivia are generally associated with foreign trade activities and, of course, with banks. Any changes in world commodity prices or currency values are rapidly reflected in these groups. The recent world inflation found in them a direct mechanism for spreading the additional inflation to the quantitative factors reviewed above.

No further explanations are necessary to realize that all these forms of "importing" external inflation were facilitated, extended and magnified by structural factors which have adverse effects whatever the direction of the current movements. In situations of external bottlenecks, these factors aggravate the crises and hamper any plan or programme which under different circumstances would have been able to palliate them. In a boom situation such as that recently occurring in Bolivia's external sector, the structural deficiencies in that economy prevented it from reaping the full benefit and fostered the importation of external inflation.

(d) *The decline in the rate of inflation*[52]

The appreciable decline in the rate of inflation in the second half of 1974 (see table 25) was not in line with the sharp increases in liquidity in the economic system (see table 29) or with the level of imported inflation in that period.

Similarly, the fiscal situation at the end of 1974 pointed to a rise in prices. Although fiscal revenue grew more than expenditure (106 per cent compared with 92 per cent) and the fiscal deficit represented a substantially lower proportion of income than in previous years, it must be taken into account that a large part of the higher revenue came from export royalties the growth of which must be attributed mainly to the rise in export prices. In other words, the collection of revenue under this head did not mean the restriction of liquidity, since it originated from Central Bank issues for the purchase of foreign exchange gener-

[52] It should be borne in mind that the indicator of inflation used has some limitations, including the absence of imported items in the sample of products considered.

ated by exporters, part of which entered the Treasury in the form of royalties; 56 per cent of total revenue consisted of such royalties and taxes on exports.

Moreover, it is pointed out that the 92 per cent increase in fiscal expenditure took place within the context of a fairly inflexible production structure, which may also have had inflationary repercussions.

Accordingly, the slowing down of the inflationary process seems to have been associated more with the bigger supply of goods (total supply grew by 8.8 per cent in 1974, imports by 22.6 per cent, and the agricultural product—although at a low rate—increased more than in previous years).

In the face of this favourable evolution of supply, the restrictive wage policy curtailed real demand of the wage-earning sector and constituted another of the factors accounting for the slower rate of inflation. In fact, the concentration of income brought about by the external situation and domestic inflation itself depressed the purchasing power of wages and salaries.

Lastly, as will be seen later, the maintenance of the exchange rate attenuated the effects of international inflation. In practice, in a situation of rising external and domestic prices, the fixed exchange rate became a kind of import subsidy and a form of revaluation of the Bolivian peso.

As a rule, inflationary processes experience fluctuations. It is still too early to say whether events in the second half of 1974 constitute the beginning of a definite trend towards the control of inflation, or the recurrent wave of a cycle which may continue to expand. In any case, the restrictive wage policy, the fixed exchange rate and the considerable availability of international reserves increase the radius of action of the anti-inflationary economic policy, although these are obviously somewhat precarious situations which may easily alter as a result of either changes in the external sector or internal developments.

D. INFLATION AND ECONOMIC POLICY

1. *The frame of reference*

The first fact which should be stressed is the non-existence of an explicit economic policy. The basis and main features of the development policy in general and the economic policy in particular corresponded to very general principles and objectives. At this level, it is impossible to pin down an over-all idea which includes clear-cut intentions and specific policies for the different sectors of the economic system and for the different areas of economic policy.

In a context in which serious structural problems had to be faced and government policy was to give definite support to private enterprise, stability and growth objectives were not, of course, wholly compatible, In pursuance of these objectives use was made of economic policy instruments the scope of which was fairly limited, considering the type of underdevelopment to be found in Bolivia.

In this connexion, it would perhaps be relevant to define the radius of action of conventional economic policy measures. In a country seriously affected by structural problems, which consequently suffers from serious distortions in the functioning of socio-economic activity, the use of the classic machinery of economic policy has definite limitations. Just as architectural construction, however boldly and well planned it may be, cannot make much headway in the face of geological faults in the earth's crust, an economic policy which confines itself to action on the surface of the production and distribution system is necessarily limited. Bearing this in mind in the case of Bolivia, such a policy will only directly influence a small core of the population, and as far as the economic phenomena which it covers are concerned, the full extent of its influence is to achieve a certain basic balance at the macro-economic level, and even here, only with serious difficulties. The diversity of grassroot situations which is a result of the structural heterogeneity which has so frequently been referred to, deprives the over-all economic policy instruments of their efficacy while serious incompatibilities affect their use. In the enumeration of the main economic policy measures below, it is essential that this contrast between the limited area for manoeuvre and the deep-rootedness of the problem which they endeavour to solve should not be forgotten.

On the same lines, there would appear to be a similar lack of adjustment between a development policy which takes its basic support from private enterprise and its main orientation from market forces, and a policy whose objective is to correct the structural disequilibria of which repeated mention has been made.

Despite its major influence, the private sector finds itself before a fairly limited prospect in terms of its scale of production. The small size of the consumer market in Bolivia, in view of the level and distribution of income, limits the expansion of the industrial product. The most vigorous management activities in recent years were those connected with the external sector and those producing goods and services for the wealthiest sectors of society, i.e., those activities which had a safe market ensured for them. The narrow limits of domestic markets are consequently a visible impediment to any industrialization process of

consideration based on efficient private enterprise, with a minimum of competition. This means that the low level of purchasing power of the majority of the population does not provide an adequate stimulus in the form of economic viability to undertaking activities which imply risks and terms of maturity which are not necessarily brief.

It should be observed that the small scale of production of the majority of the enterprises makes for high unit costs, overlaid by large profit margins resulting from the special structure of demand. Price formation was affected by this double effect which inflation and the expectations it aroused became responsible for aggravating.

Another important element in the frame of reference of the economic policy of the last four years which merits further comment, is the abrupt change in the volume of external trade operations. As has already been said, international inflation has brought to light certain limitations of public administration. In the context of a continuing bottleneck in the external sector the State apparatus had developed certain responses, i.e., its abilities were directed at defending itself from what were generally deficit situations. The increase in export prices has in this sense completely reversed the situation. Spending capacity for productive investment was not in line with the growing availability of foreign exchange. Similarly, imported inflation signified an entirely new problem, of considerable impact and rapid dissemination in the country's economy; the economic policy aimed at tackling it did not have the same amplitude and speed with which inflation spread its effects throughout the country.

It should not be overlooked that during the same inflationary period being studied here, the structure of economic and political power underwent an appreciable change compared with previous years. The possibilities of regulating the operation of the economic system, especially in a context of inflation, decreased as the influence of the private sector on the decision-making centres increased. Private sector pressures on prices, credits and taxes were powerful limitations on the adoption of government decisions.

The situation outlined above made the conception of a clear and well-defined economic policy very difficult. From the point of view of inflation, the description of which is the aim of the present document, it is impossible to identify any open and continuing policy of stabilization; rather the reverse, State action tended to provide pragmatic responses to economic events. The type of underdevelopment existing in Bolivia, among other factors, hindered the advance of the socio-economic process and the operation of economic policy machinery basically consisted of a series of responses to the phenomena which materialized and not of a preconceived implementation of the country's development policy.

2. *The main measures adopted*

The economic policy process which began in 1972 was markedly different from earlier processes. Throughout the period 1959–1971 the high priority objective of the conception and implementation of the different economic policies which can be identified was to prevent structural disequilibria from coming to the surface of the economic system in their political, social and economically most harmful manifestations. Generally speaking, the handling of the financial variables was in keeping with this aim. It may be concluded from the observation of the increases in money supply, credit, the fiscal budget, etc., that monetary programming throughout this entire period was very much tied to not exceeding annual increases of around 6 per cent in price rises; this objective was, generally speaking, achieved.

The economic policy decisions adopted as from 1972 constituted a basic change, especially in connexion with the expansion of public expenditure and the increase in credit to the private sector, and the liberal sales of foreign exchange. This change of economic policy meant that the structural disequilibria typical of Bolivia's economy forced their way to the financial scene, in the form of marked inconsistencies between supply and demand, which the market forces, as has already been stressed, took on the responsibility of correcting by means of changes in the system and increases in price levels. The limited ability of the apparatus of production to respond to stimuli originating in the financial sphere became obvious.

(a) *Wages and prices policy*

The Government's main concern, once the modification in the exchange rate had been decided upon, was to regulate price increases.[53] In practice, however, the maximum limits for the increase in prices were exceeded. The annual target of 25 per cent for the price increases between October 1972 and October 1973 was unable to withstand the pressures from costs and demand which were activated by the devaluation and the monetary expansion.

The policy aimed at controlling the progress of prices consisted of various stages: the freeze decided upon in the first instance was disrupted by the aforementioned pressures; successive requests

[53] More detailed comments on the devaluation appears in ECLA, *Economic Survey of Latin America, 1973*, (E/CN. 12/974), mimeographed version, pp. 285 *et seq.*

by the producers and the market forces themselves were the cause of a further chain of increases; and, lastly, the disparity between the prices of some products in the markets of neighbouring countries and those existing in the domestic market encouraged contraband which the Government endeavoured to control on a basis of adjustments which brought some domestic prices close to international levels. These examples clearly show the shifts in price policy, which moved from an attempt at strict control and regulation to an endeavour to follow the pressures of external demand. If it is also borne in mind that the increase in import prices determined increases in the production and distribution costs of products with the whole range of demonstration effects implied, it will be seen that price-decisions were the object of restrictions of the most varied types. The implementation of a stable policy in this respect was therefore not possible.

From the point of view of wages, the policy had more lasting and clearly-defined trends. On the one hand, the majority of the adjustments were on a basis of fixed sums, in an attempt to benefit the low-income workers, and on the other hand there was considerable control in the handling of this variable, with a view to slowing down the excessive growth of demand and ensuring that the higher costs which would be generated by the larger adjustments should not constitute additional pressures on prices.

Together with the devaluation, a fixed adjustment equivalent to 135 pesos per month was granted to all Bolivian wage earners.[54] The magnitude of the ensuing price increases resulted in the granting of subsidies to low-income workers according to the number of dependants: 20 pesos per worker plus 25 pesos for each dependant. Later, in mid-1973 as a result of new price increases, an extra payment of one month's wages per worker was decreed. Lastly, following the wake of inflation, a further adjustment of 120 pesos per worker was granted in 1973.

Very rough estimates would seem to show that the average wage in the Central Goverment, thanks to the above-mentioned adjustments, had increased by approximately 45 per cent between October 1972 and October 1973. During this same period prices increased between 52 and 66 per cent according to different sources of information. That year, a large proportion of wage-earners experienced varying degrees of decline in their standard of living. As regards the low-income population, especially the rural population, it is not possible to evaluate their gains or losses owing to the lack of price indicators in rural areas. In view of their low incomes, fixed sum adjustments and the output of subsistence farming, it is to be hoped that their standard of living did not deteriorate during this period.

On the other hand, exporters, importers, the groups closely associated with the financial market and industrialists in general increased their share in the product. The external bonanza was mainly concentrated in these nuclei, while, as is usually the case, the inflationary process itself meant a larger share of the surpluses for these groups. There is still no complete data available on the capital formation which may be attributed to these sectors, in order to determine to what extent the regressive trend in income distribution was offset by increases in growth potential, or whether the flight of capital once again was the means of taking large sums from them.

(b) *Exchange policy*

The most important decision in this area was the maintenance of the exchange rate at the level of 20 pesos to the United States dollar as from October 1972. Similarly, the free sale of foreign exchange to private persons and the compulsory surrender of foreign currency from exports, were the main complementary measures which made up the exchange policy as from the date mentioned. The maintenance of the exchange rate has constituted a form of subsidizing imports in view of the high level of domestic prices, and, of course, constituted a type of subsidy to hoarding in hard currency. It is the only asset which has not undergone any price increase since then. Only a reasonable supply of foreign exchange can guarantee a liberal policy of this type, in a situation in which there exists a high level of liquidity in the economic system. Up till now, the vigorous growth of external demand was the mainstay of the free sale of foreign exchange and the fixed exchange rate. On the one hand, this resulted in cushioning the effect of imported inflation and, on the other, it represented a channel for the flight of foreign exchange and, in particular, greatly facilitated smuggling. Owing to the lack of detailed data on the structure of imports, it is not easy to evaluate the positive and negative results of the way in which this instrument was handled. Considerations like the above, however, and even more so the clear indications that legal and illegal imports of luxury goods may be reaching levels hitherto unknown, cast doubts on whether this exchange policy is compatible with making the most of the external economic situation which could mean the

[54] As a point of reference, the average monthly salary in the Central Government was estimated at approximately 1,090 pesos in 1972. (See CIAP Sub-Committee on Bolivia, op. cit., tables IV-5 and IV-6.) On the other hand, the total remunerations for the Central Government increased in 1973 by slightly over 30 per cent (see table 30).

acquisition of permanent benefits for the country. The following could be taken as an example: while the consumer price index underwent an increase of 126.5 per cent between October 1972 and July 1974, the price of the dollar remained steady.

Since domestic inflation is considerably higher than external inflation, the subsidizing of the exchange rate should have produced a drastic change in the system of prices in the sense of fairly meaningful reductions in the prices of imported products. Incomplete data available suggest that such a change did not take place and this would imply that the single, fixed and free sale exchange rate is one of the mechanisms through which the regressive distribution of income is channelled to the importer groups.

The growing supply of foreign exchange, basically as a result of external prices, provided Bolivia with an important defence mechanism against imported inflation, since it was able to keep its exchange rate unchanged. While its external trade continues along the same lines, it will be able to continue to absorb some of the effects of this foreign inflation. The doubt will remain, however, whether alternative policies would not in fact have had more promising effects. It proves very difficult to evaluate such alternatives while the structure of imports is not known in detail, as has already been stressed. It should also be recalled that the above reflections basically cover the economic area; socio-political restrictions play a basic role in the control of an instrument as sensitive as the exchange rate. A more general appreciation would of course have to take them into account.

(c) *Tax policy*

At the same time as the currency was devalued, important tax measures were adopted. Mention should be made of the revaluation of assets, by 60 per cent for imported goods and 20 per cent for buildings and other goods of domestic origin, with a tax of 5 per cent on this revaluation. Measures were taken at the same time to revalue assets in gold and foreign currency at the new rate of exchange, with a tax of 20 per cent on the increase.

Also with a view to attracting the benefits implied in a devaluation, new taxes were created: 60 per cent on the import value of stocks of imported articles in commerce; 40 per cent on the net value of exports of minerals, hydrocarbons and cotton already produced or exported but pending payment and the compulsory surrender of foreign exchange; 20 per cent on the net value of all new exports of minerals, metals, hydrocarbons, cotton and meat; and 15 per cent on the value of exports of other goods.

A year later, in October 1973, a tax reform was introduced, aimed at simplifying tax legislation and exercising a stricter control over the very considerable tax evasion.[55]

This tax reform introduced modifications in personal income tax, tax on the income of enterprises, sales tax, and selective consumption taxes. The most important feature of the personal income tax was the replacement of a schedule system by a global system in which a single progressive scale was applied. The most outstanding features of the tax on the income of enterprises are: the extension of the universe of contributors to include agricultural and livestock enterprises; the distinction made between enterprises with sales exceeding 200,000 pesos annually (approximately 1,500) and the smaller enterprises, and the increase from 26.4 to 30 per cent in the tax on profits. Moreover, clear incentives are given for investment and reinvestment of profits and for the utilization of labour-intensive production techniques.

The results of this modification in taxation cannot be evaluated using available information. From the point of view of its effects on inflation, however, it may be stated that the results were only secondary. The increase in domestic revenue between 1973 and 1974 was less than the general increase in prices; the rise in prices as a result of tax reform was apparently more than compensated for by the reduction in real demand which the reform itself implied. In any case, besides the other factors of inflation which have already been analysed, the effect of taxes as has already been said, was of little importance.

(d) *Fiscal finance policy*

From the fiscal viewpoint, the traditionally most important items of income did not undergo significant changes. The increases in the sums collected, referred to as internal and customs revenue, were less than the increases in prices; tax evasion increased considerably to judge from some partial indicators. The so-called royalties from production and taxes on exports of minerals, gas and petroleum showed extraordinary increases, however. As may be seen from table 30, during the fiscal year 1973 and particularly throughout the period January-July 1974, their contributions increased significantly. While in 1972 these items accounted for barely 18 per cent of current earnings, in the first seven months of 1974 they came to account for 50 per cent. Obviously, there was a

[55] As an example of this, it should be noted that the most dynamic area in the country, the Department of Santa Cruz, generated less tax revenue in 1973 than in 1972 and contributed a smaller quota to the Exchequer than the Department of Cochabamba where economic activity is at an appreciably lower level.

change in this type of source of fiscal financing and dependence on external trade increased. The increases noted meant that the fiscal deficit was considerably smaller and that it reduced to a similar extent Central Bank credit requirements (see table 30). From the point of view of inflation, however, the short-term situation had not changed very much. The increases in income came from issues originating in purchases of foreign exchange from exporters. Issues which were not occupied in financing the fiscal deficit were used to accumulate reserves and this meant an increase in the liquidity of the economic system; while this foreign exchange does not become real supply, inflationary pressure will continue to take their course.

The Government took action to obtain a large flow of external credit, which helped to meet its financial requirements. The increase in the external public debt, comparing the balances at the end of 1971 and 1973, was approximately 136 million dollars, which meant an increase in the debt of 23.7 per cent during this period. The external public debt at 31 December 1973 amounted to the sum of 721.6 million dollars,[56] which was nearly two and a half times the value of exports of goods and services in that year.

(e) *The financing of the private sector*

As regards the financing of the private sector, it has already been stressed that bank credit underwent extraordinarily large increases. Government policy in this respect was exceedingly indulgent with its financial requirements, so much so that the increase in liquidity which resulted from the inflationary process described above must be largely attributed to the increases in this form of financial support. Furthermore, the external credit obtained by this sector made up a large share of the country's debt. During 1972, external financing for these entrepreneurial activities was 40.3 million dollars, and in 1973 it was 47.2 million dollars.[57]

[56] See CIAP Sub-Committee on Bolivia, op cit., table V-10.

[57] IMF, *Balance of Payments Yearbook.*

The traditional problems of the external bottleneck which the Bolivian economy came up against in the past, did not arise in recent times since here too the private sector had access to ample external finance facilities. In the face of these well-defined incentives, the speed of response of private activity does not appear to have manifested itself in as vigorous a form as might have been expected, if the data available for 1972 is taken into account.

In this regard it should be mentioned that private investment in the main sectors of production in 1972 was significantly lower than in 1971 (see table 31). No data is available for investment in housing and the services sectors, which probably increased, but if tentative figures for investment in the basic productive sectors are confirmed, there may be reason to believe that the performance of the private sector far from constituted a dynamic element, despite the major role assigned to it in the beginning. If to this is added the decline in foreign investment during the year, and if these movements are compared with the various types of stimulus given to private enterprise, it will be understood that it is other problems—arising out of structural heterogeneity—which determine the failure of intentions to materialize in more rapid rates of growth.

Table 31. Bolivia: estimated investment in the private sector
(Millions of pesos at current prices)

Sector	*1970*	*1971*	*1972*
Agriculture	46	49	38
Mining and quarrying	109	115	89
Industry (manufactures)	71	75	58
Hydrocarbons	199	210	163
Energy	63	66	50
Total	*488*	*515*	*398*

SOURCE: Secretariat of the Consejo Nacional de Economia y Planificación. Dirección de Planificación Global. The original source indicates that some data are estimates and subject to modification.

2. BRAZIL

A. INTRODUCTORY NOTE

Inflation in Brazil must be analysed in a wider setting than would be required for other Latin American countries. It is in fact part of an over-all economic policy project which has been applied for the last 10 years. Questions relating to manner of growth and matters concerning the inflationary process are thus very closely interrelated. Consequently, the study on Brazil is more lengthy and detailed than those of other countries; this is also because a variety of background facts is provided on features of development during this period, and in particular as from 1968, which marks the beginning of a period of high growth rates in the economy of Brazil.

Table 32. Brazil: gross domestic product at factor cost, by sector of economic activity
(*Growth rates*)

	1965-1969	*1970*	*1971*	*1972*	*1973*	*1970-1973*
Agriculture	2.4	5.6	11.4	4.5	3.5	6.4
Mining	10.1	12.7	11.0	14.3	11.5	12.3
Manufacturing	10.2	11.0	11.3	14.1	15.8	13.7
Construction	9.7	14.9	8.4	12.9	15.5	12.2
Subtotal goods	*6.5*	*8.8*	*11.3*	*10.1*	*10.9*	*10.8*
Electricity, gas and water	9.2	10.1	11.4	11.1	12.5	11.7
Transport and communications	8.7	15.0	8.4	8.1	14.0	10.1
Subtotal basic services	*8.8*	*13.7*	*9.1*	*8.9*	*13.6*	*10.5*
Commerce and finance	7.8	9.1	12.3	11.4	12.5	12.1
Commerce	8.1	8.9	12.8	11.9	13.0	12.6
Finance	7.0	9.5	11.3	10.4	11.4	11.0
Ownership of dwellings	7.0	9.5	11.3	10.4	10.5	10.7
Government	7.0	9.5	11.3	10.4	10.4	10.7
Miscellaneous services	4.2	9.5	11.3	10.4	10.4	10.7
Subtotal other services	*6.6*	*9.3*	*11.8*	*10.9*	*11.4*	*11.4*
Total	*7.0*	*9.5*	*11.3*	*10.4*	*11.4*	*11.0*

SOURCE: ECLA, on the basis of official statistics.

B. OUTSTANDING FEATURES OF THE EVOLUTION OF THE BRAZILIAN ECONOMY

1. *Evolution of the gross domestic product and its components*

Table 32 shows the performance of Brazil's gross domestic product by the sectors of economic activity which compose it.

As may be seen, the growth of the economy put on a spurt as from 1968, and the average growth of the product increased from around 7 per cent during the period 1965-1969 to 11 per cent during the years 1970-1973. This increase in tempo was predominantly linked with the favourable performance of the secondary sector, both on account of its importance in the total product (27 per cent of the gross domestic product during the years 1971-1973) and because of the natural repercussion on the growth of other sectors, for example, trade, finance and transport and communications.

The boom in Brazil's economy is explained mainly by the steady growth of industry, with growth rates of 10.2 per cent during the period 1965-1969 and 13.7 per cent in the years 1970-1973.

The growth of the sub-sectors which make up the industrial sector, however, was not homogeneous. In fact, a wide disparity is to be observed in rates of growth, and this should be stressed in order to show clearly where the dynamic core of the sector lies and hence the root of the growth of the total product.

Table 33 shows that the expansion of the industrial sector was linked to a large extent to the favourable progress of the industries producting "heavy" consumer durables, such as appliances, motor-vehicles, etc., and the basic metals industries. It may be observed that the rates of growth of the metallurgical, engineering, electrical and transport materials industries are very much higher than those of the "traditional" sectors and the sectors producing intermediate articles.

Table 33. Brazil: annual average growth rates in manufacturing
(*Percentages*)

	1966-1969	*1969-1972*	*1966-1972*
Non-metallic mineral products	11.0	11.7	11.3
Metallurgical industry	9.8	10.8	10.3
Engineering industry	9.9	23.0	16.2
Electrical equipment	15.8	13.6	14.7
Transport equipment	13.0	16.4	14.7
Wood	9.7	...	...
Furniture	−2.5	...	...
Paper and paper products	11.6	4.6	8.0
Rubber	9.5	14.6	12.1
Hides and skins	6.4	...	...
Chemical products	10.3	15.0	12.6
Toilet preparations	13.7	...	...
Textiles	6.0	1.4	3.7
Clothing and footwear	6.0	10.2	8.0
Food	11.0	7.6	9.3
Beverages	3.3	7.6	5.4
Tobacco	6.0	5.7	5.8
Total	*9.5*	*11.1*	*10.3*

SOURCE: ECLA, on the basis of official statistics.

Table 34. Brazil: quantum indexes of manufacturing by categories of goods
(1966 = 100)

Categories of goods	*1968*	*1969*	*1970*	*1971*	*1972*	*Average annual variation 1968-1972*
Capital goods.	117.2	124.4	140.1	173.0	210.8	15.8
Durable consumer goods . .	125.5	156.9	168.8	198.6	239.9	17.6
Non-durable consumer goods .	116.7	125.4	134.5	137.2	147.9	6.1
Intermediate goods	119.9	131.3	150.3	167.6	188.5	12.0
Total	*118.9*	*131.3*	*145.0*	*159.6*	*180.3*	*11.0*

SOURCES: Insituto de Planejamento Económico e Social (IPEA), and Ministry of Industry and Trade.

Table 34 gives a clearer picture of this phenomenon, and makes it easy to identify the industrial sectors of greatest relative dynamism, by categories of use. Consumer durables grew at an average rate of around 17.6 per cent during the period 1968-1972, and most certainly contributed to the acceleration of industrial growth, followed by the production of capital goods with an annual average growth rate of 15.8 per cent. However, the output of non-durable consumer goods evolved along lines similar to its traditional course and the rates of increase of the output of intermediate goods barely exceeded the total industrial average.

It may be deduced from the foregoing that the growth of the Brazilian economy in recent years was tied up with the higher rates of growth observed in the consumer durables and capital goods industries.

For this dynamic core to have grown rapidly, certain requirements had to be fulfilled:

(i) favourable evolution of internal and external purchasing power in respect of its products;
(ii) a finance policy which contributed the resources required for the growth of these industries at the right moment;
(iii) no narrow limits to import requirements; and
(iv) investments in supporting infrastructure and in complementary industries.

It could be said that these requirements for the dynamic sectors of industry were fulfilled thanks to the application of a growth policy which laid the necessary bases for the restructuring of the economy round this key core.

2. *The bases for growth*

Although the present analysis does not attempt to explain the recent development model of the Brazilian economy, an explanation may however, be given of certain factors which more obviously laid the bases for expansion. These factors were associated with the reformulation of the finance schemes, the opening-up of the economy to the exterior, public investment policy and the evolution of the structure of income distribution.

(a) *The reform of the finance system*

During the five-year period 1964-1968 Brazil introduced a reform of the national finance system, which brought profound changes to the finance schemes existing in the economy, in that new forms of attracting and distributing resources were created, and played an important role in activating the system and in particular in speeding up industrial expansion. The main changes introduced with this reform are described below.[58]

In connexion with the finance system, an operational modernization of its functions took place, with the diversification of financial instruments and the introduction of some degree of specialization of functions, which meant the more flexible operation of the money and credit markets, and the emergence of an institutionalized capital market, as from 1968.

As regards the immediate financing of the private and public sectors, the changes made led to a considerable growth of liquidity which was independent of the primary expansion of the means of payment as a result of the development of loans schemes outside the banking system and machinery for the tapping and intersectoral circulation of surpluses, by means of the issue of index-tied bonds and debentures.[59]

On the other hand, the financing of capital in the long and medium term benefited considerably from important government measures aimed at attracting foreign capital in the form of money loans and import financing.

[58] M. C. Tavares, *Da substituição de importações aõ capitalismo financeiro recente*, Editorial Zahar, Rio de Janeiro, 1972, pp. 211 et seq.
[59] Adjustments in terms of price increases.

As far as the financing of consumption was concerned, steps were taken to promote the expansion and diversification of consumption of durable goods by the urban middle-income strata, and this played an important part in the recovery and growth of the modern sectors of industry.

As regards long-term financing, several special public funds were set up in association with national and regional development agencies. However, since domestic supply of this type of credit proved inadequate for the needs of the economy, the Government complemented it with external financing (the importance of the external resources used to back up credit in the short, medium and long term will be analysed below).

As from 1968, the capital market began to develop effectively, with the creation of investment banks, the reorganization of the traditional finance sectors, the merging of financial groups, the opening up of entrepreneurial capital and the progressive activation of the direct securities markets, mainly on the stock exchange.

Lastly, mention should be made of the establishment of specialized sub-systems for financing housing, linking up methods of compulsory savings (guarantee fund of length of service)[60] and voluntary savings housing bonds. The Banco Nacional de la Vivienda, the executive agency of the system, taps compulsory savings and is the discount house for the real estate credit documents issued by finance or real estate companies.

Tables 35 and 36 show some of the changes which took place, such as, for example, the loss of importance of the banking sector and the significant diversification of financial institutions. The 80 per cent share of the banking system in total private credit in 1964 decreased to about half in 1973, while the amount of diversified financial intermediation increased by a similar proportion; this was represented in particular by the finance companies (predominantly consumer credit), investment banks (mainly financing for working capital) and the schemes for financing housing.

From another point of view, the new forms of tapping resources significantly changed the structure of the financial assets of the economy (see table 36). A drop in the share of money assets may be observed (from 92 per cent in 1964 to 43.1 per cent in 1973) alongside the increase in the importance of the characteristic instruments of institutions outside the banking system—bills of exchange[61] (16.9 per cent in 1973), fixed-term index-tied deposits (12.6 per cent) and housing bonds (3 per cent). Also of note is the importance in 1973 of index-tied debentures, which had a share of 17.7 per cent in the total financial assets of the system.

The new structure of the financial intermediation in the economy, briefly summarized here,[62] contributed to a considerable extent to maintaining high growth rates during the period.

[60] This Fund was set up in 1966, and consists of a monthly deposit in a special bank account of 8 per cent of the total remunerations paid by the enterprises.

[61] Credit orders accepted by the borrower, negotiable in the market by the financial institution lending the resources which is jointly responsible for the order. The institution advances the resources to the borrower and replaces its liquidity by selling the order on the market.

[62] For a more detailed analysis, see M. C. Tavares, op. cit.

Table 35. Brazil: number of financial institutions operating at end of year

	1964	*1968*	*1971*	*1973*
Commercial banking institutions	336	231	155	115
Development banks	2	4	12	13
Federal	1	1	2	2
State	1	3	10	11
Banco Nacional de la Vivienda	1	1	1	1
Investment banks	–	21	40	45
Savings banks	26	26	6	6
Federal	22	22	1	1
State	4	4	5	5
Finance companies	134	245	170	152
Insurance companies	144	157	157	110
Real estate credit societies	–	25	45	44
Savings and loan associations	–	21	34	36
Brokers' associations	–	377	421	414
Distributors' associations	...	556	572	569
Investment societies	...	6	–	–
Credit co-operatives	–	–	318	324

SOURCE: Banco Central do Brasil, *Relatório Anual*, 1969 and 1973.

Table 36. Brazil: main financial assets
(Percentage share)

	1964	*1968*	*1970*	*1973*
Monetary assets	*92.0*	*67.0*	*55.5*	*43.1*
Paper money in the hands of the public	21.0	12.8	10.5	7.9
Sight deposits	71.0	54.2	45.0	35.2
Non-monetary assets	*8.0*	*33.0*	*44.5*	*56.9*
Savings deposits	...	1.0	3.3	6.7
Fixed-term deposits	2.5	4.5	6.9	12.6
Non index-tied	2.5	1.2	0.2	–
Index-tied	–	3.3	6.7	12.6
Bills of exchange[a]	4.2	14.3	15.3	16.9
Housing bonds	–	2.0	3.1	3.0
Federal debentures (ORTN and LTN)[b]	1.3	11.1	15.8	17.7
Total	*100.0*	*100.0*	*100.0*	*100.0*

SOURCE: Annual reports of Central Bank of Brazil.
[a] See foot-note 61.
[b] For this classification the traditional criterion was used; as regards the LTN, it may be observed that their degree of liquidity gives them more resemblance to monetary assets.

Obviously, it implied a viable solution to the basic problem of the current financing of the enterprises, and made for greater flexibility of supply in the more dynamic sectors of the economy.

The growth of consumer credit, mainly represented by the extension of the operations of the finance companies, which showed an annual average rate of real growth of credit of approximately 41 per cent between 1967 and 1973, was a decisive factor in maintaining urban demand, especially in respect of consumer durables.

Mention may also be made of the creation of the system for financing housing, which in 1973 accounted for 13 per cent of total private sector financing; it produced an increase in the growth of the civil construction industry, which is highly labour-intensive, and constituted an important source of intersectoral demand in the industrial sector.

The restructuring of the capital market not only provided support to investment by the enterprises but also—and this was its major contribution—it made possible an increase in the intersectoral mobility of the capital invested in productive activities, and helped to centralize it in the dynamic core of the economy.

However, despite the fact that it was possible to finance consumption, working capital and investment simultaneously and adequately, no appreciable increase would appear to have been achieved to date in the real rate of domestic savings, which was the main explicit objective for reformulating the national finance system.

(b) *The changeover to outward-directed growth*

Mention should be made here of the important role of the external sector in maintaining the high rate of growth of the economy.

During the period 1968-1972 Brazil changed the direction of its growth model, turning it outwards, and came to depend increasingly on the external sector as a source of capital for current and long-term financing, as an important source of export demand for some sectors, and as a complement to domestic savings, through the increasing deficits in current transactions.

In connexion with imports, a more liberal policy was followed, consistent with the aim of avoiding bottlenecks in the increased rate of growth of the economy. Total imports therefore increased at average rates of around 20 per cent during the period 1967-1970, increasing to 34.5 per cent in recent years (1970-1973), which raised the import coefficient from 4.7 per cent in 1967 to 11 per cent in 1973.

It should be observed that this speeding-up of growth was basically due to the performance of industrial imports which accounted for more than 80 per cent of total imports, and within these, to imports by the most dynamic sectors, e.g., metallurgy, engineering, electrical materials, transport materials and chemicals (see table 37). The importance of these industrial imports in the growth of the domestic supply of the manufacturing sector may be seen from table 38; it will be observed that the percentage increases in the coefficient are particularly meaningful in the sectors producing capital goods.

Table 37. Brazil: imports CIF by sector of economic activity
(Millions of dollars at current prices)

Sector of economic activity	*1965*	*Percentage share*	*1970*	*1972*	*Percentage share*
Metallurgical industry	128	11.7	363	514	10.8
Engineering industry	153	14.0	510	1,060	22.4
Electrical equipment	48	4.3	241	424	9.0
Transport equipment	72	6.5	277	416	8.8
Paper	19	1.7	60	103	2.2
Chemical products	217	19.8	520	799	16.9
Textiles	4	0.3	35	48	1.0
Food	45	4.1	89	98	2.0
Other sectors	47	4.2	211	379	8.0
Total industry	*733*	*67.0*	*2,306*	*3,841*	*81.1*
Total imports	*1,096*	*100.0*	*2,849*	*4,730*	*100.0*

SOURCE: Instituto de Planejamento Econômico e Social (IPEA).

Table 38. Brazil: percentage share of imports in total industrial supply, by sector of economic activity
(Percentages calculated on the basis of current values)

	1962	*1966*	*1970*	*1972*
Non-metallic mineral products	3.8	3.1	3.2	3.9
Metallurgical industry	12.5	16.9	18.7	18.7
Engineering industry	43.1	28.8	35.6	40.4
Electrical equipment	15.6	11.1	20.6	24.9
Transport equipment	17.0	8.8	14.8	14.1
Paper and paperboard	16.3	7.7	11.6	14.6
Rubber	0.5	0.5	1.8	4.0
Chemical products	21.2	16.0	19.6	17.7
Pharmaceutical products	4.9	4.0	5.7	...
Textiles	0.3	0.3	2.0	2.1
Food	2.0	2.8	2.7	2.2
Beverages	2.0	0.7	1.7	2.4
Printing and publishing	3.2	3.9	3.2	...
Miscellaneous	16.2	14.0	28.8	...
Total	*11.1*	*10.0*	*13.3*	*15.2*

SOURCE: Instituto de Planejamento Econômico e Social (IPEA).

It may be noted that the growth of imports in the economy of Brazil, together with the substantial increase in the import coefficient, was unquestionably bound up with the expansion of the dynamic core of industry, which played an important role in ensuring and maintaining high growth rates for the product. While on the one hand this provided a possibility of speeding up growth, on the other it constituted the vulnerable aspect of such growth, in that it imposed increasing rigidity on the pattern of imports, which could come to constitute a bottleneck in the future.

In another area, as from 1964 Brazil began to apply an active policy to attract foreign capital, which was accepted without restriction in any economic activity, with the sole legal exception of the production and refining of petroleum. New forms of external borrowing were created and adopted, thus enabling full advantage to be taken of external resources. External loans could be directly and freely arranged between enterprises abroad and in Brazil, for medium-term financing, while the commercial and investment banks and the Banco Nacional do Desenvolvimento Económico (BNDE) were authorized to contract medium and long-term foreign loans, with the guarantee in both cases of the availability of the foreign exchange required for amortization payments and remittances of interests.

As a result of the measures adopted and in conjunction with a favourable international

Table 39. Brazil: situation of external debt at end of period
(Millions of dollars at current prices)

	1967	*Percentages*	*1968*	*Percentages*	*1969*	*Percentages*	*1970*	*Percentages*	*1971*	*Percentages*	*1972*	*Percentages*	*1973*	*Percentages*
Compensatory loans	...		...		*548.4*	*12.4*	*381.5*	*7.2*	*300.6*	*4.4*	*240.9*	*2.5*	*203.3*	*1.6*
Financing of imports	...		...		*1,355.2*	*30.8*	*1,709.3*	*32.5*	*2,201.5*	*33.3*	*2,783.8*	*29.3*	*3,486.8*	*27.8*
International agencies	278	8.5	306	8.1	363.9	8.3	456.0	8.7	576.2	8.7	762.0	8.0	971.8	7.8
Government agencies	...		...		340.3	7.8	394.4	7.5	469.9	7.1	518.7	5.5	601.0	4.8
Suppliers' credits	497	15.1	520	13.7	651.0	14.7	858.9	16.3	1,155.4	17.5	1,503.0	15.8	1,914.0	15.2
Money loans	*671*	*20.5*	*1,083*	*28.7*	*1,604.7*	*36.5*	*2,284.6*	*43.3*	*3,193.0*	*48.3*	*5,528.3*	*58.1*	*7,848.5*	*62.5*
Resolution 63	...		...		432.5	9.8	653.2	12.4	983.3	14.8	2,018.4	21.2	2,398.1	19.1
Edict 289	...		...		373.5	8.5	381.2	7.2	294.8	4.5	207.4	2.2	71.1	0.6
Act 4 131	...		...		798.7	18.2	1,250.2	23.7	1,914.8	29.0	3,302.5	34.7	5,379.3	42.8
Other	...		...		*895.0*	*20.3*	*919.8*	*17.0*	*926.5*	*14.0*	*968.0*	*10.1*	*1,032.9*	*8.1*
Total	*3,281*	*100.0*	*3,780*	*100.0*	*4,403.3*	*100.0*	*5,295.2*	*100.0*	*6,621.6*	*100.0*	*9,521.9*	*100.0*	*12,571.5*	*100.0*
International reserves	199		257		656		1,187		1,746		4,183		6,417	

SOURCE: Central Bank of Brazil.

Table 40. Brazil: structure of exports
(Millions of dollars at current prices)

	1964–1967	Percentages	1968	Percentages	1971	Percentages	1972	Percentages	1973	Percentages
Primary products . .	1,317	82.0	1,492	79.3	1,988	68.6	2,725	68.3	4,096	66.1
Industrial products . .	281	17.5	380	20.2	821	28.3	1,222	30.6	1,941	31.3
Semi-manufactures .	139	8.7	178	9.5	240	8.3	310	7.8	476	7.7
Manufactures . .	142	8.8	202	10.7	581	20.0	912	22.8	1,465	23.6
Other products . . .	7	0.5	9	0.5	65	2.2	44	1.1	162	2.6
Total	*1,605*	*100.0*	*1,861*	*100.0*	*2,904*	*100.0*	*3,991*	*100.0*	*6,199*	*100.0*

SOURCE: Carteira de Comércio Exterior (CACEX).

economic situation, Brazil received a substantial inflow of capital, especially as from 1968. Table 39 shows the evolution of the inflow of resources in its two main forms: financing of imports (suppliers' credits) and money loans. As a result, Brazil's external debt increased at an annual average rate of 25 per cent, and grew from 3,300 million dollars in 1967 to 12,600 million in 1973; the servicing of this debt accounted for an average of 53 per cent of the value of exports during the three-year period 1971-1973.

The considerable inflow of capital made it possible to finance the growing deficits in current transactions, with the result that the economy's balance of payments reflected a surplus which enabled international reserves to be stockpiled over the last two years and reach the sum of 6,400 million dollars in 1973 (see table 39). It also came to constitute an important factor in the increase in domestic levels of finance for working capital and investment, although it could be said that the credit granted was to a large extent selective, since it benefited the relatively more dynamic activities or those controlled by foreign capital, or both. It should also be observed that the large intake of external resources dangerously increased the external vulnerability of the economy, and also represented a constant factor of inflationary money growth.

In view of the external debt and the increasing deficits in current transactions it was necessary to adopt an aggressive export policy, which made it possible to finance the growth of imports and remittances of interests and profits, and also cope with servicing the debt itself. The vigorous growth of exports also contributed to complementing the domestic markets, resulting in a more active demand and a better use being made of the economies of scale and of the internal standards of efficiency of the more dynamic enterprises. It is hard to imagine that the high rates of growth observed in recent years could have been maintained without a decisive contribution from exports.

In order to promote exports, especially of manufactures, a broad-based incentive policy was applied. Exports were exempted from indirect taxes; income tax ceased to be applied to export profits; sales of manufactures were subsidized, special interest-subsidized lines of finance were set up for products for the external market; and as from 1968, a system of periodic devaluations of the cruzeiro was adopted (frequent small adjustments) in order to achieve a stable balance between domestic and external prices.

As a result of this policy, Brazilian exports increased at an average annual rate of 24.5 per cent during the period 1967-1973, and their money value increased from 1,600 million dollars to 6,200 million dollars (see table 40). Of this total, exports of manufactures, which were insignificant in 1964, accounted for 1,900 million dollars in 1973, or 31.3 per cent of total exports.

The real importance of the increase in exports, however, is not to be found in the additional demand which they imply for the system, especially as regards exports of manufactures. Although their share in the industrial product doubled, they accounted for only 6.3 per cent of the product in 1973 (see table 41).

In fact, the success of the export policy was

Table 41. Brazil: shape of exports of manufactures in the industrial product
(Millions of cruzeiros at 1960 prices)

Year	Exports of manufactures (A)	Manufacturing product (B)	Share (A)/(B)
1968 . . .	26.2	849.1	3.1
1969 . . .	35.9	940.8	3.8
1970 . . .	47.0	1,069.8	4.4
1971 . . .	67.2	1,190.7	5.6
1972 . . .	83.4	1,358.6	6.1
1973 . . .	99.3	1,573.3	6.3

SOURCE: ECLA, on the basis of official statistics.

rather in constituting the axis of outward-directed growth, and led to a liberal policy of imports of capital goods and inputs, which were of basic importance to industrial growth, and which came to be the basis for the considerable absorption of external resources.

(c) *The role of the public sector*

Among the factors of expansion of the new stage of growth in Brazil's economy, may be mentioned the evolution of public investment as from 1967 in both quantitative and qualitative terms.

It is fairly difficult to elucidate this point in the case of Brazil, since there are no official data referring to the public sector as a consolidated whole, including State entrepreneurial activity, which is especially important in the economy of Brazil, particularly because of the presence of public enterprises in such dynamic sectors of industry as petroleum, steel, chemicals, mining, electric energy, and transport and communications.[63] The State presence in the economy can thus only be measured on the basis of data provided by the central government, including independent public enterprises, foundations and some special funds. Even so, the importance of the central administration is not negligible in terms of its effects on the system, since government investment accounted for around 17 per cent of the gross fixed capital formation of the economy during the years 1971-1973 and for 35 per cent of the economy's total savings in 1972-1973.

As will be understood, the consideration of the public sector as a consolidated whole would greatly increase this impact. It may indeed be estimated that public investment, including that of Government bodies and public enterprises, could account for between 11 and 12 per cent of the gross domestic product,[64] which means that its share in gross fixed capital formation would be over 40 per cent.

Apart from its volume, public investment played an important role in the recent growth of the Brazilian economy, particularly because it was directed towards the activities with most influence on the system. In this context, as from 1967, the public sector destined resources on a massive scale for investment in electric energy, transport and communications, petroleum and petroleum products, mining and steel. The public investment programme, conceived as a complement to and a harmonious part of the growth of the dynamic core of industry, represented a substantial demand directed towards the communications, metal manufactures and machinery, electrical equipment and chemical industries, and came to be one of the bases for the rapid growth of industry.

(d) *The evolution of income distribution*

The aim in the foregoing pages was to show that the growth of the Brazilian economy in recent years was basically associated with the rapid growth of some dynamic sectors of industry which coincided with the consumer durables and capital goods sectors.

Of course, to propose an increase in growth in some branches of industry means, among other things, proposing an increase in the growth of purchasing power directed at the products of these industries. In other words, in a process of growth, the structure of supply should be consistent with that of demand. The growth of the dynamic sectors of industry must thus have been accompanied by the corresponding changes in the profile of demand.

Some of the mechanisms which contributed to the profile of demand evolving along the same lines as the dynamic sectors of industry were already dealt with when the changes in the system of financing (especially as regards consumer credit), the expansion of industrial exports and the structure of public investment were considered. Although these factors played an important role in the reformulation of demand, they can hardly explain all the changes which took place in recent years. In fact, the profile of demand is conditioned above all by the structure of income distribution and this is where the main basis for its makeup must be sought.

In this respect, table 42 is fairly revealing. It shows that between 1960 and 1970 income distribution in the Brazilian economy underwent a process of marked concentration, with a drop in the share of total income of 80 per cent of the economically active population, which would go to show that the dynamic purchasing power of the system was concentrated in the top 20 per cent of the income pyramid. In the case of Brazil, it may be observed that this would represent a pattern of high-level consumption for around 20 million persons.[65]

From a different standpoint, the same conclusion may be suggested from the observation of table 12, which gives the percentage increase in

[63] Of Brazil's 20 major enterprises, 11 are State-owned (see M. H. Simonsen and R. Campos, *A nova economia brasileira*, Editorial José Olympio, Rio de Janeiro, 1974, p. 205).

[64] M. H. Simonsen, "*O modelo brasileiro de desenvolvimento*", in M. H. Simonsen and R. Campos, op. cit., p. 14.

[65] Preliminary estimates by ECLA indicate that in 1972 the top 20 per cent had an annual *per capita* income of over 2,000 dollars (at 1970 prices).

Table 42. Brazil: income distribution among the economically active population

Decile of the economically active population	*Percentage of total income*	
	1960	*1970*
1st decile	1.17	1.11
2nd decile	2.32	2.05
3rd decile	3.42	2.97
4th decile	4.65	3.88
5th decile	6.15	4.90
6th decile	7.66	5.91
7th decile	9.41	7.37
8th decile	10.85	9.57
9th decile	14.69	14.45
10th decile	39.66	47.79
Poorest 40 per cent	11.56	10.01
Next 40 per cent	34.09	27.75
Richest 20 per cent	54.35	62.24
Total	*100.00*	*100.00*

SOURCE: M. H. Simonsen and R. Campos, op. cit., p. 188.

real *per capita* income for the different income groups. The average annual rates of growth of real income increase sharply after the seventh decile, showing that income is concentrated in the upper-middle and upper income groups. That data also show that the real income of the poorest 40 per cent of the population is increasing at an accelerated pace, especially in the case of the first 10 per cent. However, the importance of this growth, from the point of view of purchasing power in respect of the products of the dynamic industries is fairly secondary, since absolute levels of *per capita* income in these groups constitute a minor market for consumer durables. The rapid growth of purchasing power in respect of goods with a more sophisticated degree of manufacturing is therefore unmistakably associated with the upper income groups which correspond in particular to the top 20 per cent of the economically active population.

Table 43. Brazil: percentage increase in real *per capita* income by class of income, 1960-1970

Decile of the economically active population	*Increase in real* per capita *income 1960/1970*
1st decile	27.1
2nd decile	18.4
3rd decile	16.4
4th decile	11.8
5th decile	6.8
6th decile	3.4
7th decile	5.0
8th decile	18.2
9th decile	31.8
10th decile	61.5
Poorest 40 per cent	16.0
Next 40 per cent	9.1
Richest 20 per cent	53.5
Total	*34.0*

SOURCE: M. H. Simonsen and R. Campos, op. cit., p. 189.

The concentration of personal income, with the profile of demand which it influences, therefore played a decisive role in the resumption and maintenance of recent growth in the economy of Brazil.

C. MAIN FEATURES OF ANTI-INFLATIONARY POLICY

The anti-inflationary policy applied in Brazil must be interpreted with reference to a much longer period than is usually taken into account in this type of analysis in Latin America. In effect, the continuity of stabilization efforts has been maintained throughout the terms of office of four governments and extends over the 10-year period of 1964-1974.

Although the control of inflation has followed harmonious lines, it is possible to distinguish three major periods, in which the keynotes of stabilization policy have differed, with varying results, attributable to policy implementation or to changes in the international situation, or to a combination of both.

The first was the three-year period 1964-1966, in which stabilization was the primary objective of economic policy, pursued essentially through strict control of demand. Although the rate of increase of prices dropped rapidly (from 91.9 per cent in 1964 to 34.5 per cent in 1965), the concomitant was a severe "stabilization crisis", with mediocre growth rates of the product.

Nevertheless, this crash policy, combined with a strong swerve towards outward-directed development, created the right conditions for combating inflation more gradually, in such a way that the rate of increase of prices declined gently, from 24.3 per cent in 1967 to 20.2 per cent in 1969, 19.2 per cent in 1970 and 15.5 per cent in the two-year period 1972-1973, while the product expanded at annual rates of over 9 per cent. This period of growth combined with decreasing inflation extended from 1967 to 1973, and marked a second phase of policy.

During the last two years of the period under consideration, Brazil's economic development, closely linked as it is to the external sector, was considerably affected by the contraction in the European financial markets; the high growth rates were maintained, but were accompanied by an inflation which resumed its active role in the

economy, with prices rising by 34.6 per cent in 1974. On this account, rapid changes had to be introduced in stabilization policy, and thus began the third phase of Brazil's anti-inflationary policy.

1. *The crash policy, 1964-1966*

As from 1961, inflationary trends sharpened in the Brazilian economy, and although attempts were made to apply stabilization programmes, the process steadily worsened up to 1964.

The anti-inflationary policy applied from 1964 onwards was based on the diagnosis that the prevailing inflation was one of demand, and stemmed from three main causes: the cash deficits of the National Treasury; the over-expansion of credits to the private sector; and wage adjustments disproportionate to the increase in productivity.[66] Thus, the chief policy instruments were concentrated in the conventional spheres of fiscal, credit and wage policy, in different degrees of intensity as circumstances dictated. In practice, the primary objective of economic policy was the drastic control of increases in total demand.

(a) *Growth patterns of the product and of prices*

The evolution of the economic sectors and of the product in 1964-1966 may be observed in table 44, where the slow rate of economic growth is plainly evident. It should be noted that the highest rate for the gross domestic product does not exceed 4.4 per cent, and that in the most important sectors of production, such as agriculture and industry, violent fluctuations took place. Although it must be recognized that the previous three years had been a period of economic crisis, development in 1964-1966 was radically affected by the crash anti-inflationary policy. In 1965, for example, manufacturing showed a negative growth rate of about 4.9 per cent, which reflected the profound "stabilization crisis" affecting it. Had it not been for the exceptional results obtained by the agricultural sector, thanks to favourable weather conditions, the rate of increase of the product in that year would not have reached 2.5 per cent, and the *per capita* growth rate would have been negative. In 1966, in contrast, manufacturing regained its dynamic impetus, and it was in agriculture that the rate of development was negative, with the consequent depressive effect on the increase in the total product. In the following year, agriculture and industry again switched roles, their respective growth rates being 9.6 per cent and 1.8 per cent; manufacturing underwent a second "stabilization crisis", which began at the close of 1966.

From another angle, price trends in the period show how the pace of inflation quickened up to 1965, in which year, as in 1964, the rates of increase reflected in the over-all price index exceeded 90 per cent (see table 45). From 1965 onwards, with the adoption of a strict anti-inflationary programme, the process of inflationary expansion was definitely disrupted, and the result was the "stabilization crisis" of 1965.

In the following year, the inflexibility of stabilization policy was slightly relaxed, and price indexes rose again, showing the stubborn resistance of rates of inflation to reduction below a limit of about 35 per cent per annum.

(b) *Main lines of stabilization policy*

Anti-inflationary policy in 1964-1966 centred on measures relating to fiscal, monetary, wages and price policy.

With respect to fiscal policy, the strategy

[66] Ministerio do Planejamento, *Programa de Ação Econômica de Governo 1964-1966*, p. 28.

Table 44. Brazil: gross domestic product by sector of economic activity
(Annual percentage growth rates)

Sector	*1960-1965*	*1964*	*1965*	*1966*
Agriculture, forestry and fishing	5.7	1.3	13.8[a]	−2.0
Mining and quarrying	13.5	18.4	12.0	12.2
Manufacturing	3.7	5.1	−4.9	11.8
Construction	−2.8	2.2	0.7	11.7
Electricity, gas and water	6.3	7.0	4.7	11.7
Transport and communications	5.3	3.6	0.8	5.7
Commerce and finance	3.8	3.1	5.0	5.5
Ownership of dwellings	3.6	3.6	3.6	3.6
Public administration and defence	2.4	2.4	2.4	2.4
Miscellaneous services	3.0	3.0	3.0	3.0
Total	*4.2*	*3.1*	*3.8*	*4.4*

SOURCE: ECLA, *Economic Survey of Latin America*, 1965 and 1966.
[a] Excluding coffee.

Table 45. Brazil: percentage variations in selected price indexes

Index	*1962*	*1963*	*1964*	*1965*	*1966*
Cost of living in Guanabara	88.5	80.6	86.5	45.3	41.1
Cost of living in São Paulo	61.8	80.5	85.5	41.1	46.3
Wholesale prices in general	50.2	81.9	93.3	28.2	37.4
Wholesale prices excluding coffee	45.7	83.0	84.0	31.3	41.6

SOURCE: ECLA, *Economic Survey of Latin America*, 1967.

adopted consisted in reducing the deficit through the expansion of income and the restriction of public spending. In view of the inflexibility of the structure of expenditure, despite the partial contraction of public investment achieved, the emphasis was on action to increase revenue, an emergency tax reform being introduced in the second half on 1964. In real terms, public sector income expanded at an average annual rate of 8.7 per cent over the three-year period, whereas the annual growth rate of expenditure did not rise about 1.7 per cent (see table 46),

The rest of the fiscal deficit was financed through the compulsory and voluntary sale of official securities in the form of the newly-created Adjustable Treasury Bonds, which were safeguarded against devaluations of the currency, and of which the redemption period, originally fixed at three years, was subsequently reduced to one year. It was thus possible to finance 54 per cent of the fiscal deficit in 1965 and to collect revenue in excess of the deficit in 1966, so that the National Treasury became a net source of funds for the monetary authorities (see again table 46).

While this fiscal policy did succeed, on the one hand, in reducing the deficit and thus obviating a primary expansion of the means of payment on the other hand it had heavily depressive effects on the level of economic activity, causing a greater contraction of total demand than the Government had desired.

The second front in the anti-inflationary battle was constituted by wage policy. This was based on a diagnosis to the effect that wage adjustments during the post-war period had outstripped the increases in the average productivity of the economy, and that in consequence it was necessary to re-establish the structure of income distribution as between wage-earners and the other groups. A new system of wage adjustments was therefore applied, under which the average real wage for the past 24 months was restored, with the incorporation of the increases in productivity achieved in the preceding period plus an estimate of the expected rise in prices in the period during which the new wage would be in force ("inflationary residuum"). This method of adjustment considerably reduced the real minimum wage since it was based on rates of inflation projected by the Government (25 per cent, 10 per cent and 15 per cent for 1965, 1966 and 1967, respectively), which fell short of the price increases that actually occurred (see table 47). Thus, wage policy became yet another depressive factor affecting demand in the economy, besides playing an important part in the redistribution of income in favour of the higher brackets, as was shown in the first section of this chapter.

The aim of credit policy was to mobilize the savings of private enterprises for the financing of their normal operations. To that end, the credit provided by the Banco do Brasil (which is responsible

Table 46. Brazil: national treasury. Evolution of the fiscal budget
(Millions of cruzeiros at current prices)

Year	*Income*	*Real income (cruzeiros at 1964 prices)*	*Expenditure*	*Real expenditure (cruzeiros at 1964 prices)*	*Deficit*	*Financing of deficit*		*Deficit as a percentage of gross domestic product*
						Monetary authorities	*General public*	
1964	2,129	2,129	2,857	2,857	−728	736	−8	3.2
1965	3,907	2,491	4,500	2,869	−593	270	323	1.6
1966	5,910	2,733	6,500	3,006	−587	−190	606	1.1

SOURCE: Central Bank of Brazil.

Table 47. Brazil: evolution of legal minimum wage

Year	Minimum monthly wage (cruzeiros)	Index of evolution of minimum wage in real terms (1965 = 100)	
		Guanabara	São Paulo
1964	40.25	108	105
1965	62.00	100	100
1966	81.00	93	90

SOURCE: P. Auberger, *Le modèle brésilien de lutte contre l'inflation. Problémes d'Amérique Latine*, December 1973.

for one third of total credit) was severely restricted, and strict control was exercised over the private commercial banks' capacity to expand the means of payment (see table 48). The real value of bank loans during the three-year period was kept far below the average for 1960-1962. Enterprises, faced with the impossibility of converting their immovable assets (accumulated as a safeguard against inflation) into ready cash, exerted pressure on the financial market, thus forcing up the real rate of interest. In addition, the Government itself aggravated the financing problem by competing on advantageous terms with the private sector in the tapping of savings and of the monetary reserves existing in the system, through the sale of the Adjustable Treasury Bonds.

Aside from these measures, but with no less significant repercussions, the prices that had remained frozen or had lagged behind during the preceding five-year spell of inflation were adjusted. The "corrective inflation", as this line of action was termed at the time, affected exchange rates, rents, public utility tariffs, prices of transport and fuels and, in general, prices of the inputs produced by the public enterprises. Its impact made itself felt in pressures on costs, which made their appearance in the economy from 1965 onwards.

The crash programme applied during the three-year period 1964-1966 succeeded in drastically reducing price increases, and definitely checking the advance of inflation. This anti-inflationary policy, however, had negative effects on the level of economic activity, through the contraction of real disposable income and the consequent insufficiency of total demand. At the same time, other cost pressures emerged in the economy, with the imposition of heavier taxation, the raising of the real rate of interest, and the price increases deriving from the so-called corrective inflation.

Table 48. Brazil: loans to the private sector
(Thousands of millions of old cruzeiros at 1960 prices)

Year	Banco do Brasil	Commercial banks	Total
1963 . .	181.4	298.7	480.1
1964 . .	165.0	286.4	451.4
1965 . .	173.5	379.7	553.2
1966 . .	170.8	336.9	507.7

SOURCE: ECLA/ILPES, *A evolução recente da economia brasileira*, Rio de Janeiro, 1967.

2. *Growth with relative stability. The gradualist policy applied in 1967-1973*

To judge by the rates of inflation and by economic growth, the achievements of the gradualist policy are obvious. In the evolution of the rate of inflation, measured by the variations in the over-all price index, three different periods can be distinguished: the two-year period 1967-1968, in which rates of inflation fluctuated between 24.3 and 25.4 per cent; the three years 1969-1971, in which annual rates ranged from 19 to 20 per cent; and the period 1972-1973, in which the annual variation in the index was 15.5 per cent (see table 51). Moreover, the expansion of economic activity reflected annual growth rates of the product exceeding 9 per cent from 1968 onwards. These indicators illustrate the steady decline in the rates of inflation and the attainment of the growth objective in the period analysed.

If the anti-inflationary policy pursued in Brazil as from 1967 is to be correctly interpreted, it must be considered in the broader context of an economic policy with growth as its primary objective, by which stabilization policy is conditioned.

Although at times both objectives—stability and growth—were furthered by the same expedients (as in the case of the reform of the national financial system and the strengthening of internal credit by means of external loans), this was not always the case. In the second phase, growth became the predominant aim, and in consequence an expansionist monetary policy was adopted, which was intended to stimulate demand and support production, but which at the same time constituted an inflationary factor.

It is, of course, obvious that stabilization

efforts were greatly favoured by the changes introduced in the financial system, as briefly described in the first section of this chapter. While, on the one hand, the broadening and diversification of the financial system was designed to lay the foundations for the expansion of the dynamic core of economic development, another aim was to put into practice financing programmes which were based on the tapping of private savings and monetary reserves and which would progressively replace the traditional modes of financing, based on inflationary expansion of the means of payment and on the over-dependence of enterprises on internal sources of funds. In the last analysis, the reform of the national financial system permitted the creation of liquidity in the economy, independently of the primary expansion of the means of payment (see table 36). Moreover, the flow of external resources was favourable to the proposed expansion of economic activity; the growth of imports, especially of capital goods, was strongly supported by external financing. From the point of view of inflation, however, it must be recognized that the inflow of capital constituted the most dynamic factor of monetary expansion during the period under consideration, an expansion which was offset by the implementation of an active open-market policy.

Access to external credit made enterprises less dependent upon the traditional sources of internal financing, which suggests that without this foreign backing the rate of inflation might have been higher.

With respect to monetary and credit policy, the period was characterized by a relatively tolerant attitude towards the expansion of the means of payment, as a means of ensuring the encouragement of demand. The aim was not to eradicate inflation over the short term, but to compromise with declining rates that would be compatible with the accelerated growth of the product. In this context, stabilization policy was concerned mainly with applying mechanisms to counteract those effects of inflation that made for disequilibrium (periodical devaluation of the exchange rate, generalized monetary adjustments), rather than with stringent measures to prevent a moderately inflationary expansion of the means of payment, although the monetary authorities had at their disposal a great many fiscal, credit, financial and monetary instruments by means of which they could extend their control over the expansion of liquidity in the economy.

From another standpoint, the more drastic stabilization measures sought to keep under control certain cost items considered to be of strategic importance; this enhanced the significance of wage policy, of action taken to stabilize rates of interest, and of price control policy.

(a) *Sources of inflationary pressures during the period*

The main sources of inflationary pressures through expansion of the means of payment during the period 1968-1973 are shown in table 49. It can be seen that monetary expansion in the period was essentially linked to the increase in credits to the private sector and the national currency counterpart of the increment in international reserves.

The annual rate of expansion of credit to the private sector averaged 38 per cent during the quinquennium, while the growth rate of reserves was 50 per cent per annum between 1969 and 1973.

It is of interest to note that these two factors were closely related to the maintenance of the rate of economic growth, and were the result of the economic policy aim of applying a specific growth model, thus making it clear that the stability objective was subordinated to the proposed growth targets.

From a different point of view, linked to cost pressures in the economy, a major role was played by the raising of the rate of interest, which from 1967 onwards became increasingly positive. Table 50 shows the evolution of real rate of interest, which from a negative value of about 30 per cent in 1964 rose by 1969 to positive rates of 8.4 per cent and 19.3 per cent for bank loans and bills of exchange, respectively.

Special mention must also be made of the expectation factor in the maintenance of rates of increase in prices during the period under consideration. The persistence of an active inflationary process in the recent past had incited enterprises to adjust their prices largely as a function of the rate of inflation expected for the coming period, thus introducing a factor of self-propagation of the inflationary process. This factor, operative in the early years of the period, lessened in importance as the rate of inflation was reduced. By no means negligible, however, was the similar role played in refuelling inflation by such mechanisms as monetary adjustment and the flexible exchange rate, which were established to mitigate some of the effects of inflation.

Lastly, attention must be drawn to the traditional role of the agricultural sector in the Brazilian economy. It operates as an autonomous factor of expansion or contraction of prices in accordance with the variations in agricultural production, exposed as it is to the vicissitudes of weather conditions and to greater price flexibility. Agricultural price fluctuations are reflected directly in the rate of inflation, through changes in the wholesale price index, in which they carry a weight of approximately 37 per cent. It is worth

Table 49. **Brazil: monetary sector operations and means of payment**

	Absolute variations (millions of cruzeiros at current prices)						*Relative variations*				
	1968	*1969*	*1970*	*1971*	*1972*	*1973*	*1968*	*1969*	*1970*	*1971*	*1972*
I. *Expansionist factors*	*13,390*	*12,356*	*14,391*	*20,643*	*30,869*	*41,910*	*56.5*	*38.2*	*33.1*	*35.8*	*34.8*
Loans	8,335	7,603	9,508	13,012	17,254	30,535	56.8	32.0	30.3	33.3	29.5
To the public sector	1,410	−583	173	−3,582	−6,694	−4,400	42.3	−12.0	4.1	–	−834.0
National Treasury	1,075	−1,025	−833	−3,364	−7,670	−5,721	44.0	28.3	−32.1	–	−484.3
State governments, municipal authorities and other public institutions	335	442	1,006	−218	976	1,321	34.5	36.0	60.0	−24.5	−3.1
To the private sector[a]	6,925	8,186	9,335	16,594	23,948	34,935	61.1	43.2	34.4	45.5	43.6
Liquid foreign reserves	36	2,822	3,498	2,246	15,123	14,004	3.2	328.8	137.5	67.2	216.3
Other foreign exchange accounts[b]	391	362	1,803	−1,456	−4,313	−1,001	21.7	8.2	−41.4	−29.4	−1.8
Official securities in the hands of commercial banks (adjustable National Treasury bonds and National Treasury bills of exchange)		706	1,051	1,613	3,033	4,656		73.4	63.0	59.3	71.7
Other accounts of the Banking system (liquid balance)	4,628	863	2,137	5,228	−228	−6,284	76.1	22.2	61.6	68.9	−24.6
II. *Contractionist factors*	*6,969*	*5,388*	*6,821*	*9,402*	*13,713*	*13,142*	*79.6*	*49.0*	*45.2*	*43.2*	*38.2*
Time deposits	391	164	629	2,103	2,908	1,748	65.2	21.5	67.9	135.2	77.8
Other deposits	–	582	898	699	1,864	2,559	–	29.6	35.2	20.7	−2.6
Coffee Fund	597	1,397	1,180	479	408	−196	198.9	86.2	41.1	11.4	8.7
Own resources of monetary authorities and commercial banks[c]	5,981	3,245	4,114	6,121	8,533	9,031	66.0	53.6	56.5	48.4	46.6
III. *Expansion of liquid money supply* (I − II) = (A + B)	*6,421*	*6,968*	*7,570*	*11,241*	*17,156*	*28,768*	*43.0*	*32.6*	*26.7*	*31.3*	*32.6*
A. Sight and short-term deposits	5,285	5,658	6,240	9,405	14,164	23,152	44.1	30.4	27.2	32.2	32.1
Private sector	3,978	4,504	5,108	8,384	13,314	19,750	40.6	32.6	27.9	32.0	31.7
Public sector	1,307	1,154	1,132	1,021	850	3,402	61.5	33.0	24.3	33.7	35.1
B. Paper money in the hands of the general public	1,136	1,310	1,330	1,836	2,992	5,616	38.6	32.1	24.7	27.3	35.1

SOURCE: Reports of Central Bank of Brazil.

[a] 1969: excluding coffee.

[b] Monetary authorities and commercial banks.

[c] 1968, 1969 and 1970: including counterpart of external resources.

Table 50. Brazil: average annual rates of interest on loans, deflated by the over-all price index
(Percentages)

Year	Commercial banks	Banco do Brasil	Bills of exchange	Resolution No. 63[a]
1960	−7.4	−15.2	9.9	–
1961	−11.8	−18.0	10.9	–
1962	−17.5	−25.1	5.5	–
1963	−25.6	−35.0	−2.8	–
1964	−30.1	−37.5	−4.9	–
1965	−14.1	−21.7	14.1	–
1966	−2.3	−9.1	24.2	–
1967	4.5	−5.1	16.1	9.3
1968	7.6	8.4	17.7	28.9
1969	8.4	–	19.3	11.1
1970	–	–	19.9[b]	8.6

SOURCE: Donald Syvrud, *Estrutura e Politica de Juros no Brasil*, 1960-1970, January-March 1972.

[a] Resolution of the Central Bank under which domestic enterprises were granted access to external credit, through the commercial and investment banks.

[b] May.

noting, however, that in 1967-1968 increases in agricultural prices were lower than those shown in the other price indexes. As from 1969 the situation was reversed, and agricultural prices rose faster than the rest (see table 51). Paradoxically enough, the changes in the price system determined by the greater increases in the agricultural prices coincided with the decline of inflation and the speeding-up of the growth rate of the product.

(b) *Control of inflation*

(i) *Fiscal policy.* The main concern of fiscal policy in relation to the stability objective was the control and financing of the fiscal deficit.

As has already been shown, the aim of the first line of action, initiated in the preceding period (1964-1966), was to improve fiscal revenue through the implementation of a tax reform, which expanded the sources of taxation and promoted the redistribution of fiscal revenue between the Federal Government and the states. By virtue of these measures, it was possible to increase revenue more rapidly than prices rose, as can be seen in table 52.

This increment made no appreciable difference to the proportion of the gross domestic product represented by the tax burden. The increase in the share of the Federal Government was offset by the decrease in that of the local governments and other public institutions (see table 53).

The real increase in public expenditure was

Table 51. Brazil: indexes of prices
(Percentage rates of variation)

Year	Indexes of wholesale prices			Index of cost of living in Guanabara[a]	Index of cost of construction	Over-all price index[b] (internal availabilities)
	Total demand	Agricultural products	Industrial products			
1967	22.5	21.1	23.1	24.1	41.3	24.3
1968	25.0	16.7	34.6	24.5	32.7	25.4
1969	21.8	31.7	15.1	24.3	12.3	20.2
1970	19.3	20.3	18.9	20.9	18.7	19.2
1971	20.2	24.7	16.7	18.1	12.7	19.8
1972	17.5	22.3	15.4	14.0	19.8	15.5
1973	16.7	16.7	16.6	13.7	21.1	15.5

SOURCE: Fundação Getúlio Vargas.

[a] Index of consumer prices.

[b] Synthesis of indexes of total supply (wholesale prices), cost of living in Guanabara and cost of construction, weighted by 0.6, 0.3 and 0.1, respectively.

Table 52. Brazil: national treasury. Evolution of the fiscal budget
(Millions of cruzeiros at current prices)

	1967	*1968*	*1969*	*1970*	*1971*	*1972*	*1973*
Income	6,814	10,275	13,953	19,194	26,980	37,738	52,863
Percentage rate of variation . . .	15.3	50.7	35.8	37.6	40.5	39.9	40.1
Expenditure	8,039	11,502	14,709	19,932	27,652	38,250	52,568
Percentage rate of variation . . .	22.9	43.1	27.9	35.5	38.7	38.3	37.4
Deficit	−1,225	−1,227	−756	−738	−672	−516	295
Gross domestic product	71,486	99,879	133,117	174,624	234,005	298,902	406,221
Income as a percentage of the gross domestic product	9.5	10.3	10.5	11.0	11.5	12.6	13.0
Expenditure as a percentage of the gross domestic product	11.2	11.5	11.1	11.4	11.8	12.8	12.9
Deficit as a percentage of the gross domestic product	1.7	1.2	0.6	0.4	0.3	0.2	–
Evolution of over-all price index	24.3	25.4	20.2	19.2	19.8	15.5	15.5

SOURCE: Central Bank, and Fundação Getúlio Vargas.

Table 53. Brazil: evolution of tax revenue

	Rates of taxation in relation to gross domestic product	
	1968	*1971*
Federal government . .	10.6	12.0
Local governments . .	10.1	9.1
Other public bodies . .	7.8	6.9
Total	*28.5*	*28.0*

SOURCE: P. Auberger, op. cit.

approximately 14 per cent per annum in 1967–1973, which reflects a considerable expansion and a heavier incidence on the Brazilian economy. To analyse the growth of public spending from the standpoint of the interpretation of inflation, two important facts must be taken into account: the type of financing of the fiscal deficit and the changes in the structure of public expenditure.

The maintenance of the policy launched in 1964–1966, which consisted in financing the deficit through the sale of Adjustable Treasury Bonds, obviously meant that there was no direct expansion of liquidity in the economic system under this head. Moreover, the success achieved with these bonds was such that from 1969 onwards the National Treasury was in a position to supply the monetary authorities with funds, as will be shown later.

With regard to the structure of public expenditure, attention must be drawn to the greater expansion of investment, consistent with the desire to keep growth rates high over the period under review. The share of current expenditure, which had been about 75 per cent of total outlays in 1966–1967, decreased to 63 per cent in 1972, so that the capital budget was able to expand more rapidly, especially the proportion allocated to infrastructure, and a safeguard was provided against undesirable increases in the fiscal deficit.

As a result of the changes indicated in both income and expenditure the deficit in question was substantially reduced. Whereas in 1962 it had represented 1.7 per cent of the product, by 1972 it accounted for only 0.2 per cent, and in 1973 it had even given place to a small surplus (see table 52).

(ii) *Monetary and credit policy*. Monetary and credit policy in the period was subordinated to the maintenance of levels of liquidity in the economy which would be compatible with the attainment of high growth rates. In this connexion, unremitting care was taken to keep the money supply constant as a proportion of the product, thus forestalling, above all, liquidity problems which might have a depressive effect on economic activity. The experience of the previous two years, when monetary policy had gone too far in slowing down the growth rate of the means of payment, counselled the maintenance of an easy flow of operations in the financial sphere. Thus, the monetary supply

Table 54. Brazil: evolution of means of payment
(Millions of cruzeiros at current prices: balances at end of period)

	1967	1968	1969	1970	1971	1972	1973
Means of payment .	14,931	21,352	28,350	33,638	44,514	61,550	90,490
Rate of increase .	42.6	43.0	32.8	18.6	32.3	38.3	47.0
Evolution of over-all price index . .	24.3	25.4	20.2	19.2	19.8	15.5	15.5
Gross domestic product .	71,486	99,879	133,117	174,624	234,005	298,902	406,221
Means of payment as a percentage of the gross domestic product .	20.9	21.4	21.3	19.3	19.0	20.6	22.3

SOURCE: Fundação Getúlio Vargas, *Conjuntura Econômica.*

expanded at an average annual rate of 35 per cent in 1967-1973, and the proportion of the product that it represented hovered between 19 and 22 per cent (see table 54).

The variations in the means of payment and prices during the years 1970-1973 refute assumptions that these variables are closely associated within a context of rapid growth. In actual fact, whereas from 1970 onwards the means of payment expanded at increasing rates, the over-all price index, precisely in that period, showed a clearly-defined downward trend.

It should be recalled, of course, that the changes introduced through the reform of the national financial system made it possible to give the economy increased liquidity independently of the primary expansion of means of payment, as was explained in the first section of this chapter (see again table 36).

It is worthwhile repeating that another factor which enlarged the sphere of operation of the monetary authorities was the possibility of avoiding the financing of fiscal deficits through primary issues. As has been stated, fiscal deficits were successfully covered by issues of Adjustable Treasury Bonds which were sold to public institutions, commercial banks and the general public. The growth of these sales is worthy of note, for by 1969 the operations of the National Treasury had already become an important factor of monetary contraction (see table 55). In 1972 the funds collected by this means amounted to 8,282 million cruzeiros, or the equivalent of 20.6 per cent of fiscal revenue in that year, so that in this expedient monetary policy had an efficient instrument for the regulation of liquidity. The contraction of

Table 55. Brazil: financing of fiscal deficit
(Millions of cruzeiros)

Year	Deficit	Financing	
		Monetary authorities	General public
1967 . .	−1,225	699	526
1968 . .	−1,227	1,077	150
1969 . .	−756	−1,026	1,782
1970 . .	−738	−833	1,571
1971 . .	−672	−3,368	4,036
1972 . .	−516	−7,766	8,282
1973 . .	295	−6,016	5,721

SOURCE: Central Bank of Brazil.

the money supply assumed considerable proportions from 1971 onwards, largely by virtue of the steady improvement in the fiscal situation.

Thus, the expansion of the means of payment in the period was linked to factors which had a bearing on the aim of economic policy: primary expansion as the result of a balance-of-payments surplus, and secondary expansion, via a monetary multiplier, through an increase in credits to the private sector.

As was previously shown, the national currency counterpart of the inflow of foreign capital was the most dynamic item among the increases in over-all liquidity; so much so, indeed, that as from 1972 deposits of this counterpart in proportions ranging from 25 to 40 per cent of the foreign loans concerned were made compulsory as a means of controlling its inflationary repercussions.

Table 56. Brazil: financial system. Loans to the private sector
(Millions of cruzeiros at current prices)

	1967	*Percentage of total*	*1967, at 1973 prices*	*1970*	*1971*	*1972*	*1973*	*Percentage of total*	*Average annual rate of expansion in real terms, 1967-1973 (percentage)*
Bank system	12,008	69.5	34,991	36,002	52,182	78,180	113,831	48.1	22.0
Commercial banks	8,456	49.0	24,641	23,824	34,121	51,330	73,346	31.0	19.9
Banco do Brasil	3,552	20.5	10,350	12,178	18,061	26,850	40,485	17.1	25.5
Development agencies	1,598	9.3	4,657	3,512	5,226	8,018	11,185	4.7	15.7
Credit and investment companies and investment banks	2,276	13.2	6,632	13,185	20,840	37,297	63,989	27.0	46.0
Credit and investment companies	1,579	9.1	4,601	7,850	11,823	19,790	35,946	15.2	41.0
Investment banks	697	4.1	2,031	5,335	9,017	17,507	28,043	11.8	54.5
House purchase financing system	540	3.1	1,574	7,464	12,558	19,393	30,427	12.9	64.0
Others	844	4.9	2,459	4,364	6,594	10,103	17,148	7.3	38.0
Total	*17,266*	*100.0*	*50,313*	*64,527*	*97,400*	*152,991*	*236,580*	*100.0*	*29.5*

SOURCE: Reports of Central Bank of Brazil.

The other expansionist factor—credits to the private sector—although not so highly dynamic as the inflow of foreign funds, because of its relative importance among the expansionist factors (more than 80 per cent) and its steady annual growth, became the principal source of liquidity. Indeed, the quest for a degree of liquidity compatible with high growth rates led to an expansion of bank credit at the real annual rate of 22 per cent in the period 1967-1973, and in particular, loans granted by the Banco do Brasil, which was more responsive to government policy, increased by 25.5 per cent per annum (see table 56).

Another point to note is the growth of credit extended by the investment banks to finance circulating capital, which in 1973 came to represent 11.8 per cent of total loans to the private sector, with an average rate of expansion of approximately 54.5 per cent. The boom in the operations of the credit and investment companies specializing in loans for consumption purposes is also worthy of comment; by 1973 these associations accounted for 15.2 per cent of total credit to the private sector, with an average growth rate during the period of about 41 per cent in real terms. Lastly, the rapid expansion of the system for financing house purchase is reflected in a share of total loans amounting to roughly 12.9 per cent.[67] In the aggregate, these changes highlight the system's capacity to expand liquidity in the economy, keeping demand brisk and reasonably independent of primary expansion of the means of payment.

As an indispensable complement to this definitely expansionist monetary and credit policy, the Government, as from 1971, initiated open market operations, partly substituting them for the traditional monetary manoeuvres based on rediscounting and compulsory deposits, and thus securing increased flexibility and more effective control of liquidity in the economy.

To this purpose, use was made chiefly of National Treasury Bills of Exchange, securities which were issued weekly, maturing in periods of 91 to 182 days, or monthly, maturing at the end of one year; they were sold chiefly to enterprises and the general public (34 per cent in 1973), and to the commercial banks (25 per cent) (see table 57).

In practice, these operations represented the most important instrument for controlling the money supply in Brazil, and although they were started only recently thay can be credited with 60 per cent of the effect produced by the factors making for contraction of the money supply in 1973. Furthermore, to give an idea of the volume of resources handled in these operations, suffice it to say that in 1973 the Central Bank's National Treasury Bills transactions amounted to 114,600 million cruzeiros in absolute terms, and were equivalent to 30 per cent of the monetary value of the gross domestic product in that year.

If Central Bank operations with the National Treasury Bills are taken together with the Adjustable Bond transactions negotiated mainly for the financing of the fiscal deficit, an idea can be formed of their contractionist impact on the liabilities of the monetary authorities, in comparison with the annual expansion of the liquid money supply (see table 58). As will be noted, in 1972 this impact came to represent an amount equivalent to 40 per cent of the annual expansion of the means of payment. In face of the liberality of credit policy and the accumulation of foreign

[67] The mechanisms for financing consumption and house purchase played a supplementary role in the process of concentration of income, in the sense that they brought the profile of demand into line with the structure of production, allowing the growth of private consumption to outstrip that of disposable personal income.

Table 57. Brazil: principal holders of National Treasury Bills of Exchange
(Balances in millions of cruzeiros)

	1970	*1971*	*1972*	*1973*
Central Bank of Brazil	204	1,810	2,150	5,906
Commercial banks	...	683	2,623	4,381
Official	...	167	729	1,571
Private	...	516	1,894	2,810
Federal Savings Bank	...	...	388	831
Social Integration Programme	–	–	57	104
State savings banks	–	0	1	14
Federal Development Banks	...	140	183	24
Reinsurance Institute of Brazil	–	8	8	12
Private enterprises and general public	496	1,239	4,794	5,911
Total	*700*	*3,880*	*10,204*	*17,400*

SOURCE: Central Bank of Brazil, *Relatório anual 1973.*

Table 58. Brazil: monetary authorities. Impact of National Treasury Adjustable Bonds and Bills of Exchange on monetary liabilities
(Millions of cruzeiros)

	1968	*1969*	*1970*	*1971*	*1972*	*1973*
Contractionist effect	1,307	5,117	13,202	19,802	45,957	96,230
Subscription of National Treasury Adjustable Bonds and Bills of Exchange	1,186	1,962	4,089	11,215	22,531	32,421
Sales of National Treasury Adjustable Bonds and Bills of Exchange by the Central Bank	121	3,155	9,113	8,587	25,426	63,809
Expansionist effect	1,153	4,097	11,863	18,045	40,758	93,823
Redemption of National Treasury Adjustable Bonds and Bills of Exchange	1,116	3,775	9,888	13,001	22,594	37,847
Purchases of National Treasury Adjustable Bonds and Bills of Exchange for the Central Bank portfolio	37	322	1,975	5,044	18,164	55,976
Balance	−154	−1,020	−1,339	−1,757	−7,199	−2,407
Expansion of liquid money supply	6,421	6,998	7,570	11,241	17,156	28,768

SOURCE: Annual reports of Central Bank of Brazil.

reserves, factors which constantly generated powerful inflationary pressures, the importance of the policy of monetary absorption through open-market operations can be readily understood.

From another standpoint, a main objective of monetary policy in the period was the control of the rate of interest, because of its obvious repercussions on the production costs of enterprises. As has already been noted, real interest rates increased continuously from 1964 onwards until they became positive, since the nominal rates decreased at a slower pace than the rate of inflation. This evolution seems to be explained by the rising levels of demand for circulating capital, investment and consumption resources which resulted from the maintenance of high growth rates, and which exerted pressure on the financial resources of the economy, despite the expansionist monetary policy and the reform of the financial system that enabled the degree of liquidity to be increased. This pressure on resources meant that the element of speculation in financial movements was considerable, thus partly accounting for the tenacity with which the real rate of interest withstood reduction.

In these circumstances, the policy of the monetary authorities was mainly directed towards cutting the operational costs of the bank system, through incentives to bank mergers[68] and to the reorganization or closing-down of branches run at a loss. Furthermore, from 1968 onwards commercial banks were allowed to maintain increasing proportions of their compulsory deposits (55 per cent as from 1971) in the form of National Treasury securities (Adjustable Bonds and Bills of Exchange), by which means, concurrently with the creation of remunerative conditions for a large proportion of the compulsory deposits and the improvement of the bank system's rates of return, the market for public debt securities was expanded and stabilized. Nevertheless, these incentives do not seem to have brought about any significant reduction of the real rate of interest.

Such traditional instruments of monetary policy as rediscounting and compulsory rates of reserves, were somewhat cautiously utilized in the period under review, largely owing to the success achieved in open-market operations, by which they were advantageously superseded. Thus, rediscounting was used mainly as an instrument for the sectoral allocation of credits, special rates being established which enabled the banks to refinance credits assigned the production and marketing of agricultural commodities in general and of certain agricultural export products such as coffee, cocoa, tobacco, etc., and to the production of manufactures for export. With regard to compulsory reserves, rates varied very little during the period, fluctuating around 27 per cent for banks operating in the developed parts of the country and 18 per cent for those in the less developed areas, and no anti-inflationary objectives were pursued.

(iii) *Wage policy.* The wage policy formulated

[68] At the end of 1973 there were 87 commercial banks in existence, with a total of 5,540 branches, whereas in 1969 there had been 164 establishments with 5,659 branches. See Central Bank of Brazil, *Relatório, 1973.*

in the three-year period 1964-1966 was maintained during the period under discussion. As already noted, this policy implied the abandonment of the traditional principle of adjusting wages proportionally to the rise in the cost of living, replacing it by a formula which calculated wage adjustments in such a way that during the twelve months for which the new nominal wage was in force, average real wages were equivalent to the average for the preceding 24 months, augmented by a percentage representative of the increase in productivity. This formula, which took into account a projection of future inflation ("inflationary residuum"), was slightly modified as from 1968, when it was established that if the "inflationary residuum" had been underestimated for the previous twelve months, this would be taken into consideration in the calculation of the new nominal wage levels. Although this change brought the evolution of wages closer to that of the cost of living, real wages continued to decrease up to 1972, and thenceforward began to show increases too modest to restore their 1964 purchasing power (see table 59).

The importance of this wage policy formula can be measured not only by its application to the adjustment of the so-called legal minimum wage,[69] but also by its utilization in the adjustment of public sector salaries and in cases of collective wage bargaining, apart from the fact that it constituted the frame of reference for fixing the lowest salary levels in the economy. In other words, wage policy affects a range of remunerations considerably wider than the earnings of recipients of the legal minimum wage.

While it is true that this wage policy was of decisive importance in the gradual reduction of rates of inflation, and enabled the price-wage spiral to be broken, it had significant effects on the allocation of resources in the system. As can easily be understood, it was a powerful factor in the concentration of personal income which, as previously pointed out in the first section of this chapter, was one of the bases for the high growth rates recorded in the period. Wage policy had a depressive effect on basic wages in the economy, favouring a redistribution of income which benefited the upper-middle and upper income strata, in whose hands the dynamic purchasing power of the system lay. Only thus is it comprehensible that real private consumption in the economy was able to expand at an average annual rate of 12.1 per cent during the period 1967-1973,[70] just at a time when the real minimum wage—the standard of pay for a large proportion of the economically active population—was diminishing.

(iv) *Price policy.* The price control policy applied during the period may be regarded as a necessary complement of an expansionist monetary policy and a fiscal policy compatible with high rates of growth of the product. In this connexion, attempts were made to use mechanisms which without blocking prices would be capable of controlling them, and preventing increases that would anticipate inflation or substantially boost profits. In contrast, the aim pursued was that rising prices should reflect real increases in costs. Thus, price policy was applied to agricultural and industrial products and to the tertiary sector, with varying results.

For the agricultural sector a twofold objective was pursued. In the first place, price policy sought to protect the sector's income through the fixing of minimum guaranteed producer's prices; secondly, the intention was to keep agricultural

[69] Estimates prepared by the Ministry of Labour and Social Security show that, in 1968, 51 per cent of wage-earners in Brazil were earning less than 1.23 times the legal minimum wage (see P. Auberger, op. cit., p. 28).

[70] Primary data taken from the *Economic Survey of Latin America*, 1968 and 1973.

Table 59. Brazil: evolution of legal minimum wage in the State of Guanabara

Year	*Percentage variation in minimum wage*	*Cost of living in Guanabara*	*Index of evolution of real minimum wage*
1964	91.7	91.5	105
1965	54.0	65.9	100
1966	30.6	41.3	93
1967	25.3	30.6	89
1968	21.6	22.3	89
1969	19.2	22.1	87
1970	20.0	22.7	85
1971	20.6	20.2	85
1972	19.2	16.5	88
1973	16.1	12.7	89

SOURCE: Central Bank, and Fundação Getúlio Vargas, *Conjuntura Econômica.*

prices within a margin compatible with the control of inflation, and prevent them from following international trends, since this might have represented a serious internal inflationary pressure.

With the object of maintaining certain minimum prices, credit policy was directed towards the continued extension of loans by the Banco do Brasil for financing the storage and purchase of products; this constituted a factor of monetary expansion in the economy, but did not unduly affect the placements of the monetary authorities.

As regards general agricultural price policy, the principal measures were those applied to exports of certain commodities, such as coffee, cocoa and beef, and the establishment of quantitative export restrictions, which affected, *inter alia*, cotton, maize, sisal hemp, soya beans, beef, cocoa, etc. The aim of these measures was to prevent internal agricultural prices from rising in consequence of the development of export lines at prices more remunerative than those obtainable in the domestic market (see table 60).

As regards prices of industrial goods, a succession of different types of control was established in the period, reflecting a somewhat wavering policy in respect of the use of various instruments. The first measure adopted was the application of a system of incentives to enterprises that kept their prices within the margins fixed by the Government, guaranteeing them rediscount facilities in respect of their Central Bank credits, supplementary credits from the Banco do Brasil, lengthening of time-limits for tax payment, etc. This system was subsequently replaced by another of automatic price adjustments, based on the index of wholesale prices, at intervals of three months. Some months later the type of control was changed again, and as from 1968 adjustments of the prices charged by enterprises were determined by equivalent increases in costs, subject to prior authorization by the Inter-Ministerial Price Commission (IPC). This control is at present applied to about 4,500 industrial enterprises. Failure to comply with the regulations laid down by the IPC may incur sanctions such as the suppression of Banco do Brasil credits, loss of Central Bank rediscount rights, or, in extreme cases, official intervention in the running of the enterprise. Generally speaking, control of industrial prices does not seem to have had unfavourable repercussions on the sector, to judge by the rates of return of industrial enterprises, which have been rising since 1967 (see table 61).

The controls imposed on other domestic prices, as in the commerce and services sectors, for example, were of a somewhat piecemeal character, and had no significant repercussions on anti-inflationary policy.

(v) *Handling of the exchange rate.* From another point of view, a feature worth noting in over-all price policy during the period is the establishment, as from 1968, of a flexible exchange rate system, one of the basic instruments of the effort to neutralize the effects of inflation.

Up to 1968, it had been the practice of the monetary authorities to move the exchange rate closer to more realistic levels, at intervals of 10 to 14 months, a procedure which was clearly disadvantageous in respect of the deterioration of real export earnings, and, furthermore, favoured speculative movements of capital.

From 1968 onwards, Brazil's economic development became outward-directed, and depended more and more upon a growing inflow of capital, a vigorous expansion of exports and a rapid increase in imports. In these circumstances, the policy pursued in fixing the exchange rate needed to be more flexible and realistic. Thus, in 1968 the system of periodic devaluations was introduced as a necessity imposed by the country's

Table 60. Brazil: percentage variations in prices of agricultural products

	1970	*1971*	*1972*	*1973*	*1974*
Index of wholesale prices of total supply					
Industrial products	16.8	17.5	16.0	14.7	27.9[a]
Agricultural products	28.7	25.3	22.3	19.0	25.1[a]
Index of export prices					
Sugar	7.6	9.2	60.6	2.0	156.6[b]
Soya beans	−0.8	21.8	8.7	113.2	−10.7[b]
Cotton	0.8	34.2	9.5	16.7	−36.7[b]
Coffee	36.1	−23.5	26.5	22.8	14.5[b]
Beef	...	56.4	−1.9	41.6	...

SOURCE: Fundação Getúlio Vargas, *Conjuntura Econômica.*
[a] Up to September 1974.
[b] Up to July 1974.

Table 61. Brazil: rates of return of industrial enterprises, by branches of activity
(Percentages)

Branch of activity	*1967*	*1968*	*1970*	*1972*
Consumer goods (textiles, food, beverages, tobacco, paper, etc.)	14.9	15.6	17.7	16.5
Intermediate goods (non-metallic minerals, products of metallurgical and chemical industries, etc.)	13.5	14.7	17.5	17.5
Capital goods (products of the metal manufactures and machinery industry, electrical applicances, transport equipment, etc.)	9.4	16.9	16.1	20.8
Miscellaneous products	7.9	26.5	9.1	16.1
Total	*12.6*	*16.0*	*16.5*	*17.8*

SOURCE: P. Auberger, op. cit., on the basis of estimates prepared by the Fundação Getúlio Vargas in respect of the 500 largest enterprises in Brazil.

style of development. In essence, the new system was put into practice in the form of frequent small adjustments in the exchange rate, from seven to ten times a year on an average, the devaluations ranging from 0.5 per cent to 2.5 per cent, (see table 62), so as to make for an adjustment between the rate of increase of domestic prices and the trends followed by external inflation. This system was complementary to the policy of incentives to exports and afforded protection for real export earnings, acting as a basic factor in their expansion. Moreover, the fact that devaluations took place so frequently and at intervals of unknown length discouraged speculative movements of capital. In addition, these periodic devaluations played an important part in the policy of tapping foreign resources, since they meant that capital could be repatriated at a real value comparable to that of the original contribution. With regard to imports, the periodic adjustability of the exchange rate obviated the explosiveness of violent devaluations, mitigating their psychological effects and helping the economy to adapt itself better to the new costs.

(vi) *Monetary adjustability*. As a second mechanism for neutralizing the effects of inflation, ample use was made of the monetary adjustability instituted in 1964. Its application was a cornerstone of Brazil's entire financial policy, and, in particular, paradoxical as it may seem, of anti-inflationary policy too, since it gradually covered a high proportion of transactions in the Brazilian economy. It meant that instruments of indebtedness could be utilized in an inflationary situation, by virtue of the constant updating of liabilities.

Adjustability, which at first covered only the National Treasury's Adjustable Bonds, progressively spread to public utility tariffs, rentals, mortgages, balance-sheets of enterprises, loans, taxes, etc., reducing the volume of speculative operations and consequently weakening one of the causes of inflationary pressures, and safeguarding the real value of savings. At the same time, as was previously shown, it constituted an efficient instrument for regulating the liquidity of the economy, especially where the issue of adjustable securities was concerned (the National Treasury's Adjustable Bonds and Bills of Exchange).

It must be borne in mind, however, that although periodic devaluations and monetary adjustability mitigated some of the effects of inflation and permitted a sort of compromise with it, in a certain sense they also tended to institutionalize it. The mechanism of adjustability exercised a pervasive influence on the whole behaviour of the agents of the economic process, encouraging a propensity to expect price increases which came to be taken as a matter of course.

In inflationary situations, in which producers and distributors tend to defer their sales, while consumers seek to spend their earnings in advance, imbalances between supply and demand are generated, and obviously exert pressure on prices. Tendencies to go in for stockpiling and borrowing in national currency likewise undermine the financial savings of individuals and enterprises.

The potency of the propagating effects of the institutionalization of inflation seems to be in inverse ratio to the virulence of the disease. In cases of galloping inflation, with annual rates of over 30 to 40 per cent, deeper-rooted causes exist which detract from the relative importance of these economically superficial self-propagating factors. On the other hand, when the rate of inflation has been reduced to 10 or 15 per cent per annum, the inertia caused by the adjustability mechanism may become a serious hindrance to the combating of inflation.

Table 62. Brazil: variation in exchange rates between 1968 and August 1974

Date	Period (number of days)	Dollar purchasing power of cruzeiros	Annual percentage variation	
			Exchange rate	Prices
4-1-68	236	3,200		
27-8-68	28	3,630		
24-9-68	56	3,675		
19-11-68	20	3,745		
9-12-68	57	3,805		
31-12-68		3,805	18.9	25.5
28-1-72	47	5,750		
16-3-72	53	5,810		
8-5-72	68	5,880		
14-7-72	53	5,930		
5-9-72	42	5,990		
17-10-72	36	6,060		
22-11-72	23	6,130		
15-12-72	61	6,180		
31-12-72		6,180	10.4	15.5
14-2-73	69	5,995		
24-4-73	76	6,060		
9-7-73	73	6,090		
20-9-73	85	6,120		
14-12-73	48	6,180		
31-12-73		6,180	0.0	15.5
31-1-74	20	6,300		
20-2-74	55	6,415		
16-4-74	50	6,515		
5-6-74	20	6,640		
25-6-74	14	6,775		
9-7-74	36	6,845		
15-8-74	34	6,980	12.94	25.6

SOURCE: Central Bank of Brazil.

D. THE RECRUDESCENCE OF INFLATION (1974)

After almost a decade in which considerable control over inflationary pressures was achieved, in 1974 the upward trend of prices regained momentum; by the end of the year the rate of increase had reached 34.6 per cent, as against 15.5 per cent in the two-year period 1972-1973.

Basically, as from the second half of 1973, the resurgence of the inflationary process was linked in two ways to the behaviour of the external sector. In the first place, the economy was affected by the repercussions of the world petroleum crisis and the rise in prices of raw materials, including, of course, the raw materials exported by Brazil; secondly, the increase in the prices of imports struck the Brazilian economy a particularly heavy blow, in view of its sensitiveness to the vicissitudes of the external sector.

(a) *Sources of inflationary pressures*

In analysing the causes of the recent acceleration of the rate of inflation in Brazil, certain trends in the economy during 1973 must be taken into account.

To begin with, it is of interest to note the high balance-of-payments surplus in 1973, which gave rise to a marked increase in foreign currency assets (2,300 million dollars), so that pressure was exerted on the expansion of the domestic monetary supply. This phenomenon had been in evidence since 1972, in which year the surplus had amounted to 2,400 million dollars (see table 63). These surpluses were primarily attributable to the abundant inflow of foreign capital in the form of medium and long-term loans. Although in August 1973 such inflows of funds were to some extent checked by the application of a 40 per cent rate of retention to the cruzeiro counterpart of foreign

Table 63. Brazil: balance of payments
(Millions of dollars)

	1970	1971	1972	1973
I. *Trade balance*	232	−363	−244	182
Exports FOB	2,739	2,882	3,991	6,198
Imports FOB	2,507	−3,245	−4,235	−6,016
II. *Services*	−462	−538	−730	−846
Income	328	398	424	569
Expenditure	−790	−936	−1,154	−1,415
III. *Goods and services* (I + II)	−230	−901	−974	−664
IV. *Returns on capital*	−353	−420	−520	−662
Profits and dividends	−119	−118	−161	−191
Interest	−234	−302	−359	−471
V. *Transfers*	21	14	5	36
VI. *Balance on current account* (III + IV + V)	−562	−1,307	−1,489	−1,290
VII. *Liquid movements of capital*	1,015	1,846	3,492	3,680
Investment	108	168	318	900
Loans and financing (medium- and long-term)	767	1,187	3,098	2,937
Loans (short-term)	77	486	21	−171
Others	63	5	55	14
VIII. *Errors and omissions*	92	−9	436	−63
IX. *Balance-of-payments position*	545	530	2,439	2,327
Arrears and trade credits	–	–	–	–
International Monetary Fund	−177	−47	−70	−33
Assets minus short-term liabilities	−378	−483	−2,369	−2,294

SOURCE: Central Bank of Brazil.

loans, the amount remained at practically the same level as in 1972, i.e., about 3,000 million dollars. This was the main factor making for the expansion of the means of payment in 1973.

The growth rate of credit to the private sector—another important factor of monetary expansion—was 46.7 per cent in 1973, and 52 per cent in the case of credit granted by the Banco do Brasil.

These two principal lines of expansion led to a 47 per cent increase in the means of payment in 1973, as against one of 38.3 per cent in the preceding year. This expansion, which was much greater than had been envisaged by monetary policy, proved incompatible with the programmed rate of inflation. Thus, pressure on price levels began to make itself felt as early as the second half of 1973, and became more marked in the early months of 1974.[71]

By the second half of 1973, there was already evidence of speculation in immovable assets, a sharp increase in the volume of imports, shortages of raw materials and basic inputs such as steel, iron and chemical products, speculative stockpiling and other symptoms of renewed impetus in total demand in the economic system.

The second source of inflationary pressures in the recent period was associated with the so-called raw materials crisis and with the development of world inflation; both these generated disequilibria in the economy which became major causes of the inflationary trend of prices.

To begin with, the considerable increases in import products are noteworthy. If January-June 1974 is used as a reference period, it may be seen that imports increased in value by 122.5 per cent compared with the previous year, while the increase in quantity was only 14.7 per cent (see table 64). In the case of basic commodities which include imports of petroleum and wheat, the value of imports increased by 225 per cent.

It is important to observe, however, that the share of basic commodities in the total value of imports was only 32 per cent during this period, and thus does not explain the total increase in

[71] The rate of inflation programmed for 1973 was 12 per cent, whereas in fact it was 15.5 per cent. In the preparation of the over-all price index, however, artificially fixed prices were utilized, which were much lower than the real market prices, so that the rate of inflation in that year was underestimated.

Table 64. Brazil: structure of imports in the first half of 1973 and 1974

	Quantities (thousands of tons)			*Value (millions of dollars)*		
	1973	*1974*	*Percentage*	*1973*	*1974*	*Percentage*
Basic commodities	18,999.8	19,806.5	4.3	548.9	1,784.7	225.1
Processed products	3,445.5	5,921.2	71.9	1,930.4	3,741.7	93.8
Semi-manufactures	3,209.2	5,579.4	73.9	855.1	2,177.2	154.6
Manufactures	236.7	341.7	44.6	1,075.3	1,564.2	45.5
Special transactions	6.2	16.5	167.3	21.2	38.4	81.0
General total	*22,451.5*	*25,744.2*	*14.7*	*2,500.7*	*5,564.6*	*122.5*

SOURCE: Fundação Getúlio Vargas, *Conjuntura Econômica*, October 1974.

growth of expenditure on imports. In fact, imports of semi-manufactured and manufactured products played a decisive role, with an increase in quantity of the order of 74 per cent in the case of semi-manufactures and 44 per cent for manufactures; price increases also affected them, especially in the case of semi-manufactures. These imports are to be explained by the large-scale stockpiling of raw materials, as a result of the expectations created as regards future trends in prices in world trade and the possibilities of profit speculation. Still in the context of imports, another source of inflationary pressures should be mentioned, in the form of the upward trend in prices of similar goods produced locally. The lack of consistency between domestic and external prices meant that some local industrial products, which benefited from customs protection, came to have prices lower than those of similar imported goods. When local production proved unable to cope with the entire demand of the domestic market, which was the case in the majority of instances, the price of locally-produced goods tended to increase to the price-levels of imported goods.

From another viewpoint, the increase in international prices also contributed to inflation through the increase in the prices of some products exported by Brazil. In fact, products whose external prices underwent rapid increases (see table 65) shifted part of their supply from the local to the external market, causing problems in domestic supply and a consequent rise in prices. This was the case of meat, soya beans and cotton, among the most obvious instances, and it became necessary to adopt a series of special measures, such as export quotas, the establishment of fixed proportions of sales to external and internal markets, the fixing of domestic prices, the introduction of export rates, etc. In the majority of cases, however, it was impossible to avoid closing the gap between external and domestic market prices, and this gave rise to pressures to push up prices, which made themselves felt late in 1973 and in the first few months of 1974.

Lastly, the role of the neutralizer elements of inflation should be stressed, as for example, currency readjustments, the use of which is generalized in the economy of Brazil. As may be understood, the monetary readjustments, which are

Table 65. Brazil: international prices of export products
(*Dollars*)

Product	*Unit*	*1970*	*1973*	*January/ February 1974*
Beef	100 pounds	41.32	63.67	...
Cocoa	100 pounds	32.25	61.26	67.05
Coffee	100 pounds	53.94	66.53	69.60
Cotton	100 pounds	25.10	56.10	85.00
Sisal	100 pounds	7.30	24.40	34.00
Soya beans	Bushel	2.70	6.00	6.14
Sugar	100 pounds	8.09	10.25	15.01
Wool	100 pounds	27.20	95.90	101.80
Iron ore	Tons	7.47	8.07	9.09

SOURCE: Fundação Getúlio Vargas, *Conjuntura Econômica*, October 1974.

always *a posteriori*, tend to increase the effects of inflation when this is in the ascendent, exactly as in the case of the recent evolution of inflation in Brazil.

As a result of these major factors, the rate of inflation jumped up from 15.5 per cent in the period 1972-1973 to 34.6 per cent in 1974. Actually, 1973 had the advantage of some arbitrary elements in the economic policy which made it possible to put off until 1974 part of the inflationary pressures which made themselves felt, particularly in the second half of the year. Examples of such measures may be found in the subsidies, the fixed prices, and the policy of the fixed exchange rate adopted in the second half of the year. As may be seen from table 66, the exchange rate was adjusted by only 1.6 per cent between June and December, and the policy of periodic devaluations was relaxed in an endeavour to postpone the domestic effects of the increases in prices of imported products.

Naturally, these measures contributed to a later increase in prices in 1974; a particularly active inflationary trend was recorded in the first four months of the year, with rates of growth of the general price index increasing from 2.9 per cent in January to 5.1 per cent in the month of April, and later dropping to 2 per cent in July, with a cumulative growth of 22.6 per cent in the first half of the year.[72] However, once the months of readjustment and absorption of the pressures of the previous year were over, the rate of inflation slowed down, and the year came to an end with an increase of 34.6 per cent in the general price index.

(b) *Anti-inflationary policy in 1974*

In the context of the growth of inflation, the policy introduced during 1974 may be considered as an emergency policy, aimed at dealing rapidly with an economic situation considered to be of a temporary nature. This, however, did not mean the abandonment of the main lines of policy applied from 1967. Although inflation showed upward growth rates, the main objective of maintaining high rates of growth was not lost sight of, and continued to delimit the anti-inflationary policy's area of manoeuvre.

(i) *Money and credit policy.* Money and credit policy during the period aimed at the implementation of a financial budget which would bring down the growth of the means of payment in the course of the year by 35 per cent; this was considered consistent with a high rate of growth of the product and the reduction of the rate of inflation.

The implementation of such a budget, however, pursued rather an irregular course during the year. During the first half of the year when the main effects of inflation sank in, money supply was rigidly controlled. Table 67 shows that the means of payment increased by 13.6 per cent during the period January-July while loans to the private sector increased by 23.1 per cent. If it is considered that during the first half of the year the rate of growth of prices was of the order of 22.6 per cent, it will be understood that the economy found itself involved in a current liquidity crisis.

During the second half of the year, once the main impact of inflation was over, monetary policy was redirected towards a more rapid growth of money supply so as to enable the economy to function in a more dynamic form. The means of payment thus increased by 22.9 per cent during the period July to December while loans to the private sector recorded a growth of 15.4 per cent in the four-month period between July and October. This helped in part to alleviate the problems of liquidity in the economy.

As a result of the strict application of the monetary policy, the budget was implemented with only slight variation from that programmed, and showed a total annual growth in the means of payment of around 34 per cent. This forced the Government to adopt a series of complementary monetary measures to cope with the strong pressures and constraints of the money supply.

Among the factors which most inhibited the levels of the economy's liquidity were the performance of the Treasury and the evolution of the external sector.

An examination of the Treasury's cash movement shows the reduction in the money supply throughout the year. Table 68 shows that with the exception of the months of July, August, October and December, the Treasury's cash movement constituted a major factor in reducing the money

[72] The index refers to the basket of goods which make up domestic supply.

Table 66. Brazil: price of the dollar, 1973
(*Cruzeiros*)

January	6,215
February	6,116
March	6,030
April	6,046
May	6,100
June	6,100
July	6,122
August	6,130
September	6,140
October	6,160
November	6,160
December	6,195

SOURCE: Fundação Getúlio Vargas, *Conjuntura Econômica*, August, 1974.

Table 67. Brazil: monetary distribution, 1974
(*Millions of cruzeiros*)

	Paper money in the hands of public	*Sight deposits in commercial banks*	*Sight deposits in the Banco do Brasil*	*Means of payments*	*Loans to the private sector*		
					Commercial banks	*Banco do Brasil*	*Total*
January	15,815	56,213	14,873	86,901	74,164	37,824	111,988
February	16,086	58,729	16,000	90,815	76,729	38,864	115,593
March	16,317	60,489	17,051	93,857	78,861	40,626	119,487
April	16,575	60,367	18,068	95,010	80,420	41,922	122,342
May	17,160	60,310	19,166	96,636	83,475	43,950	127,425
June	17,192	64,783	18,910	100,885	86,570	47,866	134,436
July	16,712	62,670	19,301	98,683	88,864	48,959	137,823
August	17,653	64,810	21,242	103,705	92,119	50,392	142,511
September	17,109	66,472	19,993	103,574	95,539	53,439	148,978
October	17,399	67,038	21,806	106,243	98,705	56,419	155,124
November	18,984	71,425	29,950	113,359	101,666	...	...
December	20,798	79,788	20,681	121,267	106,910	...	...
December 1973				90,490			

SOURCE: Preliminary estimates of the Central Bank of Brazil and the Fundação Getúlio Vargas.

supply, especially in the months of February and September, when major increases were recorded, and the economy's liquidity problems were aggravated. This surplus basically derived from Treasury income which increased by approximately 41 per cent during the period January-October 1974, compared with the same period in 1973. This was essentially due to the increase in earnings from the tax on manufactures, which was *ad valorem* duty and benefited from the increasing rates of inflation. Public expenditure increased by 33.5 per cent during the period January-October, as no policies were applied to restrict spending (see table 69).

Table 68. Brazil: Treasury cash movements, 1974[a]
(*Millions of cruzeiros*)

Month	*Value*
January	277.6
February	2,870.1
March	3,150.9
April	3,703.5
May	4,103.1
June	4,899.3
July	4,616.4
August	3,541.0
September	5,343.9
October	4,655.0
November	4,998.0
December	2,700.0

SOURCE: Fundação Getúlio Vargas, *Conjuntura Econômica*, and Central Bank of Brazil.
[a] Cumulative flows in the course of the year up to the month considered.

Table 69. Brazil: national Treasury, fiscal budget
(*Millions of cruzeiros*)

	1973[a]	*1974*[a]	*Percentage variation*
Income	41,576.4	58,602.1	41.0
Expenditure	40,398.6	53,947.1	33.5
Surplus	1,177.8	4,655.0	295.2

SOURCE: Fundação Getúlio Vargas, *Conjuntura Econômica*, December 1974.
[a] January-October.

The balance of payments in 1974 reflected a deficit of 1,400 million dollars, basically as a result of the vigorous increase in the value of imports which accounted for a not insignificant decrease in liquidity. In order to counter this, and guarantee that the level of liquidity programmed would be met, the Government applied a series of emergency measures in the second half of the year which increased the supply of money in the economy.

From then on, open market operations were intensified, but in the reverse of the traditional direction; this time the aim was to pump money into the system through purchases of Treasury Bills by the Central Bank and the reduction of the quantities on sale to the public.

As table 70 shows, the monetary balances of operations with Treasury Bills increased up to the

Table 70. Brazil: Treasury Bills, 1974[a]
(Millions of cruzeiros)

Period	*Treasury Bills*
January	16,348
February	15,988
March	15,778
April	16,636
May	18,249
June	19,801
July	19,653
August	18,050
September	16,200
October	14,101
November	13,500[b]
December	15,950[b]

SOURCE: Central Bank of Brazil.
[a] End-of-period balances.
[b] Preliminary estimates.

month of June, with a moderate decrease in the means of payment. However, as from July, open market operations reversed their trend and began to supply the economy with liquidity, with a marked reduction in the money value of the operations.

In addition, subscriptions to Adjustable Treasury Bonds were suspended, thus avoiding a further flow of resources into the Treasury.

The credit policy sought to increase liquidity by reducing the compulsory loans of the commercial banks, raising the maximum limits for agricultural credit generated by the Banco do Brasil, creating a special Central Bank credit line of approximately 2,000 million cruzeiros for the financial operations of the commercial sector, and establishing another special Banco do Brasil credit line for the industrial sector, of 1,300 million cruzeiros.

Some fiscal policy measures were also introduced, with temporary reductions of the tax on manufactures, affecting electrical domestic appliances, furniture and the textile industry, and the postponement for one month of collections of payments of this tax for the majority of manufactures.

With this group of special measures it was possible to rise above the economy's liquidity crisis and implement an anti-inflationary financial budget, bounded by considerably stricter limits than the budgets of earlier years.

(ii) *Price policy.* In 1974 the price policy played a rather more flexible and important role than in previous years.

In the face of rising inflation the policy to control prices gained in importance as one of the main instruments for restraining the expectations of price increase which came to exist in the economy, especially during the first half of the year.

Control began to be applied by the Inter-Ministerial Prices Commission (IPC) and by the National Office for the Superintendence of Supply (SUNAB) as from the second quarter of the year, when a more stable level of prices was reached. During the first quarter, the Government was forced to readjust by considerable amounts a group of prices which had been frozen in 1973, in an endeavour to delay the effects of the increases.

In effect, the type of price control practised by the IPC in particular (industrial prices) was similar to the wage policy formula[73] applied as from 1968. The adjustment was based on the following principles: in the first place, it required the enterprises to absorb part of the rise in the cost of inputs by increasing productivity; secondly, the estimates of the increase in the cost of inputs was not made by comparing two adjustment dates, but was based on their average value during the period in which old and new prices were in force; this meant the establishment of *a posteriori* correction measures in the event of sizable underestimates. This provided an extra shock-absorber in prices, always provided that the rate of inflation anticipated was less than that observed in the past.

In addition, the prices of goods produced by State enterprises were the object of direct restrictions, and adjustments exceeding 15 per cent in the course of the whole year were prohibited.

The price controls used were sufficiently effective to disappoint expectations of an upswing in prices and to enable inflation to be slowed in the second half of the year. However, their radius of action continues to be limited to industrial and agricultural prices in particular, with a fairly moderate impact on the marketing of the products.

(iii) *Wage policy.* In 1974 the same wage policy that had existed in Brazil since 1965 was maintained. A change was introduced, however, in the formula for calculating the adjustments which had been applied since 1968. Since then, the mode of calculation had endeavoured to represent the real average wage of the 24 months previous to the adjustment, taking into consideration the forceast of the future rate of inflation and the correction of the same to allow for underestimation, including in it 4 per cent to account for the increase in productivity. The change introduced in 1974 established that the calculation of the adjustment should represent the real average wage of the 12 months previous to it, maintaining the same

[73] See page 132.

formula in other respects. The result of this was a closer approach of trends in wages to increases in the cost of living.

The adjustment of wages took place in two stages, with a special increase of 10 per cent as from 1 December 1974, and the final adjustment of around 43 per cent as from 1 January 1975 (less the emergency 10 per cent).

The new adjustment based on the new calculation formula introduced in 1974 is the largest wage increase which the Government has permitted in the last 10 years, during which time wage policy played an important role in the struggle against inflation.

(iv) *External sector policy.* The evolution of the external sector in 1974 was characterized by a deficit of 1,400 million dollars in the balance of payments. Basically, this disequilibrium originated in the balance of current transactions, which was a heavy deficit that could not be offset by the inflow of capital (see table 71).

From the point of view of the anti-inflationary policy the evolution of the external sector acquired importance in three main aspects. In the first place, as has already been said, this policy tightened up the supply of the means of payment of the system—the opposite of what happened in 1972 and 1973, when it became one of the most important factors in monetary growth. Although in one sense this was of assistance in implementing a strict financial budget, in another it caused difficulties because it brought down the level of liquidity in the economy, especially because of the existence of an unexpectedly large deficit at the beginning of the year.

Secondly, the rather slow inflow of external resources in the form of loans and financing made itself felt particularly in the first half of the year. As a result, large-scale enterprises, particularly those bound up with foreign capital, brought pressure to bear on domestic supplies of credit, jeopardizing in particular small and medium-scale enterprises which were unable to compete successfully for access to the system's sources of finance. A policy which would attract more foreign capital was thus required, together with the abandonment of the restrictions imposed in 1973, so as to cover the deficit in current transactions and at the same time expand external sources of financing. This was the reason for the elimination at the beginning of the year of the retention of 40 per cent of the cruzeiro counterpart of external loans, while the minimum duration for foreign capital was reduced in September from 10 to 5 years. In October, completing the group of the main measures for attracting foreign capital, the tax on remittances of interest abroad was reduced from 25 to 5 per cent. Although the net inflow of capital was inadequate to cover the deficit in current transactions, it amounted to 5,600 million dollars, which represented an increase of 52 per cent compared with the level for 1973.

Lastly, with reference to the policy of fixing the exchange rate, Brazil returned to the tradition of periodical devaluations which had been abandoned in 1973, and the economy was adjusted to rates of inflation which showed an upward trend. As may be seen from table 72, the exchange rate was devalued by 19 per cent in the course of the year and was forced to adapt to an adverse trend in the balance of payments; a level of growth consistent with the emergency anti-inflationary policy applied during the year was, however, maintained, the devaluation of the exchange rate being substantially less than the increase in domestic prices.

Table 71. Brazil: balance of payments, 1974
(*Millions of dollars*)

Trade balance	
Exports	7,700
Imports	12,400
Liquid balance	−4,700
Services	*−2,300*
Current transactions	*−7,000*
Capital	
Direct investment	1,000
Loans and finance	6,400
Amortization payments	−1,800
Liquid balance	5,600
Deficit	*−1,400*

SOURCE: Preliminary estimates of the Central Bank of Brazil.

Table 72. Brazil: price of the dollar, 1974
(*Cruzeiros*)

December 1973	6,195
January	6,224
February	6,381
March	6,455
April	6,505
May	6,555
June	6,690
July	6,867
August	6,959
September	7,068
October	7,142
November	7,262
December	7,371

SOURCE: Fundação Getúlio Vargas, *Conjuntura Econômica.*

3. COLOMBIA

A. INTRODUCTORY NOTE

This study covers the period from 1971 to 1974 inclusive.

The period starts in 1971 because that year marked a spurt in the inflationary process, after several years in which price movements had been moderate. For the same reason, from that date onwards the government authorities attached increasing priority to the implementation of a large group of stabilization measures.

In the years 1972-1974, inflation accelerated owing to the effects of the rapid expansion of the external sector on demand and prices, which necessitated the adoption of new measures aimed at mitigating the growing inflationary pressures that were making themselves felt.

In the second half of 1974, with the change in the administration, important modifications were introduced in the anti-inflationary policy in force. For many purposes, therefore, the analysis made in this study has a unified approach only in so far as it relates to the period up to mid-1974.

B. MAIN FEATURES OF THE TREND OF THE COLOMBIAN ECONOMY

During the period 1971-1974, Colombia's economy was marked by the influence of a number of significant external and internal factors of a general nature, on the trends examined below.

In the first place, and particularly in the three years 1972-1974, the country was strongly affected by the demand and price levels deriving from the rapid and persistent expansion of the economy and of world trade. At the same time, and for a number of reasons that will be analysed below, the country's productive system demonstrated a fair degree of flexibility in its reaction to external incentives.

Secondly, the combination of two mutually complementary factors was particularly important from the domestic standpoint. On the one hand, the management of government functions in almost the whole period under consideration (up to August 1974) was in the hands of the same political administration. On the other, a National Development Plan—generally known as "The four strategies"[74]—was introduced which defined and gave consistency to the economic policy measures applied during the three-year period.

[74] These four strategies relate to: (*a*) urban development and housing; (*b*) rural incomes and agricultural productivity; (*c*) exports; and (*d*) distribution of income.

The significance of these external and internal factors cannot be underestimated since it was they that gave the economic policy of the period its relative unity, consistency and homogeneity.

1. *Growth trends*

In the early 1970s, the Colombian economy grew more rapidly than during the period 1965-1970 and during the 1950s and 1960s in general. The average growth rate of the gross domestic product, for example, was 6.5 per cent in 1970-1974, compared with 5.8 per cent in 1965-1970 (see table 73).

ECLA estimates indicate that, between 1970 and 1974, Colombia's *per capita* gross domestic product rose from about 509 dollars to 578 dollars (at constant 1970 prices).[75] This growth rate (3.2 per cent per year) is about 30 per cent higher than that of the period 1965-1970 and twice that of the 1960s; it therefore represents a substantial change in the country's rate of economic expansion. At the same time, the growth of the population has shown little change, remaining at about 3.2 per cent annually since the 1950s—a fairly high figure in Latin American terms.[76] At the end of 1974, the total population of the country was about 24 million.

(a) *Total supply and demand*

The table illustrating total supply and demand shows that this somewhat faster growth rate coincides with a fairly rapid expansion of exports which, at constant prices, registered an average annual increase of 8.9 per cent during the period 1970-1974, as opposed to 5.2 per cent in 1965-1970. As will be seen below, the export figures expressed in dollars at current prices show more clearly the fundamental change that took place from 1970 onwards.

Another striking feature of total demand was the slight increase in the rate of investment from 1970 onwards. In terms of the gross domestic product, the gross domestic investment coefficient rose from 19 per cent around 1965 to 20.4 per

[75] During the same period, the average *per capita* gross domestic product for Latin America as a whole (19 countries) is estimated to have risen from 640 to 743 dollars at 1970 prices.

[76] It should be noted that the targets set in the International Development Strategy for the variables referred to are: about 3.5 per cent annually for the *per capita* gross product and at least 6 per cent annually for the over-all product, allowing for an annual demographic growth rate of 2.5 per cent. Consequently, the figures for Colombia during the period 1971-1974 are close to the established targets, save in respect of the increase in population.

Table 73. Colombia: total supply and demand
(*Millions of pesos at 1970 prices*)

	1970	Annual growth rate (percentages)						
		1965-1970	1970-1974	1970	1971	1972	1973	1974[a]
Total supply	151,230.4	6.3	5.9	8.2	5.5	4.6	6.8	6.5
Gross domestic product (at market prices)	130,590.8	5.8	6.5	6.6	5.5	6.8	7.5	6.1
Imports	20,639.6	10.6	2.1	18.7	5.4	-8.6	3.3	9.5
Total demand	151,230.4	6.3	5.9	8.2	5.5	4.6	6.8	6.5
Exports	18,515.8	5.2	8.9	-2.5	5.1	13.4	9.5	7.6
Gross domestic investment	28,130.3	8.1	5.6	15.2	9.7	-0.9	6.1	11.2
Gross fixed investment	25,850.3	9.0	6.9	13.1	6.9	1.8	12.5	10.4
Total consumtpion	104,584.3	6.1	5.4	8.6	4.4	4.6	6.4	5.1
General government	9,961.6	6.9	5.5	14.0	23.6	-14.6	5.8	4.6
Private	94,622.7	6.0	5.4	8.0	2.4	7.0	6.5	5.1

SOURCE: ECLA, on the basis of official statistics.
[a] Preliminary figures.

cent in 1973-1974; capital formation, however, continued at much the same level as in the first part of the 1960s, when the coefficient was close to 21 per cent (see table 74).[77] Moreover, this increase bears no relation to the increase in total public investment during the same period; according to the calculations of the World Bank, the coefficient for the latter rose from under 7 per cent of the gross domestic product in 1965 to approximately 12 per cent during the three years 1971-1973.[78]

[77] See ECLA, *Tendencias y estructuras de la economía de Colombia en el último decenio* (E/CN.12/915), 8 September 1971, pp. 21 and 22.
[78] IBRD, *Economic position and prospects of Colombia*, Report No. 138-CO (15 May 1973), p. 17.

Total consumption and its components fluctuated during the period 1971-1973, as a result of which their average growth rates, and especially that of consumption of the general government, were lower than in 1965-1970.

(b) *The sectoral structure of the product and employment*

An analysis of the sectoral structure of the gross domestic product during 1971-1974 shows that the acceleration of the over-all growth rate coincided with, as was a consequence of, the fairly balanced development of the various productive sectors, with the sole exception of mining and quarrying whose share of the product declined. Consequently, although sectoral growth rates

Table 74. Colombia: structure of total supply and demand
(*Percentages*)

	1965	Average 1969-1970	1970	1973	1974[a]
Total supply	112.6	115.0	115.8	113.0	113.4
Gross domestic product (at market prices)	100.0	100.0	100.0	100.0	100.0
Imports	12.6	15.0	15.8	13.0	13.4
Total demand	112.6	115.0	115.8	113.0	113.4
Exports	14.6	14.8	14.2	15.3	15.5
Gross domestic investment	19.2	20.8	21.5	19.9	20.9
Gross fixed investment	17.0	19.3	19.8	19.4	...
Total consumption	78.8	79.4	80.1	77.8	77.0
General government	7.2	7.4	7.6	7.5	7.4
Private	71.6	72.0	72.5	70.3	69.6

SOURCE: ECLA, on the basis of official statistics.
[a] Preliminary figures.

varied, given the increase in the over-all product they were for the most part more or less consistent with the development requirements of a country such as Colombia (see tables 75 and 76).

The contribution of the agricultural sector to the gross domestic product increased at the same rate in 1970-1974 as in 1965-1970. The average growth rate recorded (4.8 per cent) was higher than the target set in the International Development Strategy and even compared favourably with the sector's usual rate of development in Latin American countries. Although it declined, the share of agriculture in the gross domestic product in 1973-1974 was still fairly high (27 per cent).

In 1970-1974 the manufacturing sector was more dynamic and stable than in the period

Table 75. Colombia: gross domestic product by sector of economic activity
(Millions of pesos at 1970 prices)

	1970	Annual growth rate (percentages)						
		1965-1970	1970-1973	1970-1974	1971	1972	1973	1974[a]
Agriculture	34,880.5	4.8	4.5	4.8	2.5	5.5	5.3	5.5
Mining	2,457.7	1.5	-2.1	-2.8	-4.6	-6.0	4.8	-5.0
Manufacturing	20,976.7	6.4	9.6	9.0	7.9	10.0	10.9	7.0
Construction	6,281.1	12.3	6.7	8.1	7.1	1.8	11.5	12.5
Subtotal goods	*64,596.0*	*5.8*	*6.2*	*6.3*	*4.4*	*6.2*	*7.8*	*6.4*
Electricity, gas and water	1,787.9	8.5	9.1	...	10.0	13.7	13.3	...
Transport and communications	8,881.1	6.6	7.5	...	6.4	7.3	8.6	...
Subtotal basic services	*10,669.0*	*6.9*	*8.3*	...	*7.0*	*8.4*	*9.4*	...
Commerce and finance	20,521.2	6.6	8.2	...	7.3	9.1	8.2	...
Ownership of dwellings	6,886.9	5.8	6.3	...	7.1	5.9	5.9	...
Government	8,283.5	4.9	8.1	...	6.8	4.2	7.1	...
Other services	9,069.7	4.7	7.4	...	7.4	7.9	7.0	...
Subtotal other services	*44,761.3*	*5.8*	*7.7*	...	*7.2*	*7.5*	*7.4*	...
Total	*120,026.2*	*5.7*	*6.7*	...	*5.5*	*6.8*	*7.5*	*6.1*

SOURCE: ECLA, on the basis of official statistics.
[a] Preliminary figures.

Table 76. Colombia: structure of the gross domestic product by sector of economic activity
(Percentages)

	1965	Average 1966-1970	1970	1973	1974[a]
Agriculture	30.4	29.7	29.1	27.1	26.9
Mining	2.5	2.2	2.0	1.6	1.4
Manufacturing	16.9	17.2	17.5	18.8	18.9
Construction	3.9	5.1	5.2	5.2	5.5
Subtotal goods	*53.7*	*54.1*	*53.8*	*52.7*	*52.7*
Electricity, gas and water	1.3	1.4	1.5	1.7	...
Transport and communications	7.1	7.2	7.4	7.5	...
Subtotal basic services	*8.4*	*8.6*	*8.9*	*9.2*	...
Commerce and finance	16.4	16.8	17.1	17.7	...
Ownership of dwellings	5.7	5.8	5.7	5.6	...
Government	7.2	6.9	6.9	7.1	...
Other services	8.0	7.7	7.6	7.7	...
Subtotal other services	*37.2*	*37.2*	*37.3*	*38.1*	...
Total	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*

SOURCE: ECLA, on the basis of official statistics.
[a] Preliminary figures.

1965-1970 (an annual growth rate of 9 per cent in the former period compared with 6.4 per cent in the latter). As a result, the industrial growth rate in the last three years was higher than the 8 per cent minimum target set in the Strategy.[79]

As already observed, a notable feature of the trend of the other sectors producing goods and basic services was the absolute decline in the contribution of mining and quarrying to the gross domestic product, owing mainly to a drop in the production of crude petroleum from 1971 onwards. Moreover, the growth rate of construction was unsatisfactory compared with that of 1965-1970, especially considering the emphasis placed on its promotion in the National Development Plan. Only in 1973 and 1974 were there any real signs of revival.

Seen from the standpoint of employment of the labour force, there are other structural characteristics of the sectoral composition of the product that should be taken into account.

In the first place, although more or less recent information on the country's employment situation is fairly scarce, unemployment would seem to be a serious problem. It should be borne in mind that the average rate of visible urban unemployment at the end of the 1960s was reckoned to be around 10 per cent, and in general even higher in the larger cities of Colombia, excluding Bogotá. This situation would not appear to have improved or changed to any great extent in recent years.[80] The fundamental reason for this trend towards unemployment is that the urban labour force is increasing by over 5 per cent annually, and is obviously not all being absorbed into new employment opportunities in the cities.

Secondly, and related to the previous point, the proportion of the population employed in agriculture continued to decline fairly rapidly (from 42 per cent of the total in 1969 to about 38 per cent in 1974);[81] in fact, the absolute number of agricultural workers remained at virtually the same level or increased only very slightly. At the same time, considering the moderate increase in their share of the gross domestic product and certain figures for their capacity to absorb employment during the 1960s,[82] the industrial sectors and sectors providing basic services are unlikely to have increased their relative share of total employment to any extent.[83] The combination of these two factors led, on the one hand, to the appearance of serious employment problems in urban areas, and, on the other, to an increasing need for new employment oppotunities in the services sectors, thereby emphasizing a trend which was already very much apparent in the 1960s.

2. *The external sector*

The main features of the external sector during the period 1971-1974 were as follows. In the first place, the combined effect of internal and external factors, including the constant use of policy measures, brought about a substantial expansion (88 per cent over 1966-1970) and diversification of exports of goods; although there was in any case an increase in the unit value of exports, there was also a substantial increase in the volume exported.

Secondly, the value of imports at current prices was on average 63 per cent higher than in 1966-1970, owing mainly to the application of rather liberal importation policies, except in 1972. Because of the constant and increasing upward trend of the unit value of imports, however, the comparable increase at constant prices was 24 per cent.

Thirdly, the considerable improvement in the goods trade balance was mainly responsible for the reduction in the balance-of-payments deficit on current account, which dropped from 449 million dollars in 1971 to 57 million in 1973 and rose to 153 million in 1974.

Fourthly, together with this drop in the deficit on current account—and for accounting purposes, therefore, the lesser need for transfers of external savings to the country—the country's external financing policy enabled about 350 million dollars per year of medium and long-term non-compensatory external capital to be used during the period under consideration.

Finally, the combination of this trend in the deficit on current account and of the use of external loans enabled the country's gross foreign exchange reserves to rise from about 200 million dollars at the end of 1971 to over 530 million dollars at the end of 1973, though they dropped to 450 million in 1974 (see tables 77, 78 and 79).

[79] Unfortunately, no industrial production indexes providing more details regarding the growth of Colombia's manufacturing sector, particularly construction, are available in the country.

[80] See ILO, *Hacia el pleno empleo*, un programa para Colombia (Geneva, 1970); ECLA, *Tendencias y estructuras de la economía de Colombia en el último decenio*, op. cit., pp. 29-32; and IBRD, Report No. 138-CO, op. cit., p. 5.

[81] Estimates based on information supplied by DANE.

[82] See ECLA. *Tendencias y estructuras de la economía de Colombia en el último decenio* op. cit., pp. 12-16.

[83] According to the four strategy Plan, the generation of new employment opportunities should result from the rapid growth of construction and minor (non-traditional) exports. In the first case, the point has already been made that there was only any real increase in the sector's activity in 1973 and 1974; as regards exports, the development of this sector will be examined below, although no data are available on its impact on employment.

Table 77. Colombia: trend of exports and imports of goods

	Average 1966-1970	*1970*	*1971*	*1972*	*1973*	*1974*[a]	*Average 1971-1974*
(1) Exports of goods (FOB, in millions of dollars)	632.2	788.0	755.0	958.6	1,334.1	1,700.0	1,186.9
(2) Exports of goods (in millions of dollars, 1970 = 100)	80.2	100.0	95.8	121.6	169.3	215.7	150.6
(3) Unit value index of exports of goods (1970 = 100)	85.8	100.0	90.0	98.0	124.9	145.0	114.5
(4) Constant value index of exports of goods [(2):(3) x 100] (1970 = 100)	93.5	100.0	106.4	124.1	135.5	148.8	128.7
(5) Imports of goods (FOB, in millions of dollars)	633.6	802.0	878.0	813.1	1,022.9	1,420.0	1,033.5
(6) Imports of goods (in millions of dollars, 1970 = 100)	79.0	100.0	109.5	101.4	127.5	177.1	128.9
(7) Unit value index of imports of goods (1970 = 100)	96.0	100.0	104.0	109.9	130.0	158.0	125.5
(8) Constant value index of imports of goods [(6):(7) x 100] (1970 = 100)	82.3	100.0	105.3	92.3	98.1	112.1	102.0

SOURCE: ECLA, on the basis of official statistics.
[a] Preliminary figures.

Table 78. Colombia: balance of payments
(*Millions of dollars*)

	Average 1966-1970	*1971*	*1972*	*1973*	*1974*[a]	*Average 1971-1974*
Current account						
Exports of goods and services	806.6	984.0	1,198.4	1,626.0	2,044.0	1,463.1
Goods FOB	632.2	755.0	958.6	1,334.1	1,700.0	1,186.9
Services	174.4	229.0	239.8	291.9	344.0	276.2
Imports of goods and services	903.4	1,260.0	1,216.8	1,487.1	1,980.0	1,486.0
Goods FOB	633.6	878.0	813.1	1,022.9	1,420.0	1,033.5
Services	269.8	382.0	403.7	464.2	560.0	452.5
Net external investment income	−125.6	−176.0	−197.7	−207.4	−230.0	−202.8
Profits	−55.6	−71.0	−69.5	−67.5	−73.0	−70.3
Interests	−70.0	−105.0	−128.2	−139.9	−157.0	−132.5
Net private transfer payment	1.0	3.0	10.9	12.0	13.0	9.7
Balance on current account	−221.4	−449.0	−205.2	−56.5	−153.0	−215.9
Capital account						
Net external financing (*a* + *b* + *c* + *d* + *e*)	221.4	449.0	205.2	56.5	153.0	215.9
(*a*) Net external non-compensatory capital	266.8	383.0	281.2	193.5		
Direct investment	45.8	43.0	18.4	26.4		
Long- and medium-term loans	225.4	290.0	420.2	369.1		
Amortization payments	−90.6	−144.0	−165.0	−162.3		
Short-term liabilities	59.8	163.0	−16.3	−67.3	61.6	264.1
Official transfer payments	26.4	31.0	23.9	27.6		
(*b*) Domestic non-compensatory capital or assets	−9.6	−12.0	−23.9	−39.7		
(*c*) Errors and omissions	−5.4	55.0	83.6	38.5		
(*d*) Allocation of SDRs	4.2	17.0	18.5	0.0	–	
(*e*) Net compensatory financing (increase −)	−34.6	6.0	−154.2	−135.8	91.4	−48.2

SOURCE: ECLA, on the basis of official statistics.
[a] Preliminary figures.

Table 79. Colombia: foreign exchange reserves
(Millions of dollars at current prices)

	1965	*1966*	*1967*	*1968*	*1969*	*1970*	*1971*	*1972*	*1973*	*1974*
(1) Total foreign exchange reserves at the end of the period	96	77	83	173	221	206	203	325	534	449.0
(2) Imports of goods and services	653	867	696	866	939	1,149	1,260	1,216.8	1,487.1	1,980.0
(3) Imports of goods and services (monthly average)	54.4	72.3	58.0	72.2	78.3	95.8	105.0	101.4	123.9	165.0
(4) Number of months of imports financed out of foreign exchange reserves	1.8	1.1	1.4	2.4	2.8	2.2	1.9	3.2	4.3	2.7

SOURCE: IMF, *International Financial Statistics*, September 1972 and May 1975.

A further factor of a general nature which affected the external sector was the exchange system that was applied during the period. Following the policy introduced in 1967, a principal or unified exchange rate valid for the various foreign trade operations was applied throughout the period under review. At the same time, the unified rate of exchange was subject to moderate and periodic devaluations (mini-devaluations) which made it possible to keep the real value of the dollar fairly constant in terms of Colombian pesos, allowance being made of course for domestic inflation in the United States. Table 80 shows that, between 1969 and 1974, the real value of the dollar in pesos did not vary by more than 5 per cent.

An exception to this general rule was the existence of two special rates. One of these was used for exports of coffee and the other for the payment of purchases of crude petroleum for refining in the country.

The rate of exchange for coffee was also subject to mini-devaluations but throughout the period it

Table 80. Colombia: trend of the "real" value of the principal exchange rate

Year	*(1) Principal exchange rate (pesos per dollar–annual average)*	*(2) Implicit deflator of the gross domestic product of Colombia (1970 = 100)*	*(3) Implicit deflator of the gross national product of the United States (1970 = 100)*	*(4) (2) : (3) x 100 Ratio between the implicit deflators of Colombia and the United States (1970 = 100)*	*(5) (1) : (4) x 100 Trend of the "real" value of the principal exchange rate (base year, 1970) (pesos per dollar–annual average)*
1969	17.37	90.7	94.8	95.7	18.15
1970	18.50	100.0	100.0	100.0	18.50
1971	20.02	111.6	104.7	106.6	18.95
1972	21.94	126.0	107.9	116.8	18.78
1973	23.69	155.1	118.7	130.7	18.13
1974[a]	26.06	197.0	136.0	144.9	18.00

SOURCE: Banco de la República of Colombia, and Department of Commerce of the United States, *Statistical Abstract 1973*.
[a] Preliminary figures.

stood at 80 per cent of the principal rate in peso terms. In other words, exports of coffee were subject to a proportional tax of 20 per cent.

In the case of petroleum, a fixed rate of exchange was applied which was not subject to moderate and periodic devaluations. In the middle of 1971, the rate was raised from 9 to 20 pesos per dollar—similar to the principal rate—and remained at this level up to and including 1974. Consequently, the gap between the rate of 20 pesos per dollar and the principal rate of exchange became progressively greater.

(a) *Exports of goods*

With regard to exports, the policy measures applied allowed for separate treatment of coffee sales and minor or non-traditional exports.

In the case of coffee, the policy throughout the period under consideration was designed to control the quantity of the product produced and exported in view of its important role in the national economy, the large share of Colombian exports in the international coffee market, the movement of prices and the terms of the International Coffee Agreement. In addition, the coffee-producing countries signed an international agreement in 1973 which led to the retention of 10 per cent of the volume of their sales in order to reduce world supply.

The volume of coffee exported by Colombia between 1968 and 1974 was fairly stable, fluctuating around 6.5 million 60-kilogramme bags. As regards prices, on the other hand, the situation was reversed: the average annual price per pound in New York, which had not varied greatly from 45 United States cents from 1965 to 1969, fluctuated widely in the years 1970-1974, reaching a peak of 77.4 cents in 1974. Naturally, this fluctuation was reflected in the value of exports in current prices (see table 81).

The promotion of minor or non-traditional exports was one of the four strategies of the National Development Plan; what happened in practice was that a policy which had been applied since 1967 was maintained and strengthened. Briefly speaking, non-traditional exports were stimulated mainly by the following measures: (i) maintenance of a rate of exchange with a constant "real" value, as mentioned above; (ii) issue of certificates of drawback (CAT) which, in several cases, represented as much as 15 per cent of the value exported;[84] (iii) the preferential granting of fairly cheap bank credit (with negative real rates of interest); and (iv) the possibility of importing equipment and intermediate goods required for the production of minor exports without import control or customs duties. A study conducted by the International Monetary Fund calculated that the exchange subsidy on exports of manufactures resulting from the combined application of measures (ii), (iii) and (iv) represented 30 per cent.[85]

It is not easy to make an accurate estimate of the real effect of the policy measures referred to above,[86] generally speaking because of the favourable climate of recent years for all minor exports, but there can be no doubt that they expanded very rapidly and that they were further encouraged by the development of the Andean Common Market and, in general, by the large demand and high prices in the world markets.

[84] During the period under consideration—and particularly at the end of 1974—this percentage changed and, moreover, showed some tendency to vary according to the characteristics of the merchandise exported. There was also some fluctuation in the redemption period of the CAT.

[85] See IBRD, Report No. 138-CO, op. cit., p. 27.

[86] An analysis of this kind has been carried out by Carlos F. Díaz Alejandro in *Las exportaciones menores colombianas*, FEDESARROLLO, January 1973.

Table 81. Colombia: exports of coffee

	Average 1965-1969	*1970*	*1971*	*1972*	*1973*	*1974*[a]	*Average 1971-1974*
(1) Exports/thousands of 60-kg bags)	6,071	6,506	6,569	6,528	6,769	6,898	6, 691
(2) Price per pound in New York (U.S. cents)	45.09	56.42	49.27	56.70	72.35	77.41	63.93
(3) Value of exports of unroasted coffee (millions of dollars)	338.00	466.70	395.40	429.60	597.00	631.20	513.30

SOURCE: Banco de la República of Colombia, FEDECAFE, and IMF, *International Financial Statistics*, May 1975.

[a] Preliminary figures.

In the case of several export lines, particularly manufactures, the existence of production capacity which was not being utilized owing to the inadequacy of domestic demand was also an inportant factor.

For certain exports of food products, the substantial increase in international prices, which established a price differential in favour of exports as opposed to domestic sales, was decisive. Typical examples were meat, leather and cotton. This situation also led to an increase in the domestic price of these products, to temporary shortages on the domestic market and to the adoption of provisional measures forbidding their export. This aspect is dealt with in greater detail below.

A look at the composition of exports of goods shows that, between 1966-1970 and 1971-1974, the combined share of coffee and crude petroleum dropped from 71.6 per cent to 50.8 per cent while that of non-traditional products rose from 28.4 per cent to 49.2 per cent (see table 82). This sharp increase was attributable to certain major products, particularly cotton, sugar, meat, emeralds, yarns and textiles, metal manufactures and machinery, electrical equipment, furs and leather, and chemical and pharmaceutical products.

(b) *Imports of goods*

The policy measures implemented during the period under review had a decisive influence on imports. Basically, they involved the use of exchange and tariff instruments, lists of permitted or prohibited imports, prior deposits and monthly foreign exchange budgets.

By and large, the import policy was more or less liberal—in its application of the various instruments—according to the trend of exports, the country's import capacity and the level of foreign exchange reserves. Logically enough, it was found that the measures adopted took some time to affect the values and volumes imported. This delay was about six months and, in certain cases, close to a year.

The increase in imports of goods between 1970 and 1971 thus responded to a gradual liberalization of the policy applied as a result of the favourable trend of the foreign currency inflow between 1968 and 1970. Similarly, the drop in exports in 1971 led to the adoption of more restrictive measures which, the following year, caused a reduction in the volume imported. Finally, the improvement in the foreign exchange situation which began to take place at the beginning of 1972 brought about a progressive liberalization of import controls,[87] which made

[87] The provisions adopted were: (*a*) progressive increase in the monthly volume of import licences approved by the Monetary Board; (*b*) increase in the number of kinds of merchandise whose importation was permitted; (*c*) reduction of customs tariffs; (*d*) reduction of prior import deposits.

Table 82. Colombia: composition of exports of goods
(*Percentages*)

	Average 1966-1970	*1970*	*1971*	*1972*	*1973*	*1974*[a]	*Average 1971-1974*
1. Coffee	61.9	62.7	54.9	47.5	47.4	41.1	47.7
2. Crude petroleum	9.7	8.0	7.0	3.4	2.0	...	3.1
3. Non-traditional exports	28.4	29.3	38.1	49.1	50.6	58.9	49.2

SOURCE: ECLA, on the basis of official statistics.
[a] Preliminary estimates.

Table 83. Colombia: composition of imports of goods
(*Percentages*)

	Average 1966-1970	*1970*	*1971*	*1972*	*1973*	*Average 1971-1973*
1. Consumer goods	8.8	10.7	10.4	12.4	14.1	12.3
Non-durable	4.0	5.6	4.9	5.8	6.6	5.8
Durable	4.7	5.1	5.5	6.6	7.5	6.5
2. Raw materials[a]	45.2	44.7	48.9	46.7	48.4	48.0
3. Capital goods	45.3	43.9	40.0	39.5	36.1	38.5
4. Miscellaneous[b]	0.6	0.7	0.7	1.4	1.4	1.2

SOURCE: ECLA, on the basis of official statistics.
[a] Including construction material.
[b] Including fuels.

possible a substantial increase in the value imported in 1973 and 1974 and, to a lesser extent, in the corresponding volume, owing to the effect of the higher unit value of imports in those years (see table 77). Between 1965 and 1969, there had been similar variations in the import policy and in the value of imports brought into the country.

As regards the structure of imports of goods, between 1966-1970 and 1971-1973 there was a considerable increase in the relative share of imports of consumer goods and to lesser degree, of raw materials. By contrast, there was a marked reduction in the share of capital goods in the total (see table 83).

(c) *Other aspects of the trend of the external sector*

Colombia has managed to devise an external financing strategy based on the permanent operation of an *ad hoc* consultant group headed by the World Bank, and on the continuous and satisfactory formulation of investment projects which the international financial institutions and industrialized countries are keen to finance with loans granted on softer terms than private credits. This factor has also helped to improve the external debt-servicing situation—owing to the more favourable composition of the debt—with the result that the increase in the resources needed for the payment of amortization and interest on the debt has been moderate and compatible with the trend of exports.[88]

[88] See IBRD, *Annual Report, 1974*, table 6.

The balance-of-payments figures show that 420 million dollars in medium- and long-term loans were utilized in 1972, the corresponding estimate for 1973 being 370 million dollars, and slightly less for 1974. It was also found that about 70 per cent of these amounts was used to finance the total investment of the public sector.[89]

C. THE RECENT INFLATIONARY PROCESS

1. *Background*

Following the four-year period 1967 to 1970 during which domestic price increases in the Colombian economy were below 9 per cent per year, the rate of inflation rose to approximately 14 per cent in 1971 and 1972, and to 25 per cent in 1973.[90] This acceleration in the rate at which prices increased contrasts with the pattern of the previous two decades, which shows a "current" rate of inflation of less than 10 per cent per year, upward variations in this trend taking place only in a few of the years (1957, 1963, 1965 and 1966) and being linked with substantial devaluations of the peso following fairly long periods with a

[89] Including the national government and decentralized institutions, as well as direct and indirect investment (see CIAP, op. cit., table IV-6).

[90] The figures refer to changes from December to December in the consumer price index. This index, which is considered to be a good indicator of inflationary trends, treats the situations of salaried employees and wage-earners separately, the calculations being made for seven cities (Bogotá, Medellín, Cali, Barranquilla, Bucaramanga, Manizales and Pasto) (see table 84).

Table 84. Colombia: trend of consumer prices

	Average 1965-1969	*1970*	*1971*	*1972*	*1973*	*1974*
1. National consumer price index (December to December, percentage variations)[a]						
(*a*) Salaried employees (total)	10.2[b]	7.2	12.6	14.1	22.1	25.2
(*b*) Wage-earners (total)	9.8[c]	6.3	14.7	14.0	25.1	26.9
(*c*) Salaried employees (food-stuffs)	9.6	5.0	15.0	16.2	30.6	30.3
(*d*) Wage-earners (food-stuffs)	10.2	3.6	17.1	16.0	31.5	30.8
2. National consumer prices index (between averages, 1970 = 100)						
(*a*) Salaried employees (total)	93.2[d]	100.0	110.9	125.5	150.2	185.2
(*b*) Wage-earners (total)	93.7[d]	100.0	111.8	127.3	155.2	194.3
(*c*) Salaried employees (food-stuffs)	94.4[d]	100.0	112.6	129.0	164.3	212.7
(*d*) Wage-earners (food-stuffs)	94.7[d]	100.0	112.6	130.0	167.5	216.3

SOURCES: Departamento Administrativo Nacional de Estadística (DANE) and the National Planning Department.

[a] Includes the following cities weighted differently: Bogotá, Medellín, Cali, Barranquilla, Bucaramanga, Manizales and Pasto.

[b] Variations were 7.6 per cent in 1967, 6.7 per cent in 1968 and 8.5 per cent in 1969.

[c] Variations were 7.0 per cent in 1967, 6.4 per cent in 1968 and 8.7 per cent in 1969.

[d] Index value in 1969.

pegged rate of exchange. In other words, the inflationary "tradition" of the country was relatively limited, in contrast with the turn inflation took in other countries of the region, while furthermore, the occasional upward variations which took place in the past seem to have had causes different from those of recent years, particularly as regards the problem of the exchange rate.

Similarly, as in other developing nations with a *per capita* income similar to that of Colombia, the item "food" exercises a very strong influence on the evolution of domestic prices, and this is reflected in the high weighting given to this item in the price indexes.[91] Moreover, the variations in food prices—particularly those of staple goods—are those that have the clearest and most immediate effect on consumers as a whole.

[91] In the national consumer price index for the country, the weighting of the item "food" is approximately 40 per cent for salaried employees and approximately 50 per cent for wage-earners.

Over the three-year period 1971-1974 it was observed that food prices increased more rapidly than those for other goods and services. Thus, between 1970 and 1973 the relative consumer prices of food-stuffs increased by approximately 20 per cent compared with other items in the index (housing, clothing and miscellaneous items).[92] A similar trend can be seen in respect of wholesale prices, if agricultural prices are compared with those for manufacturing industry and mining (see table 85).

Other notable relative price changes occurred between 1970 and 1974. With the exception of coffee,[93] domestic wholesale prices for export products showed a marked upward trend, which coincided with that recorded by the unit values for

[92] See table 84 and figures for items for the consumer price index published by DANE and the Banco de la República.

[93] This upward trend was particularly strong in 1973, when the item in question showed an increase of 39 per cent, while the variation in the total wholesale price index amounted to 28 per cent.

Table 85. Colombia: trend of other price indexes

	1969	*1970*	*1971*	*1972*	*1973*	*1974*
1. Index of general wholesale prices (between averages, 1970 = 100)						
(*a*) Total	–	100.0	111.5	131.9	168.7	229.3
(*b*) According to economic and use						
Capital goods	–	100.0	107.8	124.8	146.0	206.9
Raw materials and intermediate products	–	100.0	108.1	127.6	170.8	240.7
Consumer goods	–	100.0	117.2	139.8	173.9	223.3
(*c*) By branch of economic activity						
Agriculture, forestry, hunting and fishing	–	100.0	116.0	136.4	182.0	246.7
Manufacturing industry	–	100.0	109.5	126.0	155.2	215.0
2. Index of general wholesale prices (between averages, 1970 = 100)						
(*a*) Total	–	100.0	111.5	131.9	168.7	229.3
(*b*) By origin of article						
Products consumed	–	100.0	112.6	134.1	170.6	226.3
Imports	–	100.0	109.8	128.4	164.1	232.7
Exports	–	100.0	102.6	126.1	171.7	254.1
Exports (excluding coffee)	–	100.0	111.0	133.8	186.1	...
3. Index of prices for building materials in Bogotá (between averages, 1970 = 100)	90.0	100.0	109.4	122.9	147.7	200.8
4. Coffee; average price in pesos in the country (1970 = 100)	75.3	100.0	95.5	115.0	148.6	169.2

SOURCES: Banco de la República and the National Planning Department.

exports mentioned earlier. On the other hand, the price indexes for capital goods and building materials showed relatively marked downturns; in both cases the drop was approximately 20 per cent with respect to agricultural prices, and 13 per cent with respect to the general index.[94]

In the light of the foregoing it can be seen, put briefly, that in the period under study the acceleration in the growth rate of prices coincided with significant changes in the pricing system which, on the one hand, favoured agricultural and exporting activities, with the exception of coffee, and on the other operated to the detriment of manufacturing industry, especially some branches of production such as building materials.

2. *Factors which influenced the acceleration of the inflationary process*

In examining the intensity of annual price movements, two stages in the inflationary process stand out: 1971 and 1972 on the one hand, and 1973 and 1974 on the other. However, examination of the elements which intervened in the process leads to a further subdivision: thus, the origins of price trends in 1971 seem to differ from those in 1972–1974. This makes it desirable to examine what occurred in the first year separately from that which occurred in the last three.

(a) *The 1971 experience*

Consumer food prices, which had increased by less than 5 per cent during 1970 in terms of the average for both salaried employees and wage earners, rose by more than 15 per cent in 1971. This substantial change in the rate of growth exercised a decisive influence on the over-all acceleration of inflation, which rose from 7 per cent in the first year to approximately 14 per cent in the second.[95]

Information available on the performance of the agricultural sector during the year shows that prevailing climatic conditions–particularly the extremely heavy rainfall in the early part of 1971–caused a considerable drop in agricultural production, especially in some crop-farming items. Official figures put the loss of potential production at approximately 100 million dollars, so that the over-all growth of the contribution of agriculture to the gross domestic product was only 2.5 per cent, or approximately half the rate recorded in the previous 5 years. Apart from coffee, the agricultural products which suffered most in the first half of 1971 were cotton, non-irrigated rice, beans, potatoes and soya, the shortfalls compared with a similar period for the previous year being between 10 and 30 per cent.[96]

A month by month analysis of the consumer price index shows that the change in the rate of inflation took place in the early part of the year and that, moreover, the rises in the prices of agricultural products which were in extremely short supply exercised considerable influence on the process.[97] Other foods and other components of the index (clothing and miscellaneous items) continued to increase at a pace similar to that of the previous year.

In addition, the unexpectedness and the unprecedented size of shortfalls in certain products prevented the timely application of import and domestic policy measures to control, even partially, the supply and prices of the articles in short supply.

Another factor which had a considerable impact on the price increases was the exchange rate, in spite of the fact that, as already stated, a mini-devaluation policy had been followed since 1967. This impact was caused by the fixing in June 1971 of a new rate of exchange of 20 pesos to the dollar, applicable to purchases of crude petroleum for domestic refining. Since September 1965 the rates had been fixed at 9 pesos per dollar, so this big difference rapidly had an effect on the prices of fuels and lubricants, and this was transferred, with varying intensity, to a range of goods and services whose inputs consisted to a significant proportion of petroleum products.[98]

Examination of the trends of other variables which are of significance for the inflationary process suggests that during 1971, or in the immediately preceding months, other factors had no major impact on the evolution of prices. This general impression can be confirmed by examining the different indicators shown in table 86.

As regards the external sector, there was a drop of 10 per cent in the unit value of exports of goods, mainly as a result of the reduction in coffee prices, and there were only moderate increases on the international markets for some of the main products exported by the country.

The unit value of imports of goods increased by 4 per cent, compared with an increase of 8.2 per

[94] See table 85.

[95] See table 84. The approximate variations for both salaried employees and wage-earners for the period December to December are taken together.

[96] See CIAP, op. cit., CIAP/591, pp. 21 et seq., and table AE-1.

[97] For example, between September 1970 and September 1971 the prices of beans rose by 70 per cent and those of vegetable fat by 30 per cent. See DANE, *Boletín Mensual de Estadística*, November 1971, p. 72.

[98] This even had an important impact on the cost of dwellings as calculated in the consumer price index, because of the weighting of fuels and services in this group. See DANE, *Boletín Mensual de Estadística*, November 1971, p. 68.

Table 86. Colombia: relationship between price changes and some important variables
(*Percentage variation*)

	1969	*1970*	*1971*	*1972*	*1973*	*1974*[a]
1. National consumer price index (December to December)						
(*a*) Salaried employees (total)	8.5	7.2	12.6	14.1	22.1	25.2
(*b*) Wage-earners (total)	8.7	6.3	14.7	14.0	25.0	26.9
2. Index of unit value in dollars for imports of goods (between averages)	2.1	3.0	4.0	5.7	18.3	21.5
3. Index of unit value in dollars for exports of goods (between averages)	−1.2	23.4	−10.0	8.9	27.4	16.1
4. Main exchange rate (between averages)	6.0	6.5	8.2	9.6	8.0	10.0
5a. Unit value of imports by rate of exchange (2 x 4) (between averages)	8.2	9.7	12.5	16.0	27.7	33.7
5b. Unit value of exports by rate of exchange (3 x 4) (between averages)	4.7	31.4	−2.6	19.4	37.7	27.7
6. Money: total means of payment (at year-end)[b]	22.3	15.5	11.9	27.1	30.7	20.0
7. Total central government expenditure[c]	18.7	25.8	19.6	26.3	13.6	25.4
8. Total central government expenditure (as a percentage of GDP at market prices)	9.4	10.0	10.2	10.7	9.2	8.9
8a. Central government investment (as a percentage of GDP at market prices)	3.9	4.2	3.9	4.5	3.5	3.3
9. Current income of central government	16.9	24.7	20.6	11.6	24.8	29.5
10. Current income of central government (as a percentage of GDP at market prices)	8.6	9.2	9.4	8.7	8.2	8.1
11. Central government deficit (as a percentage of GDP at market prices)	0.7	0.9	0.8	2.0	1.0	0.8
12. Investment and current expenditure of whole public sector	15.9	22.1	27.3	19.2	16.9[d]	...
13. Investment and current expenditure of whole public sector (as a percentage of GDP at market prices)	24.0	24.8	26.9	26.6	23.5[d]	...
13a. Investment of whole public sector (as a percentage of GDP at market prices)	9.8	11.5	12.7	12.3	10.9[d]	...
14. Nominal wages						
(*a*) Minimum wages	–	–	–	30.0[e]	–	40.0[f]
(*b*) Industrial wages				14.8	20.0	13.1
(*c*) Weighted nominal wage	3.4	9.9	6.6	10.6	...	...

SOURCES: Items 1 to 5: ECLA, on the basis of official statistics; 6, 7, 9, 11: IMF, *International Financial Statistics*, August 1974; 12 and 13a: IBRD, Report No. 138-CO, op. cit., table II.2; 8, 10, 11, 13: GDP at current market prices, see table 88; 14a: CIAP, op. cit., CIAP/591, table AE-3; 14b: FEDESARROLLO, *Coyuntura económica*, April 1973 and 1974; and 14c: DANE, *Boletín mensual*, April 1974, p. 118.

[a] Preliminary figures.
[b] As defined by IMF.
[c] Current expenditure plus investment.
[d] Estimates.
[e] About 30 per cent as from April; not adjusted since 1969, when it was adjusted by approximately 20 per cent after remaining unchanged for 6 years.
[f] About 40 per cent as from November.

cent in the principal rate of exchange. The average increase in the cost of imports, expressed in terms of national currency, was therefore 12.5 per cent. This figure, although somewhat higher than that for previous years, is relatively modest and does not seem to provide an explanation for variations of real importance, on the cost side, in the rate of increase in prices.

Although the available information on the evolution of wages is both limited and incomplete, the data are not indicative of any significant inflationary pressures coming from this area. The weighted nominal wage[99] increased by 6.6 per cent, which would imply a drop, compared with 1970, of approximately 4 per cent in real wages. Furthermore, the minimum urban and rural wages[100] were not adjusted during 1971, in spite

[99] Calculated by DANE on the basis of data provided by the Instituto Colombiano de Seguros Sociales (ICSS). In June 1973 this institution had a membership of 1,173,000.

[100] These wages are fixed by decrees passed by the Government on the basis of studies prepared by the National Wages Council. There is no legal obligation to change them every year, and the records show that since 1950 they have been adjusted at intervals varying between one and six years.

of the fact that the last increase had been granted in August 1969.

From the point of view of other possible inflationary pressures, particularly those stemming from changes in a few of the principal financial variables, there did not seem to be any significant relation between them and the acceleration of price increases.

Thus, during 1971 the quantity of money increased by 11.9 per cent whereas in the previous year the increase was 15.5 per cent:[101] these moderate and decreasing figures may be contrasted, for example, with the increase of 22.3 per cent recorded in 1969.

Nor were treasury operations one of the causes of inflation, since the rate of expansion of the national government's current income was faster than that of total expenditure, with the result that the government deficit[102] fell from 0.9 per cent of the gross domestic product in 1970 to 0.8 per cent in 1971. In addition, it was observed that the whole of this deficit was covered by using foreign loans, which did not have the effect of expanding the monetary mass owing to the over-all balance-of-payments position.

As a result of this, there was a drop in the country's international reserves between the end of 1970 and 1971.[103]

It may be noted, it is true, that the anti-inflationary trend of fiscal policy coincided with a considerable expansion in central government expenditure—particularly current expenditure—and also in consolidated public sector expenditure, so that between 1970 and 1971 the share of these two variables[104] in the GDP increased and thus maintained a trend that had been observed since the end of the 1960s. Nevertheless, the simultaneous presence of the factors referred to—among which the balance-of-payments deficit on current account played a leading part—helped to offset to some extent the possible disequilibria that could have been generated by public sector finance operations.

(b) *Trends in 1972-1974*

The elements identified earlier which exercised some influence on the acceleration of prices in 1971 ceased to a great extent, to have any effect either on the rate of inflation in 1972, or on the stepping up of the rate in 1973-1974. During those years, as has been pointed out, there was a tendency towards relatively balanced development in the various productive activities, and more specifically in agriculture, which grew at a satisfactory average rate of about 5.5 per cent.[105] In general, normal conditions prevailed as regards production, and there was a marked improvement in the growth rate of the GDP.

The basic explanation of the inflationary trend in the three-year period 1972-1974 rested on developments in the external sector and the various impacts this had on some basic variables and situations. The impact impinged, on the one hand, on the government monetary position as well as on the liquid resources in the hands of exporters and, on the other, on the extent of the influence of increased unit values for imports and exports on domestic costs and prices, and in some cases on supply. To these two combined forces, which acted in the same direction, other supplementary factors were added, a notable one being the drop in imports in 1972. However, it is interesting to note that in 1974 the importance of the first group of factors diminished, while that of the second group increased.

(i) *Financial over-expansion.* The evolution of the means of payment showed clear signs of over-expansion, for they increased by 27.1 per cent in 1972, 30.7 per cent in 1973 and 20 per cent in 1974 (see table 86). These figures are higher than those recorded in 1970-1971.

In 1972-1973, the behaviour of the public finances was the main factor which affected developments in the monetary field, as a result of the deficit financing by the national government (and by the public sector), the measures taken to cover it and the balance-of-payments situation during these years.

In 1972, a substantial increase in government expenditure (particularly in investment), which was not accompanied by similar growth in current income, resulted in a deficit of approximately 3,700 million pesos (2 per cent of the GDP)—three times the figure for 1971. In 1973, there was a sharp drop in the relative increase in government expenditure—in current values, investment remained practically at a standstill—and in spite of

[101] The 1970 increase in the means of payment is also taken into account because in some interpretations of the variations in prices it is recognized that delays of up to six months could take place before the effect of the increase in the quantity of money on prices is felt.

[102] Defined as the difference between total expenditure and current income (see table 86).

[103] See tables 86, 87 and 88 and also tables 78 and 79.

[104] See table 86. The government investment coefficient fell from 4.2 per cent in 1970 to 3.9 per cent in 1971, whereas that of public sector investment rose from 11.5 per cent at the end of the first year to 12.7 per cent in the second.

[105] Only some temporary problems in connexion with shortfalls in the production of certain foods were observed. In this respect, the most noteworthy case was that of potatoes, during the first half of 1973.

Table 87. Colombia:
(Millions of pesos

	1968	*1969*	*Percentage variation*	*1970*
1. Current income[b]	8,194	9,581	16.9	11,950
2. Current expenditure	4,902	6,061	23.6	7,649
3. Surplus on current account (1 – 2)	3,292	3,520	6.9	4,301
4. Investment	3,866	4,344	12.4	5,442
5. Total central government expenditure[d] (2 + 4)	8,768	10,405	18.7	13,091
6. Total central government deficit (5 – 1) or (4 – 3)	574	824	43.6	1,141
7. Deficit financing[d]				
(*a*) External debt (net)	1,063	1,272	19.7	1,458
(*b*) Internal debt (net)[e]	–489	–448	–	–317
8. Share of investment financed by external borrowing (7a): 4 (percentages)	27.5	29.3		26.8

SOURCES: IMF, *International Financial Statistics*, August 1974; and ECLA, on the basis of data provided by the Tesorería General de la República.

[a] Preliminary estimates.
[b] Excluding certificates of drawback (CAT) and Tourist Development Certificates (CDT).
[c] Excluding certain special military purchases.
[d] Excluding amortization of the internal and external debt.
[e] Including variations in cash holdings.

Table 88. Colombia:
(Millions of pesos at current prices,

	1968	*1969*	*Percentage variation*	*1970*
I. *Structure of monetary resources*				
1. Money	15,858	19,396	22.3	22,397
2. Quasi-money	2,216	2,696	21.7	3,381
3. Deposits for imports	1,879	2,159	14.9	2,402
4. Long-term external debt	682	980	43.7	1,333
5. Other items (net)	1,971	1,788	–9.3	2,191
Total	*22,606*	*27,019*	*19.5*	*31,704*
II. *Monetary expansion and absorption factors*				
6. International reserves (net)	–1,276	–1,198	–	–1,360
7. Domestic credit	23,882	28,217	18.2	33,060
(*a*) Central government (net)	5,139	5,024	–2.2	4,696
(*b*) Public institutions	647	935	44.5	1,266
(*c*) Private sector	18,095	22,258	23.0	27,098
Total	*22,606*	*27,019*	*19.5*	*31,704*
8. GDP at current market prices[a]	–	110,953		130,591
9. GDP at market prices: money[b] (8 :1)	–	5.7		5.8
10. Direct issue (primary money) of the Banco de la República	14,766	18,739	26.9	20,573

SOURCE: IMF, *International Financial Statistics*, August 1974; and ECLA, on the basis of official statistics.

[a] GDP generated over the entire year.
[b] This ratio as it stands does not reflect the true situation, since the GDP figure is for the entire year, whereas that of money was calculated at the end of each period.

central government accounts
at current prices)

Percentage variation	*1971*	*Percentage variation*	*1972*	*Percentage variation*	*1973*	*Percentage variation*	*Percentage[a] variation 1974*
24.7	14,416	20.6	16,085	11.6	20,073	24.8	29.5
26.2	9,747[c]	27.4	11,397	16.9	13,991	22.8	23.1
22.2	4,669	8.6	4,688	0.4	6,082	29.7	44.2
25.3	5,903	8.5	8,362	41.7	8,458	1.1	29.5
25.8	15,650	19.6	19,759	26.3	22,449	13.6	25.4
38.5	1,234	8.2	3,674	197.7	2,376	−35.3	−9.0
14.6	1,235	−15.3	3,290	166.4	3,051	−7.3	–
–	−1	–	384	–	−675	–	–
	20.9		39.4		36.1		–

monetary trends
at the end of each period)

Percentage variation	*1971*	*Percentage variation*	*1972*	*Percentage variation*	*1973*	*Percentage variation*	*Percentage variation 1974*
15.5	25,064	11.9	31,854	27.1	41,647	30.7	20.0
25.4	4,128	22.1	5,856	41.9	11,663	99.2	...
11.3	2,144	−10.7	2,496	16.4	1,163	−53.4	...
36.0	1,959	47.0	2,595	32.5	2,798	7.8	...
22.5	2,796	27.6	3,666	31.1	2,822	−23.0	...
17.3	*36,091*	*13.8*	*46,467*	*28.8*	*60,093*	*29.3*	
–	−3,054	–	527	–	5,502	–	...
17.2	39,145	18.4	45,937	17.4	54,592	18.8	...
−6.5	6,333	34.9	6,413	1.3	5,810	−9.4	...
35.4	1,540	21.6	2,009	30.5	3,628	80.6	...
21.7	31,272	15.4	37,515	20.0	45,154	20.4	...
17.3	*36,091*	*13.8*	*46,467*	*28.8*	*60,093*	*29.3*	...
	153,766		185,092		244,507		–
	6.1		5.8		5.9		–
9.8	22,522	9.5	27,505	22.1	35,950	30.7	–

the fact that current income grew at a lower rate than the nominal GDP, the deficit was reduced to 2,400 million pesos (1 per cent of the GDP).

These deficits were financed through the use of net external credits, no use being made of domestic borrowing in the two-year period as a whole. Thus, in 1972 the national government used external loans in the amount of some 150 million dollars, whereas in the following year the figure for comparable operations was approximately 130 million. These figures may be compared with those for the period 1970-1971, when the average amount used was in the region of 70 million dollars per year (see table 87).

In addition, estimates for the whole public sector indicate that net foreign resources used also doubled between 1970-1971 and 1972-1973 (from an annual average of approximately 140 million dollars to one of some 300 million).

While the national government and the public sector were increasing their dependence on external credit, the balance-of-payments situation changed significantly, as reflected in the drop referred to in the deficit on current account. The result of this was, roughly, that foreign credit in 1972-1973—which was more than 300 million dollars compared with the 140 million dollars for 1970-1971—was put to better use by the public sector, and went in its entirety to swell the international reserves of the country (see table 79).

The monetary series show that this increase in international reserves was the main factor behind the accelerated expansion of the quantity of money, and they also show that in 1972 and 1973 total domestic credit increased at a rate almost identical to that recorded in 1969-1971. As regards the components of domestic credit, only the loans granted to public institutions showed a higher average rate of growth (see table 88).

Another factor which exercised some influence on the evolution of the quantity of money was the development shown by the monetary absorption factors, as they are usually called. Thus, a moderating influence was exercised by the rapid increase of quasi-money resulting from the introduction of the system of readjustable savings and loans for housing.[106]

In 1974 the rate of increase in the means of payment decreased. This was due, on the one hand, to the fact that in terms of current prices the total deficit of the national government was about the same as in the previous year, which meant that its share in the GDP was reduced to 0.8 per cent. On the other hand, although the proportion of the deficit financed with domestic credit increased substantially—with the decrease in convertible external loans contracted by the Treasury—this expansive effect was largely offset by the loss of international reserves in covering the balance-of-payments deficit.

Another aspect of the phenomenon of financial over-expansion to be taken into account is the rapid and substantial increase experienced in those years in the spending power of the exporting sectors. In this respect, a special feature of Colombian exports is that they are supplied by a large number of small national enterprises or economic units which pay a relatively low rate of taxation. A substantial portion of non-traditional exports and, to a lesser extent, coffee exports share this feature. Should exports increase, such a situation could lead to an increase in domestic demand—particularly for consumer goods—which may be more intense and sudden in Colombia than in those countries where the export sector is cornered by a small group of enterprises which are subject to higher rates of taxation and have to exercise a greater degree of restraint in their outlay, and/or in cases of total or partial government ownership of a major proportion of exporting enterprises.

Such a situation, together with the substantial increases in exports of goods which took place in 1972 and 1973 (27 and 39 per cent in dollars at current prices, respectively, and 39 and 50 per cent in their equivalent in Colombian pesos), leads to the assumption that demand pressures stemming from the increased capacity of exporting activities to incur greater expenditure may have had a considerable impact on the acceleration of the inflationary process under study.

(ii) *External pressures on domestic prices.* The most direct effects of external inflation (or "imported" inflation, as it is frequently called) on domestic prices were more marked in 1973, and were of special importance in the acceleration of inflation in that year, adding yet another dimension to the problem of financial over-expansion already examined. In 1972, the impact of these factors was not as strong.

It has also been observed that the increases in the international prices of commodities in the world market spread to the domestic economy through imports and, moreover, through their effects on the national prices of goods exported to Colombia.

As regards imports and exports, the price increases which had the greatest relative impact were related to the trade in agricultural products,

[106] The system, introduced in May 1972, operates on the basis of units of constant purchasing power (UPAC), which are subject to daily readjustment in accordance with the estimated change in consumer prices. Towards the end of 1973, UPAC deposits amounted to the equivalent of 4,500 million pesos (this figure corresponded to 11 per cent of the quantity of money). However, by that date 3,400 million had already been spent on the construction of houses, so the net absorption effect of the system must have been a good deal smaller.

more particularly food-stuffs. This is so for two main reasons. First, because these were the commodities which experienced comparatively higher increases in international prices.[107] Secondly, because—as already stated—food-stuffs have the highest weighting in Colombian price indexes, and particularly in the consumer price indexes.

This relatively faster rate of growth of prices for agricultural products was also noted in the Colombian price structure in 1973 and 1974, maintaining a trend which had begun in 1970. Thus, this feature was present both in consumer prices (food-stuffs) and in wholesale prices (agricultural commodities and others) (see tables 84 and 85).

In addition, one of the qualities of the Colombian economy which ought to be borne in mind when studying the impact of imported inflation on the economy is its relative openness and flexibility in foreign trade operations.[108] In practice, this means that the Government lays down general guidelines for the operation of the external sector but, save in exceptional cases, participates only to a limited extent in fixing quantities, and particularly prices, for the various goods which are imported and exported.

Therefore, the effects of external inflation tended to be imported with some ease and speed, and in very few instances was any attempt made to isolate to any significant extent the domestic price situation from that prevailing in international markets. This was so in spite of the fact that there were certain important elements which could have helped in any attempt to ensure such isolation: first, the favourable balance-of-payments situation which existed from 1972 onwards and its further improvement in 1973, though not in 1974; secondly, the fact that the country is self-sufficient in the majority of food-stuffs consumed, and thirdly, the relatively balanced and satisfactory growth of the GDP recorded in the three years 1972-1974.

– *The inflationary impact transmitted through imports.* First evidence of the greater inflationary impact which the import trade had in 1973 and 1974 is provided by the average variation in the dollar unit value of imports, which increased in those years by 18 and 21 per cent, respectively, or, in other words, more than three times as much as in 1972. This higher rate of increase in the unit value of imports may have meant an additional inflationary impact in 1973 of up to three percentage points over the 1972 figure,[109] and four points in 1974.

[107] In this connexion, it should be remembered that, on average, between 1972 and 1973 the international prices in dollars for agricultural food and non-food products on the world market increased by approximately 50 per cent, whereas the comparable rise for all commodities traded internationally was 20 per cent. See United Nations, *Monthly Bulletin of Statistics*, September 1974, pp. xiv and xv.

[108] To this should be added a factor of no small importance, namely, the possibility, often put into practice, of indulging in contraband trade with neighbouring countries, particularly over the extensive frontiers which this country shares with Venezuela and Ecuador.

[109] This calculation is based on 1972 estimates prepared by the Fundeción pare le Educación Superior y el Desarrollo (FEDESARROLLO) (see *Coyuntura económica*, vol. II, No. 4, pp. 2–3).

Table 89. Colombia: production, imports, and price fluctuations of selected agricultural products

	1971 (thousands of tons)		*1972 (thousands of tons)*		*1973 (thousands of tons)*		*1972/1973*		
	Production	*Imports*	*Production*	*Imports*	*Production*	*Imports*	*Percentage price variation in dollars*	*Percentage price variation in dollars per exchange rate*	*Estimate of percentage variation in domestic prices*
1. Barley . . .	112	68	106	12	94	15	–	–	
2. Beans . . .	45	6	44	–	46	–	–	–	
3. Maize . . .	915	47	872	21	824	94	95	110	80
4. Sorghum . .	219	–	238	21	398	37	103	119	–
5. Soya . . .	83	23	102	–	99	14	153[a]	200[a]	–
6. Wheat . . .	49	385	79	416	91	249	113	130	70

SOURCES: ECLA, on the basis of DANE and National Planning Department statistics.
[a] Variation between 1971 and 1973.

In addition to this general trend, the case of wheat and, to a lesser extent, that of maize deserve special consideration. As can be seen from table 89, during 1973 substantial quantities of these two products were imported, particularly wheat.[110] The average prices in dollars paid by Colombia for wheat increased by 113 per cent while those for maize increased by 95 per cent, representing increases of 130 and 110 per cent respectively in terms of national currency. At the same time the domestic price of wheat rose by approximately 70 per cent and that of maize by 80 per cent, so that, in view of the widespread consumption of these products, this may have had an inflationary impact—and may have caused a cutback in the basic consumption of the country—not fully reflected in the more general calculations presented earlier.

Similarly, the difference between the variation in the international price of wheat and the domestic price resulted in losses for the Instituto de Mercadeo Agropecuario (IDEMA).[111] This form of subsidy—which was intended to be temporary—was financed by loans granted to IDEMA by the Banco de la República. It is estimated that these funds brought about an additional expansion of the quantity of money of approximately 2 per cent.[112]

Lastly, it is worth commenting on events in connexion with edible oils. Although the country imported a limited quantity of inputs for the manufacture of this product in 1973, the sharp rise in the international price of soya and other oilseeds was a factor which exercised a decisive influence on the increase of approximately 75 per cent in its price on the domestic market during the year.

– *The effect of the price increases of export products.* The sharp increase in international prices for agricultural products also exercises obvious inflationary pressures on the Colombian economy, because of the relative openness and flexibility of the foreign trade operations of the country. Thus, when a price differential is established in favour of the export sales of a large proportion of national production, domestic prices tend to rise on a par with international ones, thus countering the attraction of the foreign market vis-à-vis the domestic one and avoiding the generation of internal problems of short supply.

This trend was strengthened for two additional reasons. Firstly, since a high proportion of the country's exports consists of products of agricultural origin, national exporters are quite familiar with the international markets for those products, and the opportunities open to them for expanding agricultural exports significantly and promptly are excellent. Secondly, no important economic policy measures were adopted in 1973 and 1974, nor in earlier periods, to reduce the price differential which was building up in favour of foreign sales.

In 1973 and 1974 the dollar unit value of exports of goods increased by 27.4 and 16.1 per cent respectively, taken together with the variations in the main rate of exchange, gave increases of 38 and 28 per cent in the unit values expressed in terms of national currency. These rates were double the increase in 1972 and provide one of the first indications of the inflationary pressure stemming from this area.

Furthermore, if coffee is excluded from the calculation of the unit value of exports in terms of national currency, it can be seen that in 1973 and 1974 the average increase was approximately 50 per cent in contrast to a comparable change of less than 10 per cent in 1972. This sharp change of pace had a most powerful impact on the domestic prices of certain agricultural products.

In this connexion, reference may be made to some opposite examples of the way prices developed in 1972 and 1973. Firstly, the wholesale prices of meat increased by approximately 45 per cent, the increase being even higher for quality meats. Secondly, increases in domestic prices for other export products such as tobacco,[113] were higher than 40 per cent. Lastly, as regards cotton, prices for the inland crop increased by 40 per cent during the year, and it was agreed that part of the coastal crop would be purchased at international prices, which increased by more than 100 per cent between 1972 and 1973.[114]

(iii) *Wages and salaries.* In general, the available information does not seem to indicate that the evolution of wages and salaries was an important factor in the inflation which took place in the three-year period 1972–1974, and, in particular, in the acceleration which occurred in the last two years considered.

In April 1972, minimum urban and rural wages

[110] This cereal is the only agricultural product traditionally imported by Colombia in significant quantities.

[111] This is a decentralized official institution which markets both national and imported agricultural products.

[112] See table 88. It is thought that in 1973 the cost of the subsidy may have exceeded 500 million pesos, notwithstanding the fact that domestic reserves of the cereal built up at the end of 1972 made it possible for 1973 imports to be lower than usual.

[113] See DANE, *Boletín Mensual de estadística,* September 1974, p. 82.

[114] See FEDESARROLLO, *Coyuntura económica,* April 1974, p. 55.

were adjusted by an average of approximately 30 per cent—the first increase since August 1969. However, in 1972 the weighted nominal wage increased by only 10.6 per cent, which meant a further drop in real wages of more than 3 per cent compared with 1971 (see table 86).

On the other hand, some data which it was possible to collect[115] on the evolution of industrial wages in 1972-1974 show that the nominal increases in the manufacturing sector—which is probably one of the productive activities where conditions are more favourable to wage adjustments—amounted to 14.8 per cent in 1972, and 20 per cent in 1973 and 13 per cent in 1974. These figures imply that real wages in industry showed practically no change in 1972, while they decreased by about 5 per cent between 1972 and 1974.

Lastly, new minimum urban and rural wages were established in November 1974. The adjustments approved ranged from 33 to 48 per cent, and averaged around 40 per cent. Naturally, the inflationary repercussions of this measure were not reflected in the 1974 price indexes.

D. Main features of anti-inflationary policy

1. *General remarks*

The emphasis laid on anti-inflationary policy in the period 1971-1974 was of course closely linked to the trends followed by price indexes and to the interpretations placed on the main factors that affected the inflationary process, especially as the foreign trade situation fluctuated. This meant, in practice, that concern for the problem of inflation grew steadily throughout the period and that an even-higher priority was accorded to the formulation and implementation of stabilization measures. Influence in this direction was also exerted by the fact—to which atttention has already been drawn—that the acceleration of price movements in 1971 was due, in essence, to temporary supply difficulties in respect of certain agricultural commodities.

The analysis of anti-inflationary policy presented in this section relates to what took place in 1972-1973 and only part of 1974, owing to the fact that August 1974 marked the beginning of a period of government by a new administration and that in the next few months, particularly October, a number of measures were adopted which meant the introduction of some important changes in the stabilization strategy implemented by the previous administration. Moreover, emphasis is placed on the analysis of events in 1973 because more quantitative and qualitative data were available for that year, which permitted a more far-reaching study of the policy measures adopted in the face of the acceleration of inflation during the period concerned.

It should be noted that the gathering momentum of the inflationary process and the increasing priority assigned to measures for coping with it did not lead to the formulation of a single anti-inflationary programme as such, in which the action to be taken in the various fields of economic policy was established on a global basis and with some degree of precision. Thus, what is observable during the period is, in the main, the gradual emergence of several stabilization measures which were enacted and co-ordinated as time went by, primarily in the light of the course followed by Colombia's foreign trade.

What, then, were the main objectives, explicit or undeclared, of the stabilization measures applied?

The paramount aim was, of course, to keep the rate of inflation within reasonable limits, which implied adhering fairly closely to the rate at which prices had risen in 1967-1970, and, specifically, ensuring that price increases did not exceed 10 per cent per annum.[116]

Concurrently, steps were taken to make stabilization policy compatible with the pursuit of other objectives. Outstanding among these were the growth of the domestic product at an annual rate of not less than 7 per cent and a gradual improvement in the existing state of affairs in respect of urban employment, rural levels of living and income distribution.

This definition of multiple objectives, although relatively general, should be assessed at its true value, inasmuch as it significantly influenced the authorities' choice of alternative stabilization policies. For example, it may be said at the outset that the measures applied were invariably prompted by the intention of mitigating the inflationary process or keeping it within reasonable or "functional" bounds, and not by any idea of abruptly curbing or completely eliminating the upward pressures that made themselves felt.

2. *Stabilization measures*

Following much the same arrangement as for the interpretative analysis of the latest inflationary

[115] Calculated by FEDESARROLLO on the basis of direct surveys carried out in 50 industrial enterprises (see *Coyuntura económica*, April 1973 and 1974).

[116] However, already in the course of 1974 it was throught that in view of the spread and intensification of world inflation this target might be too ambitious, and that a rise in prices of about 15 per cent annually would be admissible.

trends, the study and evaluation of stabilization policy can be based on classification of the measures adopted in two broad and, of course, interdependent groups. Thus, on the one hand, it will be worth while to take a look at what happened in the monetary and financial fields, while, on the other, the action taken in the supplies, prices and income area will be reviewed.

As a result of this classification by functions rather than by types of measures, relevant aspects of certain policies may be considered under the heads defined; one of the clearest cases in point is foreign trade policy, with reference to the handling of international reserves in the one context, and to regulations primarily relating to exchange rates in the other.

(a) *The monetary-financial field*

In the stabilization policy of the period paramount importance was assigned to the handling of monetary-financial variables, and especially to the control of the annual increase in the money supply. An attempt was made to programme the evolution of the means of payment and of other financial assets on lines which in turn would allow the liquidity of the economy to expand as far as was compatible with the anti-inflationary and development objectives already defined.

In quantitative terms, the basic target was to confine the annual rate of expansion of the means of payment to approximately 17 per cent. According to Planning Department experts, this increase was felt to be compatible with an annual growth rate of 7 per cent for the gross domestic product, and a price rise not exceeding 10 per cent per annum (see footnote 116).

There are a number of justifications for the preponderance of such an aim by which the authorities were largely swayed in deciding upon their programmes of action.

In the first place, decisive weight was carried by the fact that the primarily "monetaristic" explanation of price variations appeared reasonable to a significant group of government technical experts. Furthermore, the management of monetary policy had a certain amount of tradition behind it, and institutional conditions in its favour—in particular the existence and co-ordinated operation of the Monetary Board (Junta Monetaria) and the Banco de la República.

Secondly, the assignment of priority to monetary-financial policy stemmed from a somewhat cautious evaluation of the possibilities of using other forms of economic policy, including, for example, more direct and generalized State action through fiscal policy and/or income and price policies. This approach implied, from other standpoints, that the end in view was to regulate price movements without bringing about, at the same time, changes in the system of prices for goods and services and for the factors of production that were significantly different from those determined by market forces.

Lastly, an evaluation of the probabilities that an essentially monetary policy will be successful in controlling inflation may be based on another consideration. Price increases had quickened their pace, but without going too far or getting completely out of hand; and this suggests that the comparative absence of automatic adjustability mechanisms in the Colombian economic system detracts from the self-propelling power of the inflationary process. In Colombia, for example, wages, taxes and rentals are not automatically adjustable; and it may be added that only on the exchange front and in parts of the machinery for tapping savings are some procedures found which do display the characteristic of adjustability. Undoubtedly, the fewer the mechanisms which set up a direct and automatic chain reaction among the various price movements that may be taking place, the greater the possibility of making relatively easy and effective use of monetary instruments.

However, notwithstanding the precision with which the ceiling for the increase of the means of payment was set, and the grounds there were for according priority to the monetary-financial variables and assuming their potential efficacy, a study of the measures adopted in 1972 and 1973, though not in 1974, reveals that the action taken to control the actual sources of the expansion of the money supply was relatively limited in scope and drive. In contrast, most of the measures enacted were designed to reduce the multiplier effect on the means of payment of an increase in the direct issue of currency.

(i) *Measures relating to fiscal policy and management of international reserves.* It will be recalled that the factor which decisively expedited the growth of the money supply between 1972 and 1973 was the size of the government deficit and the way in which it was financed through external credits, at a time when foreign trade trends had brought about a substantial reduction of the balance-of-payments deficit on current account. This led to an increase in international reserves and a parallel and equivalent expansion of the direct issue of national currency printed by the Banco de la República, since in practice, that institution absorbed the National Government's and the public sector's sales of foreign exchange deriving from the use of external credits.

In other words, the possibility of controlling the expansion of the means of payment at the source depended essentially upon the measures

relating to fiscal policy and to the manipulation of international reserves which could feasibly be put into effect.

Faced with this situation, fiscal policy did little to reduce the government deficit or to change the method of financing it, which would have been the best way of lessening dependence on foreign credit.

Thus, in the first place, it was not until the end of 1974 that any really important moves were made—particularly in the field of taxation—to raise or maintain the share of the Government's current income in the gross domestic product; on the contrary, between 1971 and 1973 the proportion it represented substantially declined, although the improvement in the economic growth rate and especially in foreign trade might have facilitated a possible increase in taxation. Secondly, where public expenditure was concerned, only in 1973 was some check imposed on its rapid rate of growth, mainly through severe restriction of fiscal and public investment.

Nor did any new provisions for dealing with the problem emerge in other areas of fiscal policy. With regard to inflows of capital in national currency, it has previously been shown that no net internal borrowing took place during the period. At the same time, in order to tap capital resources, the Government continued to issue bonds of the traditional non-adjustable type, which became less and less attractive as the rate of inflation rose and as other competing instruments came to the fore, in particular the Constant Purchasing Power Units (Unidades de Poder Adquisitivo Constante—UPAC), which, in contrast, were adjustable. However, in the second half of 1974 the monetary correction for UPACs was limited to 20 per cent annually.

As far as capital inflows in foreign currency were concerned, not only was the preceding years' rate of net external borrowing doubled, but also foreign commercial loans were contracted on a considerable scale (over 60 million dollars yearly in 1972 and 1973). These were used almost in their entirety to finance expenditure in national currency.

Concomitantly, the policy applied in respect of management of international reserves was unsuccessful, or insufficiently energetic, in slowing down the rate of accumulation of reserves and/or mitigating its monetary effects.

As has already been noted, it was only in 1973 that the gradual liberalization of import regulations, started in 1972, was stepped up and began to show results, which were fully evident in 1974. In contrast, between 1971 and 1972 total imports of goods decreased in absolute terms by over 60 million dollars, in contradiction with the anti-inflationary measures that were being taken. It may be added that in 1972 reserves would not have increased as they did by 120 million dollars if in that year imports in terms of dollars at current prices had exceeded the 1971 figure by 5 per cent.

In the field of exports, the possibilities for action posed a more complex question, because—naturally enough—it was very difficult, and hardly advisable for the authorities, to launch a programme of reduction of export incentives, at a time when the original basic problem largely derived from public-sector financing, and when such a reduction would have been at variance with the export promotion strategy that had been pursued for several years past. Accordingly, up to August 1974, no major changes were introduced in the system of incentives.[117] The sole exception was that the practice of granting advances to exporters was done away with; and even so, this measure was offset by the allocation of additional resources to the Export Promotion Fund (Fondo de Promoción de Exportaciones—PROEXPO).

An additional point of interest is that a conceptual alternative which was not mooted or which never took concrete shape might have been adopted for the purpose of cushioning or rather regulating the immediate impact of expanding exports on liquidity. When exporters are profiting by increasingly favourable circumstances—inasmuch as they are simultaneously receiving the benefits deriving not only from larger export volumes and rising international prices but also from the continuance of the incentives they enjoy—it would seem fairly logical that in certain cases there should be some curtailment of the liquidity of the national currency resources they obtain from the sale of their foreign exchange earnings. In other words, certain operational formulae might be established which would provide, for example, for a proportion of the foreign exchange liquidated by exporters to be paid for not in money but in government securities of some sort, with specific terms in respect of redemption periods, adjustability and interest rates.[118]

To pass on to other questions related to

[117] It is true that other measures were adopted which did affect exports, such as, for example, the establishment of certain prohibitions and of export quotas. They will be discussed later, however, inasmuch as they were more directly prompted by price and supply problems.

[118] It seems out of place in the present report to go into much detail on this point, but it may be suggested that the proportion not payable in money could be increased monthly or quarterly in accordance with the gradual expansion—for the country as a whole or, alternatively, for some exporters of staple exports—of the monthly or quarterly amount of export earnings.

reserves policy, it may be noted that during the period the monetary authorities were not empowered to influence the public sector's rate of external borrowing, even where commercial loans were concerned. On the other hand, they did take action with regard to foreign credits obtained by the private sector; so much so, that in 1973 the Monetary Board suspended the authorization of private persons to contract external loans.[119]

(ii) *Monetary and savings policy measures.* Essentially, it fell to monetary and savings policy to abate the multiplier effect on the means of payment produced by the central banks direct issue of currency. It should be borne in mind that in 1972 and 1973 this issue increased relatively fast (by 22.1 per cent and 30.7 per cent, respectively, as compared with less than 10 per cent in 1970 and 1971).

From the data available it can be seen that the task in question was successfully performed in 1973. In 1971 and 1972, as well as in 1970, the percentage increases in the means of payment were about one fourth higher than the corresponding increases in the direct issue, whereas in 1973 the changes in these two variables were the same in relative terms. From a different point of view, the (marginal) multiplier of the Banco de la República issue decreased from 1.37 in 1971 to 1.16 in 1973.[120]

This reduction was achieved through the monetary policy measures brought into force in the course of 1973. Among the main provisions adopted, mention may be made of the following:

– During the year two increases in the Bank's legal cash reserves were approved, with the result that the average rate for the system rose from 31.5 per cent in 1972 to 36.1 per cent in 1973;[121]

– The policy of fixing ceilings, at quarterly intervals, for the growth of bank credits, which had been initiated early in 1972, was continued. The ceiling was set at 15 per cent for the whole of the year, and was closely conformed to in the case of credits subject to control. The more rapid growth of other bank loans that were not directly controllable, however, boosted internal credit to the private sector by about 20 per cent;

– A new system of prepayments was established for import operations, under which importers were obliged to deposit 35 per cent of the national currency equivalent of the value of the goods to be imported. In practice, this mechanism completely cancelled out the expansionist effect produced by the gradual suppression of the system of prior import deposits which had begun a couple of years before;

– Two additional provisions were adopted, which were described earlier. On the one hand, external borrowing on the part of private persons was suspended–and steps were even taken to encourage the return of loans already brought into the country–and, on the other hand, advances were no longer granted to exporters.

No other significant changes were introduced in monetary policy. For example, the bank system continued to extend its credits at nominal and relatively stable rates of interest, which worked out as negative after the effect of inflation had been discounted.[122] This meant, in effect, that demand for credit swelled, and became increasingly hard to meet with efficacy, as the higher rate at which prices rose enhanced the attractions of obtaining and using bank loans.

Savings policy underwent a reform which has already been discussed. The monetary adjustment mechanism was introduced with the establishment of a savings and loan system for housing purposes and of the UPAC, whereby large sums were channelled into the said system. A high proportion of these resources was used during the same period for the financing of urban construction.

The rest of the machinery for tapping savings, however, continued to operate on the basis of traditional-type instruments, with negative real interest rates–despite the raising of some of the nominal rates–with no clauses providing the monetary adjustment or automatic adjustability, and with a low degree of short-term liquidity. Even the Banco de la República itself held no securities of which the terms were such as to facilitate the transaction of open-market operations.

In short, savings policy as a whole probably made but a modest contribution to the task of slowing down the rate of expansion of the means of payment. Even the resources that were channelled into the savings and loan system for housing purposes may to some extent have reflected a reorientation of financial savings rather than a net addition to them.

[119] See Banco de la República, *Informe Anual del Gerente a la Junta Directiva* (*Annual Report of the Manager to the Board of Governors*), 1973, p. 46.

[120] To make this calculation the absolute variations in the money supply are related with those of the Banco de la República issue.

[121] See Banco de la República, op. cit., p. 157. Incidentally, between 1970 and 1972 the average rate in question had dropped from 35 per cent to 31.5 per cent. In other words, the trend it followed contrasted with the speeding-up of the inflationary process which took place over that period.

[122] Throughout the whole of the period 1970–1973, the Banco de la República's rediscount rate was 14 per cent per annum; and not until the beginning of 1974 was it raised to 16 per cent.

(b) *Policies for dealing with supply, price and income problems*

The economic policy measures adopted to deal with problems in this area may be grouped under three heads: (i) exchange policy; (ii) supplies and prices policy; (iii) income policy.

(i) *Exchange policy*. Here the anti-inflationary role played by exchange measures proper should be considered since other aspects of foreign trade policy will be examined in conjunction with supplies and prices policy.

A key feature of exchange policy derived from the application of a system of periodic "mini-devaluations", discounting the internal inflation in the United States, which enabled the "real" peso value of the principal exchange rate to be kept relatively stable between 1970-1974. Indeed, between 1971 and 1974 this value depreciated by 5 per cent, which reflects a certain deliberately programmed slowness of pace in the average devaluations in 1972-1974 (see table 80).

It was decided that the policy of mini-devaluations initiated in 1967 should be maintained, since this course was thought to be consistent with the "functionalist" conception of anti-inflationary strategy and with other development policy objectives, especially in the fields of allocation of resources and export promotion. Moreover, Colombia's own experience in the operation of exchange rates with pegged foreign currency values afforded additional evidence of the risks of possible exchange "explosions" and of other undesirable secondary effects which may be precipitated by a policy of this type.

It was also considered that by discounting the internal inflation in the United States[123] it would be possible to offset, at least in part, the pressure on domestic prices exerted by the increase in the unit value of imports in terms of dollars. The pace of this increase, however, far outstripped that of inflation in the United States,[124] especially in 1973 and 1974, in consequence of two additional facts. In the first place, more than one third of Colombia's imports come from industrialized countries whose currencies have undergone revaluations in relation to the dollar since 1971 and this must have led to a more than average increase in the dollar price of the goods imported. Secondly, although it has not been possible to verify the point in the present study, Colombian imports from the dollar area probably showed price increases higher than those reflected, on average, in the rate of inflation in the United States economy.

Another exchange measure which may have had net anti-inflationary effects in 1972-1974—reversing the 1971 position—was the stabilization of the petroleum exchange rate, which was held firm at 20 pesos to the dollar.

Nevertheless, this policy generates several problems which cast some doubt on its advisability. For example, it involves subsidizing domestic consumption of petroleum and its derivatives, notwithstanding that in recent years domestic production of crude oil has been rapidly declining, and it is forecast that in the next few years the country will become a net importer of petroleum. Moreover, a fixed exchange rate is at variance with a flexible exchange policy, and is bound, in the long run, as the peso values of the principal exchange rate and the petroleum rate move further apart, to lead to maxi-devaluations of the exchange rate applied to imports of crude oil to be refined in Colombia.

As regards other measures that affected import flows and costs, mention has already been made of the progressive liberalization which began in 1972 and led to a substantial increase in the current value of imports in 1973 and 1974.

As a complementary measure, to bring down the domestic price of imported goods during 1972, and especially in the course of 1973, the customs tariffs for several import products were reduced. This reduction, however, was selective and limited—and, therefore, must have had only a restricted anti-inflationary effect—because the average level of the Colombian customs tariff is relatively low[125] (about 40 per cent) and, furthermore, because no significant duties were payable on imported foods.

Likewise with the aim of making imports cheaper, throughout the period 1971-1973 the system of prior import deposits was gradually being abolished. In 1973, however, as noted above, the concern aroused by the rapid expansion of the means of payment led to the setting-up of the import prepayment mechanism. In global terms, therefore, at least in 1973, this line of action must have done virtually nothing to lower the cost of imports.[126] Accordingly, the case under review

[123] The implicit deflator of the gross domestic product of the United States increased by 4.7 per cent in 1971; by 3.1 per cent in 1972; by approximately 10 per cent in 1973 and 15 per cent in 1974; in all, that is, by 36 per cent between 1970 and 1974.

[124] The unit value of imports in dollars rose by 58 per cent between 1970 and 1974 and by 18.3 and 21.4 per cent, respectively, in the years 1973 and 1974 taken by themselves.

[125] Especially in comparison with the tariff in force in other countries signatories to the Cartagena Agreement.

[126] At the end of 1972 the amount represented by prior import deposits was about 2,400 million pesos, while by the end of 1973 the cumulative total of prior deposits and prepayments was approximately 3,000 million (500 million in deposits and 2,500 million in prepayments).

clearly exemplifies the mutually contradictory effects that may be produced by the adoption of measures pertaining to different branches of economic policy, in this instance to monetary policy and to foreign trade policy.

(ii) *Supplies and prices policy*. The anti-inflationary policy pursued did not include the more or less generalized adoption of various forms of direct control of domestic prices. In this connexion it should be repeated that the key-notes of the stabilization programme were, on the one hand, the control and scheduling of the growth of monetary and financial variables, and, on the other, the promotion of the normal development of production and supplies, for which purpose the correct and flexible operation of the price mechanism was of vital importance.

But, within this general context, during the period considered, and especially in 1973 and 1974, a number of more direct measures of supplies and prices policy were brought into operation.

In the first place, in those cases in which domestic production of certain foods fell short of requirements, the State undertook–through the Agricultural Marketing Institute (Instituto de Mercadeo Agrícola–IDEMA)–the importing and marketing of the volumes needed to satisfy demand. In 1973, for example, besides importing about 50 million dollars' worth of wheat–a product traditionally in short supply in Colombia–the authorities allocated a similar sum to imports of maize, barley, soya bean and cocoa, in view of the sudden reductions that took place in domestic production of those commodities.

Although between 1972 and 1973 world market dollar prices of these agricultural commodities rose, on an average, by about 100 per cent, it was only in the case of wheat–owing to the large scale on which it was imported and the diffused effect that an increase in wheat prices produces–that the decision was taken definitely to subsidize domestic wheat prices, although only partially, a step which, as has been shown, caused IDEMA heavy operational losses. It is interesting to note that this trend changed radically in the second half of 1974. In other cases, the authorities preferred to allow domestic prices greater freedom of movement, taking advantage of the fact that imports were equivalent to a relatively low proportion of domestic production.

Secondly, in face of the rapid boom in the world prices of certain agricultural commodities exported by Colombia but widely consumed at home, the aim of the policy adopted was to prevent domestic prices of these goods from rising suddenly in the same proportion as world prices, and/or to forestall the generation of internal shortage problems. Thus, the upward trend of the domestic prices of a few selected products was regulated fairly flexibly, by limiting the volumes exported. The most representative examples of this tendency were constituted by the measures adopted in 1973–1974 to establish beef export quotas, and by the total suspension of sugar sales abroad.

In any event, this is a complex field, in which the Colombian authorities themselves, rather than taking final decisions, settled for *ad hoc* solutions to the various problems arising. Thus, in practice the principles of freedom to export and of flexibility in respect of prices and production were counterpoised by more immediate needs to safeguard domestic supplies and to smooth out sudden violent upswings in the prices of agricultural commodities with a high incidence on the population's basic consumption.[127]

An alternative measure, which was not adopted but which was discussed by some sectors in Colombia, might have served the purpose of reducing the price differential in favour of exports–besides producing other secondary effects–when world prices rose steeply. It could have consisted in the establishment of export duties at rates varying in accordance with the levels reached by international prices.[128] A policy of this type may, of course, have undesirable secondary effects–such as, for example, increased contraband in dutiable goods–but from the standpoints of the more efficient operation of the economic system and of equitable taxation, its application may be advisable, especially when a favourable balance-of-payments position makes it permissible to run

[127] On this subject, the following opinion has been expressed: "It is reasonable that exports of goods which are in short supply in a given country, and in some cases in the world, should be prohibited, especially where the goods concerned, on account of their high costs, or because of natural disadvantages, or for any other reason, are unfitted to compete on the world market either today or in the foreseeable future. There are more than sufficient grounds for applying this norm to subsidized domestic consumer goods or goods whose processing is significantly dependent upon these, since in such cases the subsidy would become more burdensome without implying immediate or even remote benefits for export policy. Of course, with exceptions where advisable, the general principle of freedom to export should continue to prevail, since its application has produced very satisfactory results. This is particularly true of articles whose incidence on vital consumption is not great." See Banco de la República, op. cit., p. 61.

[128] A variant of this formula may consist in the progressive elimination of export subsidies, which was done in the second half of 1974. In Colombia, however, the so-called Certificates of Drawback (Certificada de Abono Tributario–CAT) are of virtually no importance for exports of agricultural commodities as such; generally speaking, they are subsidies that have been vigorously operative in the case of exports of manufactured goods.

certain risks, and when, at the same time, it is necessary to augment the savings generated by the Government.

Only the government authorities, however, can evaluate as a whole the merits and demerits of the adoption of provisions such as that suggested.[129] Furthermore, any application of differential export taxes should be co-ordinated—and might even conflict—with other alternative measures, in particular with the possible mechanism (suggested above) for programming the liquidity of export earnings in accordance with the periodic fluctuations in their amount.

Thirdly, another important line of action in respect of prices and supplies pertained to IDEMA's normal function of marketing a number of agricultural commodities. This function included the establishment of support prices, at which the Institute regularly bought considerable quantities of agricultural commodities, and which were altered periodically as internal and external circumstances rendered it advisable.

Fourthly, it should be pointed out that the domestic price of coffee was also subject to internal regulation, as agreed upon between the Government and the National Coffee-Growers' Federation (Federación Nacional de Cafeteros). Thus, it was raised periodically, while at the same time this measure was co-ordinated—in the light of changes in the world market situation—with variations in other components of coffee policy. For example, between the beginning of 1971 and 1973 the dollar price of coffee on the world market rose by about 45 per cent, while the variation in the domestic price in national currency was approximately 50 per cent.[130]

It is worth while to add that the whole coffee policy pursued reduced the potential anti-stabilization effects that might have been produced by this export activity, especially in contrast with what happened in the case of a substantial proportion of non-traditional exports.

In addition to the fixing of the internal sales price, coffee was subject to other provisions, among which the following may be mentioned: (*a*) the regular stipulation of a reference price which closely followed world market coffee quotations; (*b*) the application of a special exchange rate for the liquidation of export earnings which, as indicated above, was about 20 per cent lower than the principal exchange rate; and (*c*) regulation of the quantities that could be exported, through the periodic adjustment of the "coffee retention quota". Between mid-1972 and mid-1973—which was the period when world coffee prices soared most rapidly—the proportion of the quantity exported which was handed over by exporters to the National Coffee-Growers' Federation expanded from 23 per cent to 35 per cent. This led to a substantial increase in the stocks of coffee maintained in Colombia by the National Coffee Fund (Fondo Nacional del Café).

To illustrate the joint effect of the measures described, it is worth noting that according to World Bank estimates, between 1972 and 1973 the coffee-producers' net relative share in the world market sales price of coffee dropped from 40 per cent to 33 per cent.[131]

Lastly, with regard to price controls for other products, especially manufactures, the functions fulfilled by the Office of the Superintendent of Production and Prices (Superintendencia de Producción y Precios) deserve special mention. This agency was empowered throughout the period to monitor price trends, which in practice implied that after price increases had taken place studies could be undertaken and action initiated on the basis of their findings, with the aim of reconsidering the increases in question and/or deciding upon certain civil sanctions. Unfortunately, it is not easy to assess how far the application of such measures proved efficacious.

(iii) *Income policy*. As far as wage policy was concerned, free negotiation between employers and workers was the general rule. To begin with, as already noted, during the period under study there was no system of annual adjustment linked to price variations which covered broad sectors of the population. Only at the beginning of 1972 and the end of 1974 were increases in minimum urban and rural wages decided upon, on the lines and with the effects reviewed above.

Moreover, in the private sector the participation of the trade union organizations in wage negotiations was relatively small. It is estimated that about 30 per cent of the working population was grouped in trade unions and operated on the basis of discussion of lists of wage petitions. For the rest of the workers, much of the process of negotiating wage increases is still split up among small units, which often have little information and scanty power to secure wage adjustments that keep pace with the rise in prices.

Nor did any systems of periodic and automatic increases operate in the case of public-sector

[129] Similarly, instead of resorting to taxation, some governments may prefer a management of exchange policy based definitely on differential rates. Argentina's experience in the years 1972-1974 largely reflects the application of this principle.

[130] See Banco de la República, op. cit., pp. 71-73.

[131] See IBRD Report 138-CO, op. cit., p. 20.

employees. What has been ascertained, however, is that in 1972 and 1973 their salaries were raised through several piecemeal decisions, by a yearly average of over 10 per cent, which must have implied that in real terms their remunerations were reduced.

In other fields of income policy, no specific anti-inflationary measures are known to have been adopted. For example, no significant provisions were brought into force to control the growth of the profits of enterprises (apart from the above-mentioned operation of the Office of the Superintendent of Production and Prices) and that of rentals.

4. COSTA RICA

A. INTRODUCTORY NOTE

As far as the different forms and degrees of inflation in Latin America in recent years are concerned, the case of Costa Rica is both interesting and illustrative. Its inflationary problem has very particular features, as regards its origin and evolution and later increase in pace.

The contrast between the long period of stability which characterized Costa Rica in the past, and the inflation of recent years constitutes one of the most outstanding peculiarities. The level and structure of the external trade of the country and the inflationary pressures imported combined with other factors of inflation to give rise to a very singular process.

Lastly, the features of its economic, political and social systems make up a picture in which inflation acquires fairly heterodox implications. It may be recalled that this is a country with a very homogenous population whose peasants, generally speaking, are not living at subsistence level. The education and health indexes are the highest in the region and income distribution does not show the same degree of disparity as the majority of Latin American countries. The lack of armed forces not only affects the assigning of public resources, but also contributes to a fair measure of generosity in social development.

B. RECENT ECONOMIC TRENDS

Generally speaking, the economic activity of Costa Rica has shown considerable fluctuations over the last three years. It may be seen from different indicators that the cyclical movements which have been typical of this economy would appear to be continuing to function. It should be mentioned that this type of variation is not reproduced simultaneously in all the macroeconomic variables; some action taken by the State, and some phenomena affecting the country's external sector, have changed the characteristic uniformity of the cycles.

An over-all analysis shows that the dynamism present in the economy of Costa Rica in the 1960s may basically be attributed to such factors as its entry into the Central American Common Market, the evolution of world markets in certain agricultural products, the growth of public spending and the inflow of foreign capital. The combined action of these factors produced a decided expansion of the economy, despite the low price of coffee and the agricultural problems caused by the eruptions of the Irazú volcano.[132]

The explanation of the drop in growth rates in the period 1971-1974 would appear to lie in modifications and a different combination of the above-mentioned factors. An examination of each of them shows its direct connexion with the external sector, which explains the great vulnerability of the economy to fluctuations in the international markets. It is thus possible to see from the analysis of the external sector the conditions and restrictions which affect economic activity in Costa Rica. It would therefore seem appropriate to begin the description of the economy as a whole during the four-year period 1971-1974 by pointing out the main movements in external trade and in Costa Rica's international financial relations. Once the most important events in this field have been identified, the evolution of total supply and demand and the structure of the product will be described. The description of the most important phenomena in this context will be useful for the subsequent interpretation of inflation in Costa Rica and the economic policy actions connected with it.

1. *The external sector*

The influence of this sector in the economy of Costa Rica is doubly important. It consists of a core of activities directly involving a significant share of the functions of production and distribution. Unlike other countries, it is not a mere supplier and receiver of foreign exchange; the structure of its exports, in which agricultural items predominate, is a basic feature of this economy. The high export and import coefficients of Costa

[132] See Planning Office, *Plan Nacional de Desarrollo de Costa Rica*, vol. 1, "*Diagnosis*", 1973.

Table 90. Costa Rica: structure of the value of exports
(Millions of dollars at current prices)

Product	*1969*	*Percentages*	*1970*	*Percentages*	*1971*	*Percentages*	*1972*	*Percentages*	*1973*	*Percentages*	*1974*	*Percentages*	*Percentage variation 1970-1974*
Coffee	55.8	29.4	73.1	31.6	59.3	26.3	77.9	27.9	94.0	27.7	125.2	29.1	71.3
Bananas	51.5	27.2	66.8	28.9	64.4	28.4	82.8	29.5	93.3	27.5	93.6	21.8	40.1
Livestock and meat	15.1	8.0	18.0	7.8	20.5	9.1	30.3	10.8	32.7	9.6	31.2	7.2	73.3
Sugar	9.1	4.8	10.1	4.4	12.9	5.7	13.1	4.7	13.6	4.0	14.9	3.5	47.5
Cocoa	7.1	3.7	1.9	0.8	1.5	0.7	3.0	1.0	4.4	1.3	6.0	1.4	215.8
Other agricultural products	10.0	5.3	7.8	3.4	8.5	3.8	9.3	3.3	11.4	3.4	159.0	37.0	159.4
Industrial products	41.0	21.6	53.5	23.1	58.6	26.0	64.5	23.0	89.9	26.5			
Total	*189.6*	*100.0*	*231.2*	*100.0*	*225.3*	*100.0*	*280.9*	*100.0*	*339.3*	*100.0*	*429.9*	*100.0*	*85.9*
Annual percentage variation			21.9		−2.6		24.7		20.8		26.7		

SOURCES: Dirección General de Estadística y Censos and Central Bank of Costa Rica. ECLA estimates for exports of industrial products and other agricultural products in 1969.

Rica reflect a very close link between the performance of the external sector and general economic activity.

On the other hand, the fluctuations in export prices and the persistent increase in import prices have severely affected the normal external trade flows. The fluctuations of the former and the increases in the latter led to awkward balance-of-payments situations, which, in view of the importance of the external sector, affected a large part of economic activity.

(a) *Export trends*

Before going on to describe the evolution of exports and their basic components it should be made very clear that products of agricultural origin are of basic importance in their composition. Three quarters of the value of exports originates in this sector, and exports of coffee and bananas account for more than half. Although exports of industrial products reveal an increasing share in the whole (26.5 per cent in 1973), the predominance of agricultural products is a feature of the structure which it will be necessary to keep in mind both in the analysis of the economy as a whole and in the description of inflation in Costa Rica (see table 90).

The current value of exports of goods underwent significant variations in the three-year period 1971-1973. In fact, after recording a drop of 2.6 per cent in 1971 compared with the previous year, it showed annual increases of 24.7 per cent in 1972, 20.8 per cent in 1973 and 24.3 per cent in 1974 (see table 90). These fluctuations are a result of very uneven variations in the export values of the different products; it may be noted that while there are items which underwent increases of 131.6 per cent in the three-year period described (cocoa, for example), there are others like coffee, which only increased by 28.6 per cent. Variations of this magnitude necessarily subject export activities, and those of the economy as a whole, to ups and downs which affect rates of growth.

The variations in the current values of exports may be explained by movements of consideration in prices and quantities. It may be seen from table 91 that different indexes showed relatively unfavourable changes; apart from the fact that there was a drop of 5 per cent in prices in 1971, the volume increased by a mere 3 per cent, with the result that there was a subsequent reduction in the value exported. These events played an important part in the drop in the rate of general economic activity as from 1971. In 1972 and 1973 the indexes show asynchronisms which prevented a more vigorous growth of the value exported. When, as in 1972, the volume increased significantly, prices rose more slowly; conversely, when prices underwent significant increases, as in 1973, the volume went up less rapidly.

A detailed analysis of the main export products shows more clearly how variations in international prices and in the quantities exported affected the economy of Costa Rica. Tables 92 and 93 contain the above-mentioned information.

Since coffee and bananas are the most important products, not only among exports but also among items of general production, the variations they underwent in the three years 1971-1973 were factors which determined the evolution of the economy. The volume of coffee exported underwent considerable changes—a drop of 7.4 per cent in 1971, an appreciable recovery of 34.6 per cent in 1972, and a further decline of 15.3 per

Table 91. Costa Rica: indexes of exports of goods
(1970 = 100)

	1971	*1972*	*1973*	*1974*
Price index	95	100	120	143
Quantum index . . .	103	119	124	129
Index of export value .	97	119	148	184

SOURCE: ECLA estimates based on official data.

Table 92. Costa Rica: evolution of the volume of agricultural exports

Product	*1970*	*1971*	*1972*	*1973*	*1974*	*Percentage variations 1970-1974*
Coffee (thousands of quintals) . .	1,500	1,390	1,871	1,585	1,965	31.0
Bananas (thousands of stems) . .	29,414	32,859	38,599	42,112	38,820	32.0
Livestock and meat (thousands of kilogrammes)	17,475	18,617	26,131	21,763	23,835	36.4
Sugar (thousands of quintals) . .	1,465	1,807	1,683	2,438	1,592	8.7
Cocoa (thousands of quintals) . .	71	77	132	103	97	36.6

SOURCES: Dirección General de Estadística y Censos and Central Bank of Costa Rica.

Table 93. Costa Rica: evolution of prices of agricultural exports
(*Dollars at current prices*)

Product	*1970*	*1971*	*1972*	*1973*	*1974*
Coffee (per quintal)	48.66	42.67	41.60	59.31	63.70
Banana (per stem)	2.27	1.95	2.15	2.22	2.41
Meat (per kilogramme) . . .	1.03	1.10	1.16	1.50	1.31
Sugar (per quintal)	6.93	7.15	7.78	5.59	9.39
Cocoa (per quintal)	27.30	19.93	22.67	42.44	62.20

SOURCES: Dirección General de Estadística y Censos and Central Bank of Costa Rica.

cent in 1973. Furthermore, in 1971 the price of a quintal of coffee fell by 12.4 per cent and in 1972, when production reached a maximum, the price dropped to a minimum level.[133] The sudden price increase in 1973 coincided with a decline in the production of coffee. In short, price and quantity both played a recessive role in 1971 and offset each other in the next two years, thereby reducing the variations in export values.

As regards bananas, a sustained growth of the volume exported was recorded at an annual average rate of around 13 per cent. Banana prices, however, showed an appreciable decline in 1971 (16 per cent), and the recovery of the next two years did not bring the price back up to 1970 levels.

The significance of the year 1971, a very critical period which had a decisive influence on the economic performance of the country at a later date, should not be lost sight of. Many of the problems faced by the economy of Costa Rica were due to this decline, from the effects of which an open economy could hardly escape.

As far as exports of meat and sugar are concerned, it should be mentioned that a persistent increase in prices was not always accompanied by similar increases in the volume exported. Livestock and meat showed a decrease of 17 per cent in 1973, and sugar a decline of 7 per cent in 1972, further aggravated by a drop of 22 per cent in price the following year.

Mention should be made of the increase in the export values of industrial products; these rose by around 150 per cent between 1970 and 1974, which meant that their share increased from 23 to 37 per cent in that period. Despite this increased diversification, however, the importance of export products of agricultural origin which are affected by the variations in prices and quantities has a decisive influence on the country's vulnerable external sector.

[133] As will be understood, the increase in production did not affect price changes, because of the small share of Costa Rican supply in the world market.

(b) *The performance of imports*

It is worth repeating that the economy of Costa Rica is strongly conditioned by imported supplies. The import coefficient which reached values of between 32 and 35 per cent during the period 1971-1974 is an indicator which needs no further comment. In an economy as open as this the evolution of the actual material flows of imports and their financial counterparts have a considerable influence.

The current value of imports showed sharp increases in the early 1970s (see table 94). The figures for 1973 and 1974, when the growth rate was 18.6 and 50 per cent, respectively, are particularly striking. The performance of the components, however, indicates that these increases in value are largely due to the increase in the prices of imported products and only a very small proportion can be attributed to increases in the quantities imported, except in 1974. In fact, the increase in the pace of the price rises is patent: 3 per cent in 1971, 8 per cent in 1972, 15 per cent in 1973 and 31 per cent in 1974; on the other hand, the volume, following an increase of 7 per cent in 1971, decreased by around 1 per cent in 1972, showed a slight increase of around 3 per cent in 1973, and rose by 15 per cent in 1974. In other words, the financial counterparts in the form of payments abroad have increased much more rapidly than the actual physical entry of foreign products. Once again, the external sector, and this time through imports, is showing its influence and its adverse effects on the economy of Costa Rica.

Table 94. Costa Rica: indexes of imports of goods
(*1970 = 100*)

	1971	*1972*	*1973*	*1974*
Price index	103	111	128	168
Quantum index . . .	107	106	109	125
Index of import value .	110	118	140	210

SOURCE: ECLA estimates based on official data.

An analysis of the structure of imports confirms the foregoing considerations. The important influence of raw materials and capital goods and their increasing share in total imports may be seen in table 95. Imports of consumer goods, however, show fluctuations with a slight tendency to increase and a relatively decreasing share in the total, although they do in any case represent fairly considerable levels. Industry and construction are the sectors which depend most heavily on imported supplies, and also have a significant share in imports of capital goods, while the transport sector is also included here with high absolute levels which tend to increase.

The features mentioned would appear to be enough to confirm that any change in import flows affects the base of the system of production and rigorously conditions the supply of final consumer products. In view of the international situation as regards price increases, it may be pointed out that inflation in Costa Rica is closely linked to the movements produced in the external sector, mainly in imports. The rising prices of imports mean higher production costs, while the slow growth of the volume explains the economy's loss of dynamism.

(c) *The balance of payments*

An analysis of the current account brings out the size of the trade deficits (see table 96). In fact, the deficits recorded between 1971 and 1974 were much higher than those of the preceding five-year period and their size accounts for most of the equally large deficits on current account.

Although the trade deficit in goods and services declined to a signficant extent in 1972 and 1973 especially compared with the deficit of 107 million dollars recorded in 1971, the increase in the payments of profits and interest on foreign capital expanded appreciably. It may be noted that in 1973 this item tripled as compared with the value recorded for 1970. The situation in 1974 was even more unfavourable, since the deficit on current account was more than double the deficit in previous years. The two imbalances thus combined to produce increasing deficits in the period under review (see table 96). A comparative examination of the deficit averages for the period 1971-1974, which more than doubled those of the five-year period 1966-1970, shows clearly the deterioration in the external sector in Costa Rica. This one indicator is sufficient to show once again, that one of the main problems of the country's economy originates in the external sector. In this context it may be recalled that Costa Rica does not produce petroleum and that increased import costs of this commodity will have adverse repercussions on the trade balance. It is estimated that the cost of petroleum imports for 1974 amounted to about 50 million dollars, with easily foreseen consequences on domestic costs of production and distribution. Since the input in question is widely used, this will have repercussions on a large part of economic activity and certainly on the level of living of the population. If recent trends in the price increases of other imported products are also considered, it will be agreed that the prospects of disequilibria in external trade are not particularly encouraging. Exports of industrial products and

Table 95. Costa Rica: structure of imports of goods
(CIF values in millions of dollars at current prices)

	1970	*Percentages*	*1971*	*Percentages*	*1972*	*Percentages*	*1973*	*Percentages*
Raw material for industry and mining	102.2		111.4		128.3		170.9	
Raw material for agriculture	9.2		9.0		9.4		11.9	
Construction material	17.3		16.8		15.2		18.3	
Fuels and lubricants	6.3		6.9		7.5		12.4	
Total inputs	*135.0*	(42.6)	*144.1*	(41.2)	*160.4*	(43.1)	*213.5*	(47.1)
Capital goods for industry and mining	25.7		25.4		26.7		42.4	
Capital goods for agriculture	6.2		9.0		9.4		10.7	
Capital goods for construction	10.2		13.1		14.6		13.5	
Capital goods for transport	23.2		30.7		36.6		36.1	
Other capital goods	13.4		15.7		20.5		21.6	
Total capital goods	*78.7*	(24.9)	*93.9*	(26.9)	*107.8*	(28.9)	*124.3*	(27.4)
Non-durable consumer goods	69.7		74.1		71.9		76.9	
Durable consumer goods	33.3		37.6		32.6		38.5	
Total consumer goods	*103.0*	(32.5)	*111.7*	(31.9)	*104.5*	(28.0)	*115.4*	(25.5)
Total imports	316.7	(100.0)	349.7	(100.0)	372.7	(100.0)	453.2	(100.0)

SOURCES: Dirección General de Estadística y Censos and Central Bank of Costa Rica.

Table 96. Costa Rica: balance of payments
(Millions of dollars)

	Average 1966-1970	*1970*	*1971*	*1972*	*1973*	*1974*	*Average 1971-1974*
Current account							
Exports of goods and services	210.3	280.1	283.8	346.3	416.5	521.3	392.0
Goods FOB	173.9	231.0	224.6	278.8	341.5	429.9	318.7
Services	36.4	49.1	59.2	67.5	75.0	91.4	73.3
Imports of goods and services	254.8	346.5	390.7	418.0	491.3	729.9	507.5
Goods FOB	207.6	286.8	316.3	337.1	399.3	606.5	414.8
Services	47.2	59.7	74.4	80.9	92.0	123.4	92.7
Net external investment income	−16.1	−13.6	−14.6	−34.7	−41.0	−49.2	−34.9
Profits	−8.0	−3.8	−3.4	−21.0	−24.4	−28.0	−19.2
Interest	−8.1	−9.8	−11.2	−13.7	−16.6	−21.2	−15.7
Net private transfer payments	4.1	3.4	3.5	4.0	3.6	3.6	3.7
Balance of current account	−56.5	−76.6	−118.0	−102.4	−112.2	−254.2	−146.7
Capital account							
Net external financing ($a+b+c+d+e$)	56.5	76.6	118.0	102.4	112.2	254.2	146.7
(a) Net external non-compensatory capital	64.4	79.1	128.0	106.3	98.7	157.6	122.6
Direct investment	17.1	26.4	22.0	25.8	26.8	27.7	25.6
Long- and medium-term loans	44.6	42.2	68.4	94.4	121.4	184.0	117.0
Amortization payments	−23.9	−19.2	−30.6	−38.3	−58.0	−63.7	−47.7
Short-term liabilities	22.7	27.2	64.3	21.8	9.0	9.6	26.2
Official transfer payments	3.9	2.5	3.9	2.6	−0.5	...	1.5
(b) Domestic non-compensatory capital or assets	−9.1	−5.9	−19.8	−46.2	−38.0	57.5	18.5
(c) Errors and omissions	6.9	−9.5	20.3	38.9	61.3		
(d) Allocation of SDRs	0.8	4.2	3.4	3.7	–	–	1.8
(e) Net compensatory movements (increase −)	−6.5	8.7	−13.9	−0.3	−9.9	39.1	3.8

SOURCE: ECLA on the basis of official statistics.

the promising trend in the prices of coffee, sugar, cocoa and meat apparently do not seem able to offset higher import costs.

An analysis of the capital account shows the extraordinary increase in long and medium-term loans (see table 96). These quadrupled in 1973 compared with 1970, in response to a sustained trend in the intermediate years. Amortization payments also recorded sharp increases and, given the latest debt levels, will continue to rise, thus constituting a factor absorbing considerable quantities of foreign exchange.

At the end of 1973 the external debt amounted to 440 million dollars,[134] which is moderate compared with the value of exports. However, it could become a serious problem if the deficits on current account and the recent trends observed in the annual state of indebtedness are maintained.

[134] Central Bank of Costa Rica. The external public debt accounts for 228 million dollars, and the external private debt for 152 million.

Direct foreign investment also shows a tendency to increase (see table 96). The average for 1971-1974 was 50 per cent up on the five-year period 1966-1970, reaching 27.7 million dollars in 1974. Attention has already been drawn to the magnitude of the transfers of foreign exchange abroad under the head of factor payments. Remittances of profits, which in 1972, 1973 and 1974 tripled those of the previous five-year period, were very close to balancing direct investment during those years. If the trend in the inflow of non-compensatory capital continues, profits on foreign investment will have an increasing incidence in the current account deficit.

The magnitude of the figures for errors and omissions is noteworthy. In 1973 this figure was 61.2 million dollars, or more than half the net external financing in that year. A thorough investigation of the structure of this figure might result in appreciable changes in the balances of the other accounts. It may well be that no small part of this

total represents illegal or not officially controlled exports and imports.

The movements of accounts described above, especially the increase in indebtedness and the inflow of direct investment, not only financed the deficits on current account but also meant that the country increased its international reserves between 1971 and 1973. Of particular importance were the increases in reserves in 1971 and 1973 (13.9 and 9.8 million dollars, respectively). The loss of 39 million dollars in 1974 indicates an extremely awkward balance-of-payments situation for Costa Rica. It is estimated that total net international reserves at the end of 1973 amounted to 42.4 million dollars. As a point of reference, it may be noted that this amount is more than double that for 1969 and almost seven times that for 1970.[135] Despite these increases, however, the 1973 level was only sufficient to finance one month's imports. Generally speaking, the level is considered to be adequate when it is equivalent to three or four months' imports; however, this is only a reference relationship, which in some cases may not be very meaningful.

To conclude the description of the most important features of the external sector as far as inflationary pressures are concerned, it is pointed out that the terms-of-trade effect has been adverse in recent years (see table 97). If 1970 is taken as the reference year, it may be noted that in the last four years fairly considerable losses were recorded in trade. In fact, the cumulative loss over that period was 157 million dollars at 1970 prices. If this figure were updated to dollars at 1974 prices, it would almost cover the deficit on current account for that year. These figures are thus not insignificant and it is easy to forecast that, in view of import price trends, they may increase significantly in the future.

[135] See International Monetary Fund, *International Financial Statistics*, November 1974.

Table 97. Costa Rica: indicators of external trade
(Millions of dollars at 1970 prices)

	1971	*1972*	*1973*
Purchasing power of exports	275.5	310.4	331.3
Export quantum	298.1	348.5	361.9
Terms-of-trade effect with reference to 1970	−22.6	−38.1	−30.6
Index of terms of trade (1970 = 100)	92.2	90.1	93.7

SOURCE: ECLA estimates based on official data.

2. *The evolution of total supply and demand*

The state of these main variables of supply and demand shows up clearly the loss of dynamism manifest in the economy of Costa Rica. The real growth recorded in the three-year period 1971-1973 is in frank contrast to that of the period 1966-1970 (see table 98). As regards supply, both the product and imports grew much more slowly. A comparison of the annual rates for both periods showed that the growth of the product declined from 6.9 per cent to 4.3 per cent annually, while imports similarly slowed their growth rate from 10.1 per cent to 3.5 per cent annually between the two periods considered. This decline in the above-mentioned rates constitutes one of the factors which should be taken into account in a description of inflation in Costa Rica. It should, however, be pointed out that 1970, the period of reference in the evolution of the last three-year period, was an exceptional year as far as imports are concerned; the real growth rate recorded by this variable was 25.3 per cent. In any case, the drop in the annual rates in the last three-year period, both in imports and in the product show a loss of dynamism which can be attributed only to a relatively small extent to the exceptional figures recorded in 1970.

Taking the structure of over-all supply, the growing share of imports to the detriment of the gross domestic product may be observed (see table 99). Whether the two-year period 1969-1970 or a more distant period, such as 1965, is taken as reference, the relatively greater importance of imports in the last few years is notable. The import coefficient, which was 31.6 per cent in 1965, rose to 36 per cent in 1971, while the average for the period 1971-1974 was of the order of 34.1 per cent. Although the rate of economic growth has slowed in recent years, this change in the share of external supplies is extremely significant and constitutes another element which must be borne in mind in describing the re-emergence of inflation in Costa Rica as from 1973.

Obviously, in the analysis of demand, the rates observed are somewhat slower for the last four-year period than in the five-year period 1965-1970 (see table 98). Most of the components had lower growth rates; while in the period 1965-1970 the annual growth rates of exports and consumption were 13.8 per cent and 6.5 per cent respectively, in the last four-year period, these rates were 7.5 per cent and 3.8 per cent. Gross domestic investment, on the other hand, increased more rapidly in the latter period, the annual rate rising from 5.8 per cent in the previous five-year period to 11.7 per cent in the last four years, with an exceptionally high rate in 1971 (28 per cent, following the 11.7 per cent recorded the previous

Table 98. Costa Rica: total supply and demand
(Millions of colones at 1970 prices)

	1970	1971	1972	1973	1974	Annual growth rate						
						1965-1970	1970-1974	1970	1971	1972	1973	1974
Total supply	*8,807.4*	*9,445.3*	*9,902.4*	*10,409.9*	*11,064.3*	*7.7*	*5.9*	*10.9*	*7.2*	*4.8*	*5.1*	*6.3*
Gross domestic product at market prices	6,524.5	6,946.3	7,418.6	7,878.6	8,201.6	7.0	5.9	6.6	6.5	6.8	6.2	4.1
Imports	2,282.9	2,499.0	2,483.8	2,531.3	2,862.7	10.1	5.8	25.3	9.5	−0.6	1.9	13.1
Total demand	*8,807.4*	*9,445.3*	*9,902.4*	*10,409.9*	*11,064.3*	*7.7*	*5.9*	*10.9*	*7.2*	*4.8*	*5.1*	*6.3*
Exports	1,841.2	1,959.5	2,314.5	2,344.7	2,459.1	13.8	7.5	10.6	6.4	18.1	1.3	4.9
Gross domestic investment	1,339.9	1,565.9	1,501.9	1,737.0	2,083.3	5.8	11.7	28.3	16.9	−4.1	15.7	19.9
Gross fixed investment	1,269.8	1,477.7	1,547.0	1,592.5	1,719.9	6.4	7.9	14.3	16.4	4.7	2.9	8.0
Public	289.6	350.4	378.4	353.8	364.4	14.5	5.9	11.0	21.0	8.0	−6.5	3.0
Private	980.2	1,127.3	1,168.6	1,238.7	1,355.5	7.7	8.4	15.3	15.0	3.7	6.0	9.4
Total consumption	5,626.3	5,919.9	6,086.0	6,328.2	6,521.9	6.5	3.8	7.5	5.2	2.8	4.0	3.1
General government	819.8	912.4	918.6	961.8	1,029.1	7.6	5.8	8.0	11.3	0.7	4.7	7.0
Private	4,806.5	5,007.5	5,167.4	5,366.4	5,492.8	6.4	3.4	7.4	4.2	3.2	3.9	2.4

SOURCE: ECLA, on the basis of official statistics.

year). This fact should also be recalled when the origin of the inflationary pressures in Costa Rica is interpreted.

From the point of view of the structure of total demand, significant changes may be observed (see table 99). If the 1974 structure is compared with that of the two-year period 1969-1970 and, better still, with a more distant period such as 1965, it may be observed that the most important changes were in exports and consumption. The export coefficient increased in the periods under consideration from 21.6 per cent in 1965 to 27.7 per cent in 1969-1970, reaching a peak of 30 per cent in 1974. On the other hand, the share of consumption, especially private consumption, declined. The growth rate of this variable in 1974 was far below the rates recorded in previous years. (See table 99.)

It is worth giving special attention to the analysis of consumption and, in particular, of investment. The movements of these variables reflect crucial options in the allocation of resources. It is obvious that the efforts made to maintain the growth rate of fixed capital formation were offset, from the domestic point of view, by a reduction in the share of consumption, accompanied by considerable external financing, as will be seen below.

The coefficient of fixed capital investment in the economy of Costa Rica reaches considerable levels. It fluctuated within a narrow range around 23 per cent and if the trend in the structure of investment manifested up to 1972 is maintained, a by no means insignificant industrial base will be consolidated. Furthermore, the National Development Plan of Costa Rica assigns special priority to the inclusion of resources which have still not been exploited and their subsequent processing.[136]

In the over-all analysis of gross domestic investment a clear differentiation should be made between what has taken place in gross fixed investment and as regards changes in stocks. Investment in fixed capital goods shows fluctuations, but reveals a faster growth than that of the product during the four-year period, and records annual rates well above those of consumption.

As regards changes in stocks, a highly significant fact may be observed. In 1972 there was a negative variation which reflected the disparity between the growth of supply in terms of volume (4.8 per cent) and demand measured in current monetary terms. The decrease in stocks and, of course, the increase in prices were the mechanisms which restored the balance in real terms.

It is useful to note that the greater part of investment is private sector investment while only around one fifth is public sector investment (see table 99). It should, however, be mentioned that between 1970 and 1973 the share of public investment in capital formation increased appreciably: from 19.6 per cent it rose to 22 per cent, which is the more significant if it is borne in mind that the growth rate of total investment in the last four-year period was fairly high, except in 1972. Furthermore, the data in colones at current prices

[136] Summary of the National Development Plan of Costa Rica 1974-1978. The chapter on the strategy and over-all plan states that the inclusion of unprocessed resources is not desirable since this would lead to the re-establishment of the classic international division of labour in which Costa Rica would continue to figure as an exporter of primary products.

Table 99. Costa Rica: structure of total supply and demand
(Percentages)

	1965	*Average 1969-1970*	*1970*	*1971*	*1972*	*1973*	*1974*	*Average 1971-1974*
Total supply	*131.6*	*132.5*	*135.0*	*136.0*	*133.5*	*132.1*	*134.9*	*134.1*
Gross domestic product	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Imports	31.6	32.5	35.0	36.0	33.5	32.1	34.9	34.1
Total demand	*131.6*	*132.5*	*135.0*	*136.0*	*133.5*	*132.1*	*134.9*	*134.1*
Exports	21.6	27.7	28.2	28.2	31.2	29.8	30.0	29.8
Gross domestic investment	25.7	18.9	20.5	22.5	20.2	22.0	25.4	22.6
Gross fixed investment	22.8	18.8	19.5	21.3	20.9	20.2	21.0	20.8
Public	5.2	4.3	4.5	5.0	5.1	4.5	4.4	4.7
Private	17.6	14.5	15.0	16.2	15.8	15.7	16.5	16.1
Total consumption	84.3	85.9	86.2	85.2	82.0	80.3	79.5	81.6
General government	13.5	12.5	12.5	13.1	12.4	12.2	12.5	12.5
Private	70.8	73.4	73.7	72.1	69.6	68.1	67.0	69.1

SOURCE: Table 98.

given in table 100 indicates still more pronounced changes towards an increasing public share in investment.[137] The most significant aspect of this information indicates the main type of investment made by each sector. It may thus be seen that private enterprise concentrated mainly on the purchase of machinery and equipment, while state activity was primarily directed towards construction. In fixed capital formation as a whole, given the size of investment in each sector, machinery and equipment increased more rapidly than construction (see table 101).

Another aspect of great interest in the study of the capital formation process in the economy of Costa Rica concerns the destination of investment by sectors of economic activity.

The structure and trends of investment, generally speaking adequately reflects the changes in the structure of production. In the case of the economy of Costa Rica, unmistakable signs of changes in the structure of production may be observed, judging by the distribution of investment in the different sectors in 1971 and 1972 (see table 102). Industry, transport, ownership of dwellings and general government were the activities which most benefited. From the point of view of increases in allocations of resources in the period 1971-1972, of particular note are the electricity sector which grew by 118 per cent, construction of which increased by 75 per cent, transport by 60 per cent, and general government whose growth rate was 115 per cent. Although these increases are in terms of current values, they are not without meaning, since it was in that period that inflationary pressures began to appear, as will be seen below.[138] In contrast to the increases mentioned, the drop in investment in the agricultural sector is particularly striking (see table 102).

The above data and the volume of investment in the industry and transport sectors are, as has been said, clear indications of the transformation of the typical agricultural export model which characterized the economy of Costa Rica in the past. The industrialization process which gathered impulse in the second half of the last decade, has

[137] These data differ from those of table 98 because the current values involve variations in prices and particularly in exchange rates which the conversion to real values attempts to eliminate.

[138] The increases in wholesale prices were approximately 6.7 per cent in 1971 and 5.4 per cent in 1972.

Table 100. Costa Rica: public and private investment
(Millions of colones at current prices)

	1970	*Percentage*	*1971*	*Percentage*	*1972*	*Percentage*
Fixed public investment	*287.6*	*22.7*	*408.2*	*25.9*	*562.3*	*31.2*
Construction . . .	228.1	18.0	304.2	19.3	430.3	23.9
Machinery and equipment . .	61.5	4.7	104.0	6.6	132.0	7.3
Fixed private investment	*980.2*	*77.3*	*1,170.3*	*74.1*	*1,237.7*	*68.8*
Construction . . .	408.6	32.2	449.8	28.5	385.1	21.4
Machinery and equipment . .	571.6	45.1	720.5	45.6	852.6	47.4
Total fixed investment	*1,267.8*	*100.0*	*1,578.5*	*100.0*	*1,800.0*	*100.0*

SOURCE: Central Bank of Costa Rica.
Note: No data are available for 1973.

Table 101. Costa Rica: structure of investment
(Millions of colones at current prices)

	1970	*Percentage*	*1971*	*Percentage*	*1972*	*Percentage*
Investment in construction . . .	636.7	50.1	754.0	47.8	815.4	45.3
Investment in machinery and equipment . .	633.1	49.9	824.5	52.2	984.6	54.7
Total investment . .	*1,269.8*	*100.0*	*1,578.5*	*100.0*	*1,800.0*	*100.0*

SOURCE: Central Bank of Costa Rica.

Table 102. Costa Rica: fixed capital investment by sector
(*Millions of colones at current prices*)

Sector	*1970*	*Percentage*	*1971*	*Percentage*	*1972*	*Percentage*
Agriculture	191.0	15.0	196.6	12.5	157.9	8.7
Manufacturing	245.6	19.3	251.2	15.9	307.5	17.1
Construction[a]	81.2	6.4	116.4	7.4	142.2	8.0
Electricity	79.1	6.2	142.5	9.0	172.2	9.6
Transport	190.7	15.0	232.2	14.7	304.1	16.9
Commerce	86.1	6.8	93.0	5.9	88.6	4.9
Banking	24.8	2.0	16.6	1.0	27.9	1.5
Ownership of dwellings	173.0	13.6	248.2	15.7	221.1	12.3
Services	46.8	3.7	51.6	3.3	53.5	3.0
General government	151.4	12.0	230.2	14.6	325.0	18.0
Total	*1,269.7*	*100.0*	*1,578.5*	*100.0*	*1,800.0*	*100.0*

SOURCE: Central Bank of Costa Rica.
[a] Construction and machinery equipment.

maintained its momentum in the present decade, as shown by the steady rates of growth achieved.

Lastly, it is also interesting in analysing investment to examine the preferences of foreign private enterprise as regards the sectors in which it invests. From the data given in table 103, it may be concluded that agricultural and industrial activity attracted a major share of foreign investment, since the export capacity and rate of return of these sectors offer distinct advantages for foreign capital. It should also be mentioned that between 1970 and 1973 foreign capital increased by 33.3 per cent, although it still has not reached 10 per cent of total investment.

3. *The product and its sectoral structure*

The annual growth rates of the gross domestic product during the period 1970-1974 were, as has already been said, lower than those recorded in the five-year period 1965-1970, the annual average rate of which was estimated at 7 per cent. It should not be lost sight of that the *per capita* product for Costa Rica is relatively high among the developing countries. In fact, different estimates for 1973 place this indicator at levels of over 800 dollars.[139]

An analysis of sectoral performance during the four-year period 1971-1974 shows that the loss of dynamism reflected in the growth rate of the product is the result of the slow growth of the agricultural and services producing sectors. Manufacturing maintained the rate reached in the reference five-year period, and construction showed a significant increase in its rate of growth (see table 104).

From the standpoint of the description and interpretation of inflation in Costa Rica, of special importance is the drop in the rate of growth of the agricultural sector and the fluctuations experienced, because of its influence on external trade, its capacity to absorb employment and its incidence in over-all economic growth. This sector is of key importance because of its direct relationship with inflationary pressures.

[139] The *per capita* product in dollars fluctuates to a significant extent depending on the exchange rates used for the conversion.

Table 103. Costa Rica: structure of private foreign investment[a]
(*Millions of dollars at current prices*)

Sector	*1970*	*Percentage*	*1971*	*Percentage*	*1972*	*Percentage*	*1973*	*Percentage*
Agriculture	16.1	61.0	10.0	45.5	22.2	85.7	23.8	67.6
Manufacturing	6.1	23.0	5.9	26.8	4.0	15.4	12.8	36.4
Transport	−0.5	−2.0	3.0	13.6	0.2	0.8	−0.2	−0.6
Services	0.5	2.0	0.7	3.2	0.2	0.8	0.2	0.6
Commerce	1.0	4.0	−1.1	−5.0	−0.7	−2.7	−2.7	−7.7
Other sectors[b]	3.2	12.0	3.5	15.9	–	–	1.3	3.7
Total	*26.4*	*100.0*	*22.0*	*100.0*	*25.9*	*100.0*	*35.2*	*100.0*

SOURCE: Central Bank of Costa Rica. Preliminary estimates.
[a] Data recorded in the balance of payments.
[b] Including the finance sector.

Table 104. Costa Rica: gross domestic product by sector of economic activity
(Millions of colones at 1970 prices)

	1970	1971	1972	1973	1974	Annual growth rate						
						1965-1970	1970-1974	1970	1971	1972	1973	1974
Agriculture	1,452.1	1,533.4	1,620.8	1,737.5	1,703.4	5.1	4.1	2.0	5.6	5.7	7.2	−2.0
Mining[a]	—	—	—	—	—	—	—	—	—	—	—	—
Manufacturing	878.4	962.7	1,047.4	1,152.1	1,256.5	9.5	9.4	8.4	9.6	8.8	10.0	9.1
Construction	275.2	297.2	316.5	327.6	370.3	4.8	7.7	12.8	8.0	6.5	3.5	13.0
Subtotal goods	*2,605.7*	*2,793.3*	*2,984.7*	*3,217.2*	*3,330.2*	*6.4*	*6.3*	*5.2*	*7.2*	*6.9*	*7.8*	*3.5*
Electricity, gas, water and sanitary services	114.3	125.8	141.4	156.0	163.2	9.8	9.3	7.9	10.1	12.4	10.3	4.6
Transport and communications	276.7	297.4	321.2	342.8	358.5	7.6	6.7	8.7	7.5	8.0	6.7	4.6
Subtotal basic services	*391.0*	*423.2*	*462.6*	*498.8*	*521.7*	*8.2*	*7.5*	*8.5*	*8.2*	*9.3*	*7.8*	*4.6*
Commerce and finance	1,299.7	1,378.8	1,514.4	1,590.8	1,659.2	8.9	6.3	12.2	6.1	9.8	5.0	4.3
Ownership of dwellings	485.5	507.8	539.3	559.8	585.5	3.1	4.8	3.1	4.6	6.2	3.8	4.6
Government	693.2	738.3	744.2	774.7	810.3	7.8	4.0	6.8	6.5	0.8	4.1	4.6
Miscellaneous services	324.2	334.9	351.0	364.0	380.8	6.6	4.1	5.0	3.3	4.8	3.7	4.6
Subtotal other services	*2,802.6*	*2,959.8*	*3,148.8*	*3,289.3*	*3,435.8*	*7.3*	*5.2*	*8.3*	*5.6*	*6.4*	*4.5*	*4.5*
Total	*5,799.3*	*6,176.2*	*6,596.3*	*7,005.2*	*7,292.4*	*7.0*	*5.9*	*6.6*	*6.5*	*6.8*	*6.2*	*4.1*

SOURCE: ECLA, on the basis of official statistics.

[a] Mining is included in manufacturing.

It should be noted that the lower growth rate of economic activity was not merely limited to the production of agricultural goods, but there were also appreciably lower rates in certain sectors producing services. It is common to observe in other countries that the services sectors take longer to show the crises which appear at the base of the economic system. In the case of Costa Rica, as has already been mentioned, economic activity in general is closely linked to external trade, so that the problems of the latter are directly and immediately disseminated throughout most of the system of production.

On account of the above growth of the various sectors, the structure of the product suffered fairly considerable modifications in recent years (see table 105). First the increased share of manufacturing should be noted. Exports by this sector to the central American market explain this increase, despite the adverse effect of the price increase of its imported inputs; it may be observed that its share increased steadily in each year of the present decade. Moreover, attention is drawn to the significant increase in the share of commerce and finance: from an average of 15.6 per cent in the period 1966-1970 it rose to 22.7 per cent in the four years 1971-1974.

In this description of the over-all economy in the period 1971-1974, it is pointed out that the situation deteriorated significantly in the last year. The growth rates of most of the sectors were appreciably lower than in previous periods. With the exception of manufacturing, which maintained its growth, and construction which showed a distinct recovery, the loss of momentum extended to highly important activities. The drop in agricultural production (–2 per cent) was the most significant factor; it is unnecessary to stress its repercussions on economic and social activity in Costa Rica.

In describing the evolution of the economy of Costa Rica in the last four-year period, only the phenomena of most significance and use for the interpretation of inflation in the country were analysed. There has been no attempt to give an appraisal of the economic process, and still less an exhaustive description. The following analysis of inflation requires that this general frame of reference be borne in mind.

C. Appearance and acceleration of inflation

One of the main features of the Costa Rican economy has been the relative stability of domestic prices, and it is within this context that the performance of its production agents evolved. In the whole period 1964-1970, for example, the consumer price index rose by 12.6 per cent (2 per cent annually). Clearly, there were no inflation problems and, more important still, problems of this kind do not seem to have been latent or kept under control by a direct policy of restraint. In view of the characteristics of its population, the distribution of income and the rates of economic growth during this decade, it is hard to believe that there were hidden inflationary pressures as

Table 105. Costa Rica: structure of GDP by sector of economic activity[a]
(Percentages)

	1965	*Average 1966-1970*	*1970*	*1971*	*1972*	*1973*	*1974*	*Average 1971-1974*
Agriculture	28.0	26.6	25.0	24.8	24.6	24.8	23.4	24.4
Mining[b]	–	–	–	–	–	–	–	–
Manufacturing	14.9	16.2	15.2	15.6	15.9	16.4	17.2	16.3
Construction	5.6	5.0	4.7	4.8	4.8	4.7	5.1	4.8
Subtotal goods	*48.5*	*47.8*	*44.9*	*45.2*	*45.2*	*45.9*	*45.7*	*45.5*
Electricity, gas, water and sanitary services	1.7	1.9	2.0	2.0	2.1	2.2	2.2	2.2
Transport and communications	4.4	4.5	4.8	4.8	4.9	4.9	4.9	4.9
Subtotal basic services	*6.2*	*6.3*	*6.7*	*6.8*	*7.0*	*7.1*	*7.1*	*7.0*
Commerce and finance	15.0	15.6	22.4	22.3	23.0	22.7	22.8	22.7
Ownership of dwellings	8.7	7.8	8.4	8.2	8.2	8.0	8.0	8.1
Government	11.8	12.3	12.0	12.0	11.3	11.1	11.1	11.3
Miscellaneous services	10.3	10.3	5.6	5.4	5.3	5.2	5.2	5.3
Subtotal other services	*45.8*	*45.9*	*48.3*	*47.9*	*47.7*	*47.0*	*47.1*	*47.4*
Total	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*

SOURCE: Table 104.
[a] 1970 prices.
[b] Mining and quarrying are included in manufacturing.

occurred in other countries, where long periods of relative stability were sometimes achieved by curbing the growth of consumption of broad sectors of the population. On the whole, the steadily increasing demands of the social and productive process found a response in flexible supply, in which imports played a decisive role.

The prices situation changed radically in the 1970s. Already in 1970 and 1971 there were unusually large price increases, at rates which accelerated considerably in 1973 and 1974. The purpose of these pages is none other than to identify the most important characteristics of the emergence, spread and acceleration of the inflationary process.

In this connexion, two observations are necessary. First, given the fact that this is a recent phenomenon and in view of its characteristics, attention has been centred mainly on identifying the inflationary factors and considering them in order of importance. This is not intended to be a complete study. There are still some unknown factors, particularly as regards the expectations of producers and consumers and their conduct vis-à-vis a process which is beginning to affect them severely. The collection of relevant data and the choice and adaptation of new analytical instruments will entail additional efforts in order to further clarify the problem.

Moreover, it must be pointed out that this is a partial attempt, since it excludes any analysis of the political process, which would no doubt have supplied additional criteria. Government action in this field, and the action of economic and political groups, make up a frame of reference which lies outside the scope of economic analysis. A task of that magnitude, however, apart from concentrating efforts which would have exceeded the scope of this study, requires information which is not generally compiled and for which the only substitute can be the most important day-to-day political developments.

1. *The general context*

In order to interpret the inflation which has recently affected Costa Rica it is necessary to identify the salient features of over-all economic development, and, in particular, the evolution of the external sector, which was attempted in the previous chapter.

Some facts which should be recalled here are the loss of dynamism of economic activity in the last four years, the public sector's increasing share in capital formation and the continuous nature of the industrialization process. Moreover, from the standpoint of the external sector, an important feature was the considerable rise in import prices and the fluctuations in volume and prices of the traditional export commodities. The effects of these movements were reflected in large and persistent balance-of-payments deficits on current account, which is especially important because of their significant impact on a major part of economic activity. It is in the external sector that many of the factors which have disrupted the basic equilibria and have led to changes in the system and rises in the level of domestic prices may be found.

2. *Indicators of levels of inflation*

For an indication of the trend of inflation, among the price indicators generally chosen are consumer and wholesale price indexes and the implicit deflator of the product.[140] Information has been collected on these indexes as a first criterion, which provides orders of magnitude of the price trends in Costa Rica. Table 106 shows the variations in these indexes.

The three indicators show that in the period 1966-1969 price increases were fairly small. In 1957-1969 the wholesale price index, apparently the most sensitive of the three, rose by less than 3 per cent annually, thus indicating virtual price stability.[141] If this rate is compared with the movements of prices in other Latin American countries during this period, including those described as stable, the foregoing observation does not seem exaggerated.[142]

In contrast with this historical background of price stability, as already mentioned, the first few years of the 1970s show significant changes. The first inflection point was reached in 1970: the three indexes chosen show appreciably higher rates than in the immediately preceding periods, thus marking the start of inflationary pressures in Costa Rica. The other important milestone was in 1973, when the growth rates of the two indexes available tripled the annual rate of the period 1966-1972. Available data for the first half of 1974 indicate an acceleration which leaves no room for doubt regarding the persistence of the pressures on prices, constituting what can already be termed

[140] The implicit deflator of the product is generally defined as the harmonic mean of sectoral price indexes and is interpreted as an indicator of the general level of prices in the economy. It represents the ratio of the product at current prices to the product at constant prices.

[141] The evolution of this index is shown in a study presented by Mr. Otto Kikut, Alternate Director of the National Planning Office (OFIPLAN), at the Seminar on Economic Policy held under the sponsorship of the National Planning Office of Costa Rica in October 1974.

[142] The following annual rates of price increases for the same period in other countries of the region are useful for reference purposes: 29 per cent in Argentina, 5.4 per cent in Bolivia, 42 per cent in Brazil, 3.4 per cent in Mexico and 6.7 per cent in Peru.

Table 106. Costa Rica: price indexes

Period	*Wholesale price index*[a]		*Retail price index*[b]		*Implicit deflator of the gross product*[c]	
	1966 = 100	*Percentage annual variation*	*1964 = 100*	*Percentage annual variation*	*1967-1969 = 100*	*Percentage annual variation*
1966 . . .	100.0	–	99.5	–	97.9	–
1967 . . .	103.3	3.3	100.7	1.2	98.4	0.5
1968 . . .	108.4	4.9	104.8	4.1	99.3	0.9
1969 . . .	113.0	4.2	107.6	2.7	101.9	2.6
1970 . . .	120.0	6.2	112.6	4.6	107.7	5.7
1971 . . .	128.0	6.7	116.1	3.1	113.0	4.9
1972 . . .	135.0	5.4	121.4	4.6	119.6	5.8
1973 . . .	157.0	16.4	132.7	9.3	...	...

SOURCES: [a] Central Bank of Costa Rica.
[b] National Planning Office.
[c] International Bank for Reconstruction and Development, *Economic Report of Costa Rica*, 15 March 1974, vol. II.

the recent inflationary process in Costa Rica. In the second half of 1974, however, the virulence of the inflation seems to have diminished, to judge from the rise of only 10 per cent in prices recorded in that period (see table 107). It is difficult to determine, in the light of this fact, how far an effective control of the inflationary process was achieved. Information on price increases in the early months of 1975 does not clarify the matter.

3. *Disparities in price increases*

It is interesting to note the uneven increase in wholesale prices according to the origin of the products. The sample of this index contains domestic and imported products, and the variations in both are useful for elucidating and studying the origins of inflation in Costa Rica (see table 108).

It will be noted that between 1971 and 1973 imported goods experienced appreciably higher price increases. If prices in June 1974 are com-

Table 107. Costa Rica: recent domestic price trends
(Percentage variations)

Period	*Wholesale price index*	*Retail price index*[a]
December 1972–June 1973	9.3	6.9
June 1973–December 1973 . . .	15.7	8.5
December 1973–June 1974	26.0	18.1
June 1974–December 1974 . . .	–	–
June 1973–June 1974	45.8	28.2

SOURCE: Banco Central de Costa Rica, *Boletín estadístico mensual*; and estimates of the United Nations Advisory Group in OFIPLAN.
[a] This index is no longer published officially because it is not regarded as truly representative. The wholesale price index is considered to be the most appropriate indicator for estimating price variations.

Table 108. Costa Rica: components of the wholesale price index
(1966 = 100)

	1971	*1972*	*1973*	*Percentage variation 1971–1973*	*June 1974*	*Percentage variation 1971–June 1974*
Average general index of domestic goods .	131.2	137.8	158.4	20.7	224.9	71.4
Average general index of imported goods .	118.1	126.9	154.1	30.5	221.3	87.4
General index . . .	128.0	135.0	157.0	22.7	223.7	74.8

SOURCE: Central Bank of Costa Rica.

Table 109. Costa Rica: wholesale price index by groups of products
(1966 = 100)

	General index	*Production of animal origin*	*Production of vegetable origin*	*Beverages and other food-stuffs*	*Fuels and electricity*	*Textile products and hides*	*Construction materials*	*Chemical products*	*Miscellaneous products*
June 1971	128.3	134.9	182.5	117.0	113.9	114.5	131.9	107.2	115.3
December 1971	130.3	136.8	187.8	117.7	114.1	120.3	127.0	106.1	123.9
June 1972	135.3	140.3	208.6	118.1	118.7	123.8	132.9	110.3	125.7
December 1972	140.4	142.7	209.2	121.1	119.9	134.7	143.9	114.9	132.9
June 1973	153.5	160.1	239.0	122.9	127.8	147.9	161.1	124.2	145.3
December 1973	177.6	170.3	267.6	162.6	143.9	189.9	185.6	138.1	159.4
June 1974	223.7	206.6	319.1	198.6	242.1	226.2	234.7	182.6	184.3
December 1974	245.5	208.8	284.6	210.2	270.6	241.2	249.8	205.9	210.0
Variation between June 1971 and June 1974	74.4	53.3	74.8	69.7	112.6	97.6	77.9	70.3	59.8
Variation between June 1973 and June 1974	45.7	29.0	33.5	61.6	89.4	52.9	45.7	47.0	26.8

SOURCES: OFIPLAN and Dirección General de Estadística y Censos.

pared with the average for 1973, the components show a similar growth (42 and 43 per cent). When an attempt is made to explain the causes of Costa Rican inflation, its first effects and subsequent spread, it will be useful to revert to this point.

A breakdown of this index by types of products also reflects disparities which help to discover other useful characteristics in diagnosing inflation. Table 109 contains a breakdown by groups of products.

The various groups of products show very uneven rates of increase. Obviously, the most spectacular rise was in fuel and electricity, i.e., one-and-a-half times the general index. Products of animal origin and miscellaneous products, mainly clothing, recorded the lowest rates. The effect of import prices is clear at the two extremes; the different import content of the two groups and their respective prices are clearly reflected in the domestic prices. In the last six-month periods the uneven rates of acceleration persisted, and beverages and other food-stuffs, with a high import content, are included among the most dynamic groups.

It seems idle to go any further into a description of the inflationary situation in Costa Rica. The information given is sufficient to identify the period in which prices started to rise, the magnitude of the increases, their acceleration and disparities. Obviously it would have been more illuminating to analyse a larger group of price indicators, but a broader coverage would yield only marginal benefits and would not change the essence of this description.

D. THE PHASES OF INFLATION

Contrary to what happens in other countries, especially those characterized by long-established inflationary processes, inflation in Costa Rica does not appear to have its main root in structural origins. Although obvious structural traits may be identified in the external sector, especially if it is recalled that bananas and coffee, with their traditional fluctuations in prices, continued to be decisive in the structure of exports, and that there is heavy dependence on imported supplies, this is not the case from the point of view of the production function, the nature of the ownership system or the perspective of the capital formation process. In other words, the whole situation of structural inadequacies typical of some other countries is not repeated here. The high rates of growth and capital formation recorded in the 1960s and the price stability which accompanied them and characterized the economy, suggest a situation in which economic growth was accompanied by a satisfactory degree of balance in the variables and components of the sytem. The price rises of recent times, however, obviously indicate the presence of maladjustments in this coherent state of affairs.

To describe inflation in Costa Rica, two phases must be distinguished in its evolution—the initial impulses, and the speeding-up of the process. Each of these phases appear to fit in with one of two types of inflationary factors—those known as conjunctural factors and structural factors.

A reflexion of a general nature may, however, be included at this point. In other countries, the origins of the persistent price rises were generally to be found in the base of the economic system, and stemmed from structural disequilibria: conjunctural phenomena explained the rapid dissemination and virulence of the inflation, and the interaction of the two types of disequilibria made up the classic pattern of inflation. The analysis of inflation in Costa Rica, both in its initial stage and in its re-emergence, suggests the possibility that the reproduction sequence of the inflation may have taken the opposite course: the price rises made their appearance basically motivated by domestic and external phenomena connected with the situation, while the structural features proper, especially as regards dependence on imported supplies, would explain the propagation of the phenomenon.

The above considerations tend to give State action as regards economic policy considerable manoeuvring space in steering the economic system. This is not the case in other countries, overwhelmed by generalized structural problems, where economic policy decisions only marginally modify the operation of economic activity.

1. *Inflation in 1970–1971*

The data on the annual movements of prices showed a first change of pace at the beginning of the 1970s. The rate of increase in the period 1965–1969 was about 4 per cent; in 1970 this rose to 6.2 per cent and in 1971 to 6.7 per cent.[143] Although these amounts may seem small, it is to be noted that they signify an increase of more than 50 per cent compared with the rate of the previous five years; they obviously constitute the beginning of recent inflation in Costa Rica. It seems clear that these increases are directly related to the increase in the liquidity of the economy which did not find response in dynamic supply. In the first part of the present document the drop in the growth rate of the product of agriculture, which is the main sector of economic activity, was

[143] Rates for the wholesale price index (see table 106).

Table 110. Costa Rica: monetary balance
(Millions of colones at current prices: balances at end of each period)

	1969	*Annual rate*	*1970*	*Annual rate*	*1971*	*Annual rate*	*1972*	*Annual rate*	*1973*	*Annual rate*	*1974*	*Annual rate*
Composition of monetary resources	1,497.2	9.0	1,591.2	6.3	2,251.1	41.4	2,629.2	16.8	2,965.3	12.8	3,928.0	32.4
Money	1,014.5	14.5	1,099.1	8.3	1,416.0	28.8	1,617.3	14.2	2,007.7	24.1	2,394.0	19.2
Quasi-money	299.2	7.8	336.7	12.6	640.8	90.2	855.6	33.5	951.1	11.2	1,604.0	68.6
Long-term indebtedness	54.9	−27.5	40.5	−26.2	69.0	70.4	79.1	14.6	72.6	−9.2	198.0	172.7
Other items (net)	128.6	−4.9	114.9	−10.7	125.3	9.1	77.2	−39.4	−66.1	–	−268.0	–
Factors of monetary expansion and contraction	1,497.2	9.0	1,591.4	6.3	2,250.8	41.4	2,629.3	16.8	2,965.5	12.8	3,927.0	32.4
Reserves	114.3	−65.5	42.2	−63.1	173.4	310.9	189.1	9.1	276.4	46.2	−116.0	–
Domestic credit (net)	1,382.9	3.1	1,549.2	12.0	2,077.4	34.1	2,440.2	17.5	2,689.1	10.2	4,043.0	50.4
(*a*) To the Government	258.5	−8.1	207.4	−19.8	251.7	21.4	379.0	50.6	274.8	−27.5	337.0	22.6
(*b*) To official institutions	20.3	−43.8	29.3	44.3	73.5	150.9	83.3	13.3	163.3	96.0	340.0	108.2
(*c*) To the private sector	1,104.1	7.9	1,312.5	18.9	1,752.1	33.5	1,977.9	12.9	2,221.3	12.3	3,366.0	51.5

SOURCE: International Monetary Fund, *International Financial Statistics*, November 1974 and June 1975.

described. Consequently, other conjunctural variables require to be analysed since, as stated previously, they would appear to explain to a considerable extent the first advances of inflation. Table 110 sums up the monetary balance of Costa Rica, the outstanding features of which are variations in the monetary flows which coincide exactly with the increases in prices.

The changes in monetary resources are notable for their magnitude. It may be seen that money showed an increase of 8.3 per cent in 1970 and 28.8 per cent in 1971; quasi-money similarly recorded appreciable increases: 12.6 per cent in 1970 and 90.2 per cent in 1971. Although long-term indebtedness declined in 1970, it increased by 70.4 per cent in 1971.

As regards the factors of expansion, the increases in domestic credit at rates of 12 per cent and 34.1 per cent in the first two years of the present decade indicates an appreciable increase in the liquidity of the economic system. The private sector figures as the main beneficiary of the increase in money. During 1970, the increase in the credit granted to it by the financial system was 18.9 per cent, while this increase was 33.5 per cent in 1971; this meant that its share in the absorption of credit exceeded 80 per cent of the total. The absolute figures of these volumes of credit nearly doubled the amounts of fixed capital investment which the private sector made during those years.

The structure of credit to the private sector has clear inflationary implications. While in the five-year period 1966-1970 nearly 90 per cent of this type of credit was devoted to financing industrial and agricultural activities, the percentage dropped to 54 per cent in 1971, giving way to personal type and service credits which reached increasingly large proportions.[144] It is not difficult to see that this variation in the structure of the credit goes against the flexibility of supply and generates demand effects which put pressure on prices. The disparities observed in the price increases of different items may have a complementary explanation in terms of the products most in demand by the socio-economic groups benefiting from the credit policy.

Although the increased liquidity of the economic system originated mainly in the credit extended to the private sector, the liquidity promoted by the public sector was by no means insignificant. If fiscal performance is examined, the exceptional increase in the budget deficit during 1971 stands out (see table 111). It was twice that for 1970, and amounted to 216 million colones, more than 40 per cent of which was financed with domestic credit. The magnitude of this budgetary imbalance may be explained by the slow increase in income (3.1 per cent) vis-à-vis the significant expansion of current expenditure (18.1 per cent) and capital expenditure (36 per cent). Consequently, fiscal performance in 1971 offered an additional boost to inflationary pressures, particularly if the increases in money are related to the magnitude of the deficit in the two-year period under analysis. These appreciations coincide with those which emerge from the analysis of the amounts of credit granted to the Government and other official institutions by the finance system (see tables 110 and 111).

[144] Inter-American Committee on the Alliance for Progress (CIAP), Sub-Committee on Costa Rica (18-22 September 1972), document prepared by the secretariat, p. 44.

Table 111. Costa Rica: fiscal situation of the public sector
(Millions of colones at current prices)

	1969	*1970*	*Annual rate*	*1971*	*Annual rate*
Current income of central government	719	883	22.8	910	3.1
Current expenditure of central government	685	769	12.3	908	18.1
Savings in current account	34	114	–	2	–
Savings of rest of public sector	133	191	–	262	–
Total public savings	167	305	–	264	–
Capital expenditure	352	361	2.5	491	36.0
Amortization of the debt	115	139	20.9	151	8.6
Gross deficit	298	195	-34.6	378	93.8
Financing	298	195	-34.6	378	93.8
External credit	83	174	109.6	216	24.1
Domestic credit	215	21	-90.3	162	671.4

SOURCE: CIAP, Sub-Committee on Costa Rica (18-22 September 1972), document prepared by the Secretariat, table II-12.

The other element which affected the expansion of the monetary system was the performance of international reserves. The decline noted in 1970 contrasted with the extraordinary growth of 1971, i.e., 70 per cent compared with 1969 and 311 per cent compared with 1970. The increased liquidity apparent in the economy of Costa Rica found a major cause in the growth already mentioned, the magnitude of which in 1971 accounted for over 40 per cent of the increase in the money supply (see table 110).

The description in the foregoing pages of the main movements of the financial variables leaves no doubts as regards the impact of internal inflationary factors when inflation began in Costa Rica. Although during 1970 the influence of some factors was partially countered by others, in 1971 it is clearly to be noted that they all point in the same direction. The policy of re-activating the economy by granting increasing credits to the Government, to official institutions and, principally, to the private sector, did not have further violent repercussions on the level of prices, basically because imports increased in real terms by 25.3 per cent in 1971 and 9.5 per cent in 1972, while stocks declined to a significant extent. Both variations constituted factors of flexibility in the supply of goods which in fact made it possible to mitigate the effect of inflation. It is also necessary to take into account a further element which played its part against inflation during the period under analysis. The behaviour of consumers and producers was deeply rooted in the period of stability which previously characterized Costa Rica. Expansions like those observed in 1970 and more particularly in 1971, in countries whose agents are accustomed to defending themselves against inflation, would probably have had a greater effect on prices.

Up to this point an attempt has been made to describe the main features of the first period of inflation in Costa Rica: conjunctural imbalances which later combined with structural factors and marked the beginning of inflationary pressures which later hit the economy of Costa Rica harder. The analysis of the main economic policy measures, particularly in exchange, which have certainly played a role of some importance has deliberately been left for the last chapter.

2. *Inflation during the period 1972-1973*

The break-up of the basic stable aspects of the economic system, which was described in the analysis of the period when the first inflationary pressures emerged, does not seem to have been remedied in the years which followed, despite the Government's efforts. In 1973 a group of new inflationary factors originating in the performance of the external sector appeared in this area which was in itself fertile ground for new price increases. The international markets showed unexpected price movements and decisively influenced the economy of Costa Rica. A description of the evolution of prices since 1972 to the present day requires the previous identification of the main factors of inflation which originate in the external sector, and their effects on economic activity.

(a) *Imported inflation*

The important increases in the prices of a large number of commodities involved in international trade first affects importing countries through the rise in prices of products from abroad, with clear repercussions on domestic prices. Although these repercussions vary according to whether the imports are final goods or inputs, their multiplier effects on domestic prices are obvious. Increases in production and distribution costs are a direct repsonse to this type of exogenous movement, and through their demonstration effect they frequently unleash price rises in other products, even those which have nothing to do with external trade. The situation of international prices, however, does not only affect the levels of domestic prices through imports; increases in export prices, although they have an unquestionably favourable effect on the balance of payment, may give rise to inflationary pressures. Any unusual growth in the value of exports generates liquidity in national currency which does not always find an immediate response in increases in total supply; nor do imports, and even less production, react as rapidly as the increases in demand appear in the market. On the other hand, the structures of these two types of variation do not always coincide, and this produces maladjustments which may affect the system and the level of prices.

An increase of any size in export prices may also have inflationary effects when external market prices attract a growing share of production, causing shortages in the domestic market; this is the case of activities destined for export or aimed at satisfying the requirements of the domestic market. It should be recalled that in countries where it has been attempted to rectify this situation by fixing export quotas in order to safeguard national supply, heavy flows of illegal trade have appeared and aggravated the problems of scarcity.

Increases of any size in international reserves, especially those which originate in conjunctural movements of export prices or inflows of foreign finance, also tend to have inflationary effects. Spending capacity on investment producing this type of surplus does not always stand at the same level as the consumer's spending capacity.

Lastly, it should be added that the behaviour of the agents of the socio-economic system, in the case of manifest inflation and even more so in an international situation of rising prices, constitutes a factor of inflation which is by no means to be despised. In their haste to defend themselves and on occasion to profit from the inflation itself, they act in such a way that they promote new price increases. In such cases, the importer groups, when they introduce criteria for the cost of replacing imported merchandise in setting their selling prices, become in turn agents for the import of inflation.

(b) *Factors of inflation*

The main feature of the re-emergence of inflation in Costa Rica lies in the simultaneous presence of three factors of inflation: the slower growth of production in certain sectors, the persistent increase in the liquidity of the system and the violent impact of imported inflation.

The growth rates of sectoral production described in the first part make unnecessary any comment on the evolution of economic activity; it is, however, worth repeating that the slow growth of agriculture is one of the most significant facts.

As regards increases in liquidity, the persistent increase of the factors of monetary expansion may be observed. Credit grew by 17.5 per cent in 1972 and 10.2 per cent in 1973; similarly, international reserves showed growth rates which also signified a considerable monetary expansion, when they increased by 9.1 per cent in 1972 and 46.2 per cent in 1973 (see table 110).

These increases in the factors of expansion may be explained partly by the growing deficit in the budget, as may be seen from table 112.

The budget deficit shows appreciable increases, especially in 1973 (over 28 per cent) and it is financed for the most part by domestic credits.

The increases in credits to the private sector may be explained by an important transformation in the finance system stemming from the operation of new financial institutions, as will be seen when the main economic policy measures are described.

Table 112. Costa Rica: Financing of budgetary expenditure
(Millions of colones at current prices)

	1971	*1972*	*1973*
Total expenditure . .	1,250.7	1,433.4	1,892.3
Current income . . .	908.4	1,040.3	1,386.6
Deficit	342.3	393.1	505.7
Financing.			
With external credit .	106.9	175.2	198.2
With domestic credit	174.0	232.3	302.6
With other resources	81.4	−14.4	4.9

SOURCE: Ministry of Finance of Costa Rica.

Table 113. Costa Rica: indicators of inflation
(Percentage variations)

	Monetary expansion	*Growth of the product*	*Import price index*	*Wholesale price index*
1972 . .	17	5.0	8%	5.4
1973 . .	13	3.9	15%	16.4

SOURCES: Tables 91, 101, 106 and 110.

As from 1972 and especially in 1973, the external sector of Cost Rica underwent a fundamental change as regards prices. Import prices in this period showed unexpected increases (8 per cent in 1972 and 15 per cent in 1973) compared with an annual 3 per cent during the period 1965-1971. This sudden increase, together with the large share of imports in the country's economy, affected domestic prices as a matter of course. As has already been observed, inflation speeded up after 1973 and the heavy dependence on imported supplies lessened the possibilities of cushioning the effects of imported inflation.

The indicators summarized below show clearly that the behaviour of the three factors of inflation already mentioned was compatible with the speeding-up of inflation (see table 113).

Analysing of inflation during the period in greater detail, it may be seen that the indicators of inflation for 1972 give evidence of certain asynchronisms which have no convincing explanation (see table 106). On the one hand, the speeds of growth of the three indicators mentioned do not coincide. Both the retail price index and the implicit deflator of the product show increases greater than those recorded the previous year, while the wholesale price index shows a slower rate than in 1971. Attempts to reduce increases in monetary expansion would seem to have been successful in mitigating the rise in prices (see table 110), despite the extremely small increase in the volume imported (1.1 per cent in 1972).

As has already been seen, the events of 1973 were very different. In this year the different factors of inflation acted in the same direction, complementing one another and forming an extremely clear picture. There is no doubt that the initial impulse for the re-emergence of price increases came from imported inflation. Heavy dependence on imported inputs and final goods was a very vulnerable flank of the Costa Rican economy, and paved the way to the spread of the initial impetus. It is not easy to say what share the different factors analysed have in the process of inflation, since reciprocal interaction reproduces

price increases the origin of which it is difficult to identify. However, during this last period the reasons given above tend to assign imported inflation a more decisive influence and this opinion is confirmed by the detailed analysis of the price increases given below.

(c) *The evolution of inflation*

Tables 114 and 115 contain detailed information on the variations in wholesale prices during the two half-year periods of 1973, and this makes possible a more authentic identification of the recent process of inflation. The items which show the largest price increase during that period and which, in view of their weighting within the whole, have a strong influence on wholesale price movements have been selected.

The data given in table 114, which refer to the first half of 1973, indicate the important influence of the price increases in agricultural commodities, such as meat, fresh fruit and vegetables and, following these in order of importance, the price of construction materials and various paper products. As regards meat and hides, which carry great weight in the economy of the country and in the general level of prices, the importance of the changes in their export prices should be underlined. The international price of beef rose during the first half of 1973 by approximately 65 per cent. This increase, of course, had a favourable effect on the balance of payments, but at the same time produced increases in domestic prices. It is usual for producers, faced with differently priced markets, to direct their sales so as to make maximum profits. If it is also borne in mind that exchange modifications were a further stimulus to exports, the pressures on domestic prices were bound to find expression and materialize in increases such as those described (see table 114).

Among other items where price rises cannot be attributed to seasonal variations, mention may be made of construction materials, fertilizers and miscellaneous paper products. In such cases, the modifications in domestic prices are basically to be explained by price increases in imported inputs and final products, to which should be added the modifications in the exchange rate which will be analysed at a later stage.

Lastly, fresh fruit and vegetables showed surprising increases. In the case of the former there is a distinct problem with middlemen who take

Table 114. Costa Rica: variations in wholesale prices during the first half of 1973
(*Percentages*)

	Variation between December 1972 and June 1973	*Weighting at 31 December 1972*	*Incidence in the general index*
Meat	27.9	7.5	2.1
Vegetables	19.2	5.5	1.0
Fresh fruit	31.8	10.5[a]	3.3
Textile products	15.4	1.1	0.2
Hides	21.3	0.7	0.1
Construction materials	12.0	13.3	1.6
Fertilizers	12.9	1.9	0.2
Clothing	9.5	4.4	0.4
Footwear	9.8	1.4	0.1
Household articles	9.7	1.4	0.1
Miscellaneous paper products	15.0	3.0	0.4
Group of above items	18.7	50.7	9.5
Remaining items in the index[b]	−0.4	49.3	−0.2
General index	*9.3*	*100.0*	*9.3*

SOURCE: OFIPLAN, estimates of the United Nations Advisory Group.

[a] The heavy weighting of this item is particularly striking.

[b] There is a small difference in calculation compared with the source used.

Table 115. Costa Rica: variations in wholesale prices during the second half of 1973
(*Percentages*)

	Variation between June 1973 and December 1973	*Weighting at 30 June 1973*	*Incidence in the general index*
Vegetables	35.4	6.0	2.1
Alcoholic beverages	18.5	3.7	0.7
Other food-stuffs	53.3	6.0	3.2
Textiles and wool yarn	208.3	0.3	0.6
Textiles and cotton yarn	23.0	3.8	0.9
Jute and hemp	25.0	0.3	0.1
Hides	19.0	0.8	0.2
Construction materials	15.2	13.6	2.0
Fertilizers	25.7	2.0	0.5
Miscellaneous paper products	20.6	3.2	0.7
Group of above items	27.6	39.7	11.0
Rest of items in the index	7.9	60.3	4.7
General index	*15.7*	*100.0*	*15.7*

SOURCE: OFIPLAN, estimates of the United Nations Advisory Group.

Among other items where price rises cannot be attributed to seasonal variations, mention may be made of construction materials, fertilizers and miscellaneous paper products. In such cases, the modifications in domestic prices are basically to be explained by price increases in imported inputs and final products, to which should be added the modifications in the exchange rate which will be analysed at a later stage.

Lastly, fresh fruit and vegetables showed surprising increases. In the case of the former there is a distinct problem with middlemen who take

profit margins which are unreasonably excessive; the differences between producer prices and wholesale distribution prices are considerable.

As regards vegetables, the representative product is the bean, a component of the basic diet, four fifths of which is imported. The import price of this product underwent excessive increases: the cost of importing one ton rose from 270 to 970 dollars between the beginning of 1973 and April 1974.

The influence of the external sector in the increase of domestic prices in the first half of 1973 is therefore clear. It is, however, useful to point out once again that these exogenous pressures were accompanied by significant increases in the liquidity of the Costa Rican economy.

It may be seen once again in table 115, which sums up the main price rises during the second half of 1973, that external inflation continued to have a decisive influence. Vegetables, other food-stuffs, textile products, fertilizers and miscellaneous paper products are closely linked to some form of external supply and are thus subject to international variations in their prices. Construction materials experienced the effect of external prices, and also faced a growing domestic demand, which at times caused problems of shortage and gave impulse to the increasing trend.

3. *Inflation in 1974*

In 1974, inflation in Costa Rica followed different trends in the two six-month periods. Data available for the first six months show clearly that the inflationary process became stronger. The half-yearly rate recorded for the wholesale price index was 26 per cent, well above previous half-yearly variations. In the second half of the year the increase in prices was 9.8 per cent (see table 18).

It would appear that the inflationary factors of importance during 1973 continued in full force in the first half of 1974, since monetary expansion recorded a rate of increase of the order of 9 per cent and import prices increased by 31 per cent in 1974.

Some preliminary estimates of the current value of imports during the first half of 1974, which fluctuated around 300 million dollars–nearly 50 per cent up on imports for the same period in 1973–show clearly the impact of import prices, while the volume imported, using the same estimates, shows no significant increase.[145]

The products which underwent the largest increases during this period confirm the above considerations (see table 116). The most important increases were, of course, in fuels, fertilizers, electricity and electrical articles for domestic use, soap, wax, insecticides and fungicides; important increases are also to be seen in milk products, sugar, bread, cereals, etc.

Table 116. Costa Rica: variation in wholesale prices during the first half of 1974
(Percentages)

	Variation between December 1973 and June 1974	*Weighting at 31 December 1974*	*Incidence in the general index*
Fuel	85.5	3.9	3.3
Electricity	36.8	2.1	0.8
Dairy products	38.1	3.2	1.2
Meat	16.7	8.2	1.4
Processed products of animal origin	20.4	1.8	0.4
Cereals	29.3	3.6	1.1
Dried fruit	23.5	2.3	0.5
Sugar, bread and other	35.6	8.0	2.8
Cotton fabrics	29.4	4.0	1.2
Construction materials	26.5	13.5	3.6
Fertilizers	57.4	2.2	1.2
Insecticides and fungicides	34.4	0.7	0.2
Soap and wax	41.1	3.3	1.4
Men's clothing	21.6	4.1	0.9
Household electrical articles	32.7	1.2	0.4
Group of above items	31.6	62.1	19.6
Rest of items in the index	16.9	37.9	6.4
General index	*26.0*	*100.0*	*26.0*

SOURCE: OFIPLAN, United Nations Advisory Group.

Although 15 items showed rises of over 20 per cent during the half-year, the most serious effects were concentrated in fuels, constructions materials and sugar, bread and others. In that the price increases were 85.5 per cent for fuels, 26.5 per cent for construction materials and sugar and 35.6 for bread and others, their impact on the structure and level of prices was considerable. The extraordinary increase in the price of an input as extensively used as fuel causes very widespread and sometimes multiple repercussions in the price structure of an economy. Price increases in construction materials also have a great dissemination capacity. Price increases in sugar and bread are no less important, these two products being very closely linked to the cost of living. From this angle, the Government's intention to maintain the purchasing power of wages and pressures from the

[145] Preliminary estimates of OFIPLAN.

trade union sectors became part of the group of elements which affected prices.

In the second half of 1974, as stated previously, the rate of inflation declined. It is not easy to say whether this trend is likely to continue in the future. The increasing liquidity of the economy, the rise in import prices and the drastic fall in the rates of domestic production are not compatible with the slowing down of the inflationary process. A notable fact, however, is that the 13.1 per cent increase in imports meant an increase in supply which undoubtedly favoured the easing of inflationary pressures. In any case, it is too early to hazard any opinion regarding this inflexion of inflation. The fluctuations that normally characterize these processes open a question which will be elucidated only in the light of the price increases in 1975.

4. *The peculiarity of inflation in Costa Rica*

The description and analysis of the above points enable inflation in Costa Rica to be qualified as a very special, and in some aspects a typical phenomenon. External inflation which determines the formation of domestic prices has direct repercussions on the base of the economic system and filters into the rest of the economic sphere in some very curious forms. When it does not suffer the direct impact of import prices, it shows the indirect effects of the variations in export prices, which eventually also take the form of pressures on domestic prices. An example to illustrate this is that of dairy products, which underwent a price rise of 38.1 per cent in the first half of 1974: international prices provided an incentive for livestock activity to produce beef, to the detriment of the production of milk and milk products.

The basic elements of a price, when the system is stable, are basically the cost of production, the cost of distribution, taxes and the different profit margins in the various cases of intermediation between the producer and the consumer. The profit margins are in turn mainly a function of the supply and demand relationship of the product. In situations of manifest inflation, as in Costa Rica, these components undergo pressures both from costs and from demand. The first effect of external inflation, as has been seen, was to increase the cost of imported inputs and final products, and this may be qualified as a case of inflation of costs of external origin; as has already been said, the high import coefficients of Costa Rica make the country very vulnerable to this type of inflation. This feature of the structure of the economy meant that the first impact was propagated and reproduced fairly freely in economic activity. The increase in import prices meant heavy deficits on the current account, while the inflow of external finance made increased imports possible and signified disequilibria in the monetary system which in turn gave rise to new inflationary pressures.

The different factors of inflation succeeded each other in time and finally as from mid 1973 made up a process in which the inflationary pressures were receiving internal and external stimuli, while their dissemination in the economic system was made easier by the structural disequilibria already described.

E. INFLATION AND MAIN ECONOMIC POLICY MEASURES

The purpose of the previous chapters was to examine the most important economic phenomena connected with the interpretation of the recent inflationary process in Costa Rica. Government measures affecting variations in domestic prices have been expressly excluded from this interpretation, since it would have been difficult to examine economic policy measures simultaneously with the factors of inflation. Now that the latter have been identified, it is easier to evaluate the effect of the principal measures and instruments, which shed additional and invaluable light on the subject.

It must be clearly understood from the outset that during the period under review there was no anti-inflationary policy of the kind adopted by other countries long affected by inflation, in which it is even possible to identify different attempts based on a variety of strategies. In the case of Costa Rica, inflation was a new phenomenon and the measures put into effect by the Government over the last three-year period were the result of pragmatic decisions rather than of an integral conception of stabilization policies. Moreover, the principal measures had other objectives, but inflation in some degree distorted the expected results, and thus triggered a different type of inflationary pressure.

1. *Public sector financing policy*

The figures for total budget expenditure shown in table 117 indicate a trend towards the strengthening of the public sector's position. The growth of public investment at a rate of 36 per cent in the last three-year period confirms this view. The implementation of this policy was financed with funds from abroad and with domestic resources.

The most important measure from the standpoint of public sector financing and as an instrument for guiding the economic process was

Table 117. Costa Rica: total budget expenditure and financing
(Millions of colones at current prices)

	1971	*1972*[a]	*1973*
Budget expenditure	1,242.9	1,409.3	1,865.4
Administration expenditure	718.2	853.0	1,023.6
Legislature	15.5	17.6	19.6
Executive	649.8	772.0	905.1
Judiciary	45.5	52.7	61.5
Elections tribunal	7.4	18.7	36.4
Current and capital transfers	314.3	326.0	460.2
Debt service payments	188.9	214.5	287.9
Investment in semi-public enterprises	–	–	69.2
Floating debt	–	–	12.0
Loans to public institutions	21.9	8.8	12.5
Adjustments 13th month and other	7.8	24.1	26.9
Total expenditure	1,250.7	1,433.4	1,892.3
Current income	908.4	1,040.3	1,386.6
Deficit	342.3	393.1	505.7
Financing of the deficit			
With external credit	106.9	175.2	198.2
With domestic credit	174.0	232.3	302.6
Other resources	81.4	−14.4	4.9

SOURCE: Ministry of Finance of Costa Rica.
[a] Some minor discrepancies in 1972 derive from the preliminary data available.

undoubtedly the tax reform of March 1972.[146] The principal changes introduced at that time relate to the general sales tax and selective taxes on consumption, and to taxes on income of private persons and enterprises.

With respect to the tax on transactions in goods and services, a distinction was made between the general sales tax and the selective taxes on goods according to the extent to which they were considered to be essential products. A general rate of 5 per cent was established on the price of transactions–a single rate payable at one stage only–and a supplementary group of rates ranging from 10 to 50 per cent, also payable in one stage, for a specific list of products. The Executive was authorized to alter the content of this list and the respective rates, so that this instrument would have the required flexibility.[147]

As regards personal income tax, the main feature of the reform is that the rates are more progressive, although bigger deductions are made for dependants. The old scale comprising 30 income strata, with rates ranging from 1 to 30 per cent, was converted into a scale of 12 strata, the rates ranging from 5 to 50 per cent. In the same spirit, the minimum income for professionals, which was assumed to be 10,000 colones annually, was raised in accordance with a scale extending from 40,000 colones for professionals with studies of four years' duration to 70,000 colones for surgeons.

The reform of taxes on profits of enterprises also introduced more progressive rates; four strata were established with rates ranging from 5 to 40 per cent. As regards taxes on profits remitted abroad, on the whole the rates were increased and other single taxes were levied.[148]

These reforms had a significant effect on the amount and structure of government income: table 118 shows the amounts collected in respect of the principal items.

A particularly striking fact in the analysis of inflation in Costa Rica is the extraordinary increase in indirect taxes on consumption. These

[146] Banco Central de Costa Rica, "*Ley de Reforma Tributaria*", *Memoria Anual*, 1972, vol. 3.
[147] Banco Central de Costa Rica, "*Ley de impuesto sobre ventas y ley de consolidación de impuestos selectivos al consumo*", op. cit.

[148] The following items are identified:
(*a*) Public entertainment: the rate was raised from 5 to 10 per cent;
(*b*) News service, records, etc.: the rate was fixed at 20 per cent:
(*c*) Fees paid to members of boards of directors and for technical services and royalties: 20 per cent;
(*d*) Dividends and shares: fixed at 15 per cent;
(*e*) Interest on loans: fixed at 10 per cent;
(*f*) Income from films for cinema, television, etc.: raised from 5 to 10 per cent.
SOURCE: Inter-American Committee on the Alliance for Progress (CIAP), Sub-Committee on Costa Rica, report mentioned previously.

Table 118. Costa Rica: composition of tax revenue
(Millions of colones at current prices)

	1971	1972	1973	Percentage variation 1971-1973
Tax revenue	826.2	934.5	1,254.2	51.8
Direct taxes	190.3	227.7	309.5	62.6
Income tax	182.8	213.0	291.1	59.2
Other direct taxes	7.5	14.7	18.4	145.3
Indirect taxes	635.9	706.8	944.7	48.6
Taxes on cigarettes and alcoholic beverages	79.4	85.0	99.9	25.8
Taxes on consumption	39.4	121.9	201.8	412.2
Taxes on sales	115.6	131.5	160.3	38.7
Taxes on gasoline consumption	56.9	62.5	68.6	20.6
Import taxes	192.0	159.4	196.8	2.5
Export taxes	4.8	5.6	6.7	39.6
Taxes on coffee	29.3	27.2	67.8	131.4
Stamp tax	11.1	12.9	17.3	55.9
Economic stabilization tax	62.7	50.4	64.8	3.3
Other indirect taxes	44.7	50.4	60.7	35.8

SOURCE: Ministry of Finance of Costa Rica.

taxes rose by over 400 per cent between 1971 and 1973, which raised their share in indirect taxes from 6.2 per cent to 21.4 per cent over those years. The transfer of these taxes to prices was legally authorized,[149] so that their effect on price levels was an additional factor of inflation, especially if it is considered that the increased tax collections financed more public spending, with all its implications in terms of the growth of demand for goods and services.

It will be recalled that the years 1972 and 1973, in particular, showed rising deficits, and the financing of these deficits, with external resources or domestic credit, led in one way or another to an increase in the money in circulation (see table 117). Capital expenditure, which expanded significantly, was not generally reflected in increases in the supply of goods and services which might have counteracted the pressures on prices. The maturity periods and rate of investment generated demand effects, and only marginally produced some indirect flexibility of supply. As may be observed, the higher taxes, which had already had some inflationary impact, financed an appreciable expansion of budget expenditure, which also affected price levels.

[149] Tax Reform Law, chapter VIII, article 18. Price control: the Department of Internal Trade of the Ministry of Industry and Trade shall ensure that prices of goods not subject to selective consumer taxes are not adjusted as a result of the promulgation of this Law, and also that the prices of goods liable to tax are not increased unduly owing to the levying of these taxes.

2. *Private sector financing*

As regards the financing of the public sector, it is useful to note that the establishment of a group of financial institutions in September 1972 marked an important change in the general system of financing. Up to that time it had been the exclusive prerogative of State banks to tap savings deposits and grant loans to enterprises and private persons; since then this right has been accorded to other financial intermediaries engaged in the following activities:[150] provision of funds, working capital and general financing for activities performed by other enterprises, associations or physical persons; and purchase of shares, bonds, securities and other financial or credit instruments or securities issued by other enterprises or associations. Physical persons engaged in these activities were also included in this category of financial associations. The boom experienced by these institutions, which tapped an increasing amount of savings, is accounted for by the fact that they paid higher interest rates than the banks. They supplied operating capital to industrial and commercial enterprises, which in their turn were able to give credit to their clients, particularly for the purchase of durable consumer goods. This mechanism has obviously affected prices, both from the standpoint of the higher cost of money and from that of its faster circulation and the consequent

[150] *"Ley de regulación de sociedades financieras de inversión y de crédito especial de carácter no bancario"*. *La Gaceta*, No. 180, 22 September 1972.

increase in the propensity to consume which is generally the result of consumer credit.

In discussing the increases in liquidity in the economic system, it was noted that the private sector was the main beneficiary of the credit granted, since it obtained a consistently high proportion of it (see table 110). The figures for the monetary balance show that the policy of providing financial backing for private activities, basically those connected with exports of manufactures, has been the Government's constant concern in the period under review.

3. *Foreign exchange policy*

The balance-of-payments position in 1969 and 1970 was the cause of significant reductions in international reserves (65 per cent in the first year and 63 per cent in the second). Since projections for 1971 also indicated an unsatisfactory situation with regard to foreign trade, the Government decided to modify its foreign exchange policy.

As from the middle of June 1971, the Costa Rican monetary authorities introduced modifications involving the establishment of a dual system of foreign exchange.[151] An official market was established for essential transactions for economic development purposes, with a rate of 6.65 colones to the dollar, and a free market for other operations. A month later a system of exchange surcharges was introduced whereby imports were grouped in three categories according to how far they were considered as essential goods. The first category of products was exempt, while the other two were liable to surcharges of 15 and 30 per cent. As in the previous case, the distinction was based on the nature of the imports in relation to development aims.

Although the dual and foreign exchange surcharge systems enabled a certain control to be exercised over the use of foreign exchange, they did not have the desired results since other items were gradually added to the preferential import list and operations on the official market amounted to about 90 per cent of the total. The main reason for enlarging the list was the difficulty of placing exports in the Central American market, in view of the rise in production costs as a result of the exchange surcharges.

At the beginning of 1972, Costa Rica returned to the dual exchange system, but the preferential list continued to have a decisive effect, since almost 80 per cent of the transactions in terms of value were effected on the official market. Since by the middle of 1972 the position with regard to the balance of payments and international reserves had not shown much improvement, in October of that year the preferential list was drastically cut down, only 85 items of the Central American Standard Customs Nomenclature (NAUCA) remaining out of the 450 on the previous preferential list.

These new restrictions in obtaining foreign exchange on the official market made imports more expensive, which raised the production costs of export industries relying on imported inputs. To offset the higher production costs and ensure that such exporters' possibilities of competing on the Central American market were not jeopardized, they were authorized to liquidate on the free market 50 per cent of the foreign exchange obtained from exports. This benefit was also accorded to exporters of non-traditional agricultural and fisheries products. The free market rate of exchange was 8.60 colones to the dollar, or 30 per cent higher than the rate on the official market. Although the list of 85 items was increased, operations on the official market came to represent 22 per cent of total imports, a proportion which rose to 30 per cent in 1973 when new import items were introduced in this market.

The concession of liquidating on the free market 50 per cent of the foreign exchange obtained from non-traditional and agricultural exports was also extended to the independent banana producers, for a proportion of up to 39 per cent of their total sales abroad.

The policy of discrimination in the use of foreign exchange slowed the growth of imports during the first half of 1973, an additional factor being the increased prices, mainly of raw materials for industry and, of course, fuels.

From the angle of interpreting the inflationary process, the exchange policy adopted in the period 1970–1974—whether through the dual foreign exchange market or foreign exchange surcharges—has in different ways made certain imports more expensive. It is even likely, from this point of view, that the efforts to solve the balance-of-payments problem have given additional impetus to the rise in production costs. A wide range of imported inputs, besides becoming more expensive in terms of foreign exchange owing to external inflation, underwent further increases in national currency due to the rise in the exchange rate. The combination of these effects exerted pressure on domestic prices on the cost side.

Furthermore, the reduction in the amount of money in circulation which is attributable to the sales of foreign exchange at higher exchange rates, was more than offset by the increases in liquidity resulting from bank credit to the private and

[151] See Banco de Costa Rica, *"Exposición sobre medidas adoptadas para corregir el problema de la balanza de pagos"*, *Memoria anual*, 1971, vol. 3.

public sectors and the inflow of foreign capital. In addition, the possibility of a major part of the value of exports being liquidated on the free market at a rate of 8.60 colones to the dollar meant significant surpluses on that market, while the official market, in view of its exchange rate of 6.65 colones to the dollar, recorded a constant deficit. The Central Bank was compelled to purchase foreign exchange resulting from the surplus on the free market to cover the deficit recorded by the official market. The monetary expansion involved in this operation amounted to 87.8 and 193.7 million colones in 1972 and 1973, respectively.[152]

Costa Rica's foreign exchange policy should be evaluated within the general context of external inflation, in terms of the increasing liquidity which its economy experienced and taking into account that the rate of growth of the most important sectors of production declined. The exchange mechanism has not, of course, been the decisive factor of the inflationary pressures. The adjustments in the exchange rates took place throughout a period in which other inflationary factors were fully in operation and did no more than join forces with the other sources generating inflation. However, the maintenance of the exchange rate from 1973 onwards in the face of increasing domestic inflation undoubtedly lessened the effect of imported inflation.

The foreign exchange policy described above, owing to its flexibility and the appearance of the external factors indicated, does not seem to have had the desired impact on the balance of payments. The trends of imports of non-essential consumer goods have not changed, despite the increase in prices. On the whole, the inflationary processes stimulated a sometimes regressive redistribution of income owing to the differing capacity of the factors of production to transfer their increasing costs to the consumer and to benefit from the growth of demand for their products.

4. *Prices and wages policy*

In a country which until a short while ago recorded constant indexes of stability, it would be difficult to find price policies which do not respect the basic equilibria of the economic system. The appearance of inflation in the last few years encountered a public apparatus which was not accustomed to this type of concern. Nevertheless, at the first signs of inflation, government action in connexion with prices had two basic aims: first, to control prices of essential goods in order to safeguard the level of living of the population and, secondly, to guarantee the possibilities of competition of non-traditional exports in the Central American market.

As regards the first point, it is only in the last few years, and basically as a result of tax reform, that the government decisions have had a more direct influence on the fixing of prices. In the face of the new situation of changing costs and prices, the first government measures were aimed at containing speculation. It was not easy, however, to enter into a territory where there had formerly been no need for drastic action. The capacity for exercising the necessary control in this field was gradually formed. The Department of Internal Trade of the Ministry of Industry and Trade, which is the agency mainly responsible for implementing the prices policy, has redoubled its efforts in terms of studies, costs and control programmes designed to improve the efficiency of this important aspect of general economic policy and give it a more organic structure.

One of the instruments used to guarantee competitive prices of non-traditional exports, as mentioned previously, was the exchange rate. The concession of liquidating 50 per cent of the foreign exchange obtained from these activities at a higher exchange rate on the free market was an important palliative in the face of the rising price of inputs and distribution costs.

Much the same observations as those made on the prices policy are applicable to the wages policy: the price stability during the past decade and the rapid growth of economic activity did not confer on this aspect the vitally urgent character which recent inflation has given it. A report of the Ministry of Labour and Social Security[153] comments on the lack of any wages and employment policy, and points out that the institutional structure of the State does not permit any planned action in this respect. However, the wages policy found expression mainly in the establishment of minimum wages, which in some degree provides a frame of reference for determining the wages of other categories of labour. There is a system in force in Costa Rica for the establishment of minimum wages for the private sector, with the exception of workers in the banana companies.[154]

[152] Data supplied by the Central Bank of Costa Rica.

[153] *Antecedentes para una política nacional de salarios en Costa Rica*, June 1974.

[154] "All workers shall have a right to a periodically readjusted minimum wage for a normal working day, which will ensure their livelihood and well-being. It shall always be an equal wage for equal work under equal conditions of efficiency. All matters related to the establishment of minimum wages shall be the responsibility of the technical body designated by law" (Political Constitution of 1949, article 57).

A National Wages Council, which is a permanent technical body, is responsible for establishing minimum wages for each branch of economic activity: agriculture; mining and quarrying; manufacturing and processing industry; trade; transport, storage and communications; services; and other activities. The National Wages Council is composed of nine members with equal representation of the State, employers and workers. The main criteria underlying the establishment of minimum wages are, first, to ensure for the worker and his family adequate food, housing and clothing, education for his children and any other needs established for the minimum level of families with the lowest purchasing power.[155] Secondly, the payment capacity of the various activities is considered and their profit-making capacity safeguarded. In view of the conditions of price stability prevailing in Costa Rica, it was stipulated that the minimum wages should, generally speaking, be reviewed every two years.

The establishment of minimum wages is important not only in so far as the wages themselves are concerned, but also because the variations in the minimum wage are taken as a point of reference for settling other levels of remuneration.

The wages policy in the public sector, where the workers are covered by the civil service system, is based on the Law on Wages in the Public Administration.[156] There are two mechanisms in this law for raising wages: on the basis of seniority and in terms of increases in the price index, provided it rises by at least 4 per cent annually.

Lastly, both individual and collective contracts may be freely entered into, provided the parties do not fix wages below the established minimum.

It is clear from the above account that mechanisms exist for maintaining the purchasing power of wages. When the price increases were small, these adjustment mechanisms usually served their purpose. In the three years 1971-1973, however, in the face of substantial increases in the level of domestic prices and the loss of dynamism of economic activity, it is possible that the general increases, at least for a large sector of wage-earners, did not manage to maintain the purchasing power of labour remuneration.

Table 119 shows the minimum wages by sector of economic activity. As can be seen, there is considerable disparity between the increases in the minimum wages for the various activities, and between the wages in absolute terms. In view of the price increases in 1973 and the early months of 1974, in April of the latter year the Government decreed an extraordinary adjustment of all minimum wages, in accordance with the scale shown in table 120, before the expiry of the previous wage scale on 1 October.

The redistributive nature of this adjustment, which establishes higher rates for the lower wage levels, has basically benefited the agricultural worker. This adjustment has had repercussions on freely contracted wages; the workers organized in trade unions have based their petitions on the highest percentage adjustment in the minimum

Table 119. Costa Rica: minimum wages by sector of economic activity
(Colones at current prices per day)

	1970-1972	*1972-1974*	*Percentage variation*
Agriculture			
Coffee (worker)	12.00	12.90	7.5
Bananas (worker)	18.50	20.80	12.4
Ice-cream factories (worker)	12.40	14.40	16.1
Bakeries (baker)	20.70	23.80	15.0
Textile factory (weaver)	15.00	17.25	15.0
Shoe factories (cutter)	16.15	20.40	26.3
Shirt factory (cutter)	16.10	18.05	12.1
Printing offices (type-setter)	38.50	41.20	7.0
Soap factory (worker)	13.60	15.25	12.1
Electrical workshop (skilled worker)	25.90	28.50	10.0
Construction (skilled worker)	27.75	28.50	2.7
Commercial activities (assistant)	15.80	13.70	12.0
Public transport (driver)	21.20	23.20	9.4
Laundries (various occupations)	14.80	17.00	14.9

SOURCE: Ministry of Labour and Social Security, Wages Office.

Table 120. Costa Rica: adjustment of minimum wages, April 1974

Minimum daily wages	*Percentage adjustment*
12.80 to 15.00	41.0
15.10 to 17.50	35.0
17.60 to 20.00	30.0
20.10 to 25.00	25.0
25.10 to 30.00	20.0
30.10 to 35.00	15.0
35.10 to 96.20	10.0
96.30 and over	–

SOURCE: Ministry of Labour and Social Security, Planning, Programming and Statistical Department.

[155] *Ibid.*
[156] Law No. 2166 of 9 October 1957.

wages. Moreover, the Government granted an across-the-board adjustment of 200 colones a month for all workers in the public sector.

Despite the Government's plausible aims of maintaining the purchasing power of wages and basically of the lowest incomes, the recrudescence of inflation seems to be affecting the wage-earners' purchasing power. A report of the Integrated Working Groups for the restructuring of the Central American Common Market states that the level of wages in the lowest income sectors is not keeping pace with the increase in the prices of mass consumption goods. It further states that between May 1973 and May 1974 the cost of the basic basket for a family with a weekly income of 100 colones increased by 63 per cent, and that for families earning 200 colones weekly by 43 per cent. These two income strata comprise 65 per cent of the total Costa Rican labour force. To judge from these data, the prices and wages policy would seem to be one of the most delicate areas in the economic policy field.

The conception and implementation of a wages policy which will benefit the broad masses and at the same time will not create inflationary pressures is hampered at present by two important obstacles. First, the persistence of imported inflation on whose effects State action, in the case of Costa Rica, has less room for manoeuvre and secondly, the slow growth of production, particularly in 1974, which shows no signs of any significant improvement. To achieve consistency between the production and financial spheres, while respecting the purchasing power of wages within the context described in this study, constitutes a serious challenge in terms of the conception and implementation of an over-all economic policy.

5. ECUADOR

A. INTRODUCTORY NOTE

The review presented in this document concerning inflation in Ecuador covers a comparatively short period from about 1968 to 1974. This is because inflation is a recent development in Ecuador, which began to acquire some importance only in the late 1960s.

The domestic price distortions became definitely serious, however, at the end of 1972 and in 1973-1974, when the Ecuadorian economy started to receive the full impact deriving from its newly assumed status as a petroleum-exporting country.

This resulted, on the one hand, in a very substantial increase in Ecuador's exports, international reserves and capacity to import and, on the other hand, in making its economy more sensitive to international market price fluctuations, which were intensified in those years.

Therefore, stabilization policies gradually took shape in what was, for various reasons, virtually an unknown context to the government officials concerned. In fact, the stabilization measures were determined and adjusted on the spot in the course of 1973 and 1974. This circumstance was as far as possible taken into account in preparing the present study.

B. SALIENT FEATURES OF ECONOMIC TRENDS IN ECUADOR

During the period 1971-1974, the development of the Ecuadorian economy was influenced by a number of predominant factors.

First, in mid-1972 the country started to export petroleum in significant quantities--which within a short time had reached over 200,000 barrels a day--as the culmination of the process initiated in 1967-1968 with the discovery of oil reservoirs, which in its turn led from 1969-1970 onwards to substantial direct investment by foreign companies.

The operation and, previously, the installation of this new mining activity had various far-reaching effects on the whole economy, which it is difficult to specify and examine briefly in summarized form. It seems evident, however, that the most important repercussions made themselves felt in the acceleration of the over-all growth rate, in the expansion of external sector and public sector activities, and in different effects on price movements.

Secondly, the existence of two closely linked situations continued to be observed during the period under review. On the one hand, the trend recorded by the agricultural sector was far from dynamic, which resulted in low rates of growth for agricultural production. On the other hand, over the same period examined there was no eloquent decrease in the high proportion of the economically active population, which is excluded from the market for manufactures and which makes up what is normally called the marginal population of the country.[157]

[157] See CIAP, *Situación, principales problemas y perspectivas del desarrollo económico y social del Ecuador* (CIAP/635), 19 October 1973, p. 17.

Thirdly, it is worth noting the increasing significance acquired by the inflationary process, which culminated in 1973, and particularly in the first part of 1974, in periodical rates of price increases far higher than ever recorded before in Ecuador, and even similar to the parallel rates observed in other Latin American countries with a "tradition" of inflation.

The creation of this problem, the study of its origins and the review of the anti-inflationary policies adopted–together with the relation between these aspects and the dominating factors mentioned above–constitute the central theme of this document.

Lastly, it is interesting to note that during the period under review, specifically in February 1972, a change took place in the country's political administration. The main economic policy guidelines of the new administration were established in the Integrated Plan for Change and Development (*Plan Integral de Transformación y Desarrollo*) 1973-1977.

1. *Growth trends*

Between 1970 and 1974 the rate of growth of the Ecuadorian economy–in terms of the growth of the gross domestic product–showed a rising trend, averaging 8 per cent annually, which meant a considerable acceleration over the rate of 5.5 per cent recorded in the period 1965-1970 (see table 121).

In view of the fact that since the middle of the 1960s the population growth rate had remained steady at around 3.4 per cent annually, this acceleration was even more evident in the trend shown by the *per capita* GDP (2 per cent in 1965-1970 and 4.5 per cent in 1970-1974). According to ECLA estimates, Ecuador's population–which at the end of 1974 was around 7 million–obtained for that year a GDP amounting to some 500 dollars per head compared with about 400 dollars in 1970, both values in terms of constant 1970 prices.[158]

(a) *Total supply and demand*

A study of the total supply and demand situation reveals that, in the years 1970-1974, dynamic growth coincided with a rapid expansion of exports. As a result of this trend, the ratio of exports to the GDP rose from 15.8 per cent in 1970 to 21.8 per cent in 1973 (although it dropped to 18.3 per cent in 1974, for reasons connected with the price of oil), which is undoubtedly a substantial change demonstrating the new outward-looking approach of the Ecuadorian economy (see table 122).

Another important aspect was the trend of the investment rate. Up to the middle of the 1960s the ratio of gross fixed investment to the GDP declined steadily to values of around 11 per cent in 1965-1966, compared with an average for Latin America of about 18 per cent. In 1967 this ratio started to rise rapidly and steadily, reaching a relative peak of 24 per cent in 1971. Investment in oil production activities was mainly responsible for this increase; in fact, in 1971 it represented over

[158] It is estimated that the average *per capita* GDP for Latin America as a whole (19 countries) amounted, in dollars at 1970 prices, to 640 in 1970 and 730 in 1973. In other words, the value for Ecuador represented 63 per cent of the Latin American average in 1970, and 68 per cent in 1973.

Table 121. Ecuador: total supply and demand

	Millions of sucres at 1970 prices 1970	*Annual growth rate (percentages)*			
		1971	*1972*	*1973*	*1974*[a]
Total supply	*43,130*	*8.5*	*4.5*	*11.1*	*12.4*
Gross domestic product (at market prices)	35,501	6.5	6.2	10.5	9.2
Imports	7,629	17.7	−2.5	13.8	26.6
Total demand	*43,130*	*8.5*	*4.5*	*11.1*	*12.4*
Exports	5,590	8.3	25.7	27.2	−8.5
Gross domestic investment	6,936	41.2	−10.4	13.6	18.9
Gross fixed investment	6,327	44.0	−11.0	15.0	13.1
Total consumption	30,604	1.1	5.1	6.6	...
General government	4,152	0.2	6.5	7.2	...
Private	26,452	1.2	4.9	6.5	...

SOURCE: ECLA, on the basis of official statistics.
[a] Preliminary figures.

Table 122. Ecuador: structure of total supply and demand[a]
(*Percentages*)

	1970	*1973*	*1974*[b]
Total supply	*121.5*	*122.5*	*126.0*
Gross domestic product	100.0	100.0	100.0
Imports	21.5	22.5	26.0
Total demand	*121.5*	*122.5*	*126.0*
Exports	15.8	21.8	18.3
Gross domestic investment	19.5	22.5	24.4
Gross fixed investment	17.8	21.0	21.8
Total consumption	86.2	78.2	...
General government	11.7	10.7	...
Private	74.5	67.5	...

SOURCE: ECLA, on the basis of official statistics.
[a] At 1970 prices.
[b] Preliminary figures.

one third of the country's total fixed capital formation.[159]

In 1972-1974 the investment made by oil companies fell off upon completion of the necessary facilities for putting the oil reservoirs into operation, so that the fixed investment coefficient dropped to an average of around 20 per cent. The fixed investment levels of the mid-1960s were not regained, because between that date and 1973-1974 the public sector and the domestic private sector more than doubled their levels of capital formation, in terms of constant prices, while the GDP grew by about 50 per cent.[160]

Import trends were affected by the purchase of materials and equipment necessary for the oil companies' investments. This factor mainly accounts for the high growth rates of imports recorded in 1970 and 1971 and the decline observed in 1972. In 1973 and 1974 the rapid increase in imports is attributable to the effects of the liberalization measures adopted as the country's capacity to import expanded.

(b) *Sectoral structure of the product and employment*

The accelerated growth of the GDP coincided with a fairly balanced development of the various production activities. Apart from mining, whose contribution to the GDP rose at an average annual rate of 55 per cent, other sectors–manufacturing, construction, transport and communications, and services in general–grew at rates compatible with this acceleration. In contrast, agriculture and electricity, gas, water and sanitary services recorded unsatisfactory rates of growth, lower even than the population growth rate (see table 123).

Between 1970 and 1974, agriculture grew at an average rate of barely 1 per cent annually, which was only slightly higher than the rate recorded between 1965 and 1970 (0.8 per cent). Thus the situation of evident stagnation in agricultural activity, which had been especially manifest since the mid-1960s, continued. In this respect, it should be recalled that in the years 1960-1965 this sector's contribution to the product increased by about 3 per cent annually, compared with approximately 4 per cent annually in the 1950s.[161] The trends described above caused the share of agriculture in the GDP to drop far more rapidly (from 33 per cent in 1965 to 23 per cent in 1973) than normally happens in the development process of countries with *per capita* income levels similar to Ecuador's (see table 124).

It seems clear that the basic problem consists in the typically low levels of productivity in the agricultural sector in general. This in its turn is a result, among other factors, of the prevailing system of land tenure–under which the latifundio-minifundio system still exists–of the scant capital formation in the sector, of the abundant unskilled manpower engaged in agriculture, and of the shortcomings of the prices, marketing and other policies affecting this activity.[162]

Taken together, the goods producing sectors kept their share in the GDP comparatively stable

[159] See Banco del Ecuador, *Memoria 1973*, table 1-5.a-1.
[160] *Ibid.*, table 1-5.b.
[161] See ECLA, *Tendencias y estructuras de la economía del Ecuador en el último decenio* (E/CN.12/926), 9 March 1972, table 1.
[162] See, for example, document CIAP/635, op. cit., pp. 121 et seq.; and FAO/IDB Mission, *Estudio del sector agropecuario del Ecuador, identificación de áreas prioritarias de inversión*, 1973.

Table 123. Ecuador: gross domestic product at factor cost by sector of economic activity
(Millions of sucres at 1970 prices)

	Millions of sucres at 1970 prices 1970	*Annual growth rate*			
		1971	*1972*	*1973*	*1974*[a]
Agriculture	9,404	−1.4	4.5	−1.4	2.5
Mining	449	48.6	56.8	170.3	4.0
Manufacturing	5,713	8.6	7.3	11.1	14.0
Construction	1,387	50.0	−22.2	11.7	8.3
Subtotal goods	*16,953*	*7.5*	*4.3*	*13.5*	*7.1*
Electricity, gas, water and sanitary services	418	10.0	3.5	...	...
Transport and communications	2,091	5.1	8.9	9.6	5.6
Subtotal basic services	*2,509*	*5.9*	*8.0*	*7.9*	*5.0*
Commerce and finance	4,505	14.6	3.1	1.0	14.8
Ownership of dwellings	1,948	5.1	9.3	6.3	6.3
Government	3,275	−0.5	8.8	3.4	20.5
Miscellaneous services	2,238	7.5	5.1	4.0	7.0
Subtotal other services	*11,966*	*7.6*	*5.9*	*3.1*	*13.4*
Total	*31,428*	*7.4*	*5.2*	*9.3*	*9.2*

SOURCE: ECLA, on the basis of official statistics.
[a] Preliminary figures.

Table 124. Ecuador: structure of gross domestic product at factor cost, by sector of economic activity[a]
(Percentages)

	1970	*1973*	*1974*[b]
Agriculture	29.9	24.7	23.2
Mining	1.4	7.3	6.9
Manufacturing	18.2	19.1	19.9
Construction	4.4	4.6	4.6
Subtotal goods	*53.9*	*55.7*	*54.6*
Electricity, gas, water and sanitary services	1.3	...	...
Transport and communications	6.7	6.8	6.6
Subtotal basic services	*8.0*	*8.0*	*7.7*
Commerce and finance	14.4	13.9	14.6
Ownership of dwellings	6.2	6.1	6.0
Government	10.4	9.5	10.4
Miscellaneous services	7.1	6.8	6.7
Subtotal other services	*38.1*	*36.3*	*37.7*
Total	*100.0*	*100.0*	*100.0*

SOURCE: ECLA, on the basis of official statistics.
[a] At 1970 prices.
[b] Preliminary figures.

between 1970 and 1974. The decline recorded by agriculture was offset by a sharp rise in the share of mining, and smaller increases in the shares of manufacturing and construction. The purely service activities, which generate around 40 per cent of the GDP, continued to represent a fairly high proportion of the product, considering the *per capita* income levels in Ecuador and the coefficients observed in other countries of the region.[163]

When, in addition, the sectoral composition of the product is examined from the standpoint of

[163] See ECLA, *Trends and structure of the Latin American economy* (E/CN.12/884), 4 March 1971, table 25.

the distribution of manpower, other structural features are observable which are worth while taking into account.

First, available data on the sectoral composition of the labour force indicate that from the mid-1960s to the years 1971-1972 there were very slight variations in the relative absorption of manpower by the different economic activities. Thus, for example, agriculture continued to employ about 56 per cent of the labour force and manufacturing reduced its share of around 14 per cent to about 13.4 per cent.[164]

These trends, considered simultaneously with the evolution of the GDP and its sectoral structure, accentuated the disparities noted between the average labour productivity in agriculture and that recorded in the rest of the economy, which already at the beginning of the 1970s stood at a ratio of 1 to 4. Similarly, the rapid economic development in 1972-1974 must have even further widened the gap.[165]

Secondly, some data on open unemployment trends indicate that the average unemployment rate after reaching a peak of 10 per cent in 1968 apparently descended to around 8 per cent in 1972-1973. This was still a relatively high rate—particularly in the towns—and was higher, for example, than that recorded in the first half of the 1960s. Of course, the degree of open unemployment in the towns depended essentially on the level and persistence of the disguised unemployment situation in the country.

2. *The external sector*

(a) *General aspects*

The production and export of petroleum had a decisive effect on the balance of payments in the period 1971-1974.

In the first place, the exports initiated in August 1972 meant an income of approximately 60 million dollars in 1972, 270 million in 1973 and 820 million in 1974, the latter figure representing over 65 per cent of total exports of goods in that year.

Secondly, in the years 1971 and 1972 the investments made by oil companies in Ecuador averaged more than 120 million dollars annually. Deducting the direct imports effected by those same companies—which amounted to some 70 million dollars annually—the investments generated a net annual income of approximately 50 million dollars, or more than one fifth of the normal level of exports at the beginning of the 1970s (see table 125).

Another salient feature of the external sector's development was the change experienced between 1971 and 1974 in the over-all balance of payments position.

In 1971 the stagnation of exports and a sharp upturn in imports produced a large current account deficit (218 million dollars).[166] The income on capital account—notwithstanding the increase recorded in foreign investment—was not enough to cover the current account deficit, so that a net sum of 30 million dollars had to be used of the international reserves.

In the years 1972-1974, on the other hand, the balance of payments showed average surpluses of around 100 million dollars annually. The rapid growth of exports and a delayed increase in imports reduced the current account deficit from 218 million dollars in 1971 to 98 million in 1973, and led to a current account surplus of 100 million in 1974. The income on capital account was bolstered in its turn in 1972 by a bigger influx of long- and medium-term loans, and in 1973 by a strong inflow of unidentified private external resources which are included in the balance of payments under the head of errors and omissions. In 1974, on the other hand, there was less need for long- and medium-term loans (see table 125).

Between end-1970 and end-1971, the level of gross international reserves dropped from 83 to 65 million dollars, the latter figure covering the equivalent of less than two months' imports. In 1972, on the other hand, the level rose to 143 million dollars and in the following years to 241 million and 350 million respectively. In other words, there was a fairly rapid and substantial increase in the country's international reserves, which reached a relative peak of 450 million in mid-1974 (see table 126).

(i) *The exchange system.* Since November 1971 a dual system of exchange has operated in Ecuador, with an official and a free market.[167] The official exchange rate was established at 25 pesos to the dollar in August 1970 and remained unchanged up to and including 1974, in line with the country's traditional policy of not making periodical adjustments in the exchange parity and of adjusting it only at intervals of a certain number of years.

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[164] Estimates based on data supplied by the Planning Board of Ecuador to missions of the International Monetary Fund.

[165] See document CIAP/635, op. cit., pp. 8 et seq.

[166] This was the culmination of a trend begun in 1966-1967 towards a progressive deterioration of the country's trade balance and current account.

[167] Between August 1970 and November 1971 the free market was eliminated on a temporary basis only, and a single controlled market was established.

Table 125. Ecuador: balance of payments
(Millions of dollars)

	Average 1966-1970	1971	1972	1973	1974[a]	Average 1971-1974
Current account						
Exports of goods and services	224.1	269.8	354.0	613.0	1,302.0	634.7
Goods FOB	205.4	242.9	323.2	574.1	1,261.0	600.3
Services	18.8	26.9	30.8	38.9	41.0	34.4
Imports of goods and services	274.0	459.7	473.8	627.5	1,031.0	648.0
Goods FOB	203.7	360.7	366.5	491.9	826.0	511.3
Services	70.3	99.0	107.3	135.6	205.0	136.7
Net external investment income	-26.9	-35.7	-45.6	-100.4	-190.0	-92.9
Profits	-19.6	-25.2	-34.3	-93.4	-192.0	-86.2
Interest	-7.3	-10.5	-11.3	-7.0	2.0	-6.7
Net private transfer payments	5.1	7.7	6.3	16.8	19.0	12.5
Balance on current account	-71.7	-217.9	-159.1	-98.1	100.0	-93.7
Capital account						
Net external financing (*a* + *b* + *c* + *d* + *e*)	71.7	217.9	159.1	98.1	-100.0	93.7
(*a*) Net external non-compensatory capital	71.9	193.1	245.9	108.8		
Direct investment	37.8	162.1	149.8	54.3		
Long- and medium-term loans	42.1	49.0	111.7	60.3		
Amortization payments	-17.0	-29.8	-28.3	-33.7	7.0	160.8
Short-term liabilities	1.2	3.8	3.3	6.4		
Official transfer payments	7.8	8.0	9.4	21.5		
(*b*) Domestic non-compensatory capital or assets	-0.4	-3.2	-5.5	-10.4		
(*c*) Errors and omissions	2.7	-5.8	17.4	96.2		
(*d*) Allocation of SDRs	0.8	3.5	3.8	0.0	0.0	1.8
(*e*) Net compensatory movements (increase -)	-3.4	30.3	-102.5	-96.5	-107.0	-68.9

SOURCE: ECLA, on the basis of official statistics.
[a] Preliminary figures.

Table 126. Ecuador: international reserves
(Millions of dollars at current prices)

	1969	1970	1971	1972	1973	1974
(1) International reserves (totals at end of period)	65.0	83.2	64.7	143.4	241.1	349.9[a]
(2) Imports of goods and services	281.5	375.5	459.7	473.8	627.5	1,031.0
(3) Imports of goods and services (monthly average)	23.5	31.3	38.3	39.5	52.3	85.9
(4) Number of months of imports financed by international reserves	2.8	2.7	1.7	3.6	4.6	4.1

SOURCE: IMF, *International Financial Statistics*, September 1972 and May 1975.
[a] At the end of June 1974 the reserves stood at 444.4 million dollars.

Between the end of 1971 and 1973-1974 the value of the free dollar came closer and closer to that of the official dollar, as the strong inflow of foreign exchange on the free market led the Central Bank to establish a permanent purchasing power, at a rate similar to the official, in order to absorb the foreign exchange surpluses generated in that market.

The prevailing exchange system meant—if the internal price variations in Ecuador and the United States are taken into account—that the real value of the Ecuadorian currency decreased by 11 per cent between 1971 and 1973, owing to the faster increase in domestic prices (see table 127).

An additional feature of the exchange system prevailing in the period under review was the

Table 127. Ecuador: trend of real value of exchange rate

	(1) Average exchange rate[a] (sucres to the dollar)	(2) Implicit deflator of Ecuador's GDP (1970 = 100)	(3) Implicit deflator of the United States GDP (1967 = 100)	(4) (2)/(3) x 100 Relation between implicit deflators of Ecuador and United States (1970 = 100)	(5) (1)/(4) x 100 Trend of real value of average exchange rate (base 1970–sucres to the dollar)
1969	19.16	93.4	94.8	98.5	19.45
1970	21.67	100.0	100.0	100.0	21.67
1971	25.71	108.8	104.7	103.9	24.74
1972	26.0	118.4	107.9	109.7	23.70
1973	24.85	133.9	118.7	112.8	22.03
1974[b]	24.85	165.1	136.0	121.4	20.47

SOURCES: Central Bank of Ecuador, and United States Department of Commerce, *Statistical Abstract, 1973.*

[a] Weighted average of exchange rates in force in the markets for current external transactions.
[b] Preliminary figures.

large-scale levying of taxes on *ad valorem* exports. These were designed, in particular, to generate fiscal revenue and to take the place of other possible forms of domestic taxes which did not already exist. Notable among the export taxes were those levied on bananas (31.4 per cent), coffee (26.5 per cent), cocoa (25 per cent) and sugar (23.75 per cent).[168] The revenue obtained from all these export taxes in 1971 represented about one tenth of the total current income of the central government. It should also be noted that a 15 per cent tax on petroleum exports was established in August 1972.

As regards import taxes, Ecuador's customs tariff provides average protection of 40 per cent and includes duties ranging, in general, from 30 to 50 per cent, the latter rate being levied on products with a lesser degree of processing. By virtue of several development laws and special contracts, however, over one third of the imports were not liable to customs duties. In any case, import taxes in 1971 accounted for about 30 per cent of the central government's total current income.[169]

Lastly, with the purpose of establishing an additional control of imports, a system was adopted of classifying them in two schedules: those on schedule I were considered as essential and semi-essential products, and those on schedule II as less essential and luxury items. About one fifth of total imports in the period 1971-1974 were products on schedule II, subject, on the one hand, to the payment of relatively higher customs duties (including a 20 per cent surcharge) and, on the other hand, to the requirement in force up to the beginning of 1973 of making prior import deposits.

(b) *Exports of goods*

In terms of current values, exports of goods increased by 33 per cent in 1972, by 78 per cent in 1973 and by 120 per cent in 1974, while exports in 1974 were five times the figure for 1971. Up to 1972, the whole increment over 1970 was the result of a larger volume of exports (38 per cent), while between 1972 and 1974 there were simultaneous increases in the quantity exported and the unit value, particularly in the latter which more than tripled (see table 128).

Petroleum exports alone accounted for rates of increase in total exports of 24 per cent in 1972, 67 per cent in 1973 and 95 per cent in 1974, they represented about four fifths of the total increase between 1971 and 1973. In 1973 the volume of petroleum output averaged 210,000 barrels a day, or approximately 75 million barrels a year. Of this total, a little over 71 million barrels were exported at an average price of about 3.70 dollars a barrel. In 1974, 59 million barrels were exported at an average price of 13.84 dollars per barrel.

The share of total exports represented by bananas, traditionally Ecuador's main export com-

[168] Several of these rates were raised 10 to 15 percentage points as a result of the devaluation in 1970, but from 1973 onwards various pressures were created aimed at reducing the additional charges established. See document CIAP/635, op. cit., table VI-9.

[169] *Ibid.*, pp. 264 et seq.

Table 128. Ecuador: trends of exports and imports of goods

	Average 1966-1970	*1970*	*1971*	*1972*	*1973*	1974[a]
(1) Exports of goods (FOB, millions of dollars)	205.4	234.3	242.9	323.2	574.1	1,261.0
(2) Exports of goods (millions of dollars, 1970 = 100)	87.7	100.0	103.7	137.9	245.0	538.2
(3) Index of unit value of exports of goods (1970 = 100)	92.8	100.0	96.0	99.9	138.0	329.0
(4) Index of constant value of exports of goods [(2)/(3) x 100] (1970 = 100)	94.5	100.0	108.1	138.0	177.5	163.6
(5) Imports of goods (FOB, millions of dollars)	203.7	266.2	360.7	366.5	491.9	826.0
(6) Imports of goods (millions of dollars, 1970 = 100)	76.5	100.0	135.5	137.7	184.8	310.3
(7) Index of unit value of imports of goods (1970 = 100)	96.0	100.0	104.0	109.9	127.9	166.0
(8) Index of constant value of imports of goods [(6)/(7) x 100] (1970 = 100)	79.7	100.0	130.3	125.3	144.5	186.9

SOURCE: ECLA, on the basis of official statistics.

[a] Preliminary figures.

modity,[170] shrank progressively to 10.5 per cent in 1974, owing to the fact that their current value rose by only 9 per cent between 1970 and 1974. As regards the trend in world banana prices, the average price in 1973-1974 (7.5 cents per pound) was equal to the average for 1970 and similar to that recorded at the beginning of the 1950s.[171]

Other changes which took place in the structure of exports in 1971-1973 were also due to the increase in the share of petroleum and the decline in that of other export items (see table 129).

Nevertheless, over and above the observations about the share acquired by exports of marine products, it is interesting to note that exports of a number of items increased by over 50 per cent in value between 1970 and 1973, reaching a total of 40 million dollars. These items include a wide range of manufactured and semi-manufactured products.

(c) *Imports of goods*

Between 1966-1970 and 1971-1973 the current value of imports of goods doubled, rising from an annual average of 200 million to 400 million dollars. Since during the same period, however, the unit value of imports rose 19 per cent, the increase in terms of constant prices is estimated at 68 per cent. In 1974 the current value of imports rose to 826 million dollars (see table 128).

[170] At the beginning of the 1960s, exports of bananas represented 60 per cent of the country's total exports, and at the beginning of the 1970s their share was still over 50 per cent.

[171] In fact, bananas are among the basic commodities which have suffered the sharpest cuts in terms of constant purchasing power on the world markets. See ECLA, *Economic Survey of Latin America, 1973*, Part One.

Table 129. Ecuador: structure of exports of goods
(*Percentages*)

	Average 1966-1970	*1970*	*1971*	*1972*	*1973*	*1974*
Petroleum	0.1	0.4	0.8	18.9	47.4	64.7
Bananas	53.0	51.8	50.4	40.5	23.1	10.5
Coffee	18.2	22.6	15.0	13.2	11.4	5.2
Cocoa	12.7	10.0	10.1	7.2	4.7	8.1
Sugar	4.0	3.6	5.5	5.3	2.1	2.8
Marine products	–	–	6.0	6.9	4.1	2.6
Miscellaneous	12.0	11.6	12.2	8.0	7.2	6.1

SOURCE: ECLA, on the basis of official statistics.

Table 130. Ecuador: structure of imports of goods
(Percentages)

	Average 1966-1970	*1970*	*1971*	*1972*	*1973*	*Average 1971-1973*
(1) Consumer goods .	14.6	14.0	14.1	14.8	12.4	13.6
(*a*) Durable . .	5.2	5.1	4.0	3.8	3.6	3.8
(*b*) Non-durable .	9.4	8.9	10.1	11.0	8.8	9.8
(2) Raw materials[a] . .	42.5	41.1	42.4	42.5	48.1	45.0
(3) Fuels	6.7	7.6	7.6	7.0	4.5	6.0
(4) Capital goods . .	36.0	37.0	35.8	35.3	35.1	35.3
(5) Miscellaneous . .	0.2	0.3	0.1	0.4	0.0	0.1

SOURCE: ECLA, on the basis of official statistics.
[a] Including construction materials.

Within the general fairly accelerated growth trend of nearly all import items, some salient features are worth considering (see table 130).

First, up to and including 1972, and particularly up to 1971, substantial purchases were made of materials and equipment necessary for the installation of the new oil production activities in Ecuador. In 1971 these purchases may be estimated at over 80 million dollars, declining to less than 60 million in 1972, and to approximately 30 million in 1973.

Secondly, the period 1971-1973 marked a rapid growth of imports of food and similar items and of raw material inputs for the food industry. In terms of current values, these imports rose from 37 million dollars in 1970 to 97 million in 1973, i.e., by 163 per cent, while the increase in total imports was 85 per cent.

Lastly, between 1966-1970 and 1971-1973 imports of capital goods retained their share in the total at around 35 per cent, while the share of durable consumer goods and fuels declined, especially that of fuels in 1973.

C. THE RECENT INFLATIONARY PROCESS

1. *Background*

Ecuador is one of the countries of Latin America where inflation and the accompanying preoccupation with combating it constitute a relatively new phenomenon. During the 1950s, the annual average rate of increase in prices fluctuated around 1 per cent, while during the 1960s–up to 1968 inclusive–although higher it continued to be moderate, reaching an annual 3.5 per cent.

Only from 1969 onwards did annual price rises of more than 5 per cent begin to appear: this is the lowest figure usually considered to be indicative of the appearance of inflationary distortions of any importance.

However, since 1966-1967 food prices had been registering annual increases of more than 5 per cent, and were thus increasing more rapidly than domestic prices on average. Between 1965 and 1969 the prices of the food and beverages section of the Quito consumer price index increased at an annual average rate of 7 per cent, while the comparable annual increase in the housing and clothing sections was approximately 2.5 per cent. Thus, between the two years considered the relative price of food increased by 18 per cent.[172]

In 1970 the rate of inflation continued to increase, rising to over 8 per cent but then dropping slightly to around 7 per cent in 1971 and 1972. In 1973, however, the inflation rate accelerated sharply to over 20 per cent. This increase continued to be in evidence during the early months of 1974, with the result that between April 1973 and April 1974, the price increase for the year was close on 30 per cent. After reaching this relative peak, however, there was a drop in July 1974 and throughout the second half of the year in general, so that the annual rate of inflation declined to slightly over 20 per cent–similar to that recorded at the end of 1973[173] (see table 131).

As in the period 1965-1969, food prices increased between 1969 and 1974 at a faster rate

[172] See Instituto Nacional de Estadística (INE), *Indice de precios al consumidor* (consumer price index). In addition to the monthly calculation of changes in the Quito index, the INE also prepares consumer price indexes for the cities of Guayaquil and Cuenca. In order to simplify our analysis, the price series for Quito is used in the present report. However, no wholesale price series were available to complement the analysis.

[173] In order to identify these changes in the rate, the figures used cover the period from one month of one year to the same month in the next year, since this is a more sensitive method for short periods than making estimates on the basis of averages.

Table 131. Ecuador: trends in consumer prices
(*Percentages*)

		Average 1965[a]-1969	*1970*	*1971*	*1972*	*1973*	*1974*	*April 1973 to April 1974*
1. Consumer price index[a]–Quito	(variation December to December)							
(*a*) General		5.9	8.3	6.8	6.9	20.5	21.2	29.6
(*b*) Food and beverages		8.5	5.0	6.3	10.7	31.1	28.0	45.0
2. Consumer price index[a]–Quito	(variation between annual averages)							
(*a*) General		4.6	5.1	8.4	7.9	12.9	23.4	–
(*b*) Food and beverages		6.9	3.3	6.5	11.1	20.3	32.4	–
3. Consumer price index[a]–Quito	(variation between annual averages 1970 = 100)							
(*a*) General		95.2[b]	100.0	108.4	117.0	132.1	163.0	–
(*b*) Food and beverages		96.8[b]	100.0	106.5	118.3	142.3	188.4	–

SOURCE: Instituto Nacional de Estadística (INE), consumer price index.

[a] Of families with low and medium incomes.
[b] Value of the index in 1969.

than those of the other goods and services considered in the price indexes, particularly in 1972-1974. Thus, in the city of Quito, prices in the food and beverages section increased by 11 per cent during 1972, 31 per cent in 1973, 45 per cent between April 1973 and April 1974, and 28 per cent in 1974.

Between 1969 and 1974 relative food prices increased by over 12 per cent with respect to the housing and clothing sections. This increase, on top of the 18 per cent rise which took place between 1965 and 1969, meant that between 1965 and 1974 the total increase in the relative prices of food-stuffs was 33 per cent, which obviously meant a substantial advance in their position.

2. *Factors which influenced the speeding up of inflation*

As we have already seen, the country's past inflation shows two stages or levels in the acceleration of the growth rate of prices. The first stage covered 1969 and 1970, although its immediate origins went as far back as 1966-1967. The second stage was observed in 1973, and particularly in the early months of 1974, following some deceleration of inflation in 1971 and 1972.

Examination of the factors which influenced the evolution of prices during the two stages identified shows that some common elements were present in both, together with others which were different; the intensity of their effects also varied.

Outstanding among these common elements, without any doubt, was the performance of the agricultural sector, both because of its intrinsic importance and because of its links with other economic variables. This, then, is one of the structural factors of inflation which has been most investigated, and the following section is devoted to analysing the phenomenon. The next two sections review the accessory elements in inflation which appeared, first during the acceleration of 1969-1970 and then in the re-acceleration of 1973-1974.

(a) *The problem of agriculture*

The slow growth of the agricultural sector, analysed above, is even more obvious when the trend of *per capita* agricultural output is taken into account. During the 1950s, this increased by approximately 1 per cent annually, dropped slightly between 1960 and 1965 and decreased by around 2.5 per cent annually between 1965 and 1974. This meant that in absolute and constant terms, the *per capita* agricultural product in 1974 was around 20 per cent less than in 1965.

This substantial reduction in *per capita* agricultural output was a factor of great inflationary potential and significance, particularly in a country like Ecuador, where food accounts for 60 per cent or more of the expenditure of low- and middle-income families. The extent to which this inflationary potential materialized in actual pressures of varying intensity on domestic food prices, and indirectly on the prices of other goods and services, depended in its turn on several elements. These include the evolution of over-all demand and demand for agricultural products and the evolution of imports of food and similar products

aimed at reinforcing domestic supplies. The relation between the prices of imported products and the prices of locally-produced products were also of consequence, as were the policy measures adopted as regards marketing and the fixing of food prices.

As regards the evolution of local demand for food-stuffs, it was observed that this increased at progressively high rates as the economy's rate of development accelerated. Taking the annual rate of population growth of 3.4 per cent and an income-food-stuffs elasticity of between 0.5 and 0.6, it may be estimated that between 1965 and 1970 the increase in domestic demand for food-stuffs was over 4 per cent annually, while in 1970-1974 the comparable rate was approximately 6 per cent, and in 1973-1974 in particular the increase was more than 7 per cent.[174]

In keeping with this trend, and in contrast to the annual variations in agricultural output, the rate of increase of the demand for food-stuffs exceeded the annual increase in domestic food output by around 3 per cent in 1965-1970, 5 per cent in 1970-1974 and 8 per cent in 1973 considered separately. The inflationary importance of this excess demand was particularly noteworthy, in view of its magnitude, persistence and continuing increase.

During the period 1966-1970 imports of food and similar products and inputs for food manufactures fluctuated without major variation around 35-37 million dollars, i.e., they did not offset the inadequate increase in the domestic output of agricultural products with respect to the increase in the demand for them.

Later, imports of food and other related items, expressed at constant 1970 prices, increased by around 40 per cent in 1971, remained stable in 1972 and again increased by around 40 per cent in 1973. No accurate data were available for 1974. It is estimated that during the period 1970-1974 these imports increased the local supply of food-stuffs by about 3 per cent annually over the levels provided by domestic output, so that the annual 5 per cent excess demand already referred to was reduced to less than half. In 1973, however, the shortfall would appear to have been more than 4 per cent of agricultural output.

In other words, taking into account the strengthening of domestic supply achieved through larger imports, agricultural output showed an annual deficit of around 3 per cent during the whole period 1966 to 1974, in the light of the evolution of demand.

In addition to these over-all quantitative trends which influenced the process of inflation there were also, of course, partial disequilibria in the levels of specific food products and groups of products. Mention may be made, for example, of the inadequate domestic supply of rice and potatoes between 1972 and 1974.

As regards the ratio of the domestic prices of food products to their international prices, it was observed, generally speaking, that the prices in Ecuador were, and still are, distinctly lower than international prices, by as much as 50 per cent. Thus, with the increase in imports of food products, the difference in price became increasingly marked. This situation got worsened in 1973 and the first part of 1974, when sizable imports of food-stuffs coincided with large and continuing increases in the international prices of these products.

The inflationary pressures stemming from this difference in prices led to the granting of government subsidies in respect of imports of food effected and marketed by public institutions, mainly the Banco Nacional de Fomento (BNF), but also, as from 1973-1974, the Empresa Nacional de Almacenamiento y Comercialización de Productos Agropecuarios (ENAC) and the Empresa de Productos Vitales (EMPROVIT). It was thus frequent for imported products to be sold in the country below cost price, the losses so created being financed by credits granted by the Central Bank to the above-mentioned institutions.

Moreover, since the Government fixes and controls the retail prices of a large number of food-stuffs, it took the opportunity during the period under review, and particularly in 1973-1974, to increase the prices of several food products by varying amounts, especially when such products were imported and this made the price difference between them bigger and more evident.

These and other aspects of the inflationary impact of the agricultural problem will be referred to again later, in the examination of the evolution of other variables of the economic system

(b) *The inflationary situation of 1969-1970: other explanatory factors*

As already noted, from 1969 onwards the increases in domestic prices began to be significant and to warrant genuine concern, although food prices had already been showing increases of some magnitude since the mid-1960s.

Later, during the period 1968-1970, some other inflationary elements appeared in the economic situation in addition to the basic and longer-standing pressures deriving from the slow growth of the supply of agricultural commodities. These elements consisted of a more rapid increase in over-all demand, and of considerable independent increases in the cost of some economic variables.

[174] See document CIAP/635, op. cit., table IV-6.

(i) *The activation of over-all demand.* As from 1968, there was an increase in the growth rate of real demand for several simultaneous reasons.

The most noteworthy of these was the performance of gross domestic capital formation, which is analysed above. Its resurgence, which began in 1967, speeded up in 1969 and 1970, when investment in current values increased by 24.5 per cent and 53.4 per cent respectively (see table 132). Although it is true that during this period the imported element of investment would appear to have grown, the increase in capital formation in national currency was in any case substantial, and it is this which most directly influences the progress of domestic demand.

During the period 1968-1970, largely in keeping with the evolution of investment, the *per capita* GDP increased at a much higher rate than in

Table 132. Ecuador: relations between price movements and some important variables
(Percentage variations)

		1968	1969	1970	1971	1972	1973	1974[a]
1. Consumer price index–Quito	(December to December)	4.2	6.5	8.3	6.8	6.9	20.5	21.2
2. Index of unit value in dollars of imports of goods	(between averages)	0.0	3.2	2.0	4.0	5.7	16.4	29.8
3. Index of unit value in dollars of exports of goods		−5.5	5.8	9.9	−4.0	4.1	38.1	138.4
4. Exchange rate		2.3	0.4	13.1	18.6	1.1	−4.4	–
5. Unit value of imports by exchange rate (2 x 4)		2.3	3.6	15.4	23.3	6.9	11.3	29.8
6. Unit value of exports by exchange rate (3 x 4)		−3.3	6.2	24.3	13.9	5.2	28.2	138.4
7. Nominal remunerations								
(*a*) Average monthly wage of workers in manufacturing industry		8.8	21.6	6.9	12.9	18.5	7.2[b]	...
(*b*) Average monthly salary of employees in manufacturing industry		5.1	4.3	5.6	10.1	8.9	13.2[b]	...
8. Agricultural output								
(*a*) Contribution to GDP of the agriculture, forestry, hunting and fishing sector		−1.3	0.5	0.7	−1.4	4.5	−1.4	2.5
(*b*) Contribution to *per capita* GDP		−4.6	−2.8	−2.7	−4.7	1.1	−4.7	−0.8
9. *Per capita* GDP (at market prices)		2.2	1.4	4.3	3.0	3.7	6.9	5.6
10. Money–total means of payment[c] (at end of year)		18.5	13.3	24.5	11.4	21.6	30.7	36.5
11. Total central government expenditure (at current prices)		25.0	11.0	25.3	17.0	4.1	29.7	79.8
12. Total central government expenditure (as a percentage of GDP at market prices)		13.5	13.5	14.2	14.2	12.3	12.5	16.7
13. Current central government income (at current prices)		−3.6	15.3	26.2	19.0	24.7	46.7	86.7
14. Current central government income (as a percentage of GDP at market prices)		9.2	9.5	10.0	10.2	10.6	12.2	16.9
15. Total deficit of central government (as a percentage of GDP at market prices)		4.3	4.0	4.2	4.0	1.7	0.3	−0.2
16. Gross domestic capital formation (at current prices)		15.9	24.5	53.4	28.4	4.0	11.0	...

SOURCES: Items 1 to 6 and 10 to 15: ECLA, on the basis of official statistics; 7: INE, *Estadísticas del trabajo*; 8, 9 and 16: Banco Central del Ecuador, *Memoria 1973* and ECLA, on the basis of official statistics.

[a] Preliminary figures.
[b] Variation between the first quarters of 1972 and 1973.
[c] According to IMF definition.

previous years, and the growth rate of demand for food-stuffs gradually increased accordingly, as we have already seen.

Secondly, if the performance of the monetary variables is analysed, it will be seen that the rate of growth of the money supply was much higher during the period 1968-1970 than in the preceding years, more exactly during the three-year period 1964-1967. Thus, during the first-mentioned period, the annual average increase in the means of payment was 19 per cent, compared with a rate of only 9 per cent in the earlier period, which was similar to the rate observed during the early years of the 1960s (see table 133).

Naturally, this change in the growth rate of the quantity of money was of particular importance in an economy which was, generally speaking, not much "monetized"[175] and which was also little accustomed to variations in the means of payments of 10 per cent or more per year. Moreover, during the period 1968-1970 the contrast between the rate of increase of the quantity of money and the average increase of the GDP was substantial, since the latter came to an annual average of only 6 per cent.

It may also be observed that 1968 marked the beginning of a new stage in the economy of Ecuador, characterized by frequent sizable imbalances between the growth rate of real variables and that of financial variables. Previous to this date, the usual situation was a relative balance between the evolution of these two groups of variables.

A more detailed examination of monetary trends shows that the more rapid increase in the means of payment was originally due, especially in 1968 and 1969, to a large increase in the domestic credit granted to the Government (87 per cent in 1968 and 63 per cent in 1969). This expansion was aimed at financing the total deficit of the central government, which during those years amounted to around 1,200 million sucres per period, or more than 4 per cent of the GDP (see tables 132, 133 and 134). The excessive volume of the deficit originated in 1968, when total government expenditure increased by 25 per cent, while its current income decreased by around 4 per cent.

The lack of elasticity in the Government's current income system, especially as regards income from taxes on domestic activities, has been and continues to be a structural feature of the economy of Ecuador. It appears in connexion with both taxes and the rates of public enterprises. In addition, there is a high degree of specificity as regards tax yields, in that various percentages of the resources entering the Treasury have already been legally allocated in advance to specific functions.

In 1970 the growth of domestic credit to the Government continued to be substantial, and the Government continued to run a total deficit of more than 4 per cent of the GDP, but the balance-of-payments situation was such as to give an increase of 18 million dollars in the country's international reserves. This increase—due in particular to the flow of foreign investment already mentioned—caused a considerable expansion in the money supply, unlike the situation in 1968 and 1969.

During the entire three-year period 1968-1970 placements in the private sector increased at relatively high rates. Between 1967 and 1970 the average annual rate of growth was 16 per cent, while between 1964 and 1967 the rate had been only about 6 per cent.

(ii) *The "independent" increases in prices.* The main element of inflation here was the 39 per cent devaluation of the sucre[176] decided upon in August 1970 following a period of nearly a decade during which the exchange rate remained stable. This devaluation more or less coincided with the percentage increase experienced in domestic prices during the period in which the exchange rate remained unchanged.

The above-mentioned devaluation naturally caused several inflationary effects, but where it was intensely felt was in the local prices for imported goods and goods produced in Ecuador with a high import component.

In the case of exported goods, inflationary repercussions on the country were lessened to some extent owing to the export tax increases of 10 and 15 per cent decided upon at the same time as the devaluation. In practice, however, the effect of this adjustment was reduced because in 1970 the unit value of exports increased by 10 per cent, which was a relatively big increase compared with the trends of previous years.

As far as the evolution of wages and salaries is concerned, the data which it has been possible to collect are scanty and partial.[177] It may be deduced from these data, however, that from the point of view of labour earnings, the inflationary pressure of greatest importance occurred in 1969,

[175] The GDP/money ratio is approximately 7 to 1, compared with ratios of around 5 to 1 frequently found in other countries of the region.

[176] The official parity of the dollar increased from 18.18 to 25.25 sucres (seller).

[177] These data correspond to indexes of the average monthly remuneration, in sucres at current prices, of workers and salaried workers (taken separately) who work in manufacturing industry and in mining and quarrying. The indexes are calculated by the Instituto Nacional de Estadística (INE).

Table 133. Ecuador: monetary trends

(Millions of sucres at current prices, at the end of each period)

	1968	*Percentage variation*	*1969*	*Percentage variation*	*1970*	*Percentage variation*	*1971*	*Percentage variation*	*1972*	*Percentage variation*	*1973*	*Percentage variation*	*1974*	*Percentage variation*
I. *Structure of monetary resources*														
1. Money (means of payment) . .	3,830	18.5	4,341	13.3	5,404	24.5	6,020	11.4	7,320	21.6	9,568	30.7	13,064	36.5
2. Quasi-money . .	1,539	38.9	1,705	10.8	1,984	16.4	2,557	28.9	3,019	18.1	3,598	19.2	4,604	28.0
3. Bonds	1,332	10.1	1,409	5.8	1,456	3.3	1,619	11.2	1,844	13.9	2,135	15.8	2,568	20.3
4. Others (net) . .	64	−52.2	507	692.2	917	80.9	−176	–	664	–	219	−67.0	1,074	390.4
Total . . .	*6,765*	–	*7,962*	–	*9,761*	–	*10,022*	–	*12,847*	–	*15,518*	–	*21,310*	–
II. *Factors of expansion and contraction*														
5. Domestic reserves (net) . . .	963	−14.4	1,042	8.3	1,401	34.7	696	−50.4	3,199	360.3	5,874	83.6	9,653	64.3
6. Domestic credit .	5,802	27.2	6,920	19.3	8,360	20.8	9,326	11.6	9,648	3.5	9,644	0.0	11,657	20.9
(*a*) to the Government (net) . .	929	86.9	1,514	63.0	1,911	26.2	2,233	16.8	1,821	−18.5	211	−88.4	−1,458	–
(*b*) to the private sector . .	4,873	19.9	5,406	10.9	6,449	19.3	7,093	10.0	7,827	10.3	9,433	20.5	13,115	39.0
Total . . .	*6,765*	–	*7,962*	–	*9,761*	–	*10,022*	–	*12,847*	–	*15,518*	–	*21,310*	–
Direct issue (primary generation) by the Central Bank . .	3,537	13.4	5,067	43.3	7,046	39.1	6,768	−3.9	9,418	39.2	12,219	29.7	18,684	52.9

SOURCE: IMF, *International Financial Statistics*, May 1975.

Table 134. Ecuador: central government finance
(Millions of sucres at current prices)

	1967	*1968*	*Percentage variation*	*1969*	*Percentage variation*	*1970*	*Percentage variation*	*1971*	*Percentage variation*	*1972*	*Percentage variation*	*1973*	*Percentage variation*	*1974*[a] *Percentage variation*
1. Current income	2,649	2,554	−3.6	2,945	15.3	3,716	26.2	4,423	19.0	5,514	24.7	8,088	46.7	86.7
2. Total expenditure	3,027	3,785	25.0	4,200	11.0	5,261	25.3	6,156	17.0	6,407	4.1	8,313	29.7	79.8
3. Total deficit of the central government (2 − 1) . . .	378	1,231	225.6	1,255	1.9	1,545	23.1	1,733	12.2	893	−48.5	225	−74.8	–
4. Financing of total deficit[b]														
(*a*) External indebtedness (net) . .	34	66	94.1	17	−74.2	11	−35.3	−56	–	955	–	−67	–	–
(*b*) Internal indebtedness (net)[c]	344	1,165	238.6	1,238	6.3	1,534	23.9	1,789	16.6	−62	–	292	–	–

SOURCES: 1967-1971: IMF, *International Financial Statistics*, August 1974; 1972 and 1973: Banco Central del Ecuador, *Memoria 1973*, tables V-1 and V-2; 1974: ECLA, on the basis of official statistics.

[a] Preliminary figures. Include FONADE operations: 3,555 million sucres of income and 2,527 million sucres of expenditure, which produced a surplus of 1,028 million sucres.

[b] After deduction of amortization payments on the external and internal debt.

[c] Including variations of cash balances.

when the average remuneration of workers in manufacturing increased by more than 21 per cent compared with the previous period. In 1968 and 1970, however, the comparable increases were approximately 9 per cent and 7 per cent respectively (see table 132).

(c) *The speeding up of inflation in 1973-1974: some of the main elements which provoked it*

In 1971 and to a lesser extent in 1972, the rate of inflation dropped because several factors which had fostered the significant price movements of earlier years were no longer present. Thus, the growth rate of over-all demand declined on the one hand, while on the other the external sector did not have a destabilizing influence, since the exchange rate remained stable and the unit values of imports and exports did not undergo increases of any great consideration (see table 132).

As from the end of 1972, this situation was completely changed and inflation received a new impetus, which took on particular force during 1973 and the first part of 1974. The evolution of the external sector was of particular importance in this process, although other complementary aspects were also significant. It is therefore worth examining these two groups of causes, always bearing in mind the general and continuing influence of agriculture on the distortions caused by inflation.

(i) *Evolution of the external sector.* As already stated, as from mid-1972 the country's position as an exporter of petroleum had a decisive influence on the development of its external sector. It may be recalled that exports of goods increased from an average annual level of 240 million dollars in 1970-1971 to 320 million dollars in 1972, 570 million in 1973 and 1,260 million dollars in 1974. Imports of goods, for their part, which amounted to an annual average of around 310 million dollars in 1970-1971, increased to 370 million in 1972, 490 million in 1973 and around 830 million in 1974.

At the same time, and especially in 1973 and the first part of 1974, there were important variations in the unit values of imports and exports, which also caused noteworthy repercussions.

Influences on the trend of over-all demand. The expansive tendency of over-all demand from the end of 1972, as a consequence of the external sector trends, was manifested in three main ways.

In the first place, taking the most generic indicator available, the increasing rate of growth of the GDP is worthy of note. In 1971-1972 the increase in the *per capita* GDP was less than 3 per cent, while in 1973 and 1974 the average annual increase was around 6.3 per cent.

It is not necessary to expatiate on the importance of this increase in the GDP growth rate and the inflationary pressures which arose from it, since a description has already been given of the effect produced on the demand for food-stuffs. However, attention should be given to the basic change, of a more general nature, which was felt throughout the system of production and supply when an economy which was "accustomed" to an annual growth of around 2 per cent in terms of the *per capita* GDP saw its rate of growth more than tripled.

Secondly, there was a rapid growth in the Government's current income—a rise of 47 per cent in 1973 and 87 per cent in 1974—due in particular to the increase in foreign currency earnings coming from the participation, revenue and taxes connected with the development of petroleum. At the same time, tax revenue in national currency also rose considerably as a result of the taxes on the growing imports. This did not occur with other current domestic income, however, because of the lack of elasticity of the system which has already been commented upon.

This relative abundance of current income, though it made it possible to eliminate the total deficit of the central government, led at the same time to an expansion of government expenditure which tended to be further intensified during 1974, when the Fondo Nacional de Desarrollo (FONADE)[178] came into full operation. In 1973, then, total central government expenditure at current prices increased by 30 per cent, while public investment increased by 50 per cent.[179] In 1974 total expenditure rose 80 per cent and public investment is estimated to have grown by over 100 per cent.

Apart from the direct expansive effect of the increase in public activity, another important factor was the fact that the Government, because of the inadequacy of its current income in national currency, had to resort to selling foreign currency to the Central Bank to finance its increased expenditure. In other words, the form of financing the fiscal year had clear repercussions on the monetary system.

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[178] This agency, which is made up of the ministers and other high officials from the economic sector and is presided over by the Minister of Finance, operates independently of the budget. It receives the earnings from petroleum in excess of the reference price of 7.30 dollars per barrel and is aimed at financing only new investment projects not included in the budget. It is estimated that during 1974 about 150 million dollars entered FONADE i.e., rather more than the total public investment in 1973.

[179] See table 132 and Banco Central del Ecuador, *Memoria 1973*, op. cit., table I-5a.

A third notable factor was the trend recorded in the means of payment. In 1971, these increased by 11.4 per cent, while in 1972 they increased by 21.6 per cent, in 1973 by 30.7 per cent and in 1974 by 36.5 per cent.

An examination of the monetary series shows that up to 1973 the accumulation of international reserves was the only factor behind this development since the total domestic credit in the system remained practically stable between the end of 1971 and 1973. The repayment of the Treasury's debts with the Central Bank had a decisive influence in the latter connexion, because domestic credit to the private sector increased by 10 per cent in 1972 and 20 per cent in 1973. In 1974, on the other hand, total domestic credit rose by 21 per cent and credit to the private sector by 39 per cent (see table 133).

It should be added that in 1972 and 1973 the net purchases of foreign exchange by the monetary system amounted to a total of around 200 million dollars. This figure coincides approximately with the increase in international reserves reflected in the balance of payments and with the probable net sales of dollars by the Government to the Central Bank. In 1974, the net purchase of foreign exchange by the monetary system was over 100 million dollars, but in the first half of the year some 200 million dollars' worth had been purchased. The links existing between the operations on the external accounts, the fiscal accounts and the monetary variables were thus clear (see tables 126, 133 and 134).

More direct pressures on prices and costs. The first more direct influence exerted by trends in the external sector on domestic prices was connected with the growing degree of openness in the economy of Ecuador and the consequent increase in its import and export coefficients.

In the case of food-stuffs, in particular, this fact made the price difference of imported commodities increasingly more evident and significant. This introduced additional elements–quite apart from the slow increase in agricultural output–which impelled agricultural producers to press for and obtain an improvement in real prices.

Secondly, this process was accompanied by a large increase in the unit value of imports of goods, which rose on average by over 16 per cent in 1973 and by 30 per cent in 1974. Furthermore, the increase in the international dollar prices of the agricultural commodities imported by Ecuador cannot have been less than 50 per cent annually on average, to judge by available data on this subject.[180]

Despite government action involving the partially subsidized import and marketing of agricultural commodities, some selected examples show the local inflationary impact of the increase in the international prices of some food-stuffs imported by Ecuador.

Thus, in the case of wheat, the increase of over 100 per cent observed in 1973 in the dollar price of this product led to an increase of nearly 60 per cent in the price of bread in Quito between the end of 1972 and of 1973, while the 150 per cent increase in the international prices of soya beans in 1973 was a direct cause of the rise of over 50 per cent in local prices of oil and vegetable fat during that year.

As far as the repercussions of the change in the unit value of exports are concerned, in 1973 this value increased by 22 per cent, without taking into account petroleum and petroleum products. From the structure of the country's exports, it may be deduced that this increase basically reflected increases in the international prices of sugar, cocoa and coffee, since the unit value of bananas did not change. In the three cases identified, the domestic prices of the commodities or products in question rose in 1973 by amounts fluctuating around 50 per cent.

Lastly, as regards the domestic prices of petroleum and petroleum products, it should be noted that the price increases at the international level had little influence on domestic prices because the Government decided to keep fuel prices stable. Agreements were therefore reached with the petroleum companies to regulate sales procedures for fuels in Ecuador.

(ii) *Other inflationary factors.* Among possible additional pressures on costs was the fact that the exchange rate fixed in August 1970 was not modified during 1973 and 1974. It may be noted, however, that between 1971 and 1974 the "real" value of the exchange rate dropped, so that no inflationary pressure came from this direction (see table 127).

Moreover, the trend of wages did not appear to have been an important inflationary factor either, at least in 1973. Between the first quarters of 1972 and 1973,[181] the nominal remuneration of workers in manufacturing increased by 7.2 per cent, compared with increases of 12.9 per cent in 1971 and 18.5 in 1972 (see table 132).

At the same time it should be mentioned that the basic wage adjustments granted by the Government were relatively moderate. In March 1974 the Wages Commission fixed a compensatory adjustment of 250 sucres (10 dollars) per month for workers receiving monthly wages of between

[180] See United Nations, *Monthly Bulletin of Statistics*, September 1974, and Banco Central del Ecuador, *Memoria 1973*, op. cit.

[181] No more recent data were available.

1,000 and 5,000 sucres. It has been estimated that on average this was equivalent to an adjustment of 10 per cent, i.e., around one third of the rise in prices during the 12-month period preceding the grant of the wage adjustment.

The above information only gives an idea of the increases in remunerations in some sectors of the working population obviously not related with the active development of the external sector and other related activities. The qualitative data which it was possible to collect directly in Ecuador showed that the remunerations and adjustments in the petroleum sector and other import, trading and construction activities connected with the sector were substantially higher than in the rest of the economy.

This brought about inflationary pressures not reflected in the available wage indexes, which affected costs—directly and also in terms of a somewhat limited demonstration effect—and actual demand of the workers in the above-mentioned sectors.

In broader terms, the entire incorporation of the petroleum industry and the various related activities in the economy of Ecuador signified a rapid and intensive expansion of the most "modern" part of the system. Meanwhile, however, there was no outstanding progress in the more "primitive" part of the production apparatus, which continued to employ more than 50 per cent of the economically active population.

As the characteristic dual nature of the country's system of production became more extensive and more pronounced, substantial additional inflationary pressures which are difficult to quantify were unleashed. Thus, as the income recipients in the modern sector became relatively more numerous and more significant in terms of their level of spending—particularly in some geographical areas—the fact that they were prepared to pay higher real prices to obtain the goods and services they required took on greater importance, particularly when there were problems of inadequate supply of some goods. In other words, there was a tendency for corrections to be generated in a system of prices which, generally speaking, was consistent with low levels of productivity and *per capita* income.

Phenomena like that described, or similar to it, are of course inherent in development processes. Even so, they assumed particular importance in the recent evolution of the Ecuadorian economy because, on the one hand, the modernization of part of the economy was relatively widespread and very rapid, while the state of stagnation and low productivity per worker in the rest of it was deep-rooted and generalized.

D. Principal aspects of anti-inflationary policy

1. *Background*

In reviewing the anti-inflationary policy introduced by the Ecuadorian authorities one should not lose sight of some questions of a general nature whose impact on the bases, and on the framework in which the policy was to be carried out, was considerable.

First, it should be stressed that inflation is relatively new to the country and that, likewise, experience in the formulation and application of stabilizing measures is also limited and of recent date.

Secondly, the conditions which gave rise to the acceleration of inflation during 1973-1974 were also new, for the present world inflationary process, its intensity and the varied and far-reaching impact that it has on the peripheral economies have resulted in a situation hardly familiar to these economies, and even less so to Ecuador.

Finally, Ecuador's notable opening towards the exterior, initiated in 1972 with the launching of its petroleum exports, resulted—almost paradoxically and notwithstanding other beneficial effects—in the impact of external inflation being transmitted with great intensity throughout the country. A further contributory factor was the low flexibility of domestic supply—particularly of agricultural products—resulting from an economy in which relatively primitive forms of production continued to predominate.

Furthermore, it is worth pointing out that the assignment of priority to and the application of anti-inflationary measures began, in practice, only in 1973 and coincided with the acceleration of inflation in that year, at the very time that the destabilizing effects provoked by the developments mentioned in the external sector were having their maximum impact. Similarly, although the anti-inflationary measures adopted were far-reaching in scope, they did not provide a framework for a stabilization programme as such, in which the actions to be taken in the various fields of economic policy could find comprehensive and precise expression.

Bearing the foregoing in mind, this section will make a separate examination of the policies implemented, emphasis being placed on events which took place in 1973 and, where possible, and when adequate data were available, in 1974.

First, the actions taken with a view to tackling some structural causes of inflation will be examined, followed by a review of measures aimed rather at dealing with the conjunctural factors which arose during the period under study.

2. *Basic policies*

(a) *Agricultural policy*

Recognizing the serious nature of the problem caused by the limited growth of food production, the government authorities gave top priority to the programme for the agricultural sector, which was incorporated in the Integrated Change and Development Plan, 1973-1977.[182] This programme laid down a number of quite detailed targets and measures aimed at achieving, during the period of the Plan, an annual average growth of in the agricultural product of 5.3 per cent, i.e., a rate about five times higher than that recorded between 1965 and 1972.

Of course, in this document it is not feasible to evaluate the degree to which the various measures envisaged in the programme mentioned contributed and are continuing to contribute to the gradual elimination of the causes of inflexibility in agricultural production. This task is beyond the scope of the study and, moreover, the agricultural programme covered a much longer period which, in general, did not coincide with the period of accelerated inflation referred to above.

Notwithstanding the foregoing, however, examination of the price aspect of agricultural policy–an aspect more directly linked with the subject dealt with in this report–reveals some important points.

(i) *Price controls.* During the period under study a scheme aimed at fixing and controlling the price of a considerable number of food-stuffs (among others, milk, rice, sugar, coffee, several types of meat) was in operation and was gradually strengthened. Thus, in addition to action in the marketing of national and imported products already taken by the public institutions referred to, a Price Control Board was set up in April 1973 with wide powers to supervise the enforcement of controlled prices.

It is difficult to judge the results obtained through the price control mechanisms, but it may be noted that some studies carried out by international institutions suggest that during 1973 the prices of controlled food-stuffs increased less than those of non-controlled goods. In several cases the control of prices was made possible because domestic supply was strengthened by subsidized imports and/or restricted exports, or because temporary shortages of some articles were accepted.

From another point of view, price control produced some contradictory effects. First, on some occasions, when there was a big difference with respect to the international prices it was necessary to approve remarkably high increases in fixed prices. This provoked several adverse consequences–shortages in supplies and disincentives to production–which could have been avoided if smaller price adjustments had been authorized earlier.

Non-controlled food-stuffs, for their part, experienced considerable rises in prices which undermined the efforts and progress made in containing inflation through price control.

In addition, the distortions which arose between the prices of controlled products and those which were not controlled had some secondary effects. On the one hand, there was a tendency to intensify the production of non-controlled food-stuffs–to the detriment of controlled food-stuffs–and to sell controlled food-stuffs illegally in the country, or in neighbouring countries, at prices higher than those stipulated by the authorities. On the other, there were occasions when the product concerned was not marketed in its original form, but processed and sold in other forms which were exempt from price control.[183]

Lastly, the control of prices of some food-stuffs must have had negative repercussions on one of the basic objectives of the growth policy (and hence the anti-inflationary policy) of the country, because it failed to provide adequate price incentives to stimulate the production of several food items. This contradiction was even more marked in those cases where stricter controls were applied.

(ii) *Other complementary measures.* The agricultural policy also had limitations in other fields which were unfavourable to growth and anti-inflationary objectives. The best example of this was the absence of supporting price programmes and of programmes to provide complementary marketing facilities.

For all practical purposes the only supporting price programme effectively applied was that for wheat, and even in this case it was only in operation for a few months of the year. For other basic food products, such as rice and maize, no such programmes were in operation nor was suitable storage space available for temporary stocks of these goods.

As a result of this there were sharp and unnecessary fluctuations in the prices of some food-stuffs, since imbalances were created in the course of the year between the supply and demand for the product, while at the same time large

[182] The plan for the agricultural sector is divided into four principal sub-programmes: (*a*) agrarian reform; (*b*) land settlement; (*c*) the marketing of agricultural products, and (*d*) production.

[183] This occurred specifically in the case of milk, a considerable part of the production of which was diverted to the manufacture of cheese which was exported as well as sold in the country.

portions of some harvests were lost, thus adversely affecting the growth possibilities of the agricultural sector.

(b) *Fiscal policy*

As the current income earned by the central government from the levying of taxes in the petroleum sector increased, the rapid growth of government income in foreign currency accelerated, while income in national currency increased at a slower pace. At the same time, the relatively rapid increase in government expenditure forced the Central Bank to liquidate foreign exchange holdings to meet such expenditure.

Two fundamental traits of the fiscal structure, which did not change during the period under study, influenced this trend.

On the one hand, no important measures were adopted to strengthen the share in tax revenue of taxes levied on domestic activity. Outstanding in this respect is the limited influence which personal income tax and urban and rural property taxes continued to have.[184]

Although the need to make important changes in these taxes was recognized,[185] and such changes would have helped, moreover, to improve the elasticity of the system and to obtain other positive economic effects, in practice progress made in putting them into effect was limited.

On the other hand, although it is true that some partial progress was made, the system of earmarking government income for a number of specific predetermined expenditures continued, thereby standing in the way of a more flexible fiscal system, more in line with an anti-inflationary strategy.

The foregoing is further compounded by the fact that the rising oil income was also affected in different ways by specific allocations, so that a new element was introduced into the automatic income-expenditure relation. Of course, the inflationary potential of such a situation tended to be still greater when, on account of the balance-of-payments and the monetary account situations, income in foreign currency was used to finance expenditure in national currency.

It may be noted also that the role played by the State in attracting domestic funds through the sale of government bonds was relatively moderate. The sums involved in this type of operation amounted to approximately 500 million sucres per year (20 million dollars). Furthermore, no substantial changes were made in the terms of issue of public bonds in order to improve their real yield, and the nominal rates of interest earned lagged behind the inflation rate.

As regards the policy followed to control and channel government expenditure, the substantial increases in 1973 and 1974 in total government expenditure and in the public investment thus made possible are worthy of note. In general, although expenditure policy was expansive, the information available indicates that the growth in current expenditure was subject to greater restrictions than that of investment.

3. *Complementary policies*

(a) *Monetary policy*

The measures adopted by the monetary authorities were dictated principally by the need to curb the rate of growth of the money supply, since the direct issues by the Central Bank had increased rapidly, spurred on by the purchases of international reserves which the institution had to make. Nevertheless, during the period 1972-1974 no over-all quantitative targets were set or announced for the annual variation in the means of payments.

In 1972, 1973 and 1974 the relative increases in the direct issue were 39, 30 and 53 per cent respectively, while the comparable increases in the means of payment amounted to approximately 22 per cent, 31 per cent and 37 per cent. In other words, in 1972 a greater degree of success was achieved in the proposed task (see table 133).

Of particular note among the provisions introduced was the application of "portfolio growth ceilings" which limited the expansion of the total placements of the banking system to 3 per cent per quarter. During 1973, this measure does not seem to have been very effective, for the portfolio holdings subject to the growth ceiling increased by approximately 22 per cent, i.e., at almost double the rate for the previous year.[186]

Another measure aimed at reducing the multiplier effect of the direct issues by the Central Bank was a modification of the system of minimum legal cash reserves. Thus, through regulations adopted in June and December of 1973, it was stipulated that the compulsory legal cash reserves for banks must actually be held in cash. The aim, of course, was to make the operation of this instrument of monetary policy more restrictive.

It should be noted that it was not possible to obtain adequate information on changes in liquidity ratios during the period under study. However, it is felt that the way they were handled

[184] In 1972-1973 the yield from these taxes amounted to less than 20 per cent of total current income (2 per cent of the GDP).

[185] See document CIAP/635, op. cit., pp. 227 et seq.

[186] See Banco Central del Ecuador, *Memoria 1973*, pp. 63 et seq.

and the continued increase in these ratios was not a major element in the monetary policy followed.

From 1973, onwards, the Central Bank began to carry out open market operations, and through the placing of short-term Stabilization Bonds it managed to withdraw substantial sums of money from circulation. Thus, in the first year of operations, it tapped off 400 million sucres–a figure equal to one fourth of the increase in quasi-money recorded in 1973 and not much lower than the figure for the sale of government bonds referred to previously.

In addition to these quantitative monetary policy guidelines, some complementary qualitative aspects are worthy of note.

On the one hand, the system of funds set aside for special development purposes was strengthened and extended with the aim of intensifying the selective credit control policy in force by the Central Bank. Of special importance in this connexion is the volume of funds channelled through the Banco Nacional de Fomento, which received an additional 700 million sucres in credit from the banking system between the end of 1972 and the end of 1973. This figure corresponded to approximately 40 per cent of the expansion in bank placements for the year, and a fair share of this sum was used to finance the imports of food-stuffs effected by the Banco Nacional de Fomento.

On the other hand, there were no important changes in interest rate policy. The banking system continued to grant credit at nominal rates of interest, which were maintained without variation during the period 1972-1974. These rates became increasingly negative, in real terms, as inflation accelerated. An indication in this respect is the fact that the discount rate of the Central Bank remained steady at 8 per cent per year up to and including 1974 after having risen from 5 to 8 per cent in 1970.

(b) *International reserves management policy*

It is not surprising that the international reserves in the hands of the monetary authority increase rapidly when the exports of a country grow in a relatively short period at the pace and to the extent they did in Ecuador. For this reason, the main objective in circumstances like those of the years 1972-1974 would normally be to achieve both a relatively gradual and continuous increase in reserves and a reduction in the intensity of the monetary impact of the accumulation of reserves.

As regards the first aspect, total reserves amounted to 65 million dollars at the end of 1971, reached a relative maximum of 444 million by mid-1974, and then diminished after this date.[187] In other words, in the space of two and a half years the level of reserves increased seven-fold (see table 126).

Within this trend, the most rapid increases took place during 1972 and in the first half of 1974. In both cases, but particularly in 1972, the import policy did not manage (and to some extent did not even endeavour) to bring about a more rapid rise in imports. Thus, the measures for the liberalization of imports which were introduced during 1972 did not have any effect in that year, and in practice the imports of goods in 1972 were almost equal to those of 1971 in terms of current values, and were 4 per cent lower in constant values.

In the first part of 1974 the situation was different, because the strong and unforeseen increase in the price of petroleum which took place towards the end of 1973 and early in 1974 prevented the flow of imports from following more closely the month-by-month trends in exports. However, the new import liberalization measures introduced towards the end of 1973 and in the early months of 1974 resulted, in 1974, in the high level of 900 million dollars worth of imports, a good deal more than half of this amount being imported during the second half of the year.

From another standpoint, it should be borne in mind that so rapid an increase in the imports of the country could have resulted in an increase in the share of capital goods, since these constituted the imported component of new investment projects. This possibility was restricted, however, by the fact that there was a scarcity of projects and, moreover, a greater generation of domestic savings would also have been required to finance the greater investment which, theoretically, could have been made.

In the field of exports, the policy for handling international reserves was subject, in the main, to the use the Government made of the foreign exchange deriving from its share in the petroleum industry. As stated earlier, the greater the Government's need to sell foreign currency to the Central Bank to meet its expenditure in national currency, the more intense and direct were the repercussions on the monetary supply.

(c) *Exchange policy*

The policy of a pegged rate of exchange which was followed and the drop in the real value of the dollar exchange rate, as mentioned earlier, acted as an anti-inflationary factor.

[187] Between August and December 1974 reserves fluctuated around approximately 360 million dollars.

Thus, for example, between 1971 and 1974 the unit dollar value of imports of goods increased by 60 per cent, while the average real value of the rate of exchange fell by 11 per cent. In this way the inflationary effect which changes in import prices might have caused was reduced, for it would have been much greater if the real value of the dollar in sucres had been kept constant through periodic devaluations.[188]

An alternative exchange policy which was considered and discussed by the government authorities and by international agencies consisted of the revaluation of the sucre. By this means the reduction in the real value of the rate of exchange would have been greater, as would the anti-inflationary effect on imports as well as on the domestic prices of exported goods, while the monetary situation would also have been improved by the growth in reserves.

Apart from the anti-inflationary aspect, other grounds for the proposed revaluation included the low cost of petroleum production and the relative abundance of foreign exchange in the country.

Finally, however, it was decided not to revalue the sucre, since it was felt that the need to plan the medium-term and long-term development of the country on the right lines and to promote the export of non-traditional products must be taken into account, as well as the need to ensure more lasting equilibrium in the balance of payments. Furthermore, it was felt that as a possible anti-inflationary measure it was full of risks, and that it was preferable to have recourse to the use of other economic policies.

Considering another aspect of exchange policy, it is interesting to note that in 1973 and particularly in 1974, with the aim of reducing the domestic price of imports, customs tariffs for a large number of imports were reduced. In this connexion, note should be taken of the reduction (from 20 or more per cent to zero) in the tariff on agricultural inputs and implements. The reductions approved for several industrial inputs and products were also considerable.

In spite of the foregoing, however, in the case of food-stuffs the reduction in customs tariffs had little anti-inflationary impact, owing to the fact that the duties on such items were already quite insignificant.

In keeping with this target of cheaper imports—and also to liberalize their inflow—the system of prior deposits was abolished in 1973. At the end of 1972 the accumulated balance of these deposits amounted to 1,150 million sucres: quite a large figure, when it is considered that it was equivalent to 15 per cent of the money supply. Of course, the abolition of the measure referred to had a bad effect as regards monetary expansion, for it contributed to the acceleration experienced in the growth of the means of payments in 1973.

As regards exchange measures aimed at making foreign sales of national products less attractive by raising their prices, no new provisions of particular importance were introduced during the period under review. Indeed, as already mentioned, several measures were being proposed in 1973 aimed at reducing the export surtax, introduced at the same time as the 1970 devaluation, on bananas, coffee, cocoa and sugar. More specific information is not available on the turn events have taken in this respect.

(d) *Wages and salaries policy*

In the private sector, free bargaining between employers and workers was the general rule, with only limited participation by trade unions.

During the period under study no annual adjustment system linked to price changes was in operation for really substantial sectors of the population. Only at the beginning of 1974 was an adjustment in minimum wages approved, under the arrangements and with the effects mentioned previously. It is interesting to note, furthermore, that the active population working in the more "primitive" sector of the economy was practically left out of the provisions adopted on wages.[189]

Public servants were not given periodic or automatic adjustments either, but they did receive the compensatory bonus granted in March 1974.

Finally, it should be noted that the wages and salary policy failed to fix any more or less definite targets regarding the evolution which the real income of workers should follow.

[188] It should be remembered that in calculating this "real" value, domestic inflation in both Ecuador and the United States was taken into account (see table 127).

[189] However, it is possible that inflation affected this sector of the population to a lesser extent, since the majority of them practice a system of production whereby they supply their own needs.

6. URUGUAY

A. INTRODUCTORY NOTE

The review contained in this document of developments and policies in connexion with inflation in Uruguay has been structured differently from the rest of the country studies included in the present chapter, in view of the special features of Uruguay's experience.

Thus, the first part of this study deals with the development of the inflationary process since its beginnings in the mid-1950s, in order to identify the links existing between the stagnation of the economy and the creation of basic inflationary pressures, and to analyse the role played by the propagating mechanisms in the spread and multiplication of those pressures.

For various reasons, the period covered in the first part of the study extends up to and including 1971, since it is considered that this year closes an important phase in the course of inflation in Uruguay.

The second part examines events in the three years 1972-1974, taking into account that this more recent experience called for special consideration, in view of the general lines of this chapter of the *Economic Survey*.

Moreover, 1972 was the logical point of departure for the sub-period considered, because that year marked a change in the position of the government authorities regarding the problem of inflation and the need to adopt stabilization programmes to curb it, and because from that year onwards the impact of imported inflation began to make itself felt in Uruguay.

B. LONGER-TERM PROSPECTS: STAGNATION AND INFLATION

1. *Background*

Inflation in Uruguay has its own particular features which distinguish it from inflation in other countries of the region. Thus, in addition to being a fairly longstanding, continuing and virulent process, its main feature has been the clear association existing between economic stagnation and the creation of pressures which are a threat to price stability.

Concurrently with the arresting of growth, the start of the inflationary process may be placed almost exactly in 1957, when the rate of price increases, which had fluctuated around 6 to 7 per cent annually over the whole period 1939-1956, rose to about 20 per cent annually. Since 1957 there have been successive periods of acceleration and deceleration of the rate of price increases,[190] in keeping with the evolution of some basic variables and of the economic and stabilization policies put into practice, but the strong inflationary trend of the country's economy and the great difficulty or impossibility of achieving relative price stability for several consecutive years predominated.

The characteristics and roots of the complex phenomenon of Uruguay's economic stagnation have been studied in depth in a number of studies undertaken by national and international institutions.[191] In view of its nature and scope, however, the present study does not seem to be the place to consider this aspect; it is more important here to identify the main links between lack of growth and inflationary pressures.

In any case, in order to have in view some of the magnitudes identifying the size of the problem of stagnation, the trend of some representative indicators may be observed (see table 136).

Although the annual population growth rate was reduced from 1.5 per cent at the beginning of the 1950s to 1.2 per cent so far in the 1970s, the *per capita* gross domestic product reached a peak value of 960 dollars (at 1970 prices) in 1956, 10 years later it had dropped to below 900 dollars, and up to and including 1974 it fluctuated around this figure.[192]

As regards the goods producing sector, two outstanding facts are that the *per capita* agricultural production reached at the beginning of the 1950s has not since been exceeded,[193] and that *per capita* manufacturing production reached its peak in 1956, when it was more than 10 per cent higher than the figure recorded in 1973-1974.

The trend of external variables indicates that it was not until 1973 that exports of goods expressed in dollars at current prices exceeded the value of exports in 1950-1951, while over the whole period 1957 to 1968 export levels were about 40 per cent (or 100 million dollars annually) lower than those recorded at the beginning of the 1950s.

The trend of imports was similar to that of exports, although the biggest reduction occurred in the period 1964-1968, when the value of imports of goods was 40 per cent lower than in the early 1950s.

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[190] See table 135. Roughly, the periods of acceleration were 1957-1959, 1962-1967 and 1970-1974, while the rate of inflation decreased in 1960-1962 and 1968-1970.

[191] See, for example, Investment and Economic Development Committee (CIDE)-which in 1967 became the Plannning and Budget Office- *Estudio económico del Uruguay-evoluciones y perspectivas*, Montevideo, 1963; and *Plan Nacional de Desarrollo Económico y Social 1965-1974*, Montevideo, 1965; and OAS, *Evaluación del Plan Nacional de Desarrollo Económico y Social de la República Oriental del Uruguay 1965-1974*, Washington, D.C., 1967.

[192] While between 1956 and 1974 Uruguay's *per capita* gross domestic product fell by about 8 per cent, the average value for Latin America rose by over 60 per cent.

[193] On the whole, the growth of livestock production has been slower and less subject to annual fluctuations than crop production, but it still accounts for nearly 70 per cent of total agricultural output.

Table 135. Uruguay: trend of prices and related variables
(Percentages)

	Consumer price index			Variation in the dollar for imports (between annual averages)	Wages and salaries in manufacturing		Liquidity coefficient money supply GDP	Variation in money supply December to December	Total Government deficit as a percentage of GDP	Relative prices in agriculture[a] (December 1963 = 100)
	1957 = 100	Variation between annual averages	Variation December to December		Variation between annual averages	Index of real wages and salaries 1957 = 100				
Average 1939–1949	–	6.0	–	–	–	–	–	–	–	–
Average 1949–1954	–	6.6	–	–	–	–	–	–	–	–
1955	–	7.5	10.3	5.6	–	–	–	5.0	–	–
1956	–	6.7	6.0	14.6	–	–	–	12.8	–	–
1957	100.0	14.7	18.5	20.8	–	100.0	–	6.1	–	118.0
1958	117.5	17.5	19.5	15.8	15.3	98.1	15.6	30.8	–	90.0
1959	163.9	39.5	48.5	48.5	25.2	88.0	15.4	43.0	–	161.0
1960	227.5	38.8	36.3	102.0	44.3	91.5	13.6	30.6	–	121.0
1961	278.7	22.5	10.3	11.1	27.7	95.4	13.1	21.8	–	108.0
1962	309.1	10.9	11.2	0.0	14.7	98.6	12.7	1.0	–	112.0
1963	372.8	20.6	43.6	29.6	18.6	97.0	12.6	28.8	–	100.0
1964	533.8	43.2	35.4	16.7	35.6	91.9	11.4	42.0	–	94.0
1965	835.4	56.5	88.0	90.4	48.6	87.2	12.0	102.7	3.6	86.0
1966	1,449.4	73.5	49.4	103.6	93.5	97.2	10.7	40.1	0.3	93.0
1967	2,743.7	89.3	136.0	64.0	78.0	91.4	9.9	110.4	2.8	99.0
1968	6,184.3	125.4	66.3[b]	121.1	114.2	87.4	9.0	53.5	1.1	82.0
1969	7,476.8	20.9	14.5	0.0	28.5	92.4	10.0	61.3	2.3	86.0
1970	8,710.5	16.5	20.9	0.0	11.4	88.4	12.0	15.0	1.6	87.0
1971	10,792.3	23.9	35.7	4.0	27.4	90.8	14.0	51.1	5.6	106.0
1972	19,048.4	76.5	94.7	117.6[c]	48.5	76.4	13.0	52.1	2.4	126.0
1973	37,525.3	97.0	77.5	61.3[c]	90.3	73.8	13.0	74.5	1.1	116.0
1974	66,494.8	77.2	107.3	29.0[c]	75.0[d]	79.2[d]	12.0	62.2	3.0	92.0[e]

SOURCES: Dirección General de Estadística y Censos, *Indice de los precios del consumo;* Banco Central del Uruguay, *Indice de precios al por mayor de productos nacionales;* and ECLA estimates based on official statistics.

[a] Calculated by dividing the price index for agricultural products by the price index for manufactured products.

[b] Between December 1967 and June 1968 the increase was 63.7 per cent; between June and December 1968 it was 1.6 per cent.

[c] Variation from June to June.

[d] Average value calculated for the period January–September.

[e] Value for September.

Table 136. Uruguay: some indicators of economic trends

	1950	*1951*	*1956*	*1961*	*1966*	*1971*	*1972*	*1973*	*1974*
Total population (thousands of inhabitants)	2,193	2,227	2,397	2,590	2,754	2,921	2,956	2,990	3,025
Gross domestic product (1970 = 100)	68	74	87	86	91	99	98	99	100
Per capita gross domestic product (dollars at 1970 prices)	827	883	962	911	898	907	884	883	883
Exports of goods (millions of dollars)	254	236	216	175	190	197	242[a]	328	370
Per capita exports of goods (dollars)	116	106	90	68	69	67	82	110	122
Imports of goods (millions of dollars)	184	237	159	183	132	203	179	249	420
Per capita imports of goods (dollars)	84	106	66	71	48	69	61	83	139
Index of unit value of exports (1970 = 100)	114	159	101	90	98	101	131	190	204
Index of unit value of imports (1970 = 100)	82	98	102	90	91	106	111	133	209
Terms of trade (1970 = 100)	139	162	99	100	108	95	118	143	98
Export quantum index (1970 = 100)	99	66	95	87	87	87	82	77	74
Import quantum index (1970 = 100)	111	119	76	100	71	94	79	92	141
Agricultural production index (1970 = 100)	72	79	86	86	95	99	96	99	101
Per capita agricultural production index (1970 = 100)	95	102	104	96	100	98	94	96	96
Manufacturing production index (1970 = 100)	59	65	87	84	89	98	98	97	99
Per capita manufacturing production index (1970 = 100)	78	84	105	94	93	97	96	94	95

SOURCE: ECLA estimates based on official statistics.

[a] Including 28 million dollars' worth of non-monetary gold.

The course of the unit value of exports—which reflects the international prices of goods exported by Uruguay, mainly meat and wool—played a decisive role in the evolution of the external sector. Thus the favourable situation in the first half of the 1950s as regards world prices of these commodities did not occur again until 20 years later,[194] when world inflation spurted. Because of the impact of inflation on the unit value of Uruguay's imports, however, the terms of trade failed to regain in 1973 the levels recorded in 1950-1951 and in 1974 they reverted to a level comparable with that registered in 1970.

The trend of capital formation was consistent with that of the economy in general and the availability of foreign exchange for imports. The rate of investment in relation to the gross domestic product, which had reached around 20 per cent at the beginning of the 1950s, declined steadily from then onwards to levels of 15 per cent in the early 1960s and 10 per cent in the middle of that decade. Subsequently, the investment coefficient recovered slightly, remaining at around 11 per cent.

Among other circumstances, this reduction in the investment rate took place concurrently with an absolute decrease in domestic saving, particularly that generated by the public sector. In fact, since the end of the 1950s, the Treasury and the public sector have frequently shown deficits or very small surpluses on current account. Over the past 15 years, private saving has remained at or below the levels reached before 1960.

2. *Origins of inflation: structural factors and propagating mechanisms*

A study of the factors contributing to inflation in Uruguay and of the relationships between the growth and inflationary processes sheds light on some basic and more lasting features of the problem under review and, in particular, makes it possible to distinguish between those usually called structural factors and those identified as propagating factors of the basic disequilibria.

On this question, the *Economic Survey* of almost 10 years ago[195] contains several observations which are still relevant today.

On the one hand, it was stated that:

> "The various analyses of Uruguay's economy show the structural background of the present situation, which seems to be attributable to two basic factors. Firstly, the relative stagnation—and recently the recession—of agricultural production, which has ceased to fulfil its two traditional functions: to provide food and inputs for the domestic market and to create an exportable surplus that would make it possible to import the supplementary capital goods, primary products and consumer goods required if the national system is to develop properly. The general result of this trend has been the low growth rate of the domestic product, which, allowing for population growth, shrank in absolute terms by about 12 per cent between 1957 and 1965.
>
> "This circumstance is at variance with the second basic factor: social resistance to a decline in real income, a phenomenon which takes a highly individual form in Uruguay, which has a well-integrated and highly organized society. The population is thus fighting a rearguard action with a wide range of devices and instruments that enable each group to defend its own interests with some measure of success."[196]

In addition, the unfavourable course of agricultural production coincided with a situation where the relative prices for agriculture were actually quite encouraging for the sector. Thus, for example, a series covering real agricultural prices calculated on the basis of 1935-1937 = 100 shows that throughout the post-war period up to and including 1963 the index values fluctuated around 140.[197] In other words, the evolution of the agricultural sector acted as a structural factor of inflation, both because of the slow growth of production and because of the pressures it brought to bear on the general level of prices with the improvement in its relative position.

In connexion with the propagating mechanisms, on the other hand, the 1965 *Economic Survey* affirms that:

> "One such factor derives from the most vulnerable point of Uruguay's present economy—its trade balance. The inadequacy of the agricultural sector has led to persistent disequilibrium in Uruguay's external accounts, which in turn has prompted periodical devaluations of the national currency, both as a response (usually belated) to the basic maladjustment and as a means of curbing the

[194] The index of the unit value of exports (in dollars at current prices), with base year 1970 = 100, reached 135 in 1950-1954, fluctuated around 100 throughout the period 1958-1970, and soared to an average of over 190 in 1973-1974.

[195] See ECLA, *Economic Survey of Latin America, 1965* (United Nations Publication, Sales No. 67.II.G.1), pages 43-45.

[196] See *Economic Survey of Latin America, 1965*, op. cit., page 44.

[197] See *Evaluación del Plan Nacional de Desarrollo Economico y Social de la República Oriental del Uruguay 1965-1974*, op. cit., page 269. The real price series was obtained by deflating the agricultural price index by a representative index of general price trends.

demand for imports by raising their relative prices.

"Devaluation, which has raised the official rate of the dollar from approximately 11 pesos in 1961 to nearly 60 at the end of 1965, is another "propagating" factor of inflation, inasmuch as the consequent adjustment of the prices of imported goods provokes a defensive reaction on the part of those affected by such changes, whether wage-earners, who in the face of these price increases will try to obtain wage adjustments, or entrepreneurs, who will try to meet the higher cost of their imported inputs by raising the prices of their products. Simultaneously or successively, these two mechanisms of the inflationary spiral have set in motion the mechanisms involved in the fiscal and monetary sectors. The government machine, which in Uruguay employs a sizable proportion of the labour force, has had to satisfy to a greater or lesser extent the petitions of its active or retired personnel, and for that purpose it has had to raise taxes or resort to financing by the currency issuing institution. It is worth while noting the contradiction underlying public sector decisions on devaluation. On the one hand, devaluation opens the way to obtaining funds from additional export or import charges or from the credit expansion made possible by the increase in the value of the reserves. On the other hand, devaluation has the effects alluded to above, with the resulting increase in expenditure. This contradiction has also occurred or is occurring in other countries beset by the same type of problems, but it is especially significant, perhaps, in Uruguay because of the scale of employment in the public sector and its high level of organization.

"Thus, the various factors of fiscal disequilibrium–from the standpoint of both receipts (increases in taxes or currency issues) and expenditure (increases in wages and in transfers to other public sector agencies)–constitute the third important mechanism responsible for the spread of inflation.

"To use a simplified approach, the above-mentioned factors might be said to affect a fourth determinant of inflation–the monetary sector. It is a well-known fact that, theoretically at least, it is this sector which gives way to or resists the pressures that originate from various sources and require an increase in the money supply to meet the higher levels of nominal income and consequently of prices."[198]

[198] See *Economic Survey of Latin America, 1965,* op. cit., page 44.

It was also noted that in the course of the inflationary process the structural factors gradually lose part of their original significance, particularly in the more accelerated bursts of inflation, while the more immediate or propagating mechanisms acquire more importance.

With a view to illustrating the behaviour of the propagating mechanisms in the period 1955-1974 and its relationship with price trends, several indicators which have been considered useful for the purpose are presented in table 135. Some main conclusions may be drawn from these figures.

First, it is not easy to establish well-defined causal links or the order of importance of the various propagating mechanisms and the sequence in which they operated, since this is a circular process of interaction which, in addition, is constantly changing.

Secondly, the devaluations of the Uruguayan peso, according to their frequency and intensity, seem to have constituted the most active and direct of all the propagating mechanisms, which tends to confirm a hypothesis put forward in the above-mentioned *Economic Survey*. Moreover, the periods of decline in the rate of price increases (1959-1962 and 1968-1970) followed periods in which drastic devaluations in one or several consecutive years had made it possible temporarily to manage the economy with fewer financial and material pressures and with a slower rate of devaluation of the national currency.

Thirdly, wage adjustments were primarily a defensive mechanism in response to price variations. In this respect, the series on wages and salaries in manufacturing[199] reveals that the nominal wage adjustments lagged at least a year behind the changes in the rate of inflation. Thus, during spurts of inflation there were significant decreases in real wages and salaries, which were usually compensated for, often only in part, when adjustments were obtained to offset former price increases, or the rate of increase in prices slackened, or both.[200]

Fourthly, the behaviour of the monetary mechanism was different before and after 1968. Before that year it was a passive rather than an active factor, which gave way to the pressures

[199] The Statistics and Census Department also calculates wage and salary indexes for other sectors, but the manufacturing series was used here, since the available data cover a longer period and it has been subject to less frequent changes in the method of preparation.

[200] Although the limitations of the real wage and salary series are recognized, it may be noted in terms of broad trends that the relevant index, with base year 1957 = 100, dropped to below 90 in 1959, recovered to about 100 in 1962, fell again to less than 90 in 1968, recovered slightly up to 1971 and dropped to around 80 in 1974. This point will be dealt with again later.

originating outside it, and the periodical percentage variations in the money supply were consistently lower than those recorded in prices. This trend contributed to the decrease in the liquidity coefficient (money supply/gross domestic product) from values of over 15 per cent in 1958-1959 to less than 10 per cent in 1967-1968. This trend was reversed after 1968 and the coefficient rose to levels of around 13 per cent in the last few years, except in 1974.

Lastly, the government finances have generally been an element contributing to financial and price instability, first because there have frequently been fiscal–and public–deficits[201] which have been covered to a great extent, with issues by the monetary authorities and, secondly, because the size of the deficits has fluctuated widely.

Some available data suggest that in 1956-1957 the fiscal deficit began to have some relative importance upon reaching 2 per cent of the gross domestic product.[202] In subsequent years up to and including 1961, the deficit was maintained or reduced, but started to rise in 1962 and by 1965 it was over 3.5 per cent of the gross domestic product. From that year until 1974, the deficit decreased in one year and increased again in the next–except in 1973–the highest relative values being recorded in 1967, 1969, 1971 in particular, and 1974 (see table 135).

Two supplementary observations on the size of the fiscal deficit and its fluctuations are called for here. As regards its origin, a predominating role was played by the greater or lesser annual revenue obtained from export taxes, which increased substantially in periods when the devaluations were most drastic.[203]

As regards financing the deficit, there was an obvious link between the greater fiscal disequilibria and the higher rates of increase in the money supply. This was partly due to the fact that other sources of financing to cover the deficit, such as external loans and the sale of government bonds–as distinct from direct issues by the monetary authorities–were of little relative importance and had a small range of compensatory flexibility.

3. *Stabilization efforts up to 1971*

(a) *Experience prior to 1968-1971*

Within the context of this long history of inflation, as the annual price increases became more violent and the adverse economic and social effects of the problem snowballed and spread, more importance and priority were attached to the framing and implementation of anti-inflationary policies, which became progressively more complex and more difficult to define.

Thus, "at the outset, when inflationary pressures had but a moderate and somewhat intermittent effect on prices, the remedies adopted were piecemeal and sporadic so far as the range of instruments used was concerned. Various expedients to curb the demand for imports were combined with others aimed at stepping up exportable surpluses (for example, by endeavouring to reduce domestic consumption), while at the same time, or at other stages, more importance was attached to tightening the money supply or to increasing public revenue".[204]

At a later date, other more intergrated stabilization systems were formulated; in some instances these were applied in their entirety, but not in others, or only to a partial extent. Among the latter was what was known as the Annual Programme (referring to 1965), the anti-inflationary project which formed part of the National Development Plan 1965-1974, prepared by CIDE. This programme constituted the beginning of a rather longer-term stabilization plan–consistent with the development plan–and favoured a "gradualist" approach to containing inflation. It also defined a group of measures and institutional arrangements aimed at simultaneously getting rid of the structural factors and the propagating mechanisms which were causing inflation.

Among the measures considered, mention should be made of the proposal to draw up a social agreement between the Government, the entrepreneurs and the wage workers, which would allow a periodic definition and co-ordination of the general norms which should govern wage policies and some basic prices and the remuneration of the capital factor.

For various reasons, particularly of a political nature, the Annual Programme and subsequent programmes, and the Development Plan were implemented to only a small extent. However, many of the ideas and lines of action proposed in them materialized as specific measures in later years.[205]

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[201] Fiscal deficits are defined as the difference between total expenditure (current and capital) and current income.

[202] See *Evaluación del Plan Nacional de Desarrollo Económico y Social de la República Oriental del Uruguay 1965-1974*, op. cit., page 514.

[203] Frequently, in those periods, there was the twofold effect of higher revenue resulting from the devaluation itself and that resulting from the rise in export taxes.

[204] See *Economic Survey of Latin America, 1965*, op. cit., page 45.

[205] Notable examples of these which may be mentioned were the creation of the Central Bank and the Planning and Budget Office in 1967 and the priority given as from that date to the substantive and financial programming of the economy and also to the co-ordination between the two.

It should also be borne in mind that up to 1966 inclusive, the anti-inflationary policies introduced were affected by the restricted powers and the institutional limitations which characterized the Uruguayan Executive.

This situation underwent a basic change in March 1967, with the beginning of the administration of a new Government, elected in November 1966, and the adoption at the same time of constitutional reforms introducing a presidential system and granting the Government broader powers.

During 1967 and the first half of 1968, however, the rate of inflation increased, particularly as a result of the violent fiscal and monetary shock of the adjustment of over 100 per cent in public sector salaries,[206] which came into force at the beginning of 1967, and because of the repercussions from an external trade situation in which low export levels coincided with sharp devaluations of the local currency (see tables 135 and 136).

At the same time as the rate of price increases accelerated, the opinion was gaining consensus in government circles that it was essential to introduce an energetic stabilization programme which would enable the increasingly imminent risk of hyperinflation to be avoided. Finally, in June 1968—in circumstances in which it was estimated that if the price trends of the first half of the year were to continue throughout the year a possible annual rate of increase in prices of not less than 200 per cent would be reached—the Government decided to go forward with an anti-inflationary policy, clearly differentiated from those which had been applied previously.

(b) *The stabilization policy 1968-1971*

The strategy followed as from the second half of 1968 was aimed at bringing inflation to an abrupt halt, i.e., the type of stabilization usually known as shock treatment, as opposed to the gradualist approach, was chosen.

(i) *The programme and its results.* A central element of the policy was the prices, wages and incomes freeze—at their June 1968 levels—which was brought into force as from July of that year.

In order to make the freeze effective, a system of almost total centralization was established for determining prices and wages, while previously existing machinery was done away with, principally such machinery as was outside the direct radius of action of the Government. Thus, the tripartite wages councils disappeared together with the freedom to fix wholesale and retail prices for the main products handled in the economy of Uruguay. In order to carry out these new functions, a Productivity, Prices and Incomes Commission (COPRIN), was set up, where, despite tripartite representation, it was the Executive which carried the decisive weight in the making of decisions.

With the creation of COPRIN—and the ample powers granted to it—the State took control of practically all prices, of merchandise and factors, in the economy, in both the public and the private sector. The fixing, control and very occasionally the revision of prices and wages, ranged from the most general and relatively most important cases to other more specific cases which were less important to the functioning of the production and marketing system.

A second basic element of the stabilization policy followed consisted in maintaining a fixed rate of exchange (of 250 pesos to the dollar) applicable to commercial and financial operations with the exterior, while at the same time existing controls for regulating the inflow and outflow of foreign exchange in the commercial and financial markets were tightened.[207]

The maintenance of a fixed exchange rate was considered feasible for a relatively long period, because the authorities were of the opinion that the sizable devaluations agreed upon towards the end of 1967 and in the second quarter of 1968 had led to a possible over-pricing of foreign exchange, a situation which had not arisen in the country for a long time. This over-pricing, in its turn, would spur on agricultural production and exports and strengthen the fiscal finances—though increased returns from withholdings—especially if the prices and wages freeze decreed were successful.

Lastly, by means of the careful handling of fiscal and monetary instruments, it was hoped to maintain a reasonable balance between the evolution of financial and material variables, so as to avoid a situation of over-expansion of liquidity, particularly in an economy where prices and wages must remain stabilized.

The measures indicated and other secondary measures which it does not seem necessary to review in the present document, were applied during a period of approximately three years which lasted till the second half of 1971.

Without going into too much detail regarding the probable repercussions of the anti-inflationary strategy on growth and its structure and on

[206] For constitutional reasons, the 1966 adjustment had not been granted, since it was just previous to the elections.

[207] Nevertheless the so-called "parallel" market continued to function, although in a limited and illegal form.

income distribution,[208] it seems obvious that this strategy succeeded in containing the growth of prices, especially in the second half of 1968 and in 1969.

The consumer price index, which had increased by 136 per cent between December 1966 and December 1967 and by 63.7 per cent between December 1967 and June 1968, increased by only 1.6 per cent between June and December 1968, and by 14.5 per cent during 1969. The rates of inflation in 1970 and 1971 were 20.9 per cent and 35.7 per cent, respectively (see table 135).[209]

(ii) *The breakdown of the programme*. In the course of time, and especially in 1971, numerous pressures were generated, which undermined the base of the anti-inflationary programme. These pressures may be ascribed basically to the fact that the traditional inflation propagating mechanisms in Uruguay were regaining strength, combined in 1971 with an adverse economic situation and increasing operational complications in the implementation of the stabilization programme.

In the first place, it should be observed in connexion with these propagation mechanisms, that there was a progressive accumulation of various elements which made it increasingly difficult to maintain the rate of exchange established in June 1968. Local prices continued to rise, although to a moderate extent, which eliminated the over-pricing of foreign currency recorded in mid-1968; it became increasingly difficult to contain the demand for imports, in a situation where at one and the same time there was a relative decrease in local prices of imported articles and a significant increase in over-all demand, in real and financial terms; local exporters, particularly of meat, wool and hides, began to accumulate stocks and postponed selling abroad as they waited for a more favourable exchange rate;[210] and in 1970 and 1971 the balance of payments was stabilized by means of a decrease of approximately 30 million dollars per year in net international reserves (see table 137).

[208] Between 1967 and 1971 the gross domestic product increased by around 3 per cent annually. Real wages in industry--and average wages for the economy as a whole--remained fairly stable throughout the period 1967–1971. See Central Bank of Uruguay, *Indicadores de la actividad económico-financiera*, published monthly.

[209] The wholesale price index for domestic products recorded a trend very similar to that of consumer prices. The variations in the wholesale index were: 124.7 per cent in 1967; 63.7 per cent in the first half of 1968 and 1.4 per cent in the second half; 7.3 per cent in 1969, 17.9 in 1970 and 40 per cent in 1971. See *Indicadores de la actividad económico-financiera*, op. cit.

[210] Or sold a percentage of their goods outside legal channels within the country and/or in border countries.

Table 137. Uruguay: balance of payments
(Millions of dollars)

	Average 1966-1970	*1971*	*1972*	*1973*	*1974*	
Current account						
Exports of goods and services	250.6	252.7	310.8	409.8	463.4	
Goods FOB	190.5	196.8	242.0	327.6	370.1	
Services	60.1	55.9	68.8	82.2	93.3	
Imports of goods and services	233.7	302.9	279.3	366.3	566.4	
Goods FOB	157.5	203.0	178.7	248.6	419.7	
Services	76.2	99.9	100.6	117.7	146.7	
Net external investment income	−23.2	−21.6	−23.5	−25.1	−39.5	
Profits	−1.0	–	–	–	–	
Interest	−22.2	−21.6	−23.5	−25.1	−39.5	
Net private transfer payments	−0.2	−0.6	−0.2	−0.2	–	
Balance on current account	−6.5	−72.4	7.8	18.2	−142.5	
Capital account						
Net external financing ($a + b + c + d + e$)	6.5	72.4	−7.8	−18.2	142.5	
(*a*) Net external non-compensatory capital	26.3	83.1	69.8	47.4		
Direct investment	–	–	–	–		
Long- and medium-term loans	21.1	57.0	59.9	31.6		
Amortization payments	−14.8	−19.3	−25.1	−47.2		
Short-term liabilities	10.5	36.5	23.1	44.0		85.3
Official transfer payments	9.5	8.9	11.8	19.0		
(*b*) Domestic non-compensatory capital or assets	−0.6	−2.6	0.6	−25.7		
(*c*) Errors and omissions	−16.6	−44.8	−56.8	−82.4		
(*d*) Allocation of SDRs	1.8	7.4	8.1	0.0		
(*e*) Net compensatory financing (– increase)	−4.4	29.3	−29.4	42.5		57.2

SOURCE: ECLA, on the basis of official statistics.

Table 138. Uruguay: central government finances
(Thousands of millions of pesos at current prices)

	1969	*1970*	*Percentage variation*	*1971*	*Percentage variation*	*1972*	*Percentage variation*	*1973*	*Percentage variation*	*1974*[a]	*Percentage variation*
(1) Current income	61.8	82.9	34.1	103.1	24.4	167.6	62.6	370.2	120.9	606.1	63.7
(2) Total expenditure	73.5	91.2	24.1	145.2	59.2	199.4	37.3	406.4	103.8	734.7	80.8
(3) Total central government deficit (2 – 1)	11.7	8.3	–29.1	42.1	407.2	31.8	–24.5	36.2	13.8	128.6	255.2
(4) Financing of the total deficit[b]	–	8.3	–	42.1	–	31.8	–	36.2	–	128.6	–
(*a*) External credit	–	1.1	–	0.8	–	2.9	–	8.1	–	5.0	–
(*b*) Domestic credit	–	7.2	–	41.3	–	28.9	–	28.1	–	123.6	–
(i) Monetary authorities	–	(3.2)	–	(36.4)	–	(24.8)	–	(20.9)	–	(102.3)	–
(ii) Other sources (including Treasury bonds)	–	(4.0)	–	(4.9)	–	(4.1)	–	(7.2)	–	(21.3)	–

SOURCES: IMF, *International Financial Statistics*, February 1975; and ECLA, on the basis of official statistics.

[a] Estimates.
[b] After deduction of amortization payments on the domestic and external debt.

Table 139. Uruguay: monetary trends
(Thousands of millions of pesos at current prices)

	1969	*1970*	*Percentage variation*	*1971*	*Percentage variation*	*1972*	*Percentage variation*	*1973*	*Percentage variation*	*1974*[a]	*Percentage variation*
I. *Composition of the monetary resources*											
(1) Money	72.0	82.8	15.0	125.1	51.1	190.3	52.1	331.9	74.5	538.2	62.2
(2) Quasi-money	28.8	38.7	34.4	56.5	46.0	96.6	71.0	164.3	70.1	–	–
II. *Factors of expansion and contraction*											
(3) Domestic credit	76.8	104.4	35.9	173.8	66.5	337.2	94.0	510.3	51.3	950.0	86.0
(*a*) to the public sector	18.7	20.3	8.6	42.5	109.4	76.8	80.7	84.3	9.8	–	67.0
(*b*) to the private sector	58.1	84.1	44.8	131.3	56.0	260.4	98.3	426.0	63.6	–	94.0
(4) Net international reserves	–1.8	–10.5	–	–7.0	–	–	–	–	–	–	–

SOURCES: IMF, *International Financial Statistics*, February 1975; and ECLA, on the basis of official statistics.

[a] Estimates.

In response to these pressures, the currency was devalued from 250 to 370 pesos to the dollar in the last quarter of 1971, and this gave renewed impetus to a propagation mechanism which had remained inactive for more than three years.

Secondly, the money supply—at times under pressure mainly from the growth of credit to the public sector (in 1969 and 1971), and at others from the increase in credit to the private sector (in 1970)—grew more rapidly than prices and economic activity, with the result that the liquidity coefficient increased steadily and significantly between 1968 and 1971 (from 9 per cent to 14 per cent; see table 135).

Although it may be argued that this increase in liquidity was to be expected since inflationary expectations were slumping, it is also true that it made for a more vigorous growth—perhaps excessively so—of total demand, including that for imports, and also determined a relatively larger supply of financial resources, which was a potential risk should other factors tend to upset price stability, as was the case in 1971.

Thirdly, in 1971 the fiscal situation deteriorated notably because total government expenditure increased by around 60 per cent while the increase in current income was 24 per cent (see table 138). The increase in expenditure basically reflected the large increase in public sector wages in that year. The slow growth of current income was influenced by the fact that the return from withholdings dropped owing to the stability of the exchange rate and the decrease in exports.

As a result of these trends, the fiscal deficit increased in relation to the gross domestic product from 1.6 per cent to 5.6 per cent, and had to be financed almost entirely by direct issues by the Central Bank in favour of the Government. In 1971, fiscal activities were thus of great importance as a factor of monetary expansion, in a situation where the rate of increase in the quantity of money rose from 15 per cent in 1970 to 51 per cent the following year (see tables 135 and 139).

In the fourth place, the role of wage adjustments as a propagation mechanism was not of outstanding importance, except as already noted, for public sector wages in 1971. It should be recalled that real wages in the private sector, more precisely in industry, remained relatively stable between 1967 and 1971.

As far as conjunctural factors are concerned, it should be recalled that 1971 marked the end of a Government and a year of presidential elections. In the circumstances, the outgoing Government implemented the stabilization programme which it had set for itself rather less energetically than in previous years.

Lastly, in connexion with the increasing operational complexity of centralizing wage and price control, in the course of time the work of COPRIN became unquestionably more complicated and overloaded, which hampered efficient functioning of the stabilization system. One instrumental factor was the increase in the number of requests for the review of prices and wages which reached COPRIN, and the fact, already commented upon, that the field in which this institution was enpowered to act and exercise control was very wide and very diverse.

C. THE PERIOD 1972-1974: REACTIVATION OF THE MOVEMENT OF PRICES AND IMPORTED INFLATION

1. *The general setting*

The evolution of inflation and the economy in Uruguay during the period 1972-1974 has some main features.

The first aspect of note is the rapid reactivation of inflation, after the breakdown of the stabilization policy brought in during the three-year period 1968-1971 had become more pronounced at the end of 1971.

In any case, after annual price increases of around 100 per cent were reached in 1972, inflation remained at about this level in 1973 and 1974, with no indications of any later increase or, conversely, any decrease in its rate (see table 140).

Secondly, during the last three-year period, not only was the strategy applied in the previous period abandoned as far as stabilization policies and measures are concerned, but a scheme of action different to that of 1968-1971 progressively took shape.

The shock treatment alternative which had been followed was repiaced by another system characterized by the flexibility of its price mechanism and the functional nature of movements in the level and system of prices. The rates of inflation considered acceptable by the authorities largely took second place to other economic policy priorities, especially as regards the direction and requirements of growth.

In the third place, to the endogenous factors which contributed to the existence and duration of disequilibria in domestic prices was added an exogenous influence as from 1972—imported inflation—which is still active and has acquired more force with the passage of time.

It should be noted that the internalization of the repercussions of externally generated inflation was facilitated by the magnitude of the rises in

Table 140. Uruguay: recent consumer and wholesale price trends
(Percentage variations)

	1970		*1971*		*1972*		*1973*		*1974*	
	Between annual averages	*December to December*	*Between annual averages*	*December to December*	*Between annual averages*	*December to December*	*Between annual averages*	*December to December*	*Between annual averages*	*December to December*
(1) Consumer price index . .	16.5	20.9	23.9	35.7	76.5	94.7	97.0	77.5	77.2	107.3
(2) General index of wholesale prices of domestic products	13.7	17.9	20.4	40.0	89.9	114.6	114.9	91.7	–	51.0[a]
(*a*) Manufactured products	13.2	17.5	17.1	32.1	80.4	102.8	118.0	97.2	–	62.1[a]
(*b*) Agricultural products	15.3	19.1	29.7	61.6	113.9	141.0	108.4	81.3	–	28.3[a]

SOURCES: Dirección General de Estadística y Censos, *Indice de los precios del consumo;* and Banco Central del Uruguay, *Indice de precios al por mayor de productos nacionales.*

[a] Variation between December 1973 and September 1974.

international prices; by the fact that the country was undergoing a process of domestic inflation of some consideration; and by the policy being followed of bringing domestic prices up to the level of international prices, particularly as food prices in the world market had increased substantially.

Lastly, another outstanding feature of the period 1972-1974 was the resumption of the old tendency of the Uruguayan economy to stagnate following a brief interruption of this trend, as has already been observed, in the years immediately preceding this period, especially during 1968-1970.

In fact the data given in tables 141 to 144 show that between 1971 and 1974 the gross domestic product showed an annual average growth rate of 0.5 per cent, i.e., the annual *per capita* product decreased by 0.7 per cent.

It may also be seen from an examination of the trends of the various sectors of economic activity that the gross domestic product generated by agriculture remained static, in terms of absolute values, between 1971 and 1974, and that industry grew during the same period at a slower rate than the population. Only construction continued to develop at a speed similar to that of previous years, i.e., an annual rate of around 4 per cent (see table 143).

As regards the evolution of total supply and demand in this general setting of stagnation, the further drop in the investment coefficient during 1972-1974, following its recovery in 1968-1971, is worthy of note.

Table 141. Uruguay: total supply and demand

	(Thousands of millions of pesos at 1970 prices)		*Annual growth rate*					
	1970	*1974*[a]	*1965-1970*	*1971-1974*	*1971*	*1972*	*1973*	*1974*[a]
Total supply	*688.7*	*680.7*	*3.2*	*0.3*	*-2.0*	*-2.4*	*1.8*	*2.5*
Imports	76.6	65.1	12.8	-1.7	-10.6	-11.9	9.4	8.2
Gross domestic product	612.1	615.6	2.3	0.5	-1.0	-1.3	1.0	1.9
Total demand	*688.7*	*680.7*	*3.2*	*0.3*	*-2.0*	*-2.4*	*1.8*	*2.5*
Exports	71.6	64.6	-3.0	2.9	-17.1	10.8	-9.9	8.9
Gross domestic investment	70.0	64.0	7.2	-5.3	7.7	-12.0	-3.0	-0.5
Gross fixed investment	68.5	...	7.1	...	2.6	-17.9	-4.6	...
Total consumption	547.1	552.1	3.7	0.8	-1.3	-2.5	3.8	2.2
General government	92.1	83.2	5.7	-1.0	-6.8	-6.0	3.4	-0.3
Private	454.9	468.9	3.3	1.1	-0.2	-1.9	3.9	2.6

SOURCE: ECLA, on the basis of official statistics. [a] Preliminary figures.

Table 142. Uruguay: structure of total supply and demand[a]
(Percentages)

	1965	*Average 1969-1970*	*1970*	*1971*	*1972*	*1973*	*1974*
Total supply	*107.7*	*111.8*	*112.5*	*111.3*	*110.1*	*110.9*	*111.6*
Gross domestic product	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Imports	7.7	11.8	12.5	11.3	10.1	10.9	11.6
Total demand	*107.7*	*111.8*	*112.5*	*111.3*	*110.1*	*110.9*	*111.6*
Exports	15.2	11.8	11.7	9.8	11.0	9.8	10.5
Gross domestic investment	9.1	11.1	11.4	12.4	11.1	10.7	10.4
Gross fixed investment	8.9	11.1	11.2	11.6	9.6	9.1	–
Total consumption	83.4	88.8	89.4	89.1	88.0	90.4	90.7
General government	12.8	14.6	15.0	14.2	13.5	13.8	13.5
Private	70.6	74.2	74.4	74.9	74.5	76.6	77.2

SOURCE: ECLA, estimates based on official statistics. [a] At 1970 prices.

Table 143. Uruguay: gross domestic product, by sector of economic activity

	(Millions of pesos at 1970 prices)		Annual growth rate					
	1970	1974[a]	1965-1970	1971-1974	1971	1972	1973	1974[a]
Agriculture	67,164	66,600	2.8	0.1	-1.2	-3.4	3.1	0.8
Manufacturing[b]	128,760	129,995	2.4	1.0	-1.8	-0.3	-0.4	3.6
Construction	20,182	24,084	4.3	4.1	5.8	5.5	-2.0	9.1
Subtotal goods	*216,106*	*220,679*	*2.7*	*1.0*	*-0.9*	*-0.7*	*0.5*	*3.3*
Electricity, gas, water and sanitary services	7,919	8,749	5.0	1.7	5.1	4.2	5.2	-4.1
Transport and communications	45,496	45,917	0.1	-0.7	3.0	-6.3	0.6	3.9
Subtotal basic services	*53,415*	*54,666*	*0.7*	*-0.3*	*3.3*	*-4.7*	*1.4*	*2.5*
Commerce and finance	91,603	87,201	0.9	-0.2	-4.1	-4.5	1.2	2.6
Ownership of dwellings	27,436		1.9		1.5	1.5	0.7	
Government	76,734	170,263	4.3	0.3	-2.2	0.0	0.7	-0.4
Miscellaneous services	66,336		2.3		-1.0	1.2	0.7	
Subtotal other services	*262,109*	*257,464*	*2.3*	*0.1*	*-2.2*	*-1.1*	*0.9*	*0.6*
Total	*531,630*	*534,560*	*2.3*	*0.5*	*-1.0*	*-1.3*	*1.0*	*1.9*

SOURCE: ECLA, on the basis of official statistics.

[a] Preliminary figures.
[b] Including mining.

Table 144. Uruguay: structure of gross domestic product, by sector of economic activity[a]
(Percentages)

	1965	Averages 1966-1970	1970	1971	1972	1973	1974
Agriculture	12.3	12.2	12.6	12.6	12.3	12.6	12.5
Manufacturing[b]	24.0	24.1	24.2	24.0	24.3	23.9	24.4
Construction	3.4	3.7	3.8	4.1	4.3	4.2	4.5
Subtotal goods	*39.8*	*39.9*	*40.6*	*40.7*	*40.9*	*40.7*	*41.5*
Electricity, gas, water and sanitary services	1.3	1.4	1.5	1.6	1.7	1.7	1.6
Transport and communications	9.5	8.9	8.6	8.9	8.5	8.4	8.6
Subtotal basic services	*10.8*	*10.3*	*10.0*	*10.5*	*10.1*	*10.2*	*10.2*
Commerce and finance	18.4	16.9	17.2	16.7	16.2	16.2	16.3
Ownership of dwellings	5.3	5.3	5.2	5.3	5.4	5.4	
Government	13.1	15.2	14.4	14.3	14.5	14.4	31.9
Miscellaneous services	12.4	12.6	12.5	12.5	12.8	12.8	
Subtotal other services	*49.2*	*50.0*	*49.3*	*48.7*	*48.9*	*48.8*	*48.2*
Total	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*

SOURCE: ECLA estimates based on official statistics.

[a] At 1970 prices.
[b] Including mining.

2. *Internal factors of inflation*

In the reactivation of inflation which took place as from late 1971, the role of the propagation mechanisms was again decisive. However, it is noteworthy that owing to special conditions some of these propagation mechanisms proved to be more persistent or more intensive than in previous periods, or showed both these characteristics.

In the first place, during the last few years an attempt was made to channel inflation along corrective lines, the main aim being to ensure systematically better prices for exports and agricultural products. With this end in view, two mechanisms or guidelines of great importance for the operation of the system were introduced.

One of these was the establishment, early in 1972, of an exchange procedure which consists in periodical mini-devaluations of the national currency. Thus, after the two maxi-devaluations at the end of 1971 and the beginning of 1972 (which raised the value of the import dollar from 250 to 500 pesos), movements of the exchange rate continued to take place at intervals.

Another was the acceptance–or rather the pursuit–of an improvement in the relative prices of agricultural products. Influence in that direction was exerted by exchange policy itself, by a more liberal approach to the determination of agricultural prices (to which end the number of food products subject to official price-fixing was considerably restricted), and by the exposure of domestic industry to external competition, in consequence of the elimination of quantitative import controls.

In line with this policy, between the end of 1970 and the year 1972, wholesale prices of agricultural commodities, in relation to those of manufactures, rose by about 45 per cent, thus becoming a major factor in the propagation of inflation. Subsequently, once the over-all annual rate of price increases had reached 100 per cent, in the years 1973 and 1974, prices of manufactures increased faster than those of agricultural products (see tables 135 and 140).

Secondly, the role played by the monetary system as a propagating mechanism was actually contradictory. Generally speaking, in the three-year period 1972-1974 the percentage variations in the money supply were smaller than those in prices, which led to a gradual reduction of the liquidity coefficient of the economy and, up to a point, relegated the monetary instrument to a mainly passive function.[211]

On specific occasions, however, the authorities endeavoured to prevent the decrease in the liquidity coefficient, which was exercising a moderating influence on inflationary trends, from being carried too far and consequently producing depressive effects. For example, action was taken to that end at the beginning of the last quarter of 1973, when the contractionist monetary programme that had been applied during the rest of the year was adjusted and expanded with the aim of adapting the growth of the money supply to the needs of the economy.

Thirdly, wage adjustments did not play a very active part as a mechanism of inflationary propagation. During the period 1972-1974, they fell short of price increases. Thus, between 1971 and 1974 the index of real wages in manufacturing industry showed a decrease of about 10 per cent (see table 135). The average index of wages in the economy as a whole declined in a similar proportion.[212]

Lastly, the action of the fiscal sector as a factor of propagation–especially on account of its linkage with monetary expansion–was particularly important in the year 1974. Since current expenditure increased faster than current income,[213] the total central government deficit rose by over 250 per cent, and, in order to finance it, the monetary authorities had to quintuple the volume of resources that they had earmarked for the purpose in 1973 (see table 138).

3. *Imported inflation*

Imported inflation was brought into Uruguay in a context which allowed its repercussions to spread intensively and with ease, combining with the inflationary pressures generated on the domestic front.

Indeed, when the external impact began to make itself felt, the re-acceleration of inflation had already gained impetus on its own account, and, complementarily, the economic policy which gradually took shape during the period aimed more and more unequivocally at approximating internal to international prices. Naturally, this approximation could be most rapidly achieved in the case of agricultural products, with the ensuing inflationary effects. On the other hand, it was necessarily a slower business where manufactures were concerned, despite the fact that in their case the resulting repercussions might ultimately have proved anti-inflationary, in view of the high relative costs of domestic industry.

In accordance with the classification suggested in the analysis of inflation in Latin America made elsewhere in the present study, the direct influence of imported inflation will first be considered, and its indirect repercussions will then be examined.

(a) *Direct effects*

In 1972 the increase in the unit value of exports of goods, in terms of dollars at current prices, was already substantial, amounting to 30 per cent (see table 145). Basically, given the structure of Uruguay's exports, this variation derived from the rise in the world market price of beef, which in that year exceeded 30 per cent, and had been as much as about 80 per cent between 1970 and 1972 (see table 146).

This movement was paralleled by the upswing in the average domestic price of beef, which, having already increased by over 75 per cent in 1971, soared by an additional 130 per cent,

[211] It is worth while, however, to bear in mind an earlier comment to the effect that the reduction noted is consonant with an increase in the expectations of inflation and in the speed of circulation of the means of payments.

[212] See Central Bank of Uruguay, *Indicadores de la actividad económico-financiera*, March 1975. The nominal series are deflated by the consumer price index.

[213] Compensatory wage and pension adjustments covered by the national exchequer and a slower increase than had been expected in revenue from export taxes largely account for this trend.

Table 145. Uruguay: trends in selected foreign trade indicators

	Average 1966-1970	*1971*	*1972*	*1973*	*1974*
(1) Exports of goods (FOB, millions of dollars)	190.5	196.8	242.0	327.6	370.1
(2) Exports of goods (millions of dollars, 1970 = 100)	85.0	87.8	108.0	146.0	165.1
(3) Index of unit value of exports of goods (1970 = 100)	93.6	101.0	131.0	190.0	203.7
(4) Index of constant value of exports of goods (1970 = 100) [(2)/(3) x 100]	90.8	86.9	82.4	76.8	81.1
(5) Imports of goods (FOB, millions of dollars)	157.5	203.0	178.7	248.6	419.7
(6) Imports of goods (millions of dollars, 1970 = 100)	77.6	100.0	88.0	122.4	206.7
(7) Index of unit value of imports of goods (1970 = 100)	95.4	106.0	110.9	133.0	208.5
(8) Index of constant value of imports of goods (1970 = 100) [(6)/(7) x 100]	81.3	94.3	79.4	92.0	99.1
(9) International reserves (millions of dollars, at close of period)	175.0	181.0	198.0	232.0	170.0[a]

SOURCE: ECLA estimates, on the basis of official statistics. [a] Relates to October.

Table 146. Uruguay: percentage composition of exports of goods

	Average 1969-1970	*1971*	*1972*	*1973*	*1974*[a]
Wool	20.8	21.6	15.4	17.7	5.6
Meat and meat products	34.6	33.6	48.1	39.2	25.4
Live animals	1.1	1.4	0.9	0.4	–
Hides and bristles	11.1	10.4	10.7	8.0	2.3
Yarns and textiles	14.5	12.2	12.7	15.4	2.3
Unprocessed agricultural products	4.5	6.8	0.6	5.4	3.5
Processed agricultural products	6.5	4.7	5.2	3.2	19.8
Mineral products	1.8	1.5	0.6	1.0	5.1
Miscellaneous	5.0	7.8	5.8	9.7	36.0[b]
Total	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*

SOURCES: ECLA, on the basis of official statistics, and data supplied by the Organization of American States (OAS).
[a] Exports effected in January-August 1974.
[b] Relates to Chemical products (22.3 million dollars) and products of miscellaneous industries (80.6 million dollars).

approximately, in 1972 (see table 147). Price variations such as these in the case of a product like meat are of special significance in Uruguay, where meat consumption is of high relative importance in the structure of the diet. Furthermore, as regards supplies of protein, meat substitutes are relatively scarce and costly, and their price trends closely follow those of meat.

In 1973 the direct effects of imported inflation were felt more widely and intensively, since, on the one hand, the unit value of exports in terms of dollars increased by 45 per cent–that is, even more rapidly than in 1972–and, on the other hand, the index of import prices rose by 20 per cent, which meant that the rate recorded in the preceding years was approximately quadrupled.

Among the major export products, world prices of meat rose by 70 per cent, while those of wool doubled. In both cases, the higher prices were

Table 147. Uruguay: variations in consumer prices of selected goods[a]
(Annual rates)

	1971	*1972*	*1973*
Beef	75.5	128.9	108.4
Rice	2.5	107.9	123.9
Wheat flour	7.1	139.3	135.0
Edible oil	18.0	64.5	151.9

SOURCE: Dirección General de Estadística y Censos, *Indice de los Precios del Consumo.*
[a] December to December.

Table 148. Uruguay: percentage composition of imports of goods, by major economic groups

	Average 1969-1970	*1971*	*1972*	*1973*	*1974*[a]
Consumer goods	8.0	8.8	6.5	7.1	6.5
Raw materials	51.0	51.3	59.2	62.5	51.5
Construction materials	2.0	2.0	1.3	2.1	2.0
Fuels	13.7	14.5	20.4	19.3	32.1
Capital goods	24.6	21.9	11.2	8.3	7.3
Miscellaneous	0.7	1.5	1.4	0.7	0.6
Total	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*

SOURCE: ECLA estimates, on the basis of official statistics.
[a] Imports effected in January-August 1974.

reflected in domestic price trends, although these were to some extent offset by the fact that withholdings, (*detracciones*), in terms of national currency, were periodically and significantly raised during the year. This subject will be reverted to at a later stage.

The rise in the unit value of imports was essentially due to substantial increases–generally ranging from 30 to 50 per cent–in the prices of several agricultural commodities of which Uruguay is an importer: for example, wheat, maize, sugar, coffee and tea. The domestic prices of these goods tended to reflect the upward movement of world prices, as well as the devaluations affecting the exchange rate.

Probably one of the most representative cases in point was that of wheat; domestic prices of wheat flour shot up in 1972 and 1973 at an annual rate of about 140 per cent.

In 1974, the direct effects of imported inflation were intensified, but in contrast to what had happened in the previous years, the pressure deriving from world prices of exports diminished, and that originating in the external prices of imports increased.

The unit value of exports of goods rose by only 7 per cent, owing to an interruption of the upward trend of world prices of wool and meat. Moreover, difficulties in exporting meat, in particular to the European Economic Community (EEC) countries, left large disposable surpluses which had to be sold to Brazil or marketed at home.

In contrast, the average unit value of imports increased in 1974 by 57 per cent, which gives a first rough idea of the inflationary pressure introduced through this channel.

In the case of certain products, however, the pressure exerted on domestic prices far exceeded the average. The most obvious instances were afforded by petroleum and petroleum products, of which the country is not a producer, and which showed price increments of approximately 200 per cent or over; and by some agricultural and industrial raw materials whose international prices increased rapidly (see table 148).

Similarly, prices of manufactures and capital goods–especially those expressed in terms of dollars–were pushed up even further by the effects of world inflation on the international prices of these goods.

(b) *Indirect dissemination: some repercussions*

One of the indirect effects observable in 1973 resulted from the increase in international reserves. Thanks, in particular, to the favourable trend of exports, between the end of 1972 and the close of 1973 gross reserves climbed from 198 to 232 million dollars (see table 145).

Although the series compiled on the evolution of the means of payment give no separate indication of the monetary effect of the variation in net international reserves, it can be deduced from table 139 that in 1973, for the first time in many years, this variation acted as an expansionist factor. The money supply increased by 74.5 per cent, and quasi-money by 70 per cent, while the growth rate of total domestic credit was 51 per cent (see table 139).

The effect in question ceased in 1974, when a loss of reserves occurred; and the relative increase in domestic credit (86 per cent) was greater than the increment in the money supply (62 per cent).

Another indirect repercussion of some importance also made itself felt in 1973, when the Uruguayan exporters' capacity for spending increased rapidly and substantially, inasmuch as the value of their exports rose by 35 per cent in terms of dollars at current prices.

The expansionist effect of this trend was lessened, however, by the fact that the revenue obtained by the Government in 1973 from withholdings exceeded its 1972 level by the national

currency equivalent of about 20 million dollars.[214] Thus, the net value refunded to meat and wool exporters–less the amount withheld–increased from about 120 million dollars in 1972 to 140 million in 1973, while the gross value of the exports in question rose from about 150 million in the first of these years to 190 million in the second.

Although exports of hides were also subject to the system of withholdings, the data available were insufficient for the preparation of an estimate similar to that made for meat and wool.

4. *Additional aspects of anti-inflationary policy*

During the period 1972-1974, the formulation and implementation of stabilization measures was subordinated, as has already been pointed out, to certain basic lines of action laid down by over-all economic policy, which were pursued with gradually increasing vigour as time went by.

It should be borne in mind that before the effects of imported inflation began to make themselves felt, the strategy determined on had implied acceptance of a functional modicum of inflation, while at the same time, by virtue of the flexibility of the price mechanism, internal prices for domestic production were to be progressively equalized with the corresponding external prices.

Moreover, the decision taken with regard to imported inflation itself and its internal repercussions was that its "internalization" should be tolerated–with a few minor and temporary exceptions that may have occurred–both in relation to domestic prices of goods exported by Uruguay and in respect of internal prices of imported goods or domestically-produced goods using inputs from abroad.

Accordingly, the various types of economic policy that may be differentiated evolved along the general lines described.

Exchange policy operated on the basis of the existence of two markets, one commercial and the other financial.

In the former, which is the more important, since it comprises export and import operations, the system applied was one of periodic mini-devaluations of the national currency, which closely followed domestic price trends. Only in the early months of 1974, for reasons not clearly identified, was the rate of devaluation slower than that of internal inflation, but a radical change took place in this respect in the second half of the year.[215]

Uruguay also opted for the progressive liberalization of its import trade, to which end certain restrictions and bans on imports were eliminated. At the same time customs duties were gradually reduced, although in this respect the authorities acted with caution. In 1973 and 1974 the result of the application of these measures was a rapid increase in imports of goods.

The financial market–whose operations were subject to certain limitations and which mobilized relatively small quantities of resources–was broadened and liberalized in September 1974 and the value of foreign currency was left to the free play of supply and demand. From the time of this reform onwards, the so-called "parallel" market diminished greatly in size.

Fiscal policy was aimed at reducing the inflationary repercussions of the Government's financial operations. With this end in view, various measures were adopted during the period considered, with the aim of restricting the growth rate of fiscal expenditure, strengthening mechanisms for tapping the sources of current income and financing the sector's deficit by means of non-inflationary expedients.

Nevertheless, the evolution of government finances continued to show considerable fluctuations, according to whether the Government had to grant larger or smaller compensatory wage adjustments to its employees, and, in view of the weakness of the system of taxation on internal activity, according to the variations in the returns from withholdings and import taxes in line with export and import trends. In any case, throughout the period under study the fiscal sector generated deficits on current account.

In 1974, when the fiscal situation deteriorated notably for the reasons set forth above, investment acted as a factor of adjustment, since it was frozen, in nominal values, at the 1973 level.

At all events, when the total fiscal deficit increased rapidly–as happened in 1974–the only feasible form of financing it in significant amounts continued to be an issue of currency by the monetary authorities. There were two reasons for this: on the one hand, external credit played little part in the structure of capital inflows,[216] and, on

[214] It is roughly estimated that the return from withholdings (*detracciones*) in respect of exports of meat and wool amounted to the national currency equivalent of 30 million dollars in 1972 and 50 million in 1973.

[215] Between December 1973 and June 1974 the national currency value of the dollar increased by 20 per cent, whereas between June and December 1974, the comparable increase amounted to 41 per cent.

[216] This state of affairs was due, *inter alia*, to the low relative level of public investment in Uruguay (in 1974 it amounted to about 33 million pesos, i.e., the equivalent of less than 30 million dollars).

the other hand, it was impracticable for the sale of official securities to mount spectacularly from one year to the next.[217] Nevertheless, measures were adopted, particularly in 1974, with the aim of ensuring positive returns on such documents in real terms.

Significant progress was made in the financing of autonomous institutions. Through a realistic policy in relation to public rates, which were periodically adjusted, the negative rate of savings usually shown by such institutions was successfully eliminated, and they even succeeded in generating an increasing surplus on current account, which, in the last two years, seems to have financed approximately half their investment.[218]

Monetary policy operated on the basis of flexible annual programmes, which were revised several times in the course of each year, and were designed to make the increases in the money supply compatible with the estimated—and also the actual—variations in prices and in economic activity. Generally speaking, monetary policy played a passive role, in the sense that no attempt was made to resort to a major restriction of the rate of expansion of the means of payment as a decisive weapon in the battle against inflation.

The policy in question might rather be said to have been concerned mainly with ensuring that the increases in the money supply which were considered acceptable should be compatible with the fluctuations of demand for greater credit resources on the part of the public and private sectors.

Lastly, with regard to *prices and wages policy* some indication has already been given of the principal lines followed, especially in respect of prices.

In relation to instruments influencing prices, it should be recalled that in the course of the three-year period the previously established mechanisms for the centralization and control of commodity and factor prices were gradually eliminated, giving place to a régime of increasing freedom in pricing and the assignment of greater importance to internal and external competition in the operation of the economic system.

The wage policy applied was based on the granting of adjustments every six months, the aim of which was to ensure that during each half-year real wages should be maintained at much the same level as in the immediately preceding period.

Subsequently, towards the end of 1974, this formula was replaced by a non-periodic system of wage adjustments designed to relate average real wages to their 1968 levels for the various sectors.

In any case, the result of these wage policy variants depended, once the nominal adjustments had been granted, upon whether the rate of inflation increased or decreased during the period over which the new wage was in force.

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[217] To give some idea of the position, it should be noted that in 1974, sales of Treasury bonds amounted to 20,000 million pesos, while the monetary authorities' issue of currency reached 100,000 million (see table 138).

[218] See Inter-American Committee on the Alliance for Progress (CIAP), *El Esfuerzo interno y las necesidades de financiamiento externo para el desarrollo del Uruguay*, CIAP/584, 1973, vol. I; and International Bank for Reconstruction and Development (IBRD), *Economic memorandum of Uruguay*, August 1974.

Part Two

THE LATIN AMERICAN ECONOMY IN 1974

Chapter I

GENERAL TRENDS

1. AN OVER-ALL APPRAISAL

For Latin America, 1974 had some very special features. The second half of the year, in particular, marked an interruption in the favourable trends which had been prevailing in the region's external sector for several years past and had actually further improved in 1973. Except in the case of the oil-exporting countries, this interruption is shown by the drop in the purchasing power of the region's exports, after this power had gone up considerably in the two previous years. At all events, however, even for the countries which are not oil exporters external trade continued to be very dynamic compared with past levels such as, for example, those of the 1960s.

The second element to be appraised is the situation created by the weakening in the growth rate of the central economies, the average growth rate of which is estimated to have been less than 1 per cent. In the case of the United States, whose economic evolution is of special importance for most of the countries of the region, the growth rate was even less. This fact, as may well be realized, directly affected the prices and volumes of Latin America's external transactions, giving rise to the results described in the preceding paragraph.

Finally, imported inflation was another negative element which affected almost all the countries of the region to different extents and in different ways, either as a decisive factor or as an accessory impulse.

In spite of these inauspicious circumstances, however, Latin America managed to maintain quite a satisfactory growth rate which was almost equal to that of 1973, when these circumstances had been much less unfavourable. Furthermore, as we shall see later, the structure of the over-all average was more balanced than the year before. In fact, leaving aside Brazil, the rest of the countries improved on the growth rate of the product achieved in 1973.

Does this mean that the region, or at least most of the countries in it, has reached the stage of self-sustaining development which will permit it to free itself from contingencies as important as those referred to above? To use an expression which was very much in vogue a few years ago, is the time now past when every sneeze in the northern hemisphere gave the countries south of the Rio Grande pneumonia?

One would have to be a great optimist to nourish the hopes implicit in these questions. It seems more rational and cautious to presume that underlying the differences in question is a problem of sequences or moments in a given conjuncture or trend. In other words, if the Latin American growth rate was relatively satisfactory in 1974, then this was due mainly to the fact that the negative elements in question had not yet "matured" or made themselves felt with their full force. An indication of this is that the difficulties seemed to be more acute in many countries towards the end of the year, thus in some respects giving a foretaste of what 1975 could be like.

Even if this more pessimistic evaluation of the situation is adopted, however, this does not mean that we should underestimate what has taken place, which is also of substantial importance. In practice, most of the economies have shown a degree of flexibility which they certainly did not have in the past. Moreover–and perhaps this is the most important feature–the economic policies in various countries have shown flexibility and imagination in using and combining a variety of instruments, and this undoubtedly played a part in achieving these results against a background of deteriorating conditions.

It seems evident that the external conditions as regards export prices and markets for the region will be more difficult in 1975, and it will be no

easy matter to overcome the inflationary pressures which were unleashed or intensified recently. On the other hand, however, the forecasts about the behaviour of the central economies have improved slightly.

Latin American economic policy must be worked out within this contradictory panorama, which, of course, includes many other important variables, and the experience of 1974 thus gives ground for thinking that the region's capacity for coping with events has improved.

2. ECONOMIC GROWTH IN 1974

In 1974, for the third year running, there was marked economic growth which was reflected in an increase of the order of 7 per cent per year in the region's gross domestic product. This rate is slightly below that noted in 1973, however, and reflects to a considerable extent the loss of dynamism in the economic evolution of Brazil, and particularly in the manufacturing sector of that country. If we exclude the considerable influence of Brazil in the regional total, then we see that the product grew in 1974 by 6.1 per cent, which is an improvement on the 5.6 per cent recorded the year before (see table 149 and figure I).

Other countries of major relative economic importance which suffered a decline in their growth rate in 1974 were Mexico, Colombia and, to a lesser extent, Venezuela. In contrast, the growth rate of Argentina grew sharply from 3.8 per cent in 1973 to 7.2 per cent in 1974, there was a marked recovery in Chile after the drop recorded in 1973, and in Peru too the product grew faster than the year before.

In the other countries, the behaviour of the product in 1974 was very uneven. If the evolution of the countries in the last two years is compared, it may be noted that in 1973, of the 19 Latin American countries for which information is available, seven grew at the same rate or faster than the regional average, three others grew by between 6 and 7.2 per cent, and in the nine remaining countries the product grew by an average of 3.1 per cent.

Table 149. Latin America: evolution of gross domestic product[a]

Country	*Total*			Per capita				
	1970-1972	*1973*	*1974[b]*	*1970*	*1974*	*1970-1972*	*1973*	*1974[b]*
	Annual growth rates			*Dollars[c]*		*Annual growth rates*		
Argentina	3.5	3.8	7.2	1,213	1,370	2.3	2.4	5.7
Bolivia	4.5	5.4	5.7	260	287	1.8	2.7	3.0
Brazil	10.8	11.4	9.6	445	596	7.7	8.3	6.5
Colombia	6.4	7.5	6.1	509	578	3.2	4.2	2.8
Costa Rica	6.6	6.2	4.1	656	739	3.7	3.3	1.2
Chile	4.8	−4.0	5.0	779	798	2.8	−5.7	3.2
Ecuador	6.2	9.3	9.2	372	440	2.9	5.8	5.7
El Salvador	5.2	5.1	6.0	397	432	1.9	1.8	2.7
Guatemala	6.4	7.6	4.7	415	471	3.1	4.3	1.7
Haiti	5.0	4.5	3.0	99	106	2.5	1.9	0.4
Honduras	3.8	5.0	−0.5	289	283	0.3	1.3	−4.0
Mexico	5.3	7.6	5.9	893	991	2.0	4.1	2.4
Nicaragua	4.9	2.2	7.7	432	459	1.5	−1.2	4.3
Panama	7.3	6.5	4.0	868	991	4.6	3.6	1.2
Paraguay	4.9	7.2	8.0	362	403	2.1	4.3	5.0
Peru	6.3	6.0	6.6	526	598	3.3	3.0	3.5
Dominican Republic	11.5	11.2	8.9	347	459	7.9	7.6	5.3
Uruguay	−1.2	1.0	1.9	927	889	−2.4	−0.1	0.7
Venezuela	3.3	5.9	5.1	1,176	1,244	0.3	2.9	2.1
Total 19 countries	*6.4*	*7.2*	*7.0*	*640*	*743*	*3.4*	*4.2*	*4.0*
Total (excluding Brazil)	*4.8*	*5.6*	*6.1*	*748*	*825*	*2.0*	*2.7*	*3.2*

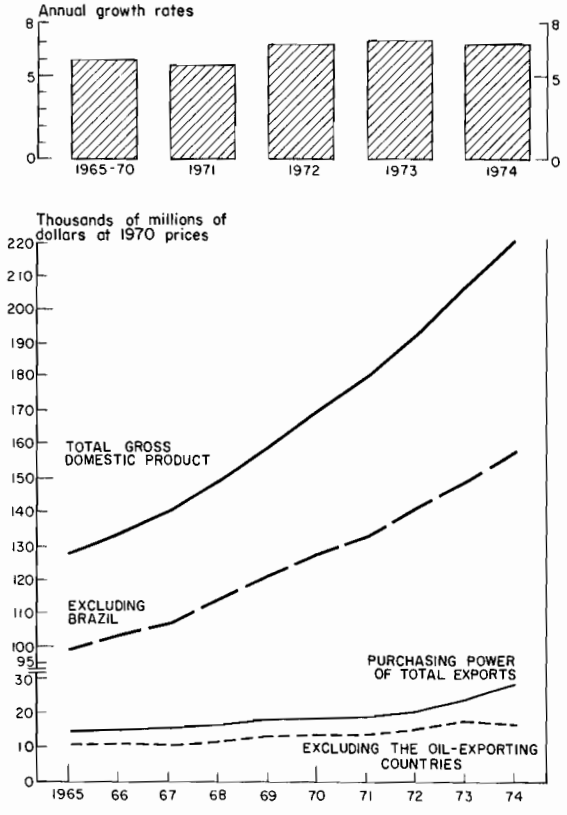
SOURCE: ECLA, on the basis of official statistics.

[a] At factor cost.

[b] Preliminary figures.

[c] The amounts in national currency at 1970 prices were converted into U.S. dollars on the basis of exchange parities calculated by ECLA for that year by extrapolating the purchasing power equivalents originally calculated for 1962 through the use of price indexes.

Figure I. Latin America: growth of the gross domestic product and the purchasing power of exports
Natural scale



In 1974, in contrast, only six countries showed a growth rate higher than the average of 7 per cent, while three others recorded a rate of 6-7 per cent. In the other ten countries, however, the average growth rate was 5.4 per cent, which was more than in 1973. It may be recalled that the IDS calls for a growth rate of 6 per cent per year (3.5 per cent *per capita*) in the gross domestic product of the developing countries during the present decade.

The developments described above represent increases in the average *per capita* product of 4.2 per cent in 1973 and 4 per cent in 1974, but only six countries exceeded this average in 1974, and another twelve failed to reach 3.5 per cent. For the 10 countries which showed an average growth rate of 5.4 per cent in the total product in 1974, the corresponding *per capita* increase was only 1.6 per cent, but this was still much more than the average of 0.5 per cent achieved by the nine countries of least relative growth in 1973.

The economic evolution recorded in 1974 was influenced by various factors. From the point of view of the sectoral production figures, the outstanding feature was the speeding-up of agricultural activity after its slow growth in earlier years, and the significant loss of dynamism of the manufacturing sector. Construction and basic services showed an even more pronounced rising tendency, but this was less marked in the case of other services (see table 150).

After having grown at an annual rate of 3 per cent since the beginning of the decade, agricultural production suddenly grew by 5.8 per cent in 1974. Most of the countries of the region had some part in this, but the most important contributions came from Brazil and Argentina, where the growth rates of 3.5 and 5.5 per cent respectively recorded in 1973 rose to over 8 per cent in 1974, and from Chile, whose agricultural growth rate of 17.3 per cent in 1974 marked a full recovery from the 15 per cent drop in production in the previous year.

Generally speaking, 1974 was a good year for agriculture, both because of the favourable weather conditions which predominated in the region and because of the high world prices for certain export products, which encouraged their cultivation. The higher prices which had to be paid for imported inputs, tools and machinery were an adverse factor, however.

The drop in the growth rate of manufacturing from 9.5 per cent in 1973 to 6.5 per cent in 1974 is largely attributable to the sudden drop in the figures for Brazil. That country's manufacturing product, which increased at the rate of 12.7 per cent per year in 1970-1972 and rose by 15.8 per cent in 1973, grew by only 7.1 per cent in 1974, the decline being noted in the most diverse lines of manufactures.

Latin American imports showed an extraordinary increase in 1974, due partly to the large international reserves which some countries had been accumulating since 1973, and despite the considerable rise in the prices of imports, the volume of goods and services imported by Latin America as a whole increased by 19.1 per cent.

This increase in the volume of imports, plus the expansion of domestic production and the stagnation of exports in volume terms, meant that during the year the real domestic availability of goods and services increased by around 9 per cent, which is more than in previous years and was reflected on the domestic demand side in an increase of 13.4 per cent in gross capital formation, the coefficient of which with respect to the gross domestic product has risen considerably since the beginning of the decade (from 20 per cent in 1970 to approximately 23.5 per cent in 1974). Consumption expenditure also increased more than in previous years, particularly in the case of private consumption (see table 151).

Table 150. Latin America: evolution of
(Annual

Country	*Agriculture*			*Mining and quarrying*			*Manufacturing*		
	1970-1972	*1973*	*1974*[d]	*1970-1972*	*1973*	*1974*[d]	*1970-1972*	*1973*	*1974*[d]
Argentina	−2.0	5.5	8.1	−0.7	−20.2	2.1	6.3	6.8	6.8
Bolivia	3.4	2.1	3.5	−0.1	3.0	–	4.1	6.5	6.0
Brazil	7.9	3.5	8.5	6.6	10.7	...	12.7	15.8	7.1
Colombia	4.1	5.3	5.5	−5.3	4.8	−5.0	8.9	10.9	7.0
Costa Rica	5.6	7.2	−2.0	e	e	e	9.2	10.0	9.0
Cuba									
Chile	−0.5	−15.2	17.3	−0.6	2.1	19.5	8.5	−5.3	0.6
Ecuador	1.5	−1.4	2.5	55.0	170.3	4.0	7.9	11.1	14.0
El Salvador	2.6	4.9	5.4	4.7	2.2	5.0	5.8	5.9	6.2
Guatemala	7.4	9.1	4.3	−6.4	14.3	35.3	6.3	8.1	4.9
Haiti	3.4	0.6	1.2	0.4	30.0	9.4	7.3	10.8	3.9
Honduras	4.6	4.5	−7.4	3.2	26.8	15.8	6.6	8.1	5.5
Mexico	1.2	0.6	2.4	4.3	3.0	13.8	5.8	8.8	5.6
Nicaragua	6.1	1.7	10.0	−0.3	12.6	9.6	5.7	1.8	8.3
Panama	3.3	3.4	3.4	8.4	37.9	−2.5	7.2	4.2	2.1
Paraguay	4.6	9.7	9.7	53.0	2.4	20.0	4.8	5.2	5.6
Peru	−2.4	0.7	4.4	0.6	1.5	2.5	7.9	7.5	8.0
Dominican Republic	4.5	6.6	3.2	80.0	47.4	10.1	30.0	13.0	11.2
Uruguay	−2.3	3.1	0.8	e	e	e	−1.1	−0.4	3.6
Venezuela	0.5	5.8	6.7	−6.3	6.7	−8.2	8.0	7.7	9.8
Total 19 countries	*3.0*	*3.1*	*5.8*	*−1.0*	*5.4*	*4.0*	*8.2*	*9.5*	*6.5*
Total (excluding Brazil)	*1.4*	*3.0*	*4.9*	*−1.7*	*5.1*	*3.8*	*6.5*	*6.9*	*6.2*

SOURCE: ECLA, on the basis of official statistics.
[a] Includes agriculture, mining and quarrying, manufacturing and construction.
[b] Includes electricity gas and water, and transport and communications.

Table 151. Latin America: total supply and demand
(Annual growth rates)

	1970-1972	*1973*	*1974*[a]
Total supply	*6.4*	*7.5*	*8.2*
Imports	6.6	10.0	19.1
Gross domestic product	6.4	7.2	7.0
Total demand	*6.4*	*7.5*	*8.2*
Exports	3.3	7.4	0.1
Domestic demand	*6.7*	*7.5*	*8.9*
Gross domestic investment	8.7	12.0	13.4
Total consumption	6.2	6.3	7.6
General government	6.7	7.5	7.3
Private	6.1	6.1	7.6

SOURCE: ECLA, on the basis of official statistics.
[a] Preliminary figures.

3. THE PERSISTENCE AND EXTENSIVENESS OF THE INFLATIONARY PROCESS

Various sections of this *Survey* contain descriptions and analyses of the recent inflationary process, identifications of the domestic conjunctural and structural inflationary factors, and considerations on the incidence of imported inflation.

Although the phenomenon is analysed in some detail for only six countries, the Latin American inflationary picture in 1974 and the factors which explain it suggest that the main conclusions of the above analyses could well have a good deal of validity for many of the countries of the region.

Imported inflation, of course, has become generalized, and although its repercussions have manifested themselves to different degrees and in different ways in the individual countries, its effect on domestic price systems and levels has been decisive.

Judging from the variations in price indexes the Latin American inflationary picture in 1974 confirms the tendencies shown the year before. When it is noted that in 1973 the great majority of the countries showed price rises greater than those of previous periods, and that most of them showed even higher rates of increase in 1974, there can be no doubt about the greater amplitude and virulence of the phenomenon (see table 152).

It may be noted that in 12 of the 22 countries considered, the price rises in 1974 were appreci-

main sectors of economic activity
growth rates)

Construction			*Goods*[a]			*Basic services*[b]			*Other services*[c]		
1970-1972	*1973*	*1974*[d]	*1970-1972*	*1973*	*1974*[d]	*1970-1972*	*1973*	*1974*[d]	*1970-1972*	*1973*	*1974*[d]
2.3	−9.8	12.5	3.5	4.0	7.5	3.1	5.3	6.6	4.2	3.2	6.8
1.9	7.2	14.0	2.4	4.0	4.2	4.9	5.9	6.0	6.4	6.5	7.1
10.6	12.5	11.2	11.0	12.0	8.0	9.1	13.6	15.2	11.0	...	10.1
4.4	11.5	12.5	5.4	7.8	6.4	7.8	9.4	...	7.9	7.4	...
7.2	3.5	13.0	7.0	7.8	3.5	8.8	7.8	...	6.0	4.5	...
−0.7	−12.0	13.5	4.4	−5.6	7.8	5.5	...	...	4.9	...	...
8.0	11.7	8.3	5.9	13.5	7.1	6.9	7.9	5.0	6.8	3.1	13.4
21.3	−11.0	15.9	4.9	4.0	6.4	4.8	4.8	5.9	5.7	6.1	5.7
9.8	18.0	4.7	7.2	9.3	4.6	9.6	11.4	6.5	4.9	6.1	4.9
15.8	15.4	17.2	4.4	3.6	2.7	11.2	3.5	5.3	5.5	6.4	3.2
−8.5	5.7	3.1	4.0	6.4	−2.1	4.4	5.5	2.2	3.3	2.6	1.5
7.0	14.8	6.3	4.6	7.0	5.7	8.5	11.9	...	5.8	7.6	...
6.2	6.2	32.0	5.9	2.2	10.9	4.8	1.8	10.6	3.6	1.8	4.9
15.3	6.3	3.9	6.6	4.4	3.0	12.4	11.6	13.2	7.5	6.5	2.8
8.2	16.3	20.0	5.0	8.6	8.2	10.1	13.6	15.8	4.3	4.6	5.6
11.0	8.2	17.0	3.4	4.3	7.1	8.9	7.2	...	7.1	6.5	...
28.0	13.9	12.6	13.4	13.4	8.0	10.2	8.8	7.1	9.4	8.8	9.8
5.7	−2.0	9.1	−0.8	0.5	3.3	−0.8	1.4	2.5	−1.6	0.9	0.6
21.0	10.8	2.8	1.1	7.4	0.7	8.5	6.0	8.8	5.5	5.4	8.4
8.1	*8.9*	*9.8*	*5.8*	*7.2*	*6.3*	*6.9*	*8.6*	*9.3*	*6.9*	*8.1*	*7.2*
7.1	*6.2*	*9.1*	*4.1*	*5.5*	*5.6*	*6.2*	*6.8*	*7.1*	*5.5*	*5.7*	*6.0*

[c] Includes commerce and finance, ownership of dwellings, public administration, and defence and other services.
[d] Preliminary figures.
[e] Mining is included in manufacturing.

ably greater than those recorded in 1973; of the other countries, six showed price increases of the same order as the year before, and in only four countries was there a significant reduction in the rate of increase.

Looking at the incidence of imported inflation and price rises in 1974, it is possible to distinguish three categories of countries in the region which display quite marked homogeneity from the point of view of inflation.

The first category is made up of countries where exogenous influences were predominant in the inflationary process and there were fairly moderate price rises ranging between 10 and 22 per cent. Although 14 of the 22 countries come under this group, these countries only represent 40 per cent of the population and 44 per cent of the product of the region.

In the second category, which contains the countries which showed price increases of between 30 and 40 per cent in 1974, the influence of internal factors and so-called imported inflation was more or less equal. In the inflationary processes of the countries of this group (Argentina, Bolivia, Barbados, Brazil, Colombia and Costa Rica), inflation from abroad found fertile ground for spreading and increasing side by side with domestic inflationary factors which were already in an advanced stage of activity or were beginning to act in the financial sphere. The cases of Bolivia and Costa Rica are particularly noteworthy in this group of countries, since throughout the 1960s and up to 1971 these two countries had maintained virtual price stability.

Finally, in the third category of countries the conjunctural and structural internal factors predominate over the external factors as far as the generation and continuation of their inflationary processes are concerned. In other words, in these countries imported inflation only came on top of domestic situations which were already marked by great instability as far as prices and financial flows were concerned. The price increases of 107 per cent in Uruguay and 376 per cent in Chile reflect forms of inflation which are at once chronic and acute.

The immediate future, as far as it can be forecast on the basis of the events of 1974, seems to hold in store even more difficult situations. Although there are indications that the inflation-

Table 152. Latin America: variation of consumer price indexes
(*Percentage variation*)

	December–December			*1974 compared with December 1973*			
	1971	*1972*	*1973*	*March*	*June*	*September*	*December*
Predomination of imported inflation							
Paraguay	6.3	9.5	14.2	22.3	20.0	17.7	21.9
Ecuador	6.8	6.9	20.5	8.0	12.3	17.7	21.2
Mexico	−0.8	5.2	20.2	5.0	8.0	13.5	21.1
Jamaica	5.2	9.3	29.6	5.4	9.8	17.7	20.8
El Salvador	−0.6	5.2	7.9	5.0	9.4	18.8	20.3[a]
Haiti	13.3	7.3	19.7	9.2	11.7	15.2	19.3[b]
Peru	7.7	4.3	13.7	5.7	12.5	15.2	19.1
Trinidad and Tobago	5.0	8.0	24.4	2.8	9.3	14.1	18.6
Panama	1.0	6.8	9.6	6.4	11.2	14.0	16.7
Guatemala	3.0	1.1	17.5	1.9	8.9	11.1	15.9
Honduras	1.5	6.8	5.0	6.2	12.2	12.7	13.0
Venezuela	3.0	3.5	5.7	0.6	1.7	8.9	12.2
Guyana	1.4	7.1	15.2	2.5	6.7	8.7	11.6
Dominican Republic	10.6	8.0	17.3	1.3	2.2	5.6	10.5
Combination of imported inflation and domestic factors							
Argentina	39.1	64.2	43.8	−3.1	6.7	14.9	40.1
Bolivia	3.3	23.6	34.9	32.6	37.8	35.7	38.8
Barbados	10.1	10.4	26.0	12.0	24.2	30.3	36.6
Brazil	18.1	14.0	13.5	11.1	20.8	27.5	34.1
Colombia[c]	14.1	16.4	21.1	12.7	17.3	20.1	31.5
Costa Rica[d]	−1.9	6.2	15.4	8.9	21.1	20.6	30.8[a]
Predomination of domestic inflationary factor							
Chile	22.1	163.4	508.1	62.2	145.6	242.6	375.9
Uruguay	35.6	94.8	77.5	23.4	34.9	62.1	107.2

SOURCE: International Monetary Fund (IMF), *International Financial Statistics*, vol. XXVII, Nos. 8 and 9, vol. XXVIII, No. 4; United Nations, *Monthly Bulletin of Statistics*, vol. XXVI, No. 5, vol. XXVIII, No. 11, vol. XXIX, No. 3.

[a] Variation October 1973–October 1974.
[b] Variation November 1973–November 1974.
[c] Consumer price index (manual workers) for Bogotá.
[d] Wholesale price index for San José.

ary pressures from the exterior may be reduced, there can be no doubt that the domestic inflationary processes attributable to this cause have now acquired a life of their own and—what is worse—are not likely to be accompanied this time by the positive repercussions which international inflation had on the balance of payments of some of the countries of the region. In other words, only the most pernicious effects of imported inflation will remain.

Even if there are moderate price rises, the above events and forecasts are elements likely to cause serious disturbances in the development of social and economic activity. Their effects on the processes of accumulation of wealth, income distribution and distortion of consumption patterns not only make it more difficult to achieve reasonable objectives in this field but may even, in some cases, lead to regrettable loss of ground.

4. THE EXTERNAL SECTOR

(a) *Latin American trade*

The boom in the prices of Latin America's commodity exports which was a main feature of economic development in 1973 continued in 1974, albeit at a lower level, except in the case of oil prices.

These price increases were maintained in general up to the middle of the year. From then on the prices of some tropical products such as coffee, cocoa and cotton and of some temperate-zone products such as meat and wool began to weaken, but the prices of sugar, vegetable oils and soya beans remained firm (see table 153 and figure II).

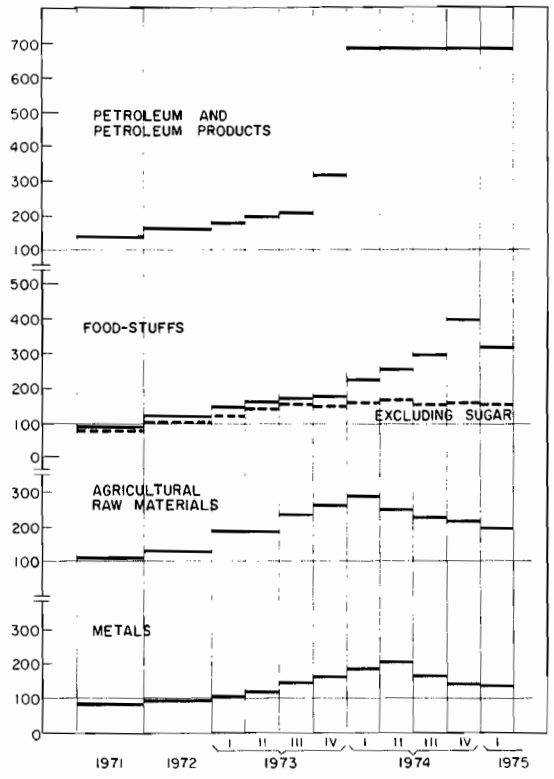
These price trends were closely linked with the results of world agricultural production in 1974, since output overtook demand in some cases,

Table 153. Latin America: prices of major exports[a]
Annual and quarterly averages
(Index 1970 = 100)

	1971	1972	1973				1974				1975
			I	II	III	IV	I	II	III	IV	I
Food and beverages	*99.6*	*120.6*	*145.3*	*160.8*	*168.4*	*172.1*	*223.9*	*255.4*	*294.1*[b]	*394.3*	*311.5*[b]
Tropical zone	*96.7*	*121.9*	*146.4*	*156.8*	*158.2*	*163.5*	*226.5*	*266.4*	*315.0*	*442.6*	*340.7*
Sugar (free market)	121.0	196.5	242.3	253.2	247.9	280.6	513.0	611.4	807.1	256.9	873.4
Sugar (exports to the United States)	105.6	112.4	115.6	123.5	132.0	138.7	197.7	283.8	390.8	589.7	431.8
Bananas	96.8	100.6	111.5	129.4	105.8	95.5	87.2	99.4	94.9[b]	94.2[b]	125.0[b]
Cocoa	79.5	96.6	121.4	187.3	242.9	207.8	219.3	315.5	287.0	276.1	242.5
Coffee (Manizales)	87.4	100.5	128.0	130.0	130.7	126.6	138.1	144.9	132.8	136.2	133.3
Coffee (Santos No. 4)	82.1	93.4	111.4	120.2	128.4	130.4	131.9	133.9	115.4	117.4	131.0
Temperate zone	*109.6*	*116.1*	*141.6*	*174.7*	*203.5*	*201.7*	*214.9*	*217.4*	*221.9*	*227.2*[b]	*209.7*[b]
Beef	120.3	134.2	140.1	190.4	183.6	178.2	166.3	211.0	192.6	184.8[b]	210.0[b]
Maize	94.8	89.0	128.6	149.4	198.8	197.0	218.7	205.5	229.1	240.7	182.4
Wheat	112.8	127.5	185.9	189.9	292.6	339.6	386.6	276.5	311.4	347.0	288.6
Agricultural raw materials	*106.2*	*123.0*	*182.2*	*182.0*	*240.9*	*267.3*	*281.8*	*250.8*	*222.3*	*214.2*	*192.7*[b]
Linseed oil	85.7	90.4	125.7	149.6	324.4	391.7	501.3	475.7	492.2	522.6	386.5
Cotton (Sao Paulo type 5)	121.4	126.3	139.1	161.7	203.8	275.6	287.1	278.7	228.6	192.9	184.2[b]
Cotton (Mexicano S.M.)	115.3	122.2	136.2	167.4	218.2	319.2	272.3	220.5	195.8	173.6	157.7
Fish meal	89.9	105.3	217.0	226.6	253.7	226.1	269.7	212.8	202.2	191.4[b]	154.3[b]
Wool (Buenos Aires 5/6's)	104.2	172.9	287.5	–	310.4	310.4	312.5	312.5	210.4[b]	210.4[b]	218.8[b]
Soya	107.4	118.1	167.4	157.4	227.4	208.7	227.9	203.2	–	264.3	247.0[b]
Metals	*89.7*	*92.0*	*101.4*	*118.7*	*141.6*	*161.2*	*185.4*[b]	*210.4*[b]	*161.0*[b]	*142.6*[b]	*137.4*[b]
Aluminium	102.0	95.6	90.9	95.9	101.0	102.3	103.9	123.4	132.8	138.0	147.0
Copper	76.7	75.6	91.2	115.1	142.4	154.6	166.6	196.8	122.1	96.6	83.1
Tin	97.0	104.3	112.0	121.6	138.3	161.1	205.9	253.9	244.3	203.1	207.9
Iron ore	104.0	109.7	112.6	116.4	118.6	118.6	179.6[b]	187.6[b]	187.6[b]	187.6[b]	187.6[b]
Lead	84.6	100.9	115.1	134.7	150.8	173.1	214.8	216.4	182.6	178.9	180.4
Zinc	106.4	130.1	147.4	197.0	313.3	504.5	505.9	564.4	352.6	276.9	274.4

SOURCE: ECLA, on the basis of official statistics.
[a] World market prices in dollars at current prices.
[b] Estimates.

Figure II. Latin America: prices of major exports
(Annual and quarterly averages)
(Index: 1970 = 100)
Natural scale



whereas in others production and the accumulated reserves continued to fall short of demand.

Furthermore, from the third quarter onwards there was a spectacular drop in the price of metals (copper, lead, zinc and tin) as a result of the economic recession in the industrialized countries.

The picture at the end of the year was one of an even greater generalized slump in commodity prices because of the prospects of bigger winter harvests and the worsening of the recession in the industrialized countries. The declining trend speeded up in the first quarter of 1975.

The situation with respect to international prices contrasted with that of domestic inflation in the industrialized countries, which was reflected in the sustained rise in the prices of what the Latin American countries had to pay for their imports of manufactures, added to which were the effects of the weakening of the dollar against the currencies of the EEC countries.

(i) *Exports*. The unit value of the region's exports increased 65 per cent in 1974, their total value rising from 26,250 million dollars in 1973 to some 44,400 million in 1974. This meant an increase of 69 per cent, thus exceeding the rate achieved in 1973 (44 per cent) and also exceeding for the second year running the rate of expansion of world trade (38 per cent in 1973 and 50 per cent in 1974). In contrast, there was only a small increase in the volume of Latin America's exports: 2.4 per cent compared with 6.7 per cent in 1973 (see table 154).

The results of external trade were very different during the year for the major oil-exporting countries (Venezuela, Ecuador, Bolivia and Trinidad and Tobago) compared with the rest.

Sales of the former increased 2.7 times in value owing to the fact that prices, particularly of petroleum, tripled; their volume, however, decreased by 10 per cent. Except in Trinidad and Tobago, the volume of exports declined in these countries, especially in Venezuela, as a result of a deliberate policy of reducing oil production, combined with a smaller demand on world markets. Another factor was the breakdown of the oil pipeline in Ecuador due to damage by storms.

The rest of the Latin American countries increased the value of their exports by 33 per cent, which was less than in 1973 (43.5 per cent). The unit value of exports, which had risen by 34.5 per cent in 1973, went up by 25.7 per cent in 1974. Moreover, the volume of exports increased by 5.9 per cent, which was slightly less than in 1973. There were small reductions in the volume of sales of Argentina, Brazil, Paraguay and the Dominican Republic.

The reduction in the physical volume of Argentina's exports was due to the drop in its sales of meat (closure of the EEC market) and wool (lower world demand), although these were largely compensated by increases in other exports such as cereals and manufactures. In Brazil, the bad harvests of the year before led to a considerable reduction in exports of certain products such as sugar, soya beans, cotton, coffee, etc., although this was almost completely made up for by bigger sales of other commodities such as iron ore, manganese, cocoa, maize, etc., and manufactures. The volume of Honduras' exports dropped as a result of the damage caused by hurricane Fifi, and Paraguay's sales of meat were lower because of difficulties in placing it abroad.

The performance of the countries of this group as regards the value of their exports also varied according to the particular impact of the boom in the prices of and the demand for their main export commodities in 1974.

Thus, the countries which mainly export sugar and bauxite (Dominican Republic, Jamaica, Guyana and Barbados) were particularly favoured by the rise in the world prices of those products and increased the value of their sales by 55 per cent. Mexico took advantage of its widely diversi-

Table 154. Latin America: annual variations in exports and imports of goods
(Percentage, on the basis of data in dollars at current prices)

Year	Exports			Imports			Purchasing power of exports
	Volume	Unit value	Value	Volume	Unit value	Value	
1960–1970	4.5	1.2	5.8	4.5	1.7	6.2	4.0
1970–1974	3.5	27.0	31.4	12.0	16.2	30.1	13.1
1971	–	3.7	3.7	6.9	4.3	11.5	−0.6
1972	4.8	12.7	18.2	8.2	5.7	14.4	11.8
1973	6.7	34.8	43.9	11.1	18.3	31.4	21.6
1974	2.4	65.2	69.1	22.5	39.8	71.2	20.9
I. *Oil-exporting countries* (Venezuela, Bolivia, Ecuador, Trinidad and Tobago)							
1960–1970	4.0	−1.3	2.7	3.2	2.2	5.5	0.5
1970–1974	−2.4	54.0	50.3	10.9	16.1	29.0	29.5
1971	−5.7	24.4	17.3	8.1	6.6	15.2	10.0
1972	−0.6	14.5	13.7	9.6	5.0	15.1	8.3
1973	6.6	35.2	45.0	2.4	16.7	19.5	24.2
1974	−9.8	194.5	165.5	24.8	38.8	73.3	91.3
II. *Non-oil exporting countries* (19 countries)							
1960–1970	4.7	2.3	7.1	4.9	1.5	6.4	5.5
1970–1974	5.2	16.7	22.8	12.3	16.2	30.5	5.7
1971	2.0	−2.6	−0.7	6.7	3.7	10.6	−4.2
1972	6.5	12.6	19.9	7.9	5.9	14.2	13.2
1973	6.6	34.5	43.5	13.3	18.7	34.4	20.9
1974	5.9	25.7	33.1	21.9	40.1	70.8	−5.0
(a) *Large countries* (Argentina, Brazil, Mexico)							
1960–1970	5.2	1.4	6.7	4.0	1.8	5.8	4.8
1970–1974	5.5	20.6	27.2	16.2	17.4	36.4	8.3
1971	1.4	1.8	3.2	8.7	4.0	13.0	−0.8
1972	7.2	18.1	26.6	12.9	6.3	20.0	19.1
1973	13.4	35.5	53.7	18.1	19.4	40.9	28.7
1974	0.5	29.8	30.4	25.9	43.9	81.2	−9.4
(b) *Medium-sized countries* (Colombia, Chile, Peru)							
1960–1970	3.1	4.4	7.6	4.9	1.2	6.1	6.3
1970–1974	5.1	10.1	15.8	7.8	13.7	22.7	1.8
1971	2.3	−13.1	−11.1	5.8	3.1	9.0	−13.8
1972	2.8	2.3	5.1	1.1	5.8	7.1	−0.7
1973	−2.5	41.1	37.6	4.8	18.9	24.5	15.7
1974	19.3	17.1	39.7	20.5	29.1	55.6	8.2
(c) *CACM countries* (Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua)							
1960–1970	8.4	1.4	9.9	8.8	0.6	9.4	9.2
1970–1974	5.5	11.6	17.8	8.2	14.3	23.7	3.1
1971	3.6	−1.9	1.7	2.6	3.8	6.5	−2.0
1972	12.2	7.8	21.0	−1.6	6.7	5.1	13.4
1973	1.8	20.9	23.1	13.3	18.3	34.1	4.2
1974	4.7	21.4	27.1	19.6	30.0	55.6	−2.2
(d) *Small countries mainly exporting sugar and bauxite* (Dominican Republic, Jamaica, Guyana, Barbados)							
1960–1970	2.4	3.1	5.6	7.4	1.6	9.2	3.9
1970–1974	6.2	14.7	22.0	4.9	13.0	18.5	8.0
1971	6.5	−0.1	6.5	3.0	3.3	6.4	3.1
1972	11.3	6.3	18.3	7.8	2.6	10.7	15.3
1973	−0.2	13.6	13.3	2.8	13.9	17.0	−0.5
1974	7.7	43.5	54.6	6.1	35.0	43.2	14.5

Table 154. (*continued*)

Year	Exports			Imports			Purchasing power of exports
	Volume	Unit value	Value	Volume	Unit value	Value	
(e) *Remaining small countries* (Haiti, Panama, Paraguay, Uruguay)							
1960-1970	5.4	1.1	6.6	4.3	1.1	5.5	5.4
1970-1974	-1.1	17.7	16.4	3.4	17.6	21.6	-1.0
1971	-4.4	2.3	-2.3	3.1	4.0	7.2	-6.1
1972	-1.3	16.6	15.2	-1.2	4.1	3.0	10.7
1973	-2.3	32.3	29.3	6.7	16.7	24.5	10.8
1974	3.5	21.8	26.0	5.2	51.3	59.2	-16.7

SOURCE: ECLA, on the basis of official statistics.

fied exports to secure an increase of 45 per cent, and Chile benefited from the speculative buying of copper which took place in the first half of the year and the improvement in the prices of iron ore and nitrates, finally securing an increase of 54 per cent in the value of its exports. Peru, with its diversified exports, increased its export sales by about 40 per cent due to the rises in the prices of sugar, cotton and metals (copper, zinc, silver, etc.) and the resumption of sales of fish meal. Nicaragua, too, expanded its export sales by almost 40 per cent, mainly as a result of the increased prices and bigger volume of cotton exports.

In the rest of the non-oil-exporting countries, however, including Argentina and Brazil, the average increase in the value of exports was generally below 33 per cent.

(ii) *The purchasing power of exports*. The evolution of this variable clearly reflects the effect of the tripling of oil prices in 1974. While in the four oil-exporting countries the purchasing power of exports increased by 91 per cent, in the rest of the Latin American countries it dropped 5 per cent (see figure II).

In 1973 there was little difference between the increases in the purchasing power of both these groups of countries. This situation was fortuitous, since in the early 1970s, as also in the 1960s, the evolution of this variable was very uneven in the individual countries, reflecting the fluctuations in each case of the prices of the main export commodities and the possibilities of placing them on the international markets (see table 153 and figure II).

Over the period 1970-1974, the purchasing power of exports of the region as a whole rose by 13 per cent annually (compared with 4 per cent annually in the 1960s) thanks to increases of 9.3 per cent in the terms of trade and 3.5 per cent in the volume exported.

In 1974 the evolution of the terms of trade affected most seriously those non-oil-exporting Latin American countries which were most dependent on imports of manufactures, food-stuffs and other agricultural raw materials and fuels, since the international prices of these products rose more, and of course much faster, than the prices of the goods exported by those countries.

In this respect it may be noted that in 1974 the unit prices of Uruguay's exports rose by scarcely 7.2 per cent (because of a drop in the prices of wool and only a small rise in those of meat), while the prices of imports rose by 56.8 per cent because of Uruguay's heavy dependence on imported raw materials, chemical products and construction materials (50 per cent), machinery and other manufactures (31 per cent) and fuel (19 per cent). As a result of these differences in price rises, the terms of trade deteriorated by 31.6 per cent and the purchasing power of Uruguay's exports dropped by 28 per cent. In Brazil the deterioration in the terms of trade was 18 per cent; in Chile 16 per cent; in Haiti 13 per cent, and in Honduras 11 per cent. In Argentina, Colombia, Peru, Costa Rica, El Salvador, Guatemala, Nicaragua and Panama the deterioration in the terms of trade was between 2 and 10 per cent.

In contrast, in Mexico, in the countries mainly exporting sugar and bauxite (Dominican Republic, Jamaica, Guyana, and Barbados) and in Paraguay the terms of trade improved.

Finally, of the countries whose terms of trade deteriorated only Chile, Peru, Colombia and Nicaragua were able to counter the effects of this by increasing the volume exported sufficiently to achieve greater purchasing power. In the other cases, the deterioration in the terms of trade signified a drop in the purchasing power of exports, even though the volume exported increased, albeit not sufficiently, in several of the countries.

(iii) *Imports*. In 1974 the considerable increase in the exports of Latin America as a whole was accompanied by an equally large increase in imports, so that while the value of exports rose by almost 70 per cent, that of imports rose by 71 per cent. While on the export side this considerable increase represented an increase of scarcely 2.4 per cent in the volume and an actual decline in the growth rate of the volume compared with the two previous years, on the import side the volume rose by 22.5 per cent, which was twice as much as in the year before.

Over the last three years the region's propensity to import was considerably stimulated by the increase in the purchasing power of exports. Thus, the volume of imports increased between 1970 and 1974 at an annual rate of 12 per cent, and although the volume of exports only increased by 3.5 per cent per year, their purchasing power grew by 13.1 per cent annually (see table 154).

Examining the situation by groups of countries allows us to observe that imports grew at a similar rate in both the major oil-exporting countries and the non-oil-exporting countries in 1974 (about 70 per cent). The increases in volume were also fairly similar: 23 and 25 per cent, respectively. This similarity in the trend of imports of both groups occurred despite the fact that in the non-oil-exporting countries the purchasing power of exports dropped by 5 per cent, with the result that their current account deficits increased and so also did their external indebtedness. In contrast, the oil-exporting countries not only increased their external purchasing power by 91 per cent, but improved their net external position.

Of the oil-exporting countries, the increase in the volume of imports in 1974 was slightly greater in Venezuela (30 per cent) than in Ecuador and Bolivia. In Trinidad and Tobago, because of smaller purchases of crude for refining, there was no change in the total imports.

In the non-oil-exporting countries the volume of imports grew more rapidly in the large and medium-sized countries than in the smaller ones, and the amount imported actually went down in Barbados, Haiti and Jamaica.

In the group of large countries (Argentina, Brazil and Mexico), the volume of imports increased by 26 per cent per year. In the period 1970-1974, however, only Brazil showed a steady rate of increase, the growth rate of Argentina's imports being the most irregular.

In 1974, the medium-sized countries increased the amount imported by 20.5 per cent, but Peru increased the volume of its imports by over 50 per cent, largely owing to a considerable reactivation of the external financing obtained by that country. In Colombia the increase was 14.2 per cent, and in Chile only 1.4 per cent.

Among the small countries, the Central American countries increased the growth rate of the volume of their imports for the second year running, the average rate of increase being 20 per cent and the rate in Nicaragua and Guatemala being even higher.

Of the countries mainly exporting sugar and bauxite, the Dominican Republic is the only one which expanded the volume of its imports in 1974 by a considerable amount (20 per cent) compared with the level of previous years (6 per cent).

Finally, in Panama, Paraguay and Uruguay, the volume of imports rose by around 6 per cent, which represented a considerable slowing-down for the last two countries compared with the growth rates of the previous year.

(b) *The Latin American balance of payments in 1974*

The significance for the oil-exporting countries of the high oil prices reached is clearly evident in the balance-of-payments movements. Even more striking is the magnitude of these results when contrasted with those of the rest of the countries in the region, several of which are important hydrocarbon importers.

For the four oil-exporting countries the external payments position changed radically in 1974 when their exports rose 166 per cent, or nearly 2.3 times the increase in their imports. Thus the trade surplus rose from 2,270 million dollars in 1973 to 10,574 million in 1974. Unlike what happened in the previous year, the four countries recorded trade surpluses in 1974 (see table 155).

Net payments of profits on direct foreign investment and interest payments on loans amounted to 4,736 million dollars (1,900 million in 1973) on account of the participation of foreign capital in the development of petroleum in these countries, except in the case of Bolivia. This represented 25 per cent of the total export earnings and absorbed 45 per cent of their trade surplus in 1974. In particular, this situation reflects the case of Venezuela, whose remittances under this head amounted to 4,270 million dollars in 1974.

To sum up, the oil-exporting countries of the region closed 1974 with a current account surplus of 5,750 million dollars, which was much higher than the level recorded in 1973 (285 million) notwithstanding the substantial increases in external payments in respect of profits and interest and imports.

The other Latin American countries presented a completely different picture in 1974. The much bigger increase in imports compared with the growth of exports (71 and 34 per cent, respec-

Table 155. Latin America: balance of payments for the
(Millions

	Exports FOB		*Imports FOB*		*Other non-factor net services*		*Trade balance*	
	1973	*1974*	*1973*	*1974*	*1973*	*1974*	*1973*	*1974*
Latin America (23 countries)	26,253	44,387	23,544	40,314	−1,460	−2,509	−1,249	1,564
Oil-exporting countries	*7,134*	*18,941*	*4,297*	*7,445*	*−568*	*−922*	*2,269*	*10,574*
Venezuela	5,573	14,920	2,840	4,529	−482	−782	2,251	9,609
Bolivia	273	560	253	390	−56	−83	−36	87
Ecuador	574	1,261	492	826	−97	−164	−15	271
Trinidad and Tobago	714	2,200	712	1,700	67	107	69	607
Non-oil exporting countries	*19,119*	*25,446*	*19,247*	*32,869*	*−892*	*−1,587*	*−1,020*	*−9,010*
Large countries	*11,931*	*15,558*	*11,921*	*21,603*	*−346*	*−674*	*−336*	*−6,719*
Argentina	3,266	4,010	1,978	3,160	−189	−242	1,099	608
Brazil	6,199	7,968	6,192	12,530	−1,010	−1,340	−1,003	−5,902
Mexico	2,466	3,580	3,751	5,913	853	908	−432	−1,425
Medium-sized countries	*3,801*	*5,310*	*3,414*	*5,310*	*−562*	*−823*	*−175*	*−823*
Colombia	1,334	1,700	1,023	1,420	−172	−216	139	64
Chile	1,325	2,037	1,362	1,891	−282	−375	−319	−229
Peru	1,142	1,573	1,029	1,999	−108	−232	5	−658
Small countries	*3,387*	*4,578*	*3,912*	*5,956*	*16*	*−90*	*−509*	*−1,468*
CACM countries	*1,692*	*2,150*	*1,695*	*2,637*	*−144*	*−261*	*−147*	*−748*
Costa Rica	341	430	399	607	−17	−32	−75	−209
El Salvador	364	460	340	510	−66	−84	−42	−134
Guatemala	440	585	388	608	−35	−63	17	−86
Honduras	259	275	244	372	−25	−34	−10	−131
Nicaragua	288	400	324	540	−1	−48	−37	−188
Small countries mainly exporting sugar and bauxite	*1,026*	*1,587*	*1,312*	*1,879*	*6*	*−34*	*−280*	*−326*
Dominican Republic	448	650	428	670	−72	−119	−52	−139
Jamaica	396	605	575	790	44	49	−135	−136
Guyana	135	262	158	232	−18	−25	−41	5
Barbados	47	70	151	187	52	61	−52	−56
Remaining small countries	*669*	*841*	*905*	*1,440*	*154*	*205*	*−82*	*−394*
Haiti	53	69	73	103	−11	−14	−31	−48
Panama	160	232	456	741	213	288	−83	−221
Paraguay	128	170	127	176	−12	−16	−11	−22
Uruguay	328	370	249	420	−36	−53	43	−103

SOURCE: ECLA, on the basis of official statistics.

tively) pushed up the trade deficit of these countries from 1,020 to 9,010 million dollars between 1973 and 1974. It is estimated that 42 per cent of this deficit—or some 3,760 million dollars—was due to the higher cost of imported fuels.

Profit and interest payments on foreign capital increased from 3,397 to 4,281 million dollars in the last two years, which represented just under 17 per cent of total export earnings. It is interesting to note that the amount of these payments made by those 19 countries was less than the total payments made under the same head by the four oil-exporting countries.

By the end of 1974 the current account deficit of the non-oil-exporting countries had almost reached the 13,000 million dollar mark, or 3.2 times the deficit recorded in 1973.

Such divergent results as those obtained by both groups of countries in their current transactions were logically reflected in their external financing needs. The current account surplus of 5,229 million dollars achieved by Venezuela helped to give a balance-of-payments surplus of

region and for the individual countries
of dollars)

Net payments of profits and interest		*Balance on current account*		*Movements of capital*		*Balance of payments before compensation*		*Percentage variation*			
								Exports		*Imports*	
1973	*1974*	*1973*	*1974*	*1973*	*1974*	*1973*	*1974*	*1973*	*1974*	*1973*	*1974*
–5,226	*–9,017*	*–3,765*	*–7,241*	*7,457*	*11,129*	*3,692*	*3,888*	*43.9*	*69.1*	*31.4*	*71.2*
–1,899	*–4,736*	*285*	*5,750*	*434*	*–1,058*	*719*	*4,692*	*45.0*	*165.5*	*19.5*	*73.3*
–1,690	–4,270	456	5,229	182	–1,120	638	4,109	46.7	167.7	21.2	59.5
–23	–21	–54	71	48	52	–6	123	34.5	105.1	29.1	54.2
–100	–192	–98	100	194	12	96	112	77.7	119.7	34.1	67.9
–86	–255	–19	350	10	–2	–9	348	20.0	208.1	3.0	138.8
–3,327	*–4,281*	*–4,050*	*–12,991*	*7,023*	*12,187*	*2,973*	*–804*	*43.5*	*33.1*	*34.4*	*70.8*
–2,357	*–3,102*	*–2,595*	*–9,709*	*5,593*	*8,788*	*2,998*	*–921*	*53.7*	*30.4*	*40.9*	*81.2*
–394	–352	716	258	4	–163	720	95	68.3	22.8	19.4	59.8
–812	–1,230	–1,792	–7,097	3,971	5,881	2,179	–1,216	57.3	28.5	47.7	102.4
–1,151	–1,520	–1,519	–2,870	1,618	3,070	99	200	31.1	45.2	43.6	57.6
–471	*–583*	*–629*	*–1,382*	*514*	*1,473*	*–115*	*91*	*37.6*	*39.7*	*24.5*	*55.5*
–207	–230	–56	–153	180	68	124	–85	39.1	27.4	25.8	38.8
–89	–154	–408	–379	155	269	–253	–110	54.4	53.7	25.1	38.8
–175	–199	–165	–850	179	1,136	14	286	20.7	37.7	22.5	94.3
–499	*–596*	*–826*	*–1,900*	*916*	*1,926*	*90*	*26*	*21.1*	*35.2*	*23.4*	*52.2*
–177	*–167*	*–225*	*–830*	*334*	*818*	*109*	*–12*	*23.1*	*27.1*	*34.1*	*55.6*
–41	–49	–112	–254	123	215	11	–39	22.2	26.1	18.4	52.1
–12	–14	–42	–136	36	146	–6	10	20.5	26.4	36.0	50.0
–48	–54	9	–112	70	102	79	–10	30.6	32.9	31.1	56.7
–33	–3	–39	–102	39	77	0	–25	24.5	6.2	37.9	52.5
–43	–47	–41	–226	66	278	25	52	15.7	38.9	58.0	66.7
–237	*–319*	*–447*	*–576*	*410*	*667*	*–37*	*91*	*13.2*	*54.7*	*16.9*	*43.2*
–78	–108	–101	–220	121	207	20	–13	29.1	45.1	26.6	56.5
–139	–186	–240	–287	209	350	–31	63	4.8	52.8	8.7	37.4
–13	–17	–53	–11	26	52	–27	41	–6.2	94.1	22.5	46.8
–7	–8	–53	–58	54	58	1	0	27.0	48.9	19.8	23.8
–86	*–111*	*–154*	*–494*	*172*	*441*	*18*	*–53*	*29.4*	*25.7*	*24.3*	*59.1*
–6	–7	–16	–33	10	23	–6	–10	23.3	30.2	19.7	41.1
–45	–52	–137	–285	137	266	0	–19	9.6	45.0	11.5	62.5
–10	–12	–19	–33	38	63	19	30	48.8	32.8	60.8	38.6
–25	–40	18	–143	–13	89	5	–54	35.5	12.8	39.1	68.7

4,109 million dollars after exports of capital amounting to the net sum of 1,120 million dollars. In 1973 there was still a net inflow of capital.

The remaining oil-exporting countries (Bolivia, Ecuador and Trinidad and Tobago) also showed a balance-of-payments surplus in 1974, which strengthened the position of their international reserves by 583 million dollars although there was scarcely any inflow of capital except in the case of Bolivia, where the inflow of funds was slightly greater than the year before.

The non-oil-exporting Latin American countries, on the other hand, were able to increase their imports to the extent to which they did because of the inflow of capital, which, as a result of the high degree of international financial liquidity, increased from 7,023 to 12,187 million dollars between 1973 and 1974, thus strengthening their import capacity, which was being undermined by the deterioration in the purchasing power of exports. Despite this considerable increase, however, the inflow of capital was not sufficient to cover the external current account deficit completely and the balance of payments of this group of countries closed with a deficit of some 800 million dollars, unlike the year before

when there had been a balance-of-payments surplus of 2,973 million dollars.

In 1974 the external financing facilities continued to be unequally distributed among the Latin American countries. The flow of capital to Brazil and Mexico (5,881 and 3,070 million dollars respectively, or 73 per cent of the total) continued to increase, thus helping the extraordinary expansion of those countries' imports. While the flow of capital to Mexico was sufficient to finance the deficit and contribute to the strengthening of reserves, however, in the case of Brazil the foreign funds were not sufficient, and there was a net deterioration in the country's external position of some 1,200 million dollars. In Argentina, for its part, there was an increase in net international reserves, although the trade surplus was much smaller than in 1973 and a net disinvestment was to be observed.

As regards Colombia and Chile, the net external position deteriorated in 1974 because of the limited inflow of capital. In Colombia, the increase in the current account deficit was accompanied by a considerable reduction in the inflow of capital which made it necessary to use international reserves. In Chile, the volume of exports increased, but as there was only a relatively small increase in the price of copper, it was only possible to achieve a slight reduction in the current account deficit, and although there was some reactivation of the inflow of capital (return of Chilean funds transferred abroad) this was not enough to avoid a net deterioration in the external situation, which was mainly reflected in an increase in the liabilities of the Central Bank (renegotiation of the external debt and the use of the Oil Facility to pay for the higher fuel costs).

In Peru there was a big inflow of capital in 1974 (1,136 million dollars) after the country's access to external financing had been restricted since 1968. This made it possible to double imports without any deterioration in international reserves. In 1974 Peru thus came in third place, after Brazil and Mexico, as a major beneficiary from the massive inflow of capital. Its external current account deficit came to 54 per cent of its exports, as against past figures of only 10 per cent.

During the last year, the inflow of capital into the Central American countries rose by a factor of 2.5. Imports were thus able to increase more than exports and the trade deficit widened. As a result, the external current account deficit came close to 60 per cent of exports in Costa Rica and Nicaragua, where the inflow of capital was greatest. Despite the increase in the inflow of capital, the amount was still insufficient in Costa Rica, Honduras and Guatemala, and the net external position of these countries deteriorated, especially in the case of the first two, whose liabilities increased because they used funds from the Oil Facility.

The external capital needs of the countries mainly exporting sugar and bauxite also increased in 1974. The extraordinary increase in the price of sugar and a readjustment in the price of bauxite checked the growth of the trade deficit in Jamaica and Barbados and even made possible a small trade surplus in Guyana. The Dominican Republic, however, increased its imports more than its exports, so that its current account and trade deficits increased, as did the capital requirements for financing them. Even so, the deterioration in its net reserves was slight, owing to the use of a contingency credit.

As far as the other countries are concerned, in Uruguay the increased inflow of foreign funds is worthy of note, but these were not sufficient to prevent a deterioration in the country's reserves and an increase in its liabilities because it had to make use of the Oil Facility. In Panama the external financing needs increased more in 1974 because of the increase in the trade deficit, and the same occurred in Paraguay and Haiti, although on a much smaller scale.

The allocation of the inflow of capital in 1974 continued to favour certain countries, such as Brazil and Mexico. At the same time, however, the reactivation and amount of the inflow of external funds into Peru, and the amounts received in Nicaragua, the Central American countries, the Dominican Republic, Uruguay and Paraguay represented an increase in the number of countries benefiting and also in the amount of capital provided. The volume of the inflow of capital helped to increase the capacity to import and countered the deterioration in the purchasing power of exports which had been affecting almost all the countries in question, thus obviating restrictions on imports needed for domestic economic development, although at the cost of greater external indebtedness.

This high level of inflow of external resources, maintained for a long period, helped to increase Brazil's imports to such an extent that its external purchases in 1965 were equivalent to only one month of its present imports. The internal rigidities which arose in the course of the acceleration of the country's economic activity were compensated with the growing imports, which were financed with external resources.

Finally, it should be pointed out that the improvement in the net external position of the region as a whole, which recorded a balance-of-payments surplus of some 3,900 million dollars in 1974, was due to the trade surplus of the Latin American oil-exporting countries and Argentina,

and not to the surplus external financing which was characteristic of the situation in previous years and almost exclusively affected Brazil. Indeed, after a number of years, Brazil showed a considerable balance-of-payments deficit of some 1,200 million dollars as a result of the rather sluggish behaviour of its exports and the inadequacy of the inflow of capital to finance its large imports. It generally happens in the region that a greater inflow of capital does not occur at the beginning of a period of weakening of exports or of their purchasing power, that is, just when it is most needed to pay for the imports required by domestic production activity, which of course leads to the deterioration of the net external position of the country.

(c) *Inter-Latin American trade*

During 1974 trade between eighteen countries of the region (as measured by the CIF value of imports of goods) increased by 71 per cent. This increase, which was considerably greater than the increase of 38 per cent recorded in 1973, was also greater than the growth of the total exports of these eighteen countries, which amounted to 65 per cent. Trade between the LAFTA countries likewise increased by 71 per cent (taking into account the countries of the Andean Group), while trade between the countries of the Central American Common Market increased by 38 per cent. In the Andean Group, subregional trade increased by 107 per cent (see tables 156, 157 and 158).

The countries which increased their share of intra-regional trade in 1974 were Bolivia, Colombia, Chile, Ecuador, Honduras and especially Venezuela on account of the higher value of its sales of oil. Brazil and Argentina, however, continued to account for the biggest shares (18 and 17 per cent), followed by Venezuela (12 per cent), Chile (9 per cent) and Mexico (7 per cent). In 1973 and 1974 only the Dominican Republic had a share of less than 1 per cent, while 12 countries had a share of between 1 and 5 per cent.

In 1974 the oil-exporting countries appreciably increased their trade surpluses with the region. Thus, Venezuela's trade surplus rose from 170 million dollars in 1973 to 725 million in 1974, that of Bolivia from 19 to 54 million dollars, and that of Ecuador from 89 to 187 million dollars. Argentina, which has traditionally had a trade surplus with the rest of the region, also increased its surplus, from 325 to 393 million dollars, but between 1973 and 1974 a number of countries increased their deficits with the region, the most significant cases being Brazil, Chile, Peru, Uruguay, the Central American countries and Panama. For the eighteen countries considered, the ratio of the trade balances to total regional trade, which had increased from 0.17 in 1971 to 0.20 and 0.22 in 1972 and 1973, reached a figure of 0.26 in 1974. This indicates that the trade imbalance between the countries continued to increase.

Table 156. Inter-Latin
(CIF values of imports of

Importing country \ Country of origin	Argentina	Bolivia	Brazil	Colombia	Chile	Ecuador	Mexico
Argentina	–	32.2	205.1	13.1	82.1	11.5	23.2
Bolivia[a]	37.7	–	18.0	3.6	1.0	0.3	–
Brazil	343.6	19.6	–	6.4	36.5	3.7	56.9
Colombia	15.6	1.3	14.9	–	6.6	16.5	22.6
Chile[a]	165.1	17.6	34.1	9.4	–	16.5	38.1
Ecuador[a]	6.2	–	6.7	6.7	1.0	–	5.7
Mexico[a]	30.3	0.2	43.0	4.2	8.1	3.0	–
Paraguay	29.8	–	16.3	0.2	0.6	0.1	0.7
Peru	27.6	10.5	38.0	39.3	5.9	14.9	15.4
Uruguay	61.8	3.1	48.1	0.3	1.7	0.2	1.9
Venezuela[a]	40.6	–	89.9	14.5	2.9	–	40.6
Costa Rica	2.4	–	4.6	4.8	–	0.1	11.3
El Salvador	0.6	–	1.0	2.8	–	0.3	10.1
Guatemala	1.5	–	1.5	2.3	–	0.1	16.0
Honduras[a]	0.7	–	0.6	2.1	–	–	5.1
Nicaragua	1.0	–	0.7	2.5	–	–	8.0
Cuba	–	–	–	–	–	–	–
Haiti	–	–	–	–	–	–	–
Panama	2.2	–	2.7	8.5	0.1	51.3	9.4
Dominican Republic[a]	1.2	–	4.0	5.0	–	–	–
Total Latin America	*767.9*	*84.5*	*529.3*	*125.7*	*146.5*	*118.5*	*265.0*

SOURCE: Official foreign trade statistics. Cuba, Haiti and the CARIFTA countries are not included for lack of information.

Table 157. Inter-Latin
(CIF values of imports of

Importing country \ Country of origin	Argentina	Bolivia	Brazil	Colombia	Chile	Ecuador	Mexico	Paraguay
Argentina	–	65.0	270.0	33.0	95.0	25.0	46.4	60.7
Bolivia	46.0	–	45.0	8.0	1.0	0.3	–	–
Brazil	390.0	40.0	–	18.0	193.0	8.0	91.0	25.0
Colombia	40.9	2.7	29.0	–	46.5	34.7	37.2	0.6
Chile	345.1	25.5	66.1	10.1	–	46.7	30.6	1.5
Ecuador	8.0		13.0	10.0	1.0	–	5.7	0.2
Mexico	41.2	0.4	60.5	9.4	21.7	9.4	–	2.0
Paraguay	55.9	–	20.3	0.2	0.7	0.1	0.8	–
Peru	34.0	21.0	44.0	75.0	6.0	25.0	30.8	0.3
Uruguay	75.0	6.0	93.0	0.2	1.8	0.4	1.9	1.5
Venezuela	50.0	–	162.0	20.0	2.3	–	40.6	0.2
Costa Rica	3.0	–	6.0	12.0	–	0.1	22.6	–
El Salvador	0.7	–	1.3	15.0	–	0.4	20.0	–
Guatemala	1.8	–	1.9	5.0	–	0.1	24.0	–
Honduras	0.9	–	0.8	2.0	–	–	5.0	–
Nicaragua	1.2	–	0.9	4.0	–	–	8.0	–
Panama	2.7	–	3.5	22.0	0.1	80.0	14.0	–
Dominican Republic	1.5	–	5.0	8.0	–	–	–	–
Total	*1,097.9*	*160.6*	*822.3*	*251.9*	*369.1*	*230.2*	*378.6*	*92.0*

SOURCE: Official foreign trade statistics.

American trade, 1973
goods, in millions of dollars)

Paraguay	*Peru*	*Uruguay*	*Venezuela*	*El Salvador*	*Guatemala*	*Honduras*	*Nicaragua*	*Panama*	*Dominican Republic*	*Total Latin America*
20.8	18.9	5.9	23.0	–	0.3	0.4	–	6.1	–	442.6
–	4.3	0.5	–	–	0.3	–	–	–	–	65.8
23.1	20.0	16.9	78.0	2.2	0.1	0.2	–	36.9	0.1	644.2
0.4	9.8	4.2	7.6	–	0.1	0.1	–	7.2	0.3	107.9
1.2	16.5	2.4	15.3	–	–	–	–	2.4	–	318.6
–	3.1	–	–	–	0.5	–	–	–	–	29.9
1.5	5.9	6.1	90.5	0.7	2.6	0.2	2.2	17.7	–	217.4
–	0.2	1.0	0.1	–	–	–	–	–	–	49.0
0.6	–	1.7	20.2	–	0.1	–	0.3	1.5	–	179.9
2.0	1.2	–	1.8	–	–	–	–	0.1	0.9	123.1
–	8.7	–	–	–	–	–	–	5.8	–	203.0
–	0.5	–	22.9	24.0	32.8	2.9	24.0	6.9	4.8	142.0
–	0.9	–	16.2	–	59.4	–	15.6	8.0	–	132.3
–	0.2	–	26.5	57.1	–	3.2	12.4	0.7	–	138.4
–	0.8	–	20.8	–	16.2	–	9.3	1.1	–	63.6
–	0.2	–	16.9	25.8	29.3	7.1	–	3.3	–	122.5
–	–	–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–	–	–
–	0.8	0.1	33.6	2.8	3.9	0.9	2.5	–	11.4	138.7
–	0.4	–	–	0.1	3.2	–	0.6	0.5	–	15.4
49.6	*92.4*	*38.8*	*373.4*	*112.7*	*148.8*	*15.0*	*66.9*	*98.2*	*17.5*	*3,134.3*

[a] Estimates based on partial data.

American trade, 1974[a]
goods, in millions of dollars)

Peru	*Uruguay*	*Venezuela*	*Costa Rica*	*El Salvador*	*Guatemala*	*Honduras*	*Nicaragua*	*Panama*	*Dominican Republic*	*Total Latin America*
23.0	6.7	70.6	–	–	0.4	0.4	–	9.0	9.0	705.2
5.0	0.6	–	–	–	0.4	–	–	–	–	106.3
25.0	19.1	239.5	–	3.0	0.1	0.2	–	50.0	0.1	1,102.0
28.8	2.1	32.5	0.6	0.1	0.2	0.9	0.1	18.0	–	274.9
29.4	6.5	16.8	–	–	0.4	–	–	–	–	578.7
5.0	–	–	–	–	0.5	–	–	–	–	43.4
11.5	7.9	168.2	2.7	0.2	4.1	0.2	2.6	20.0	–	362.0
0.2	2.0	0.1	–	–	–	–	–	–	–	80.3
–	2.0	62.0	4.4	–	–	–	–	2.0	–	306.5
1.4	–	5.5	–	–	–	–	–	0.1	1.3	188.1
10.0	–	–	–	–	–	–	–	6.0	–	291.1
0.6	–	70.3	–	34.0	40.0	10.0	35.0	10.0	7.0	250.6
1.0	–	49.7	26.0	–	64.0	–	21.0	12.0	–	211.1
0.2	–	81.4	18.0	70.0	–	8.0	18.0	1.1	–	229.5
0.9	–	63.9	11.0	–	22.0	–	10.0	1.7	–	118.2
0.2	–	51.9	44.0	44.0	47.0	12.0	–	5.0	–	218.2
0.9	0.2	103.1	10.0	3.0	5.2	0.9	2.6	–	17.0	265.2
0.5	–	0.1	0.5	0.1	4.3	–	0.6	0.6	–	21.2
143.6	*47.1*	*1,015.6*	*117.2*	*154.4*	*188.6*	*32.6*	*89.9*	*135.5*	*25.4*	*5,352.5*

[a] Estimates based on partial data.

Table 158. Inter-Latin American trade by integration groups
(CIF values of imports of goods)

	1970		1971		1972		1973[a]		1974[b]	
	Millions of dollars	*Percentage of total*	*Millions of dollars*	*Percentage of total*	*Millions of dollars*	*Percentage of total*	*Millions of dollars*	*Percentage of total*	*Millions of dollars*	*Percentage of total*
LAFTA	1,348	72.8	1,458	72.9	1,646	72.4	2,286	72.9	3,911	73.1
CACM	299	16.1	277	13.8	306	13.4	388	12.4	534	10.0
Andean Group	(134)	(7.2)	(159)	(8.0)	(164)	(7.2)	(254)[c]	(8.1)	(525)	(9.8)
Total inter-Latin American Trade[d]	1,853	*100.0*	2,000	*100.0*	2,275	*100.0*	3,134	*100.0*	5,353	*100.0*

SOURCE: ECLA, on the basis of official statistics.
[a] Provisional figures.
[b] Estimates.
[c] Includes Venezuela.
[d] Trade between the Andean Group countries is also included under LAFTA. In addition to the countries making up the sub-regional groups, which are covered in the corresponding trade figures, the intra-regional total also includes Panama and the Dominican Republic. No data were available for Cuba and Haiti, and the CARIFTA countries were not taken into consideration.

Chapter II

THE ECONOMIC SITUATION BY COUNTRIES

ARGENTINA

1. RECENT ECONOMIC TRENDS

In 1974, the economy of Argentina achieved a growth rate of 7.2 per cent, doubling the average annual rate recorded during the period 1970-1973. This time economic growth was associated with the progressive redistribution of income with full employment, and with the relatively favourable evolution of the external variables.

As from mid-1973, the Government boosted the tempo of the economy by a large increase in demand reinforced by a general rise in wages (accompanied by price controls, which began to be applied after a period in which profit margins were considered fairly high); the impetus given to exports of manufactures; State action in the construction of dwellings; and an expansionist fiscal, monetary and credit policy. These objectives were attained to a considerable extent, added to which the agricultural year was good, with excellent harvests of fruit and vegetables, industrial crops and some cereals, while stocks of cattle reached unprecedented levels. The industrial sector responded to the increase in demand by making better use of existing productive capacity, despite some difficulties in the supply of inputs.

Under the circumstances, the growth of the gross domestic product and of consumption were much higher than they had been traditionally, while the unemployment rate dropped to minimum levels, the share of wage-earners in income increased and a large trade surplus was achieved, although it was much smaller than the previous year.

As the implementation of the policy described progressed, impediments to its continuation began to appear, mainly as a result of inadequate plans for private investment in industry.

On the other hand, the pressure on prices from imported inflation, growing demand and a shortfall in some inputs together with the slow absorption of idle capacity, were the cause of failures to observe price controls, which in some cases came to constitute actual parallel marketing circuits. In the face of this situation, towards the end of 1974 a more flexible price policy was adopted, aimed at stimulating private investment and restoring normal marketing channels.

The last months of 1974 and the first months of 1975 mark a period of transition towards a new balance between economic and social sectors, following a year of good economic results. Prices and incomes thus emerge as one of the most critical areas of the economic policy, in a situation in which the margins of State action will be narrowed by the large fiscal deficit. This situation is projected against the background of an international crisis, which will have adverse effects on the evolution of the domestic economy, although its size and nature still cannot be foretold.

2. TOTAL SUPPLY AND DEMAND

In 1974, the gross domestic product increased by 7.2 per cent. As has already been said, these figures doubled the average rate of growth of recent years. The volume of imports also showed a large increase (19.3 per cent).

Total demand also grew far more rapidly than in the past. Consumption far surpassed the rate anticipated in the Three-Year Plan,[1] while although investment had grown faster than its traditional rate it did not achieve the goal of the Plan, and the volume of exports showed no change from 1973 (see table 159).

The growth of consumption was the result of the policy of redistribution among the lowest income sectors, and it was also reflected in the increased growth of the sectors of industry producing non-durable consumer goods.

The performance of the components of gross investment was uneven. Private construction increased by around 18 per cent, boosted by the low-cost housing plans which were the respon-

[1] Three-Year Plan for Reconstruction and National Liberation.

Table 159. Argentina: total supply and demand

	Millions of pesos at 1970 prices			Structure (percentages)		Annual growth rate (percentages)		
	1970	1973	1974[a]	1970	1974[a]	1970–1972	1973	1974[a]
Total supply	*102,091*	*112,696*	*121,759*	*108.0*	*107.9*	*3.2*	*3.6*	*8.0*
Imports[b]	7,534	7,471	8,916	8.0	7.9	−0.4	−0.1	19.3
Gross domestic product	94,557	105,225	112,843	100.0	100.0	3.6	3.8	7.2
Total demand	*102,091*	*112,696*	*121,759*	*108.0*	*108.0*	*3.2*	*3.6*	*8.0*
Exports[b]	8,016	7,591	7,593	8.5	6.7	−6.2	7.7	–
Domestic demand	94,075	105,105	114,166	99.5	101.2	4.0	3.3	8.7
Gross domestic investment	18,774	21,390	23,238	19.9	20.6	7.9	−2.1	8.6
Gross fixed investment	18,463	20,114	21,803	19.5	19.3	6.3	−3.6	8.4
Public	5,572	...		5.9	...	...	...	...
Private	12,891	...		13.6	...	...	...	...
Construction	10,092	9,072	10,363	10.6	9.2	2.3	−14.0	14.2
Machinery and equipment	8,371	11,042	11,440	8.9	10.1	11.0	6.9	3.6
Total consumption	75,301	83,715	90,928	79.6	80.2	3.0	4.8	8.6
General goverment	9,047	...	...	9.6	...	2.8	...	...
Private	66,254	...	...	70.0	...	3.0	...	...

SOURCE: 1970–1972: ECLA estimates based on figures from the Three-Year Plan for Reconstruction and National Liberation; 1973: ECLA estimates based on figures supplied by the Central Bank of Argentina; 1974: ECLA estimates based on preliminary data from the Central Bank.

Note: The figures for exports and imports of goods and services were taken from balance-of-payments data expressed in dollars at current prices, which were converted to constant 1970 values by deflation, using price indexes calculated by ECLA for the purpose.

[a] Preliminary figures.

[b] Goods and services, excluding factor payments.

sibility of the Ministry of Social Welfare and by the increased demand for housing for the medium- and high-income groups. Meanwhile, public construction increased by around 10 per cent, particularly as a result of the more rapid growth of work already begun, and the start made to large-scale projects like the hydroelectric power station of Salto Grande.

In connexion with investment in machinery and equipment, the 10 per cent increase in local sales of tractors would appear to indicate an improvement in the agricultural equipment situation. On the other hand, industrial investment apparently did not react to the favourable conditions of demand prevailing throughout the year. In some cases, this tendency may be attributed to a decrease in profits; in others, to the difficulty of returning to the production circuit profits obtained in parallel marketing channels. During the latter part of the year, however, a reactivation of investment was to be observed, and this was reflected in growth during the fourth quarter and confirmed in the surveys of industrial expectations for 1975.

3. THE EVOLUTION OF THE GROSS DOMESTIC PRODUCT

The gross domestic product grew at a higher rate than the 7 per cent laid down in the Three-Year Plan for 1974. Of note was the growth of agricultural and industrial output and increased activity in the construction sector (see table 160 and figure III).

(a) *Agricultural sector*

During 1974 the growth of the agricultural sector was boosted by production of fruit and vegetables, and some industrial crops. In addition, good harvests of maize and particularly sorghum helped to offset the drop in wheat production. Livestock activity was characterized by an increase in cattle stocks (this was noteworthy in view of the retention practised in previous years) and by a slightly higher slaughtering rate than in 1973.

Output of wheat, maize and sorghum together was similar in amount to the 1973 figure, when the maximum volume of production ever recorded was obtained.

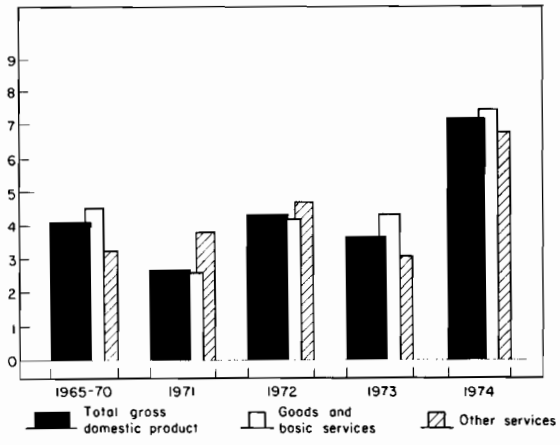
Table 160. Argentina: gross domestic product at factor cost, by sector of economic activity

	Millions of pesos at 1970 prices			Structure (percentages)		Annual growth rate (percentages)		
	1970	1973	1974[a]	1970	1974[a]	1970-1972	1973	1974[a]
Agriculture	11,217	11,363	12,288	13.2	12.1	-2.0	5.5	8.1
Mining	1,325	1,043	1,064	1.6	1.0	-0.7	-20.2	2.1
Manufacturing	25,399	30,638	32,722	29.9	32.2	6.3	6.8	6.8
Construction	4,578	4,318	4,857	5.4	4.8	2.3	-9.8	12.5
Subtotal goods	*42,519*	*47,362*	*50,931*	*50.1*	*50.1*	*3.5*	*4.0*	*7.5*
Electricity, gas and water	1,810	2,323	2,483	2.1	2.4	9.2	7.5	6.9
Transport and communications	8,548	9,274	9,885.0	10.1	9.7	1.8	4.7	6.6
Subtotal basic services	*10,358*	*11,597*	*12,368*	*12.2*	*12.2*	*3.1*	*5.3*	*6.6*
Wholesale and retail commerce, restaurants and hotels	12,526	14,345.0	15,509	14.7	15.3	5.2	3.5	8.1
Financial establishments, insurance and real estate	3,737	4,281.3	4,539	4.4	4.5	4.8	4.3	6.0
Community, personal and social services	15,812	17,301.8	18,319.5	18.6	18.0	3.2	2.7	5.9
Subtotal other services	*32,075*	*35,928.1*	*38,367*	*37.8*	*37.7*	*4.2*	*3.2*	*6.8*
Gross domestic product, total	*84,952*	*94,435.8*	*101,185*	*100.0*	*100.0*	*3.6*	*3.8*	*7.2*

SOURCE: 1970-1972: ECLA calculations on the basis of figures from the Three-Year Plan for Reconstruction and National Liberation; 1973: ECLA calculations on the basis of figures provided by the Central Bank of Argentina; 1974: ECLA estimates on the basis of preliminary data supplied by the Central Bank.

[a] Preliminary figures.

Figure III. Argentina: growth of gross domestic product
(Annual growth rates)
Natural scale



The increases of 2.1 per cent in maize and of 1.9 per cent in sorghum–over the high levels reached in 1973–are mainly attributable to the high yield per hectare harvested (4.4 per cent for maize and 9.1 per cent for sorghum), partly as a result of favourable weather conditions; they also appear to reflect some changes in production techniques. The area sown for the 1974/1975 crop year is much the same as in the previous year.

In contrast, wheat production in the 1973/1974 crop year was 17 per cent lower than the year before, as a result of a 24 per cent reduction in the area sown. This accentuated the trend begun in the 1970/1971 crop year, which may be associated with a certain degree of replacement by cattle-raising and by other crops, and may be partly a consequence of changes in relative prices. For the 1974/1975 crop year the harvest is expected to be around 5.1 million tons owing to the drought which affected some producing areas.

The production of industrial crops is estimated to have increased by around 14 per cent. Output of sugar was slightly less than in 1973 when production reached its peak of 1,540,000 tons (60 per cent higher than the average for the five-year period 1968/1972) as a result of the exceptional conditions existing in the international and local markets. Grape production for wine-making showed a growth of around 36 per cent in 1974, while fruit production recorded an exceptional increase of 33 per cent and vegetable production increased by 8 per cent.

The outstanding event in the livestock sector was the increase in stocks of beef cattle, which had begun in 1970 following the downswing in the stockbreeding cycle which took place during 1967-1969. It is estimated that towards the end of 1974 stocks of beef cattle reached a historical

maximum of around 60 million head and were possibly 57 million at 30 June 1974. This latter figure marks an increase of nearly 9 million compared with June 1969, implying an increase in stocks of around 20 per cent between the lowest point of the cycle and that date.

Although no final figures exist for the total rate of slaughter, the National Meat Board estimate was around 10 million head, i.e., slightly above the 1973 level and similar to that of 1972. Even assuming the existence of a substantial slaughter not registered by the National Meat Board, the slaughter/stocks ratio probably remained below what is considered a normal production figure (22–23 per cent) (see table 161).

Relative prices in the sector deteriorated during the year, especially for livestock production. This became more pronounced in the last few months, following the accelerated growth of industrial prices, as may be seen from table 162.

Official policy attempted to avoid this relative decrease having direct repercussion on cattle stocks. Thus in 1974 fiscal measures were taken aimed at stimulating the retention of females. In addition, in January 1975, the price of cattle was increased and tax incentives were introduced, especially in the breeding stage, with a view to reducing the rearing-period for cattle. Tax incentives were also introduced for exports of beef, in order to assist the operation of the refrigerating plants.

In view of the situation in the international markets, policy was aimed at giving more incentives to agriculture. With the fixing of prices for the farming year 1974–1975, there was a tendency for the relative price of wheat to improve compared with that of industrial goods and livestock.

As regards the general policy for the agricultural sector, it was decided still not to apply in 1975 the tax on potential normal income from land.

(b) *Mining*

The product generated by mining increased by 2.1 per cent, as a result of a drop of around 1.5 per cent in petroleum output, and increases of around 35 per cent in the production of coal, 9 per cent in natural gas and 15 per cent in other mineral products.

The drop in petroleum production may be attributed to the lower yields of the wells in production and to the lack of results of any importance in exploration. For the future, the use of secondary reserves has been programmed and, in a longer term, the development of the submarine valley.

Table 161. Argentina: indicators of cattle breeding

	1967	*1968*	*1969*	*1970*	*1971*	*1972*	*1973*	*1974*[a]
				Millions of head				
Stocks at 30 June	51.3	51.5	48.3	48.4	49.8	52.3	54.8	57.0
Slaughter for the year	12.5	12.8	13.8	12.9	9.5	10.0	9.8	10.0
				Percentages				
Slaughter/stocks	24.4	24.9	28.6	26.7	19.1	19.1	17.9	17.5
				Kilogrammes annually				
Per capita consumption	82.0	87.0	92.0	84.0	64.0	62.0	66.0	78.0

SOURCE: National Meat Board.

[a] Provisional figures.

Table 162. Argentina: relative prices of the agricultural sector
(Index: 1960 = 100)

Wholesale prices	*1969*	*1973*	*1974*	*May 1973*	*December 1973*	*June 1974*	*December 1974*
Animal production							
Non-agricultural	94.0	130.1	108.9	141.6	120.9	110.0	94.6
Vegetable production							
Non-agricultural	105.5	108.2	101.8	102.8	105.1	105.4	100.0
Agricultural							
Non-agricultural	100.2	118.9	105.3	121.7	112.9	107.7	97.4

SOURCE: Wholesale price index of the National Institute of Statistics and Censuses (INDEC).

In 1973 coal production had dropped compared with 1972, which means that the 1974 increase was largely a recovery. In 1974 the investments made (especially in modes of transport from the coalfields of Rio Turbio) will make expansion possible at a later date.

The rest of mining (metallic mineral products and mineral products for industrial uses and construction) grew by around 15 per cent, especially in response to an increase in materials for construction. During the year, iron mining activities in Sierra Grande continued, and the intention is to open up the manganese, gold and silver deposits in Aguas del Dionisio, and the copper deposits in Pachón, for production.

A scheme to promote mining was also brought into operation, mainly to assist in prospection and exploration, with the State bearing part of the commercial risk.

(c) *Manufacturing*

Manufacturing grew at a rate of 6.8 per cent, similar to that of the last five years, but its proportional share in the growth of the gross domestic product was distinctly smaller than was the case traditionally.

As has already been said, this growth was the result of a greater use of installed capacity rather than of any increase in this capacity. Exports played an important role in a wide range of industrial activities. Lastly, an additional feature of the 1974 growth, in contrast to past experience, was the dynamism of the industrial sectors producing non-durable consumer goods.

As a whole, the sectors producing food-stuffs and textiles grew more than industry on average. Of the industrial sectors, it was the textile sector which showed most growth, and exceeded the target of the Three-Year Plan; this was mainly as a result of the increase in the purchasing power of the wage-earners, while the increase in exports of some products also had some influence, although to a lesser extent (see table 163).

The activities which had been most dynamic in previous periods evolved at relatively slower rates. The chemical industries grew by 6.9 per cent and experienced some difficulties with supplies of inputs although these problems tended to be rectified towards the end of the year. In the middle of the year the Petroquímica General Mosconi plant came into operation, for the production of basic aromatic hydrocarbons.

The basic metal industries grew by 8.6 per cent. Production of pig-iron increased by 33 per cent as a result of the opening of the new SOMISA blast furnace, despite some difficulties in external supplies of coal. The expansion of this plant also contributed to a major extent to the growth of steel production, which reached 2.3 million tons (9.2 per cent more than the previous year) and covered around 56 per cent of domestic consumption. This increase in output in the basic stages of the steelmaking process was not reflected in the production of rolled steel products, which dropped by 2.5 per cent, owing principally to difficulties in supplies of scrap for the semi-integrated steel mills and of semi-processed products for re-rolling.

Table 163. Argentina: volume of industrial output
(Annual growth rate)

Product	*Quarters 1974*				*Year*		
	I	*II*	*III*	*IV*	*1972*	*1973*	*1974*
Total manufacturing	*3.8*	*7.3*	*6.5*	*9.0*	*6.8*	*6.8*	*6.8*
Food, beverages and tobacco	4.7	6.4	3.6	5.3	4.7	4.2	5.0
Textiles, clothing and leather industry	9.6	10.4	12.3	12.2	4.8	6.2	11.2
Wood and wood products, including furniture	–0.1	1.2	11.9	4.6	–2.6	–2.0	4.5
Paper and paper products, printing and publishing	3.8	7.4	10.0	15.0	–0.7	–0.7	9.2
Chemicals and chemical products, products of petroleum and coal, rubber products and plastics	3.5	7.4	8.1	7.8	2.7	1.6	6.9
Non-metallic mineral products, except products of petroleum and coal	–2.3	4.6	6.7	8.2	4.7	0.3	4.6
Basic metal industries	9.1	5.7	7.4	11.7	5.5	4.0	8.6
Metal products, machinery and equipment	2.2	8.3	4.9	10.1	15.1	14.3	6.6
Other manufacturing industries	–2.6	–1.2	1.9	2.1	–6.1	1.0	0.1

SOURCES: 1972–1973: Central Bank of Argentina; first, second and third quarters of 1974: preliminary data supplied by the Central Bank; fourth quarter and total for 1974; estimates based on preliminary data supplied by the Central Bank.

It should be mentioned that in view of the relatively low level of integration of the steel industry, the substantial growth of pig-iron production did not lead to a further expansion of the sector. It is hoped to achieve self-supply in steel around 1980, on the basis of the expansion of SOMISA, the integration of some private mills (to date two projects which will use the direct reduction process to supply sponge iron to the electric steel mills have been approved) and the establishment of new integrated mills, a study of which was carried out in 1974.

The aluminium-producing plant of Puerto Madryn came into operation, and will enable self-supply of this metal to be achieved in a few years' time.

The industries producing metal goods, machinery and equipment grew by 6.6 per cent. Car production, including non-assembled units for export, increased by around 4.5 per cent, while the production of commercial vehicles remained at a standstill. As regards the destination of output, sales to the local market decreased by 6.8 per cent for cars and increased by only 1.3 per cent for commercial vehicles; but at the same time 7,000 completed cars were exported, 8,200 commercial vehicles and 36,000 non-assembled units. Tractor production increased by 15 per cent, with sales of 20,650 units on the local market (an increase of 10 per cent), while 4,200 units were destined for export (54.4 per cent) (see table 164).

(d) *Construction*

Private construction increased by around 18 per cent, while the number of building permits in Greater Buenos Aires and the main cities in the interior increased by around 35 per cent (it should be recalled that 1973 marked a low level of activity in construction). This growth was boosted by State action, in the form of low-cost housing plans implemented by the Housing Department of the Ministry of Social Welfare, and increased finance channelled through the Banco Hipotecario Nacional and the commercial banks.

Demand for housing for the medium- and high-income groups increased sharply as from the middle of the year. This may be attributed in part to the use of funds as a means of hedging against inflation and the channelling of profits obtained outside price controls. These circumstances caused a sizable increase in real estate prices, and the absorption of unsold units accumulated in earlier periods; they also provided an incentive to completing work already begun and the initiation of new construction work, despite some problems of supply.

(e) *Energy*

The generation of electric energy increased at a rate of 4.7 per cent during 1974 as a result of increased production by the public service power stations, which offset the drop in self-supply.

Table 164. Argentina: indicators of selected activities

	1970	*1971*	*1972*	*1973*	*1974*[a]	*Growth rate 1974*
1. Motor vehicles (thousands of units)[b]	168.0	193.4	207.6	233.7	244.6	4.7
2. Commercial vehicles (thousands of units)[b]	51.6	60.3	70.6	77.9	77.7	–0.3
3. Tractors (thousands of units)	11.0	13.8	15.4	21.3	24.6	15.3
4. Pig iron (thousands of tons)	810.0	861.0	849.0	804.0	1,069.0	33.0
5. Steel (thousands of tons)	1,823.0	1,915.0	2,105.0	2,155.0	2,354.0	9.2
6. Rolled products (thousands of tons)	2,242.0	2,514.0	2,712.0	2,981.0	2,907.0	–2.5
7. Petroleum (thousands of m^3)	22,798.0	24,565.0	25,194.0	24,260.0	23,860.0	–1.6
8. Cement dispatches (thousands of tons)	4,743.0	5,515.0	5,398.0	5,195.0	5,454.0	5.0
9. Surface area for new construction permits in main cities (thousands of m^2)	13,131.0	11,140.0	9,503.0	9,293.0	12,358.0	33.0
10. Electricity (thousands of MWH)[c]	21,727.0	23,624.0	25,319.0	26,638.0	27,893.0	4.7

SOURCES: 1 and 2: Ministry of Industrial Development; 3: Asociación de Fábricas Argentinas de Tractores; 4, 5 and 6: Centro de Industriales Siderúrgicos; 7 and 10: Ministry of Energy; 8: Asociación de Fabricantes de Cemento Portland; 9: National Institute of Statistics and Censuses.

[a] Provisional figures.
[b] Including non-assembled units.
[c] Including self-supply.

Generally speaking, energy policy is aimed at a gradual replacement of petroleum by coal, natural gas and hydroelectric and nuclear energy.

In 1974 the nuclear power station of Atucha came into operation and a project for the construction of a new plant in Río Tercero (Córdoba) is under way. Progress was made in putting El Chocón into operation, and work is being carried out on the Salto Grande dam (in conjunction with Uruguay). The construction of the Futaleufú dam, which will supply energy to the aluminium plant at Puerto Madryn, suffered some delay.

Several large-scale hydroelectric projects are at present under study, and should come into operation during the 1980s. Progress was made in studies for the Yaciretá-Apipé dam, which will be built by Argentina in conjunction with Paraguay, while it is hoped to begin work on the Alicopá complex, in the Comahue area, in the near future. A study will also be made of the possibility of making use of the middle reaches of the Paraná, and priority will be given to this project.

4. THE EXTERNAL SECTOR

The evolution of the external sector during 1974 showed surpluses of 850 million dollars in the trade balance and 260 million in the current account. At the end of the year reserves covered five months of imports. The outstanding features were the large increases in import prices, especially fuels, the decrease in the volume of exports of meat, and the notable increase in the volume and price of exports of cereals and industrial products (see figure IV).

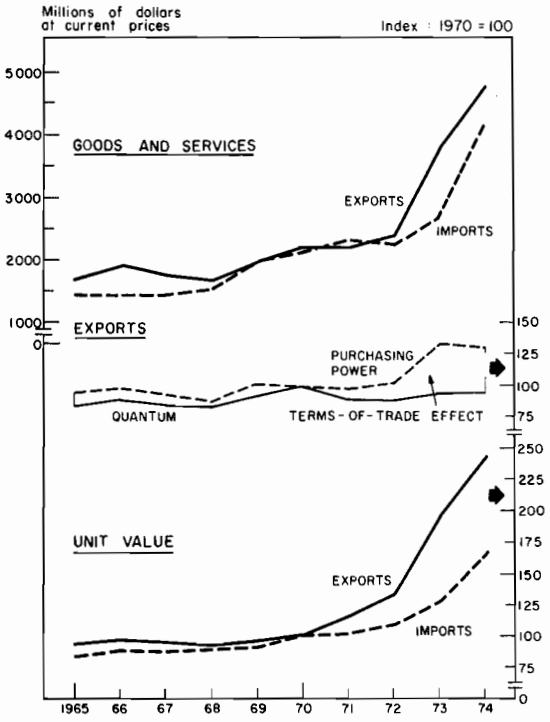
(a) *Exports*

The value of exports of goods amounted to 4,010 million dollars, i.e., an increase of 23 per cent compared with 1973 and of 73 per cent compared with the average for the last three years.

Exports of meat and meat products were substantially affected by the restrictions imposed by the European Economic Community. The 450 million dollars' worth of exports in 1973 represented a decrease of 43 per cent compared with the previous year and a drop from 24 per cent to 11 per cent in their share of total exports of goods. In addition, in the course of the year there was a drop in the average price of exports of meat, which decreased from 1,318 dollars per ton of meat including bones in January to 825 dollars in December, although the year's average remained above 1973 levels.

Wool exports dropped by 43 per cent, as a result of the decrease in the demand of Japan and the European countries.

Figure IV. Argentina: trend of external variables
Natural scale



The decreases were more than offset by the notable growth of the value of exports of cereals and manufactures. Exports of cereals increased from 864 million dollars' worth in 1973 to 1,440 million dollars' worth (an increase of 67 per cent), with the highest volume of the last 15 years despite the drop in exports of wheat. More than half these exports consisted of maize, while sorghum reached its highest figure on record. This increase in volume was complemented by a significant improvement in selling prices (see table 165).

Together with cereals, the value of other products of agricultural origin also increased by more than 50 per cent. Notable examples are fats and oils, with 260 million dollars' worth (an increase of 90 per cent), thanks to better international prices, and despite a drop in volume. Exports of sugar amounted to 200 million dollars' worth and exports of fruit were worth 100 million dollars.

Another important event was the increase of 30 per cent in exports of manufactured products of non-agricultural origin, which came to account for 22 per cent of total exports of goods. Exports include sales of machinery and vehicles, which amounted to around 350 million dollars (with an increase of around 55 per cent in value and 30 per cent in volume compared with 1973). Steel exports were worth 140 million dollars (an

Table 165. Argentina: value of exports
(Millions of dollars at current prices)

Product	*1970*	*1971*	*1972*	*1973*	*1974*[a]
Meat and offal	441	416	691	790	450
Cereals	509	534	339	864	1,440
Hides and skins	97	70	120	121	100
Wool, hair and horsehair	87	72	89	194	110
Other agricultural products	383	395	378	650	1,020
Manufactured products of non-agricultural origin	256	253	324	647	890
Total	*1,773*	*1,740*	*1,941*	*3,266*	*4,010*

SOURCE: National Institute of Statistics and Censuses.
[a] Provisional figures.

increase of 17 per cent) while chemical products amounted to 150 million dollars (50 per cent more than in 1973). The magnitude of these exports was not only the result of higher international prices but of a growth in volume. This result was affected by the tax and credit incentives policy, and the bringing of Argentine industries into line with international requirements.

(b) *Imports*

The value of imports of goods was 3,160 million dollars, i.e., an increase of 60 per cent compared with the previous year.

The item which showed most growth was fuels, the value of which increased from 172 million dollars in 1973 to 520 million in 1974 on account of increases in international prices, thus accounting for 15 per cent of the total.

Imports of intermediate and consumer goods increased by 58 per cent. Of these, imports of metal products increased by 35 per cent, in terms of dollars at current prices, mainly on account of the price increase, since up to the end of the year there were some problems of supply. Purchases of raw materials for the chemical industry amounted to 470 million dollars, with a large-scale increase in prices.

Imports of capital goods were worth 500 million dollars, i.e., an increase of 11 per cent compared with the previous year; their share in the total, however, dropped from 20 to 14 per cent.

(c) *Balance of payments*

The trade surplus was 850 million dollars (equivalent to 707 million SDRs), but it tended to decrease in the second half of the year owing to the sharp increase in the value of imports (see table 166).

Real services were in deficit by around 200 million SDRs, i.e., an increase compared with the previous year, due mainly to the rise in freights. The deficit in financial services was 293 million SDRs compared with 327 million the previous year, owing to the decrease in the amounts of remittances of profits and dividends abroad and the slight drop in net payments of interest.

As a result of this, the balance on current account showed a surplus of 215 million SDRs, which was basically due to the favourable trend in the first months of the year.

Non-compensatory capital movements recorded a net outflow of 152 million SDRs, among other factors, as a result of payments to finance imports and amortization payments on private sector loans.

All in all, the balance of payments before compensation showed a surplus of 63 million SDRs, which was reflected in a net decrease of 110 million SDRs in compensatory borrowing (repurchase of pesos from the International Monetary Fund and amortization payments on loans from banks abroad) and other items. International reserves dropped by 47 million SDRs, and at the end of the year totalled 1,170 million SDRs, which finances around five months of imports.

(d) *External sector policy*

(i) *Exchange rate*. An important element in prices and incomes policy during 1974 was the maintenance of the exchange rate for commercial transactions at 5 pesos per dollar and at 9.98 pesos per dollar for financial operations.

At the same time, various mechanisms were employed to bring about gradual changes in the exchange rates actually used by exporters with a view to maintaining competitiveness. For this purpose, the settlement of some transactions was transferred totally or partially from the commercial to the financial market, or tax incentives, such as the refund of locally-paid taxes, were granted.

Table 166. Argentina: balance of payments
(Millions of SDR units)

	1970	1971	1972	1973	1974[a]
Current account					
Exports of goods and services	2,198.0	2,197.0	2,210.0	3,168.7	3,986.1
Goods FOB	1,773.0	1,740.0	1,788.0	2,707.0	3,334.2
Services	425.0	457.0	422.0	461.7	651.9
Transport	215.0	220.0	204.0	251.2	362.5
Travel	74.0	92.0	73.0	72.1	91.5
Imports of goods and services	2,131.0	2,327.0	2,104.0	2,258.4	3,480.7
Goods FOB	1,474.0	1,625.0	1,526.0	1,640.0	2,627.5
Services	657.0	702.0	578.0	615.0	853.2
Transport	352.0	393.0	346.0	364.7	569.6
Travel	130.0	113.0	72.0	70.5	86.5
Net external investment income	−223.0	−256.0	−307.0	−326.5	−292.6
Profits	−70.0	−46.0	−56.0	−64.6	−36.5
Interest	−153.0	−210.0	−251.0	−261.9	−256.1
Net private transfer payments	−1.0	−1.0	−1.0	9.1	1.7
Balance on current account	−157.0	−387.0	−202.0	592.9	214.5
Capital account					
Net external financing ($a + b + c + d + e$)	157.0	387.0	202.0	−592.9	−214.5
(a) Net external non-compensatory capital	463.0	−203.0	−36.0	−37.0	
Direct investment	11.0	11.0	9.0	8.0	
Long- and medium-term loans	487.0	557.0	346.0	405.0	
Amortization payments	−259.0	−360.0	−317.0	−444.0	
Short-term liabilities	226.0	−409.0	−71.0	−12.0	151.5
Official transfer payments	−2.0	−2.0	−3.0	6.0	
(b) Domestic non-compensatory capital or assets	−91.0	−21.0	59.0	−76.0	
(c) Errors and omissions	6.0	25.0	7.0	66.1	
(d) Allocations of SDRs	59.0	47.0	47.0	–	–
(e) Net compensatory financing (increase −)	−280.0	539.0	125.0	−546.0	−63.0
Balance-of-payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	–	141.0	325.0	157.0	−110.0
Amortization payments	−120.0	−1.0	−5.0	–	
Movements of foreign exchange reserves (increase −)	−84.0	272.0	−240.0	−654.0	64.0
Movements of gold reserves (increase −)	−17.0	70.0	60.0	–	–
SDRs (increase −)	−59.0	57.0	−15.0	−49.0	−17.0

SOURCE: International Monetary Fund (IMF), *Balance of Payments Yearbook*, vol. 26.

[a] Estimates based on official statistics.

In the case of agricultural exports, the public sector centralization of exports of the most important cereals assisted in separating international prices from those of the local market, thus eliminating the possible inflationary effect.

The curb on exchange rates from mid-1973 was aided in a first stage by the deceleration of local prices, while international prices became increasingly steady. These circumstances changed in the course of the year as growing domestic costs and the weakening of international prices became unable to maintain their mutual balance through the medium of the exchange-fiscal machinery. Towards the end of the year, therefore, growing pressures emerged to modify the exchange rate.

(ii) *Trade agreements*. Lines of credit were granted to various Latin American countries in order to finance their imports of products from Argentina. The agreement signed with Cuba was the most important because of its magnitude (1,200 million dollars in six years), and because of the high value-added of the products negotiated (motor vehicles, agricultural machinery, transport materials, machines, engines, etc.).

The economic co-operation agreement with Uruguay brought in some innovations. It established the drawing up of complementarity agree-

ments, the installation of bi-national enterprises and the gradual liberalization of trade.

Various agreements were also signed with countries of the socialist bloc, aimed at diversifying exports and increasing the volume of trade, participating in the installation, modernization and expansion of factories, and exchanging patents, licences, and technical procedures. They allowed for payment in freely convertible currencies with a repayment period of ten years for purchases by Argentina.

5. PUBLIC SECTOR

During 1974, the public sector increased the area of its direct action and control of the national economy.

As regards the current income and expenditure of the National Government, as in 1973, the accounts of the Treasury showed a deficit. During 1973, 36 per cent of the current expenditure paid by the Treasury was not financed by current income; and in 1974 this percentage increased to 38 per cent (see table 167).

The sum of public investment finance requirements, capital transfers and extra-budgetary expenditure gives an approximate deficit for 1974 of 30,000 million pesos, which is 53 per cent higher than that recorded the previous year. As a percentage of the gross domestic product it increased compared with the previous year, and remained at a high level (6 per cent).

The net tapping of credit resources through the sale of securities in the capital markets gave a surplus of nearly 2,900 million pesos in 1974, basically on account of the increased acceptance of bonds issued in foreign currency or readjustable bonds.

The final deficit of the Treasury year was 27,400 million pesos, 43 per cent up on the previous year. This was in spite of the considerable

Table 167. Argentina: central government movements of treasury funds
(Millions of pesos)

	1970	*1971*	*1972*	*1973*	*1974*
Current resources	7,019	8,649	13,667	20,183	30,504
Budget income	6,802	8,589	13,508	19,389	29,537
Tax income	6,059	7,532	11,111	16,791	27,514
Direct taxes	2,328	2,267	2,884	4,027	7,073
Indirect taxes	2,291	3,200	4,203	6,709	12,274
Taxes on external trade	1,440	2,065	4,024	6,055	8,167
Non-tax income	743	1,057	2,397	2,598	2,023
Extra budgetary income	217	60	159	793	967
Expenditure	*7,986*	*11,836*	*19,004*	*39,961*	*60,796*
Budget expenditure	7,684	11,396	18,320	38,256	56,413
Current expenditure	5,883	8,947	14,074	31,467	48,967
Personal services	3,153	4,033	6,080	13,067	18,501
Transfers	1,892	3,494	5,613	14,416	23,555
Others	838	1,420	2,381	3,984	6,911
Capital expenditure[a]	1,801	2,449	4,246	6,789	7,446
Substantive investment	542	781	1,511	1,890	2,283
Transfers	550	692	1,053	1,969	1,921
Others	709	976	1,682	2,930	3,242
Extra-budgetary expenditure	302	440	684	1,705	4,383
Financial results	*–967*	*–3,187*	*–5,337*	*–19,778*	*–30,292*
Net capital movements	*374*	*586*	*582*	*633*	*2,885*
Placement public debt	837	1,318	2,425	4,785	7,055
Amortization public debt	–463	–732	–1,843	–4,152	–4,170
Treasury imbalance	*–593*	*–2,601*	*–4,755*	*–19,145*	*–27,407*
Financing	*593*	*2,601*	*4,755*	*19,145*	*27,407*
Central Bank of Argentina	502	2,495	3,346	14,892	24,092
Consolidated fund of official current accounts	161	86	1,149	2,788	3,670
Other short-term operations	–70	20	260	1,765	–355

SOURCE: Ministry of Economic Affairs.

[a] Excluding public debt amortization payments.

increase recorded in the collection of tax revenue (64 per cent) and above all reflects the large increase in public expenditure as a result of increased purchases of goods and services (personal and non-personal) by the central administration and of increased financial contributions to the provinces and public enterprises.

Practically all the financing of the imbalance was charged to Central Bank credit or was covered by available funds deposited in bank accounts on behalf of State agencies.

The effect of this deficit on the creation of money was greater in the second half of the year, because the absolute volume of the deficit was substantially greater, and also because the Central Bank took a larger share in financing it (88 per cent compared with 78 per cent).

The increase in tax resources was basically due to the increased collection of tax revenue on domestic activity (80 per cent), since taxes on external trade only increased by 35 per cent. Of the taxes on domestic activity, direct taxes increased by 76 per cent, and indirect taxes by 83 per cent; of the latter, those which increased most were fuels and sales taxes.

As regards taxes on external trade, tax revenue from imports increased, and that from exports decreased by 7.6 per cent, owing to the drop in the duties paid.

The current expenditure of the Treasury increased by 55 per cent mainly as a result of increased transfers to the provinces and State enterprises, while payments for the operational costs of the Central Administration increased by 40 per cent. This expenditure reflects on the one hand the difficulties experienced by the provinces in coping with wage increases using their own tax resources and on the other the increase in the income levels of Central Administration wage-workers and employees, with the 13 per cent wage increase in April, the special half month's salary at the end of June and the 15 per cent increase in November.

The increase in the deficit and the need to control its effect on domestic prices gave rise to an austerity plan during the last quarter, which froze vacancies in administration and cut down on expenditure. The budget for 1975 reduces transfers to the provinces and public enterprises and converts them to a large extent into effectively refundable loans.

Capital expenditure payments by the Treasury showed an increase of only 9.5 per cent at current prices, indicating a large drop in constant values, which was still more pronounced in transfers to the provinces, and to State enterprises and agencies.

6. MONEY AND CREDIT

As from June 1973 liquidity began to increase (expressed as the ratio of the means of payment or the total monetary supply of private persons to the product), and this process became more pronounced towards the end of the year, increasing the effect of the seasonal variation typical of this period.

During 1974 the quantity of monetary resources expressed in real terms continued to grow. Between the end of December 1973 and December 1974 the means of payment of private persons increased by 55.2 per cent, while the cost of living index rose 40.1 per cent and wholesale prices increased by 36.7 per cent. The average liquidity coefficient for the year probably exceeded the 1973 coefficient by around 40 per cent.

As from the second half of 1973 up to mid-1974 the role of the external sector in the creation of means of payment was extremely important; during this period there was a substantial increase in international reserves and in other net assets with the exterior.

In the second half of 1974 there was a gradual decline in reserves, which came to constitute a factor of contraction. At the same time, the growth rate of credit to domestic sectors increased (see table 168).

Credit to the private and public sectors increased by 50.4 per cent, with slowly increasing monthly rates; however, radical changes occurred in the relative importance of the two sectors. On average, the public sector received 43 per cent of the increase in the balances of net domestic credit (37 per cent in 1973); its share was larger in the first and last quarters.

Parallel with the change in the final destination of credit, which was associated with the deficit situation of the national and provincial governments and of some public enterprises, a substantial change took place in the channelling of credit within the private sector as a result of the law nationalizing bank deposits, in force as from October 1973 for the commercial banks and as from February 1974 for other financial bodies.

The main features of this system are: (*a*) the commercial banks and other financial institutions affected receive deposits by the public on behalf of and by order of the Central Bank, and thus lack authority to dispose of the tapped resources, since they cannot use them for active operations without authorization from the Central Bank; (*b*) funds for loans come entirely from rediscounts granted by the Central Bank; and (*c*) the Central Bank fixes the interest rates; it is responsible for

Table 168. Argentina: origin and destination of means of payment
(Balances at end of period, in millions of pesos)

	1973				1974			
	March	*June*	*September*	*December*	*March*	*June*	*September*	*December*
Means of payment	*32,098*	*38,847*	*44,984*	*56,221*	*58,055*	*66,791*	*73,894*	*87,261*
Cash	13,395	16,400	18,901	26,406	24,307	28,298	32,191	42,162
Current account deposits	18,703	22,447	26,083	29,815	33,748	38,493	41,703	45,099
Net assets in other financial bodies	*1,931*	*2,211*	*8,172*	*384*	*61*	*933*	*1,933*	...
Factors of expansion	*58,817*	*70,281*	*81,668*	*98,286*	*108,512*	*122,754*	*131,936*	*146,338*
External sector	3,522	4,694	7,545	8,486	10,066	14,569	12,163	11,278
Domestic credit	55,295	65,587	74,123	89,800	98,446	108,185	119,773	135,060
Public sector	13,532	17,485	19,471	26,725	31,322	34,672	37,509	46,194
Private sector	41,763	48,102	54,652	63,075	67,124	73,513	82,264	88,866
Factors of contraction	28,650	33,645	44,856	42,449	50,518	56,896	59,975	61,010
Deposits with little mobility	21,999	25,730	29,809	35,778	42,048	48,247	52,078	55,414
Others	6,651	7,915	15,047	6,671	8,470	8,649	7,897	5,596

SOURCE: Central Bank of Argentina.

the interest paid and the banks and other entities of the system receive a commission for their role as agents.

A year after the introduction of the system, some results may already be seen. There has been a considerable increase in the amount of rediscounts with specific destinations, and this made it possible to increase the selectivity of total credit.

In addition, the resources channelled towards the official banks increased. Since the date on which the system came into force, more than 70 per cent of the increase in the portfolio of bank loans was accounted for by official banks, which during this period probably tapped over 60 per cent of the increase in the deposits. Consequently, the loans deposits ratio deteriorated for both national and foreign private banks.

The increase in the share of the official banks in total loans reflects the incentive policy to industry and housing through the National Development Bank and the Banco Hipotecario Nacional. Between October 1973 and October 1974, National Development Bank loans increased by 75 per cent and those of the Banco Hipotecario by 125 per cent.

The official banks as a whole gave increased importance to specific credit for investment and thus gave less priority to credit for financing commercial drawing by the enterprises.

In September an increase was decreed in the interest rate which had been decreased in June 1973, and the selective interest-rate differentials established at that time were abolished. This was due to the fact that rates of interest had become markedly negative owing to the growth of prices.

In the last quarter of the year, the lower level of liquidity and the lack of incentive for fixed-term deposits (the rate of which was negative), created conditions for the growth of money markets with less rigid rates—an acceptance market, for example. There was thus a re-emergence to some extent of a financial system outside the banking system.

7. PRICES, WAGES, INCOME DISTRIBUTION AND EMPLOYMENT

(a) *Prices*

During 1974, the annual average wholesale prices increased by 20 per cent and consumer prices by 24 per cent. These increases are relatively moderate, compared with the experience of earlier periods (see table 169).

Despite the average increase of 24 per cent in the consumer price index, the food component increased by 15 per cent, mainly as a result of the restriction on the price of meat, which meant that the increases did not come down so heavily on the lowest income groups; this is an approximation, however, since transactions at higher prices than those recorded would appear to have taken place, as well as changes in the quality and specifications of some products, with effects on real prices which are difficult to quantify.

Table 169. Argentina: evolution of domestic prices
(Annual growth rate)

	1970	1971	1972	1973	1974
Consumer prices					
General level					
Average	13.6	34.7	58.5	60.3	24.2
Annual variation[a]	21.7	39.1	64.1	43.8	40.1
Food					
Average	16.5	41.7	63.1	55.2	15.1
Annual variation[a]	29.1	42.4	66.0	36.1	33.2
Wholesale prices					
Average	14.1	39.5	77.0	50.0	20.2
Annual variation[a]	26.8	48.2	76.0	30.8	36.7
Cost of construction					
Annual average	11.9	30.9	54.3	72.2	34.7
Annual variation[a]	13.3	42.7	58.5	61.3	55.5

SOURCE: National Institute of Statistics and Censuses.
[a] December, compared with the same month of the previous year.

The average increase of 20 per cent in wholesale prices was a result of the growth of 11 per cent in agricultural prices, 24 per cent in domestic non-agricultural prices and 37 per cent in imported goods. Meanwhile, the cost of construction estimated at average values grew by 35 per cent.

An accelerated evolution of prices during the year may be observed as from April. Indeed, the consumer price index, whose average growth rate fluctuated around 1.5 per cent during the period January-March, showed monthly variations of more than 2.5 per cent as from April and a maximum of 5.2 per cent in December. Consequently, there was an increase of 40 per cent between the months of December 1973 and December 1974.

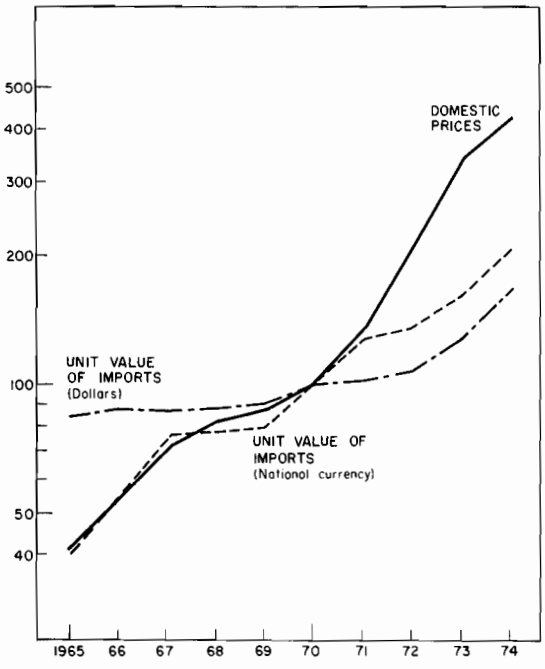
Wholesale prices developed along lines similar to consumer prices, since their monthly rate of growth during the period January-March was less than 0.5 per cent, but remained above 2.5 per cent in the next period, and rose rather more steeply at the end of the year.

Agricultural prices increased in all four quarters more slowly than prices of national and imported non-agricultural products; in the last quarter the increase in prices of local non-agricultural products was far greater than that of imported products, and thus came up to the level of the annual growth rate.

During 1973, the inflationary process slowed down as the year advanced; the annual average increase in prices was greater than the actual increase between the beginning and the end of the year. In 1974, however, the reverse occurred.

The factors of inflation were different from those of recent years. The exchange rate, meat prices and public service rates increased more slowly than the general level of prices and moderated the rise in prices, unlike the role which they had played in earlier periods when they had boosted the increases (see figure V). This was in

Figure V. Argentina: indexes of unit value of imports and of domestic prices
(Index: 1970 = 100)
Semi-logarithmic scale



response to the policy of redistribution applied by the Government and was aided by the situation of the livestock cycle, the favourable evolution of the external sector as far as exports were concerned, and fiscal policy.

The price policy was based on a price freeze as from June 1973 and on generalized control, and paralleled a wage agreement reached between the State and the workers' and entrepreneurial organizations. The Acta de Compromiso Nacional of 30 May 1973 laid down the amount of the wage increases, and the general lines of the income policies; from its introduction up to December 1973 prices were almost completely stabilized in contrast to the large-scale growth of the previous period.

As from the end of 1973, however, pressures had begun to accumulate with regard to this stabilization scheme. Increases in domestic demand and pressures on costs (mainly as a result of increased international prices), together with difficulties in the supply of some imported inputs, boosted price increases against the background of a strict freeze. Between June 1973 and March 1974, the wholesale price index of imported goods increased by 13 per cent, while the price index of domestic goods increased by less than 2 per cent and the index of national non-agricultural products by less than 1 per cent. In the circumstances, the strict freeze worked efficiently up to the beginning of 1974. In April, demands for wage increases materialized; they were a result of the fact that conditions of supply and demand had allowed some deviations as regards the frozen prices, and of the social and political desire not to stop the process of income redistribution. Authorization was thus given to transfer to prices part of the new wages and the higher cost of imported goods. However, most industrial entrepreneurs maintained that their rate of returns had decreased or had disappeared, and that increasingly large gaps were beginning to appear in the official price control and in supply. At the same time, the tendency towards inflexibility in supply for the domestic market became more pronounced, as a result of the progressive absorption of idle capacity, difficulties in the external supply of some inputs, certain speculative practices, and exports of a part of industrial output.

In the last few months, a more flexible scheme was adopted for the price policy. Without totally abandoning the price control, an attempt was made to seek a new balance in relative prices, although at a higher level.

These measures could eventually become part of an incomes policy aimed at providing an incentive to investment, eliminating the negative rate of returns declared by a number of enterprises and re-establishing the normal functioning of the marketing circuits.

(b) *Wages*

On the basis of the priority given to the growth of real wages, three general salary increases were granted in 1974, covering all wage-earners in the public and private sectors. The April increase consisted of 13 per cent of the wage and moreover, could not be less than 240 pesos; in June, an additional payment of half a month's wage or salary was decided upon; and in November, wages were readjusted by 15 per cent, with a minimum of 300 pesos. According to the policy of redistribution being followed, these increases aimed at a bigger improvement in the situation of the lowest-level wage-earners; this was why a fixed minimum was laid down for the increase.

The growth objective for real wages would appear to have been achieved, since the average increases were 9.4 per cent for the basic wage agreed upon for unskilled workers and 5.9 for skilled workers.

In the case of workers with families, the difference was greater, since the family wage showed a larger increase in the lower-income groups than the basic wage. In addition, and partly as a result of the lower unemployment index, the wages actually paid in some sectors would appear to have increased more than was established in the general wage increases.

If instead of annual averages the months of December 1973 to December 1974 are taken as reference periods, smaller increases in real wages may be observed and a standstill in the case of the skilled worker without dependants. This was due to price increases in the last part of the year (see table 170). Since this process became more accentuated during the month of January 1975, the Gran Paritaria Nacional (trade union association of employers and workers) composed of State representatives and representatives of workers' and entrepreneurial organizations, was convened in February to agree on the necessary readjustments to compensate for the deterioration in real wages since the last increase.

During 1974 the Labour Contract law was ratified, and laid down important improvements not connected with wages. Among other benefits, this law makes arrangements for more special leave (for births, marriage, etc.), and extends vacation periods; it increases the amounts of indemnities for dismissal and establishes a more favourable system for sick leave; it sets new norms for the work of women and establishes access to the enterprise's book-keeping system by wage-workers who receive commissions.

Table 170. Argentina: evolution of industrial wages[a]
(*Annual growth rate*)

Item	*1970*	*1971*	*1972*	*1973*	*1974*
Nominal average monthly wage[b]					
Skilled worker	15.6	36.4	44.9	72.1	31.4
Unskilled worker . . .	17.8	37.9	46.4	74.6	35.8
Real average monthly wage[c]					
Skilled worker	1.8	1.3	−8.5	7.4	5.8
Unskilled worker . . .	3.7	2.3	−7.6	8.9	9.3
Nominal wage (December)					
Skilled worker	13.9	43.4	48.1	65.1	38.2
Unskilled worker . . .	14.8	45.7	48.1	69.0	44.4
Real wage (December)					
Skilled worker	−6.5	3.1	−9.8	14.9	−1.4
Unskilled worker . . .	−5.7	4.7	−9.8	17.5	3.1

SOURCE: National Institute of Statistics and Censuses.
[a] Basic wages fixed by agreement in the Federal Capital.
[b] Sum of monthly wages and bonuses in the year (1960 = 100), divided by 13.
[c] Nominal monthly income deflated by consumer price index. Annual average.

(c) *Distribution of income and employment*

The target of the Three-Year Plan for 1974 was that the share of wage-earners in income should increase to 43.8 per cent compared with a percentage of 42.5 per cent in 1973. These figures are part of a progression which would bring the share of wage-earners up to 47.7 per cent in 1977, similar to that attained in 1955, during the second presidential period of General Perón. According to estimates by the Ministry of Economic Affairs, the 1974 objectives were surpassed during the year.

In addition to the redistribution among wage-earners and non-wage-earners, transfers of income within each social sector took place during 1974. Of the wage-earners, the lowest income sector benefited most, in view of the non-proportional method used for granting the increases. Consumption of food-stuffs, prices of which increased less than the average, is a bigger item in these groups; moreover, social benefits became cheaper (medical attention, social tourism, etc.) and the purchase of low-cost dwellings was subsidized.

On the other hand, the high-income groups, both wage-earners and non-wage-earners, suffered—particularly towards the end of the year—from the sharp increase in prices of some goods which form part of their normal consumption (non-frozen rents, prices and costs of vehicle maintenance, expenditure on recreation and summer vacations, etc.) since the price controls were stricter for the goods making up the "family basket".

As from April 1973, the unemployment rate underwent a steady decrease, reaching a rate of 2.4 per cent in October 1974 in the Federal Capital and Greater Buenos Aires. This is the lowest percentage on record since this information has been compiled (July 1963). In the cities of the interior, unemployment rates were also less than in previous periods.

BARBADOS

1. SOME FEATURES OF ECONOMIC TRENDS IN 1974

The outstanding developments which influenced economic trends in 1974 were the sharp rise in domestic prices, which reached a rate of 39 per cent annually; the increase of 49 per cent in the value of goods exported, resulting from the high international prices, mainly in respect of sugar, since the volume fell by 15 per cent; import restrictions and high inport prices which affected domestic supply; and the drop of 12 per cent in the sugar-cane harvest.

In these circumstances, estimates based on the limited information available indicate that during the year over-all production declined. The majority of economic activities, with the exception of tourism, show reduced growth rates, or in the best of cases, maintained their 1974 levels of production. Calculated at current prices it is estimated

that there was an increase of 23 per cent in the gross domestic product (see table 171).

As regards the inflationary process, the rate of increase of domestic prices has been rising since 1972. It rose from 11.8 per cent in 1972 to 16.9 per cent in 1973, and to 38.9 per cent in 1974. In 1974, increases were higher for household operations and furnishings (56 per cent) and foodstuffs and beverages (44 per cent), and occurred mainly during the early part of the year.

The increase in domestic prices was closely related to the increase in the prices of imported products, mainly food-stuffs, which account for a large share of consumption. Increases in wages, also helped to push up domestic costs and to increase demand pressure on production, which showed little elasticity.

2. THE PERFORMANCE OF SELECTED SECTORS

The sugar industry represents approximately 8 per cent of total production, whereas the contribution of agriculture for domestic consumption falls below this figure. In 1974 the sugar-cane harvest fell by 12 per cent, as a result of poor rainfall during the growing stage of the cane, and the lack of manpower during the reaping stage. However, since the unit yield of sugar increased during the year, the drop in sugar production was just about 2 per cent.

As regards the other agricultural products for which information is available, a general drop was observed in production, which in the case of yams and potatoes was 34 and 22 per cent respectively. Only in the production of poultry and milk was there some increase.

Tourism plays an important role in the economic activity of the country. In addition to the income it generates, which is higher than that received from the export of goods, it provides a large number of jobs and stimulates the development of other productive activities.

Information available for the period January to September, compared with that for the same period in the previous year, shows an increase of 6.5 per cent in the number of persons visiting the country. In this respect, the balance of payments for 1974 recorded an increase of 20 per cent in the inflow of foreign exchange as a result of tourist expenditure in the country, reflecting, in part, the increases in prices which occurred in that year.

As far as the value added by the Government sector is concerned, it is estimated that at current prices its growth rate was much lower than that of the total gross product in 1974, which indicates a marked deterioration in government activity expressed in real terms, in view of the increase in domestic prices. As at September, and comparing these figures with those for a same period in 1973, current expenditure had increased by 15 per cent whereas income, for the same period, rose by 9 per cent, thus increasing the current deficit. Furthermore, capital expenditure showed no major change compared with that of the previous year.

Towards the end of the year the Government increased the rates of some taxes and obtained external finance for infrastructure projects to stimulate the growth of production and provide jobs.

3. THE EXTERNAL SECTOR

In general, external transactions followed the pattern set by the movement of international prices. Higher prices for sugar and other export products meant an increase of 75 per cent in unit

Table 171. Barbados: gross domestic product at factor cost

Sector	*Millions of Barbados dollars*				*Growth rate (percentages)*		
	1970[a]	*1972*[a]	*1973*[b]	*1974*[b]	*1972*	*1973*[b]	*1974*[b]
Sugar	27.1	27.6	28.2	43.4	15.0	2.2	53.9
Domestic agriculture	13.2	16.6	...	...	18.6	...	...
Manufacturing	31.4	43.6	...	...	17.8	...	...
Construction	27.5	29.0	...	...	2.8	...	...
Distribution	71.2	84.0	105.2	134.1	7.4	25.2	27.5
Government	42.7	54.9	69.8	80.7	16.1	27.1	15.6
Transport and public utilities	20.9	27.6	...	...	15.0	...	...
Ownership of dwellings	11.1	13.4	...	...	9.8	...	...
Services	44.8	60.0	...	...	6.0	...	...
Total	*289.9*	*356.7*	*420.0*	*516.0*	*11.0*	*17.7*	*22.9*

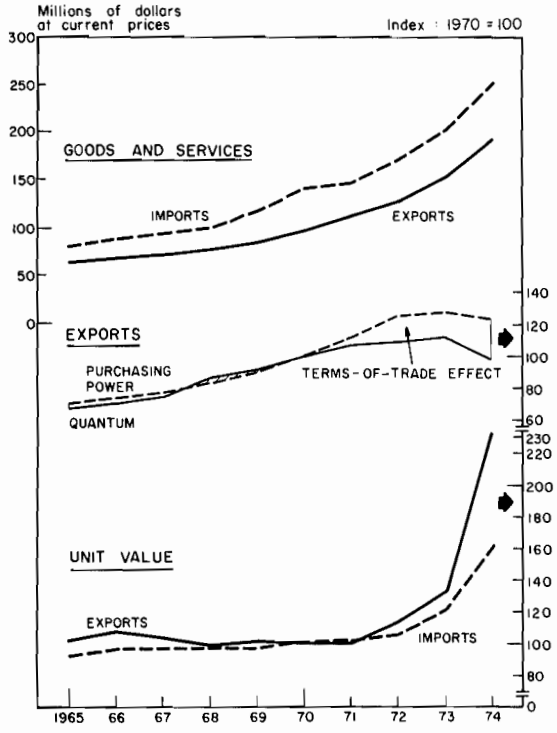
SOURCE: Economic Planning Unit, Barbados, *Economic Survey* (several issues).

[a] Provisional figures.
[b] Preliminary ECLA estimates.

values and one of 49 per cent in the total value of exports of goods. On the other hand, their volume fell by 15 per cent (see figure VI).

Meanwhile imports increased at a lower rate, 24 per cent. During the year restrictions were introduced, as a result of which their volume fell by 6 per cent; however, their prices increased by a little more than 30 per cent.

Figure VI. Barbados: trend of external variables
Natural scale



On the basis of part-year data up to August, with the exception of imports of fuels the value of which tripled, the rise was not so great in the others, in spite of the considerable increase in prices, as the purchases of meat, machinery and equipment clearly show.

In respect of exports, the increases in the value of sugar exports and its by-products, and in that of clothing exports were the most notable, on account of the favourable price situation.

An important feature of the country's external trade was the shift in direction observed during 1974, both in respect of exports and imports. Trade with the United Kingdom, traditionally the major trading partner (33 per cent of exports, and 23 per cent of total imports in 1973) dropped to second place after that with the United States. The share of trade with CARICOM also decreased in 1974, while that trade with Latin America acquired some importance, particularly in respect of imports. These changes in trade flows were dictated by conjunctural factors and reflected the changes observed in sugar exports and in petroleum imports.

In spite of the sharp rise in exports, which was twice the growth rate of imports, the trade deficit increased. This increase was offset, however, by larger net inflows from the travel account. Thus, the balance-of-payments current account closed at the end of 1974 with a deficit of 48 million SDRs, which is not much higher than in previous years (see table 172).

Meanwhile, the net inflow of non-compensatory capital remained at the same level as in recent years and international reserves showed no major change.

Table 172. Barbados: balance of payments
(Millions of SDR units)

	1970	*1971*	*1972*	*1973*	*1974*[a]
Current account					
Exports of goods and services	97.6	112.7	120.0	126.4	161.6
Goods FOB	35.2	32.0	34.1	38.9	58.2
Services	62.4	80.7	85.9	87.5	103.4
Transport	7.4	12.5	12.3	12.5	14.5
Travel	40.4	51.4	57.7	58.0	69.8
Imports of goods and services	141.3	147.5	158.0	169.5	208.3
Goods FOB	105.2	109.3	116.3	125.4	155.4
Services	36.1	38.2	41.7	44.1	52.9
Transport	17.4	18.9	19.9	23.0	28.4
Travel	3.5	4.2	4.4	5.1	6.2
Net external investment income	−3.2	−4.6	−6.1	−6.0	−6.9
Profits	−4.3	−5.0	−6.7	−6.6	−7.2
Interest	1.1	0.4	0.6	0.6	0.3
Net private transfer payments	4.4	4.3	4.3	5.0	5.5
Balance on current account	−42.5	−35.1	−39.8	−44.1	−48.1

Table 172 (*continued*)

	1970	1971	1972	1973	1974[a]
Capital account					
Net external financing ($a + b + c + d + e$)	42.5	35.1	39.8	44.1	48.1
(a) Net external non-compensatory capital	24.6	29.1	23.6	35.1	
Direct investment	8.7	12.7	15.2	11.0	
Long- and medium-term loans	5.6	7.7	5.0	15.0	
Amortization payments	–	–	–	–	
Short-term liabilities	9.5	7.7	2.1	7.8	48.1
Official transfer payments	0.8	1.0	1.3	1.3	
(b) Domestic non-compensatory capital or assets	−10.9	−5.4	−2.7	3.2	
(c) Errors and omissions	27.5	15.5	18.8	6.9	
(d) Allocation of SDRs	–	1.4	1.4	–	–
(e) Net compensatory financing (increase −)	1.3	−5.5	−1.3	−1.1	–
Balance-of-payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	–	–	–	–	–
Amortization payments	–	–	–	–	–
Movements of foreign exchange reserves (increase −)	3.3	−4.1	0.1	−1.6	–
Movements of gold reserves (increase −)	−2.0	–	–	0.2	–
SDRs (increase −)	–	−1.4	−1.4	0.3	–

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26. [a] Estimates based on official statistics.

BOLIVIA[2]

The outstanding economic trends in Bolivia in 1974 were the increased growth of some productive sectors, the performance of the external sector which showed marked fluctuations, and once again, increases in prices and changes in the price system. Keeping to this order, the major economic aspects characteristic of these trends are described below.

1. THE PRODUCT AND ITS SECTORAL COMPOSITION

Early in the current decade it was observed that the rate of growth of economic activity had shown some degree of acceleration, judging from the growth rate of the product which was 5.7 per cent in 1974, compared with 5.4 per cent in 1973 and 4.5 over the two-year period 1970-1972 (see table 173 and figure VII). The growth noted is the result of rather unequal performances by the economic sectors. Whereas agriculture continued to develop at very modest rates (3.5 per cent) and mining had obviously stagnated, the productive sectors of basic and other services, e.g., commercial and financial services, showed much higher growth rates.

The growth rate of the construction sector (14 per cent) may be considered important because of the ability of this sector to create employment opportunities and its spread effect on other activities. However, its small share of the total product (less than 5 per cent) and the relatively high proportion absorbed by housing limit its power to reactivate economic activity. Moreover, Latin American experience shows that only a long period of sustained growth in this sector could succeed in bringing about important changes in the economic infrastructure.

Recently, the highest growth rates were experienced by the service sectors located in the urban centres. In fact, the rate of growth of tertiary activities was as high as 7.1 per cent which, compared with the 4.2 per cent growth rate of the goods producing sectors, left no doubt as to the persistence of the structural heterogeneity referred to whenever Bolivian economic activity is analysed.

Thus, the composition of the product over time is tending increasingly towards the production of

[2] See, in Part One of this *Survey*, the section dealing with Bolivia, in the chapter on inflation.

Table 173. Bolivia: gross domestic product at factor cost, by sector of economic activity

	Millions of pesos at 1960 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970-1972*	*1973*	*1974*[a]
Agriculture	1,901.1	2,073.3	2,146.0	16.9	15.8	3.4	2.1	3.5
Mining	1,670.0	1,717.8	1,717.8	14.9	12.6	–0.1	3.0	–
Manufacturing . . .	1,446.4	1,668.4	1,768.9	12.9	13.0	4.1	6.5	6.0
Construction	507.0	564.6	643.6	4.5	4.7	1.9	7.2	14.0
Subtotal goods . .	*5,524.5*	*6,024.1*	*6,276.3*	*49.2*	*46.2*	*2.4*	*4.0*	*4.2*
Electricity, gas and water	218.0	268.2	284.3	1.9	2.1	6.0	9.6	6.1
Transport and communications . .	995.5	1,144.7	1,213.3	8.9	8.9	4.6	5.0	6.0
Subtotal basic services	*1,213.5*	*1,412.9*	*1,497.6*	*10.8*	*11.0*	*4.9*	*5.9*	*6.0*
Commerce and finance .	1,265.4	1,591.4	1,734.8	11.3	12.8	8.4	7.0	9.0
Government	1,021.0	1,373.3	1,441.9	9.1	10.6	11.5	8.2	5.0
Ownership of dwellings .	978.0	1,066.0	1,130.0	8.7	8.3	1.4	6.0	6.0
Miscellaneous services .	1,231.6	1,389.0	1,500.1	11.0	11.0	3.7	4.8	8.0
Subtotal other services	*4,496.0*	*5,419.7*	*5,806.8*	*40.0*	*42.8*	*6.4*	*6.5*	*7.1*
Total	*11,234.0*	*12,919.8*	*13,656.3*	*100.0*	*100.0*	*4.5*	*5.4*	*5.7*

SOURCES: 1970-1972: ECLA calculations based on figures supplied by the Ministry of Planning and Coordination; 1973: ECLA estimates based on data from the same source; 1974: provisional ECLA estimates based on incomplete data from official sources.

Note: As the individual activities and the totals were calculated independently, the sum of the former does not correspond exactly with the latter.

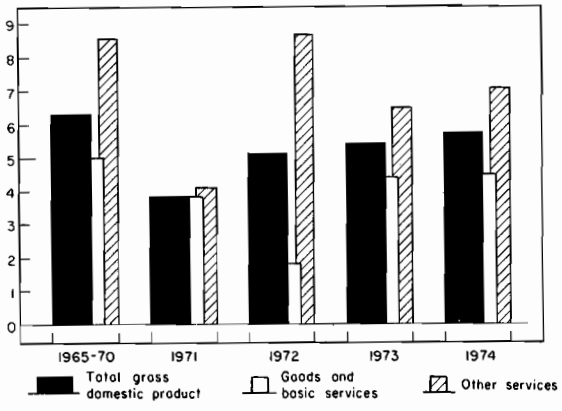
[a] Preliminary figures.

services whose share has increased from 40 per cent in 1970 to 42.8 per cent in 1974, whereas the relative importance of basic activities fell from 49.2 per cent to 46.2 per cent over the same period (see table 173).

2. THE SUPPLY OF GOODS

During 1974, total supply grew in real terms by 8.8 per cent, a figure considerably higher than that recorded in previous years (see table 174). This higher growth rate is attributable to the extraordinary increase in the volume of imports (22.6 per cent), for as pointed out above, the gross domestic product only increased by 5.7 per cent.

Figure VII. Bolivia: growth of gross domestic product
(Annual growth rates)
Natural scale



As a result, the import coefficient rose from 20.9 per cent in 1970 to 26.3 per cent in 1974. The increasing openness of the Bolivian economy is reflected in its greater dependence on imported supplies; the fact that this has resulted mainly from the increase in imports of consumer goods (87 per cent) and intermediate goods (129 per cent), and to a lesser extent from the increase in imports of capital goods (54 per cent),[3] is an indication that such dependence is growing, and this could lead to serious external imbalances if exports should not continue to expand at a similar rate.

3. THE COMPOSITION OF DEMAND

Aspects of greater importance with regard to the elements of demand are the drop in the physical volume of exports (–4.4 per cent), the sustained increase in gross domestic investment

[3] Estimates by the National Accounts Department of the CONEPLAN Secretariat, based on data provided by the Central Bank.

Table 174. Bolivia: total supply and demand

	Millions of pesos at 1970 prices			Structure (percentages)		Annual growth rate (percentages)		
	1970	1973[a]	1974[a]	1970	1974[a]	1970-1972	1973[a]	1974[a]
Total supply	*14,604*	*17,047*	*18,552*	*120.9*	*126.3*	*4.9*	*6.1*	*8.8*
Imports[b]	2,524	3,155	3,869	20.9	26.3	7.0	9.2	22.6
Gross domestic product	12,080	13,892	14,683	100.0	100.0	4.5	5.4	5.7
Total demand	*14,604*	*17,047*	*18,552*	*120.9*	*126.3*	*4.9*	*6.1*	*8.8*
Exports[b]	2,504	3,149	3,009	20.7	20.5	10.2	3.5	-4.4
Domestic demand	12,100	13,898	15,543	100.2	105.9	3.8	6.7	11.8
Gross domestic investment	1,880	2,337	2,758	15.6	18.8	-1.3	27.6	18.0
Gross fixed investment	1,666	2,106	...	13.8	...	...	...	...
Public	1,053	...	...	8.7	...	...	...	...
Private	613	...	...	5.1	...	...	...	...
Total consumption	10,220	11,516	12,785	84.6	87.1	4.7	5.0	10.5
General government	1,351	1,677	1,845	11.2	12.6	8.5	14.0	10.0
Private	8,869	9,884	10,940	73.4	74.5	4.1	3.5	10.6

SOURCES: 1970-1972: ECLA calculations based on figures supplied by the Ministry of Planning and Co-ordination; 1973: ECLA estimates based on data from the same source; 1974: provisional ECLA estimates based on incomplete data from official sources.

Note: The figures for exports and imports of goods and services were taken from balance-of-payments data expressed in dollars at current prices, which were converted to constant 1970 values by deflation, using price indexes calculated by ECLA for the purpose.

[a] Preliminary figures.

[b] Goods and services, excluding factor payments.

(18 per cent) and the unprecedented increase in consumption in the Bolivian economy (see table 174).

The fact that estimates of previous variations are preliminary, and could be subject to modifications in the light of more complete information, must be borne in mind. Thus, for example, the sharp changes in prices and the scarcity of appropriate deflator indexes, are *per se* a source of inaccuracy, and in the case of exports, a more accurate calculation of the volume of contraband goods could lead to adjustment in the drop noted.

In this connexion, the growth in investment could be shown in somewhat greater detail by preparing a complete inventory of private sector capital formation. In any event, if the rate noted were corroborated, this would be a clear pointer to greater future dynamism in economic activity.

As regards consumption, its high rate of growth can be traced, in the main, to the increase in imports of consumer goods. In fact, during 1974 imports of consumer goods totalled 122 million dollars and, as stated previously represented 26 per cent of total imports and approximately 10 per cent of private consumption. Since a considerable part of this figure is directed mainly to the satisfaction of the needs of high-income urban groups, it can be concluded that the consumption of the majority of the population grew at a lower rate than the 10.6 per cent noted for total private consumption.

4. THE EXTERNAL SECTOR

There is no doubt that the changes of greatest importance took place in this sector of the Bolivian economy. Its analysis would require a distinction to be made between movements in real terms and changes expressed in terms of current prices; such a distinction reveals highly unequal results.

The marked growth of 98.5 per cent in the current value of exports exercised great influence not only on the variables linked directly with foreign trade, but also on a large area of economic activity (see table 175). This growth can be explained exclusively by the increase in export prices, for the export volume decreased, as was mentioned earlier.

The extraordinary supply of foreign exchange stemming from the growth of exports resulted in major increases in the value and volume of imports. In fact, the corresponding rates increased to 51.1 per cent and 22.6 per cent respectively.

As a result of the movements mentioned above, there was a positive trade balance of SDR 141 million in contrast to the virtual equilibrium of previous years. The balance on current account

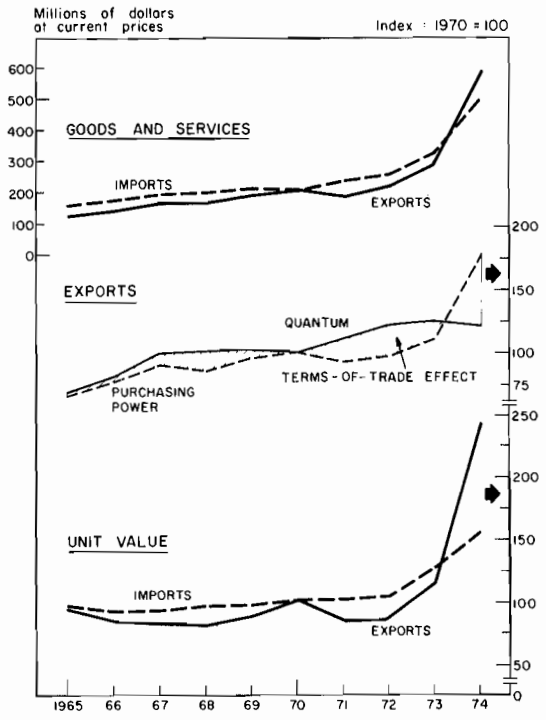
Table 175. Bolivia: balance of payments
(*Millions of SDR units*)

	1970	*1971*	*1972*	*1973*	*1974*[a]
Current account					
Exports of goods and services	210.3	198.3	206.9	247.7	491.8
Goods FOB	195.7	181.9	187.1	226.6	465.6
Services	14.6	16.4	19.8	21.1	26.2
Transport	1.7	1.7	2.4	2.3	3.6
Travel	2.5	3.8	7.9	9.6	11.5
Imports of goods and services	210.7	227.5	240.1	277.3	419.0
Goods FOB	166.2	181.4	180.3	209.6	324.3
Services	44.5	46.1	59.8	67.7	94.7
Transport	28.6	29.3	32.4	42.2	63.6
Travel	3.9	5.8	9.7	8.0	10.1
Net external investment income	−25.0	−17.0	−20.0	−19.2	−17.5
Profits	−17.0	−8.4	−5.6	−5.4	−6.7
Interest	−8.0	−8.6	−14.4	−13.8	−10.8
Net private transfer payments	1.5	2.1	4.5	4.1	4.2
Balance on current account	−23.9	−44.1	−48.7	−44.7	59.5
Capital account					
Net external financing (*a* + *b* + *c* + *d* + *e*)	23.9	44.1	48.7	44.7	−59.5
(*a*) Net external non-compensatory capital	41.7	67.7	96.1	45.7	68.6
Direct investment	−75.9	1.9	−9.7	3.9	1.1
Long- and medium-term loans	131.2	82.6	129.5	67.3	123.3
Amortization payments	−20.4	−22.0	−28.3	−40.0	−51.7
Short-term liabilities	4.4	0.2	−3.3	5.7	−9.1
Official transfer payments	2.4	5.0	7.9	8.8	5.0
(*b*) Domestic non-compensatory capital or assets	−6.1	1.7	−15.7	−0.3	−22.7
(*c*) Errors and omissions	−13.0	−31.6	−31.1	−5.9	−5.9
(*d*) Allocation of SDRs	4.9	4.0	3.9	–	–
(*e*) Net compensatory financing (increase −)	−3.6	2.3	−4.5	5.2	−99.5
Balance-of-payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	2.2	8.8	11.1	22.9	...
Amortization payments	−0.2	−4.2	−8.4	−9.0	...
Movements of foreign exchange reserves (increase −)	0.1	−1.8	−5.8	−8.7	...
Movements of gold reserves (increase −)	−3.0	−0.8	−0.8	−1.8	...
SDRs (increase −)	−2.7	0.3	−0.6	0.8	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 25.
[a] Estimates based on official statistics.

also showed a surplus of SDR 60 million, completely reversing the situation as it stood in the past. Capital account flows meant a net increase of SDR 40 million, which together with the surplus on current account resulted in an increase in international reserves of SDR 100 million. A decisive part in this result was played by long-term and medium-term loans obtained by the Government which amounted to SDR 123 million. Without this increased indebtedness the movements in the balance of payments would have resulted in a reduction in international reserves, in spite of the favourable situation in external trade. This paradox can be explained, on the one hand, by the increase in the imports of consumer goods which, as stated earlier, amounted to 122 million dollars, an increase of 87 per cent compared with the previous year, and on the other, by the increase in export smuggling and in private deposits made in foreign banks, which the Central Bank estimated at 20 and 25 million dollars respectively for 1974. The use of foreign exchange for importing non-

Figure VIII. Bolivia: trend of external variables
Natural scale



essential goods, and the outflows already mentioned were the most flagrant ways of transferring resources out of the country.

5. INFLATIONARY PRESSURES

The consumer price index, taking account of the averages for 1973 and 1974, showed an increase of 62.8 per cent which reflected the continuous inflationary pressure (see table 176).

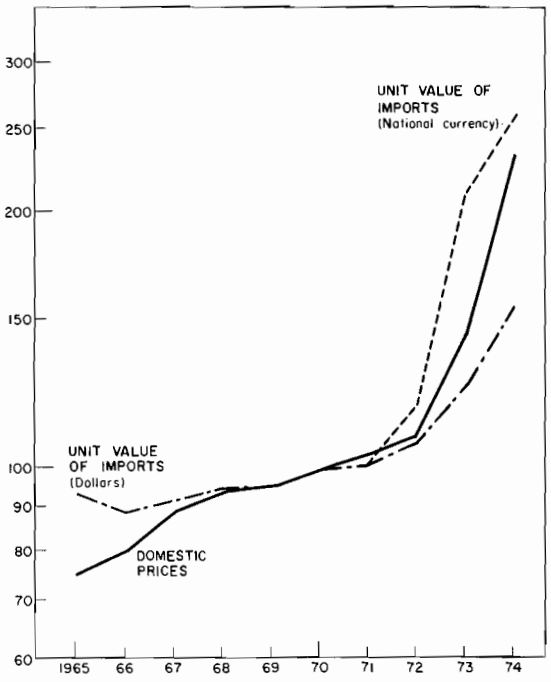
However, as regards prices, the increase during 1974 (December 1974 compared with December 1973) was 38.8 per cent; moreover, during the first two months of the year it was 29.9 per cent. This leads to the conclusion that from March 1974 the inflationary process was brought under control, for during the remaining 10 months of the year prices increased by only 6.8 per cent. This conclusion is not wholly valid, however, since the index in question does not take account of imported products whose prices and quantities increased considerably during 1974. Such an indicator does not, therefore, reflect the true dimension of the impact of imported inflation which has become more acute in recent months. Figure IX shows the trends in import prices expressed in dollars and in national currency, and

Table 176. Bolivia: changes in the consumer price index[a]
(Percentages)

	Total	*Food*	*Housing*	*Clothing*	*Other*
1973					
December to December	34.9	44.8	13.5	32.5	15.8
Between annual averages	31.5	34.9	15.0	38.5	29.6
1974					
December to December	38.8	44.7	19.5	36.0	31.0
Between annual averages	62.8	81.7	22.1	46.1	35.4
1974 (with reference to December 1973)					
January	15.9	21.1	2.2	8.2	10.7
February	29.9	39.4	5.4	13.9	22.7
March	32.6	42.4	6.5	17.8	23.5
April	33.3	42.6	7.6	20.3	24.7
May	34.5	43.9	9.0	22.1	26.0
June	37.7	48.4	9.0	22.8	27.9
July	38.1	47.3	17.3	23.9	26.4
August	38.6	46.1	19.1	30.3	27.7
September	35.7	41.5	19.1	30.3	27.7
October	34.6	39.1	18.4	33.9	28.9
November	37.7	43.8	19.1	33.8	28.9
December	38.8	44.7	19.5	36.0	31.0

SOURCE: National Institute of Statistics, CONEPLAN.
[a] Consumer price index for middle-income and low-income groups in La Paz (1966 = 100).

Figure IX. Bolivia: indexes of unit value of imports and of domestic prices
(Index: 1970 = 100)
Semi-logarithmic scale



the relationship between them and trends in domestic prices.

Furthermore, the systematic trend of rising prices for food-stuffs, compared with other items in the index, has reappeared. On account of this, its weighting in the basket of goods is underestimated, and a correction of this would result in greater increases in the level of prices.

From the point of view of liquidity in the economic system the conditions which permitted the resurgence of inflation in the past year remained unchanged. In fact, private sector credit increased by 60 per cent in 1974 compared with 68 per cent in the previous year.[4] The increase in national currency caused by the accumulation of international reserves was 828 per cent during the first nine months of the year (54 per cent of the total expansion), compared with a reduction over the same period in the previous year.[5] For this reason, the reduction in credit to the Government is of no significance. Global expansion amounted to 40 per cent during the period January-September 1974, somewhat higher than that of 1973 which only amounted to 13.1 per cent. Greater liquidity in the economic system would appear to be inconsistent with a reduction in the inflationary rate in 1974.

The smaller rises in prices appear to be more directly related to the increase in the supply of goods. Total supply, as was pointed out, showed an increase of 8.8 per cent in real terms; this unusual elasticity, brought about by the increase in imports, countered the inflationary effects of greater global liquidity.

On the other hand, the concentration of income resulting from the external economic situation, and the domestic inflationary process itself reduced the effective demand of the wage-earning sector whose income was rigorously controlled. This factor acquires greater significance in the light of the fact that in January 1975 the Government decreed a drastic reduction in import tariffs, basing the measure on the need to preserve the purchasing power of the groups most affected by inflation.

6. SHORT-TERM PROSPECTS

The principal determinant of decreasing rates of inflation would appear to lie in the future performance of the external sector. The eminently exogenous nature of its trends make its impact difficult to control and its recently acquired financial importance gives it a unique role in the operation of the economic process and, of course, in the inflationary process.

Apart from its capacity to make supply more elastic through increasing imports, the external sector has acquired enormous importance in financing the government budget.

The fall in the share of revenue from usual financial sources (internal revenue and customs duties) is well known, as opposed to the increase in royalties and taxes, mainly related to export prices. Note that 50 per cent of revenue in 1974 originated from these sources (see table 177).

Although trends in external trade are unlikely to become definitely unfavourable in the immediate future, there is the possibility of a relative deterioration; drops in the prices of some raw materials and increases in the prices of manufactured products are signs of this. To the extent that government financing is based on revenue from external trade, the fluctuations usually characteristic of this sector could create difficulties in the financial sphere of the Bolivian economy. Although it is true that revenue projected in the 1975 budget for royalties and export taxes is relatively modest, its share is nevertheless a fairly significant one.

[4] Banco Central de Bolivia, "*Balance consolidado del sistema monetario*", *Boletín estadístico*, January 1975.
[5] International Monetary Fund, *International Financial Statistics*, February 1975.

Table 177. Bolivia: national treasury operations
(Millions of Bolivian pesos at current prices)

	1973	1974	1975[a]	Rates of increase	
				1974	1975
Income	*2,469.5*	*5,104.3*	*6,564.9*	*106.7*	*28.6*
Internal revenue	905.7	1,299.1	1,462.5	43.4	12.6
Customs revenue	517.4	947.3	1,180.0	83.1	24.6
Mining royalties	190.6	903.3	596.8	373.9	−43.9
Oil and gas royalties	278.5	883.3	795.9	217.2	−9.9
Additional tax on exports	452.2	801.0	1,010.4	77.1	26.1
Other income	125.1	270.3	1,519.3	116.1	462.1
Expenditure	*2,882.0*	*5,544.8*	*6,564.9*	*92.4*	*18.4*
Personal services	1,332.2	2,313.7	2,811.3	73.7	21.5
Non-personal services, materials and supplies	386.9	553.5	825.3	43.1	49.1
Fixed and financial assets	119.9	101.9	195.0	−15.0	91.4
Public debt	433.4	679.1	717.7	56.7	5.7
Transfers and contributions	549.5	1,575.1	1,820.4	186.6	15.5
Other expenditure	60.1	321.5	195.2	434.9	−39.0

SOURCE: Banco Central de Bolivia, Boletín Estadístico, December 1974.

[a] Ministry of Finance, Budget Office, Public Sector Budget.

The expenditure budget is equally conservative. Personal services (wages and salaries) and transfers and contributions which are the most important items, are forecast as having only modest increases.

The Government's wages policy will be a crucial element of its economic policy and, in particular, its anti-inflation policy. The various restrictions on State action could make it difficult to reconcile lowering inflation rates with ensuring that the international reserves accumulated during 1974 remain in the country.

BRAZIL[6]

During 1974 the Brazilian economy underwent a variety of changes. For all its rapid growth (to which the various sectors contributed in very different degrees), the economy, and particularly the external sector, were directly affected by the world crisis. Moreover inflation, control of which was always one of the main objectives of the country's economic policy, increased sharply in 1974 after almost a decade of satisfactory progress.

This summary of the trend of the Brazilian economy concentrates on the main real variations in total supply and demand, the principal productive sectors and foreign trade.

1. SUPPLY AND DEMAND IN RESPECT OF GOODS

Although lower than in previous years, the growth of over-all supply was 10.8 per cent in 1974. This substantial and repeated increase is attributable to the growth of both the product (9.6 per cent) and imports (24 per cent). Because imports constantly increased more than the product, the import coefficient rose from 7 per cent in 1970 to 10.2 per cent in 1974 (see table 178).

As regards total demand, the drop in the real value of exports (−1.7 per cent) is striking, particularly compared with the rapid increases during previous periods (8.9 per cent in 1970–1972 and 16.1 per cent in 1973).

Although the share of exports in the economy as a whole is fairly small (about 6 per cent), its reduction is nevertheless significant in that it

[6] See, in Part One of this *Survey*, the section dealing with Brazil in the chapter on inflation.

affects an important sector of economic activity. The decline in the export coefficient in 1974 reflects a deviation in the trend, which is attributable to certain areas of production.

The high growth rate of the economy was attributable to the very rapid growth of investment; the investment coefficient rose from 21 per cent in 1970 to 26 per cent in 1974. The annual growth rate of gross fixed investment, however, declined to 14.1 per cent in 1974, after having risen from 16.3 per cent in 1970-1972 to 20.4 per cent in 1973. Although there was some decline in capital formation in 1974, its growth rate was considerably higher than that of the product (see table 178) and continued to provide a valuable incentive to production.

The growth rate of total consumption remained at the level of previous years, although its principal components followed different trends. For example, the growth rate of government consumption declined from 15.8 per cent in 1973 to 8.6 per cent in 1974, whereas private consumption rose from 8.6 per cent to 11.1 per cent during the same period. Although these changes represent large amounts, they merely revert to the earlier trend of both variables which had changed momentarily the year before.

2. PRODUCTIVE SECTORS

As already mentioned, the rapid growth of the product (9.6 per cent), although lower than in previous years, was the outcome of very different trends in the mainly goods-producing sectors (see table 179).

The substantial expansion of the agricultural sector (8.5 per cent) contrasts with the loss of dynamism of the manufacturing industry, which expanded by only 7.1 per cent in 1974, compared with 15.8 per cent in 1973 and 12.7 per cent in 1970-1972. As in the past, these two sectors registered quite different trends without there being any causal relationship to explain the phenomenon. The construction sector maintained its high rate of growth.

The over-all growth rate of the goods-producing sector was 8 per cent in 1974, which is appreciably lower than in previous years.

It must be emphasized that the increase in the production of agricultural goods is mainly attributable to the increased production of coffee, soya and wheat. Livestock production showed no variation from the previous year.

The decline in the industrial product derives from the lower growth rates of all its component

Table 178. Brazil: total supply and demand

	Millions of cruzeiros at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970-1972*	*1973*	*1974*[a]
Total supply	*221,041*	*308,341*	*341,639*	*107.0*	*110.2*	*11.5*	*12.2*	*10.8*
Imports[b]	14,476	25,587	31,742	7.0	10.2	20.3	22.0	24.1
Gross domestic product	206,565	282,754	309,897	100.0	100.0	10.8	11.4	9.6
Total demand	*221,041*	*308,341*	*341,639*	*107.0*	*110.2*	*11.5*	*12.2*	*10.8*
Exports[b]	13,660	18,795	18,465	6.6	6.0	8.9	16.1	-1.7
Domestic demand	*207,381*	*289,546*	*323,174*	*100.4*	*104.3*	*11.7*	*12.0*	*11.6*
Gross fixed investment	43,441	70,711	80,685	21.0	26.0	16.3	20.4	14.1
Public	8,273	...	...	4.0	...	...	...	...
Private	35,168	...	...	17.0	...	...	...	...
Construction	22,391	...	...	...	...	...	...	...
Machinery and equipment	21,050	...	...	...	...	...	...	...
Total consumption	163,940	218,835	242,489	79.4	78.2	10.4	9.5	10.8
General government	20,512	28,482	30,931	9.9	10.0	9.5	15.8	8.6
Private[c]	143,428	190,353	211,558	69.5	68.2	10.5	8.6	11.1

SOURCES: 1970-1973: ECLA calculations based on figures published in *Sistema de contas nacionais, metodologia e quadros estatísticos* (Getulio Vargas Foundation, September 1974); 1974: ECLA estimates based on official statistics from the same source.

Note: The figures for exports and imports of goods and services were taken from balance-of-payments data expressed in dollars at current prices, which were converted to constant 1970 values by deflation, using price indexes calculated by ECLA for the purpose.

[a] Preliminary figures.

[b] Goods and services, excluding factor payments.

[c] Including increase in stocks.

Table 179. Brazil: gross domestic product at factor cost, by sector of economic activity

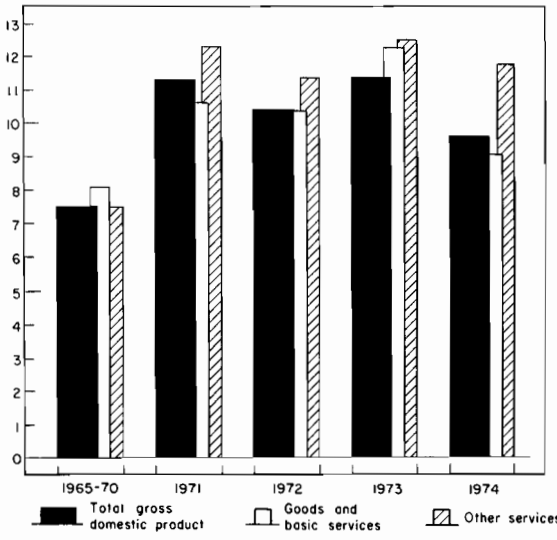
	Millions of cruzeiros at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970-1972*	*1973*	*1974*[a]
Agriculture	25,082	30,218	32,785	14.3	12.3	7.9	3.5	8.5
Mining	1,574	1,982	...	0.9	...	6.6	10.7	...
Manufacturing	43,471	63,931	68,470	24.8	25.6	12.7	15.8	7.1
Construction	10,167	14,372	15,983	5.8	6.0	10.6	12.5	11.2
Subtotal goods	*80,294*	*110,503*	*119,379*	*45.8*	*44.7*	*11.0*	*12.0*	*8.0*
Electricity, gas and water	4,106	5,717	6,405	2.3	2.4	11.3	12.5	12.0
Transport and communications	10,313	13,778	16,051	5.9	6.0	8.3	14.0	16.5
Subtotal basic services	*14,419*	*19,495*	*22,456*	*8.2*	*8.4*	*9.1*	*13.6*	*15.2*
Commerce and finance	38,232	53,821	59,740	21.8	22.4	...	12.5	11.0
Government	15,182	...	...	8.7	...	...	...	...
Ownership of dwellings	14,969	...	...	8.5	...	...	...	...
Miscellaneous services	12,429	...	...	7.1	...	...	...	...
Subtotal other services	80,812	...	...	46.0	...	...	...	...
Total	*175,526*	*240,215*	*263,275*	*100.0*	*100.0*	*10.8*	*11.4*	*9.6*

SOURCES: 1970-1973: ECLA calculations based on figures supplied by the Getúlio Vargas Foundation; 1974: ECLA estimates based on statistics from the same source.
[a] Preliminary figures.

Note: As the individual activities and the totals were calculated independently, the sum of the former does not correspond exactly with the latter.

parts, especially metal manufactures and machinery, chemicals, textiles, clothing and footwear. The so-called dynamic industries continued to expand more rapidly than any others in the sector, but without attaining the high growth rate of previous years. Motor vehicle production rose by 17.7 per cent, for example, compared with an average of 21 per cent for the period 1968-1973.

Figure X. Brazil: growth of gross domestic product
(Annual growth rates)
Natural scale



The slight decline in over-all economic growth is also attributable to the slower growth of the services sectors, which was 10.1 per cent in 1974 compared with 14.4 per cent in 1973 and 11 per cent during the period 1970-1972. The relative weight of these sectors with respect to the product was over 46 per cent.

Furthermore, the sectors producing basic services for the most part registered a fairly high growth rate, largely because of the real expansion of the transport and communications sector (16.5 per cent) and the rapid expansion of the electricity, gas and water sector (12 per cent). However, this growth did not have a greater quantitative impact because of the relatively small weight of these sectors in the economy, inasmuch as their share of the product was not more than 8.4 per cent (see table 179)

3. THE EXTERNAL SECTOR AND BALANCE OF PAYMENTS

The external sector is particularly important in Brazil's economy since, on the one hand, it is one of the cornerstones of the country's development style and, on the other, the world crisis has brought about far-reaching changes in foreign trade.

The current value of exports of goods in dollar terms rose by 28.5 per cent in 1974, thanks entirely to the 29 per cent increase in prices during the period. With regard to goods exported, the trend of industrial products differs from that of basic primary products. Whereas the former increased in value by over 50 per cent, the latter did so by only 17 per cent.[7] The drop in exports of coffee (from 1,244 million dollars in 1973 to 887 million in 1974) was partly responsible for this slower growth rate. Table 180 shows the trend in the value and volume of the principal agricultural export products and the different direction of the variations in several important items.

The current value of imports of goods rose by 102 per cent in 1974, owing to a 57.5 per cent increase in prices and 28.5 per cent increase in volume (see figure XI).

Special mention must be made of the higher price of petroleum, which in 1974 rose to four times that of 1973 while the volume imported declined by 2.2 per cent. The share of petroleum in total imports of goods was 22 per cent and its absolute value was around 2,500 million dollars.[8]

Moreover, as shown in figure XII, the trend of import prices expressed in national currency has closely followed that of domestic prices. Thus, the extraordinary increase noted in 1974 coincided with an upsurge in inflation.

In spite of the high prices of imports, the increase in the physical volume imported over previous years was such that the external sector served as a real source of supply of goods and services and was even able to meet the exceptional demand for imported products in the first half of 1974, which was largely due to the tendency to accumulate stocks in the expectation of further price increases.[9] In other words, contrary to what

[7] Estimates of the Getúlio Vargas Foundation on the basis of values expressed in dollars.

[8] According to official estimates, deposits discovered in 1974 will enable the country to be self-sufficient in petroleum by the end of the 1970s.

[9] See the section on inflation in Brazil.

Figure XI. Brazil: trend of external variables
Natural scale

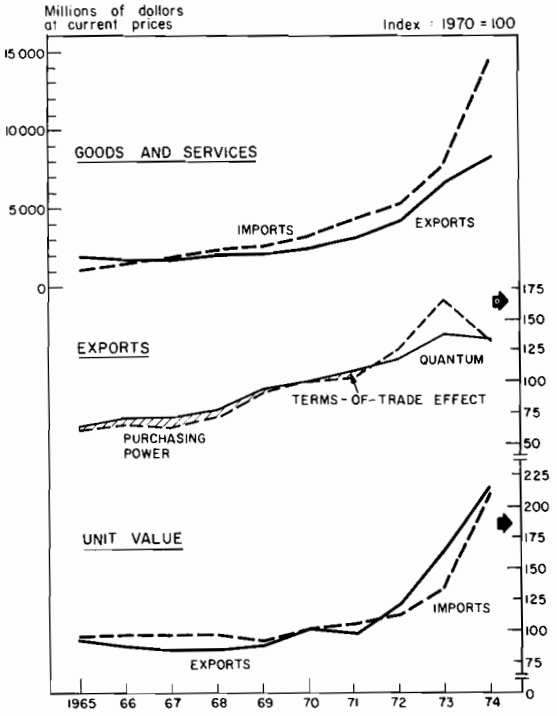
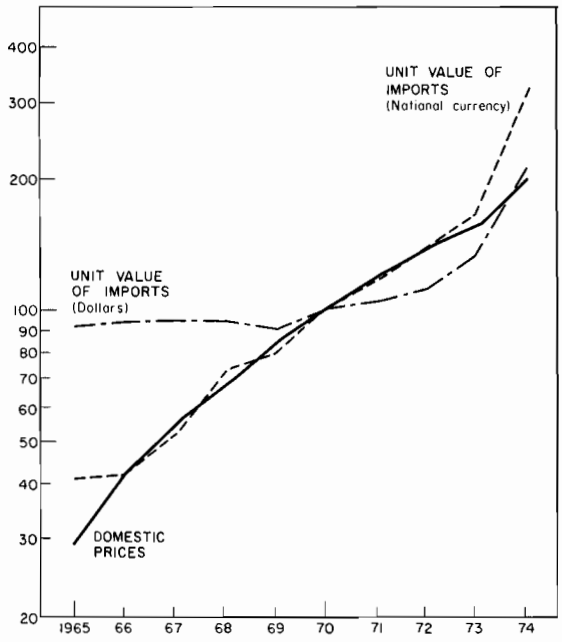


Table 180. Brazil: main agricultural exports

Product	FOB values			Volume		
	Thousands of dollars		Percentage variation	Tons		Percentage variation
	1973	1974		1973	1974	
Coffee . .	1,224,272	877,433	−29.5	1,071,377	692,001	−35.4
Soya . . .	916,788	888,076	−3.1	3,367,632	4,755,101	41.2
Sugar . . .	552,711	1,258,658	127.7	2,797,926	2,250,508	−19.6
Cotton . .	234,094	101,526	−56.6	383,833	174,360	−55.7
Meat . . .	148,547	29,532	−80.1	98,530	19,170	−80.5
Cocoa . . .	88,522	210,002	137.2	82,774	129,865	56.9
Sisal . . .	59,445	114,130	92.0	160,241	139,013	−13.2
Tobacco . .	58,458	98,981	69.3	63,599	91,442	43.8
Wool . . .	45,215	43,786	−3.2	17,792	17,996	1.1

SOURCES: Carteira de Comércio Exterior (CACEX), and Banco do Brasil (February 1975).

Figure XII. Brazil: Indexes of unit value of imports and of domestic prices
(Index: 1970 = 100)
Semi-logarithmic scale



might have been expected from the critical situation of international trade, there was no great obstacle to imports thanks to the high external payment capacity of the Brazilian economy.

The various changes in price and volume of exports and imports in 1974 led to a substantial trade deficit, compared with a small surplus in 1973. The deficit amounted to SDR 3,793 million which was equal to 53 per cent of total exports (see table 181).

The increase in non-factor service payments and profits and interest on external capital helped to swell the deficit on current account to SDR 5,901 million, which is equal to 82.3 per cent of exports in 1974 an increase of 297 per cent over 1973.

Net external financing rose to SDR 4,908 million (59 per cent higher than in 1973), in spite of which international reserves dropped by around 990 million dollars in 1974. In other words, the increased indebtedness, the direct foreign investment and the decline in reserves facilitated the flow of imports and made it possible to finance the large deficit on current account.

4. SHORT-TERM PROSPECTS

The eminently exogenous nature of the trends of the main variables in the external sector introduces an element of uncertainty in the short-term projection of the Brazilian economy. Certain signs of stabilization–if not a reversal–of the trend of export prices and the steady increase in the price of a large number of imports herald a situation in which it may be difficult to maintain the rapid growth of the economy. It is hardly necessary to point out that the sensitivity of world markets makes it impossible to make projections without a serious risk of error. Only if the signs referred to above are confirmed will the external situation suffer a certain amount of pressure.

The size of the trade deficit and deficit on current account that were recorded in the 1974 balance of payments and drop in international reserves show the type of obstacles that could arise. The growth style of the Brazilian economy would seem to be tied to an increasing inflow of

Table 181. Brazil: balance of payments
(Millions of SDR units)

	1970	*1971*	*1972*	*1973*	*1974*[a]
Current account					
Exports of goods and services	3,068.0	3,279.0	4,029.0	5,641.9	7,169.8
Goods FOB	2,739.0	2,882.0	3,630.0	5,138.6	6,625.2
Services	329.0	397.0	399.0	503.3	544.6
Transport	167.0	165.0	168.0	194.0	224.5
Travel	30.0	36.0	35.0	49.0	54.0
Imports of goods and services	3,297.0	4,182.0	4,926.0	6,473.1	12,077.2
Goods FOB	2,507.0	3,246.0	3,862.0	5,132.8	10,418.4
Services	790.0	936.0	1,064.0	1,340.3	1,658.8
Transport	349.0	421.0	470.0	706.2	947.9
Travel	160.0	171.0	199.0	218.8	245.3
Net external investment income	−428.0	−517.0	−570.0	−673.0	−1,022.7
Profits	−186.0	−188.0	−190.0	−247.0	−291.0
Interest	−242.0	−329.0	−380.0	−426.0	−731.7
Net private transfer payments	13.0	11.0	1.0	19.1	29.1
Balance on current account	−644.0	−1,409.0	−1,466.0	−1,485.1	−5,901.0

Table 181 (*continued*)

	1970	*1971*	*1972*	*1973*	*1974*[a]
Capital account					
Net external financing ($a + b + c + d + e$)	644.0	1,409.0	1,466.0	1,485.1	5,901.0
(a) Net external non-compensatory capital	1,222.0	2,257.0	3,633.0	3,226.0	
Direct investment	196.0	225.0	382.0	901.0	
Long-term and medium-term loans	1,143.0	1,838.0	4,256.0	3,921.0	
Amortization payments	−479.0	−572.0	−1,121.0	−1,440.0	4,907.8
Short-term liabilities	354.0	764.0	112.0	−160.0	
Official transfer payments	8.0	2.0	4.0	4.0	
(b) Domestic non-compensatory capital or assets	−41.0	−275.0	−302.0	−336.0	
(c) Errors and omissions	38.0	−6.0	403.0	205.1	
(d) Allocation of SDRs	59.0	47.0	47.0	–	–
(e) Net compensatory financing (increase −)	−634.0	−614.0	−2,315.0	−1,610.0	993.2
Balance-of-payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	1.0	–	51.0	–	...
Amortization payments	−101.0	−78.0	−50.0	−48.0	...
Movements of foreign exchange reserves (increase −)	−367.0	−488.0	−2,269.0	−1,562.0	...
Movements of gold reserves (increase −)	−105.0	–	–	–	...
SDRs (increase −)	−62.0	−48.0	−47.0	–	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26. [a] Estimates based on official statistics.

imports. The increasing dependence of a substantial part of the productive apparatus on imported supplies means that the external sector is a particularly important factor in future developments.

It must be borne in mind that the import coefficient rose from 7 per cent to 10.2 per cent in the space of four years, which means that the annual growth rate of imports was 22 per cent. The recent trend indicates that for every 1 per cent of growth of the product, the volume of imports must increase by over 2 per cent.

However, one-year projections must allow for the fact that the growth potential which the economy has acquired in recent years, the inflow of foreign capital and the borrowing capacity of the economy would seem to be sufficient to offset any bottleneck which may arise in foreign trade in goods and services.

Under these circumstances, the short-term outlook is that the Brazilian economy will maintain high growth indexes, although possibly not as high as in recent years.

COLOMBIA[10]

1. RECENT ECONOMIC TRENDS

In 1974, the gross domestic product increased by 6.1 per cent, which is lower than the rate recorded in 1973 but the same as the average annual growth rate for the period 1970-1972. The trend of the total product was the result mainly of a slackening in the growth of manufacturing compared with the previous year. Output of mining also decreased, particularly that of petroleum. On the other hand, agriculture and construction improved their rates of expansion (see table 182 and figure XIII).

Total supply of goods and services grew at a faster rate than the gross domestic product, owing to the considerable increase in the volume of imports of goods and services. On the demand side, exports of goods and services and total consumption increased at a slower pace than in 1973. Gross domestic investment, however, rose by over 11 per cent, which enabled the capital formation coefficient in relation to the gross

[10] See, in Part One of this *Survey*, the section dealing with Colombia in the chapter on inflation.

Table 182. Colombia: gross domestic product at factor cost, by sector of economic activity

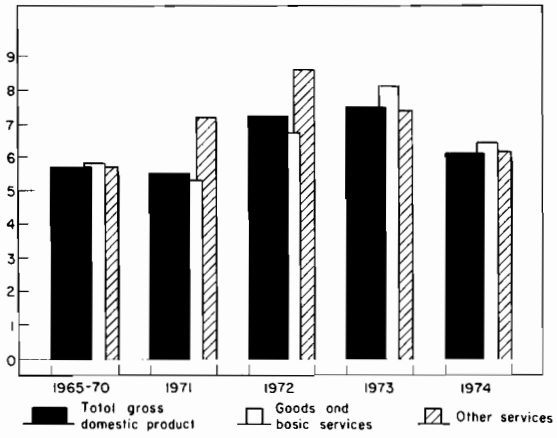
	Millions of pesos at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1973*	*1970-1972*	*1973*	*1974*[a]
Agriculture	34,880	39,831	42,021	29.1	27.1	4.1	5.3	5.5
Mining	2,458	2,309	2,194	2.0	1.6	−5.3	4.8	−5.0
Manufacturing	20,977	27,611	29,543	17.5	18.8	8.9	10.9	7.0
Construction	6,281	7,631	8,585	5.2	5.2	4.4	11.5	12.5
Subtotal goods	*64,596*	*77,382*	*82,343*	*53.8*	*52.7*	*5.4*	*7.8*	*6.4*
Electricity, gas and water	1,788	2,533	...	1.5	1.7	11.8	13.3	...
Transport and communications	8,881	11,037	...	7.4	7.5	7.0	8.6	...
Subtotal basic services	*10,669*	*13,570*	...	*8.9*	*9.2*	*7.8*	*9.4*	...
Commerce and finance	20,521	26,003	...	17.1	17.7	8.2	8.2	...
Government	8,283	10,459	...	6.9	7.1	8.6	7.1	...
Ownership of dwellings	6,887	8,266	...	5.7	5.6	6.5	5.9	...
Miscellaneous services	9,070	11,250	...	7.6	7.7	7.7	7.0	...
Subtotal other services	*44,761*	*55,978*	...	*37.3*	*38.1*	*7.9*	*7.4*	...
Subtotal services	*55,430*	*69,548*	*73,790*	*46.2*	*47.3*	*7.9*	*7.8*	...
Total	*120,026*	*146,014*	*154,920*	*100.0*	*100.0*	*6.4*	*7.5*	*6.1*

SOURCES: 1970–1973: ECLA calculations based on figures supplied by the Banco de la República; 1974: ECLA estimates based on official statistics.

[a] Preliminary figures.

Note: As the individual activities and the totals were calculated independently, the sum of the former does not correspond exactly with the latter.

Figure XIII. Colombia: growth of gross domestic product
(Annual growth rates)
Natural scale



domestic product to reach 21 per cent (see table 183).

In the external sector, exports of goods grew by 28 per cent, i.e., at a slower rate than in 1973, mainly owing to the stagnation in the value of coffee exports. Imports of goods showed a substantial increase (39 per cent), which was higher than that recorded the previous year and was due to increases of 14 per cent in volume and 21.5 per cent in unit value (see figure XIV). As a result of these trends, the deficit on current account rose to 127 million SDR units. It was financed by a net inflow of non-compensatory capital and of external resources of a compensatory nature, including the use of international reserves.

The rate of inflation increased slightly, but the steeper increases in prices were concentrated in the first half of the year, particularly as a result of the rises in food prices. At the end of the year, new levels of minimum urban and rural wages and salaries were established.

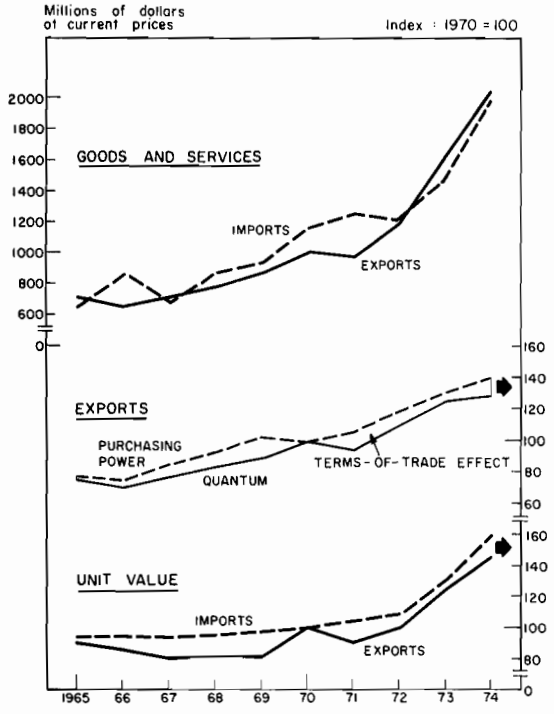
The change in the political administration which took place in August gave rise to important modifications in various lines of economic policy. Noteworthy in this respect were the emergency economic measures put into practice, the main objective of which was to redefine the anti-inflationary programme that was being implemented.

2. MAJOR SECTORS OF ACTIVITY

The agricultural sector grew by 5.5 per cent, that is, at a higher rate than that recorded for the period 1970–1973 and faster than the population growth (3.2 per cent annually). Thus, Colombian agriculture continued to show a relatively dynamic trend, which has frequently not been the case in other countries of the region. The main developments in the agricultural sector were the increases

of 30 per cent or more in output of cotton, rice, barley, beans and soya, while in the animal production sub-sector there was an increase in stock.

Figure XIV. Colombia: trend of external variables
Natural scale



The contribution of mining to the gross domestic product dropped by 5 per cent as the result of a similar drop in the production of crude petroleum, which has declined steadily since 1970, from 80 million barrels that year to about 64 million in 1974.

In manufacturing, the growth of production was 7 per cent, a lower rate than that observed in 1973 and also in the years 1970-1972. This loss of dynamism was mainly due to conjunctural factors—connected with the change of administration and the reformulation of economic policy which took place during the year—rather than to the bottleneck in the supply of inputs for industry or to the seriously restricted growth of demand for manufactures, or both factors at once.

Construction grew at a slightly faster pace than in 1973, easily exceeding the rate of increase recorded for the three-year period 1970-1972.

Altogether, the goods-producing sectors grew by 6.4 per cent, which compares unfavourably with the previous year's rate of 7.8 per cent. In line with this trend in the production of goods, the increase in the gross domestic product was estimated at 6.1 per cent, in contrast with 7.5 per cent recorded in 1973[11] (see table 182).

[11] No information was available on the variations in the sectors producing basic services and other services.

Table 183. Colombia: total supply and demand

	Millions of pesos at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1973*	*1970-1972*	*1973*	*1974*[a]
Total supply	*151,230.4*	*178,655*	*190,261*	*115.8*	*113.0*	*5.2*	*6.8*	*6.5*
Imports[b]	20,639.6	20,548	22,509	15.8	13.0	-1.8	3.3	9.5
Gross domestic product	130,591	158,107	167,752	100.0	100.0	6.4	7.5	6.1
Total demand	*151,230.4*	*178,655*	*190,261*	*115.8*	*113.0*	*5.2*	*6.8*	*6.5*
Exports[b]	18,516	24,150	25,996	14.2	15.3	9.1	9.5	7.6
Domestic demand	132,714.6	154,505.3	164,265	101.6	97.7	4.6	6.3	6.3
Gross domestic investment	28,130	31,492	35,019	21.5	19.9	2.7	6.1	11.2
Gross fixed investment	25,850	30,631	...	19.8	19.4	2.6	12.5	...
Public	7,732	...	...	5.9	...	...	...	...
Private	18,118	...	...	13.9	...	...	...	...
Construction	15,469	18,878	...	11.8	11.9	3.9	13.1	...
Machinery and equipment	10,381	11,753	...	8.0	7.5	0.8	11.5	...
Total consumption	104,584	123,013	129,246	80.1	77.8	5.1	6.4	5.1
General government	9,961	11,800	...	7.6	7.5	5.8	5.8	...
Private	94,623	111,213	...	72.5	70.3	5.1	6.5	...

SOURCES: 1970-1973: ECLA calculations based on figures supplied by the Banco de la República; 1974: ECLA estimates based on official statistics.

Note: The figures for exports and imports of goods and services were taken from balance-of-payments data expressed in dollars at current prices, which were converted to constant 1970 values by deflation, using price indexes calculated by ECLA for the purpose.

[a] Preliminary figures.

[b] Goods and services, excluding factor payments.

3. THE EXTERNAL SECTOR

Exports of goods, expressed in SDR units, rose by 28 per cent, as a result of increases of 10 per cent in volume and 16 per cent in unit values (see table 184). Coffee exports remained at much the same level as in 1973, the same quantity being exported and there being only a slight increase in the world price of this commodity.[12] On the other hand, non-traditional exports grew by over 50 per cent; thus the trend towards diversification of exports which had been observed since the end of the previous decade was accentuated.

Imports of goods rose by 39 per cent, with increases of 14 per cent in volume and 21.5 per cent in unit value. The import liberalization policy followed in 1973 and the early months of 1974 contributed to the expanding trend shown by this variable, especially as regards raw materials.

The different rates of growth of exports and imports of goods were determining factors in increasing the deficit on current account from 46 million SDR units in 1973 to 127 million in 1974.

[12] World coffee prices dropped by more than 10 per cent between April and October 1974, but recovered in the last two months of the year.

Table 184. Colombia: balance of payments
(Millions of SDR units)

	1970	*1971*	*1972*	*1973*	*1974*[a]
Current account					
Exports of goods and services	1,000.0	984.0	1,104.0	1,348.0	1,699.5
Goods FOB	788.0	755.0	883.0	1,106.0	1,413.5
Services	212.0	229.0	221.0	242.0	286.0
Transport	95.0	106.0	97.0	96.0	115.6
Travel	54.0	69.0	65.0	82.0	95.6
Imports of goods and services	1,149.0	1,260.0	1,121.0	1,233.0	1,646.3
Goods FOB	802.0	878.0	749.0	848.0	1,180.7
Services	347.0	382.0	372.0	385.0	465.6
Transport	163.0	192.0	178.0	187.0	237.0
Travel	66.0	72.0	74.0	89.0	103.9
Net external investment income	−180.0	−176.0	−182.0	−172.0	−191.2
Profits	−91.0	−71.0	−64.0	−56.0	−60.7
Interest	−89.0	−105.0	−118.0	−116.0	−130.5
Net private transfer payments	−1.0	3.0	10.0	10.0	10.8
Balance on current account	−330.0	−449.0	−189.0	−47.0	−127.2
Capital account					
Net external financing ($a + b + c + d + e$)	330.0	449.0	189.0	47.0	127.2
(a) Net external non-compensatory capital	405.0	383.0	259.0	161.0	51.2
Direct investment	43.0	43.0	17.0	22.0	
Long- and medium-term loans	308.0	290.0	387.0	307.0	
Amortization payments	−121.0	−144.0	−152.0	−135.0	
Short-term liabilities	138.0	163.0	−15.0	−56.0	
Official transfer payments	37.0	31.0	22.0	23.0	
(b) Domestic non-compensatory capital or assets	−36.0	−12.0	−22.0	−33.0	
(c) Errors and omissions	−18.0	55.0	77.0	32.0	
(d) Allocation of SDRs	21.0	17.0	17.0	–	–
(e) Net compensatory financing (increase −)	−42.0	6.0	−142.0	−113.0	76.0
Balance-of-payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	42.0	55.0	29.0	26.0	...
Amortization payments	−87.0	−42.0	−55.0	−10.0	...
Movements of foreign exchange reserves (increase −)	2.0	−2.0	−106.0	−84.0	...
Movements of gold reserves (increase −)	1.0	3.0	−1.0	−39.0	...
SDRs (increase −)	–	−8.0	−9.0	−6.0	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26.

[a] Estimates based on official statistics.

A factor which contributed to financing the 1974 deficit was the net inflow of non-compensatory capital of 51 million SDR units, even though this was much less than the 160 million the year before. It is estimated that this smaller inflow was due to a similar decrease in the amount of external public indebtedness, particularly with non-official sources.

Recourse was also had to compensatory capital to a value of 76 million SDR units, which includes the reduction which took place in the country's net international reserves.

4. THE COURSE FOLLOWED BY PRICES AND OTHER VARIABLES LINKED TO THE INFLATIONARY PROCESS

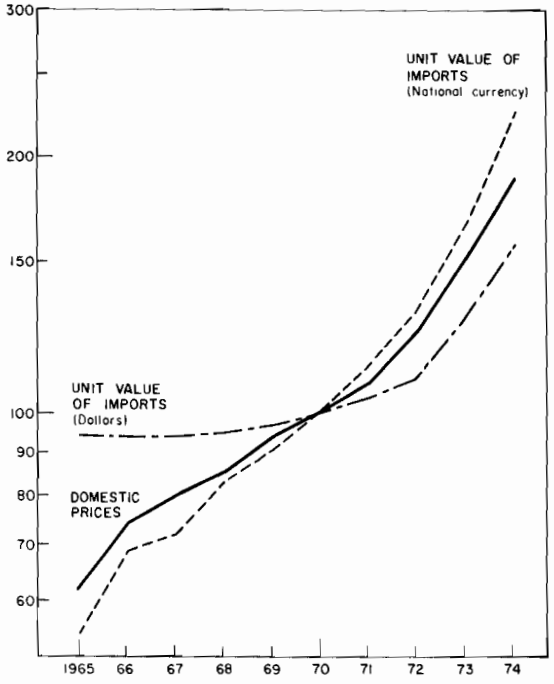
In 1974, the rate of increase in prices was slightly higher than in the previous period, since the consumer price index rose by about 26 per cent,[13] compared with 24 per cent in 1973. Food prices went up by over 30 per cent, which confirms the trend towards an improvement in their relative prices observable since 1971.

In the first three months of 1974, mainly owing to the impact produced by the internalization of imported inflation, food prices rose by 12 per cent (i.e., at an annual rate of over 50 per cent), which meant an increase of 9 per cent (about 40 per cent annually) in the general index (see figure XV, in which the trend of domestic prices is contrasted with that of the unit value of imports). Subsequently, this impact lost some of its force—added to which the stabilization policy was reformulated in August—and inflation slowed down to the annual rates indicated above.

[13] Between December 1973 and December 1974, as an average for the whole country and considering employees and workers as a whole (see National Administrative Department of Statistics (DANE), *Indice nacional al consumidor*).

Figure XV. Colombia: indexes of unit value of imports and of domestic prices

(Index: 1970 = 100)
Semi-logarithmic scale



As regards the public finances, the information collected indicates that current income of the national Government increased by 29.5 per cent, while total expenditure rose by 25.4 per cent. Therefore, in 1974 the government deficit was smaller than in 1973, net external indebtedness was practically nil, and net internal indebtedness stood at around 2,000 million pesos. The reverse situation had arisen in 1973, when external credit was an important source of financing (see table 185).

Table 185. Colombia: national government finance
(Millions of pesos at current prices)

	1973	*1974*[a]	*Percentage variation*
Current income[b]	20,073	25,995	29.5
Total expenditure	22,449	28,151	25.4
Total national government deficit . .	2,376	2,156	−9.0
Financing of the deficit[c]	2,376	. . .	. . .
(*a*) Net external indebtedness . .	3,051	. . .	. . .
(*b*) Net internal indebtedness[d] .	−675	. . .	. . .

SOURCES: IMF, *International Financial Statistics*, March 1975; and ECLA, on the basis of official statistics.

[a] Preliminary estimates.
[b] Excluding tax rebate certificates (*Certificados de Abono Tributario*—CAT) and Tourist Development Certificates (*Certificados de Desarrollo Turístico*—CDT).
[c] After deduction of amortization payments on the external and internal debt.
[d] Including variations in cash balances.

The available data on monetary trends were incomplete. Between December 1973 and December 1974 the money supply increased by 20 per cent, in contrast with the 30.7 per cent increase recorded in the previous comparable period.[14] The slackening in the growth of the means of payment was influenced by the change in the balance-of-payments position. While in 1972 and 1973 the gain in net international reserves acted as a factor of expansion within the operation of the monetary system, in 1974 the decrease in reserves acted in the opposite direction, i.e., as a factor of contraction.[15]

As regards foreign exchange, the mechanism of periodical mini-devaluations of the peso designed to maintain the real value of the national currency was continued. Between the end of 1973 and the end of 1974, the principal rate of exchange rose from 24.89 to 28.69 pesos to the dollar, i.e., by 15.3 per cent. In the second half of the year, the rate of devaluation was much more rapid than in the first.

Lastly, as regards the trend of wages and salaries, it is interesting to note that in November 1974 new levels were established for urban and rural minimum wages, which had not been adjusted since April 1972. The adjustments approved ranged from a minimum of 33 per cent in activities such as construction to a maximum of 48 per cent in transport and agriculture.

5. Some economic policy trends

A new administration initiated its period of government in August. Naturally, this change gave rise–and continued to give rise–to important modifications in the basic orientation of government economic policy, which affect both the development strategy itself and shorter-term problems, particularly as regards the combating of inflation. However, in view of the essentially conjunctural nature of this note and taking into account the emphasis which the administration has placed on "economic emergency measures" adopted in October 1974, it seems desirable at this time to refer to these measures rather than to other provisions oriented more to the medium and the long term that have gradually taken shape.

Evoking its constitutional powers, the new administration adopted a number of measures designed to intensify anti-inflationary policy and to provide better protection for the lower-income groups against the consequences for them of the continuous steep increases in prices. The measures adopted–and other supplementary action–mainly cover three spheres of action.

In the fiscal field, the basic objective was to reduce the government deficit, which it was estimated might amount to 3,000 million pesos in the second half of 1974 and over 5,000 million in 1975.

With this end in view, the severe curtailment of public expenditure was approved, subsidies for wheat imports and consumption were eliminated and incentives to encourage exports were reduced. As regards export incentives, a change was introduced in the mechanism of tax rebate certificates (*Certificados de Abono Tributario*–CAT), by virtue of which a tax incentive of up to 15 per cent was granted for non-traditional exports; as from January 1975 the maximum subsidy was reduced to 5 per cent and only 1 per mille for those products considered of vital importance for domestic supply.

Concurrently, a tax reform was introduced with the aim of stepping up the collection of fiscal revenue, in the form of an increase in sales taxes and a heavier tax on capital income and non-essential consumption. At the same time, however, preferential treatment was given to income from labour, particularly below certain minimum levels.

In the financial sector, several provisions were put into effect with a view to the more efficient co-ordination of the different instruments in operation for tapping savings. For this purpose, adjustments were made in the interest rates paid in respect of some of these instruments, and, on the other hand, the monetary correction which may be earned by the units of constant purchasing power (UPAC) used in the system of adjustable savings and loans for housing was limited to 20 per cent.

In addition, the Monetary Board introduced important changes in the management of the monetary apparatus designed to make the Board's control over its development more effective. These changes include the measures adopted as regards cash reserves, rediscount margins and regional distribution of credit.

Lastly, as regards income and prices policy, reference has already been made to the increase approved in minimum wages. To supplement this, a system of tripartite commissions was established–composed of representatives of the State, the workers and the entrepreneurs–with the object of studying and negotiating various measures designed to achieve concerted changes in prices and wages.

[14] See in Part One of this *Survey*, table 88 on monetary trends in the section dealing with Colombia in the chapter on inflation.

[15] Although the trend followed by net international reserves in 1974 is not known, as an indication of what took place it may be mentioned that between December 1973 and December 1974 the reserves of the monetary authorities declined from 534 to 449 million dollars.

COSTA RICA[16]

1. RECENT ECONOMIC TRENDS

In 1974 the Costa Rican economy expanded by a little over 4 per cent: that is to say, at a slower rate than in the last three years (see table 186).

Of particular note in the evolution of supply by sectors is the drop in agricultural activity due to the lower production of bananas, sugar-cane, maize and beans, which the increases in coffee, tobacco and beef failed to make up for. The sectors showing most growth were construction and manufacturing, the most important elements in their growth being the exports to Central America and the demand generated by capital formation in both the public and the private sector (see table 187 and figure XVI).

In general terms, the loss of dynamism of the economy as a whole was due fundamentally to events which could not be counteracted by economic policy, although it was also due to some extent to structural maladjustments, such as the lack of diversification of exports, which were quite marked in the conditions of 1974.

[16] See the section dealing with Costa Rica in the chapter on inflation in Part One of the present *Survey*.

Costa Rica faced a number of adverse circumstances of external origin which affected the initial impulse and multiplication and acceleration effects normally produced by external demand. Thus, as a result of the instability of international markets, but also partly because of certain internal difficulties which affected production, exports of

Figure XVI. Costa Rica: growth of gross domestic product
(Annual growth rates)
Natural scale

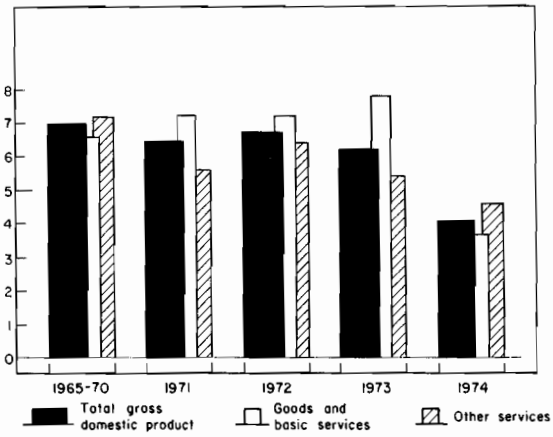


Table 186. Costa Rica: total supply and demand

	Millions of colones at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970-1972*	*1973*	*1974*[a]
Total supply	*8,807.4*	*10,409.9*	*11,064.3*	*135.0*	*134.9*	*6.0*	*5.1*	*6.3*
Imports[b]	2,282.9	2,531.3	2,862.7	35.0	34.9	4.3	1.9	13.1
Gross domestic product	6,524.5	7,878.6	8,201.6	100.0	100.0	6.6	6.2	4.1
Total demand	*8,807.4*	*10,409.9*	*11,064.3*	*135.0*	*134.9*	*6.0*	*5.1*	*6.3*
Exports[b]	1,841.2	2,344.7	2,459.1	28.2	30.0	12.1	1.3	4.9
Domestic demand	6,966.2	8,065.2	8,605.2	106.8	104.9	4.4	6.3	6.7
Gross domestic investment	1,339.9	1,737.0	2,083.3	20.5	25.4	5.9	15.7	19.9
Gross fixed investment	1,269.8	1,592.5	1,719.9	19.5	20.9	10.4	2.9	8.0
Public	289.6	353.8	364.4	4.5	4.4	14.3	-6.5	3.0
Private	980.2	1,238.7	1,355.5	15.0	16.5	9.2	6.0	9.4
Total consumption	5,626.3	6,328.2	6,521.9	86.3	79.5	4.0	4.0	3.1
General government	819.8	961.8	1,029.1	12.6	12.5	5.9	4.7	7.0
Private	4,806.5	5,366.4	5,492.8	73.7	67.0	3.7	3.9	2.4

SOURCES: 1970–1973: ECLA calculations based on figures supplied by the Central Bank of Costa Rica; 1974: ECLA estimates based on official data.

Note: The figures for exports and imports of goods and services were taken from balance-of-payments data expressed in dollars at current prices, which were converted to constant 1970 values by deflation, using price indexes calculated by ECLA for the purpose.

[a] Preliminary figures.

[b] Goods and services, excluding factor payments.

Table 187. Costa Rica: gross domestic product at factor cost, by sector of economic activity

	Millions of colones at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1973*	*1970-1972*	*1973*	*1974*[a]
Agriculture	1,452.1	1,737.5	1,702.8	25.0	24.8	5.6	7.2	-2.0
Mining	878.4	1,152.1	1,255.8	15.1	16.4	9.2	10.0	9.0
Manufacturing								
Construction	275.2	327.6	370.2	4.7	4.7	7.2	3.5	13.0
Subtotal goods	*2,605.7*	*3,217.2*	*3,328.8*	*44.8*	*45.9*	*7.0*	*7.8*	*3.5*
Electricity, gas and water	114.3	156.0	...	2.0	2.2	11.2	10.3	...
Transport and communications	276.7	342.7	...	4.8	4.9	7.7	6.7	...
Subtotal basic services	*391.0*	*498.7*	...	*6.8*	*7.1*	*8.8*	*7.8*	...
Commerce and finance	1,299.7	1,590.8	...	22.4	22.7	7.9	5.0	...
Government	693.2	774.7	...	12.0	11.1	3.6	4.1	...
Ownership of dwellings	485.5	559.8	...	8.4	8.0	5.4	3.8	...
Miscellaneous services	324.2	364.0	...	5.6	5.2	4.1	3.7	...
Subtotal other services	*2,802.6*	*3,289.3*	...	*48.4*	*47.0*	*6.0*	*4.5*	...
Subtotal services	*3,193.6*	*3,788.0*	*3,963.6*	*55.2*	*54.1*	*6.3*	*4.9*	*4.6*
Total	*5,799.3*	*7,005.2*	*7,292.4*	*100.0*	*100.0*	*6.6*	*6.2*	*4.1*

SOURCES: 1970-1973: ECLA calculations based on figures supplied by the Central Bank of Costa Rica; 1974: ECLA estimates based on official data.

[a] Preliminary figures.

bananas dropped by 11 per cent in 1974 in contrast to a rise of over 9 per cent the year before.

On top of the slowing down in this important activity there was the increase in the cost of imports–particularly of petroleum and petroleum products–which increased the inflationary pressures already quite noticeable in the previous year and affected the purchasing power of the broad sector made up of those receiving medium and low incomes, thus having repercussions on domestic demand. In contrast, the rise in the real income of the richer social groups led them to obtain foreign credit facilities for the purchase of imported consumer goods, in the expectation of a further rise in world prices. This partly explains the substantial rise of 13.1 per cent in the volume of imports of goods and services (see table 186).

The recent inflationary process, which involved a rise in wholesale prices estimated at between 35 and 40 per cent and reduced the purchasing power of large sectors of the population, led the Government in April 1974 to grant wage increases designed to palliate the deterioration in the real wages of the working classes. These increases proved to be insufficient, however, as prices continued to go up.

The change in wage levels practically coincided with the unification of the exchange rates, which had become necessary owing to the critical balance-of-payments situation but which caused considerable increases in domestic production costs and thus further depressed the purchasing power of wages.

As a result of the above developments, private consumption once again grew only slowly, its growth rate being lower than that of 1973 and actually negative in *per capita* terms (see table 186).

Apart from the measures taken to avoid a serious deterioration in the purchasing power of wages, there were compensatory elements on the domestic expenditure side. Thus, total investment and government consumption showed some degree of dynamism. Private investment, mainly in housing construction, rose 9.4 per cent, and the 7 per cent increase in government consumption expenditure was also of significance when compared with the 1972 and 1973 trends. Finally, public investment, which had fallen in 1973, rose by a modest 3 per cent in 1974, the main expenditure being on economic infrastructure programmes (among them projects in the energy field) and social progress, mainly in housing and health.

With the passage of time, the possibilities for manoeuvring in economic policy have become smaller, partly because of the increasing indebtedness of the economy which has in its turn reduced its capacity to import, and partly because of the need to allot appreciable volumes of external credit to maintaining the supply of goods and services. In 1974, against a background of a

marked deterioration in the terms of trade, the major part of the real resources from abroad–plus part of the foreign currency reserves–had to be used to finance essential imports such as fuel and other industrial inputs and to help to satisfy the demand for consumer goods.

Thus, the external sector continues to be the central element in economic activity, as well as remaining one of the basic causes of the process of rising prices. With this in mind, steps have been taken to work out unitary and convergent action on various economic policy fronts.

In this respect, the Government adopted a number of measures designed to reduce inflationary pressures and external imbalances. From the point of view of supply, the main measures taken were the fixing of support prices for producers of basic grains, the maintenance of adequate external supplies of mass consumption products, and the provision of incentives through new selective credit programmes and favourable interest rates in order to give sustained support to the productive sectors–especially manufacturing–and facilitate the expansion of exports of non-traditional products.

From the medium- and long-term point of view, the above programmes have been complemented with action designed to promote economic growth on the basis of a better utilization of resources. External loans have been obtained for new investments in agriculture, industry and tourism, and efforts have been stepped up in connexion with public works. These include strengthening of road construction programmes (with particular importance being attached to secondary roads), the beginning of the construction of a new port at Caldera, the continuation of work to modernize and expand the port facilities at Limón, the renewed impulse being given to the hydroelectric project at Arenal, and the expansion of the national telecommunications system. There is also every indication that progress is being made in the execution of high-priority investment projects such as those connected with the production of copper and aluminium and the refining and overland transport of petroleum and petroleum products.

With the aim of modifying the structure of demand, changes were made in the tax system, especially as regards the raising of the selective taxes designed to check luxury spending and the introduction of export duties. Other measures aimed at reducing pressures on the balance of payments and curbing luxury consumption include the regulation of credit purchases, the regulation of credit operations by private finance companies, and the raising of interest rates on foreign currency deposits.

2. THE EXTERNAL SECTOR AND THE BALANCE OF PAYMENTS

There was a serious deterioration in the balance of payments in 1974, when, mainly as the result of an exceptional increase in imports, the current account deficit reached the unprecendented level of 211 million SDR units (see table 188). Despite a significant inflow of capital from abroad, the capital account income was not enough to finance the current account deficit, and there was consequently a drop in net reserves of 32.5 million SDR units. It is estimated that the level of international reserves at the end of 1974 was not enough to finance the country's import requirements for two weeks. Furthermore, a considerable proportion (90 million SDR units) of the capital account income was from short-term loans.

The growth of 35 per cent in imports is to be attributed primarily to the extraordinary increase of 31.3 per cent in prices, due largely to the higher price of petroleum and petroleum products. However, even in constant terms there was an appreciable increase estimated at 13.1 per cent in imports of goods and services, due largely to purchases of a speculative nature made in the expectation that prices would soon go up. From this point of view there was no external bottleneck, and the increased cost of imports did not prevent them from growing more than in previous years, although this was achieved at the expense of greater indebtedness and the depletion of reserves.

Exports of goods, for their part, rose by 26 per cent, mainly because of the higher prices obtained (18.3 per cent) although these were of course outstripped by the rise in the prices of imports, thus leading to a serious deterioration in the terms of trade (see figure XVII).

Analysis of the main export products of Costa Rica shows an increase in both the price and the volume of exports of coffee. The increased volume was due fundamentally to the greater production achieved as a result of the favourable weather conditions prevailing during the last harvest, but the prospects for coffee are uncertain, since it is expected that next year domestic production will be smaller, mainly on account of the reduction in the use of fertilizers because of their higher price and scarcity.

The price of bananas went up, but the volume exported went down as a result of lower production caused not only by a strike lasting over a month in one of the main producing companies, but also by the negotiations regarding the establishment of an export tax.

The volume of sugar exported also declined, but the price went up considerably. The lower volume is explained by the effects of the drought

in the preceding year and also by the reduction in cutting in various areas attributed to action by producers to obtain higher prices.

In the case of meat the price went down in the second half of the year and some difficulties were encountered in placing meat on the external market, but even so the total volume exported went up.

Finally cocoa exports went up in both volume and price.

One of the most favourable factors in the external sector was the increase in exports to the rest of Central America, which made it possible to balance transactions with the other members of the Central American Common Market and helped to encourage the production of manufactures, which form the main part of such exports.

As regards capital account movements, the most significant development concerned long- and medium-term loans, since these increased by 52 per cent in 1974 to a total of 153 million SDR units. Direct investment, however, did not show any variation compared with the recent past (see table 188).

During the year, the Costa Rican Government took a number of measures designed to relieve the balance-of-payments situation. Among the most important of these was the exchange rate unifi-

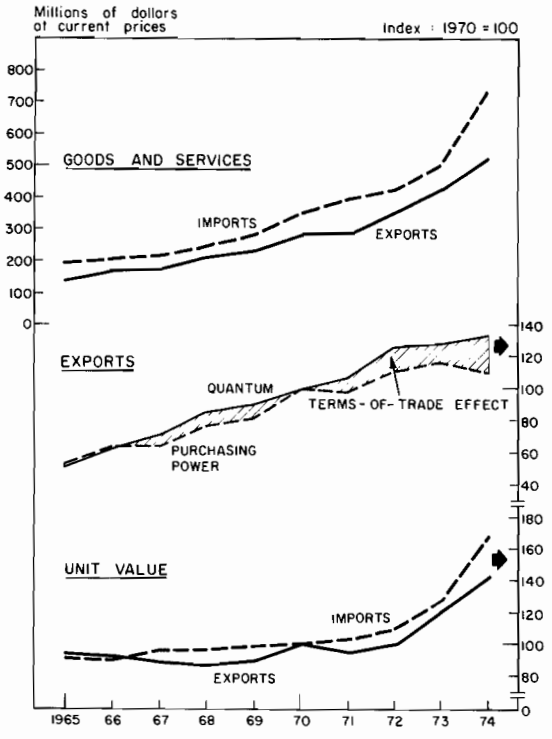
Table 188. Costa Rica: balance of payments
(Millions of SDR units)

	1970	*1971*	*1972*	*1973*	*1974*[a]
Current account					
Exports of goods and services	280.1	283.8	319.1	345.4	433.6
Goods FOB	231.0	224.6	256.8	283.1	357.5
Services	49.1	59.2	62.3	62.3	76.1
Transport	14.5	20.6	19.0	19.5	26.4
Travel	22.1	24.2	27.4	27.4	31.6
Imports of goods and services	346.5	390.7	385.2	407.4	607.0
Goods FOB	286.8	316.3	310.5	331.0	504.3
Services	59.7	74.4	74.7	76.4	102.7
Transport	35.9	44.3	43.5	46.9	67.5
Travel	12.7	17.0	17.4	17.2	19.8
Net external investment income	−13.6	−14.6	−32.1	−34.1	−40.9
Profits	−3.8	−3.4	−19.4	−20.3	−23.3
Interest	−9.8	−11.2	−12.7	−13.8	−17.6
Net private transfer payments	3.4	3.5	3.7	3.0	3.0
Balance on current account	−76.6	−118.0	−94.5	−93.1	−211.3
Capital account					
Net external financing ($a + b + c + d + e$)	76.6	118.0	94.5	93.1	211.3
(*a*) Net external non-compensatory capital	79.1	128.0	98.1	81.9	131.0
Direct investment	26.4	22.0	23.8	22.2	23.0
Long- and medium-term loans	42.2	68.4	87.1	100.7	153.0
Amortization payments	−19.2	−30.6	−35.3	−48.1	−53.0
Short-term liabilities	27.2	64.3	20.1	7.5	8.0
Official transfer payments	2.5	3.9	2.4	−0.4	...
(*b*) Domestic non-compensatory capital or assets	−5.9	−19.8	−42.6	−31.5	47.8
(*c*) Errors and omissions	−9.5	20.3	35.9	50.9	
(*d*) Allocation of SDRs	4.2	3.4	3.4	–	–
(*e*) Net compensatory financing (increase −)	8.7	−13.9	−0.3	−8.2	32.5
Balance-of-payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	1.4	3.8	15.7	1.7	...
Amortization payments	−4.2	−3.3	−8.4	−5.4	...
Movements of foreign exchange reserves (increase −)	15.7	−20.2	−3.7	−4.5	...
Movements of gold reserves (increase −)	−4.0	5.7	–	–	...
SDRs (increase −)	−0.2	0.1	−3.9	–	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26.

[a] Estimates based on official statistics.

Figure XVII. Costa Rica: trend of external variables
Natural scale



cation which eliminated the rate of 6.62 colones to the dollar and thus made it possible to bring the prices of the country's international trade goods in line with the higher prices reigning on the world market.

The rates of interest prevailing in Costa Rica were brought into line with the higher rates offered abroad, so as to stop the exit of capital and stimulate national saving.

In addition, restrictions were imposed on foreign travel and on other forms of expenditure which might affect the balance of payments. At the same time, the banks were allowed to receive term deposits in foreign currency with the aim of attracting funds and avoiding the flight of capital abroad. Stricter control was also applied to the granting of loans for the purchase of non-essential consumer goods, with the aim of avoiding the naturally unfavourable consequences on the availability of foreign exchange.

Furthermore, as already stated, export taxes were introduced which will keep in line with the prices attained by the products affected on the foreign market. These new taxes not only constitute an important instrument from the point of view of their fiscal effects but will also make it possible to reduce the possible effect of higher prices abroad on domestic prices.

Following the tax payment certificates introduced in 1973 which can be used by exporters to pay any form of taxes and thus represent a stimulus for exports, a number of additional measures was taken in 1974 to encourage exports of industrial goods. Prominent among these measures was the increase in the amount of credit made available at favourable interest rates.

3. THE BUDGET SITUATION

In 1974, for the first time in this decade, it proved possible to reduce the central government deficit as a result of an increase of 38.5 per cent in current income contrasted with increases of only 28.4 per cent in current expenditure and 15.5 per cent in capital expenditure.[17]

The bigger tax revenue was due on the one hand to the introduction of new taxes and on the other to the rise in revenue from existing taxes. Among the new taxes were the export taxes established on an *ad valorem* basis, with rates varying from 2 to 13 per cent. The lowest rate–2 per cent–is applied to exports of non-traditional products to the rest of the world, the rate of 7 per cent to exports of other goods to the rest of the world and exports to Central America and Panama in general, while the highest rate of 13 per cent is applied to traditional export products such as coffee, meat, sugar and cocoa.

The bigger revenue achieved from existing taxes is of course attributable partly to the rise in prices, but also to a number of administrative measures taken in order to check tax evasion.

The taxes which played the biggest part in this increased revenue were income tax, selective consumer taxes, sales tax and import duties. The latter, of course, reflect the considerable increases in the prices of imports.

As regards current expenditure, the increases were due mainly to the wage increases granted to central government employees and to the bigger payments which had to be made by the central government to finance similar wage increases in decentralized bodies.

The biggest expenditure on capital account corresponded mainly to the expansion of the economic infrastructure (construction of highways, airports, etc.) and the building of more schools.

As far as the financing of the fiscal deficit was concerned, it proved possible to place a considerable proportion of the bonds issued (although this proportion was less than the previous year) and thus avoid issuing more means of payment.

[17] SOURCE: Ministry of Finance and Popular Credit.

External funds, which totalled almost as much as domestic funds in 1974, played a more significant part than in 1973 in financing the deficit.

4. INFLATIONARY PRESSURES

From the information available on wholesale prices, it would appear that inflationary pressures persisted in Costa Rica during 1974, although they showed a declining trend in the second half of the year. Thus, while the increase in prices during the first half of the year was 26 per cent (an average of 4 per cent per month), the monthly rate was around 1.7 per cent in the period July-November. On the basis of this information, it may be estimated that wholesale prices rose by between 35 and 40 per cent in 1974 compared with a rise of 27 per cent in the previous year.

From the middle of 1973 onwards, imported inflation was of special significance in Costa Rican price movements. An acceleration in the rise of import prices will obviously affect domestic prices also in an economy so open to the exterior as that of Costa Rica. It may be recalled in this connexion that the prices of imports rose by 15.3 per cent in 1973 and by 31.3 per cent in 1974. Figure XVIII clearly shows this acceleration, which had far-reaching repercussions on economic activity, in view of the country's high import coefficient and its relationship with the trend of domestic prices.

One of the more important elements among the domestic inflationary factors was the greater liquidity in the economic system. Thus, over-all liquidity rose by 32.4 per cent in 1974 compared with 12.8 per cent the year before (see table 189).

The 51.5 per cent increase in credit to the private sector, which was receiving 83 per cent of total credit at the end of 1974, appears to have been the main cause of this expansion, but another contributory cause was the credits granted to the Government of official bodies, even though their total amount is much less than the credit to the private sector.

Figure XVIII. Costa Rica: indexes of unit value of imports and of domestic prices
(Index: 1970 = 100)
Semi-logarithmic scale

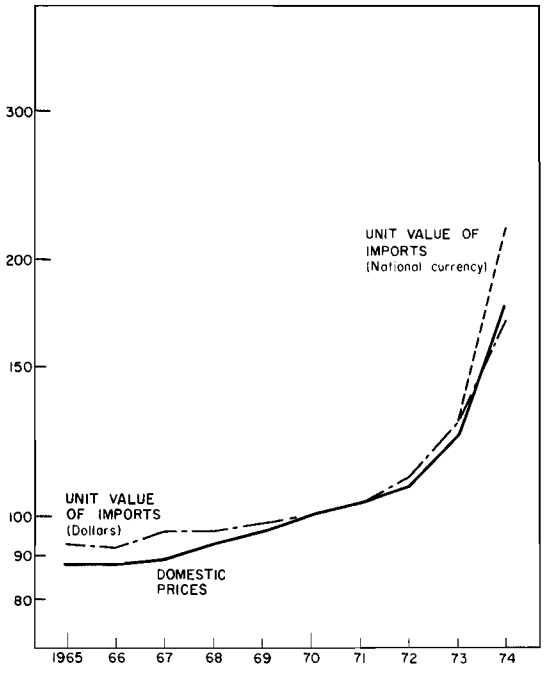


Table 189. Costa Rica: monetary position
(End-of-period figures in millions of colones)

	1972	*1973*	*1974*[a]	*Growth rate (percentages)*	
				1973	*1974*
Composition of monetary resources	*2,629.2*	*2,965.2*	*3,927.4*	*12.8*	*32.4*
Money	1,617.3	2,007.7	2,394.3	24.1	19.3
Quasi-money	855.6	951.1	1,603.6	11.2	68.6
Long-term loans	79.0	72.6	197.9	−8.1	172.6
Other items (net)	77.3	−66.2	−268.4	–	−305.4
Expansion and contraction factors	*2,629.3*	*2,965.5*	*3,927.2*	*12.8*	*32.4*
Reserves	189.1	276.4	−115.9	46.2	–
Credit	2,440.2	2,689.1	4,043.1	10.2	50.4
To the government	379.0	304.5	336.9	−19.7	10.6
To official bodies	83.3	163.3	340.2	96.0	108.3
To the private sector	1,977.9	2,221.3	3,366.0	12.3	51.5

SOURCE: IMF, *International Financial Statistics*, March 1975.
[a] Preliminary figures.

The drop in reserves acted as a form of contraction and had a fairly significant effect on the over-all liquidity of the economy.

From the point of view of monetary resources, the most important changes concerned money and quasi-money, both because of the important influence they have within the total and because of the considerable size of the variations in them, which came to 19.3 per cent and 68.6 per cent respectively in 1974.

The foregoing developments led to the adoption of a number of measures designed to achieve greater control over the whole monetary and credit system. Outstanding among these was the regulation of the non-banking finance system, which seems to be handling an appreciable amount of funds used mainly for the acquisition of non-essential consumer goods. Also noteworthy were the measures taken to fix more restrictive conditions for credit sales of consumer durables.

CHILE

1. General appreciation

The economic evolution of Chile in recent times has been influenced by political events known to all, which have had a decisive effect on the important variables considered in these annual accounts. This does not, however, prevent some objective elements, which are important and valid over and above any controversy, from being singled out.

Naturally, the very particular and obvious impact of the external economic situation on the economy of Chile draws one's attention; it once again brings to the fore certain features and weaknesses in the structure of production, and while these are not absolutely original in the context of Latin America there is no doubt that they tend to stand out particularly in Chile.

Some facts detailed below give an idea of the essence of the problem. In 1974 the country had to pay nearly 40 per cent more for imports, the volume of which increased by slightly over 1 per cent. Although the value of exports increased by a respectable 54 per cent, it is equally true that their quantity had to increase 33 per cent to produce this result.

The reasons for such uneven—and in the last instance such onerous—developments continue to be the same as affected other critical external trade situations, whether expansionist or recessive. The structure of imports with its high proportion of food products and basic inputs on the one hand, and the overdependence on copper for foreign exchange earnings on the other, make Chile highly vulnerable to fluctuations in international trade. In addition, in periods of general price increases, like that of recent years, facts (like the above) show that the protection provided by copper is far from offsetting the weakness implicit in Chile's import structure.

It cannot be ignored that these facts have an important influence on the difficulties which have affected the economy of Chile. They also aid in evaluating the initiatives and procedures aimed at expanding and diversifying the country's export base—an old but elusive objective of many attempts at an economic policy for Chile.

It should, however, be borne in mind that as a whole 1974 was a fairly good year and did not bring up any major difficulties for the administration of the external accounts. The deterioration of the situation towards the end of the year was mainly caused by the divergence between the downswing in copper and rising import costs, but in addition to this element there was a certain underestimation of the traditional vulnerability of Chile's external sector. When the optimistic estimates made in some circles at the beginning of 1974 came to nothing, it was once more seen that the margin for liberal policies in foreign exchange expenditure continued to be narrow.

The continued existence of inflation is another aspect which requires comment on account of its decisive influence in recent times. As will be seen below, despite the priority given to efforts to contain it, progress has been rather limited.

In order to form an accurate idea of this, it is indispensable to consider the variety of influences or stimuli which have kept inflation alive. Obviously, a capital element is the legacy of accelerated price increases from 1972-1973, together with the serious repercussions of imported inflation. Against this background—the inflationary potential of which requires no comment—appear the consequences of what is known as "corrective inflation" (undertaken to eliminate the price distortions which had accumulated) and of a policy of liberalized prices and periodic readjustments in the exchange rate.

Although the first two factors were outside the sphere of influence of the authorities, the others derive from the general strategy employed. Seen from this point of view, the *quid pro quo* facing this policy emerges clearly. On the one hand were

the specific objectives of "corrective inflation" and the measures for liberalization and exchange readjustments, and on the other the impact of these objectives on the increase in prices. In solving the dilemma the first group of considerations would appear to have prevailed over the second. The inherited or exogenous influences of the inflationary process were thus to some extent maintained or fortified by the directives of the economic policy already mentioned. In other words, it remains open to discussion whether the tactics were the most appropriate for reinforcing or recovering control over the development of inflation.

In any case the persistence of the phenomenon has aroused understandable controversy over these tactics. If for some their fault was in not making any attempt to moderate the powerful pressures from recent years the impact of which was redoubled by the international economic situation, for others the root of the question lies in the fact that no drastic measures were taken to check the accumulated inflationary potential at its base.

In view of the acuteness of the phenomenon and the magnitude of the unknowns laid bare by any of these criteria, it should not appear surprising that the policy has hesitated to opt finally for any one of them.

2. Recent economic trends

In 1974 the Chilean economy showed a clear recovery, and began to get the better of the squeeze which affected it the previous year. In 1974 the gross domestic product increased by around 5 per cent following its 4 per cent drop in 1973. However, this result as regards the growth of the product took the form of a rather smaller increase in real income, with the deterioration of the terms of trade as a result of the lower prices obtained by copper in the international market, especially in the second half of the year and the higher prices which the country had to pay for the products it imported (see table 190).

Table 190. Chile: growth of the product and real income
(Annual growth rate)

Year	*Gross domestic product*	*Real income*
1970	3.7	3.8
1971	7.7	4.2
1972	1.4	1.2
1973	−4.0	−1.9
1974	5.0	2.5

SOURCE: ECLA, on the basis of official statistics.

In the performance of the main sectors of production the considerable dynamism of the activities producing goods stood out, with the exception of manufacturing, compared with the poor level of growth of the services sectors. Mining output increased substantially as a result of the major increase in copper mining (basically in the first half of the year) and other smaller increases in the other mineral products. Another important factor was the recovery in agricultural and construction activities. The growth rate of the manufacturing sector was very poor, and there were sharp decreases in the output of consumer goods and in the metal manufactures and machinery sectors. There was a significant increase in the generation of electric energy compared with the result of the previous year, but it did not reach the average rate of the period 1970-1972.

Total supply increased during 1974 less than the gross domestic product, owing to the standstill in imports of goods and services (expressed in constant values). The most active components of total demand were exports (the volume of which increased by 27 per cent) and expenditure on investment. The formation of fixed capital increased by 8.5 per cent exclusively as a result of the increase in expenditure on construction. Total consumption declined much further than in 1973, as a result of a sharp squeeze in consumer expenditure in the private sector, while general government expenditure probably increased at a rate similar to that of 1973.

The increase in the value of exports was much more pronounced than the increase in imports, but since the deficit in the services account and net remittances abroad of profits and interest increased significantly, especially the latter, the decrease in the current account deficit at the end of the year did not turn out to be very large (it was reduced by around 30 million dollars). On the other hand, as total net inflows of non-compensatory capital were larger than those of the previous year–half of these were accounted for by the return of funds existing abroad but owned by Chilean residents–the balance-of-payments deficit dropped to less than half its 1973 level.

As regards the evolution of domestic prices, their growth rate showed some decrease. The consumer price index rose 375.9 per cent between December 1973 and December 1974; wholesale prices increased by 570.6 per cent over the same period. The decline in the growth rate of prices was more pronounced in the second half of the year.

As regards real wages, the results obtained during the year showed that their average level was around 6 per cent lower than that of 1973. In any case, the evolution of wages during the second half of the year came closer to the level which had

been proposed as a wage policy target, i.e., of maintaining in 1974 the 1973 level of real income.

The unemployment situation, according to data available for Greater Santiago, tended to deteriorate in the course of the year. In December 1974 the unemployment rate was close on 10 per cent, compared with December 1973 when the rate was around 7 per cent. In the last quarter an increase was to be seen in the percentage of persons seeking work for the first time and a similar trend in the indicator for the out-of-work period.

As regards the situation in government finance, there was an improvement in the tapping of resources, basically from taxes, and a much slower increase in expenditure than in income while the change in the pattern of expenditure came to place emphasis on capital formation. Thus, the share of current expenditure in total expenditure dropped from 73 per cent in 1973 to slightly over 60 per cent in 1974, with a corresponding increase in the percentage allocated to investment. The proportionally larger increase in income than in expenditure led to a reduction in the fiscal deficit, its proportion to total expenditure dropping from 35 per cent in 1973 to 21 per cent in 1974.[18]

Lastly, in connexion with monetary trends, a significant decrease—almost uninterrupted in the course of the year—was to be noted in the high growth rates of the quantity of money. While in January 1974 total money grew at an annual rate of 404 per cent and private sector money at a rate of 347 per cent, in November 1974 total money increased at the rate of 320 per cent, and private sector money at the rate of 240 per cent. Of the increase in total money over the year, the larger share was accounted for by the money supply of the fiscal sector. Between January and November total money increased by 237 per cent, private sector money by 178 per cent and fiscal sector money by 398 per cent.

The factors of expansion of money issue, which according to figures provided by the Central Bank of Chile[19] increased by 168 per cent up to October, were basically the fiscal deficit and, to a much lesser extent, domestic credit operations; exchange operations on the other hand appear as a factor of absorption. The impact of these factors, however, was different in the two halves of the year. In the first six months the fiscal deficit had a relatively smaller influence, owing to the fact that exchange operations constituted an important element of expansion because of the sizable purchases of foreign currencies, stemming from the favourable balance-of-payments situation. Domestic credit, on the other hand, was a source of absorption during this period. In the second half of the year, exchange operations became a marked factor of absorption of money issue, as reflected in the deficit which occurred in the balance of payments during those months; the opposite was the case with total domestic credit, which came to constitute a factor of expansion.

[18] Statement on the state of the Public Treasury, October 1974.

[19] Banco Central de Chile, *Síntesis monetaria*, various issues.

3. MAJOR SECTORS OF ACTIVITY

The recovery in the growth rate of the gross domestic product during 1974 reflected the favourable performance of activities producing goods, with the exception of manufacturing. As a whole they recorded an increase of nearly 8 per cent, while the growth of the services sector was estimated at barely over 1 per cent (see table 191 and figure XIX).

As regards the output of the agricultural sector, the most recent ODEPLAN estimates[20] attribute to it an increase of around 17 per cent, expressed in terms of its value added, and of around 12 per cent measured in terms of the gross value of

[20] Estimates provided by the Department of Agriculture of the Division of Social Accounts (February 1975).

Figure XIX. Chile: growth of gross domestic product
(Annual growth rates)
Natural scale

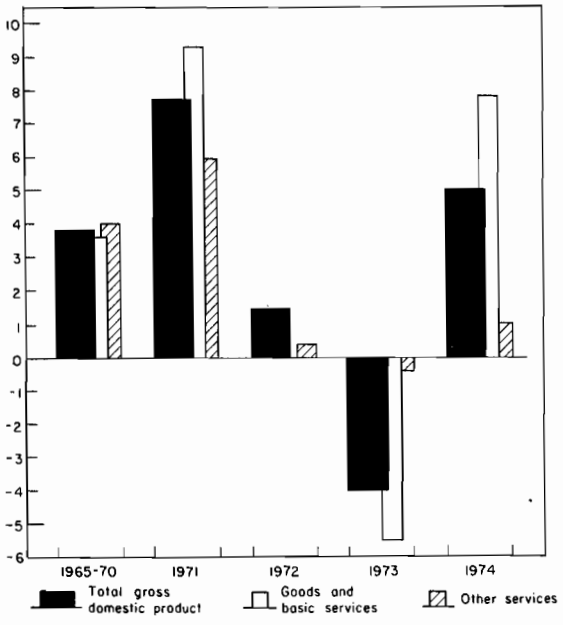


Table 191. Chile: gross domestic product at factor cost, by sector of economic activity

	Millions of escudos at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*[a]	*1974*[a]	*1970*	*1973*	*1970-1972*	*1973*[a]	*1974*[a]
Agriculture	6,386.0	5,324.6	6,247.6	7.8	6.1	−0.5	−15.2	17.3
Mining	10,101.0	10,195.3	12,182.8	12.3	11.7	−0.6	2.1	19.5
Manufacturing	23,569.6	26,260.0	26,428.0	28.7	30.2	8.5	−5.3	0.6
Construction	3,610.9	3,130.0	3,552.0	4.4	3.6	−0.7	−12.0	13.5
Subtotal goods	*43,667.5*	*44,909.9*	*48,410.4*	*53.2*	*51.6*	*4.4*	*−5.6*	*7.8*
Electricity, gas and water	1,245.4	1,606.4	1,735.7	1.5	1.8	13.0	1.0	8.0
Transport and communications	4,904.2	...	...	6.0	...	3.5	...	...
Subtotal basic services	*6,149.6*	...	...	*7.5*	...	*5.5*	...	...
Commerce and finance	14,888.5	...	...	18.1	...	5.4	...	...
Government	5,541.0	...	...	6.7	...	3.5	...	...
Ownership of dwellings	1,354.5	...	...	1.6	...	−0.2	...	...
Miscellaneous services	10,642.0	...	...	12.9	...	5.4	...	...
Subtotal other services	*32,426.0*	...	...	*39.3*	...	*4.9*	...	...
Subtotal services	*38,575.6*	*42,083.1*	*42,610.7*	*46.9*	*48.4*	*5.0*	*−1.0*	*1.3*
Total	*82,243.1*	*86,225.7*	*90,536.4*	*100.0*	*100.0*	*4.5*	*−4.0*	*5.0*

SOURCE: ECLA estimates based on official statistics supplied by ODEPLAN.

Note: As the individual activities and the totals were calculated independently, the sum of the former does not correspond exactly with the latter.

[a] Preliminary figures.

production. The explanation of this difference can only be a drop in the proportion of the inputs used by the sector as a whole.[21] This reactivation of agricultural production was motivated to a large extent by the increase in crop farming output, which was around 16 per cent above the previous year's level.

The increase in cereal production was 25 per cent in wheat and maize, which are major crops, while the harvests of oats and barley increased by nearly 40 per cent and rye by over 70 per cent. The only cereal crop showing a decrease (which had in fact been the case for several years already) was rice, with a drop in production of around 38 per cent. Pulse crops showed an increase of slightly over 17 per cent, with a large increase in peas and lentils (over 30 per cent), and a somewhat smaller one in beans and chickpeas (15 per cent for the former and 22 per cent for the latter). Of the industrial crops, sunflower production dropped by 23 per cent while sugarbeet production increased by around 7 per cent. As regards other outputs of the agricultural sector, a substantial increase was to be observed in the potato harvest (62 per cent) and a much smaller increase in fruit and vegetables. Wine-growing dropped by 12 per cent according to first estimates.

According to preliminary estimates, livestock activity grew much more slowly than crop farming and its rate probably fluctuated around 7 per cent. Several of its main components reflected the adverse effect of depressed demand and sharp increases in the price of inputs (poultry and pig production among others).

Production levels in Chilean mining were relatively favourable during 1974. The estimates available give an increase of around 20 per cent, based on an increase of 30 per cent in copper, 11 per cent in iron ore, 12 per cent in coal mining, and 6 per cent in nitrate and iodine. Production of crude oil, however, dropped by 12 per cent.

While the production of large-scale copper mining increased by 24 per cent (exceeding 760,000 tons), medium- and small-scale mining grew by 66 per cent. It is estimated that the output of this last-mentioned sector may have reached 200,000 tons. The comparable figure for 1973 was 120,000 tons.

[21] In support of this opinion, mention may be made of the fact that the increase in agricultural output was based to a large extent on the increase in the harvests of the main annual crops, almost exclusively as a result of the increase in the area under cultivation. During the 1972/1973 crop year there was a decrease of slightly over 20 per cent in the area sown to these crops. In addition, it is possible that the high prices reached by the main inputs during the year (fertilizers, cattle feed, fuels, etc.) influenced this trend.

The increase in the value of the main mineral products during 1974 was decisively influenced by the price increases of nearly all these products on the international market. In the first months of the year, copper reached the highest prices on record,[22] and while these prices dropped sharply after the month of June, the average price for the year was nearly 16 per cent higher than the average price in 1973. The price of nitrate more than doubled compared with the average for the previous year (in 1973 the price per ton was 56.2 dollars and in 1974 it was estimated at 104.7 dollars) while the price of iron also increased, although by a much smaller percentage (approximately 7 per cent).

It is estimated that manufacturing production in 1974 made a slight recovery, which may be expressed as a rate of 0.6 per cent, thus maintaining the level of the 1973 squeeze. As a whole, the industries manufacturing consumer goods showed a drop of about 3 per cent in their level of output, although this was less pronounced than in 1973 (see tables 191 and 192). The only sectors of this industrial group which escaped the downward trend were those manufacturing food products and tobacco. However, some activities in food production, such as the processing of flourmill and bakery products and the manufacture of cocoa and sugar products, remained at levels of production lower than those of 1973. The decline in the production of beverages and in the manufacture of footwear and, to a lesser extent, clothing was particularly pronounced.

The group of industries producing raw materials and intermediate goods was the only sector which achieved positive results on account of the more vigorous growth of the industries manufacturing pulp, paper and paper products (particularly pulp), non-metallic mineral products and basic metal products. However, there was a sharp drop in the leather and leather products industries and in the industry producing chemical substances and products.

[22] On 1 April the price of copper was 1.52 dollars per pound.

Lastly, the industries of the metal manufactures and machinery group also showed a drop in production which was around 5 per cent, and which was basically to be explained by the decrease in the output of machinery (with the exception of electrical machinery) and metal products. The manufacture of electrical articles and transport material showed slight increases.

The growth of construction activity, which was the third sector to make a definite comeback in 1974, reached 13.5 per cent according to preliminary figures supplied by ODEPLAN. Although this percentage contrasted with the decline which affected it in 1973 and the near-stagnation of 1970-1972, it was not sufficient for the sector to recover the level of activity it had achieved in 1970.

Fiscal expenditure on public works and the construction of dwellings showed a relatively large increase, especially during the last quarter of the year. Government expenditure on construction was mainly aimed at completing work begun in earlier periods (especially dwellings) rather than at beginning new construction work. A sharp decrease was noted in contracting as well as in the actual start of construction work in 1974.

The construction of dwellings financed by the private sector, recorded a considerable comeback, especially in the second half of the year. Available data on the surface area of dwellings constructed by this sector give an increase of nearly 25 per cent for the first 10 months of the year (monthly averages in 1973 and 1974). The activity of the Savings and Loan System (SINAP)—at least 80 per cent of private investment which goes into the construction of dwellings involves financing from SINAP—was the decisive factor of the boom in private construction.

4. TOTAL SUPPLY AND DEMAND

Total supply was 4.2 per cent up on its 1973 level, but grew less than the gross domestic product owing to the slight decrease in the volume of

Table 192. Chile: manufacturing production index

	1972	*1973*	*1974*
Manufacturing	105.6	100.0	100.6
Consumer goods industries	106.3	100.0	97.0
Intermediate goods industries	107.0	100.0	103.0
Metal manufactures and machinery industries	95.8	100.0	95.0

SOURCE: ECLA, on the basis of statistics supplied by INE, Index of manufacturing output and SOFOFA, indexes and percentage variation in volume (monthly bulletins).

imports of goods and services (0.6 per cent). This means that the larger supplies of goods and services in 1974 were exclusively due to the growth of domestic output. The ratio of imports to the gross domestic product, which had increased from 15.5 per cent to nearly 17 per cent between 1970 and 1973, dropped to 16 per cent in 1974 (see table 193).

As regards the evolution of total demand, exports of goods and services (expressed in constant values) constituted the most dynamic component, since they increased at the rate of 27.2 per cent in contrast with the decline experienced in the period 1970-1972 and in 1973 (1.2 per cent and 1.7 per cent respectively). This growth in the volume of exports is attributable to the favourable results obtained in the production of copper, and of other less important items; this situation is commented upon in the part of this study dealing with the external sector. The coefficient relating the volume of exports to the gross domestic product changed from 15.8 per cent in 1970 to 14.4 per cent in 1973 and to 17.5 per cent in 1974.

The other element of total demand which stood out as a driving factor in the domestic economy was investment expenditure. Gross fixed capital formation increased in 1974 by 8.5 per cent; this rate was inadequate but denoted a recovery compared with earlier years. Between 1970 and 1972 it had decreased by an annual average of 9.3 per cent and in 1973 it dropped by 15 per cent. This development in fixed investment was also manifested in a decrease in the coefficient of investment in relation to the product from around 15 per cent in 1970 to nearly 10 per cent in 1973, while it remained at a similar level in 1974.

Construction expenditure became the dynamic element of fixed investment in 1974, when it increased by nearly 14 per cent. Investment in machinery and equipment increased very little (not more than 2 per cent) as a result of the insignificant increase in imports of capital goods and the standstill in national output of these goods.

According to partial data, total consumption declined for the second year running as a result of the pronounced drop in private consumption. Among the indirect indicators which would support this, are the decrease in the production of industrial consumer goods (3 per cent) and the drop of approximately 6 per cent in the average

Table 193. Chile: total supply and demand

	Millions of escudos at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*[a]	*1974*[a]	*1970*	*1973*[a]	*1970-1972*	*1973*[a]	*1974*[a]
Total supply	*107,031*	*113,626*	*118,391*	*115.5*	*116.9*	*4.6*	*-2.9*	*4.2*
Imports[b]	14,358	16,465	16,372	15.5	16.9	5.0	4.1	-0.6
Gross domestic product	92,673	97,161	102,019	100.0	100.0	4.5	-4.0	5.0
Total demand	*107,031*	*113,626*	*118,391*	*115.5*	*116.9*	*4.6*	*-2.9*	*4.2*
Exports[b]	14,591	14,004	17,807	15.8	14.4	-1.2	-1.7	27.2
Domestic demand	92,440	99,622	100,584	99.7	102.5	5.4	-3.1	1.0
Gross domestic investment	15,796	..	...	17.0	...	-6.8	...	...
Gross fixed investment	13,818	9,667	10,489	14.9	9.9	-9.3	-15.0	8.5
Construction	7,478	...	...	8.1	...	...	...	...
Machinery and equipment	6,340	...	...	6.8	...	...	...	...
Total consumption	76,644	89,955	...	82.7	92.6	7.8	-1.6	...
General government	12,613	15,439	...	13.6	15.9	9.3	2.5	...
Private	64,031	74,516[c]	...	69.1	76.7	7.5	-2.4	...

SOURCES: 1970-1973: ECLA calculations based on figures supplied by ODEPLAN; 1973-1974: ECLA estimates based on preliminary official statistics.

Note: The figures for exports and imports of goods and services were taken from balance-of-payments data expressed in dollars at current prices, which were converted to constant 1970 values by deflation, using price indexes calculated by ECLA for the purpose.

[a] Preliminary figures.

[b] Goods and services, excluding factor payments.

[c] Including increases in stocks.

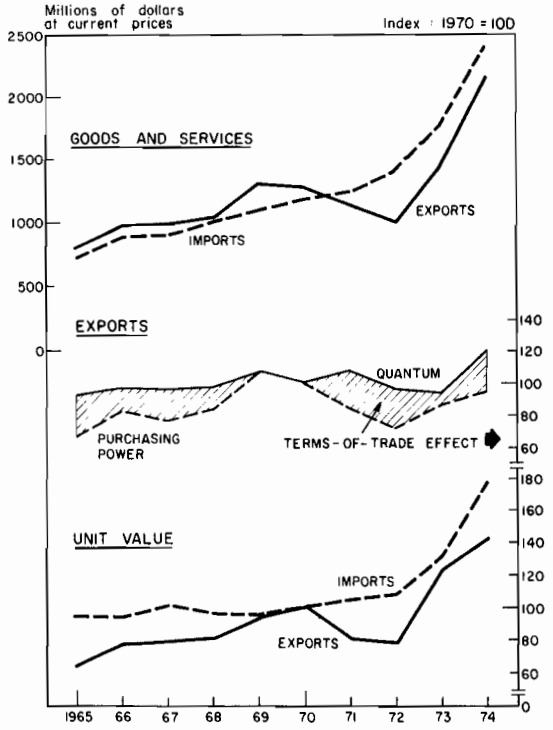
level of real wages. General government consumption expenditure maintained its 1973 growth rate (2.5 per cent).

5. THE EXTERNAL SECTOR

The general evolution of external trade in Chile in the course of 1974 was satisfactory but actually concealed fairly dissimilar performances in the two halves of the year. While income from exports increased considerably during the first half of the year, enabling the country's reserves to increase and a favourable balance-of-payments situation to be achieved, in the second half of the year there was a diametrically opposed situation, when income from exports decreased sharply, and generated a deficit in the balance of payments.

The value of exports of goods amounted to 2,070 million dollars in 1974. For the second year running a large increase was recorded of around 54 per cent, doubling the average value of exports in the period 1970-1972. As distinct from what happened in other Latin American countries in the past year, the major part of this increase was due to an increase in the volume exported (33.2 per cent), since prices went up much less (16.5 per cent).

Figure XX. Chile: trend of external variables
Natural scale



This trend was influenced to a great extent by the increase in copper exports—the value of which rose 45 per cent during the year (from 1,103 million dollars in 1973 to 1,600 million in 1974)—owing to an increase of 26 per cent in the volume exported and a rise of 15.5 per cent in price. These results were made possible by the conjunction of two factors: the favourable conditions as regards prices in the international markets during the first half of the year, and the existence of spare production capacity in the mining centres, which enabled Chile to expand its production and increase its shipments abroad.

This situation was substantially modified in the second half of the year owing to the sharp drop in international copper prices, which brought Chile and the other member countries of CIPEC to reduce production by around 10 per cent towards the end of the year, as a measure aimed at moderating the downswing in prices. To illustrate the sharp drop in the price of copper between the two halves of the year, it may be observed that while the average price during the first six months of 1974 was 117.7 US cents per pound of electrolytic copper, in the second six months this price dropped to an average of 70 cents, i.e., a decrease of 40.5 per cent.

While this was the situation in exports, expenditure on imports also increased sharply, although at a much slower rate. Consequently, the trade deficit recorded in 1973 was converted into a surplus of 150 million dollars in 1974, which helped to reduce the deficits on current account and in the balance of payments before compensation.

The value of exports of other mining products increased by 51 per cent, with a more considerable improvement in the unit value than in the volume exported. The increase in exports of nitrate and iron ore were decisive factors in the above results.

The export items with the most significant increases in 1974 were agricultural and marine products and manufactures. These exports increased 2.3 times in value (from 145 million dollars in 1973 to 330 million in 1974). Industrial products, with a value exceeding 270 million dollars, achieved an increase in 1974 which more than doubled the value and volume of the previous year (see table 194). The items which had most influence on these results were fish meal (shipments of which had increased by 492 per cent in tonnage in the first 10 months of the year) and pulp and paper, the 1974 value of which quadrupled the 1973 level. The increases recorded in exports of semi-processed copper and transport material were also significant. Lastly, the value of exports of agricultural and marine products more than doubled the 1973 levels in 1974, reflecting to

Table 194. Chile: exports of goods

	Year		Variation 1974 (percentages)	
	1973[a]	1974[a]		
	(millions of dollars)		Value	Quantity
1. Mining products	1,206.9	1,749.9	45.0	25.0
Copper	1,102.6	1,600.0	45.1	25.6
Others	99.3	149.9	51.0	17.4
2. Agricultural and marine products	25.0	55.0	120.0	64.4
3. Industrial products	120.0	273.3	127.8	100.8
Total goods	*1,346.9*	*2,078.2*	*54.3*	*32.4*
Total goods (excluding copper)	*244.3*	*478.2*	*95.7*	*63.2*

SOURCE: ECLA, on the basis of data supplied by the Central Bank of Chile, Foreign Trade Section.
[a] Provisional figures.

a large extent the satisfactory recovery of agricultural activity in the course of the year.

As a result of the dynamism of exports of agricultural and industrial products, compared with copper, the share of income generated by copper in the total value of exports of goods dropped from 82 per cent in 1973 to 77 per cent in 1974.

The exchange policy followed during the period under analysis, which consisted of periodic and differentiated adjustments in the value of foreign exchange so as to maintain its real value and achieve the unification of the different areas of exchange,[23] meant an important stimulus to the growth of exports (mainly those originating in the manufacturing, agricultural and small- and medium-scale mining sectors). The bank market rate was adjusted by 372 per cent between December 1973 and December 1974 (from E° 343.23 to E° 1,619 per United States dollar) and the brokers' market rate was adjusted by 124 per cent (from E° 775.16 to E° 1,737 per dollar). The difference between the rates in the two areas of exchange, which was 126 per cent in December 1973, was reduced to slightly over 7 per cent in December 1974.

It is interesting to compare the evolution of the exchange rate and of domestic prices in the course of the year. Table 195 gives these variations for each quarter of 1974.

As may be seen, during the first half of the year, the evolution of the rates in the two areas

Table 195. Chile: quarterly variation in exchange rates and prices
(*Percentages*)

Period	Exchange rate		Consumer price index
	Bank market rate	Brokers' market rate	
1st quarter	40.7	−3.8	62.2
2nd quarter	50.1	6.7	51.4
3rd quarter	40.8	36.1	24.1
4th quarter	58.6	60.4	38.9
Year 1974	*371.7*	*124.1*	*375.9*

SOURCES: Basic figures, Banco Central de Chile *Boletín Mensual*; and National Institute of Statistics, consumer price index.

lagged behind the increase in prices, but it was the bank market rate which was particularly out of step. While the level of consumer prices increased by 62 per cent in the first quarter and 51 per cent in the second, the bank market rate increased by 40.7 per cent and 50.1 per cent respectively over the same periods, and the brokers' market rate dropped by nearly 4 per cent in the first quarter and increased by merely 6.7 per cent in the second.

In the last two quarters, the adjustments in the foreign exchange rates in both markets exceeded the increase in domestic prices during these periods. As a result of these trends, while the level of prices rose 376 per cent in 1974, the bank market rate increased by 372 per cent, and the brokers' market rate by 124 per cent, as has already been mentioned.

Imports also increased sharply (39 per cent), although at a much slower rate than exports,

[23] The differentiated exchange rate which existed for copper returns reached the same level as the bank market rate as from August, thus reducing the areas of exchange to two as from this date.

Table 196. Chile: imports and exports of goods, 1974
(*Percentage variation*)

Imports of goods	
Value	38.9
Volume	1.4
Unit value	36.9
Exports of goods	
Value	53.7
Volume	33.2
Unit value	15.5

SOURCE: ECLA, on the basis of official statistics.

which brought the value of imports of goods to slightly over 2,200 million dollars. This increase was almost exclusively due to increases in prices. The index of the unit value of imports rose 37 per cent, while the quantum index went up by barely 1 per cent, in contrast to what happened in the case of exports where an increase of 54 per cent in value is attributable to an increase in volume of 33 per cent (see table 196).

In the performance of the different import items, of special importance was the sharp drop in imports of food and also the considerable growth of imports of intermediate goods (see table 197). Purchases of food-stuffs (finished products and raw materials for the food industry) expressed in current values, decreased by 21 per cent compared with their 1973 level. If it is considered that the prices of these products on the international market increased sharply during 1974, it may be concluded that the decrease in the volume of imported foods was much greater (it is estimated to exceed 40 per cent).

In imports of intermediate goods the increase in current values reached 103 per cent; of particular importance was the increase in the fuels and lubricants group, which in 1974 more than tripled its 1973 value owing to the increase in petroleum prices. Also of importance was the growth of purchases abroad of raw materials and spare parts, the values of which increased by 73 per cent and 97 per cent respectively compared with the 1973 levels.

In contrast, imports of capital goods grew by just over 18 per cent, while expressed in real terms they would show an even more modest growth rate.

As a result of the much faster growth of exports compared with imports, the trade deficit of 37 million dollars recorded in 1973 was converted into a surplus of about 150 million dollars in 1974, which is equal to a little over 121 million SDR units.

However, net expenditure on services increased by around one third in relation to the 1973 level, and net remittances of profits and interest abroad also rose considerably (from 74 to 128 million SDR units, i.e., by 73 per cent). This increase was mainly due to the increased expenditure in the course of the year in the form of interest on the long-term debt, the payment of which had been postponed in 1973. Remittances of profits abroad amounted to 7.5 million SDR units in 1974, while the interest on external credit lines underwent no variation.

In spite of the increased expenditure on services and payments on foreign capital, the current account deficit was reduced by 23 million SDR units, from 338 million in 1973 to 315 million in 1974 (see table 198).

In the evolution of the capital account of the balance of payments, preliminary data show that during 1974 the economy of Chile had a total net inflow of non-compensatory capital estimated at 225 million SDR units. Of this, 50 per cent corresponded to net income from foreign capital and the other 50 per cent to assets owned by

Table 197. Chile: CIF imports of goods

	1973[a]	*1974*[a]	*Variation in 1974*
	(*millions of dollars*)		(*percentages*)
Food	594.9	472.0	–20.7
Consumer goods other than food	64.0	70.4	10.0
Intermediate goods	663.8	1,350.5	103.4
Raw materials	352.5	610.8	73.3
Spare parts	141.3	278.0	96.7
Fuels and lubricants	120.0	372.7	210.6
Products of large-scale copper mining	50.0	89.0	78.0
Capital goods	285.0	338.0	18.6
Total	*1,607.7*	*2,230.9*	*38.8*

SOURCE: ECLA, on the basis of data provided by the Central Bank of Chile, Foreign Trade Section.

[a] Provisional figures.

Table 198. Chile: balance of payments
(Millions of SDR units)

	1970	1971	1972	1973	1974[a]
Current account					
Exports of goods and services	1,278.0	1,132.0	923.0	1,197.9	1,805.9
Goods FOB	1,135.0	984.0	790.0	1,098.4	1,693.7
Services	143.0	148.0	133.0	99.5	112.2
Transport	70.0	75.0	70.0	70.5	79.0
Travel	50.0	50.0	46.0	16.6	19.1
Imports of goods and services	1,183.0	1,231.0	1,297.0	1,462.0	1,996.4
Goods FOB	848.0	919.0	1,003.0	1,128.7	1,572.3
Services	335.0	312.0	294.0	333.3	424.1
Transport	194.0	210.0	218.0	260.3	345.1
Travel	86.0	46.0	13.0	27.4	29.1
Net external investment income	−164.0	−137.0	−98.0	−73.8	−128.1
Profits	−148.0	−72.0	−2.0	–	−7.5
Interest	−16.0	−65.0	−96.0	−73.8	−120.6
Net private transfer payments	–	–	–	–	3.3
Balance on current account	−69.0	−236.0	−472.0	−337.9	−315.3
Capital account					
Net external financing (*a* + *b* + *c* + *d* + *e*)	69.0	236.0	472.0	337.9	315.3
(*a*) Net external non-compensatory capital	247.0	−31.0	239.0	128.1	
Direct investment	41.0	−42.0	–	–	
Long- and medium-term loans	380.0	245.0	507.0	217.6	
Amortization payments	−140.0	−192.0	−361.0	−92.8	
Short-term liabilities	−34.0	−42.0	87.0	–	225.3
Official transfer payments	–	–	6.0	3.3	
(*b*) Domestic non-compensatory capital or assets	−7.0	25.0	−13.0	–	
(*c*) Errors and omissions	−103.0	−22.0	43.0	−0.1	
(*d*) Allocation of SDRs	21.0	17.0	17.0	–	–
(*e*) Net compensatory financing (increase −)	−89.0	247.0	186.0	209.9	90.0
Balance-of-payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	5.0	102.0	125.0	192.4	...
Amortization payments	−73.0	−40.0	−4.0	–	...
Movements of foreign exchange reserves (increase −)	8.0	202.0	29.0	15.8	...
Movements of gold reserves (increase −)	−7.0	−1.0	–	–	...
SDRs (increase −)	−22.0	−16.0	36.0	1.7	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26.

[a] Estimates based on official statistics.

persons resident in Chile, the inclusion of which was made possible under facilities granted by the Central Bank in the form of measures for legalizing holdings of foreign exchange. It should be mentioned that the net inflow of funds—which was less than in 1973—was the result of a credit for 338 million SDR units for the use of external loans and an outflow of 226 million SDR units in amortization payments.

In 1974 the monetary authorities maintained their policy of rebuilding Chile's international reserves, with the accumulation of a sum of around 244 million SDR units. Although this was the amount of gross reserves, the exceptionally large increase in external liabilities—as a result of the renegotiation of debts and the utilization of the oil facility to offset increased fuel costs—led to a deficit of 90 million SDR units in the balance of payments. In any case, this deficit was less than half that recorded in 1973 (210 million SDR units) (see table 198).

6. PRICES, WAGES AND EMPLOYMENT

(a) *Prices*

In the evolution of domestic prices in 1974, the two most noteworthy elements were the decrease in the growth rate of prices, especially during the second half of the year, although they remained at very high levels, and the marked process of change taking place in the system of relative prices.

If the trend described is measured against the consumer price index, it may be seen that the increase in prices between December 1973 and December 1974 was 375.9 per cent compared with 508.1 per cent between December 1972 and December 1973. In the first 6 months of the year, consumer prices increased by 145.6 per cent, while

in the second half of the year, this percentage dropped to 93.8 per cent.[24] The variations in the main components of this indicator (see table 199) showed a sharper increase in the prices of food, housing and miscellaneous items, while clothing showed smaller increases.

The price increases in wheat products (basically bread) and in food and vegetables, especially in the first half of the year, had a decisive influence on the performance of the food sector. Also important were the price increases recorded in oils, sugar and sweets and milk products, but their impact was less marked since they carried less weight in the basket of goods used to calculate the index. The prices for other food products showed more moderate increases, especially in the case of meat, poultry and fish, and also preserves and concentrates.

The increase in the prices of housing basically reflected the increases which had taken place in items such as rent, water supply, fuels and electricity, while the increase in expenditure on transport and communications was a decisive element in the high percentage represented by the miscellaneous section.

A consideration of the importance which each item of expenditure has in the consumer price index shows that food was responsible for an increase of 43 per cent in the general level of prices in 1974, while expenditure on housing had a share of 26 per cent and miscellaneous expenditure a share of 25 per cent; the share of clothing was 6 per cent.

As regards the evolution of wholesale prices, the index showed a growth rate for the year of 570.6 per cent (December to December), giving–as for consumer prices–a reduction in the annual rate and in the rate for the second half of the year compared with the first half (see table 199). The prices of local products increased by 518 per cent, basically as a result of the increase in industrial prices, which increased by 527 per cent. The manufactured items with the highest increases included food and beverages (588 per cent), chemical and petroleum products (635 per cent), metal products (625 per cent) and electric energy for industrial purposes (4,642 per cent). The lowest price increases took place in articles produced by the textile industry (216 per cent) and the clothing industry (322 per cent). The increase in prices of construction materials was also fairly low (390 per cent).

Although agricultural products as a whole showed smaller price increases (381 per cent), their main components gave evidence of markedly uneven variations. While the prices of the agricultural sector rose at a rate which exceeded the average for domestic products (532 per cent), those from the livestock and fishing sectors increased at much more moderate rates, the former by 288 per cent and the latter by 104 per cent.

The section including mining products grew most during the year (823.4 per cent), especially

[24] There was a weakening of this trend in the first months of 1975. In March 1975 the consumer price index had grown by 60.9 per cent, compared with 62.2 per cent for the same period in 1974.

Table 199. Chile: evolution of consumer and wholesale prices
(Percentage variation)

	1973	*1974*		
	December to December	*December to December*	*Up to June*	*Up to December*
		(a) *Consumer prices*		
General index	508.1	375.9	145.6	93.8
Food	474.2	392.0	138.8	106.1
Housing	408.5	437.5	184.2	89.1
Clothing	646.6	172.4	74.3	56.3
Miscellaneous	599.3	446.4	209.2	76.7
		(b) *Wholesale prices*		
General index	1,147.1	570.6	189.1	132.0
National products	1,021.2	517.5	191.1	112.2
Agricultural	512.9	381.0	116.7	122.0
Mining	1,503.1	823.4	305.7	127.6
Industrial	1,244.2	527.4	200.0	109.1
Imported products	1,692.2	714.5	183.6	187.2

SOURCE: National Institute of Statistics, consumer price index and wholesale price index.

in the first half of the year, since in the second half the rate of change in its prices decreased notably. This performance basically followed the evolution of copper prices on the international market during this period.

Prices of imported goods recorded one of the largest increases among the components of the general index (715 per cent), despite which this increase was only of relatively less importance, owing to its low weighting in the wholesale price index.

Imported goods of vegetable origin, as well as chemical products and petroleum products, experienced the most accelerated price increases (1,031 per cent for the former and 757 for the latter). Among the first, the magnitude of the increase in raw sugar and cotton, and among the second crude oil, stood out. The prices of other imported products evolved within lower limits (between 200 and 300 per cent).

One of the important conclusions which emerged from the analysis of the price indicators was the marked process of change in relative prices recorded in the course of the year.

In intersectoral terms, it may be observed that during the period there was a change in the price ratio of agricultural goods to industrial goods, markedly in favour of the latter. This basically occurred in the first half of the year, when the price ratio changed by nearly 40 per cent, and then remained practically at this level for the rest of the year. This result was undoubtedly adverse for the agricultural sector as a whole, and was basically due to the less pronounced variations in prices which affected the products of the livestock sector (particularly meat). The proof of this was that the livestock/crop production price ratio changed in the course of the year by 60 per cent in favour of agricultural goods.

As important as the changes which took place in the relative prices of the different sectors of the economy was the change in prices of goods and services considered individually. Table 200 shows the percentage variation in the prices of a selected group of food-stuffs in 1974.

As may be observed, while the prices of products such as bread, tea and sugar increased between seven and 10 times, those of other products such as meat and fish increased by less than one and a half times.

The price ratio of domestic goods to imported goods evolved in 1974 to the advantage of the latter. All in all, this result was influenced by the constant increase during the year in prices of imports—at similar rates in both halves of the year—and by the decrease in the growth rate of industrial prices in the second half of the year. It should be borne in mind that the increase in the prices of imported products reflects both their increase on the world markets and the periodical exchange devaluations which took place during the year.

As will be seen in figure XXI, the prices of imported goods (expressed in national currency) have increased more rapidly than domestic prices since before 1970, but the widest gap between the two indicators occurred in 1973 and 1974.

(b) *Wages*

The basic objective of the wage policy applied in 1974 was to maintain the average purchasing power of 1973 wages, the level of which was 26 per cent lower than the average for 1970. In order to attain this goal, a wage policy was implemented which, through periodic adjustments and special allocations to the lowest-income sectors, would make it possible to avoid sharp fluctuations in real wages and protect the purchasing power of these groups (see table 201).

As may be seen, in only two months of the year was the Government's target slightly exceeded (January and December), while in another three (July, August and September) there was a fair approximation to the target. During the other months, the purchasing power of wages and salaries was below the average 1973 level, while the decrease in the real incomes of wage-earners which took place between January and April was fairly pronounced (about 20 per cent). The relative recovery in real wages which took place in the months of May and June coincided with the

Table 200. Chile: variation in prices of some food products

Product	*Percentage variation between November 1973 and December 1974*
Bread	1,025
Tea	780
Sugar	733
Noodles	662
Oil	580
Pasteurized milk	567
Rice	311
Pulses	294
Eggs	250
Poultry meat	146
Cheap stewing-steak	100
Hake	79
Beef sirloin	72

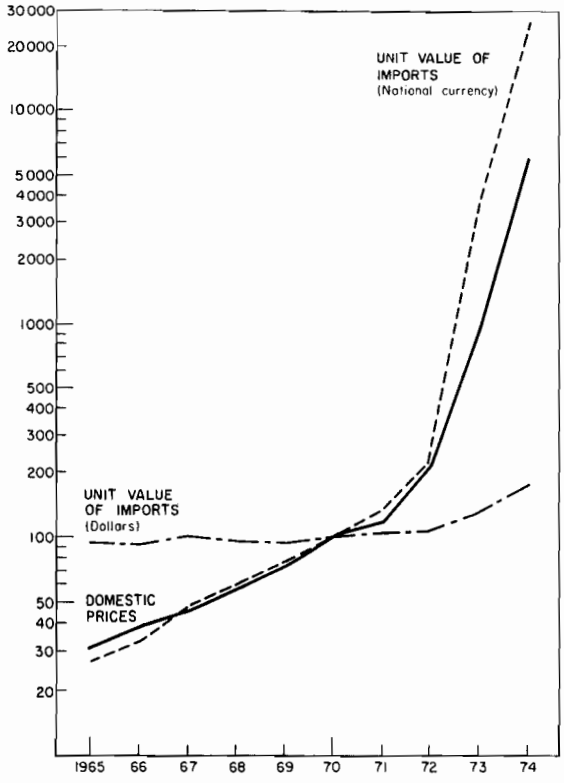
SOURCE: ECLA, based on Patricio Meyer and Jaime Ruiz Tagle P., *"El poder adquisitivo de los sectores populares y medios"*, *Mensaje* 236, January-February 1975.

Table 201. Chile: index of real wages and salaries in 1974
(Average 1973 = 100)

January	102.02	July	98.09
February	90.65	August	99.31
March	87.00	September	97.69
April	82.13	October	90.24
May	94.44	November	90.38
June	93.76	December	102.42
Average first half of the year	91.67	Average second half of the year	96.36
Average for 1974 = 94.0			

SOURCE: Universidad de Chile, Departamento de Economía, *"Comentarios sobre la situación económica, 2º semestre de 1974"* (Publication No. 18).

Figure XXI. Chile: indexes of unit value of imports and of domestic prices
(Index: 1970 = 100)
Semi-logarithmic scale



general adjustment of wages and salaries granted at this time, and with the inclusion and extension of other additional and special benefits of a compensatory nature (family, collation, transport, length of service, and other allowances). In the second half of the year the frequency of the adjustments in wages and other benefits was increased, and the fluctuations in the index became less intensive, while as from 1 October a system of automatic quarterly adjustments of wages and salaries was introduced. All in all, actual achievements remained below the target of 6 per cent fixed for 1974, while the decrease in the purchasing power of wages was much more pronounced in the first half of the year than in the second. In the first six months the decrease slightly exceeded 8 per cent and in the second six months it stood at around 4 per cent.

The drop in real average income which took place in 1974 probably varied in intensity in the different income receiving sectors. According to estimates by the Department of Economics of the Universidad de Chile, average real liquid wages in the fiscal sector decreased by 19 per cent compared with levels in the month of January 1974. Among the wage-earners of this sector there are some employees who have lost more than others and even some who have increased their real earnings, as may be seen from table 202.

Lastly, the sharper decline in the real earnings of the public sector than in average over-all wages, was offset by the fact that in the private sector the real income of the wage workers may have decreased to a lesser extent, or even increased in some cases.

(c) *Employment*

The only quantitative data in existence on the evolution of employment in 1974 as this note is written, are the quarterly reports prepared by the National Institute of Statistics (INE) and the Department of Economics of the Universidad de Chile on employment and unemployment in Greater Santiago. It may be observed that more than one third of the country's population is concentrated in this urban centre, as well as a majority share of industrial, commercial and service activities.

Table 202. Chile: index of real liquid wages, single scale
(January 1974 = 100)

	Annual average
Grade 35	97.3
Grade 33	91.7
Grade 25 without professional allocation	77.1
Grade 25 with professional allocation	86.7
Grade 17 without professional allocation	73.0
Grade 17 with professional allocation	84.1
Grade 8 without professional allocation	72.6
Grade 8 with professional allocation	84.2
Grade 4 without professional allocation	73.0
Grade 4 with professional allocation	85.1

SOURCE: Universidad de Chile, Departamento de Economía, *"Comentarios sobre la situación económica, 2º semestre de 1974"* (Publication No. 18).

According to these data, the volume of employment in Greater Santiago in 1974 grew much less than the labour force, and consequently the level of unemployment increased substantially. Between December 1973 and December 1974, according to the INE sample, employment increased by 1.7 per cent, the number of persons entering the labour force by 6 per cent, and the rate of unemployment increased from 5.6 per cent to 9.4 per cent. A similar trend may be observed in the study being prepared by the Department of Economics of the Universidad de Chile, although with a smaller difference between employment and the labour force.

If unemployment throughout the year is analysed it may be observed that, in an increasing trend, the highest level of unemployment was found between the months of June and October. In June, the unemployment rate given by the Department of Economics reached 10.3 per cent, and in October the INE index showed its highest level of 10.4 per cent.

Of the components of unemployment, both the out-of-work rate and the rate for persons seeking work for the first time increased between December 1973 and December 1974. However, the out-of-work index showed a decrease in the second half of the year. While it amounted to 7.5 per cent in June, it was 6.8 per cent in September and 6.1 per cent in December.

It may also be deduced from the survey of the Department of Economics that there was a generalized spread of unemployment to all the sectors of economic activity; the highest sectoral rates were for activities producing goods (8.3 per cent), especially construction (12.6 per cent), while services showed a lower rate (5.1 per cent).

ECUADOR[25]

1. Recent economic trends

In 1974, the gross domestic product rose by 9.2 per cent, which is slightly lower than the 1973 rate but higher than that recorded for 1970-1972. The trend of the total product was basically the result of a drop in the growth rate of mining activity in relation to 1973, the first complete year of petroleum production in the country. The construction and transport and communications sectors also reduced their rates of expansion. In contrast, the growth rate of agriculture, manufacturing and government activity improved (see table 203 and figure XXII).

[25] See, in Part One of this *Survey*, the section dealing with Ecuador in the chapter on inflation.

Table 203. Ecuador: gross domestic product at factor cost, by sector of economic activity

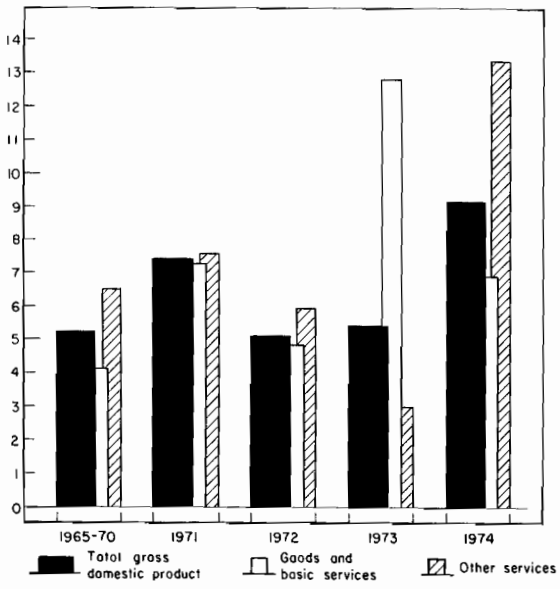
	Millions of sucres at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970-1972*	*1973*	*1974*[a]
Agriculture	9,404	9,555	9,794	29.9	23.2	1.5	−1.4	2.5
Mining	449	2,827	2,940	1.4	6.9	55.0	170.3	4.0
Manufacturing	5,713	7,397	8,436	18.2	19.9	7.9	11.1	14.0
Construction	1,387	1,807	1,957	4.4	4.6	8.0	11.7	8.3
Subtotal goods	*16,953*	*21,586*	*23,127*	*53.9*	*54.6*	*5.9*	*13.5*	*7.1*
Electricity, gas and water	418	...	...	1.3	...	6.6	...	...
Transport and communications	2,091	2,625	2,773	6.7	6.6	6.9	9.6	5.6
Subtotal basis services	*2,509*	*3,096*	*3,252*	*8.0*	*7.7*	*6.9*	*7.9*	*5.0*
Commerce and finance	4,505	5,374	6,171	14.4	14.6	8.7	1.0	14.8
Government	3,275	3,664	4,415	10.4	10.4	4.0	3.4	20.5
Ownership of dwellings	1,948	2,378	2,527	6.2	6.0	7.2	6.3	6.3
Miscellaneous services	2,238	2,630	2,815	7.1	6.7	6.3	4.0	7.0
Subtotal other services	*11,966*	*14,046*	*15,928*	*38.1*	*37.7*	*6.8*	*3.1*	*13.4*
Total	*31,428*	*38,728*	*42,307*	*100.0*	*100.0*	*6.2*[b]	*9.3*[b]	*9.2*

SOURCES: 1970-1973: ECLA calculations based on figures supplied by the Central Bank of Ecuador; 1974: ECLA estimates based on statistics from the same source.

[a] Preliminary figures.

[b] The discrepancy between the growth rate in this table and that in the table on total supply and demand is due to the fact that they measure different concepts of the product (in the first case at factor cost, and in the second at market prices).

Figure XXII. Ecuador: growth of gross domestic product
(Annual growth rates)
Natural scale



Total supply of goods and services rose at a higher rate than the gross domestic product, since the volume of imports of goods and services increased significantly. On the total demand side, a contraction is noted in the volume of exports of goods and services and a substantial rise in capital formation, following others observed in previous years. Thus, the ratio of gross investment to the gross domestic product has risen steadily, from 19.5 per cent in 1970 to 24.4 per cent in 1974 (see table 204).

The main development in the external sector was the sharp increase in the export and import trade. Exports of goods and services, in terms of SDR units, rose 113 per cent, in response to the increase in the international prices of petroleum and, on a lesser scale, sugar and cocoa. Imports of goods and services rose by 65 per cent, owing to

Figure XXIII. Ecuador: trend of external variables
Natural scale

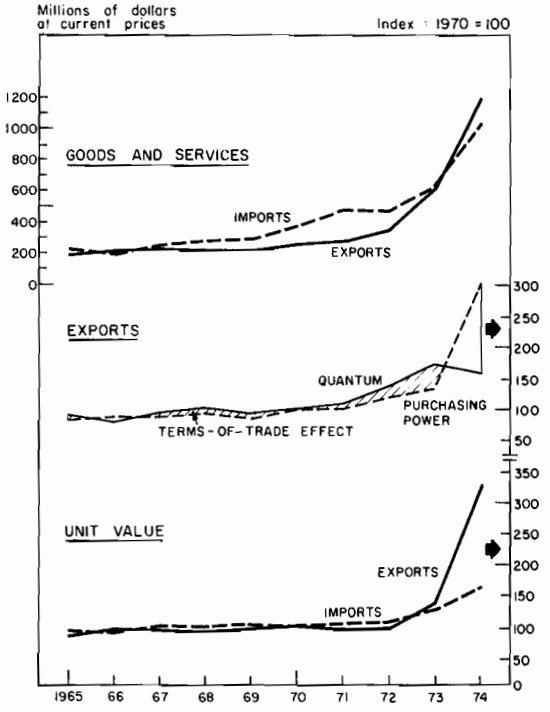


Table 204. Ecuador: total supply and demand

	Millions of sucres at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970-1972*	*1973*	*1974*[a]
Total supply	*43,130*	*54,329*	*61,068*	*121.5*	*126.0*	*6.5*	*11.1*	*12.4*
Imports[b]	7,629	9,967	12,617	21.5	26.0	7.2	13.8	26.6
Gross domestic product	35,501	44,362	48,451	100.0	100.0	6.3	10.5	9.2
Total demand	*43,130*	*54,329*	*61,068*	*121.5*	*126.0*	*6.5*	*11.1*	*12.4*
Exports[b]	5,590	9,687	8,868	15.8	18.3	16.7	27.2	-8.5
Domestic demand	37,540	44,642	52,200	105.7	107.7	4.9	8.1	16.9
Gross domestic investment	6,936	9,966	11,854	19.5	24.4	12.5	13.6	18.9
Gross fixed investment	6,327	9,323	10,541	17.8	21.8	13.2	15.0	13.1
Total consumption	30,604	34,676	...	86.2	...	3.1	6.6	...
General government	4,152	4,752	...	11.7	...	3.3	7.2	...
Private	26,452	29,924	...	74.5	...	3.1	6.5	...

SOURCES: 1970-1973, ECLA calculations based on figures supplied by the Central Bank of Ecuador; 1974: ECLA estimates based on statistics from the same source.

[a] Preliminary figures.
[b] Goods and services, excluding factor payments.

increases of around 30 per cent in both volume and unit value. The current account reflected a surplus of 83 million SDR units and the total balance-of-payments surplus stood at practically the same figure because the net inflow of non-compensatory capital was reduced.

The rate of inflation spurted, but the most serious maladjustments were concentrated in the first part of the year, particularly as a result of increases in food prices. By the end of 1974 consumer prices had increased by approximately 20 per cent over the year, or a similar rate to that observed in 1973.

2. Major sectors of activity

The agricultural sector grew by 2.5 per cent, that is, at a lower rate than the population, but higher than that recorded in the period 1970–1973. It is estimated that the exportable agricultural surplus increased by about 15 per cent, while production for domestic consumption remained at the same level.

Mining increased its contribution to the gross domestic product by only 4 per cent, since petroleum production rose by less than 3 per cent. OPEC's policy of fixing international oil prices and restricting production in the oil-exporting countries is basically responsible for the small increase in Ecuador's petroleum output.

Manufacturing production rose by 14 per cent; thus the fairly dynamic trend recorded by this sector since the end of the 1960s was accentuated. This brought industry's share of the gross domestic product to 20 per cent, compared with 18.2 per cent in 1970 and about 17 per cent in 1967. The development of manufacturing activity was favourably influenced by the trends of both factory industry and small-scale and artisan industry.

Construction grew at a rate of 8.3 per cent, which is lower than in 1973 but similar to the rate observed in the period 1970–1972.

The goods-producing sectors as a whole increased their contribution to the gross domestic product by 7.1 per cent compared with 13.5 per cent in 1973. Output of the basic services sectors rose by 5 per cent in 1974, which is lower than the rate recorded the previous year (see table 203).

The slower growth rate of the goods-producing and basic services sectors was, however, largely compensated for by the greater activity of the services sectors (a growth of 13.4 per cent in 1974 and 3.1 per cent the year before). This bigger contribution to the gross domestic product was mainly the result of the 20.5 per cent increase in government activity. In this respect, it is estimated that the number of government officials increased by 8.5 per cent and that, in terms of current prices, the total wages and salaries paid by the State rose by around 47 per cent.

3. The external sector

Exports of goods and services rose by 113 per cent, in terms of SDR units, as a result of an increase of over 120 per cent under the head of goods (see table 205). Reflecting, above all, the trend of petroleum sales and the international market conditions for this product, exports of goods dropped by 8 per cent in volume compared with 1973, while their average unit value rose by 138 per cent.

International prices of a number of export commodities increased substantially. The rise in the price of petroleum was 246 per cent, while sugar, cocoa and coffee prices rose 220, 88 and 32 per cent, respectively. In contrast, banana prices went up by only 7 per cent.

Imports of goods and services rose by 65 per cent, and those of goods, considered separately, by 68 per cent. The volume of imports of goods increased by 29 per cent, and the average price paid for them was almost 30 per cent higher than in 1973.

The significant increase in imports was due, among other factors, to the policy of progressive liberalization adopted in view of the increased capacity to import,[26] the expansion of domestic demand, and a certain tendency of local entrepreneurs to stock up imported goods in expectation of a rise in world prices. In addition, the exchange rate has been kept at 25 sucres to the dollar since 1970.

Thanks to the trend of exports and imports of goods and services, the trade balance changed from a deficit of 12 million SDR units in 1973 to a surplus of 225 million in 1974. However, mainly because payments of profits on foreign capital doubled, the balance on current account showed a more moderate movement, from a deficit of 81 million SDR units in 1973 to a surplus of 83 million in 1974.

Since the net inflow of non-compensatory capital amounted to 6 million SDR units, the total balance-of-payments surplus was 89 million SDR units, which includes the increase in the country's net international reserves.

4. The trend of prices and other variables related to the inflationary process[27]

A study of the variations from December to December in the consumer price index in Quito shows that the rate of inflation rose to 21.2 per

[26] This policy included the elimination of prior import deposits in 1973, and an appreciable reduction in customs tariffs in 1974.

[27] A special section in another chapter of this *Survey* is devoted to the study of inflation in Ecuador.

Table 205. Ecuador: balance of payments
(*Millions of SDR units*)

	1970	1971	1972	1973	1974[a]
Current account					
Exports of goods and services	258.0	269.8	326.1	508.4	1,082.6
Goods FOB	234.3	242.9	297.7	476.0	1,048.5
Services	23.7	26.9	28.4	32.4	34.1
Transport	1.1	1.0	5.0	7.7	8.3
Travel	8.5	8.9	8.4	12.3	13.3
Imports of goods and services	375.5	459.7	436.7	520.3	857.2
Goods FOB	266.2	360.7	337.7	407.8	686.8
Services	109.3	99.0	99.0	112.5	170.4
Transport	44.8	58.3	59.2	66.5	101.4
Travel	9.4	11.5	10.1	13.0	15.8
Net external investment income	−29.2	−35.7	−42.0	−83.3	−158.0
Profits	−19.2	−25.2	−31.6	−77.5	−159.6
Interest	−10.0	−10.5	−10.4	−5.8	1.6
Net private transfer payments	7.5	7.7	5.8	13.9	15.8
Balance on current account	−139.2	−217.9	−146.8	−81.3	83.2
Capital account					
Net external financing (*a* + *b* + *c* + *d* + *e*)	139.2	217.9	146.8	81.3	−83.2
(*a*) Net external non-compensatory capital	118.0	193.1	226.9	90.2	
Direct investment	88.6	162.1	138.2	45.0	
Long- and medium-term loans	49.2	49.0	103.1	50.0	
Amortization payments	−27.4	−29.8	−26.1	−27.9	5.8
Short-term liabilities	−1.8	3.8	3.0	5.3	
Official transfer payments	9.4	8.0	8.7	17.8	
(*b*) Domestic non-compensatory capital or assets	4.7	−3.2	−5.1	−8.6	
(*c*) Errors and omissions	16.2	−5.8	16.1	79.7	
(*d*) Allocation of SDRs	4.2	3.5	3.5	–	–
(*e*) Net compensatory financing (increase −)	−3.9	30.3	−94.6	−80.0	−89.0
Balance-of-payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	22.9	20.8	10.6	9.0	...
Amortization payments	−6.5	−11.0	−32.6	−24.9	...
Movements of foreign exchange reserves (increase −)	−21.3	23.3	−75.4	−58.8	...
Movements of gold reserves (increase −)	1.1	0.4	6.2	−6.4	...
SDRs (increase −)	−0.1	−3.2	−3.4	1.1	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26.

[a] Estimates based on official statistics.

cent in 1974, or slightly above the previous year's rate. On the other hand, the variations between annual averages indicate an acceleration from 12.9 per cent in 1973 to 23.4 per cent the following year (see table 206).

Moreover, pursuing the trend observable since the mid-1960s, food prices rose more than the general index in 1974. This trend has been associated with the stagnation of agricultural production and its impact as a structural factor of inflation.

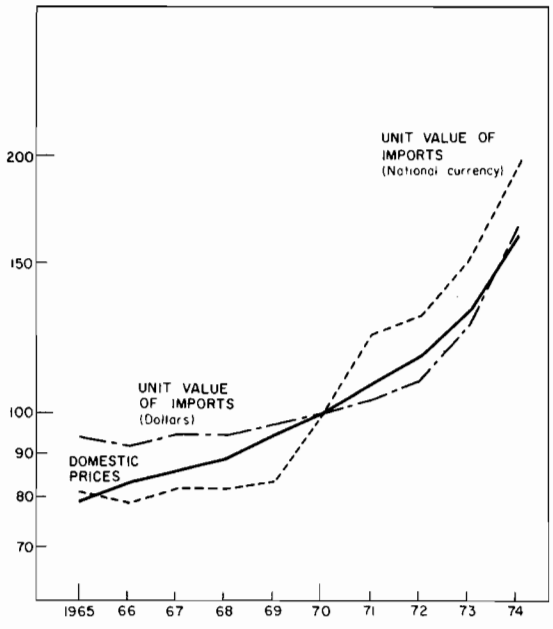
Generally speaking, the trend of the inflationary process in 1974 continued to be defined by

Table 206. Ecuador: consumer price trends in Quito
(*Percentages*)

	1972	1973	1974
Variation from December to December			
(*a*) General index	6.9	20.5	21.2
(*b*) Food and beverages	10.7	31.1	28.0
Variation between annual averages			
(*a*) General index	7.9	12.9	23.4
(*b*) Food and beverages	11.1	20.3	32.4

SOURCE: National Statistical Institute (INE), consumer price index, *Consumidor*.

Figure XXIV. Ecuador: indexes of unit value of imports and of domestic prices
(Index: 1970 = 100)
Semi-logarithmic scale



the same external factors—particularly those linked with the internalization of world inflation (see figure XXIV)—and internal factors as those identified in the special study on the subject. However, it is worth while to add some comments on developments in the fiscal and monetary areas.

As regards central government finance, total current income rose by 87 per cent. The income not directly connected with increasing petroleum output went up by 22 per cent—or somewhat less than the average rise in prices—while income obtained from petroleum rose 330 per cent. The National Development Fund (FONADE)[28] obtained an income of 3,555 million sucres (over 140 million dollars) (see table 207).

Total government expenditure grew by 80 per cent and, if FONADE's disbursements are excluded, the increase was 47 per cent. At constant prices, this increase was about 20 per cent.

The over-all operation of the fiscal finances reflected a surplus of 750 million sucres, in view of the surplus of 1,030 million sucres obtained by FONADE. Therefore, excluding FONADE, the Treasury showed a deficit of 276 million sucres, which was covered by means of internal borrowing to a value of 1,372 million, since at the same time there was a net reduction of 1,096 million in the external debt.

In addition to the expansionist effect produced by the vigorous increase in fiscal demand, the government finances were partly responsible for the increase in the means of payment, to the extent that the foreign currency income of the Government—especially of FONADE—had to be converted into national currency to finance local expenditure. This was a particularly important factor during the first half of the year when, as a result of the over-all balance-of-payments trend, the economy rapidly increased its level of gross international reserves. In the second half of the year, however, the effect was less marked, owing to the decrease in reserves on account of the sharp increase in imports.[29]

[28] The Fund, which operates independently of the budget and finances new investment projects, received all the income from petroleum in excess of the reference price of 7.30 dollars per barrel.

[29] Gross international reserves amounted to 241 million dollars in December 1973, 444 million in June 1974 and 350 million in December of that year.

Table 207. Ecuador: central government finance
(Millions of sucres at current prices)

	1973	*Percentage variation*	*1974*	*Percentage variation*	*FONADE*
1. Current income	7,810	47.0	14,853	86.7	3,555
(*a*) Excluding petroleum	6,167	–	7,517	21.9	–
(*b*) Income from petroleum	1,643	–	7,066	330.1	–
2. Total expenditure	7,692	30.0	13,831	79.8	2,527
(*a*) Excluding FONADE	7,692	–	11,304	47.0	–
(*b*) Expenditure of FONADE	–	–	2,527	–	–
3. Surplus (1 – 2)	118	–75.0	752	–	1,028
4. Composition of surplus	118	–	752	–	–
(*a*) Net external borrowing[a]	46	–	1,096	–	–
(*b*) Net internal borrowing[a]	72	–	–1,372	–	–
(*c*) Surplus of FONADE	–	–	1,028	–	–

SOURCE: ECLA, on the basis of official statistics.

[a] The plus signs indicate that there were net reductions in the external and the internal debt, while the minus signs denote net borrowing.

Table 208. Ecuador: monetary trends
(Millions of sucres at current prices)

	1972	1973	Percentage variation	1974	Percentage variation
I. *Composition of monetary resources*					
1. Money	7,320	8,568	30.7	13,064	36.5
2. Quasi-money	3,019	3,598	19.2	4,604	28.0
3. Bonds	1,844	2,135	15.8	2,568	20.3
4. Other (net)	664	219	–67.0	1,074	390.4
II. *Factors of expansion and contraction*					
5. Net international reserves	3,199	5,874	83.6	9,563	64.3
6. Domestic credit	9,648	9,644	–	11,657	20.9
(*a*) to the Government (net)	(1,821)	(211)	(–88.4)	(–1,458)	(–)
(*b*) to the private sector	(7,827)	(9,433)	(20.5)	(13,115)	(39.0)

SOURCE: IMF, *International Financial Statistics*, May 1975.

Between December 1973 and December 1974 the increase in the money supply was 36.5 per cent, that is, more than the increase in 1973 (see table 208).

A study of monetary trends given in the table shows that the variation in net international reserves and in domestic credit to the private sector acted as factors of expansion, while net credit to the Government (including FONADE) was a factor of contraction. Nevertheless, between 1973 and 1974 the percentage increase in reserves was smaller than in the previous year, while the rate of increase in credit to the private sector accelerated.

EL SALVADOR

1. RECENT ECONOMIC TRENDS

The growth rate of 6 per cent recorded by the Salvadorian economy in 1974 was the highest rate achieved in the current decade (5.2 per cent annually in the period 1970-1973), thus fulfilling the target laid down in the Development Plan (see table 209).

The growth of 7.6 per cent in demand was stimulated in particular by the considerable expansion of public investment and the significant increase in private consumption (8.2 per cent). Public investment, which included sizable inflows of capital supplemented by domestic resources in the form of bank credit, rose at a rate of over 40 per cent. This was the outcome of the convergence of efforts in connexion with a group of projects which, because of their medium- and long-term effects in overcoming the bottlenecks existing in the production system, are the object of continuing attention.[30]

[30] Among the highest priority projects are the construction of the Cerrón Grande hydroelectric dam and promotion of the Ausoles de Ahuachapán Geothermic Project which will enable better use to be made of natural resources for energy generation–thereby reducing the country's dependence on imported fuels–which will be supplemented by rural electrification programmes. Progress was also made on the installation of the Valle de Jiboa Sugar Plant, designed to spur the activity of a broad sector of medium- and small-scale sugar-cane producers.

The effect of those two factors of expenditure found a sufficiently flexible response from the domestic production sectors, which, in addition to the promotion measures, were favoured by good weather conditions for their crops, the existence of idle capacity and the accumulation of large stocks of raw materials and inputs that had been imported the year before. These circumstances stimulated the production of goods, the dynamic impetus of which was transmitted to the services sectors (see table 210 and figure XXV).

The agricultural sector, apart from the spurt provided by favourable weather conditions, responded to the policy incentives based on the increase in support prices and the expansion of credit facilities, achieving a growth of 5.4 per cent which compares favourably with the 1973 rate of 4.9 per cent and the moderate progress made in previous years. The abundant rainfall contributed to general increases in yield and the bumper coffee harvest reversed the downward trend of the year before. Thus, between green coffee and other varieties, over 3 million quintals were exported, while production for domestic consumption also increased. Cotton producers also had various incentives to maintain a high level of output, but the main stimulus came from the high international prices. In the second half of 1974, quotations for Salvadorian cotton tended to drop,

Table 209. El Salvador: total supply and demand

	Millions of colones at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970-1972*	*1973*	*1974*[a]
Total supply	*3,202.8*	*3,862.5*	*4,135.3*	*124.6*	*130.4*	*6.0*	*7.2*	*7.1*
Imports[b]	631.4	871.7	965.0	24.6	30.4	9.4	15.3	10.7
Gross domestic product	2,571.4	2,990.8	3,170.3	100.0	100.0	5.2	5.1	6.0
Total demand	*3,202.8*	*3,862.5*	*4,135.3*	*124.6*	*130.4*	*6.0*	*7.2*	*7.1*
Exports[b]	638.8	783.6	821.0	24.8	25.9	11.6	−1.6	4.8
Domestic demand	2,564.0	3,078.9	3,314.3	99.8	104.5	4.6	9.7	7.6
Gross domestic investment	340.6	484.2	519.4	13.3	16.4	3.3	33.2	7.3
Gross fixed investment	308.0	426.1	455.8	12.0	14.4	16.7	1.6	7.0
Public	72.3	119.4	171.3	2.8	5.4	30.0	−2.2	43.5
Private	235.7	306.7	284.5	9.2	9.0	12.3	3.2	−7.2
Construction	132.2			5.1		...		
Machinery and equipment	175.8			6.9		...		
Total consumption	2,223.4	2,594.7	2,794.9	86.5	88.2	4.8	6.3	7.7
General government	275.6	323.5	338.0	10.7	10.7	5.2	6.0	4.5
Private	1,947.8	2,271.2	2,456.9	75.8	77.5	4.7	6.3	8.2

SOURCES: 1970-1972: ECLA calculations based on figures supplied by the Banco Central de Reserva de El Salvador; 1974: ECLA estimates based on official statistics.

Note: The figures for exports and imports of goods and services were taken from balance-of-payments data expressed in dollars at current prices, which were converted to constant 1970 values by deflation, using price indexes calculated by ECLA for the purpose.

[a] Preliminary figures.

[b] Goods and services, excluding factor payments.

Table 210. El Salvador: gross domestic product at factor cost, by sector of economic activity

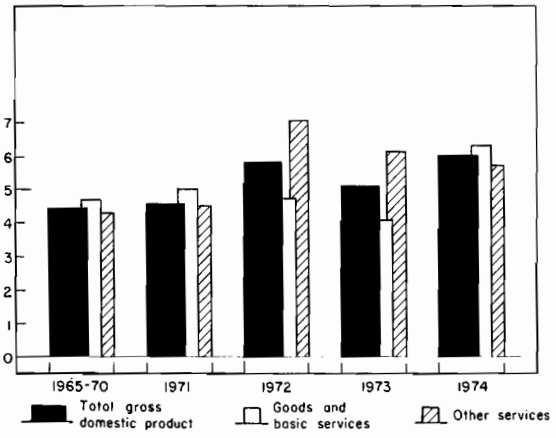
	Millions of colones at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970-1972*	*1973*	*1974*[a]
Agriculture	727.3	803.0	846.0	30.6	28.9	2.6	4.9	5.4
Mining	4.2	4.7	4.9	0.2	0.2	4.7	2.2	5.0
Manufacturing	418.0	495.3	526.0	17.6	18.0	5.8	5.9	6.2
Construction	72.4	94.8	109.9	3.1	3.8	21.3	−11.0	15.9
Subtotal goods	*1,221.9*	*1,397.8*	*1,486.8*	*51.5*	*50.9*	*4.9*	*4.0*	*6.4*
Electricity, gas and water	38.8	52.0	56.6	1.6	1.9	9.9	10.9	8.8
Transport and communications	126.3	137.9	144.5	5.3	4.9	3.1	2.7	4.8
Subtotal basic services	*165.1*	*189.9*	*201.1*	*7.0*	*6.8*	*4.8*	*4.8*	*5.9*
Commerce and finance	483.3	569.4	605.9	20.4	20.7	4.7	7.5	6.4
Government	200.2	246.2	258.5	8.4	8.8	8.0	5.4	5.0
Ownership of dwellings	94.9	108.0	111.9	4.0	3.8	4.8	3.5	3.6
Miscellaneous services	209.7	249.1	263.0	8.8	8.9	6.4	4.9	5.6
Subtotal other services	*988.1*	*1,172.7*	*1,239.3*	*41.6*	*42.3*	*5.7*	*6.1*	*5.7*
Total	*2,375.1*	*2,762.4*	*2,928.2*	*100.0*	*100.0*	*5.2*	*5.1*	*6.0*

SOURCES: 1970-1972: ECLA calculations based on figures supplied by the Banco Central de Reservas de El Salvador; 1973-1974: ECLA estimates based on official statistics.

Note: As the individual activities and the totals were calculated independently, the sum of the former does not correspond exactly with the latter.

[a] Preliminary figures.

Figure XXV. El Salvador: growth of gross domestic product
(Annual growth rates)
Natural scale



and this may have had the effect of reducing the 1974/1975 harvest, since in addition weather conditions were unfavourable in October.

The results obtained in the production of sugarcane were particularly significant. In response to external demand on the world market, especially the Middle East, the cultivated area was increased by about 10,000 *manzanas* (20 per cent) which, combined with a bigger yield, enabled production to be raised by 26 per cent. This increase, together with the high external prices, helped to boost the country's foreign exchange receipts.

With a population of 3.9 million and an area of 21,000 square kilometres, less than half of which are arable, the expansion of agriculture reached its maximum limits.

The incorporation of new agricultural land, the greater credit facilities granted and the increase in support prices acted as the main factors of the increase in the production of grains and other staple products, which exceeded the previous harvests, particularly in the case of maize, beans and rice. However, in other basic lines of agricultural production for home consumption (sorghum, tobacco, henequen, kenaf, sesame and fruit and vegetables) and in stock-raising, production was maintained at practically the same levels as the previous year. The shrimp catch, on the other hand, increased.

As regards manufacturing, the value added was 6.2 per cent higher than in 1973. The faster growth (in 1973 the rate was slightly below 6 per cent) is basically attributable to the expansion of domestic and Central American demand, the use of installed capacity being stepped up without any problems of supply, in view of the fairly large stocks of semi-processed materials and products imported in 1973.

As public investment gathered momentum, its effects were felt particularly in the construction sectors (a growth of approximately 16 per cent in value added). A significant level of activity was also recorded in electricity services and in the provision of financial services (see table 210).

In spite of the satisfactory expansion of over-all economic activity disruptions caused by an unusual intensification of inflationary pressures made themselves felt (in the first 10 months of 1974 the wholesale price index rose 25 per cent), the basic factors being the increase in import prices and the transmission to the domestic market of the situation of steadily rising prices of some export commodities. Despite the acceleration of inflation, private consumption expanded at a rate of 8.2 per cent—compared with 6.3 per cent in 1973—partly as a result of the wage adjustments designed to prevent any further deterioration of real income in the labour sector. During the year, wages and salaries were adjusted by proportions of over 20 per cent in commerce and industry, over 15 per cent in the private sector and over 10 per cent in agriculture. The rise in domestic prices, particularly of imports (30 per cent), discouraged the private sector from incurring new expenditure on capital formation, decisions to intensify the use of equipment prevailing over expansion plans and projects. Thus, private investment dropped by about 7 per cent (see table 209).

The unfavourable situation as regards international prices (the unit values of exports increased less than those of imports) led to a serious disequilibrium in current external transactions, in addition to a smaller increase in the volume of exports than in that of imports. Up to a point, this disequilibrium was due to the delay in marketing substantial coffee surpluses in the expectation of better prices, although the resulting financial pressures were eased, at least in the current financial year, by means of the active contraction of external loans by the Central Bank and other official institutions.

The measures designed to mitigate the effects of this external instability centred on financial policy instruments. Thus, not only was domestic bank credit increased, but extensive use was also made of fiscal incentives, in addition to strengthening the mechanisms favouring producers by means of support prices.

2. THE EXTERNAL SECTOR

Although exports of goods and services at current prices rose 26 per cent, the more rapid growth of imports of goods and services (44 per cent) led to a sharp increase in the balance-of-payments deficit on current account (see table 211). This deficit, which amounted to 112.5

Table 211. El Salvador: balance of payments
(*Millions of SDR units*)

	1970	*1971*	*1972*	*1973*	*1974*[a]
Current account					
Exports of goods and services	252.4	263.2	310.0	334.3	421.3
Goods FOB	231.5	238.9	277.9	301.7	382.5
Services	20.9	24.3	32.1	32.6	38.8
Transport	1.5	1.8	7.9	8.7	11.2
Travel	8.5	10.1	10.0	9.0	10.4
Imports of goods and services	253.8	291.0	299.6	369.0	532.2
Goods FOB	194.7	227.3	230.0	281.9	423.8
Services	59.1	63.7	69.6	87.1	108.4
Transport	26.3	29.8	33.2	38.4	49.9
Travel	20.4	20.4	18.8	29.6	35.6
Net external investment income	−8.8	−10.2	−10.1	−10.0	−11.6
Profits	−6.7	−6.4	−6.3	−6.3	−7.5
Interest	−2.1	−3.8	−3.8	−3.7	−4.1
Net private transfer payments	12.4	16.1	8.2	9.9	10.0
Balance on current account	2.2	−21.9	8.5	−34.8	−112.5
Capital account					
Net external financing (*a* + *b* + *c* + *d* + *e*)	−2.2	21.9	−8.5	34.8	112.5
(*a*) Net external non-compensatory capital	14.7	29.0	14.5	37.9	
Direct investment	3.7	7.0	6.1	3.0	
Long- and medium-term loans	8.7	14.7	27.6	23.0	
Amortization payments	−6.8	−10.3	−13.1	−11.4	
Short-term liabilities	7.2	16.5	−9.0	21.2	120.0
Official transfer payments	1.9	1.1	2.9	2.1	
(*b*) Domestic non-compensatory capital or assets	−6.0	−1.0	−11.4	−6.4	
(*c*) Errors and omissions	−2.7	−14.0	1.7	−0.6	
(*d*) Allocation of SDRs	4.2	3.7	3.7	–	–
(*e*) Net compensatory financing (increase −)	−12.4	4.2	−17.0	3.9	−7.5
Balance-of-payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	1.1	18.3	11.9	–	...
Amortization payments	−12.1	−13.7	−12.8	−15.1	...
Movements of foreign exchange reserves (increase −)	1.1	1.7	−14.7	19.0	...
Movements of gold reserves (increase −)	−2.5	0.1	0.2	–	...
SDRs (increase −)	–	−2.2	−1.6	–	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26.

[a] Estimates based on official statistics.

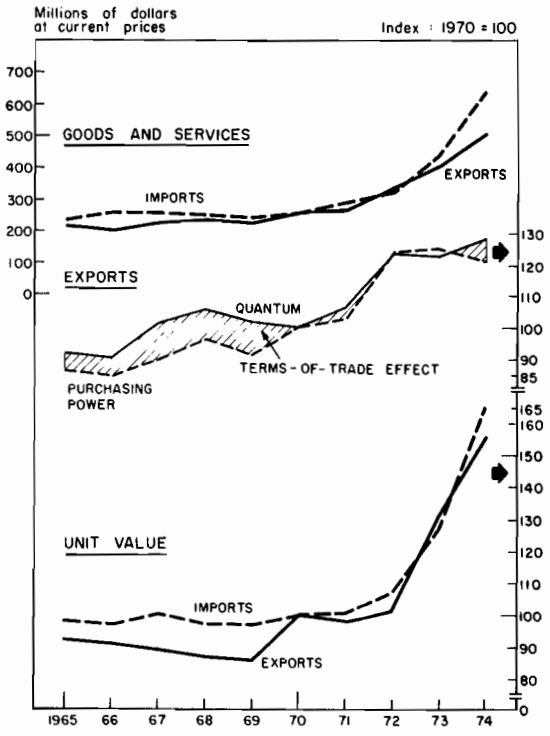
million SDR units, was exceeded by non-compensatory inflows of capital, the result being an increase of 7.4 million SDR units in net international reserves.

As regards the trade balance, there was an increase of 5.5 per cent in the volume of goods exported, which was supplemented by a 20 per cent rise in prices, resulting in an increase of 26.4 per cent in the total value of exports (see figure XXVI). The results might have been even better had it not been for the long drawn-out negotiations between coffee exporters and the principal buyers. Placing their hopes on these agreements, Salvadorian exporters held back considerable surpluses until the critical financing aspects caused them to effect a high proportion of their operations in the last three months of the year when prices had decreased significantly.

There was a 44 per cent increase in the volume of cotton exports. Sales of meat and shrimps were affected by the liberalization of the traditional quota system and the protection accorded to United States producers. Consequently, they fell short of the previous year's total, and in the case of shrimps, although the volume increased (20.8 per cent), prices fell in a greater proportion to just over 4,300 dollars per ton compared with 5,673 dollars in 1973.

In order in some degree to offset the instability of the external markets for traditional commodities, steps were taken to promote exports of new products. In this respect, various measures have been taken to promote non-traditional sales, in particular through the implementation of the law on export promotion and the organization of, and active participation in, international fairs.

Figure XXVI. El Salvador: trend of external variables
Natural scale



Imports of goods rose by 50 per cent as a result of increases of 15 per cent in volume and 30 per cent in price.

The increase in value of intermediate goods is estimated at 70 per cent, representing two thirds of the total value of imports of goods, more than one quarter of which consisted of crude petroleum and manufactured fertilizers.

As regards imports of capital goods, the increase was mainly in the public sector which, as stated previously, showed great activity in the execution of infrastructure projects.

In 1974 there was a net inflow of non-compensatory capital of 120 million SDR units, i.e., nearly four times more than the previous year. The banking sector received nearly half, and the rest were private and official transactions. The latter accounted for 20 per cent, with the contraction of medium- and long-term operations which facilitated the process of increasing basic social capital formation.

That same year, the movement of bank capital financing rose to unprecedented levels by virtue of the monetary authorities' policy which permitted external borrowing by the Central Bank, commercial banks and even private individuals to finance production.

As mentioned above, net international reserves showed a recovery of 7.5 million SDR units which, added to the balance accumulated in December 1973, brought the total to 68 million. This amount is in any case somewhat meagre, since it is estimated that it would enable the country to pay for its imports for only one and a half months. Over half of this recovery took place in the last three months of the year as a result of the greater activity in exports during that period.

As in previous years, the trade balance with Central America reflected a surplus, but it now recorded an unusual increase of 70 per cent, notwithstanding the increase in freight rates which affected trade with Nicaragua in particular, and the suspension of certain imports from that market as from mid-November.

3. PUBLIC FINANCE

The principal aim of the Government's financial policy in 1974 was to cushion some of the negative effects of the inflationary process on domestic economic activity and as far as possible to attain the goals laid down in the Development Plan.

This meant public expenditure involving a considerable deficit, as a result of the combination of several factors. First, tax collections grew by a somewhat modest rate (18.6 per cent) considering the increases in prices, owing to the adoption of a number of fiscal measures to keep the domestic market supplied by means of preferential treatment for external purchases of certain essential products, such as wheat, petroleum and manufactured fertilizers. In this way, the Government helped to maintain production and employment levels in both the agricultural and the manufacturing sector.

Secondly, it was not possible to obtain a higher fiscal revenue because of the trend of exports of some traditional commodities, mainly coffee and cotton, since the increase in the amounts collected in the form of taxes did not correspond to the increase in the value of these operations (possibly owing to marketing problems). Yet another factor was the granting of exemption in order to promote exports of manufactured products.

Current expenditure of the central government rose by 24 per cent, the share of social services (53.8 per cent) and those of the economic and administrative sectors remaining the same as in previous years.

At the same time, capital expenditure was increased by 60 per cent, mainly to provide assistance to the rest of the public sector in the form of transfers of capital, considerable support being given to the electrification programmes

being carried out by the Río Lempa Hydroelectric Executive Commission.

The autonomous institutions, for their part, more than doubled their capital expenditure of the previous year. This trend was mainly due to financial investment, while material investment increased by 40 per cent.

The Government covered the fiscal deficit by having recourse mainly to domestic credit and, on a lesser scale, to external credit. Internal borrowing, which amounted to 66.6 million colones, was affected through the sale of securities to the public via the commercial banks, which served to finance the autonomous institutions. With the new credit obtained in 1974, the public debt rose to 566.7 million colones, and continued to represent about 14 per cent of the gross domestic product.

4. Money and banks

In 1974 the means of payment increased by 35 per cent. This expansion was appreciably greater than in the year before (19.6 per cent), notwithstanding the measures adopted to prevent excessive monetary expansion.

Among the credit lines accorded during the year were those used for imports of fertilizers and raw materials for the agricultural sector.

In order to cover the credit requirements of private institutions and public investment programmes, the Central Bank increased its external indebtedness from 77.2 to 242.5 million colones (figures for November of each year), thus trebling the total reached in 1973. These resources were used basically to enable the official autonomous institutions to fulfil their investment programmes.

The credit institutions acquired securities issued or guaranteed by the State in order subsequently to sell them to the public. In this operation, minimum percentages were established for purchases by commercial banks (8 per cent of their total assets) and insurance companies (15 per cent of their technical reserves).

In the middle of the year, a policy of bank cash reserves was adopted as a means of regulating the Central Bank's credit programme, deposits at more than 90 days being included in the compulsory 30 per cent deposit.

Furthermore, bank interest rates were raised with the aim of encouraging domestic saving, discouraging the outflow of domestic capital and promoting certain economic activities. The rates paid in commercial bank operations rose by approximately 1 per cent, while the differential treatment of credit according to its use was maintained.

In order to restrict the outflow of foreign exchange, the system for the sale of foreign exchange to cover travel expenses was modified. In line with the new regulations, 20 per cent of the total value of travel expenses in excess of 600 colones per head (to be checked later) must be deposited. Moreover, new non-essential articles were added to the import lists, subject to a prior deposit; this was up to 100 per cent of their value, as in the case of cars.

GUATEMALA

1. Recent economic trends

In 1974 there was a change in the trend of the growth which had characterized the economy of Guatemala since 1970. The rate of growth of the gross domestic product, which had been 7.3 per cent in 1972 and 7.6 per cent in 1973, dropped to 4.7 per cent in 1974 (see table 212).

This took place against a background of increasing inflationary pressures which were reflected in an increase of 19.8 per cent in the gross domestic product, calculated at current prices, and in an increase of 15.9 per cent in domestic consumer prices.

Gross fixed capital investment decreased by 5.1 per cent compared with the previous year, owing to a considerable decline in the real level of public investment and to stagnation in private capital spending. This unsatisfactory state of affairs may be attributed in part to the above-mentioned inflationary pressures, which meant a substantial increase in the cost of capital goods, with the consequent decline in purchases of such goods, and the decrease in investment in the manufacturing sector in the face of continuing uncertainty as to the future of the Central American Common Market. It is to be assumed that part of the savings generated in the course of 1974 were channelled into stockpiling, owing to expectations of an upswing in prices. This may be seen in the notable increase in total gross investment which includes a considerable increase in stocks.

Among the components of over-all demand, however, public consumption and the volume of exports showed only a moderate growth in comparison. General government spending on con-

Table 212. Guatemala: total supply and demand

	Millions of quetzales at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970-1972*	*1973*	*1974*[a]
Total supply	*2,242.5*	*2,703.2*	*2,871.8*	*117.8*	*118.2*	*5.8*	*7.7*	*6.2*
Imports[b]	338.5	382.2	441.7	17.8	18.2	2.0	8.6	15.6
Gross domestic product	1,904.0	2,321.0	2,430.1	100.0	100.0	6.5	7.6	4.7
Total demand	*2,242.5*	*2,703.2*	*2,871.8*	*117.8*	*118.2*	*5.8*	*7.7*	*6.2*
Exports[b]	353.6	425.0	447.1	18.6	18.4	2.8	13.6	5.2
Domestic demand	1,888.9	2,278.2	2,424.7	99.2	99.8	6.3	6.7	6.4
Gross domestic investment	244.2	281.7	338.9	12.8	14.0	-1.0	17.8	20.3
Gross fixed investment	238.6	285.3	270.7	12.5	11.1	3.8	10.9	-5.1
Public	45.2	75.0	60.0	2.4	2.4	20.7	14.0	-20.0
Private	193.3	210.3	210.7	10.1	8.7	-0.5	9.8	0.2
Construction	70.8	...	...	3.7	...	...	...	...
Machinery and equipment	167.7	...	...	8.8	...	...	...	...
Total consumption	1,644.7	1,996.5	2,085.8	86.4	85.8	7.4	5.3	4.5
General government	151.4	154.9	166.7	8.0	6.8	1.1	-	7.5
Private	1,493.3	1,841.6	1,919.1	78.4	79.0	8.0	5.7	4.2

SOURCES: 1970-1973: ECLA calculations based on figures supplied by the Banco de Guatemala; 1974: ECLA estimates based on official data.

Note: The figures for exports and imports of goods and services were taken from balance-of-payments data expressed in dollars at current prices, which were converted to constant 1970 values by deflation, using price indexes calculated by ECLA for the purpose.

[a] Preliminary figures.

[b] Goods and services, excluding factor payments.

sumption expressed in constant prices increased by 7.5 per cent, following the stagnation of 1973.[31] This change reflects the efforts made by the public sector to attend to a series of services, the unsatisfied demand for which had been accumulating for a long time, and which at least partly offset the low rate of increase in public consumption.

Logically enough, the external sector was affected by trends in the world economy. The primary commodities exported by Guatemala profited—at least during the first half of the year—from the price increases, and for the second year running favoured the inflow of foreign exchange, but this relative advantage was countered by still higher increases in import prices, as will be described below. Exports of goods and services expressed in constant prices increased by 5.2 per cent, and unit values increased by 24 per cent. Their value at current prices increased from 534 million dollars in 1973 to 693 million in 1974 (30 per cent).

Owing to the changes which were taking place in the course of the year in the international economic situation, as 1974 advanced the balance-of-payments situation deteriorated steadily, while the position of the central government improved, for the reasons given below. The increase in the means of payment too was much greater in the first half of the year than during the second half, and the monthly price index of consumer goods suggests that inflationary pressures tended to diminish during the last quarter of 1974.

Lastly, it may be concluded from an analysis of total supply and demand in the economy, that for the second consecutive year the volume of imports grew much more than the gross domestic product. On the one hand this may be attributed to the tendency to stockpile imported goods, owing to expectations of an upswing in prices observed during most of the year, and also to the increase in the earnings of the export sector, where the tendency to consume imported products has always been strong.

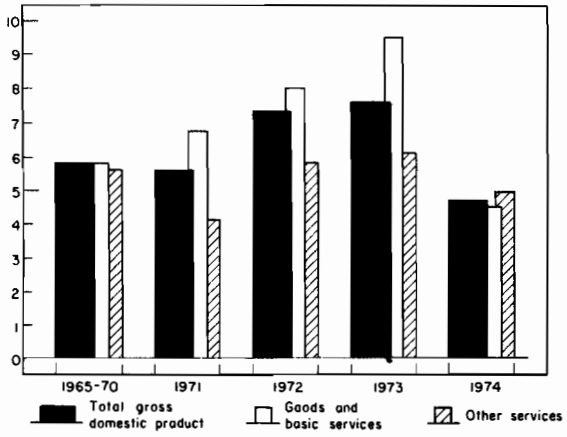
The result of the increase in the volume of imports combined with the considerable increase (30 per cent) in unit values, was an unprecedented rise (50.5 per cent) in the total value of imports of goods and services at current prices, particularly fuels. This noteworthy increase took place against the background of a decline in the purchasing power of exports on account of a deterioration in the terms of trade. The uneven growth of exports and imports resulted in a current account deficit of 112 million dollars (compared with the 10 million surplus of the previous year) and a cutback in its international reserves.

[31] Contrary to what happened in 1972 and 1973 when public sector capital expenditure was one of the factors showing most impetus.

2. MAJOR SECTORS OF ACTIVITY

From the point of view of sectoral supply, the drop in the growth rate of the main sectors of production—agriculture and industry—compared with the rates for 1972 and 1973, and the increase in the value added by the public administration (9.4 per cent) are noteworthy (see table 213). This increase did in fact result in the expansion of services to the population, and also provided a means of alleviating the problem of unemployment and underemployment, but did not contribute, in the short-term at least, to increasing the supply of goods (see figure XXVII).

Figure XXVII. Guatemala: growth of gross domestic product
(Annual growth rates)
Natural scale



As regards the agricultural sector, the partial data available show that the supply of basic foodstuffs, although slightly larger than in 1973, was inadequate to satisfy domestic demand and was even lower than in 1972. This may be attributed, at least in part, to the inadequate supply of inputs for agriculture, to the lower level of returns on such crops compared with those destined for export, and to adverse weather and other natural conditions, including the effects of hurricane Fifi in September 1974 and the eruption of Volcán de Fuego in October.[32] The output of the majority of agricultural export items increased, however, at a rate estimated at approximately 7 per cent over the 1973 levels.

The lack of dynamism in the manufacturing sector may be attributed to the slow growth of private consumption and the shortfall in the supply of some raw materials and industrial inputs, especially during the first half of 1974. It may be assumed that the drop in the real income of large strata of the population, along with inflation,

[32] Hurricane Fifi, which caused tremendous damage in Honduras, also affected the northern area of Guatemala, and led to the formation of another depression on the Pacific coast—hurricane Orlene—which caused damage of some consideration in the coastal plains of El Salvador and Guatemala. The volcanic dust from the eruption of Volcán de Fuego in October of the same year seriously affected the sesame, maize and cotton harvests. The Banco de Guatemala estimated losses at around 30 million quetzales for 1974 and at an even higher figure for 1975, particularly on account of the damage suffered by the cotton plantations.

Table 213. Guatemala: gross domestic product at factor cost, by sector of economic activity

	Millions of quetzales at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970-1972*	*1973*	*1974*[a]
Agriculture	535.8	674.7	703.9	30.1	31.0	7.4	9.1	4.3
Mining	1.7	1.7	2.3	0.1	0.1	-6.4	14.3	35.3
Manufacturing	259.8	317.6	333.2	14.6	14.7	6.3	8.1	4.9
Construction	38.6	54.9	57.5	2.2	2.5	9.8	18.0	4.7
Subtotal goods	*835.9*	*1,048.9*	*1,096.9*	*47.0*	*48.4*	*7.2*	*9.3*	*4.6*
Electricity, gas and water	15.9	20.8	22.7	0.9	1.0	9.1	10.0	8.6
Transport and communications	62.7	84.5	89.4	3.5	3.9	9.8	11.8	5.9
Subtotal basic services	*78.6*	*105.3*	*112.1*	*4.4*	*4.9*	*9.6*	*11.4*	*6.5*
Commerce and finance	489.5	580.9	607.8	27.5	26.8	4.9	7.9	4.5
Government	125.0	143.3	156.9	7.0	6.9	5.9	2.2	9.4
Ownership of dwellings	138.0	146.3	149.8	7.8	6.6	2.0	1.8	2.4
Miscellaneous services	111.9	139.2	144.6	6.3	6.4	7.5	7.6	3.8
Subtotal other services	*864.4*	*1,009.7*	*1,059.1*	*48.6*	*46.7*	*4.9*	*6.1*	*4.9*
Total	*1,778.9*	*2,168.5*	*2,271.4*	*100.0*	*100.0*	*6.5*	*7.6*	*4.7*

SOURCES: 1970-1973: ECLA calculations based on figures supplied by the Central Bank of Guatemala; 1974: ECLA estimates based on official data.

Note: As the individual activities and the totals were calculated independently, the sum of the former does not correspond exactly with the latter.

[a] Preliminary figures.

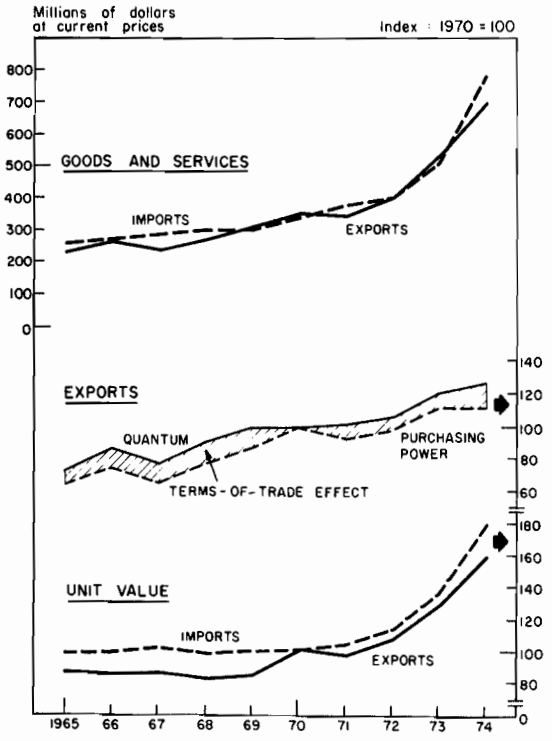
reduced domestic consumption of non-essential manufactures and shifted it towards basic foodstuffs and other essential goods and services. The decline in domestic purchases of manufactures was partially offset, as will be described below, by the steady increase in Central American Common Market demand, but despite this it was not possible to maintain the rate of industrial growth.

The construction sector also recorded a rate of growth lower than that of previous years, no doubt owing to the slowing down of the growth of public investment, while the remaining sectors, generally speaking, maintained their share of the gross domestic product.

3. THE EXTERNAL SECTOR AND THE BALANCE OF PAYMENTS

For the third year running increases were recorded in the volume and in the unit value of exports. The volume of imports of goods and services increased by 5.2 per cent. This growth was 5.5 per cent in 1972 and 13.6 per cent in 1973. The unit value of exports for its part increased by 24 per cent. The value of exports of goods increased from 440 million dollars in 1973 to 585 million dollars in 1974 and the value of services from 94 million to 108 million dollars (see figure XXVIII).

Figure XXVIII. Guatemala: trend of external variables
Natural scale



Increases of some consideration were recorded in the current value of all the main export products. These were a result of increases in volume and in prices, except in the case of meat whose volume did not change compared with 1973, and bananas the unit values of which decreased slightly. The biggest increase was recorded by sugar, thanks to the considerable growth of output and the tripling of prices. The value of sugar exports increased from 14 million dollars in 1972 to 22 million in 1973 and 56 million in 1974 (see table 214). Exports to the Central American Common Market also showed considerable dynamism, with an increase of 42 per cent between 1973 and 1974. The boom in the export sector, however, reached its peak in mid-1974, and since then the prices of coffee, cotton and meat have dropped. The second half of the year thus obscures the rather favourable picture of the first half of the year and prospects for 1975.

If the country's exports showed dynamism, however, imports grew at a much faster rate. The volume of imports of goods and services increased by 15.6 per cent and unit values by 30 per cent. Imports of goods alone increased from 388 million dollars in 1973 to 608 million in 1974, i.e., by 56.6 per cent. Services, particularly transport, increased from 130 to 171 million dollars during the same period.

As may be supposed, the value of imports of fuels and lubricants tripled, from 33 million dollars in 1973 to 105 million in 1974. Imports of raw materials increased by 53.2 per cent during the same period, despite the shortfall in international supply of specific products.

Of total imports of goods, 114 million dollars' worth (16.6 per cent) came from the Common Market, compared with 89.6 million dollars' worth in 1973. Once again a trade surplus was obtained in trade with other Central American countries, which amounted to 71 million dollars and was much higher than the surplus of 40 million dollars recorded in this trade in 1973.

External transactions of goods and services left a negative balance of 93 million SDR units in the current account of the balance of payments at the end of 1974 (in 1973 a surplus of 7.8 million had been recorded), which after deduction of the net inflow of non-compensatory capital of 82 million SDR units, resulted in a decrease of around 11 million SDR units in the country's international reserves, for the first time in the present decade (see table 215).

Table 214. Guatemala: value and quantum of main export products

	1971	1972	1973[a]	1974[b]	Annual growth rate 1970–1973	Annual growth rate 1974
			Millions of quetzales			
Coffee	96.3	105.3	145.6	163.3	13.1	12.2
Cotton	26.0	40.9	46.6	65.5	19.7	40.6
Bananas	14.5	17.2	24.7	28.8	22.0	16.6
Fresh meat	17.4	18.0	25.1	29.6	25.0	17.9
Sugar	9.9	16.1	21.9	56.1	34.0	156.2
			Millions of quetzales at 1970 prices			
Coffee	105.8	120.2	121.4	125.2	6.5	3.1
Cotton	26.2	40.0	39.9	47.3	13.6	18.5
Bananas	15.9	18.3	16.0	18.7	5.6	16.9
Fresh meat	17.0	16.1	18.1	18.1	12.6	–
Sugar	10.7	14.6	20.1	22.4	30.0	11.4

SOURCE: ECLA, on the basis of official statistics.
[a] Preliminary figures.
[b] Estimates.

Table 215. Guatemala: balance of payments
(Millions of SDR units)

	1970	1971	1972	1973	1974[a]
Current account					
Exports of goods and services	350.8	344.3	364.2	443.0	576.5
Goods FOB	298.3	290.5	310.8	364.7	486.4
Services	52.5	53.8	53.4	78.3	90.1
Transport	10.9	11.4	10.9	13.8	18.6
Travel	12.1	13.6	15.6	30.7	35.3
Imports of goods and services	337.3	373.2	365.2	429.1	647.6
Goods FOB	266.6	292.0	272.3	321.7	505.4
Services	70.7	81.2	92.9	107.4	142.2
Transport	35.4	37.9	46.6	46.6	72.0
Travel	14.5	21.5	22.4	31.7	37.4
Net external investment income	–31.2	–36.4	–43.7	–40.1	–45.3
Profits	–22.9	–24.0	–30.8	–32.4	–35.8
Interest	–8.3	–12.4	–12.9	–7.7	–9.5
Net private transfer payments	17.9	25.7	27.7	34.0	23.3
Balance on current account	0.2	–39.6	–17.0	7.8	–93.1
Capital account					
Net external financing (*a* + *b* + *c* + *d* + *e*)	–0.2	39.6	17.0	–7.8	93.1
(*a*) Net external non-compensatory capital	46.1	51.0	48.6	77.6	
Direct investment	22.5	22.8	14.1	23.0	
Long- and medium-term loans	71.7	59.3	66.6	58.2	
Amortization payments	–46.9	–33.3	–48.9	–37.3	82.4
Short-term liabilities	–1.3	3.2	18.0	33.2	
Official transfer payments	0.1	–1.0	–1.2	0.5	
(*b*) Domestic non-compensatory capital or assets	–18.5	11.8	8.6	–20.8	
(*c*) Errors and omissions	–12.1	–11.6	–3.3	–7.6	
(*d*) Allocation of SDRs	4.2	3.9	3.8	–	–
(*e*) Net compensatory financing (increase –)	–19.9	–15.5	–40.7	–57.0	10.7
Balance-of-payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	3.4	2.9	0.3	–	...
Amortization payments	–11.5	–4.0	–2.8	–5.0	...
Movements of foreign exchange reserves (increase –)	–9.6	–5.8	–32.5	–48.0	...
Movements of gold reserves (increase –)	–0.2	–2.8	–5.9	–0.1	...
SDRs (increase –)	–2.0	–5.8	0.2	–3.9	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26. [a] Estimates based on official statistics.

In capital account operations, there was an important inflow of private capital, since the balance of official and banking capital operations barely reached 12.7 million SDR units, in response to the low rate of disbursement of the international loans obtained by the public sector, which contribute to financing its capital expenditure.

4. INFLATIONARY PRESSURES AND CURRENT ECONOMIC POLICY

One of the main factors which affected the evolution of the economy in 1974, as in 1973, was the continuing and growing presence of inflationary pressures which it proved very difficult to measure accurately on the basis of the country's present price indexes.[33]

The consumer prices of 46 essential articles in Guatemala City rose by 15.9 per cent between December 1973 and December 1974. The comparable increase for the previous year was 14.4 per cent. The wholesale price index rose by 22.8 per cent, while the deflator implicit in the gross domestic product increased by 14.4 per cent compared with 11.5 per cent in 1973.

These pressures are due to a large extent to factors of external origin. The generalized increase in prices of imported goods and services which began to appear in 1972 and became worse in 1973 took on new dimensions with the dizzy rise in the price of petroleum and petroleum products. According to official figures, the unit value of imports in 1974 increased by an average of 30 per cent, while the unit value of crude rose 240 per cent. The increase in import prices also contributed indirectly to cost inflation through the incorporation of imported inputs in the goods produced by Guatemala.

Higher prices in the international markets for goods produced by Guatemala (sugar, meat, cotton, wood and also a wide range of manufactures) also brought pressure to bear on the domestic prices of those products. The boom in the export sector during 1973 and the first two or three quarters of 1974 slanted the structure of production, redirecting it towards exportable output and creating problems of domestic supply, in addition to the price increases already referred to.

Unfortunately, no reliable data are available on the evolution of wages during 1974. There are, however, some indications that wage adjustments did not keep up with price changes, with the consequent deterioration in the distribution of factor income.

The above-mentioned situations have been a source of increasing concern to the public sector. Especially during the second half of 1974, the Government adopted a series of measures to deal with them, including some aimed at stimulating supply, others aimed at maintaining an adequate level of demand, and yet others directed at mitigating the effects of cost inflation. Among the first are measures to encourage the sowing of basic grains, which include support prices, supplies of inputs at subsidized prices and concessional credits.

As far as demand is concerned, an endeavour was made to maintain the purchasing power of the wage-earning sectors, by fixing minimum wages for some sectors of activity and revising others. In addition, the central government and the majority of decentralized bodies agreed on wage adjustments for their employees. In its turn, with a view to regulating the expansion of the currency, the Banco de Guatemala raised the ceilings on passive and active interest rates (from 7 and 9 per cent annually, to 9 and 11 per cent). This measure was also aimed at stimulating savings and cutting down the flight of capital. In addition, the liquidity ratio was increased from 30 to 40 per cent and limits were set to portfolio holdings of bonds received in payment for non-essential articles, while at the same time a selective policy of incentives to production was maintained. To alleviate cost inflation, price limits were set for a selected list of essential articles. The State also adopted a selective policy of subsidies, which enabled it to maintain tariffs unchanged for electrical energy and public transport in the country's main urban areas, and made possible sales of basic grains, especially of imported origin, by the National Agricultural Marketing Institute, at prices lower than those currently operating in the market.

The great majority of the measures described came into force during the third and fourth quarters of the year. Their effectiveness, however, may be restricted by difficulties of an administrative nature, especially in the application of price limits, and by inadequacies in the machinery available to the private sector for promoting wage adjustments. All in all, the adoption of these measures indicates a more flexible response than that of 1973 and is the first integrated action to further economic stability in Guatemala.

[33] The indexes suffer from certain defects which stem from the methodology followed for data collection, the content of the basket of goods making it up, and the distant base year used (1946). The Statistical Department, the Banco de Guatemala, and the Secretariat of the National Economic Planning Council have already undertaken the preparation of a new index.

1. RECENT ECONOMIC TRENDS

An expansion of exports which practically doubled their value, as the result of high world market prices that benefited Guyana's staple export products and of increases in the sales volume of some of these goods, was the mainspring of economic activity, and in particular of that linked to the export sector. Its dynamic influence made itself apparent in an increase of 37 per cent in the gross product at current prices, according to a highly tentative estimate based on the evolution of the principal branches of production. This improvement compares favourably with the 10 per cent rise achieved in the preceding year, even when allowance is made for the greater price increases that occurred in the meantime (see table 216).

Although imports of goods were subject to restrictions, they expanded by 47 per cent–much less than exports–which implied that in real terms supplies of imported goods were 6 per cent larger than in 1973, since import prices rose by about 38 per cent. Notwithstanding this more plentiful supply of imported items available during the year, the poor results achieved in certain branches of production mainly serving the domestic market, in conjunction with other factors, such as the high prices paid for imported goods and the excessive liquidity caused by the substantial export earnings, pushed up domestic prices to higher levels than in previous years, despite the efforts made to control them.

The consumer price index, which had risen by 5 per cent in 1972 and 7.5 per cent in 1973, showed an increase of 17.5 per cent in 1974, as an annual average. From December 1973 to December 1974, however, the increase was 11.6 per cent, compared with 15.2 per cent in the previous year. In the case of the food component of the index, the rise up to October was approximately 25 per cent.

2. PRODUCTION IN SELECTED SECTORS

The high growth rate of the gross product estimated for 1974 is based on the results achieved in four main branches of agro-industrial and mining production intended mainly for export: sugar, rice, calcined bauxite and alumina. The data on other products are on the whole unfavourable as regards volumes of output (see table 217).

Production in the other sectors of the economy was adversely affected by the high prices of imported inputs and materials, as would seem to have been the case with construction and some lines of manufacturing. The government sector increased its contribution to the total product by barely 4.5 per cent in terms of current values.

Table 216. Guyana: gross domestic product at factor cost, by sectors of economic activity

Sector	*Millions of Guyana dollars at current prices*			*Annual growth rate (percentages)*		
	1972	*1973*	*1974*[a]	*1972*	*1973*	*1974*
Agriculture	92.7	93.6	...	1.6	1.0	...
Sugar-cane	(56.7)	(49.7)	(115.9)	(4.4)	(–12.3)	(133.2)
Paddy rice	(9.1)	(12.9)	(23.2)	(–18.8)	(41.8)	(80.0)
Fishing	5.9	6.8	...	9.3	15.3	...
Forestry	5.6	6.0	...	12.0	7.1	...
Mining and quarrying	89.7	80.5	117.0	–1.1	–10.3	45.3
Manufacturing	64.0	62.4	...	4.6	–2.5	...
Sugar processing	(19.9)	(17.5)	(40.7)	(4.2)	(–12.1)	(132.6)
Rice processing	(2.1)	(2.9)	(5.7)	(–34.4)	(38.1)	(96.6)
Transport and communications	32.8	37.1	...	10.1	13.1	...
Construction	42.8	47.9	...	10.9	12.0	...
Commerce	58.7	64.4	...	7.7	9.8	...
Ownership of dwellings Financial and other services	50.7	56.2	...	3.9	10.8	...
Government	79.1	121.2	126.6	13.0	53.2	4.5
Total	*522.0*	*576.0*	*790.0*	*5.4*	*10.3*	*37.2*

SOURCES: *Economic Survey of Guyana,* 1971; and information provided by the Statistical Bureau, Guyana.

[a] Provisional figures.

Table 217. Guyana: output of major products

Product	Units (thousands)	1972	1973	1974
Sugar-cane	Tons	3,566	3,252	4,050[a]
Rice (clean)	Tons	94	110	140[a]
Coconuts	Units	68,468	61,074	...
Tubers	Pounds	60,500	62,678	45,000[a]
Plantains	Pounds	52,000	55,016	22,000[a]
Citrus fruit	Pounds	23,000	23,759	22,000[a]
Bananas	Pounds	14,800	18,234	10,000[a]
Beef	Pounds	9,600	9,612	8,300[a]
Poultry[b]	Pounds	10,843	12,553	12,500[a]
Sugar	Long tons	316	266	228[c]
Edible oil	Gallons	1,171	788	182[c]
Margarine	Pounds	3,105	2,062	1,961[c]
Molasses	Gallons	19,888	17,080	...
Dried bauxite	Long tons	1,616	1,664	1,153[c]
Calcined bauxite	Long tons	690	636	557[c]
Alumina	Long tons	262	234	227[c]

SOURCES: Ministry of Agriculture of Guyana; Statistical Bureau, Guyana.
[a] Estimates.
[b] Marketed output only.
[c] Data up to September.

In the agricultural sector, output of sugar-cane exceeded 4 million tons, thus improving upon the poor preceding crop by 25 per cent. The rice harvest expanded by about 27 per cent, thanks to favourable weather conditions. These increases gain enhanced significance when multiplied by the high price levels reached during the year, and account for the noteworthy expansion of the agricultural product (at current prices), of which they represent about 67 per cent.

In the case of other agricultural products volumes of output dropped sharply, despite the Government's investment in agricultural infrastructure and the subsidies granted to farmers with the aim of increasing food production and reducing imports.

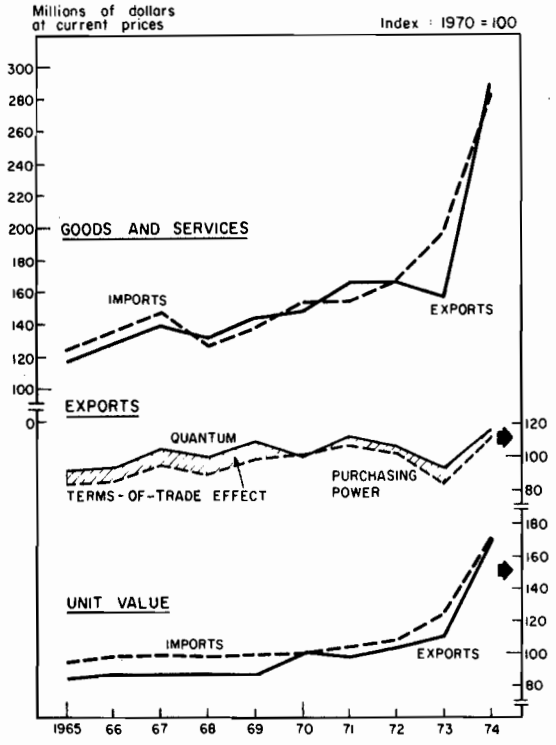
The product of the mining sector rose by 45 per cent at current prices. In terms of volume, however, output of dried bauxite (excluding refractory bauxite) contracted by about 10 per cent in the first nine months of 1974, while that of calcined bauxite and alumina increased by 25 and 21 per cent, respectively, in the same period.

Despite the diversification of the structure of manufacturing which has taken place in the past few years, the sugar industry and rice processing still account for about one third of the product of the sector.

It is estimated that output of sugar and rice expanded considerably during 1974 as a result of bumper harvests. Owing to the high levels reached by the prices of these commodities, the increases in the value added in their processing (at current prices) are estimated at 133 per cent in the case of sugar and 97 per cent in that of rice.

Generally speaking, output of other manufactures was very uneven during the year.

Figure XXIX. Guyana: trend of external variables
Natural scale



3. FOREIGN TRADE TRENDS

While the value of exports of goods almost doubled in 1974 (rising by 94 per cent), that of imports increased by 47 per cent (see table 218).

Of the export increment, a little over 50 per cent was due to the rise in prices and 28 per cent to the increase in volume (see figure XXIX). Sales of sugar alone, which more than trebled in value, accounted for about two thirds of the expansion of total exports. It is estimated that the export value of bauxite rose by about 40 per cent and that of alumina by over 50 per cent. Moreover, by October external sales of rice had surpassed the value exported in the whole of the year 1973 by 53 per cent.

The volume of imports showed an increase of 6 per cent and their unit value one of about 38 per cent, with the result that their value rose by 47 per cent, despite the import restrictions imposed by the Government on a wide range of goods, with the aim of safeguarding the country's scanty reserves of foreign exchange and promoting the substitution of domestic food production for imports. According to incomplete data for the year, increases in imports were substantial in the case of fuels and of inputs and intermediate goods, and slight in that of food. A considerable contraction was observable in imports of manufactures.

The year 1974 witnessed changes in the direction of export flows. By September the proportion of total exports shipped to the United States had climbed from 21 per cent (1973) to 30 per cent, to the detriment of exports to the United Kingdom, whose share dropped from 30 to 17 per cent. Exports to Latin American markets also showed a

Table 218. Guyana: balance of payments
(Millions of SDR units)

	1970	*1971*	*1972*	*1973*	*1974*[a]
Current account					
Exports of goods and services	148.9	165.7	152.4	130.1	239.7
Goods FOB	129.0	145.5	132.8	111.8	217.8
Services	19.9	20.2	19.6	18.3	21.9
Transport	3.8	3.9	3.4	3.4	4.1
Travel	3.4	3.4	3.1	3.0	3.5
Imports of goods and services	153.6	154.2	152.4	164.4	236.0
Goods FOB	119.9	119.7	118.7	131.1	192.9
Services	33.7	34.5	33.7	33.3	43.1
Transport	17.1	16.5	17.7	18.6	25.6
Travel	3.0	3.4	3.3	3.6	4.2
Net external investment income	−15.9	−18.1	−10.4	−10.8	−14.0
Profits	−14.2	−16.5	−6.8	−4.7	−7.9
Interest	−1.7	−1.6	−3.6	−6.1	−6.1
Net private transfer payments	−0.5	−0.2	0.8	0.7	0.9
Balance on current account	−21.1	−6.8	−9.6	−44.4	−9.4
Capital account					
Net external financing (*a* + *b* + *c* + *d* + *e*)	21.1	6.8	9.6	44.4	9.4
(*a*) Net external non-compensatory capital	14.1	9.1	10.5	26.3	42.4
Direct investment	9.0	−55.6	2.3	−0.9	
Long- and medium-term loans	9.8	69.5	10.9	25.3	
Amortization payments	−1.2	−1.7	−2.3	−3.4	
Short-term liabilities	−3.5	−4.1	0.7	2.6	
Official transfer payments	0.0	1.0	−1.1	2.7	
(*b*) Domestic non-compensatory capital or assets	1.5	4.0	1.8	−3.5	
(*c*) Errors and omissions	3.1	−4.8	4.8	−0.9	
(*d*) Allocation of SDRs	2.5	2.1	2.1	–	–
(*e*) Net compensatory financing (increase −)	−0.1	−3.6	−9.6	22.5	−33.0
Balance-of-payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	–	2.2	–	3.9	...
Amortization payments	–	−0.1	−2.1	–	...
Movements of foreign exchange reserves (increase −)	0.6	−5.4	−5.0	17.9	...
Movements of gold reserves (increase −)	−0.6	1.8	−0.6	0.6	...
SDRs (increase −)	−0.1	−2.1	−1.9	0.1	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26.

[a] Estimates based on official statistics.

relative increase, whereas the percentage represented by trade with other Caribbean countries underwent little variation.

The considerable difference between the rates of growth of exports and imports in 1974 resulted in a sharp reduction in the balance-of-payments deficit on current account. In addition, there was a bigger net inflow of non-compensatory capital which practically doubled the preceding year's, and brought about an increase of 33 million SDR units in the country's net international reserves (see table 218).

HAITI

1. RECENT ECONOMIC TRENDS

According to preliminary data, the growth rate of the economy appears once again to have slackened. It is estimated that in 1974 the gross domestic product rose by 3 per cent, which is the lowest rate recorded in the present decade, although double the rate of population growth.

The evolution of the product by sector of economic activity showed marked reductions in the growth rates of manufacturing, mining and services, excluding basic services. In contrast, a slight recovery was observable in agriculture, which accounted for nearly half of the total product, while construction stepped up even further its high rate of growth (see table 219 and figure XXX).

Haiti is one of the few Latin American countries that has not benefited from the favourable situation as regards world prices of primary products. The increase in the unit value of exports of 18.9 per cent in 1973 and 32.7 per cent in 1974 was cancelled out in the first of these years and exceeded in the second by the higher prices of imports. This state of affairs, combined with the stagnation in the volume exported in 1974, led to

Figure XXX. Haiti: growth of gross domestic product
(Annual growth rates)
Natural scale

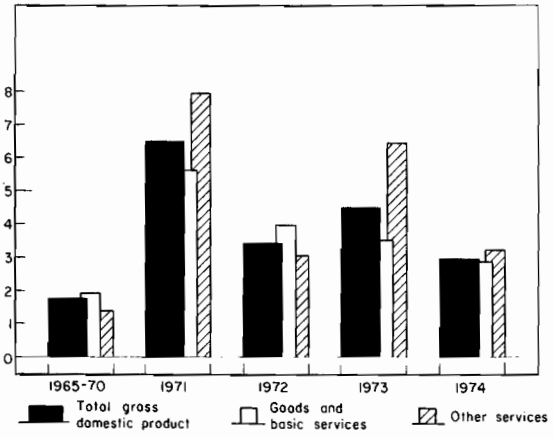


Table 219. Haiti: gross domestic product at factor cost, by sector of economic activity

	Millions of gourdes at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970-1972*	*1973*	*1974*[a]
Agriculture	1,041.0	1,120.7	1,134.0	50.8	46.6	3.4	0.6	1.2
Mining	35.0	45.9	50.2	1.7	2.1	0.4	30.0	9.4
Manufacturing	201.0	256.4	266.4	9.8	10.9	7.3	10.8	3.9
Construction	47.0	72.7	85.2	2.3	3.5	15.8	15.4	17.2
Subtotal goods	*1,324.0*	*1,495.7*	*1,535.8*	*64.6*	*63.1*	*4.4*	*3.6*	*2.7*
Electricity, gas and water	27.0	36.2	38.8	1.3	1.6	14.2	2.8	7.2
Transport and communications	49.0	61.0	63.6	2.4	2.6	9.4	3.9	4.3
Subtotal basic services	*76.0*	*97.2*	*102.4*	*3.7*	*4.2*	*11.2*	*3.5*	*5.3*
Commerce and finance	223.0	281.0	291.1	10.9	12.0	8.3	7.4	3.6
Government	95.0	113.3	120.9	4.6	5.0	2.6	13.3	6.7
Ownership of dwellings	204.0	216.9	219.6	10.0	9.0	4.1	2.2	1.2
Miscellaneous services	129.0	159.5	163.9	6.3	6.7	8.0	6.0	2.8
Subtotal other services	*651.0*	*770.7*	*795.2*	*31.8*	*32.7*	*5.5*	*6.4*	*3.2*
Total	*2,051.0*	*2,363.6*	*2,434.0*	*100.0*	*100.0*	*5.0*	*4.5*	*3.0*

SOURCES: 1970-1973: ECLA calculations based on figures supplied by the Haitian Statistical Institute; 1974: ECLA estimates based on data from the same source.

[a] Preliminary figures.

a reduction of 14.5 per cent in the purchasing power of exports, and the final result was an 8.4 per cent contraction in the volume of imports of goods and services.

The slower growth of total production, combined with the decrease in the volume of imports—and despite the stagnation in the volume of exports—was responsible for reducing the increase in the domestic supply of goods and services from 4.4 per cent to barely 1.6 per cent in 1974. This was reflected, on the demand side, in a decline in the growth of investment, and particularly of consumption, where an increase of only 1.3 per cent was recorded in private consumption, while general government consumption contracted by a similar proportion (see table 220).

The growth rate of investment expenditure dropped two points in 1974; however, it remained at the satisfactory level of nearly 7 per cent, which, together with the loss of momentum of the total product, contributed to raising the investment coefficient; this nevertheless remained at extremely low levels, rising from 7 per cent in 1970 to 8.7 per cent in 1974. Of the latter percentage, only about one quarter represented public investment, mainly in the construction of roads and the improvement of public services.

Investment by the private sector has increased rapidly since 1972, being used mainly for the construction of tourist infrastructure and the establishment of some light industries. In addition, cement production capacity was increased to 80,000 tons annually and work began on the construction of a steel plant which will use imported scrap and hydroelectric power from the Péligre station.

The slackening in the rate of economic growth in 1974 was accompanied in the second half of the year by a similar trend in domestic prices. Figures up to November indicate that consumer prices rose 18.8 per cent, i.e., inflation remained at around the previous year's rate of 20 per cent, in spite of the repercussions, particularly in 1974, of the rise in import prices (18 per cent in 1973 and 49 per cent in 1974). The unsatisfactory and uncertain results of agricultural production, especially that destined for the domestic market, accentuated the already heavy dependence on food imports and, therefore, the effect of their high prices. Added to this was the rise in the price of fuels.

The impact of external prices was counteracted by curtailing the means of payment, which at the end of September were still at the December of 1973 level. The only expansionist factor of monetary liquidity appears to have been domestic credit, which up to September had increased by 30 per cent (27 per cent of which went to the private sector), since at that date international reserves showed a decrease and quasi-money rose by 44 per cent.

2. Foreign trade and the balance of payments

The high world market prices in 1973 favoured only a few of Haiti's export commodities, such as sugar, bauxite and sisal. The price of coffee, which represents about 40 per cent of its total exports,

Table 220. Haiti: total supply and demand

	Millions of gourdes at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970–1972*	*1973*	*1974*[a]
Total supply	*2,603*	*3,011*	*3,054*	*115.4*	*114.1*	*5.3*	*4.4*	*1.4*
Imports[b]	348	412	378	15.4	14.1	6.8	3.8	−8.4
Gross domestic product	2,255	2,599	2,676	100.0	100.0	5.0	4.5	3.0
Total demand	*2,603*	*3,011*	*3,054*	*115.4*	*114.1*	*5.3*	*4.4*	*1.4*
Exports[b]	265	308	309	11.8	11.5	8.0	−0.3	0.3
Domestic demand	2,338	2,703	2,745	103.6	102 6	4.9	5.0	1.6
Gross domestic investment	157	218	233	7.0	8.7	6.2	9.0	6.9
Total consumption	2,181	2,485	2,512	96.6	93.9	4.4	4.6	1.1
General government	188	228	225	8.3	8.4	2.3	15.7	−1.3
Private	1,993	2,257	2,287	90.3	85.5	4.5	3.6	1.3

SOURCES: 1970–1973: ECLA calculations based on figures supplied by the Haitian Statistical Institute; 1974: ECLA estimates based on data from the same source.

Note: The figures for exports and imports of goods and services were taken from balance-of-payments data expressed in dollars at current prices, which were converted to constant 1970 values by deflation, using price indexes calculated by ECLA for the purpose.

[a] Preliminary figures.

[b] Goods and services, excluding factor payments.

increased much less. This trend was reflected in a rise of about 33 per cent in the unit value and a slightly smaller increase (31 per cent) in the total value of exports, due to the slight reduction estimated in the volume of exports during the year (see figure XXXI).

The value of imports of goods rose 41 per cent, owing to the prevailing high prices, particularly of food-stuffs–which account for a large proportion of Haiti's imports–and of fuels, which, for the same reason, must have absorbed about 15 per cent of total imports. Thus, the average prices of imports increased 49 per cent, while their volume decreased by about 6 per cent.

As regards the country's main export commodities, coffee sales decreased in volume, so that their value appears to have varied little with respect to 1973. The value of sugar exports is estimated to have reached 12 million dollars, i.e., over three times the 1973 figures; in addition to the extraordinary increase in sugar prices, another factor seems to have been the recovery of around 20 per cent in the volume exported, following a reduction of one third in 1973.

Exports of sisal reached some 3 million dollars–85 per cent more than in 1973–about 40 per cent of which is attributable to an increase in volume. Bauxite exports, in contrast, dropped by about 10 per cent, owing to the smaller volume of sales.

As regards other relatively important products, exports of essential oils and meat appear to have shown little change in volume with respect to 1973.

Exports to the United States of light manufactures produced locally, mainly from imported raw materials, have rapidly become more important in recent years. In 1973 they reached a value of some 40 million dollars (total exports of goods amounted to 52.5 million dollars that year,[34] 33 million of which represented products manufactured with around 29 million dollars' worth of imported inputs.

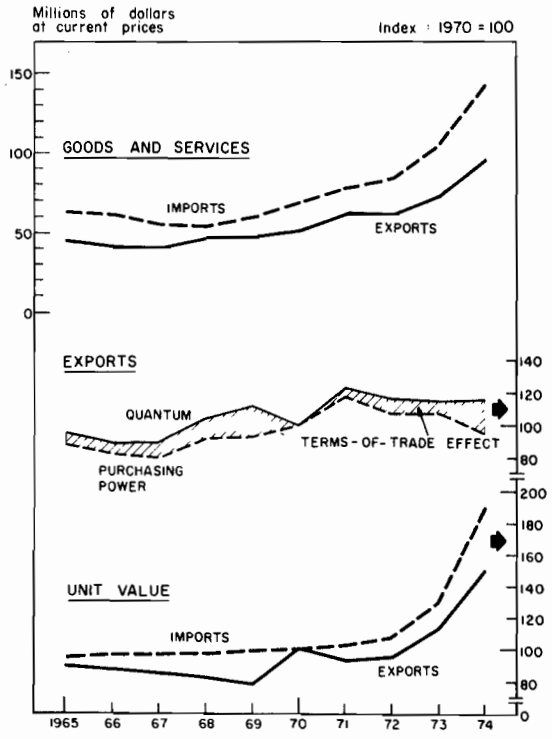
These exports consisted mainly of articles of clothing, footwear, toys and sports items, electrical apparatus and material, etc. Unfortunately, there are no data available on the trend of these exports in 1974.

The uneven growth of exports and imports during the year resulted in a trade deficit of 34 million dollars, which is 64 per cent higher than the 1973 deficit and nearly four times those recorded at the beginning of the decade. Added to this is the deficit of 14.2 million dollars resulting from the movement of services, which is mainly attributable to the considerable increase in expenditure on freight and insurance, since the net income from tourism rose from 7.5 million dollars in 1973 to 13 million in 1974.

The movement of goods and services described above, added to the net external investment income, but subtracting the large inflows which normally accrue under the head of private transfer payments (22 million dollars) resulted in a final current account deficit of 33 million dollars, which is equivalent to 27.4 million SDR units, or twice that recorded in 1973 (see table 221).

The deficit on current account exceeded the net inflow of non-compensatory capital of 18.7 million SDR units, which was considerably higher than that registered in 1973. It was therefore necessary to use international reserves to a value of 4.8 million SDR units, and 3.9 million dollars from the fund set up to compensate for the balance-of-payments disequilibria caused by the high prices of liquid fuels.

Figure XXXI. Haiti: trend of external variables
Natural scale



[34] This value represents the proportion of exports produced from local raw materials and the rest of the exports after subtracting the cost of the imported raw material used in their manufacture, i.e., approximately 7 million dollars in 1973.

Table 221. Haiti: balance of payments
(Millions of SDR units)

	1970	1971	1972	1973	1974[a]
Current account					
Exports of goods and service	52.9	64.3	57.5	61.3	80.1
Goods FOB	39.0	47.1	39.4	43.6	57.4
Services	13.9	17.2	18.1	17.7	22.7
Transport	0.3	1.0	0.9	0.5	0.7
Travel	6.6	8.7	12.4	14.4	17.3
Imports of goods and services	69.5	78.6	79.1	87.3	120.0
Goods FOB	47.7	55.9	56.0	60.7	85.6
Services	21.8	22.7	23.1	26.6	34.4
Transport	9.8	10.7	12.0	13.7	19.1
Travel	4.3	4.5	4.8	5.5	6.5
Net external investment income	−3.6	−3.9	−4.2	−4.6	−6.0
Profits	−3.2	−3.6	−3.8	−4.1	−5.3
Interest	−0.4	−0.3	−0.4	−0.5	−0.7
Net private transfer payments	15.0	13.1	22.2	17.3	18.5
Balance on current account	−5.2	−5.1	−3.6	−13.3	−27.4
Capital account					
Net external financing ($a + b + c + d + e$)	5.2	5.1	3.6	13.3	27.4
(*a*) Net external non-compensatory capital	9.8	10.6	16.5	17.3	
Direct investment	2.8	3.4	3.8	7.2	
Long- and medium-term loans	1.2	2.6	10.2	1.6	
Amortization payments	−1.3	−1.3	−2.9	−2.8	18.7
Short-term liabilities	0.2	0.1	1.0	4.1	
Official transfer payments	6.9	5.8	4.4	7.2	
(*b*) Domestic non-compensatory capital or assets	−2.6	−3.4	−2.5	−5.2	
(*c*) Errors and omissions	−0.9	3.9	−4.6	0.7	
(*d*) Allocation of SDRs	2.5	2.0	2.0	–	–
(*e*) Net compensatory financing (increase −)	−3.6	−8.0	−7.8	0.5	8.7
Balance-of-payments loans, arrears, IMF loans and other liabilities of the monetary authorities	0.3	–	0.3	0.2	...
Amortization payments	−2.9	−2.2	−1.2	–	...
Movements of foreign exchange reserves (increase −)	−0.9	−2.8	−4.4	−0.3	...
Movements of gold reserves (increase −)	–	−2.0	−0.6	0.5	...
SDRs (increase −)	−0.1	−1.0	−1.9	0.1	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26.

[a] Estimates based on official statistics.

HONDURAS

1. RECENT ECONOMIC TRENDS

In 1974 the gross domestic product of Honduras decreased by 0.5 per cent, thus reversing the trend of 1973 when it grew by 5 per cent (see table 222).

This unfavourable result of economic activity may be attributed to various factors and circumstances; the most important of these were, of course, the consequences of the hurricane which descended on the country in mid-September, and whose repercussions aggravated existing problems and also caused new bottlenecks in the country's economy.[35]

[35] Around 8,000 lives lost and about 248,000 persons affected, plus considerable damage in the physical infrastructure, stocks of agricultural and livestock capital, and national resources, with the consequent effects on income, the balance of payments and the financial situation of the public sector, were the immediate results of the disaster. For more details, see *Informe sobre los daños y repercusiones del huracán Fifi en la economía hondureña* (E/CEPAL/AC.67/2/Rev.1), October 1974, prepared by the Mexico Office in collaboration with SIECA and BCIE.

Table 222. Honduras: total supply and demand

	Millions of lempiras at 1970 prices			Structure (percentages)		Annual growth rate (percentages)		
	1970	1973	1974[a]	1970	1974[a]	1970–1972	1973	1974[a]
Total supply	*1,914.9*	*2,065.4*	*2,120.4*	*133.9*	*131.6*	*0.6*	*6.6*	*2.7*
Imports[b]	485.3	446.4	509.5	33.9	31.6	–9.7	12.9	14.1
Gross domestic product	1,429.6	1,619.0	1,610.9	100.0	100.0	3.9	5.0	–0.5
Total demand	*1,914.9*	*2,065.4*	*2,120.4*	*133.9*	*131.6*	*0.6*	*6.6*	*2.7*
Exports[b]	384.9	442.7	407.4	26.9	25.3	5.0	4.3	–8.0
Domestic demand	1,530.0	1,622.7	1,713.0	107.0	106.3	–0.5	7.2	5.6
Gross domestic investment	312.5	280.2	361.4	21.9	22.4	–13.7	20.5	29.0
Gross fixed investment	273.2	255.6	278.9	19.1	17.3	–8.9	12.8	9.1
Public	94.4	58.0	64.6	6.6	4.0	–27.3	16.2	11.4
Private	178.8	197.6	214.3	12.5	13.3	–0.6	11.8	8.5
Total consumption	1,217.5	1,342.5	1,351.6	85.1	83.9	2.6	4.8	0.7
General government	166.2	171.1	172.8	11.6	10.7	–0.2	3.3	1.0
Private	1,051.3	1,171.4	1,178.8	73.5	73.2	3.0	5.0	0.6

SOURCES: 1970–1972: ECLA calculations based on figures supplied by the Central Bank of Ecuador; 1973–1974: ECLA estimates based on data from the same sources.

Note: The figures for exports and imports of goods and services were taken from balance-of-payments data expressed in dollars at current prices, which were converted to constant 1970 values by deflation, using price indexes calculated by ECLA for the purpose.

[a] Preliminary estimates.

[b] Goods and services, excluding factor payments.

Previous to this, there had been other phenomena which played their part in weakening external demand, and through the decrease in employment and income conveyed a downward trend to the rate of growth of total demand. All this took place under circumstances in which the trend in import prices–particularly petroleum and its products–was putting pressure on production costs, and a serious deficit was building up in the balance of payments.

The effects of the hurricane were particularly disastrous for the country's economy, owing to the fact that floods affected an area which produced around 40 per cent of the agricultural product–particularly banana-growing–contributed substantially to generating employment and external resources, and also had an extensive network of roads, ports and telecommunications.[36]

Under these circumstances the current account deficit reached a level of 85.3 million SDR units as a result of the increase of 6.8 per cent in the value of exports of goods and services compared with a growth of 48 per cent in imports. This sizable increase was the result of a combination of higher international prices–especially of petroleum products–and the additional resources required to replace losses in national output and capital.

The public sector, which at the beginning of the year had undertaken a serious economic and social development effort by formulating the National Plan, had to face up to new problems and requirements as a result of the disaster; these brought a change in immediate priorities as regards expenditure and investment and also affected the amount of expenditure partly as a result of the decline in the collection of tax revenue. Preliminary estimates indicate a decline of 35 million lempiras in current income as a direct result of the hurricane. In brief, the public sector deficit was 45.5 per cent higher than in 1973 and thus made necessary a wider use of external credit, whose contribution to financing the fiscal deficit in 1974 was 58.3 per cent.

The decrease of 8 per cent in the export quantum had a decisive influence in reducing the growth rate of total demand from 6.6 per cent to 2.7 per cent between 1973 and 1974 (see table 222). Expenditure on consumption also grew less, with a drop in the rate of increase from 4.8 per cent in 1973 to 0.7 per cent in 1974. As regards private consumption, some of the factors which brought it down were the drop in earnings, the effect of price increases[37] and the relative shortage of food products; however, these effects were partly offset by the increase in wages and the price

[36] Losses in terms of national resources were estimated at 150 million dollars.

[37] With an annual increase of 13 per cent up to October 1974 in the consumer price index, inflation in Honduras was less intensive than in the rest of the Central American countries, although this rate is rather higher than the increase in local prices in October 1973 (4.1 per cent).

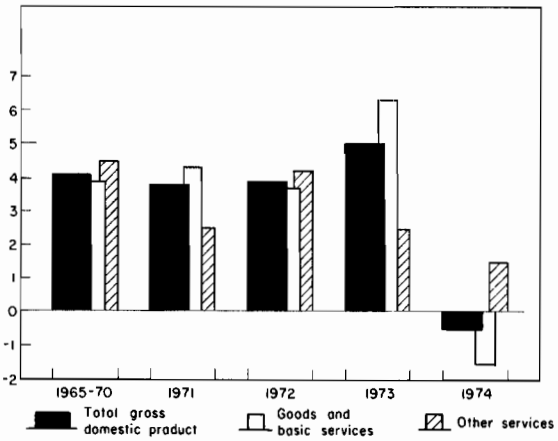
control policy applied to some products of general consumption, and the donations received from abroad to attend to the basic needs of flood victims. As far as public consumption was concerned, the drop in the growth rate may be explained in terms of the policy followed by the public sector to cut down on spending with a view to increasing the capital formation effort. The rate of growth of public investment reached 11.4 per cent, in addition to an increase of 8.5 per cent in private investment.

In 1974 appreciable quantities of stocks were accumulated as a result of the voluntary retention of coffee, the decrease in meat exports, and also of stockpiling in commerce and industry.

As far as supply was concerned, imports showed a considerable increase of 14.1 per cent in real terms, enabling the decrease in local supply to be offset at least in part. This was mainly a reflection of the need to replace the losses caused by the disaster, but it was also due to special imports made during the first half of the year in the expectation of new taxes being applied to imports, and this in turn led to the application of restrictive measures to imports of luxury goods.

As regards local output (see table 223), given the relative importance of agricultural production and in particular of banana output in the area affected by the hurricane, losses from these plantations caused the breakdown of a large part of domestic economic activity (see figure XXXII).

Figure XXXII. Honduras: growth of gross domestic product
(Annual growth rates)
Natural scale



Towards the middle of the year prospects were favourable as regards volumes of output, where the difficulties stemming from the application of the new tax on banana exports had been overcome. In addition, as a result of an improvement in prices of basic grains, more funds available from the National Development Bank and the intensive promotion work carried out, the area sown was expanded and the rice, bean and maize harvests promised to be substantially larger than in 1973. Production of sugar-cane and other minor crops

Table 223. Honduras: gross domestic product at factor cost, by sector of economic activity

	Millions of lempiras at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970-1972*	*1973*	*1974*[a]
Agriculture	446.7	510.9	473.1	34.6	32.5	4.6	4.5	−7.4
Mining	29.1	39.3	45.5	2.3	3.1	3.2	26.8	15.8
Manufacturing	180.5	221.9	234.1	14.0	16.1	6.6	8.1	5.5
Construction	64.6	57.2	59.0	5.0	4.0	−8.5	5.7	3.1
Subtotal goods	*720.9*	*829.3*	*811.7*	*55.9*	*55.8*	*4.0*	*6.4*	*−2.1*
Electricity, gas and water	17.7	18.6	19.0	1.4	1.3	0.8	3.9	2.4
Transport and communications	85.9	100.6	102.8	6.7	7.1	5.2	5.8	2.2
Subtotal basic services	*103.6*	*119.2*	*121.8*	*8.0*	*8.4*	*4.4*	*5.5*	*2.2*
Commerce and finance	208.4	224.3	227.0	16.2	15.6	1.9	2.5	1.2
Government	46.8	50.4	50.9	3.6	3.5	1.5	4.3	1.0
Ownership of dwellings	98.4	114.4	116.3	7.6	8.0	6.1	5.5	1.7
Miscellaneous services	112.5	124.0	126.6	8.7	8.7	4.3	1.4	2.1
Subtotal other services	*466.1*	*513.1*	*520.8*	*36.1*	*35.8*	*3.3*	*2.6*	*1.5*
Total	*1,290.6*	*1,461.6*	*1,454.3*	*100.0*	*100.0*	*3.9*	*5.0*	*−0.5*

SOURCES: 1970-1972: ECLA calculations based on figures supplied by the Central Bank of Honduras; 1973-1974: ECLA estimates based on official data.

Note: As the individual activities and the totals were calculated independently, the sum of the former does not correspond exactly with the latter.

[a] Preliminary figures.

was also stepped up and fallow land was opened up for the production of basic grains thanks to the establishment of rural settlements.

However, because of the floods, the volumes of output of the main crops were substantially reduced as the following figures show: bananas 21.7 per cent; maize 29.2 per cent, sorghum 11.2 per cent and cotton 13.5 per cent. Stock-breeding also suffered considerable damage, both in dairy and meat production, and the problems facing the sector were aggravated by the reduction of exports of meat to the United States market.

Some crops situated in areas which were not seriously affected by the floods, however, achieved volumes of output higher than those of the previous year. Owing in some cases to the extension of the area under cultivation and in others to improvements in production techniques with the incentive of price levels in the international market the output of coffee increased by 4.1 per cent, sugar-cane by 7 per cent, tobacco by 10 per cent and beans by 2.3 per cent, among the main crops.

In the first half of the year, manufacturing received impetus from the growth of sales of food-stuffs, beverages, textiles and non-metallic mineral products increasingly directed towards the external market, both in Central America and the United States, and also from adjustments in wages which contributed to increasing local demand. This favourable development was interrupted during the second half of the year by the paralysation of industries situated in the affected area and by the lack of supplies of agricultural raw materials. All this contributed to an increase of only 5.5 per cent in the industrial product.

The increase in Honduras exports to the Central American market, however, as a result of the special treatment granted to Honduras by the countries of the region at the end of the year, and also the effort being made to attend to reconstruction requirements and to development projects included in the plan and the support which the international community has undertaken to provide in this respect, could counteract this trend.[38]

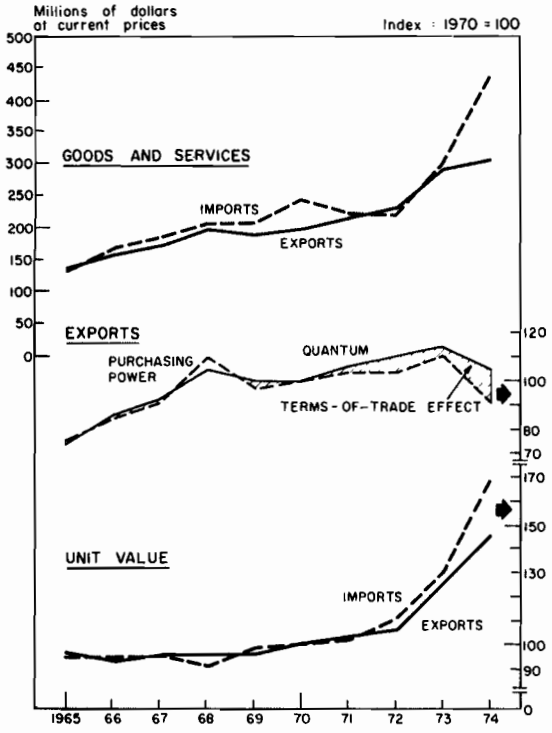
Of the other sectors of the economy, construction showed a growth rate of 3.1 per cent, which was down on that of 1973, and was affected by the performance of capital formation analysed above, particularly in the private sector. The finance sector also reduced its growth rate compared with the previous year, like the other sectors of economic activity which in one form or another showed evidence of the bottleneck caused by balance-of-payments problems and the inflationary pressures which appeared in 1974 (see table 223).

2. BALANCE OF PAYMENTS AND EXTERNAL TRADE

The origin of the current account deficit, which amounted to 85.3 million SDR units in 1974, may be found in the active growth of imports of goods (52.7 per cent in current values and 17.5 per cent at constant prices), while the value of exports of goods only increased by 6.3 per cent and the volume decreased by 8.4 per cent. Of special importance in this situation was the uneven growth rate of unit values of imports and exports; while in the case of imports the increase was 30 per cent, this growth was 16 per cent in the case of exports (see figure XXXIII).

In the course of the year problems arose in connexion with sales of meat to the United States, the voluntary retention of sizable quantities of coffee and the reduction in exports of timber. Special mention on account of its size, however,

Figure XXXIII. Honduras: trend of external variables
Natural scale



[38] See the *Report of the Ninth Extraordinary Session of the Committee of the Whole* of the Economic Commission for Latin America (E/CEPAL/AC.67/5). This meeting was convened to analyse the natural disaster which took place in Honduras and to decide on the international co-operation measures required. It was held in New York on 21-22 October 1974.

should be made of the drop of 23.8 per cent in the volume of bananas exported and the decrease of 17 per cent in their value. Exports of coffee too decreased by 25.1 per cent in terms of volume and 11.5 per cent in terms of value. Exports of meat decreased by 43.9 per cent in volume and 32.4 per cent in value. Only in the case of timber was there a growth of 17.4 per cent at current values despite a drop of 24.2 per cent in volume.

In the case of imports, however, the increase in prices, especially of petroleum and petroleum products, offset any earnings from the increase in the prices of the exports analysed above.

On top of this adverse situation in the prices of the inputs required for the development of economic activity came imports of capital goods and material for the reconstruction of the physical infrastructure. In addition, imports of goods increased by the 52.7 per cent mentioned above and the trade balance was in deficit by 97 million dollars, following positive balances of around 30 million dollars in the two preceding years. Furthermore, the uncertainty as to whether the entire banana-producing area which had been destroyed could be restored in the medium term, and the proportions which imports of fuels had come to acquire in the structure of imports, in addition to the capital equipment and raw materials required to re-establish the rate of economic growth, all in all do not offer much encouragement as regards possibilities of reducing this negative balance with any ease in the years to come.

As a result of the bilateral treaties between Honduras and Nicaragua, Guatemala and Costa Rica.[39] Honduras exports to the region grew substantially, reaching a total between January and September 1974 of 18 million dollars compared with a total of 5.8 million during the same period of the previous year. For their part, imports from these countries increased more slowly, and Honduras trade deficit with the region decreased.

At the end of July a series of measures connected with external trade was put into practice, including in particular the reduction of the credit portfolio of the banks for trade and consumption; the extension of a line of rediscounts for exports; the reduction to one year of the maximum deadline for import trade credit; the restriction of the authorization granted to the banks to obtain external medium- and long-term finance to purchases of agricultural or industrial machinery and equipment and in certain cases to financing inputs; and, lastly, the increase of between 10 and 90 per cent in duties on imports of vehicles.

As regards capital movement, in 1974 there was a net inflow of non-compensatory capital of around 64 million SDR units, which, although it was twice the amount of the previous year, was less than the deficit recorded in the current account, thus producing a decrease of 21 million SDR units in the country's net international reserves (see table 224).

3. Money and credit

As regards the external monetarization of the economy, liquidity continued to decrease, and this would offer one more explanation of why the general level of prices did not increase more sharply. Money supply followed the same trend: the balance at the end of September 1974 was only 7.3 per cent higher than in September 1973. Private sector deposits also recorded a slight decrease during the same period. It is, however, noteworthy that at the same time as primary liquidity in the hands of the public decreased, saving and time deposits increased, as did holdings of bonds and mortgage bonds in the hands of private persons, all of which helped to reduce the intensity of the pressure on prices which might otherwise have been exerted by a greater expansion of the means of payment.

As regards monetary demand, bank credit grew only moderately, and there was even a net reduction in bank financing utilized by the public sector—in line with the restrictive public spending policy adopted by the central government in the course of the year—the net debit balance of which dropped by 25 per cent compared with the previous year. However, credit to the private sector increased by 20.3 per cent, so that the growth of total credit activity in the banking system was 13.7 per cent, which was lower than the rate in 1973 (20.8 per cent).

As far as the destination of credit was concerned, the agricultural sector and industry received smaller percentages of total credit during the first half of the year than had traditionally been their lot in the past, while the share of trade increased.

However, the measures adopted in July to protect the situation of the balance of payments, and those aimed at slowing down inflationary pressures, presumably modified the structure of credit according to destination which previously existed, towards the end of 1974.

As regards inflationary pressures, the annual rate of increase in the consumer price index up to October had risen to 13 per cent, rather higher than that recorded for the period 1972-1973 (4.1 per cent). Trends running counter to each other affected the evolution of local prices. Pressure for

[39] The trade agreement drawn up in 1974 with Panama will show real results as from next year.

Table 224. Honduras: balance of payments
(Millions of SDR units)

	1970	1971	1972	1973	1974[a]
Current account					
Exports of goods and services	196.5	215.6	212.4	236.4	253.3
Goods FOB	178.2	194.8	191.4	214.6	228.7
Services	18.3	20.8	21.0	21.8	24.6
Transport	5.1	6.8	6.0	6.3	7.1
Travel	4.1	4.3	4.5	6.1	6.7
Imports of goods and services	244.3	219.5	203.5	244.2	362.9
Goods FOB	203.4	177.5	162.6	201.9	309.2
Services	40.9	42.0	40.9	42.3	53.7
Transport	20.5	20.6	19.4	21.5	31.2
Travel	11.9	12.2	12.9	12.1	12.5
Net external investment income	−22.6	−23.3	−21.0	−27.5	−2.0
Profits	−20.0	−18.6	−15.8	−20.8	6.7
Interest	−2.6	−4.7	−5.2	−6.7	−8.7
Net private transfer payments	2.9	3.1	3.0	2.9	26.3
Balance on current account	−67.5	−24.1	−9.1	−32.4	−85.3
Capital account					
Net external financing (*a* + *b* + *c* + *d* + *e*)	67.5	24.1	9.1	32.4	85.3
(*a*) Net external non-compensatory capital	57.6	33.0	29.2	38.6	
Direct investment	8.4	7.3	0.6	5.4	
Long- and medium-term loans	38.4	30.9	27.6	29.4	
Amortization payments	−5.6	−7.8	−9.5	−10.8	
Short-term liabilities	12.7	−1.1	7.5	11.8	63.9
Official transfer payments	3.7	3.7	3.0	2.8	
(*b*) Domestic non-compensatory capital or assets	−2.9	−8.0	−14.0	−8.1	
(*c*) Errors and omissions	0.9	−1.5	4.0	2.1	
(*d*) Allocation of SDRs	3.2	2.7	2.6	–	–
(*e*) Net compensatory financing (increase –)	8.7	−2.1	−12.7	−0.2	21.4
Balance-of-payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	–	0.1	0.8	5.5	...
Amortization payments	−0.9	−0.3	−0.8	–	...
Movements of foreign exchange reserves (increase –)	5.1	0.8	−10.1	0.5	...
Movements of gold reserves (increase –)	4.7	–	–	−6.2	...
SDRs (increase –)	−0.2	−2.7	−2.6	–	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26.

[a] Estimates based on official statistics.

an increase, the initial impetus for which was generated by increasing import prices, was partly controlled by the establishment of BANASUPRO, a State agency set up precisely to regulate and control the prices of basic grains and other products of general consumption. Money and credit policy and the trend of public expenditure acted in the same direction.

JAMAICA

The impact of world inflation on the Jamaican economy was particularly severe in 1974. Largely dependent as it is on imported supplies, the level of domestic prices directly reflected the inflationary conditions prevailing in the industrialized economies. The situation was aggravated by the fact that Jamaica is a hydrocarbon importing country. Therefore, all the economic variables experienced sharp increases in the current values in which they are usually measured in this country.

Consumer prices in Kingston rose by 26.5 per cent during the year, and by 32.8 per cent in rural areas. In the case of food and beverages, the increase was 33.8 per cent in the Kingston metropolitan area. By the end of the year the rate of price increases diminished, coinciding with a bigger supply of imported goods thanks to the lifting of certain import restrictions.

These conditions create a certain amount of confusion regarding the performance of the econ-

omy in 1974. It may be estimated, however, that its growth was fairly sluggish (about 3 per cent), despite the momentum gained by export activities. The activities operating on the basis of domestic demand, on the other hand, remained at a standstill or suffered a decided deterioration in real terms.

1. THE PRODUCT BY ECONOMIC SECTOR

The growth of the agricultural sector was minimal in 1974. The sugar-cane harvest, which remained at a depressed level in 1973, recorded a substantial increase which, to judge from the final products manufactured from it, was over 30 per cent.[40] Output of citrus fruit and pimentos also increased in volume. In contrast, the production of cocoa, coffee and bananas, among the export crops, declined.

With regard to crops for domestic consumption, the supply of tubers and other similar products increased, and no change was noted in that of vegetables in spite of adverse weather conditions. As regards livestock production, there were evident reductions in sales of meat, but poultry sales continued to increase.

The gross mining product rose by over 10 per cent in real terms. This activity benefited in 1974 from the rapid and, to some extent, persistent increase in world prices.

On the basis of part-year data, it is estimated that the production of bauxite rose by 12 per cent; output of alumina, Jamaica's other main export commodity, increased at a lower rate but still by over 9 per cent (see table 225).

The production of lime, on the other hand, declined owing to the contraction of domestic demand. The same situation arose in quarrying, in connexion with the production of cement.

The trends of the various branches of manufacturing varied greatly in 1974. Several of them faced difficulties in obtaining imported inputs, and others a weakened demand owing to the increase in prices. Yet others took advantage of the external or domestic market conditions to expand

[40] It is estimated that the unit yields of saccharose did not change significantly.

Table 225. Jamaica: output of some important products

Product	*Unit*	*1972*	*1973*	*January-September 1974*
Bauxite	Thousands of long tons	12,784	13,276	11,167
Alumina	Thousands of long tons	2,054	2,466	2,033
Gypsum	Thousands of long tons	373	365	130
Petroleum products	Millions of imperial gallons	425	462	343[a]
Sugar	Thousands of tons	373	326	367
Rum and alcohol	Thousands of gallons	3,657	4,034	2,969[b]
Molasses	Thousands of gallons	22,448	19,773	25,711
Beer	Thousands of gallons	11,132	12,474	9,522
Edible oil	Thousands of gallons	2,725	2,664	1,549
Edible fats	Short tons	7,452	6,247	4,781
Soap	Tons	7,960	5,921	3,964
Detergents	Tons	5,716	5,240	3,863
Condensed milk	Thousands of pounds	54,830	56,392	45,700
Textiles	Thousands of square yards	8,885	7,574	9,063[c]
Cement	Thousands of tons	424	413	283
Flour	Thousands of pounds	111,905	97,715	36,955[b]
Sulphuric acid	Tons	13,182	12,615	8,297
Paints	Thousands of imperial gallons	1,571	1,634	506[b]
Steel	Tons	16,747	17,824	...
Tyres	Thousands of pounds	5,089	5,996	...
Bagasse board	Thousands of square feet	12,413	10,190	...
Fertilizers	Tons	44,386	50,003	38,835
Aluminium sulphate	Tons	4,183	4,755	4,874
Salt	Short tons	15,313	13,669	...
Animal feeds	Millions of pounds	354	220	86[b]

SOURCES: National Planning Agency, *Economic and Social Survey*, 1973; Department of Statistics, *Statistical Abstract*, 1972; and data in ECLA's possession.

[a] Data for January to October.

[b] Data for January to June.

[c] Data for full year 1974.

production. The sector as a whole grew by about 3 per cent in 1974.

Among the sectors in which there was a drop in real supply are petroleum refining, fats, soaps and detergents, cement, chemical products, flour and animal feeds. There were increases, on the other hand, in products obtained from sugar cane, canned milk, beer, fertilizers and aluminium sulphate. It will be noted that there was no general pattern accounting for these variations.

There is no real assessment of construction activity in Jamaica. Its current value was boosted in 1974 by the rise in the price of construction materials and in wage costs.

On the other hand, building is known to have declined, not only because of the higher prices of the units constructed, but also because the private programme for the construction of hotels and other tourist accommodation was completed at the beginning of the year. This programme has not been continued because the situation in the developed economies, particularly the United States, has discouraged tourism abroad. In Jamaica it has adversely affected the hotel industry, whose indexes of activity are declining steadily.

The factor which has prevented a definite contraction in this activity and, it might be added, in urban employment is the construction programme undertaken by the Government, which has stepped up its activities in connexion with the construction of infrastructure and low-cost housing projects.

2. EVOLUTION OF EXTERNAL TRANSACTIONS

Increases of around 60 per cent in the value of exports of bauxite and alumina and of over 90 per cent in that of exports of sugar, rum and molasses

Table 226. Jamaica: balance of payments
(Millions of SDR units)

	1970	*1971*	*1972*	*1973*	*1974*[a]
Current account					
Exports of goods and services	521.6	545.2	567.4	527.8	755.8
Goods FOB	342.1	345.6	347.8	328.5	503.0
Services	179.5	199.6	219.6	199.3	252.8
Transport	27.6	29.0	31.1	30.1	40.7
Travel	95.5	109.0	124.1	106.5	133.9
Imports of goods and services	598.1	631.5	658.8	639.6	868.9
Goods FOB	449.0	473.1	486.9	476.7	656.9
Services	149.1	158.4	171.9	162.9	212.0
Transport	87.9	88.4	93.7	91.7	124.7
Travel	15.5	16.3	19.0	16.6	19.1
Net external investment income	−98.2	−102.8	−115.5	−115.0	−154.5
Profits	−103.9	−105.9	−113.9	−105.3	−140.6
Interest	5.7	3.1	−1.6	−9.7	−13.9
Net private transfer payments	26.2	26.2	31.9	27.8	29.1
Balance on current account	−148.5	−162.9	−175.0	−199.0	−238.5
Capital account					
Net external financing (*a* + *b* + *c* + *d* + *e*)	148.5	162.9	175.0	199.0	238.5
(*a*) Net external non-compensatory capital	191.0	174.9	147.2	188.3	288.4
Direct investment	162.1	174.7	89.8	61.2	
Long- and medium-term loans	14.1	27.5	37.3	129.0	
Amortization payments	−4.3	−8.1	−5.6	−12.6	
Short-term liabilities	23.5	−13.7	31.9	16.9	
Official transfer payments	−4.4	−5.5	−6.2	−6.2	
(*b*) Domestic non-compensatory capital or assets	−35.1	−7.9	3.9	−23.8	
(*c*) Errors and omissions	7.4	16.1	−4.7	−18.7	
(*d*) Allocation of SDRs	6.4	5.7	5.6	–	–
(*e*) Net compensatory financing (increase −)	−21.2	−25.9	23.0	53.2	−49.9
Balance-of-payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	–	–	13.2	18.8	...
Amortization payments	–	–	–	−5.5	...
Movements of foreign exchange reserves (increase −)	−14.6	−15.7	3.9	39.4	...
Movements of gold reserves (increase −)	−0.2	−3.8	–	–	...
SDRs (increase −)	−6.4	−6.4	5.9	0.5	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26.

[a] Estimates based on official statistics.

largely account (in a proportion of 90 per cent) for the 53 per cent increase in the total value of exports of goods in 1974.

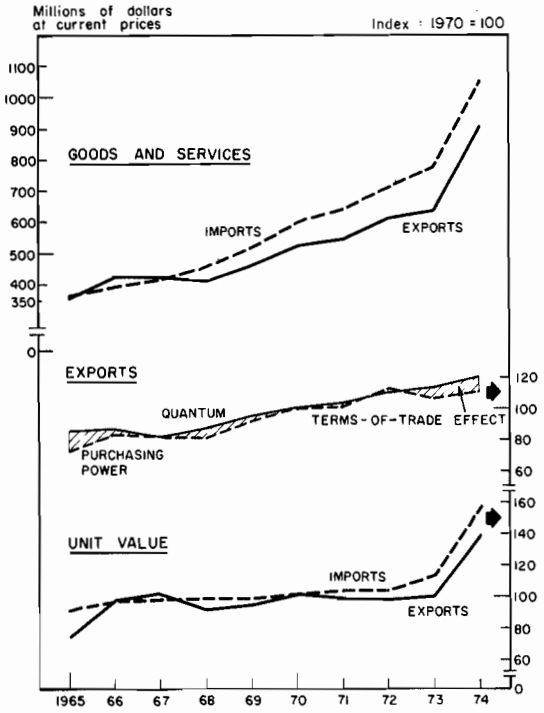
From the moment that international quotations for bauxite and alumina were related to those for aluminium in bars, their prices rose rapidly. Sugar and related products also experienced considerable price increases. Accordingly, it is estimated that the unit value of exports rose by 39 per cent and the volume by 10 per cent, taking the main export commodities, since the volume of banana, cocoa and coffee sales declined (see figure XXXIV).

The Government adopted various measures to curb imports, mainly of consumer goods and fuels. As a result, the volume of imports of goods fell slightly and the 37 per cent increase in value was exclusively due to the higher prices. Already in 1973 the volume of imports had contracted somewhat.

Notwithstanding the fact that exports of goods expanded more rapidly than imports, the trade deficit rose slightly. Moreover, the income from tourism, which is an important item in Jamaica since it represents a little over one quarter of total exports of goods, increased far less than exports (25.7 per cent). In addition, there was a larger net outflow under the head of freight, and remittances of profits and interest abroad were a third higher than in 1973 (see table 226).

This whole movement of current transactions resulted in a deficit of 238.5 million SDR units, or 20 per cent more than in 1973. However, thanks to a considerable net inflow of non-compensatory capital, which was double the flow in the previous year, net international reserves increased by 50 million SDR units.

Figure XXXIV. Jamaica: trend of external variables
Natural scale



MEXICO

1. A GENERAL APPRAISAL

The growth rate of the Mexican economy was 5.9 per cent in 1974, which compares unfavourably with that of the year before (7.6 per cent), but is higher than the average for the period 1970-1972. On the other hand, the increase in prices accelerated, at rates which are unusually high for what is considered to be one of the most stable economies in Latin America. Lastly, the rate of increase in gross fixed investment dropped in relation to 1973, with a more pronounced decrease in the public than in the private sector.

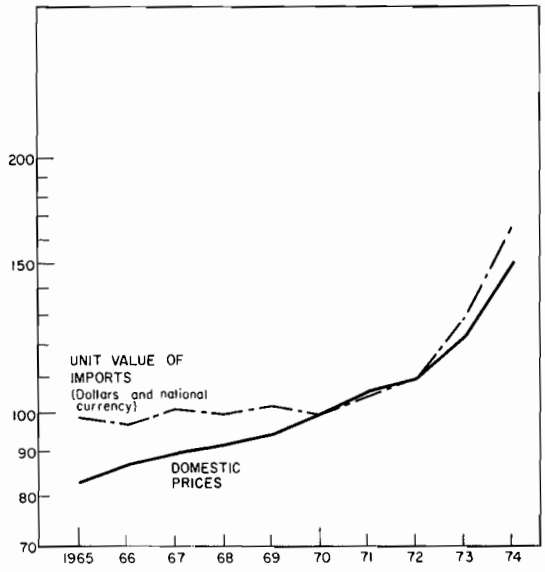
(a) *Imported inflation and its internal links*

These data on the evolution of the Mexican economy in 1974 cannot be properly evaluated unless they are considered within the context of the international situation. Imported inflation was a decisive factor in a number of aspects which affected the development of production and, particularly, the social situation. Consequently, government policy was necessarily more concerned with softening or preventing those effects than with pursuing the course and objectives laid down previously.

As in all the other countries of the region, the external situation had a serious impact, through different channels, on the level and system of prices. Up to 1971-1972, Mexico had somehow managed to contain the inflationary pressures generated abroad and its own or related pressures. As from 1973, however, the surge of rising prices was overwhelming and the rates of increase, which had been less than 6 per cent in the above two-year period, doubled in 1973 and redoubled in 1974 (12.2 and 24.2 per cent in the consumer price index) (see figure XXXV).

Moreover, as in other countries, but mainly though not exclusively as a result of the evolution

Figure XXXV. Mexico: indexes of unit value of imports and of domestic prices
(Index: 1970 = 100)
Semi-logarithmic scale



of the agricultural sector, food prices rose above the average index in 1973 and 1974. The same situation occurred in the transport and communications sector (an increase of nearly 38 per cent in 1974, which was over 40 per cent for Mexico City), owing to the need to adjust prices in line with the new oil quotations and the financing requirements of the national petroleum enterprise.

The rise in imports and exports was the most direct channel of transmission of imported inflation. In the case of imports, suffice it to say that they increased 58 per cent in value and only 23 per cent in volume. As regards exports, compared with an insignificant increase (3.2 per cent) in volume, their value in dollars at current prices rose by approximately 45 per cent.

It will be readily understood that these changes merely reflect the initial or direct impact of the rise in external prices. This was followed by often more intensive repercussions on the wide range of similar, competitive or substitute domestic goods and services, and multiplier effects in other areas (fiscal, monetary, and wages and salaries). Some principal links can be identified on the basis of the available data.

The fiscal projections are obvious. The most visible effect seems to have been the considerable increase in transfer expenditure (40 per cent in 1974) aimed in one way or another at mitigating the social implications of the rise in the prices of essential goods. In 1974, the result was an insignificant increment in fiscal–though not financial–investment, which must also involve compensatory transfers to enterprises with a view to containing increases in their prices and rates.

In the wages area, the developments analysed above caused the Government to decree a general adjustment and to establish the principle of annual reviews, as detailed in the appropriate section.

A study of monetary trends immediately reveals the very moderate rate of expansion of the means of payment (19 per cent), which was very little higher than in 1973 (17 per cent) and the immediately preceding years. This factor may conceivably have been considered as the line of resistance in slowing down the propagation and multiplication of inflationary pressures. On the other hand, there was an evident tendency to alter the distribution of monetary resources in favour of the public sector, to finance the growing deficit incurred in meeting the aforementioned requirements.

However successful those specific aims may have been, there is no doubt that this policy created a situation of scarce liquidity vis-à-vis the increases in prices, especially in the private sector. This, however, was in some degree offset by funds from external sources, a greater proportion of which also went to the public sector.

It is not possible to estimate the exact effect of those financial flows on production activity, although it seems obvious that it could not have been encouraging. In any case, if there is any reason to think that the effect was negative, it must be regarded as another unfortunate by-product of the efforts to moderate inflationary pressures.

The shortage of funds in the private sector did not, however, set in motion a vicious circle leading to widespread deterioration. Although many enterprises individually suffered liquidity crises, the leading companies had recourse to the use of private external capital, in so far as other factors made this advisable. It should be recalled here that since the mid-1960s Mexico's economic policy has linked certain financial parameters with those of the leading industrialized market economies. While keeping the rate of the peso to the United States dollar constant, Mexico has participated in a number of swap agreements with those economies. At the same time, the public sector has sold bonds on the international capital market, a resource also used independently and repeatedly by the private sector. Lastly, interest rates have been modified in the past few years, not only in accordance with internal financial parameters, but also with the aim of regulating international capital flows; this is a unique case in the region. Therefore, in Mexico, the concept of liquidity has acquired a broader dimension than it usually has in Latin America, which must be kept in mind in

examining the relationships between the financial and material aspects of its economy.

(b) *Impact of inflation on the production sector*

Viewing the problem from a different standpoint, it is necessary to analyse the reactions of the production sectors to these substantial changes in the levels and system of prices, or in the scale and composition of nominal demand.

It has, of course, already been observed that the changes and distortions inherent in the situation caused a slight drop in what might be termed Mexico's "historical" rate of growth. A more detailed examination reveals a widely varying spectrum of reactions which shows the strength and versatility of the system as well as its weak points.

As noted in the previous section, the agricultural sector was a particularly weak component of the producer complex. Incidentally, the same situation occurred in several Latin American countries, although it did not affect the other major economies (Argentina and Brazil, especially the latter). The most important factors here, as shown in detail later in this *Survey*, are long-standing structural questions, as well as clearly identified weaknesses of economic policy. Moreover, natural disasters affected the supply of such vital products as maize and beans, counteracting important government promotion measures and leading, in the case of maize, to onerous imports. This also occurred in the case of wheat, in spite of a considerable increase (about 40 per cent) in the crop.

Furthermore, incentives in the shape of higher external prices led to an increase in the proportion of output exported and to a change in the use of available land with this end in view. Thus, while exports of agricultural products rose 4.7 per cent, those destined for the domestic market went up by only 0.5 per cent. In other cases, such as that of sugar, a typical dilemma arising from this situation was brought into focus: the need to guarantee domestic supply at reasonable prices against the possibility of increasing exports at the high prices paid abroad. In placing the emphasis on the former objective, it was found that it was not possible to increase supply owing to the change-over in the use of land to other crops.

Nor was manufacturing able to react flexibly to the new situation, although its rate of expansion (5.8 per cent) conceals many disparities due to different causes. Generally speaking, the traditional consumer industries such as food-stuffs, textiles and clothing grew by less than the average rate. This trend seems to have been due both to the limited supply of agricultural inputs and to the low level of demand, owing no doubt to relatively higher prices of staple food items referred to above.

Some key industries, on the other hand, managed to exceed the average rate, but failed to regain their impetus of the previous year. A conspicuous exception was the performance of transport equipment, which grew by 25 per cent, following an expansion of 18 per cent in 1973. Estimates up to October 1974 put the increase in the number of vehicles sold at 27 per cent. These figures, in addition to others for durable consumer goods, are proof at once of the redistribution of income resulting from the changes in the price system, and the possible transfer to consumption of part of the income not used for private investment.

Lastly, and reaffirming the importance of the demand incentive, it must not be forgotten that the engineering industries maintained high rates of increase for their exports. These had been 50 per cent in 1972 and 57 per cent in 1973, and, according to data for January to October, they reached nearly 71 per cent in 1974, which in absolute figures is a little over 1,200 million dollars, or, it should be noted, nearly 60 per cent of the declared exports of goods in those 10 months. Whatever corrections may be made in these figures, the change that has taken place in the composition of exports of goods and this evidence of the Mexican economy's adjustments to the new patterns of the international division of labour cannot be overlooked.

The potential and flexibility of the system is confirmed by the performance of other major sectors, such as petroleum, petrochemicals and mining. Not only was the growth rate of mining quite satisfactory, but there was an appreciable improvement in the proportion of refined products in total exports of metals. As regards petroleum, although the 1974 transactions meant an onerous increase in the proportion of imports, it is none the less true that the discovery of new sources of production opened up for Mexico another promising basis for its economic development.

2. MAJOR SECTORS OF ACTIVITY

As mentioned above, total production rose at a slower rate (5.9 per cent compared with 7.6 per cent in 1973), owing to the weaker expansion of the manufacturing and construction sectors, as well as the scant increase in agricultural activity. Furthermore, the greater impetus of mining, petroleum and the petrochemical industry was not enough to offset the deceleration of the above-

Table 227. Mexico: total supply and demand

	Millions of pesos at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970-1972*	*1973*	*1974*[a]
Total supply	*459,904*	*549,341*	*586,406*	*109.8*	*110.8*	*5.2*	*8.0*	*6.7*
Imports[b]	41,204	49,611	57,192	9.8	10.8	3.1	13.2	15.3
Gross domestic product	418,700	499,730	529,214	100.0	100.0	5.4	7.6	5.9
Total demand	*459,904*	*549,341*	*586,406*	*109.8*	*110.8*	*5.2*	*8.0*	*6.7*
Exports[b]	34,312	45,516	44,248	8.2	8.4	9.4	10.9	-2.8
Domestic demand	425,592	503,825	542,158	101.6	102.4	4.8	7.8	7.6
Gross domestic investment	90,200	113,847	125,188	21.5	23.7	4.2	16.2	10.0
Gross fixed investment	82,200	104,221	114,151	19.6	21.6	4.2	16.7	9.5
Public	31,269	45,955	52,389	7.5	9.9	5.5	32.0	14.0
Private	50,931	58,266	61,762	12.1	11.7	3.4	7.0	6.0
Construction	44,362	...	...	10.6	...	...	...	...
Machinery and equipment	37,838	...	...	9.0	...	...	...	...
Total consumption	335,392	389,978	416,970	80.1	78.8	4.9	5.6	6.9
General government	32,575	41,311	44,203	7.8	8.4	8.9	6.9	7.0
Private	302,817	348,667	372,767	72.3	70.4	4.5	5.4	6.9

SOURCES: 1970-1973: ECLA calculations based on figures supplied by the Banco de México; 1974: ECLA estimates based on data from the same source.

Note: The figures for exports and imports of goods and services were taken from balance-of-payments data expressed in dollars at current prices, which were converted to constant 1970 values by deflation, using price indexes calculated by ECLA for the purpose.

[a] Preliminary figures.

[b] Goods and services, excluding factor payments.

Table 228. Mexico: gross domestic product at factor cost, by sector of economic activity

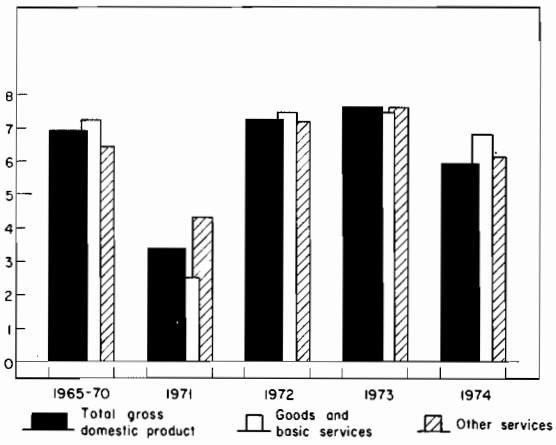
	Millions of pesos at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1973*	*1970-1972*	*1973*	*1974*[a]
Agriculture	47,179	48,654	49,822	11.8	10.2	1.2	0.6	2.4
Mining	16,184	18,112	20,611	4.1	3.8	4.3	3.0	13.8
Manufacturing	93,519	113,798	120,171	23.4	23.9	5.8	8.8	5.6
Construction	21,401	28,133	29,906	5.4	5.9	7.0	14.8	6.3
Subtotal goods	*178,283*	*208,697*	*220,510*	*44.7*	*43.8*	*4.6*	*7.0*	*5.7*
Electricity, gas and water	5,453	7,124	7,872	1.4	1.5	8.4	11.2	10.5
Transport and communications	10,363	13,721	...	2.6	2.9	8.6	12.2	...
Subtotal basic services	*15,816*	*20,845*	...	*4.0*	*4.4*	*8.5*	*11.9*	...
Commerce and finance	115,249	137,801	...	28.9	28.9	4.9	8.6	...
Government	25,971	35,055	...	6.5	7.4	11.2	9.2	...
Ownership of dwellings	30,115	34,493	...	7.6	7.3	4.0	5.9	...
Miscellaneous services	33,584	39,302	...	8.4	8.3	5.9	4.4	...
Subtotal other services	*204,919*	*246,651*	...	*51.4*	*51.8*	*5.8*	*7.6*	...
Subtotal services	*220,735*	*267,496*	*283,779*	*55.4*	*56.2*	*6.0*	*7.9*	*6.1*
Total	*399,018*	*476,238*	*504,336*	*100.0*	*100.0*	*5.4*	*7.6*	*5.9*

SOURCES: 1970-1973: ECLA calculations based on figures supplied by the Banco de México: 1974: ECLA estimates based on data from the same source.

Note: As the individual activities and the totals were calculated independently, the sum of the former does not correspond exactly with the latter.

[a] Preliminary figures.

Figure XXXVI. Mexico: growth of gross domestic product
(Annual growth rates)
Natural scale



mentioned sectors. Services in general followed the pattern of growth of the goods-producing sectors (see tables 227 and 228 and figure XXXVI).

(a) *Agriculture*

Owing to its slow expansion, the agricultural sector is becoming a bottleneck for the economy, because of its role in the development of other productive activities, the satisfaction of the population's basic consumption needs and the elimination of external disequilibrium. Moreover, approximately half the employed population works in the rural area.

Thus, before reviewing the developments in 1974, it is useful to recall briefly the various factors which have led to the gradual deterioration of agricultural production. Up to the end of the 1950s, its dynamism (5.8 per cent annually) was associated with the combined stimulus of exports and of the support provided by the public sector in the form of financial resources and, in particular, irrigation works. As from the 1960s, however, public investment–especially in irrigation projects–declined (see table 229).

Since the end of the 1960s, the full magnitude of the gradual deterioration of agriculture has been apparent. Since investment in agricultural infrastructure was not sufficiently dynamic, the expansion of production took place on dry farm land, where a heavy dependence on natural phenomena is combined with far less organizational and entrepreneurial capacity than that found in irrigation agriculture. In addition, the domestic agricultural price policy became increasingly complex and onerous and, worse still, failed to take duly into account the competition between land used for crops destined for export and for the domestic market. When the prices of export crops dropped, this policy was successful in that the domestic supply of agricultural products increased; but when export prices were favourable–which occurred in some years of the present decade–the magnitude of the resources required to orient sowings and part of the export crops towards the domestic market rendered it inoperative.

In 1974, for the third consecutive year, the performance of agriculture was unsatisfactory, since it grew at very low rates. In addition to the above-mentioned causes, this was due to natural factors which affected the products for domestic consumption. On the other hand, the higher international prices once again stimulated production for the external market.

Thus, export agriculture increased by 4.7 per cent, compared with a drop of 2.8 per cent in 1973, while the increase in production for domestic consumption was much smaller.

The favourable evolution of production for the external market was basically due to the bigger output of cotton, strawberries and tomatoes; the coffee crop, on the other hand, declined slightly. As regards cotton–Mexico's main export crop–sowings increased considerably and production rose by about 20 per cent (from 366,000 to 438,000 tons in 1974). The slight decline in coffee production, from 200,000 to 192,000 tons, was due to a reduction in cultivated area as a result of Mexico's undertaking to hold back 10 per cent of the crop.

Maize contributed a good deal to the stagnation of agricultural products for domestic consumption, with a decrease of about 15 per cent in the amount harvested. In spite of the authorities' efforts to increase maize output–in particular by raising the support prices[41]–large areas were

[41] In 1973 they were raised from 900 to 1,200 pesos per ton, and by April 1974 to 1,500 pesos.

Table 229. Mexico: area irrigated by means of federal government water projects

Year	*Hectares*	*Annual growth rate (percentages)*
1946	827,425	
1952	1,452,937	9.8
1958	2,211,037	7.3
1964	2,455,895	1.8
1970	2,849,100	2.5
1972[a]	3,028,590	3.1

SOURCE: Nacional Financiera, S.A., *La economía mexicana en cifras*, Mexico, 1974.
[a] Preliminary figures.

affected by natural phenomena (droughts, floods and frosts),[42] so that about 1,115,000 tons had to be imported to satisfy domestic demand. The production of beans, another of the population's staple food items, rose by only 3.1 per cent owing to the adverse effect of those natural phenomena.

The government programmes and higher support prices were the basic factors underlying the increase of about 40 per cent in wheat production.[43] This increase was due not only to the expansion of the area sown (from 602,000 to 777,000 hectares), but also to the high average yields, which reached 3,600 kilogrammes per hectare (an increase of 20 per cent). Even so, 823,000 tons had to be imported to meet domestic demand.

As regards raw materials for the manufacture of oils, the production of safflower and soya was affected (with decreases of 2 and 28 per cent, respectively) by the expansion of land sown to cotton, while output of sesame remained at the same level. This contraction was partly offset by the larger production of cottonseed, which increased from 650,000 to 800,000 tons.

[42] Approximately 1 million tons were lost owing to the late frosts alone.

[43] The support price was raised from 1,200 to 1,500 pesos in April 1974.

(b) *Mining*

The higher international prices, the greater demand for intermediate products and the development policy designed to promote production increased the supply of mining products which, without considering petroleum and natural gas output, grew at a rate of about 10 per cent, i.e., faster than 1973. Except in the case of precious metals, mining in general grew at an accelerated pace. Output of metals increased far above the levels reached in 1973, and non-metallic minerals pursued their rising trend although not quite so intensively (see table 230).

The production of mercury grew at the fastest rate (204 per cent), followed by output of tin (103 per cent), sulphur (49 per cent), coal (29 per cent), lead (27 per cent), iron (21 per cent), bismuth (15 per cent) and manganese (14 per cent). The external demand for zinc and lead was reflected in a rise in international prices which stimulated exports; together, exports of both these metals amounted to 71 million dollars, representing an increase of 77 per cent over 1973.

The development policy for mining activities resulted in an increase in the proportion of refined products in total exports of metals. In the case of zinc, the entry into operation of the Met-Mex Peñoles plant, with a capacity of 105,000 tons

Table 230. Mexico: variation in mining output
(*Metal content*)

	Growth rate (percentages)			
	1971	*1972*	*1973*	*1974*[a]
Precious metals	−15.3	1.9	2.5	0.1
Gold	−23.9	−3.2	−9.2	−3.3
Silver	−14.4	2.2	3.4	0.3
Non-ferrous metals for industry	−3.9	7.3	0.1	11.8
Zinc	−0.5	2.5	4.5	5.6
Lead	−11.2	2.9	11.1	27.4
Copper	3.5	24.6	2.2	6.7
Antimony	−24.8	−11.4	−19.8	0.6
Cadmium	−15.5	5.7	−15.9	1.5
Mercury	17.0	−36.4	−74.6	204.2
Bismuth	−0.2	10.4	−7.0	14.6
Tin	−10.1	−26.1	−17.5	102.7
Metals and mineral products for the steel industry	5.4	8.3	5.9	19.4
Coal	−11.0	−14.5	2.8	28.6
Iron	7.9	8.3	2.0	20.6
Manganese	−2.6	10.8	23.2	14.1
Non-metallic mineral products	−1.2	−14.4	32.5	28.2
Sulphur	−14.7	−19.8	70.3	49.2
Fluorite	20.7	−11.8	4.2	2.6
Barite	−12.3	−6.6	−2.3	1.8
Graphite	−8.5	8.2	18.7	−3.9

SOURCE: ECLA, on the basis of official statistics.
[a] Estimates.

annually, helped to increase the share of refined zinc in external sales from 6 per cent in 1973 to 22 per cent in 1974.

The proportion of refined lead exported rose from 87 to 95 per cent. The expansion of the production of copper and of metals and minerals used in the steel industry (11.9 per cent) was linked with the growth of domestic demand. Another factor in the case of the latter products was the increase in the ceiling price of coal (from 325 to 580 pesos per ton) which did much to encourage its production. Lastly, the supply of sulphur responded to the incentive of greater domestic demand and the rise in external prices deriving from the requirements for the production of fertilizers.

(c) *Petroleum and petrochemical products*

The petroleum industry showed a dynamic trend in 1974, with production increases of 19.3 per cent for crude and 15.4 per cent for refining. These compare very favourably with the rates of 3.1 and –0.2 per cent recorded in 1973 (see table 231). Two factors had a significant influence on these trends: the increase in the prices to the public put into effect on 8 December 1973 and the development of new producing areas in south-east Mexico.

In the first case, Petróleos Mexicanos (PEMEX) was able to increase its financial resources and thus facilitate the implementation of investment programmes without incurring loans. In the second case–although the oil reserves of Tabasco and Chiapas have not yet been accurately quantified–conservative estimates indicate that these explorations have raised the country's reserves by 11 per cent, to a total of 3,150 million barrels. The increase in production has strengthened Mexico's external position, converting it into a crude exporter in 1974. However, the value of external purchases of petroleum and petroleum products was far above that of exports, since in the early months of the year it was still necessary to import crude and, in addition, some purchases of petroleum products were made because of the shortage of production capacity. Imports of petroleum and petroleum products rose from 2,370 million pesos in 1973 to 3,671 million in 1974 (figures for January to October), while exports increased from 229 to 789 million.

In 1974, the petrochemical sector grew at a rate of 13.7 per cent, or slightly faster than in 1973 (12 per cent). The increases were basically in the production of vinyl, dichloro-ethane and para-xylene, as a result of the expansion of the existing installed capacity under the investment programme in course of execution. It is hoped that once PEMEX consolidates its financial position this programme will be expedited and Mexico will become self-sufficient in basic petrochemical products within the medium term.

(d) *Manufacturing*

Manufacturing grew at a rate of 5.6 per cent in 1974, compared with average rates of over 8 per cent in the years 1972–1973. The performance of the various sectors differed widely, since the industries processing paper and paper products, printing and publishing industries, and industries producing transport equipment grew more rapidly than in

Table 231. Mexico: variation in output of petroleum and petroleum products

	Growth rate (percentages)			
	1971	*1972*	*1973*	*1974*[a]
Crude petroleum (extraction)	–1.3	3.3	3.1	19.3
Refining[b]	2.2	11.0	–0.2	15.4
Natural gas	–3.5	2.8	2.5	11.9
Propane and Pemex gases	3.3	15.2	9.3	11.5
Mexolina	–3.3	–3.8	–10.7	26.7
Supermexolina	5.9	0.5	13.0	...
Gasolmex	–2.8	25.4	–5.5	...
Pemex gasoline 100 octane	14.3	–16.4	0.5	...
Avgas	6.4	–27.7	–31.7	–31.7
"Diáfano" and colourless petroleum	2.7	1.4	–2.5	19.9
Turbosina	5.7	13.9	19.6	52.1
Tractomex	–2.9	4.2	26.4	17.3
Diesel oil	2.1	12.6	9.2	31.0
Fuel oils and residues	–3.6	14.0	–0.6	36.3

SOURCE: Banco de México, S.A.
[a] Estimates.
[b] Input of processed crude and liquids.

Table 232. Mexico: variation in value added in manufacturing

	Growth rate (percentages)			
	1971	*1972*	*1973*	*1974*
Manufacturing	3.2	8.5	8.8	5.6
Food, beverages and tobacco	1.0	5.5	5.0	4.4
Textiles	5.4	8.2	7.5	−2.8
Footwear and clothing	7.6	8.4	8.3	1.2
Wood and cork products	−5.2	7.2	8.0	−8.2
Paper and paper products	−7.1	5.6	9.5	13.0
Printing and publishing	−1.1	13.1	0.5	13.7
Rubber products	11.0	10.9	10.2	−8.6
Chemical products and plastic material	10.1	14.0	10.2	6.1
Non-metallic mineral products	8.6	11.5	15.5	5.5
Basic metal industries	2.7	12.4	8.1	6.7
Machinery	0.1	6.8	10.7	8.1
Transport equipment	6.6	9.9	18.2	25.1
Other industries[a]	−6.5	4.5	9.1	9.8

SOURCE: ECLA, on the basis of official statistics.
[a] Including leather and leather products and metal products.

1973, while the industries producing textiles, rubber products, wood and cork declined. The rest of the manufacturing activities grew at lower rates than the previous year (see table 232).

The evolution of this sector was influenced by the shortage and high prices not only of domestic raw materials—owing to the saturation of installed production capacity—but also, to a lesser degree, of those purchased abroad. On the other hand, the uneven trend of demand stimulated some branches of activity and weakened others. Factors such as increases in costs and the higher cost of credit basically affected the small and medium-scale enterprises, although the first factor also affected industries subject to price controls.

The limited installed capacity of the steel and petrochemical industries resulted in insufficient output, which adversely affected the branches of industry which they supply. This occurred in the case of industries producing fertilizers,[44] chemical fibres, detergents, metal manufactures and construction items[45] (see table 233). Installed capacity for the production of aluminium and

[44] The production of fertilizers grew at a rate of 2.6 per cent in 1974 and dropped by 2.7 per cent in 1973, in contrast with a growth of over 14 per cent in the two years 1971–1972. This deceleration gave rise to a shortage, which should be covered in 1976.
[45] Construction activity was also affected by the deceleration of total investment.

Table 233. Mexico: variation in manufacturing production index

	Growth rate (percentages)			
	1971	*1972*	*1973*	*1974*[a]
Sugar plants and refineries	2.8	5.1	6.9	2.6
Beer	−12.8	17.4	17.1	15.8
Refreshments and non-alcoholic beverages	−13.8	10.0	11.4	−3.3
Cigarettes and cigars	−0.6	5.4	−9.4	12.0
Artificial yarns and fabrics	27.8	25.1	27.2	1.0
Tyres and inner tubes	10.5	12.3	5.3	0.5
Fertilizers	13.6	15.2	−2.7	2.6
Basic chemical products	8.4	5.3	11.8	11.4
Artificial fibre	25.5	21.9	19.5	8.2
Cement	2.6	16.8	13.8	7.8
Motor cars	12.0	2.8	21.9	24.4
Lorries	2.3	17.6	25.5	24.5
Oils and fats[a]	3.0	9.5	1.0	−3.7

SOURCE: Banco de México, S.A., *Indicadores económicos,* November 1974.
Note: These indicators represent 23.5 per cent of the total value of manufacturing production in 1970.
[a] Estimates.

electrolytic copper products was also insufficient, resulting in bigger imports of the former and the elimination of exports of the latter.[46]

The insufficient increase in the supply of agricultural inputs was responsible for a 3.7 per cent drop in the production of oils and fats. Sugar output increased by about 3 per cent, or less than half the 1973 rate. Moreover, the weaker demand basically affected the production of natural fibre textiles and footwear and clothing, the output of which fell below the normal levels reached in previous periods.

The industries which continued to grow at a vigorous pace were those producing transport equipment, paper and paper products, and printing and publishing industries. The bigger expansion of the transport equipment industry (25 per cent in 1974 as against 22 per cent in 1973) was largely due to the increase in expenditure on durable consumer goods.[47] Output of paper and paper products rose by 9.5 per cent in 1973 and 13 per cent in 1974, owing to the greater activity of the printing and publishing sector, the need to increase stocks and the import substitution process.

(e) *Construction*

The gross domestic product generated by construction activities reflected an unsatisfactory real growth in 1974 (6.3 per cent) compared with the rates in 1972 (17.6 per cent) and 1973 (14.8 per cent). This trend was due to factors which are only too well known in Latin America.

In the first place, the prices of completed dwellings, like those of construction materials, have increased considerably and, as from October 1974, so also have wages and salaries paid by this industry. Therefore, fewer people are in a position to purchase these dwellings. Added to this are the greater financing difficulties, since the system of compulsory cash reserves was extended to the housing financing sector during the year, thereby making the credit it provides more expensive and reducing the resources available for loans. INFONAVIT was therefore the principal agency promoting housing in 1974.

Secondly, the rest of the public sector's construction activity was affected by the reduction (in real terms) of central government capital expenditure. Although the public works in process of execution were continued, a smaller number seem to have been initiated during the year.

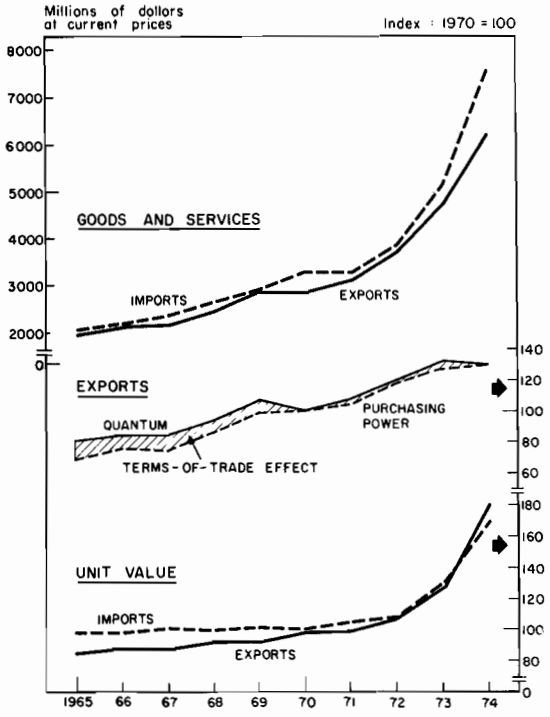
Lastly, the production of cement and steel reached a limit which did not allow construction to expand more rapidly in 1974. Although the necessary investments are being made to eliminate this restriction, it may continue to have considerable influence in the immediate future.

3. Balance of payments

The deficit on current account continued to increase appreciably, in 1974 reaching about 2,400 million SDR units, or practically double the 1973 figure. On the other hand, net capital inflows again exceeded the previous balance, once again permitting an increase in international reserves (see table 234 and figure XXXVII).

Exports of goods rose by 3.2 per cent in real terms and 41 per cent in unit value. According to available data for the period January-October, sales of agricultural commodities–both primary and processed–rose to 718 million dollars (from 611 million over the same period in 1973), partly owing to deficiencies in domestic production and weaker demand in the second half of the year. In terms of current prices, the export value of primary agricultural commodities dropped 2.9 per cent, while that of processed products rose 23 per cent (see table 235).

Figure XXXVII. Mexico: trend of external variables
Natural scale



[46] They were sold only in the form of impure bars.

[47] This is a typical trend in periods of inflation. When the real rate of interest drops, the non-entrepreneurial private sector increases its purchases of real assets which tend to keep their value.

Table 234. Mexico: balance of payments
(*Millions of SDR units*)

	1970	1971	1972	1973	1974[a]
Current account					
Exports of goods and services	2,868.0	3,106.0	3,441.0	3,918.5	5,167.6
Goods FOB	1,429.0	1,512.0	1,733.0	2,044.2	2,976.7
Services	1,439.0	1,594.0	1,708.0	1,874.3	2,190.9
Transport	47.0	61.0	73.0	71.3	87.3
Travel	1,171.0	1,317.0	1,375.0	1,468.9	1,746.1
Imports of goods and services	3,296.0	3,263.0	3,549.0	4,276.5	6,352.5
Goods FOB	2,259.0	2,181.0	2,407.0	3,109.4	4,916.5
Services	1,037.0	1,082.0	1,142.0	1,167.1	1,436.0
Transport	156.0	155.0	170.0	198.9	296.8
Travel	755.0	785.0	801.0	790.0	931.3
Net external investment income	−695.0	−738.0	−790.0	−954.2	−1,263.9
Profits	−480.0	−494.0	−546.0	−630.0	−789.9
Interest	−215.0	−244.0	−244.0	−324.2	−474.0
Net private transfer payments	48.0	50.0	50.0	53.1	62.4
Balance on current account	−1,075.0	−845.0	−848.0	−1,259.1	−2,386.4
Capital account					
Net external financing ($a + b + c + d + e$)	1,075.0	845.0	848.0	1,259.1	2,386.4
(a) Net external non-compensatory capital	769.0	810.0	1,115.0	1,769.0	
Direct investment	323.0	307.0	277.0	309.0	
Long- and medium-term loans	893.0	978.0	1,113.0	1,863.0	
Amortization payments	−573.0	−515.0	−561.0	−563.0	2,533.4
Short-term liabilities	119.0	33.0	277.0	153.0	
Official transfer payments	7.0	7.0	9.0	7.0	
(b) Domestic non-compensatory capital or assets	−89.0	−55.0	−252.0	−422.0	
(c) Errors and omissions	425.0	232.0	149.0	−35.9	
(d) Allocation of SDRs	45.0	40.0	39.0	–	–
(e) Net compensatory financing (increase −)	−75.0	−182.0	−203.0	−52.0	−147.0
Movements of foreign exchange reserves (increase −)	4.0	−171.0	−175.0	−63.0	...
Movements of gold reserves (increase −)	−31.0	29.0	11.0	11.0	...
SDRs (increase −)	−48.0	−40.0	−39.0	–	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26. [a] Estimates based on official statistics.

Table 235. Mexico: composition of exports of goods
(*January–October*)

	Millions of dollars		*Percentages*		*Increase*
	1973	*1974*	*1973*	*1974*	*1974*
Declared exports	1,441.3	2,128.8	100.0	100.0	47.7
Agricultural sector	610.5	717.8	42.4	33.7	17.6
Primary agricultural products	118.6	115.2	8.2	5.4	−2.9
Processed agricultural products	491.9	602.6	34.2	28.3	22.5
Extractive industries	75.3	123.8	5.2	5.8	64.4
Processing industries	715.2	1,220.4	49.6	57.3	70.6
Products not elsewhere classified	40.3	66.8	2.8	3.2	65.8

SOURCES: Ministry of Industry and Trade, and Statistics Department.

In the case of the extractive industries, production increases and higher world prices combined to raise the value of exports from 75 million to 124 million dollars between the first 10 months of 1973 and the same period in 1974. There was a total increase of 27 per cent in volume, consisting mainly of non-metallic minerals (38 per cent) and non-ferrous metals (20 per cent).

The Government's economic policy designed to step up exports of manufactures, together with the improved conditions for processed metals, permitted an increase of about 71 per cent in sales by the

engineering industries, which reached 1,220 million dollars in the period January-October 1974 (see table 235).

The increase in imports from 3,751 million dollars in 1973 to 5,913 million in 1974 was due to the need to maintain stocks of some materials above the normal levels in view of their relative scarcity in the world markets, and to the poor agricultural output, which made it necessary to increase imports of basic grains. In addition, there were bottlenecks in the production capacity of certain key branches of industry.

The deterioration in domestic agricultural production was reflected in the increased share of consumer goods in total imports (from 10.6 to 11.6 per cent, accumulated figures up to October). This increase was due to the more accelerated growth of imports of non-durable consumer goods[48] in terms of both volume and value (owing to the significant rise in their prices), since imports of durable goods remained at practically the same level.[49]

On the other hand, imports of basic inputs rose by 75 per cent in value at current prices (see table 236), increasing their share of the total from 44 to 49 per cent as a result of the rise in world prices, and possibly also because of buying ahead to forestall a future world shortage. There were bigger imports of oilseeds, paper, plastic materials and products for the steelmaking industry. In certain cases imports might have been even higher (scrap iron and petrochemical products) had it not been for the shortage on the world markets.

[48] Cereals and condensed, evaporated and powdered milk among other products.

[49] Their share dropped from 2.8 to 1.8 per cent, since they grew by only 3 per cent.

Lastly, apart from durable consumer goods, imports of capital goods constituted the component that showed the lowest rate of growth (27 per cent) owing to the fewer resources devoted to increasing capital assets.

The effort made by the public sector to maintain the levels of total demand is evident in the greater acceleration of its external purchases compared with those made by private enterprise. According to available data up to November, government activity absorbed about 43 per cent of the total increase in imports. Thus its share in total imports rose from 29 to 34 per cent between 1973 and 1974.

In the current account, factor payments continued to contribute, although in a somewhat lesser degree, to the increasing external disequilibrium. The high level of external indebtedness pushed up these payments to 1,264 million SDR units, which represents an increase of 33 per cent over 1973. In particular, interest payments on official debts rose 46 per cent, as a result of the high levels of public indebtedness (see table 234).

In tourism, which has always contributed greatly towards stabilizing the current account, net income rose to 815 million SDR units. Expenditure grew at much the same rate as income, although the number of tourists, which had increased 10 per cent in 1973, went up by only 4 per cent in 1974. In order to arrest this trend, the Government adopted measures designed to enlarge and improve the tourist infrastructure, increase the funds for its development and establish closer co-ordination between the relevant institutions.

Under the head of border transactions, the foreign exchange obtained rose at the same rate as the year before (approximately 15 per cent).

The capital account reflected the main economic development and trends. Direct external

Table 236. Mexico: composition of imports of goods
(January-October)

	Millions of dollars		*Percentages*		*Increase 1974*
	1973	*1974*	*1973*	*1974*	
Total[a]	*3,029.0*	*4,829.8*	*100.0*	*100.0*	*59.5*
Consumer goods	321.3	557.8	10.6	11.6	73.6
Non-durable	240.0	473.8	7.9	9.8	97.4
Durable	81.3	84.0	2.7	1.8	3.3
Producer goods	2,422.8	3,721.1	80.0	77.0	53.6
Non-durable (raw materials)	1,343.3	2,354.2	44.3	48.7	75.3
Durable (investment goods)	1,079.5	1,366.9	35.7	28.3	26.6
Products not elsewhere classified	284.9	550.9	9.4	11.4	93.4
Maquila	265.4	382.8	–	–	44.2

SOURCES: Ministry of Industry and Trade, and Statistics Department.
[a] Excluding export industries using imported inputs (*maquila*).

investment (according to data for January to September) remained at lower levels than in 1973 in line with the slower rate of private investment. On the other hand, net external credit to the private sector very probably increased so as to alleviate the liquidity problem it had to face during the year. External credit obtained by the public sector also increased, reaching a total of 1,146 million SDR units compared with 675 million in 1973. The large proportion of external resources obtained by the public sector is evident from the fact that by September 1974 the amount received in 1973 had already been exceeded.

4. PRICES AND WAGES AND SALARIES

The accelerated increase in prices continued in 1974 for the second consecutive year. The consumer price index at the national level rose by 12.2 per cent in 1973 and 24.2 per cent in 1974. Other indexes also reflect this trend.

A fact of prime significance is that, of the three major lines of consumption which in developing countries usually absorb two thirds to four fifths of the expenditure of the lower-income sectors, two registered increases well above the average. The index for food, beverages and tobacco rose 30.6 per cent in 1974; the cost of transport and communications, another indispensable item of consumption, increased by 37.8 per cent; while the index for the third group–articles of clothing–rose by less than the average, i.e., 17.9 per cent (see table 237).

The rise in food prices would have been even greater had it not been for the subsidies accorded by the central government for the main food items. The items which most seriously affect the Mexican family budget are cereals, e.g., maize and wheat. They are both produced locally, but, as explained in the section on agriculture, large amounts had to be imported in 1974. Sales of these imports, as in the case of production, were subsidized. The subsidies partly account for the 40 per cent increase in payments under the head of current transfers effected by the central government between January-September 1973 and the same period in 1974.[50] Even so, at the level of the consumer their prices rose considerably.

Table 237. Mexico: variation in consumer price index
(Percentages)

	1973	*1974*[a]
Total	*12.2*	*24.2*
Food, beverages and tobacco	15.8	30.6
Clothing	17.1	17.9
Transport and communications	5.7	37.8
Furniture and household goods	11.3	22.2
Health	7.7	13.0
Education and entertainment	8.5	19.6
Other goods and services	9.1	16.7

SOURCE: Banco de México, S.A., *Indicadores económicos*, vol. III, No. II, 1974.

[a] Annual estimate on the basis of 11 months.

The impact of the above-mentioned increases on the family budget has been fairly severe. In view of the tradition of price stability in the Mexican economy, the normal practice was to review the general wage and salary contracts every two years. In 1974 the situation changed, and since then they have been reviewed annually.

Precisely in September of that year a general increase in wages and salaries was granted. Those below 5,000 pesos (400 dollars) a month were raised 22 per cent, and those over that sum were adjusted by a fixed amount of 1,100 pesos (88 dollars), which represents a diminishing adjustment as the wage scale rises.

In addition to this adjustment, the Government established the National Consumer Fund for Workers (Fondo Nacional del Consumo para los Trabajadores–FONACOT) which is used to guarantee bank credit extended to wage-earners for purchases of consumer goods.

5. PUBLIC FINANCE

In 1974, the objectives of the central government expenditure policy changed radically. An austerity policy had been adopted in 1973, since its aim was to contain inflationary pressures that had existed in the economy since the beginning of the year and which made themselves felt intensively in the last three months. This position gradually lost ground in 1974 and, by the middle of the year, had been replaced by more decisive action designed to support and strengthen the country's economic and social development.

This change was necessary, not only to compensate for the slower growth of private investment and demand, but also to raise the fiscal workers' nominal wages in a similar proportion to the loss of purchasing power they had sustained. While the measures adopted in the first case affected public expenditure during the whole of 1974, the latter measure did so mainly in the last quarter, the increase having been granted in September.

Total central government expenditure underwent a sharp increase, reaching a figure estimated

[50] As noted in the country studies included in this *Survey*, the situation described here is found practically throughout Latin America.

Table 238. Mexico: actual federal government expenditure and income[a]
(Thousands of millions of pesos)

	1970	1971	1972	1973	1974[b]
Current account					
Expenditure	25.2	28.2	36.9	47.0	65.9
Income	33.0	35.7	41.7	51.3	65.7
Saving	7.8	7.2	4.8	4.3	–0.2
Capital account					
Expenditure	12.3	10.0	17.7	21.0	24.0
Income	0.8	0.8	0.7	0.8	0.8
Deficit	11.5	9.2	17.0	20.2	23.2
Global account					
Expenditure[c]	40.2	41.3	59.1	75.8	99.9
Income	33.9	36.5	42.3	52.1	66.5
Deficit	6.3	4.8	16.8	23.7	33.4

SOURCE: ECLA, on the basis of data supplied by the Banco de México, S.A.
[a] In a consolidated balance sheet for the public sector, total government expenditure amounts to between 40 and 50 per cent of the total.
[b] Estimate on the basis of nine months.
[c] Including expenditure in respect of indebtedness in previous financial periods.

at 99,900 million pesos. In relation to 1973, this represents a rise of 31.8 per cent, which, although higher than that recorded in 1973, is still below the 1972 increase of 43 per cent (see table 238).

A major factor contributing to the above increase was the rise in the level of current expenditure, which totalled 65,900 million pesos in 1974. Nearly half of this amount (31,000 million) was absorbed by administration expenditure, which rose as a result not only of the higher prices of goods purchased by the central government, but also of the wage and salary adjustments in September. Current transfer expenditure amounted to 25,000 million pesos, which includes the higher subsidies accorded for mass consumption food items. Lastly, the increase in the domestic debt was reflected in a 37.1 per cent increment in the payment of interest and commissions, which totalled 9,500 million pesos in 1974.

Available data up to September 1974 show only a slight increase in capital expenditure. Estimates for the year would seem to indicate that it rose from 21,000 million pesos in 1973 to 24,000 million in 1974. This variation (14.2 per cent) is less than the 24.2 per cent increase in consumer prices.

Income showed less dynamism than expenditure. Although tax reform and inflation in 1974 had the effect of pushing up its various components, there were factors which acted in the opposite sense. These include the relatively slow growth of sales of consumer goods (except motor cars), the increase in the proportion of duty-free imports in total purchases, and the decline in export prices in the second half of the year. These factors caused income to rise by only 27.8 per cent in 1974 to a total of 66,500 million pesos. In view of the variations in the nominal gross domestic product, it is probable that the tax burden may have decreased during the year.

The tax reform led to a sharp rise in revenue under the head of income tax, i.e., 36.7 per cent over the rise in prices. For the first time in the present decade, it represented over half of total income. i.e., 35,000 million pesos. Other components of income showed smaller variations.

In view of the performance of fiscal income and expenditure in 1974, the saving on current account in previous years was swallowed up and, according to provisional data, there was a small deficit of approximately 200 million pesos. Although net capital expenditure was very restricted, it nevertheless totalled 23,200 million pesos, resulting in an over-all deficit of 33,400 million pesos or the equivalent of 50 per cent of total income.

Already in 1973, the financing of this deficit had repercussions on the distribution of credit available in the domestic financing system. The institutions of this system grouped in the banking system increased their credit to the private sector by 8.2 per cent in 1973 and by 14.7 per cent in the 12 months ending in September of the same year. The increases in credit to the general government were 32.5 and 32.8 per cent, respectively. In the 12 months ending in September 1974, the amount received by the private sector rose by 13.7 per cent, and that received by the general government by 12 per cent (see table 239).

Table 239. Mexico: allocation of credit granted by the banking system[a]

	Millions of pesos balance at December		Growth rate				
			December			September	
	1970	1973	1971	1972	1973	1973	1974
Total	*130,100.2*	*192.496.0*	*18.4*	*12.6*	*11.0*	*16.6*	*13.5*
Private enterprises	117,013.0	166,680.2	18.9	10.6	8.2	14.7	13.7
Agriculture, mining, forestry and fishing	18,819.4	28,146.3	20.2	10.1	13.0	11.5	24.9
Crop farming and stock raising	17,710.3	26,165.7	20.1	10.7	11.2	9.8	23.7
Mining	793.3	1,166.8	22.1	−11.5	36.1	18.9	26.2
Other	315.8	813.8	21.7	31.8	60.6	87.2	62.5
Energy	9,913.5	17,760.2	39.1	29.5	−0.6	12.4	−11.0
Petroleum	2,157.3	5,358.5	93.6	44.9	−11.4	−2.5	−16.4
Electric energy	7,756.2	12,401.7	24.0	22.8	5.0	20.8	−8.5
Industries	44,944.9	60,870.4	15.3	9.7	7.1	15.3	20.1
Processing industries	33,267.0	42,602.7	15.7	3.9	6.6	12.9	23.4
Manufactured products	23,151.1	31,348.6	16.5	9.3	6.4	16.2	23.1
Manufacture of non-metallic mineral products	2,579.7	2,125.8	−6.9	−2.1	−9.5	−4.9	4.1
Steelmaking and metal products	5,305.1	5,989.3	15.0	−10.4	9.5	−2.8	32.0
Manufacture and repair of machinery and electrical appliances	2,231.1	3,139.0	35.0	−10.8	16.8	28.7	25.5
Construction industry	11,677.9	18,267.7	14.2	26.5	8.2	20.9	12.9
Services and other activities	22,994.7	32,042.4	11.4	5.1	19.0	20.4	8.5
Services[b]	5,484.1	7,654.1	27.5	−4.8	15.1	26.5	3.8
Transport	5,428.7	7,892.3	15.2	7.2	17.7	22.2	16.4
Communications	17.8	58.2	201.1	5.0	3.4	9.4	27.4
Film and other industries	1,068.6	1,501.0	14.8	15.0	6.4	7.2	26.0
Housing programmes	3,680.1	5,772.9	19.1	10.4	19.3	21.4	10.9
Other activities	7,315.4	9,164.9	−8.2	8.2	26.1	14.8	0.5
Commerce	20,340.5	27,859.9	24.4	8.4	1.6	12.1	11.6
Government[c]	13,087.2	25,815.8	13.3	31.5	32.5	32.8	12.0
Federal	10,359.0	20,491.8	9.5	27.0	42.2	35.9	13.2
State and municipal	2,728.2	5,324.0	27.5	46.0	4.8	22.9	7.6

SOURCE: Banco de México, S.A., *Indicadores económicos*.

[a] In addition to national and private institutions, the suppliers of credit are considered to include credit unions, bonded warehouses and trust funds of the Federal Government. The credit includes that extended by trust departments (on behalf of bailors), and credit from common funds of share certificates in Nacional Financiera S.A. The Banco de México, S.A. is not considered as a direct supplier of credit.

[b] Excluding credit between subsidiary institutions and organizations of the Mexican banking system.

[c] This figure does not coincide with that in the annual report, since the latter does not include portfolio transferred by endorsement, or credit extended on behalf of bailors.

In 1973, the high rates of expansion of credit to the general government were made possible by the banking system's rapid tapping of resources, which increased 17.1 per cent during the year. Another factor was the raising of the level of compulsory cash reserves. The drop in these rates in 1974 is accounted for by the smaller proportion of domestic financial resources tapped, and the fact that during the early months of the year the aforementioned austerity public expenditure policy was maintained.

NICARAGUA

1. OVER-ALL ECONOMIC TRENDS

The process of reconstruction consequent upon the damage done by the earthquake at the end of 1972 was in full swing during 1974, both at the public and at the private level, and largely determined the rate of expansion of economic activity in that year.

The growth rate of 7.7 per cent attained by the gross domestic product represented a marked

Table 240. Nicaragua: total supply and demand

	Millions of córdobas at 1970 prices			Structure (percentages)		Annual growth rate (percentages)		
	1970	1973	1974[a]	1970	1974[a]	1970-1972	1973	1974[a]
Total supply	*7,499.4*	*8,808.7*	*9,728.8*	*126.8*	*135.9*	*4.2*	*8.1*	*10.4*
Imports[b]	1,586.9	2,159.5	2,567.6	26.8	35.9	1.6	31.8	18.9
Gross domestic product	5,912.5	6,649.2	7,161.2	100.0	100.0	4.9	2.2	7.7
Total demand	*7,499.4*	*8,808.7*	*9,728.8*	*126.8*	*135.9*	*4.2*	*8.1*	*10.4*
Exports[b]	1,453.2	1,959.0	1,838.8	24.6	25.7	10.6	10.2	-6.1
Domestic demand	6,046.2	6,849.7	7,890.0	102.2	107.6	2.6	7.6	12.5
Gross domestic investment	1,025.1	...	...	17.3	23.4	-11.8	...	...
Gross fixed investment	895.0	1,075.1	1,412.7	15.1	19.7	-4.3	31.1	31.4
Public	230.0	321.8	413.3	3.9	5.8	13.3	9.0	28.4
Private	665.0	753.3	999.4	11.2	13.9	-11.2	43.5	32.7
Construction	358.4	...	...	6.1	...	...	...	...
Machinery and equipment	536.6	...	...	9.0	...	...	...	...
Total consumption	5,021.1	5,708.9	6,216.6	84.9	86.8	5.3	2.5	8.9
General government	496.8	521.0	580.9	8.4	8.1	1.1	2.6	11.5
Private	4,524.3	5,187.9	5,635.7	76.5	78.7	5.8	2.5	8.6

SOURCES: 1970-1972: ECLA calculations based on figures supplied by the Central Bank of Nicaragua; 1973-1974: ECLA estimates based on official data.

Note: The figures for exports and imports of goods and services were taken from balance-of-payments data expressed in dollars at current prices, which were converted to constant 1970 values by deflation, using price indexes calculated by ECLA for the purpose.

[a] Preliminary figures.

[b] Goods and services, excluding factor payments.

recovery in relation to 1973 (2.2 per cent) and a return to the dynamism that has characterized this rate over the long term (see table 240).

Thus, the activities of the public sector were invigorated by the intensification of the work of rehabilitating the disaster area. Public investment increased by about 30 per cent and general government consumption by 11.5 per cent; private investment, in its turn, again recorded a high rate of growth.

These stimuli of demand, supported by a greater inflow of external capital (returns on private reinsurance in 1973 and official external loans in 1974), as well as by the expansion of domestic credit that took place in 1973 and early in 1974, boosted income, employment and private consumption; and this upswing was combined, moreover, with highly favourable trends in certain basic lines of agricultural production and plenty of response on the part of the manufacturing and construction sectors. All these factors prevented the contractionist effects of the fall in the volume of exports of goods and services from affecting total demand, but their influence partly accounted for the increase in the external deficit on current account.

The growth rate of the gross domestic product was determined mainly by agriculture, industrial production and construction, plus the restoration and expansion of the electricity and piped water services and the increase in general government services (see table 241 and figure XXXVIII).

Diverging significantly from the trend followed in the past two years, agriculture expanded by 10 per cent, as a result of auspicious weather conditions, policy measures to support specific lines of production, and, in certain cases, favourable world market prices. In particular, cotton production flourished; not only did yields improve, but in addition the areas under cultivation were enlarged, thanks in part to the elimination of the credit restrictions that had been in force for agricultural enterprises whose yields fell short of a given minimum. Levels of production also rose considerably in the case of some of the staple items of domestic consumption, such as rice and beans (15 per cent and 18 per cent). Apart from the fact that weather conditions were more favourable, these trends reflect greater credit facilities and the establishment of remunerative guaranteed prices, which showed increases of almost 70 per cent for best-quality rice and over 50 per cent for beans.

The same was not true of meat production, which underwent a further contraction, owing to the persistence of the adverse effects on stock farming produced by the severe drought of 1972, and the decline of both prices offered by local industry and world market prices, in the second half of the year.

The growth of industrial activity (at a rate of

Table 241. Nicaragua: gross domestic product at factor cost, by sector of economic activity

	Millions of córdobas at 1970 prices			Structure (percentages)		Annual growth rate (percentages)		
	1970	1973	1974[a]	1970	1974[a]	1970-1972	1973	1974[a]
Agriculture	1,432.5	1,640.2	1,803.5	26.3	27.3	6.1	1.7	10.0
Mining	33.6	37.6	41.2	0.6	0.6	-0.3	12.6	9.6
Manufacturing	954.3	1,084.9	1,175.0	17.5	17.8	5.7	1.8	8.3
Construction	175.1	209.8	276.9	3.2	4.2	6.2	6.2	32.0
Subtotal goods	*2,595.5*	*2,972.5*	*3,296.6*	*47.6*	*49.9*	*5.9*	*2.2*	*10.9*
Electricity, gas and water	121.1	109.7	140.4	2.2	2.1	0.9	-11.0	28.0
Transport and communications	299.2	359.9	379.2	5.5	5.7	6.3	6.4	5.4
Subtotal basic services	*420.3*	*469.6*	*519.6*	*7.7*	*7.9*	*4.8*	*1.8*	*10.6*
Commerce and finance	1,062.7	1,275.5	1,344.2	19.5	20.3	4.9	9.1	5.4
Government	407.4	408.2	438.8	7.5	6.6	-1.2	2.6	7.5
Ownership of dwellings	369.6	287.2	291.2	6.8	4.4	2.6	-26.2	1.4
Miscellaneous services	596.8	688.6	716.5	11.0	10.8	4.8	5.0	4.1
Subtotal other services	*2,436.5*	*2,659.5*	*2,790.7*	*44.7*	*42.2*	*3.6*	*1.8*	*4.9*
Total	*5,452.3*	*6,130.4*	*6,606.9*	*100.0*	*100.0*	*4.9*	*2.2*	*7.7*

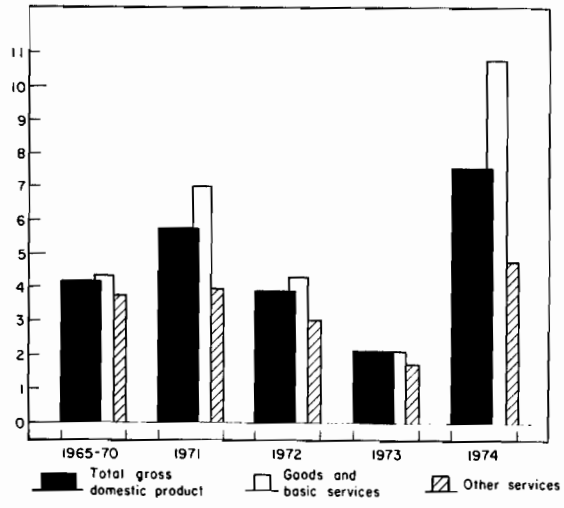
SOURCES: 1970-1971: ECLA calculations based on figures supplied by the Central Bank of Nicaragua; 1972-1974: ECLA estimates based on official data.

Note: As the individual activities and the totals were calculated independently, the sum of the former does not correspond exactly with the latter.

[a] Provisional figures.

8.3 per cent) was especially encouraged by the expansion of local and Central American demand, in particular the former, this dynamic impulse being most marked in the case of textiles and clothing, wood manufactures, plastics, chemical products and construction materials. The meagre increase in private consumption in 1973 was succeeded by a phase of buoyancy in expenditure, resultant upon the restoration of employment and income levels. Furthermore, the secondary effects of the boom in construction activities made themselves felt in the manufacturing sector.

Figure XXXVIII. Nicaragua: growth of gross domestic product
(Annual growth rates)
Natural scale



The stability of the Nicaraguan economy was exposed to powerful adverse pressures during the year, especially as inflation gathered momentum.[51] In the first place, the more rapid rise in prices of imported goods was bound to have profound internal repercussions on an economy as highly dependent upon imports as that of Nicaragua. Influence was also exerted by the increase in the prices of those goods that were produced partly for domestic consumption as well as for exports, and, in addition, by other internal factors deriving from the very process of physical reconstruction, started in 1973 and strengthened in 1974. This brought to the fore, in certain branches of production, inelasticities and bottlenecks which will be difficult to eliminate over the short term.

Various factors acting in opposite directions make their appearance on the future economic scene. On the one hand, it is estimated that the dynamic impulses generated by the rehabilitation of the areas affected by the earthquake will con-

[51] An indication that prices rose faster than in the preceding year is given by a comparison of the increment in revenue from indirect taxation in 1974 (51.3 per cent) with the increase noted in 1973 (20.6 per cent), the emergency export tax being excluded in both cases. In view of their magnitude, these variations can hardly be attributed to the larger real volume of transactions actually conducted in 1974. Nor were the adjustments of tax rates sufficient to account for the difference observable.

tinue to operate, as well as, in general, those stemming from the investment contemplated in the national development plan. These positive factors, however, are offset by the uncertain or unpromising outlook for the principal export products, which might continue to aggravate the country's precarious external payments situtation, and also by the prospects deriving from the intensification of inflationary pressures.

2. Foreign trade and the balance of payments

In 1974 the balance-of-payments deficit on current account increased considerably, rising from 34 million SDR units in 1973 to almost 190 million (see table 242). As in the preceding year, the traditional disequilibrium on the services account was combined with an imbalance on the merchandise account, this time 116 million SDR units—almost four times as large as in 1973—while the inflow of transfer payments, which had amounted to a substantial sum in 1973, returned to its normal level during 1974.

Thus, in the past two years, the increase in the value of imports of goods at current prices (58 per cent in the earlier period and 67 per cent in 1974) was much bigger than the rise in the value of exports, and became the decisive factor in the aggravation of the deficit on current transactions (see figure XXXIX).

The noteworthy increase in imports of goods in 1974 is explained not only by certain inelasticities deriving from Nicaragua's structure of production—highly dependent upon inputs and capital goods from foreign sources, and receiving a special stimulus from the role played by public expenditure, in the existing circumstances, as a basic

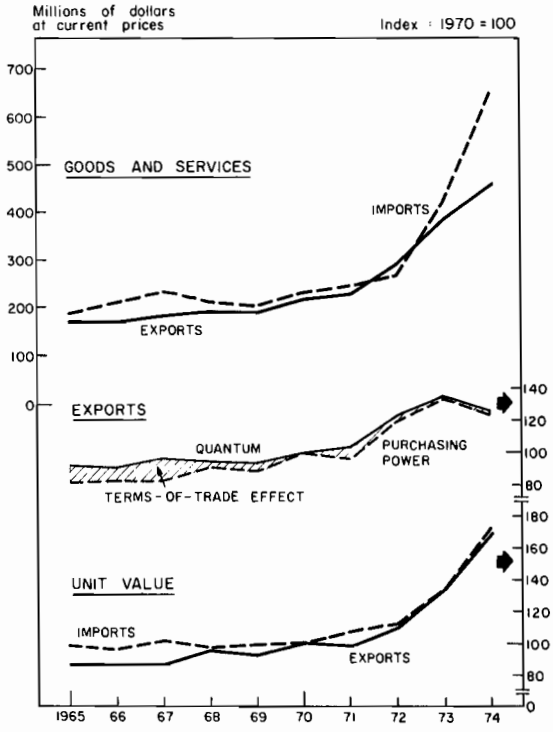
Table 242. Nicaragua: balance of payments
(Millions of SDR units)

	1970	*1971*	*1972*	*1973*	*1974*[a]
Current account					
Exports of goods and services	215.2	224.7	267.6	319.1	379.0
Goods FOB	177.8	186.5	228.9	238.4	332.6
Services	37.4	38.2	38.7	80.7	46.4
Transport	9.7	8.2	9.4	8.9	12.5
Travel	13.2	13.3	13.1	9.1	11.9
Imports of goods and services	231.4	242.4	246.8	349.9	535.6
Goods FOB	177.7	189.5	188.8	268.3	449.0
Services	53.7	52.9	58.0	81.6	86.6
Transport	24.2	22.3	23.3	29.8	49.1
Travel	15.1	16.2	15.7	13.9	17.5
Net external investment income	−29.1	−31.6	−33.4	−35.3	−38.7
Profits	−22.9	−22.4	−22.6	−21.5	−23.3
Interest	−6.2	−9.2	−10.8	−13.8	−15.4
Net private transfer payments	2.9	4.0	3.9	32.2	7.5
Balance on current account	−42.4	−45.3	−8.7	−33.9	−187.8
Capital account					
Net external financing ($a + b + c + d + e$)	42.4	45.3	8.7	33.9	187.8
(a) Net external non-compensatory capital	53.7	50.2	41.4	114.0	
Direct investment	15.0	13.3	9.2	6.7	
Long- and medium-term loans	41.4	53.7	56.5	98.4	
Amortization payments	−10.2	−14.3	−17.7	−16.9	228.8
Short-term liabilities	4.3	−3.5	−9.2	12.2	
Official transfer payments	3.2	1.0	2.6	13.6	
(b) Domestic non-compensatory capital or assets	−2.7	–	−8.5	−55.2	
(c) Errors and omissions	−1.0	−2.8	−5.5	−2.5	
(d) Allocation of SDRs	3.2	2.9	2.9	–	–
(e) Net compensatory financing (increase −)	−10.8	−5.0	−21.6	−22.4	−41.0
Balance-of-payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	10.0	4.2	4.2	15.5	...
Amortization payments	−13.8	–	−6.8	−8.0	...
Movements of foreign exchange reserves (increase −)	−4.0	−6.5	−16.7	−30.2	...
Movements of gold reserves (increase −)	−2.0	–	3.0	−0.2	...
SDRs (increase −)	−1.0	−2.7	−2.6	0.5	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26.

[a] Estimates based on official statistics.

Figure XXXIX. Nicaragua: trend of external variables
Natural scale



component of demand–but also by the function of expectations in the context of the inflationary process.

Thus, during 1974, imports of crude and partly refined oil were trebled, purchases of construction materials more than doubled, an increase of about 80 per cent was recorded in those of durable consumer goods, and imports of raw materials and intermediate products expanded by approximately 65 per cent.

It has already been pointed out that in the aggregate the volume of external sales of goods and services decreased by 6.1 per cent during 1974, although there were significant increments of 11 per cent in the volume of exports of goods and of 25.3 per cent in average prices, which raised the value of exports by 39 per cent. Among the staple export items, a substantial increase of 101 per cent took place in the export value of cotton, and a smaller one of 24 per cent in sales of shrimps and lobsters, while the value of exports of meat dropped by 59 per cent, and that of sugar exports fell for the second year in succession, whereas that of coffee sales slightly improved.

The expansion of cotton sales was mainly due to a highly significant variation in the average price and a considerable increase in volume, made possible by bumper crops. The stronger upward movement of prices, contrasting with the very modest growth recorded in 1973, was largely attributable to renegotiations of long-range contracts formalized the year before with Japan, the leading purchaser. But recent trends in world quotations, in conjunction with the rise in the production costs of Nicaraguan cotton resulting from increases in the price of inputs, suggest that the outlook for the coming year may not be so bright, especially as the high yields obtained could hardly be surpassed over the short term. On the other hand, sugar export earnings may be expected to rise, if account is taken of the inventories marketed and the expansionist trends shown by the world market.

Coffee sales climbed to a level of more than 46 million dollars (an increase of 4 per cent) despite the smaller volume exported. The higher unit values reflected the more advantageous conditions that have gradually been secured in the process of seeking new markets, initiated as a result of the suspension of the quota system in force under the International Coffee Agreement.

The marked fluctuations in Nicaragua's traditional markets, with their repercussions on domestic production and on the country's foreign exchange income, particularly affected the value of meat exports, which dropped sharply in 1974, from 44.5 million dollars to less than 20 million. This was basically due to a substantial reduction of slaughtering for export as a result of the prevailing uncertainty as to prices. Producers–who had stepped up their investment in view of the previous year's price increases–retained inventories in the hope that prices might be quoted which would counterbalance the heavier costs they had to meet.

The evolution of exports to Central America, unlike that of traditional products, was particularly dynamic. The figures for the first eight months of the year showed an increase of 67 per cent in current values in relation to the same period of 1973, the very high rate of exports to Guatemala and El Salvador being worthy of note. This expansion became an important factor in the reactivation of Nicaragua's manufacturing sector, especially in the case of the non-traditional branches (chemical products, basically polyvinyl chloride and sodium chloride). Also very significant were Nicaragua's intra-area imports, which expanded on much the same scale as exports.

The special characteristics of growth in 1974 affected the method of financing the balance of payments. In the first place, outstanding importance was acquired by the official capital which flowed in to support and supplement domestic reconstruction efforts; concurrently, non-compensatory movements of private capital, which had represented a drain on the balance of pay-

ments in 1973, became positive in 1974. According to estimates, inflows of non-compensatory capital exceeded the amount of the deficit on current account, which means that international reserves expanded by 41 million SDR units (see table 242).

3. PUBLIC FINANCE

During the year 1974 a sizable increase of 42 per cent was once again recorded in the central government's tax revenue. This improvement was due to a substantial recovery on the part of direct taxation and to the continuation of the upward trend in revenue from indirect taxation.

The most significant increases were to be found in import duties, in consequence of the marked rise in import prices and also of the increase in the volume of imports. Similarly, the revenue from the over-all sales tax rose at a rapid rate.

The very intensification of the inflation process likewise determined a significant increase in income tax revenue. On the other hand, export taxes showed a smaller increment owing partly to a slackening in sales of certain products subject to the emergency tax régime established in 1973, and partly to the fact that these exceptional tax contributions were discontinued as from mid-November 1974.

In the central government's current expenditure there was an increase of 40 per cent, slightly higher than the variation in regular income. This reflected the public sector's greater activity in the fields of reconstruction of essential services, wage adjustments granted to public employees, the effects of inflation on purchases of goods and services and the larger transfer payments intended to supplement financing and encourage higher levels of activity on the part of the decentralized public sector.

Savings on current account thus rose by about 30 per cent. Nevertheless, the marked increase in capital expenditure—which was practically doubled—seriously aggravated the over-all deficit. To cover this imbalance, the Government had at its disposal external loans mainly—medium- and short-term credits—to an amount of about 700 million córdobas with which it effectively strengthened real direct investment and financial transfers for the investment purposes of other public institutions. At the same time it paid off advances made by the Central Bank in previous fiscal periods, and reduced the volume of new inflows of funds from other internal sources. This method of financing public expenditure gave the national bank system greater flexibility to enable it to meet the needs of the private sector; nevertheless, in view of the predominance of private bank credit from foreign sources, it will be necessary to modify the structure of borrowing in coming years by increasing the participation of financing agencies that grant longer servicing periods.

The tax reform launched in 1974 was complemented by amendments to the Income Tax Act and to the regulations governing taxes on immovables, movables and consumer goods. Apart from a considerable increase in the legal possibilities for tapping resources, in view of the urgent tasks facing the Nicaraguan public sector, the objective pursued was, generally speaking, the progressive consolidation of a fiscal structure better adapted to the country's development requirements, specifically as regards the more equitable distribution of the tax burden, particular emphasis being placed on duties on imports of non-essential goods.

4. MONEY AND CREDIT

In 1974 the monetary authorities adopted various measures to regulate the financial system, with the aim of reducing internal credit pressures, strengthening the tapping of resources in the system, and promoting selectivity in the channelling of funds to encourage the recovery of specific sectors or remedy shortages of certain basic imported supplies.

In this connexion, it should be recalled that at the end of 1972 and during 1973 there was a considerable expansion of money and quasi-money; the money supply increased by about 22 per cent in the first of these years and by more than 50 per cent in the second. In the aggregate, in the two years in question growth rates of 32 per cent and 48 per cent, respectively, were recorded for liquid resources, which outstripped the requirements deriving from the increase in transactions. This expansion basically reflected the combined effects of the strengthening of the bank system's foreign exchange position—caused in its turn by the inflows of reinsurance funds and the vigorous upswing in external loans, mainly in support of the physical reconstruction process undertaken by the public sector—and of an expansionist credit policy which aimed at buttressing activities that would provide immediate employment opportunities and at facilitating the replacement of inventories and other assets.

Thus, circumstances themselves generated demand pressures which necessitated the amplification of mechanisms and instruments to mitigate their effects on price levels. These levels had already been influenced by the rise in prices of imported goods and by the shortages of various domestically-produced goods and services.

In April 1974, controls to prevent an indiscriminate supply of credit were introduced, together with adjustments in current rates of interest on the monetary market, in order to discourage any possible flight of capital abroad and counteract the deterioration in the real returns of savers. First and foremost, the legal requirements respecting cash reserves for deposits in commercial banks and other intermediary financial institutions were raised and unified–the average rate previously in force was increased by 25 per cent[52]–and secondly, limits were set to the use of external resources by the commercial banks, such loans being channelled as far as possible into the financing of credits and for coffee, cotton, fatstock rearing, tobacco and exports to markets outside the Central American area.

In addition, ceilings were established for the expansion of private bank credit: commercial loans could not exceed 100 per cent of each bank's capital and reserves, and short-term industrial credits were not to represent more than 25 per cent of the December 1973 balances. This opened up greater possibilities of meeting requests for the financing of other activities.

Furthermore, the Central Bank continued to supply resources applicable to the rehabilitation of commerce in Managua, granted larger rediscount volumes in relation to imports of raw materials needed by the industrial and agricultural sectors, opened up special one-year discount lines for the financing of imports of insecticides, fertilizers and the raw materials for these inputs,[53] and stimulated the use of loans from the Special Development Fund based on resources supplied by the Inter-American Development Bank (IDB) and the Government to support the construction industry and livestock production.

Between October 1973 and October 1974, the international reserves of the bank system came to play much less part in the creation of means of payment; domestic credit, on the other hand, remained a determining factor in the generation of bank liabilities to the public. In the Central Bank's credit operations, advances to the Government decreased from 215 to 148 million córdobas, as against an increase from 173 to 330 million córdobas in loans to the commercial banks. The growth rate of total domestic credit, however, which was 26 per cent between October 1973 and October 1974, was no higher than in the immediately preceding period.

On the other hand, the money supply, which had expanded by 58 per cent between October 1972 and October 1973, increased by only 13.3 per cent in 1974.

Despite the measures adopted, the marked falling-off in the tapping of internal resources by the bank system in 1974–a situation which apparently became so much more critical in the latter part of the year that net international reserves decreased in the calendar year as a whole–is a clear indication that although the pressures deriving from domestic credit were progressively moderated and channelled with relative success, in contrast the mechanisms capable of selectively controlling expenditure abroad seem to have been inadequate.

[52] The private banks were temporarily authorized to make up the increase in average cash reserves with National Reconstruction Bonds.

[53] In this case, the rate of interest charged to banks by the monetary authorities was graded in inverse ratio to the contribution made by each bank out of its own resources.

PANAMA

1. INFLATIONARY PRESSURES AND ECONOMIC TRENDS

The high rate of growth which the Panamanian economy had been experiencing began losing momentum from 1972 onwards, dropping to its lowest level in 1974. In fact, the growth rate of 4 per cent achieved by the gross domestic product in the past year, compared with the annual growth rate of 7.3 per cent achieved in the period 1970-1972, and that of 6.5 per cent in 1973, is evidence of this trend. It shows to what extent the economy of this country has been affected by the world recession, and also by the international inflationary process, which had an impact on domestic costs through the prices of imported inputs and, therefore, on the prices of goods produced in the country, leading in turn, to a sharp downturn in global demand and a larger deficit in the current account of the balance of payments (see table 243).

The slowing down of external demand contributed to the deterioration of the employment situation and of income levels. In fact, the volume of exports barely increased by 1.7 per cent, which follows on a similar increase in 1973. The rate of consumption also dropped considerably (3.9 per cent compared with 6.1 per cent in 1973), and in the case of the public sector this can be attributed, apart from financial difficulties, to the deliberate

Table 243. Panama: total supply and demand

	Millions of balboas at 1970 prices			Structure (percentages)		Annual growth rate (percentages)		
	1970	1973	1974[a]	1970	1974[a]	1970-1972	1973	1974[a]
Total supply	*1,470.5*	*1,766.4*	*1,837.8*	*140.6*	*137.2*	*7.6*	*3.7*	*4.0*
Imports[b]	424.7	478.2	498.1	40.6	37.2	7.9	-3.3	4.2
Gross domestic product	1,045.8	1,288.2	1,339.7	100.0	100.0	7.5	6.5	4.0
Total demand	*1,470.5*	*1,766.4*	*1,837.8*	*140.6*	*137.2*	*7.6*	*3.7*	*4.0*
Exports[b]	390.1	426.8	434.2	37.3	32.4	3.8	1.5	1.7
Domestic demand	1,080.4	1,339.6	1,403.6	103.3	104.8	9.0	4.4	4.8
Gross domestic investment	275.9	359.9	385.7	26.4	28.9	14.2	–	7.2
Gross fixed investment	255.6	336.2	360.7	24.5	26.9	14.6	0.2	7.3
Public	67.7	89.4	98.7	6.5	7.4	1.4	28.4	10.4
Private	187.9	246.8	262.0	18.0	19.5	19.0	-7.2	6.2
Construction	127.6	...	...	12.2	...	...	...	...
Machinery and equipment	128.0	...	...	12.3	...	...	...	...
Total consumption	804.5	979.7	1,017.9	76.9	75.9	7.1	6.1	3.9
General government	149.8	193.1	198.9	14.3	14.8	10.3	5.9	3.0
Private	654.7	786.6	819.0	62.6	61.1	6.4	6.2	4.1

SOURCES: 1970-1972: ECLA calculations based on figures supplied by the Statistics and Census Office; 1973 and 1974: ECLA estimates based on official data.

Note: The figures for exports and imports of goods and services were taken from balance-of-payments data expressed in dollars at current prices, which were converted to constant 1970 values by deflation, using price indexes calculated by ECLA for the purpose.

[a] Preliminary figures.

[b] Goods and services, excluding factor payments.

policy of restraint in current public spending which has been followed in recent years with a view to increasing capital expenditure. In the case of private consumption, the drop in the rate was due to the impact of higher prices. In this connexion, it should be borne in mind that oil imports represent almost 40 per cent of the value of goods purchased abroad, and that the unit value of imports increased by 53.7 per cent. The impact of the generalized rise in prices is reflected, in part, in the wholesale price index and in the consumer price index. The former shows an increase of 37.9 per cent, the biggest change occurring in the industrial sector as a result of the greater impact of oil prices. For its part, the consumer price index in Panama City shows a global increase of 21.5 per cent, and one of 30.6 per cent in respect of food-stuffs and beverages.

The inflationary impact on private consumption was partially offset by the Government's policy of reviewing wages periodically, and measures taken to control the prices of staple products. In fact, in March 1974 the Government approved three laws on prices and wages[54] in an attempt to counter the adverse redistributive effect of the generalized rise in prices. Furthermore, in the Declaration of Boquete[55] a series of measures are announced for curbing inflation, the favourable effects of which would be felt only in 1975.

Gross fixed capital investment increased at a much higher rate than the gross domestic product, and one substantially higher than the increase it recorded in 1973. Public investment–continuing a trend which began in 1972–showed a faster rate of growth than that observed in private investment. This confirms the Government's interest in the development of basic infrastructure works, and the use of the public sector investment budget as an instrument of development and transformation of the productive structure. With the advantages offered by the rapid development of the tertiary sector, the aim has been to finance the needs of the very backward agricultural sector, and a manufacturing sector, which, in spite of the high rate of growth observed in the 1960s, no longer has any great possibilities of growth owing to the narrowness of the domestic market and limited export prospects.

Public investment has been oriented primarily to assisting rural industry, transport, and housing,

[54] Under these laws, the wages of public employees and those of the private sector are increased through the operation of a scale inversely proportional to the 1973 wage levels. Increases were 20 per cent for the lowest wage levels, and 15 per cent for the highest levels. The minimum wage was increased, as well as the cash portion of domestic workers' wages, and those of construction workers were increased by 7 per cent.

[55] Meeting of the General Council of State, which was held in Boquete in the province of Chiriquí, in November 1974, to consider the consequences of inflation and propose specific policies and actions.

in accordance with government policy to combat extreme poverty in rural areas. In fact, the importance given to the agricultural sector in the 1973 and 1974 investment budgets is linked to the decision to promote the development of the most depressed areas of the country, through programmes which aim at improving food production and, with it, the income of rural workers, forming them into groups through which the programmes of technical, economical and social assistance could be channelled.

Among the most important investment allocations made in 1974, mention should be made of the Integrated Development Project at Bayano, almost completed, which combines the generation of electric energy with the irrigation of 40,000 hectares for implementing labour-intensive agricultural projects and establishing a new sugar factory, in addition to the major projects whose implementation the Government plans to accelerate.[56]

On the supply side, the drop of 3.3 per cent recorded in 1973 was carried over, for although there was a strong expansion in imports, measured in terms of current prices, there was no change in real terms. This drop was largely due to the deliberate policy of the Government to limit the expansion of imports of goods which were not indispensable for the development of the economy (see table 243).

[56] Such projects cover the fishing port, the working of the copper mines at Cerro Colorado, the transisthmus pipeline to the new factories, the container port, the expansion of the free zone at Colon, the Convention Centre, the hydroelectric plant at La Fortuna, the Bayano Integrated Project, and the new cement plant.

2. MAJOR SECTORS OF ACTIVITY

The growth of the manufacturing sector shows signs of weakening, attributable not only to the fact that the country has passed the easier stages of import substitution and that the agricultural sector is not producing enough for its industrial transformation, but also to the sluggish growth of global demand during the year. The fact is that the manufacturing sector grew at relatively high rates up to 1972, whereas in 1973 and 1974, in spite of the increase in petroleum activity, it began to lose momentum. In 1974 the contraction in the production of construction materials, fish meal and oil, and in other activities such as the manufacture of clothing and footwear, and of containers and articles made of paper and paperboard was a factor which contributed to the downturn. The production of food-stuffs, beverages and tobacco, together with the refining of petroleum, offset, on the other hand, the stagnation of other productive activities in the economy, as a result of which the value added generated showed a growth rate of 2.1 per cent, half of that of the previous year (see table 244 and figure XL). The sugar industry

Table 244. Panama: gross domestic product at factor cost, by sector of economic activity

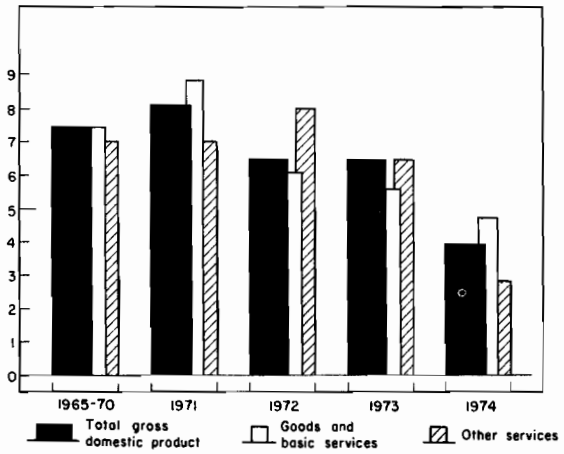
	Millions of balboas at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970–1972*	*1973*	*1974*[a]
Agriculture	198.8	219.5	227.0	20.7	18.5	3.3	3.4	3.4
Mining	2.5	4.0	3.9	0.3	0.3	8.4	−37.9	−2.5
Manufacturing	152.5	182.7	186.6	15.9	15.2	7.2	4.2	2.1
Construction	60.4	85.3	88.6	6.3	7.2	15.3	6.3	3.9
Subtotal goods	*414.2*	*491.5*	*506.1*	*43.1*	*41.3*	*6.6*	*4.4*	*3.0*
Electricity, gas and water	19.0	28.1	31.3	2.0	2.6	14.7	12.4	11.4
Transport and communications	54.3	75.3	85.7	5.6	7.0	11.6	11.3	13.8
Subtotal basic services	*73.3*	*103.4*	*117.0*	*7.6*	*9.6*	*12.4*	*11.6*	*13.2*
Commerce and finance	135.1	172.7	185.0	14.0	15.1	7.8	10.0	7.1
Government	29.5	31.3	32.2	3.1	2.6	2.3	1.5	2.6
Ownership of dwellings	57.0	75.5	79.3	5.9	6.5	9.8	10.0	5.0
Miscellaneous services	253.2	305.3	304.8	26.3	24.9	7.5	4.4	−0.2
Subtotal other services	*474.8*	*584.8*	*601.3*	*49.3*	*49.1*	*7.5*	*6.5*	*2.8*
Total	*962.3*	*1,180.7*	*1,227.9*	*100.0*	*100.0*	*7.3*	*6.5*	*4.0*

SOURCES: 1965–1972: ECLA calculations based on figures supplied by the Statistics and Census Office; 1973 and 1974: ECLA estimates based on official data.

Note: As the individual activities and the totals were calculated independently, the sum of the former does not correspond exactly with the latter.

[a] Preliminary figures.

Figure XL. Panama: growth of gross domestic product
(Annual growth rates)
Natural scale



continued to be a dynamic element, the Victoria sugar factory having been expanded to process the cane harvested on 2,000 additional hectares.

During 1974, on the basis of tenders received, a contract was awarded for the construction of the factory of Pacora, located in the region covered by the Bayano Project, which will have a grinding capacity of 6,000 tons of cane per day. It is expected to come into operation in 1977. Other studies completed in 1974 were the transisthmus pipeline project which could come into operation in 1977, and the State-owned cement plant in the Bayano area, with a capacity of 300,000 tons per year, which will double present production and make it possible to reduce imports. Moreover, the construction of the rice-hulling plant is now in its final stage.

In the Boquete Declaration the Government undertook to set up an Industrial Development Bank, the purpose of which would be to tap resources from international banks established in Panama, and to channel them into industry and new projects geared to export activity.

The growth rate of the agricultural sector was 3.4 per cent, a similar rate to that of 1973, in spite of the fact that banana production for the external market dropped by 23 per cent because cutting was suspended in July and August. On the other hand, production for the domestic market showed a high rate of growth, as a result of the price policy and the channelling of technical and financial resources to agricultural areas. Figures for the first harvest show increases of 13.5 per cent for rice, 18 per cent for maize, 100 per cent for beans, and 40 per cent for vegetables, which reflect increases in both the area cultivated and yield. Prospects for the second harvest are also favourable, and it is estimated that production for domestic consumption will have increased by 13.6 per cent (see table 244).

Public investment has played some part in the previous results, since, on the basis of the diagnosis of depressed areas, action has been taken to increase production and standards of living. One of the measures taken is the setting up of rural workers' settlements, providing them with machinery and equipment as well as advisory services so as to integrate them in the modern productive process. Some of these measures include the growing of fruit and vegetables for processing and canning, within the framework of programmes which aim at improving employment conditions.

A fair number of the projects initiated in 1973 began to show results in 1974. Among them mention should be made of the irrigation of 5,000 hectares at Coclé and the improvements introduced in the seed dressing plants at Panama and Chiriquí. Furthermore, the programmes of the Agricultural Development Bank geared towards the financing of small- and medium-sized producer units, have also contributed to the increase in production for domestic consumption. In addition, mention should be made of the Government's offer to subsidize the rates of interest on agricultural loans and to promote the agro-industrial projects for the production of cassava flour, animal feeds, and the establishmment of tomato, milk and fertilizer processing plants. There are also plans to introduce crop insurance from 1975.

Stock rearing continues to encounter serious problems which stem, in part, from the 1972 drought and also from structural difficulties. The growth rate of the total number of cattle is continually falling; from 2.3 per cent in 1972 it dropped to 1.8 per cent in 1973, and to 1.6 per cent in 1974. The wide fluctuations in foreign demand for beef and its contraction during the greater part of 1974 resulted in a cutback in investment for breeding and fattening cattle. In spite of this, the number of cattle available for slaughter increased by 3.3 per cent.

The total number of pigs fell by 6.7 per cent, compared with 1973, and poultry by almost 1 per cent, which was largely due to the bankruptcy of small farms faced with the impossibility of maintaining suitable profit margins. Perhaps for this same reason, the number of pigs supplied for slaughter increased by 7.5 per cent.

The construction sector was unable to maintain the rate of growth of the previous year owing to the glut in the supply of housing for high-income groups of the population, as well as the relative scarcity and the increase in prices of construction materials in the international market. The 23.3 per

cent reduction in the value of private construction permits reflects this situation. The public sector, on the other hand, increased construction works by 14 per cent, as a result of which the value added by the sector increased by 3.9 per cent.

Construction was begun on the projects at San Joaquín, Patio Pinal and Río Alejandro; this last is a joint venture located in Colon in which 13.8 million dollars have been invested. They are expected to provide an additional 1,602 housing units. In addition, Law 100 of October 1974 provides for tax exemptions for houses or apartment buildings intended for low-income groups.

For middle-income families the Government proposes to obtain from private banking sources an additional 20 million dollars for new housing, by means of mortgages.

The growth rate in the electricity, gas and water sector was 11.4 per cent, slightly higher than that of 1973, as a result of the increase in installed capacity in 1972 and 1973. Among ongoing projects, there is the hydroelectric plant at Bayano which will have a capacity of 300 MW; the first two stages, of 75 MW each, are in the process of construction.

3. PUBLIC FINANCE

Government financial policy continues to favour capital expenditure and restraint in current expenditure. Ordinary revenue of the central government increased by 25.9 per cent, whereas current expenditure—affected by the increase in the wages of public employees—increased by 22 per cent. This permitted a saving on current account of 23 million balboas, as a result of which capital expenditure was able to maintain its high rate.

Table 245. Panama: balance of payments
(Millions of SDR units)

	1970	*1971*	*1972*	*1973*	*1974*[a]
Current account					
Exports of goods and services	381.9	421.3	419.8	414.8	561.8
Goods FOB	130.3	137.8	134.6	132.2	192.8
Services	251.6	283.5	285.2	282.6	369.0
Transport	36.0	49.9	56.0	56.6	127.7
Travel	78.2	80.8	76.4	75.5	79.7
Imports of goods and services	421.2	466.3	483.3	483.9	746.0
Goods FOB	331.0	363.9	376.4	307.9	616.5
Services	90.2	102.4	106.9	106.0	129.5
Transport	45.8	54.1	53.7	66.2	69.9
Travel	22.7	24.0	24.4	21.6	28.0
Net external investment income	−26.5	−31.4	−30.7	−37.1	−43.1
Profits	−15.9	−14.5	−8.7	−8.7	−11.6
Interest	−10.6	−16.9	−22.0	−28.4	−31.5
Net private transfer payments	−3.6	−3.5	−3.9	−7.4	−9.7
Balance on current account	−69.4	−79.9	−98.1	−113.6	−237.0
Capital account					
Net external financing (*a* + *b* + *c* + *d* + *e*)	69.4	79.9	98.1	113.6	237.0
(*a*) Net external non-compensatory capital	271.2	280.6	622.5	1,388.3	
Direct investment	33.4	15.7	12.3	9.9	
Long- and medium-term loans	109.2	93.0	119.7	136.9	
Amortization payments	−25.4	−30.5	−30.0	−50.9	221.6
Short-term liabilities	146.6	195.2	512.4	1,284.7	
Official transfer payments	7.4	7.2	8.1	7.7	
(*b*) Domestic non-compensatory capital or assets	−129.4	−178.8	−452.7	−1,122.1	
(*c*) Errors and omissions	−70.2	−23.0	−72.0	−152.7	
(*d*) Allocation of SDRs	4.7	3.9	3.9	–	–
(*e*) Net compensatory financing (increase −)	−6.9	−2.8	−3.6	0.1	15.4
Balance-of-payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	–	–	–	–	...
Amortization payments	−1.7	–	–	–	...
Movements of foreign exchange reserves (increase −)	–	–	–	–	...
Movements of gold reserves (increase −)	−2.0	−3.4	−3.6	–	...
SDRs (increase −)	−3.2	0.6	–	0.1	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26.

[a] Estimates based on official statistics.

With reference to tax revenue, mention should be made of the sharp increase recorded in export taxes, which amounted to 5.2 million dollars, a sum made up almost entirely of revenue on banana exports. Import duties did not, however, reflect the sharp increase in prices of imported goods, for they only increased by 10.6 per cent. This is due to the fact that a large number of customs tariffs are based on specific taxes, and the fact that the main import product whose unit value increased substantially is free from customs tariffs; in addition, public sector imports are tax free.

The rate of increase in indirect taxes was lower than that in direct taxes. The increase in income tax was due mainly to adjustments in salaries, for there was, of course, a corresponding increase in the sums collected, these having increased by 25.4 per cent.

Funds from external sources contributed to the financing of four fifths of the global deficit, estimated at 83.7 million dollars, the notable difference being that private sources reduced their share in such financing, being replaced by external official sources.

The strenghthening of the international financial centre which has been operating over the last two years has been impressive, because of the advantages Panama offers owing to the nature of its monetary system and the free movement of capital. The number of foreign banks established in Panama and operating with bank funds or the funds of non-nationals is continually growing. External deposits increased from 1,107 million dollars at the end of 1972 to 2,604 million in December 1973, and stood at 4,385 million on 30 September 1974.

The support which this system provided to the economy consisted mainly in the supply of funds for some development projects. In fact, loans to the domestic sector which were 967 million dollars on 30 September 1973 increased to 1,523 million dollars by the same date in 1974, i.e., an increase of 57.5 per cent. On the last-mentioned date, credit granted to the external sector represented a sum 3.6 times higher than that of the previous year.

4. Foreign trade and the balance of payments

The increase in international prices had a strong impact on the economy of Panama, for it accentuated the imbalance in the current account which amounted to SDR 237 million, an unprecedented figure and double that of the previous year in spite of the increase in the inflow of net non-compensatory capital--which also doubled compared with the previous year--thereby making it necessary to have recourse to compensatory loans in the amount of SDR 15.4 million to cover the trade gap resulting from the higher costs of oil imports (see table 245).

The negative balance in the current account was caused by an extraordinary increase in imports of goods and services, which do not necessarily correspond to an increase in the volume imported, but rather to the alarming increase in prices. In fact, the FOB value of imported goods increased by 63 per cent, whereas, in real terms, these increased by little more than 6 per cent. At current prices, paid services also increased but to a lesser extent (2.2 per cent), which also reflects the same situation (see table 246 and figure XLI).

The explanation for the large increase in imports is to be found in the crude oil which Panama imports for processing, since the value of this product more than tripled, increasing from 88.1 million dollars in 1973 to 271.3 million in 1974. The sharp rise in prices takes on greater importance if it is realized that the imported volume fell meanwhile by 3.7 per cent.

While exports of goods also increased appreciably at current prices, 44.5 per cent, which helped

Figure XLI. Panama: trend of external variables
Natural scale

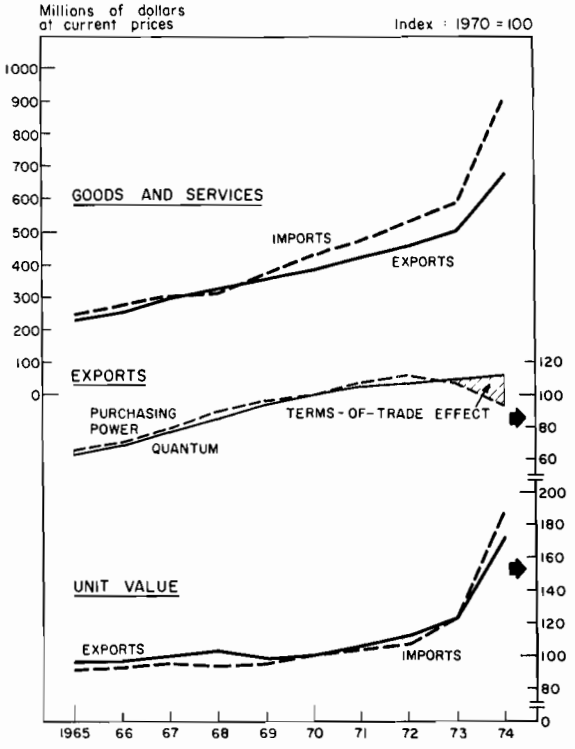


Table 246. Panama: exports of goods and services
(*Millions of dollars*)

	1970	1971	1972	1973[a]	1974[b]
Total	*383.2*	*421.6*	*455.7*	*500.4*	*675.9*
Goods	*130.3*	*137.8*	*146.2*	*159.5*	*231.9*
Bananas	60.8	62.9	64.7	63.8	49.1
Petroleum[c]	20.7	24.4	21.5	24.4	80.7
Sugar	4.9	6.3	5.9	8.8	23.0
Shrimp	10.2	12.0	14.6	16.7	17.0
Fish meal	0.8	1.0	1.4	4.0	4.0
Coffee	1.7	1.6	2.2	2.1	2.1
Meat	2.2	1.4	3.2	1.6	2.9
Sales to the Canal Zone	22.2	23.0	24.4	24.9	46.4
Miscellaneous, including adjustments	6.8	5.2	8.5	13.2	6.7
Services	*252.9*	*283.8*	*309.5*	*340.9*	*444.0*
Transport[d]	35.9	49.9	60.7	68.2	153.4
Travel	78.2	79.7	82.9	91.1	95.9
Canal Zone	37.3	38.6	39.1	39.0	39.9
Other countries	40.9	41.1	43.8	52.1	56.9
Other services to the Canal Zone	85.2	88.0	90.0	99.3	104.2
Wages and salaries, net	65.6	69.0	71.2	76.9	...
Miscellaneous	19.6	19.0	18.8	22.4	...
Free zone, Colon (net)	29.7	37.3	37.3	41.2	43.1
Miscellaneous, including adjustments	23.9	28.9	38.6	41.1	47.4

SOURCE: ECLA, on the basis of data provided by the Office of the Controller of Panama, Statistics and Census Office.

[a] Preliminary figures.

[b] Estimates.

[c] Excluding sales to ships using the Panama Canal.

[d] Including sales of petroleum products to ships using the Panama Canal.

to mitigate the impact of imports on the balance of payments, actually the exported volume also increased by a much smaller percentage (4.9 per cent). Bananas, the principal export product of the country, have over the last 20 years established a pattern of inelastic demand and unfavourable prices. In fact, between 1970 and 1973 the unit value of banana exports fell by an average annual rate of 1.1 per cent, whereas the volume exported only increased by 2.4 per cent.

Owing to the low prices for bananas, the Government of Panama together with other Central American countries decided to establish a tax of one dollar on each case exported, which led to disputes with the banana company, as a result of which there was a limit on exports and a stoppage of sales during the month of August. This led to a drop in banana exports of 23 per cent, and the unit value fell by 2.9 per cent.

Petroleum products helped to offset the drop in banana exports. Their value more than tripled, whereas their volume increased by 52.5 per cent.

As a result of the increase in the installed capacity of the factories, sugar exports increased by 24.4 per cent in volume, and 161.4 per cent in value.

The creation of import capacity through current transactions has continued to be based mainly on services, although during 1974 these showed a rate of growth (30.3 per cent) which was considerably lower than that recorded in exports of goods. The changes which occurred in this branch are due to the flow of income from the transport sector which more than doubled (126 per cent) compared with the corresponding figure for 1973. In this connexion, mention must be made once again of the influence of the prices of oil sold to ships passing through the Panama Canal. As to the other sectors of the service accounts, changes were relatively modest.

PARAGUAY

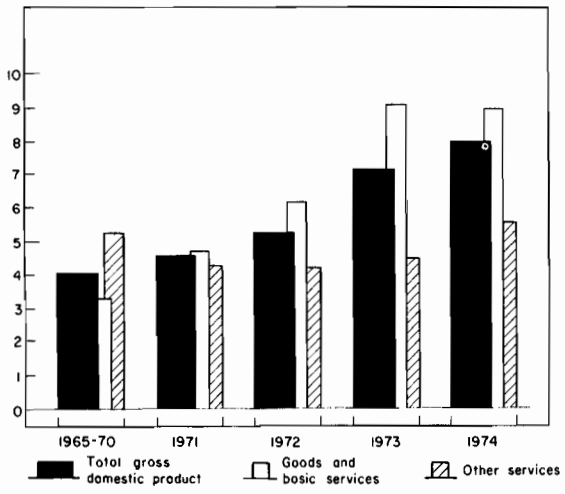
1. ECONOMIC GROWTH IN 1974

Once again, a considerable increase in exports, this time amounting to 33 per cent (as against 50 per cent in 1973) measured in dollars at current prices, fed resources and infused dynamism into Paraguay's economic activity—which is closely linked to its foreign trade—and partly accounted

for the fact that the growth rate of total production maintained and even slightly surpassed the previous year's high level, rising from 7.2 per cent in 1973 to about 8 per cent in 1974 (see table 247 and figure XLII).

Under the stimulus of continuing high prices on the world market and favourable weather conditions, agricultural production again increased, by 12 per cent. Owing to the relative weight carried by the sector (19 per cent of the total product) and its decisively important linkages with manufacturing industry and other important activities in Paraguay, this expansion was the basis of the rapid growth of the total product in the past two years.

Figure XLII. Paraguay: growth of gross domestic product
(Annual growth rates)
Natural scale



Stock farming, which is Paraguay's other basic productive activity, increased its product by 6.5 per cent—the highest rate achieved in the course of the decade—although slaughtering for export decreased, because of the contraction in external demand for meat.

For the same reason the product of the manufacturing sector, in which the relative importance of meat processing is considerable, grew by only 5.6 per cent, notwithstanding the notable increases achieved in respect of other industrial export products.

In contradistinction to what happened in 1973, when export prices rose by 44 per cent and prices of imports by only 15 per cent, in 1974 the increase in unit values was the same for imports as for exports (33 per cent in both cases), which meant that real availabilities of imported goods expanded only by a little over 4 per cent, whereas in 1973 they had done so by 41 per cent.

Internal consumption and investment resources (domestic supply, plus the balance on imports and exports of goods and services) increased by 10.3 per cent in 1973 and 8.2 per cent in 1974. In these circumstances, gross domestic investment rose by 36.8 per cent in 1973 and 12 per cent in 1974. It was private investment that set the course for this progress; public investment suffered from the effects of the policy of restricting public

Table 247. Paraguay: gross domestic product at factor cost, by sector of economic activity

Sector	*Millions of guaraníes at 1970 prices*			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970-1972*	*1973*	*1974*[a]
Agriculture	23,804.8	28,556.0	31,325.9	34.3	35.3	4.6	9.7	9.7
Mining	82.8	198.6	238.3	0.1	0.3	53.0	2.4	20.0
Manufacturing	12,004.1	13,864.0	14,640.4	17.3	16.6	4.8	5.2	5.6
Construction	2,075.7	2,824.6	2,982.8	3.0	3.4	8.2	16.3	20.0
Subtotal goods	*37,967.4*	*45,443.2*	*49,187.4*	*54.7*	*55.6*	*5.0*	*8.6*	*8.2*
Electricity, gas and water	839.7	1,490.5	1,857.2	1.2	2.1	20.4	22.4	24.6
Transport and communications	2,950.4	3,723.5	4,181.5	4.3	4.7	6.9	10.4	12.3
Subtotal basic services	*3,790.1*	*5,214.0*	*6,038.7*	*5.5*	*6.8*	*10.1*	*13.6*	*15.8*
Commerce and finance	13,529.3	16,146.9	17,035.0	19.5	19.3	4.9	8.4	5.5
Government	3,943.0	3,698.2	3,801.7	5.7	4.3	0.8	-7.7	2.8
Ownership of dwellings	2,281.0	2,580.8	2,756.3	3.3	3.1	3.3	5.9	6.8
Miscellaneous services	7,924.7	9,036.8	9,624.2	11.4	10.9	5.1	3.3	6.5
Subtotal other services	*27,678.0*	*31,462.7*	*33,217.2*	*39.9*	*37.6*	*4.3*	*4.6*	*5.6*
Total	*69,435.5*	*81,961.2*	*88,518.1*	*100.0*	*100.0*	*4.9*	*7.2*	*8.0*

SOURCES: 1970-1973: ECLA calculations based on figures supplied by the Central Bank of Paraguay; 1974: ECLA estimates based on data from the same source.

Note: As the individual activities and the totals were calculated independently, the sum of the former does not correspond exactly with the latter.

[a] Preliminary figures.

expenditure. Despite the considerable increase in investment, consumption expanded at fairly satisfactory rates of 6.4 and 7.3 per cent in 1973 and 1974, respectively (see table 248).

Another primary concern of the economic authorities which was reflected in various economic measures was the sharpening of the upward trend of domestic prices. The rate of increase of consumer prices was twice as high as in 1973 (25 per cent as an average for the year, and 22 per cent between December 1973 and December 1974). The odd circumstance about this upswing, however, was that it occurred exclusively in the first two months of 1974 (23.5 per cent); during the rest of the year prices fluctuated slightly and even fell.

In addition to the various measures adopted from 1973 onwards to counteract the price increases, such as the fixing of ceiling prices and of minimum quotas for exports of important consumer goods, the most effective lines of action were those aimed at contracting the monetary supply and the excess liquidity brought about by the growth of external income, and those restricting public expenditure. Influence in the same direction was exerted by the liberal supply of agricultural commodities for the home market, which, in the case of meat—a very important item in the customary diet—was enlarged by virtue of the reduction in external demand.

2. Trends in selected sectors of production

Agricultural production expanded by 12 per cent in 1974, having already increased by the same proportion in the preceding year. Generally speaking, however, the branches of production that showed the biggest increases in 1974 were not the same as in 1973, nor were they the most important. Thus, output of cassava, maize, cotton and sugar-cane, which represent approximately one half of total production, expanded by about 3 per cent, whereas production of wheat rose by 130 per cent, that of tung by 80 per cent, that of soya beans by 20 per cent in 1973 and 58 per cent in 1974, and that of rice by 52 per cent.

These results were attributable both to the high prices prevailing for many of these products and to favourable weather conditions.

Crop farming contributes 19 per cent of the total product, livestock production a little over 9 per cent, and forestry about 4 per cent. The

Table 248. Paraguay: total supply and demand

	Millions of guaraníes at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970–1972*	*1973*	*1974*[a]
Total supply	*86,999.2*	*103,709.8*	*111,253.1*	*116.1*	*116.4*	*4.0*	*10.3*	*7.3*
Imports	12,078.0	15,243.8	15,709.8	16.1	16.4	–2.3	32.2	3.1
Gross domestic product	74,921.2	88,466.0	95,543.3	100.0	100.0	4.9	7.2	8.0
Total demand	*86,999.2*	*103,709.8*	*111,253.1*	*116.1*	*116.4*	*4.0*	*10.3*	*7.3*
Exports	11,176.0	11,576.5	11,564.0	14.9	12.1	0.4	2.7	–0.1
Domestic demand	75,823.2	92,133.3	99,689.1	101.2	104.3	4.5	11.3	8.2
Gross domestic investment	11,033.6	18,250.3	20,440.3	14.7	21.4	10.0	36.8	12.0
Gross fixed investment	10,882.6	16,975.8	18,911.0	14.5	19.8	7.3	35.4	11.4
Public	2,954.6	...	...	3.9	...	...	...	...
Private	7,928.2	...	...	10.6	...	...	...	...
Construction	5,462.5	7,445.8	8,935.0	7.3	9.4	8.2	16.5	20.0
Machinery and equipment	5,420.3	9,530.0	9,976.0	7.2	10.4	6.5	55.1	4.7
Total consumption	64,789.6	73,883.0	79,248.8	86.5	82.9	3.5	6.4	7.3
General government	6,748.1	6,419.0	7,182.9	9.0	7.5	1.6	–7.9	11.9
Private	58,041.5	67,464.0	72,065.9	77.5	75.4	3.7	8.0	6.8

SOURCES: 1970–1973: ECLA calculations based on figures supplied by the Central Bank of Paraguay; 1974: ECLA estimates based on data from the same source.

Note: The figures for exports and imports of goods and services were taken from balance-of-payments data expressed in dollars at current prices, which were converted to constant 1970 values by deflation, using price indexes calculated by ECLA for the purpose.

[a] Preliminary figures.

product of the livestock sector rose by 6.5 per cent, the highest percentage in the decade, although the slaughtering of beef cattle for export was reduced by 24 per cent; total slaughtering, however, must have increased, owing to a recovery in slaughtering for domestic consumption purposes, which in 1973 had declined by 17 per cent.

Manufacturing industry consists almost entirely in the processing of agricultural products, a large proportion of which are exported. Industrial processing of meat for export (which accounts for about 17 per cent of the manufacturing product) decreased by 31 per cent in 1974, owing to the suspension of purchases of frozen meat by the European Common Market countries. Thus, while production of preserved meat increased by 44 per cent, that of frozen beef dropped by 64 per cent.

In contrast, other branches of production expanded: sawnwood attained an output of 200,000 tons (an increase of 12 per cent); output of edible oils rose by 20 per cent, and that of other vegetable oils at rates ranging from 60 to 80 per cent; production of wheat flour also boomed, increasing from 21,000 tons in 1973 to 50,000 in 1974.

In short, the industrial product increased by 5.6 per cent in 1974, a rate slightly higher than the preceding year's, but not reflecting the briskness of recent economic development.

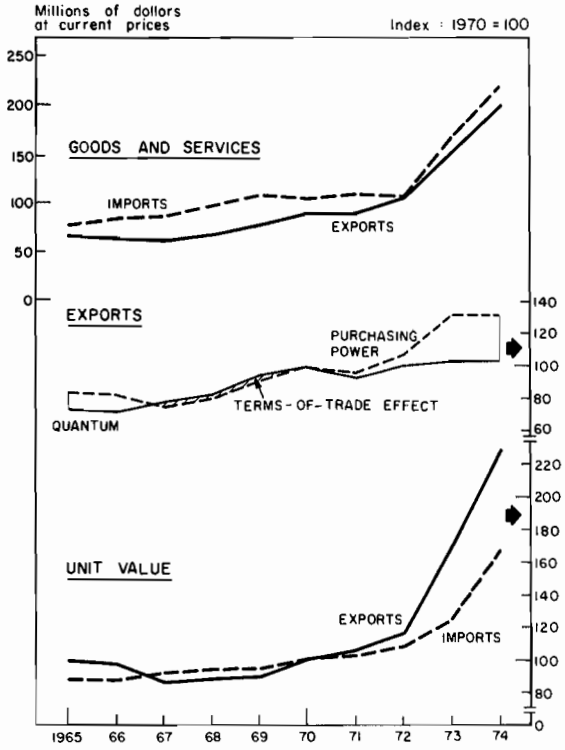
Of the other sectors, construction was the most dynamic, expanding by 16.3 per cent in 1973 and 20 per cent in 1974; next came basic services (with a growth rate of 15.8 per cent in 1974), among which electricity showed an increase of 25 per cent. It should be mentioned that since 1973 electricity is being exported to Argentina and Brazil from the Acaray power station. The growth rate of the other services, which carry a relative weight of 38 per cent in the total, was only 5.6 per cent.

3. Foreign trade and the balance of payments

A sudden upswing in exports and imports of goods–33 per cent and 38 per cent respectively–was the most outstanding economic event in 1974, because of its vital importance for economic activities. In the preceding year exports had already expanded by 50 per cent, so that in 1973 and 1974 their value practically doubled.

The 1974 increase in the value of exports is entirely attributable to the rise in prices, since there was no change in their volume. The exceptionally high levels reached by world market prices for some commodities were particularly favourable to those comprising the country's export basket, and were reflected in increases in

Figure XLIII. Paraguay: trend of external variables
Natural scale



the unit values of exports of 44 per cent in 1973 and 33 per cent in 1974. In contrast to what happened in the first of these years, however, when import prices rose by 14.5 per cent, in 1974 they increased in the same proportion as export prices, cancelling out the 1973 improvement in the terms of trade, which had been 26 per cent (see figure XLIII).

Meat sales dropped considerably from 32,000 to 15,600 tons (i.e., by 52 per cent). This downward plunge was mainly due to sales of frozen meat–which were reduced by 64 per cent for the reasons mentioned above–and offset the noteworthy increases in export volumes of other major products. For example, among oilseeds, 101,000 tons of soya beans were exported, i.e., 88 per cent more than in the preceding year–although, inexplicably, their value rose by only 45 per cent, which is not consistent with the world price trend–and the volume of tartago sold was trebled. In addition, tung oil sales expanded by 111 per cent in terms of volume, and 142,700 tons of lumber were exported, one third as much again as in 1973. The volume of tobacco sales also increased (37 per cent), and those of sugar were trebled.

In point of fact there were few products that really benefited from the price boom by virtue of a corresponding expansion of their volume. Nevertheless, among the major products, in terms

of value, sugar exports increased nine times; those of wood and vegetable oils by 117 and 102 per cent respectively; those of oilseeds by 68 per cent; and those of cotton and tobacco by 42 and 53 per cent, respectively.

Furthermore, with reference to less important exports it is worth mentioning the exceptional increases in external sales of cereals (244 per cent), pulses and vegetables (340 per cent), maté (260 per cent), Portland cement (736 per cent), and electric energy (83 per cent).

Imports of goods expanded by 38 per cent, much less than in the preceding year (62 per cent). The increase in volume was only 4.4. per cent, whereas in 1973 it had reached 41 per cent. In 1974 the biggest increments were recorded for petroleum and for wheat and wheat products, which virtually trebled in value.

The fact that imports expanded more than exports gave rise to a small trade deficit, whereas in the two preceding years surpluses had been shown. This deficit, in combination with the negative balance on services which increased considerably, in particular in freight and insurance, led to a new and even greater deterioration in the balance-of-payments position on current account. A larger net inflow of capital, however (estimated at 60 per cent above the 1973 figure), once again permitted an improvement in net international reserves of about 24 million SDR units (see table 249).

4. CONTROL OF INFLATION

The great extent to which the Paraguayan economy is dependent upon its external trade relations has been reflected in various ways in a sharpening of the upward trend of domestic prices. Consumer prices, which had been relatively stable,

Table 249. Paraguay: balance of payments
(Millions of SDR Units)

	1970	*1971*	*1972*	*1973*	*1974*[a]
Current account					
Exports of goods and services	89.3	89.1	97.1	124.0	164.1
Goods FOB	65.3	66.5	78.8	106.1	141.1
Services	24.0	22.6	18.3	17.9	23.0
Transport	2.5	1.6	1.1	1.2	1.5
Travel	14.2	14.7	10.2	9.4	10.0
Imports of goods and services	101.1	109.1	97.7	133.5	182.4
Goods FOB	76.6	83.0	72.5	105.5	146.3
Services	24.5	26.1	25.2	28.0	36.1
Transport	9.0	10.6	9.5	12.5	17.9
Travel	5.1	5.9	7.2	8.3	9.1
Net external investment income	−9.8	−10.0	−10.3	−8.3	−9.8
Profits	−2.5	−2.3	−2.3	−1.5	−2.1
Interest	−7.3	−7.7	−8.0	−6.8	−7.7
Net private transfer payments	1.9	3.8	2.2	1.7	0.5
Balance on current account	−19.7	−26.2	−8.7	−16.1	−27.6
Capital account					
Net external financing ($a + b + c + d + e$)	19.7	26.2	8.7	16.1	27.6
(a) Net external non-compensatory capital	32.9	31.1	22.3	36.6	
Direct investment	3.8	7.1	2.7	8.1	
Long- and medium-term loans	22.6	26.3	24.2	25.7	
Amortization payments	−6.5	−9.8	−9.9	−9.2	
Short-term liabilities	9.7	3.7	1.5	9.0	51.5
Official transfer payments	3.3	3.8	3.8	3.0	
(b) Domestic non-compensatory capital or assets	−2.3	−3.3	−3.2	−3.4	
(c) Errors and omissions	−5.0	−0.8	−3.6	−1.4	
(d) Allocations of SDRs	2.5	2.0	2.0	–	–
(e) Net compensatory financing (increase −)	−8.4	−2.8	−8.8	−15.7	−23.9
Balance of payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	–	0.1	–	2.6	...
Amortization payments	−0.6	−0.1	−0.1	–	...
Movements of foreign exchange reserves (increase −)	−4.3	−0.8	−6.7	−18.3	...
Movements of gold reserves (increase −)	−1.0	–	–	–	...
SDRs (increase −)	−2.5	−2.0	−2.0	–	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26.

[a] Estimates based on official statistics.

increased by 9.2 per cent in 1972, 12.8 per cent in 1973 and 25.2 per cent in 1974 (annual averages). Wholesale prices rose at even higher rates: 25 per cent in 1973 and 32 per cent in 1974.

This was partly due to the high prices that had to be paid for inputs, fuels and other imported products. The increases in world quotations for export products also forced up prices of the proportion of these goods reserved for the home market. Furthermore, the growth of international reserves and export earnings helped to increase liquidity and to step up pressure on domestic prices.

But the 22 per cent rise in consumer prices between December 1973 and December 1974 had the singular feature of being concentrated in the early part of the year. In January and February prices increased by 23.5 per cent, under the influence of the food component of the index, which rose by 24.8 per cent. In the remaining months there were slight fluctuations, which in the event resulted in the above-mentioned increase of 22 per cent.

Several factors contributed to this stabilization from March onwards. Since 1973 various measures had been adopted, such as the fixing of maximum prices for essential goods, the creation of producers' markets, and maximum export quotas as a means of preventing shortages on the home market. For example, a maximum quota of 220,000 head of beef cattle for export was established, and for the reasons already noted was not filled. In addition, the available supply of crop-farming products expanded (for the second year in succession production increased by 12 per cent), and this was undoubtedly also true of meat, because of the drop in sales abroad.

Furthermore, a restrictive monetary policy was applied which was complemented by another designed to curb government expenditure. The Central Bank took a firm stand with respect to the regulation of the rate of expansion of money and credit. The means of payment increased during the year by 25 per cent (as against 31 per cent in 1973). The main expansionist factor was the 66 per cent rise in international reserves; credit, on the other hand, increased by only 8 per cent, that assigned to the private sector rising by 17 per cent, whereas that allocated to the Government dropped by 28 per cent in relation to the preceding year, and the credit granted to the rest of the public sector remained the same.

With the same end in view—that of reducing liquidity in the economy—the regulation fixing cash reserves of banks at 42 per cent was maintained, and so was the prior import deposit requirement.

In the meantime the fiscal budget closed with a surplus on current account of 1,500 million guaraníes, which helped to reduce its pressure on monetary issues, while at the same time offical deposits in the Central Bank were increased.

PERU

1. General trends

Economic growth in Peru showed further improvement in 1974. The increase in the gross domestic product, which for the past two years had been around 6 per cent, rose somewhat to an estimated 6.6 per cent (see table 250).

A number of favourable factors were responsible for this acceleration in the growth rate. One of these is the recovery in construction activities, which increased by 17 per cent; another is the 41 per cent increase in fishing; a third is the impact of heavy investment over the last two or three years.

The demand for imports, which amounted to 1,999 million dollars, and a deficit of 850 million dollars in the current account of the balance of payments are directly related to these events. Inflows of capital, however, were larger and permitted, in addition to a considerable build-up in the country's international reserves, the continued implementation of large-scale economic projects and the addition of new ones.

2. Principal guidelines of economic policy

During 1973 and 1974, world inflation, which is discussed in Part One of this *Survey*, was a highly destabilizing factor for the economy of Peru, as well as other developing economies. It affected the level of domestic prices, those of imports and exports, current and budgeted exchange needs, the relationship between government current income and expenditure, and the economy's liquidity. Moreover, the pressure exercised was not continuous but varied in intensity and impact, forcing those responsible for economic policy to be constantly alert, and to modify their policy on repeated occasions.

Although the measures adopted failed to prove fully effective in countering its harmful effects, they made it possible to reconcile, with minor concessions, the permanent objective of economic policy, that of stable domestic prices, with more recently adopted objectives on economic growth

Table 250. Peru: total supply and demand

	Millions of soles at 1970 prices			Structure (percentages)		Annual growth rate (percentages)		
	1970	1973	1974[a]	1970	1974[a]	1970-1972	1973	1974[a]
Total supply	*274,386*	*324,666*	*361,350*	*116.1*	*119.8*	*6.0*	*5.4*	*11.3*
Imports[b]	38,140	41,608	59,610	16.1	19.8	3.8	1.2	43.3
Gross domestic product	236,246	283,058	301,740	100.0	100.0	6.3	6.0	6.6
Total demand	*274,386*	*324,666*	*361,350*	*116.1*	*119.8*	*6.0*	*5.4*	*11.3*
Exports[b]	48,012	41,779	46,302	20.3	15.3	-0.7	-11.8	10.8
Domestic demand	226,374	282,887	315,048	95.8	104.5	7.3	8.5	11.4
Gross domestic investment	28,800	39,579	48,128	12.2	16.0	10.5	12.6	21.6
Gross fixed investment	29,478	39,961	48,193	12.5	16.0	7.7	16.9	20.6
Public	11,508	...	...	4.9	...	...	...	...
Private	17,970	...	...	7.6	...	...	...	...
Total consumption	197,574	243,308	266,920	83.6	88.5	6.8	7.9	9.7
General government	28,306	35,406	38,451	12.0	12.0	7.7	7.8	8.6
Private	169,268	207,902	228,469	71.6	76.5	6.7	7.9	9.9

SOURCES: 1970-1973: ECLA calculations based on figures supplied by the Central Bank of Peru; 1974: ECLA estimates based on official data.

Note: The figures for exports and imports of goods and services were taken from balance-of-payments data expressed in dollars at current prices, which were converted to constant 1970 values by deflation, using price indexes calculated by ECLA for the purpose.

[a] Preliminary figures.

[b] Goods and services, excluding factor payments.

which involve heavy investment, but whose effect on the supply of goods will only be felt in the future. In fact, the rate of inflation in 1974 amounted to 16.9 per cent compared to 13.7 per cent in 1973, but investment continued and, as a result of this, the productive capacity of the country will increase in the years ahead.

Among the factors that contributed to the increase in domestic prices, in addition to the growing multiplier effect on the product, which could be ascribed to the expansion in investment, mention should be made of the persistent increase in prices paid for imports; the recognized inelasticity in the supply of agricultural food-stuffs, aggravated by the tendency to replace the crops of the producing areas located in the vicinity of the major cities by export crops; the increase in purchases by the fishing industry; and the increase in urban employment. Countervailing factors were the decline experienced in the second half of 1974 in prices for the major export products, the adequate supply of light industry products, and the economic policy measures introduced.

These measures included the control of bank lending. Credit in national currency extended by the commercial banking sector increased from 42,400 million soles to 45,800 million between the end of 1973 and the end of 1974, that is to say, by 8 per cent. Furthermore, it accepted deposits and other inflows, in the amount of 4,400 million soles, with the result that in 1974 funds available including cash reserves had increased by 33.5 per cent. These restrictions on commercial credit were offset by the operations of the development financing institutions which prevented a liquidity crisis in the private sector and ensured first that the financing needs of priority activities, and secondly those of durable consumer goods activities, could be met.

For its part, the central government maintained its policy of increasing savings in current account. The biennial 1973-1974 budget was not fully complied with, since under the programme current income was to exceed current expenditure by 14,100 million soles. However, because of a sharp increase in such expenditure, this figure fell, maintaining, nevertheless, the high level of 11,100 million soles at the end of the biennium. To cover the capital expenditure, which amounted to 35,700 million soles, it was therefore necessary to incur a domestic debt of 8,800 million, and to use 11,800 million of foreign reserves. The direct inflationary impact of this capital expenditure was mitigated by the wider use which was made of surplus resources in the housing financing system to take up long-term Treasury bonds in an amount similar to that of the total deficit of the central government, i.e., 3,200 million soles.

Another economic policy instrument which acted directly on domestic prices was the fixing of price ceilings and the subsidizing of certain consumer goods. Since Peru is a sugar exporter, the domestic price of this commodity did not change during 1974. The same is true of the supplies of public enterprises, such as the fish consumed throughout the country. However,

official prices were not always respected, when there were a great many producers and either temporary or continuous shortages of the product concerned.

The system of subsidies acquired some importance in 1974 when it was applied to imports of staple items of urban diet. Rice, of which Peru normally produces enough for its needs, and three other products which it has always imported were subsidized. The subsidy for rice, wheat and vegetable oil was equivalent to 40 per cent of the import price, and in the case of lard it was 20 per cent. No accurate information is available on the total amount spent on subsidies in 1974, but estimates put the figure at 8,000 million soles (202 million dollars).

The effort to arrest the increase in prices and to prevent cost inflation included a wages policy. Certain groups of workers, such as those employed in the petroleum sector, received wage increases which were higher than the increases in prices. In general, however, the wages of the other workers in the private sector fell in real terms. This is also true for public employees, judging from the very moderate adjustments awarded to major groups (master craftsmen, health workers).

As regards the second objective of Peruvian economic policy, that of investing with the aim of increasing the future productive capacity of the country, this was achieved not only through the use of domestic resources–as described in previous paragraphs–but also, and in larger amounts, through external borrowing, guaranteed by the Government, in the amount of 1,260 million dollars, 1,020 million of which were used.

These funds, together with direct investment expenditure, played a decisive role in 1974, for, owing to the rise in the prices of food-stuffs, raw materials and fuels, imports of these items absorbed 71 per cent of the value of exports of goods (41 per cent in 1973). Since these goods were indispensable, they meant severely limiting current investment and the types of investment mentioned in the previous paragraph.

The Peruvian authorities took advantage of the relatively high liquidity in the international capital market in 1973 and 1974 to attract more external savings, and to improve the position of the foreign debt. Since all barriers to the use of the United States capital market had been removed, a portion of this debt was refinanced, on better terms, by private banks in the United States. AID, the Inter-American Development Bank, and the World Bank Group, also granted loans to Peru, which began to be paid out during the year.[57]

[57] In 1973 the net amount disbursed by IDB was 9.8 million dollars. Disbursements by the United States showed a negative balance.

However, the main financial sources were those that accepted the long list of development projects of the Peruvian authorities. The United Kingdom, the Federal Republic of Germany, Japan, France and other market-economy countries increased the funds which they provided; the same was true of the Soviet Union, Romania and other COMECON countries. Moreover, during the year, new sources in Latin America and other areas were added to the list.

The financing of the Selva-Pacific Coast pipeline offers an example of the geographical diversity of sources of external funds in the Peruvian economy. Japan provided 330 million dollars, a part of which was provided jointly with the Federal Republic of Germany. The United Kingdom provided 11 million dollars, private banks in New York and San Francisco 100 million, and the USSR 7 million. Moreover, Argentina and Venezuela made loans available in the amount of 36 million and 100 million respectively, and Iran also provided 100 million dollars.

This geographical mosaic begins to attract attention as one looks at the series of projects financed, or those whose financing is at an advanced stage of negotiation. The increase in the sources of funds helped to maintain conditions which were favourable to the economic development policy.

The inflow of capital for investment projects increased from 305 million dollars in 1973 to 626 million in 1974; in 1973, 254 million were used to refinance and improve the terms of the external debt, when the amount to be repaid was fairly high, and in 1974 215 million dollars were used for these purposes (see table 251). This improvement, in addition to the accumulation of international reserves, which increased from 430 million dollars in 1973 to 702 million in 1974, is highly favourable to the achievement of the objective of economic policy, that of reconciling stability with investment for future growth.

Table 251. Peru: use of public external debt
(Millions of dollars)

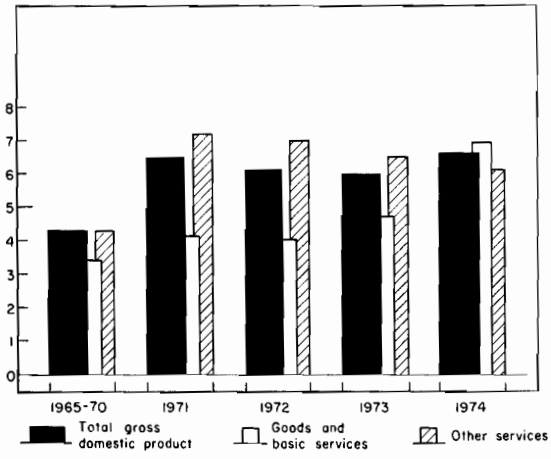
	1973	*1974*
Loans contracted	1,025	1,260
Amount disbursed	672	1,020
For investment	305	626
Refinancing	126	100
Debt substitution	128	115
Other purposes	113	179

SOURCE: Statement of the Minister of Economic Affairs and Finance, published in *El Peruano*, 14 February 1975.

3. MAJOR SECTORS OF ACTIVITY

The growth rate of 6.6 per cent in the gross domestic product in 1974 was mainly due to the expansion experienced in the following sectors: fishing, manufacturing, construction and electricity. The primary sectors–agriculture and mining–showed a relatively low growth rate, whereas services maintained rates similar to those of previous years (see table 252 and figure XLIV).

Figure XLIV. Peru: growth of gross domestic product
(Annual growth rates)
Natural scale



(a) *Agriculture*

The agricultural sector (excluding fishing) continued to restrict the growth of the Peruvian economy. On the basis of available estimates,[58] the total area of land under cultivation is 2.7 million hectares, which in relation to the population of 14.5 million gives one of the lowest indexes of the developing world. If the shortcomings in transport and in the agricultural technology applied are added to this constraint, it becomes clear how difficult it is to obtain a continuous increase in agricultural production.

According to preliminary estimates, the growth rate in 1974 in the agricultural sector was 2.3 per cent, a rate similar to that of the previous year. The sector was affected by a series of unfavourable circumstances which countered the favourable effects of agrarian reform and a larger inflow of funds. Rainfall was unfavourable, rains were heavier than usual and the season shorter, as a result of which there was drought. Early in the year there were unusual snow-falls in a large area in the south which were detrimental to agricultural production. The temperature in the Andean valleys remained low for a longer period than

[58] See FAO, *Production Yearbook 1972*, Rome 1973, table 1.

Table 252. Peru: gross domestic product at factor cost, by sector of economic activity

	Millions of soles at 1960 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1973*	*1970-1972*	*1973*	*1974*[a]
Agriculture	42,455.0	40,808.4	42,589.0	19.8	16.3	–2.4	0.7	4.4
Agriculture (excluding fishing)	36,731.0	38,626.9	39,515.3	17.1	15.4	1.3	2.4	2.3
Fishing	5,724.0	2,181.5	3,073.7	2.7	0.9	–29.8	–22.6	40.9
Mining	19,050.0	19,581.0	20,070.5	8.9	7.8	0.6	1.5	2.5
Manufacturing	35,966.0	45,052.1	48,656.3	16.8	18.0	7.9	7.5	8.0
Construction	12,550.0	16,743.1	19,589.5	5.9	6.7	11.0	8.2	17.0
Subtotal goods	*110,021.0*	*122,184.6*	*130,905.3*	*51.4*	*48.8*	*3.4*	*4.3*	*7.1*
Electricity, gas and water	2,831.0	3,412.3	...	1.3	1.4	6.6	6.1	...
Transport and communications	11,340.0	14,607.1	...	5.3	5.8	9.5	7.5	...
Subtotal basic services	*14,171.0*	*18,019.4*	...	*6.6*	*7.2*	*8.9*	*7.2*	...
Commerce and finance	34,162.0	40,931.4	...	16.0	16.4	6.3	6.0	...
Government	18,520.0	22,579.5	...	8.6	9.0	6.7	7.0	...
Ownership of dwellings	10,877.0	12,423.8	...	5.1	5.0	4.5	4.5	...
Miscellaneous services	26,410.0	34,015.4	...	12.3	13.6	9.4	7.5	...
Subtotal other services	*89,969.0*	*109,950.0*	...	*42.0*	*44.0*	*7.1*	*6.5*	...
Subtotal services	*104,140.0*	*127,969.4*	*135,775.5*	*48.6*	*51.2*	*7.4*	*6.6*	*6.1*
Total	*214,161.0*	*256,598.7*	*273,534.2*	*100.0*	*100.0*	*6.3*	*6.0*	*6.6*

SOURCES: 1970–1973: ECLA calculations based on figures supplied by the Banco Central de Reserva del Peru; 1974: ECLA estimates based on official data.

Note: As the individual activities and the totals were calculated independently, the sum of the former does not correspond exactly with the latter.

[a] Preliminary figures.

usual, delaying year-end harvests, and resulting in inadequate pasture growth.

Furthermore, a number of essential inputs were either in short supply or prices for them were comparatively high. Among these were chemical fertilizers and pesticides. Fodder for milk production and the fattening of cattle, and poultry feeds also increased in price as a result of which selling prices frequently failed to cover costs, thereby creating financial difficulties for the producers.

Cotton production increased by 3 per cent owing to the constant expansion of the area under irrigation in the extreme north, and a reversal of the trend of replacing this crop by food crops in the central and south coastal areas, brought about by the increase in international prices for this fibre, which remained at a high level until the first half of 1974, the sowing season in the areas mentioned. To prevent a greater shortage of food, the Government decided to enforce, in full, regulations which obliged coastal farmers to set aside a certain area of their lands for subsistence crops.

Sugar production increased by 2.5 per cent. On the other hand, there was a contraction in the production of coffee of approximately 17 per cent. The production of cocoa, another export crop, increased slightly. As regards products for domestic consumption, the production of cereals increased, in particular, rice; but other types of agricultural products decreased.

The limited supply of land *per capita* resulted in high priority being given to the irrigation of the coastal area under the agrarian policy, while safeguarding the continuation of the irrigation projects in the Andean valleys, and those for settlements in the Amazon area. In 1974, three projects were either ongoing or about to be completed, which would probably increase the present 600,000 hectares available on the coast by 120,000. Three further projects were under study which would add a quarter of a million hectares to this area.

As regards the settlement process mentioned, the policy, initiated the year before, of granting lands to the Sociedades Agrícolas de Interés Social (SAIS) in the Amazonian valleys, continued to be followed in 1974.[59] This organization, made up of associations of the Andean zone, sends families, equipment and cattle to the lands allocated to them. Although it is premature to make any assessment of the results, several associations have requested lands to establish a similar type of satellite organization. This policy was extended in 1974 to the sugar co-operatives whose co-ordinating body is seeking lands suitable for sugar-cane cultivation.

(b) *Fishing*

The product of the fishing sector showed a clear downturn during the current decade. This was due to a decrease each year in the anchoveta catch for fish meal, a product which not so long ago was Peru's major export. In 1973 this fish reappeared, but production in this particular line did not reach the level expected of it since it was considered necessary to maintain the ban imposed on the fishing of this species. In 1974 conditions were once more favourable and anchoveta fishing was resumed, and the increase in the catch of other species enabled the sectoral product to increase by 41 per cent.

The recovery in anchoveta fishing enabled full use to be made of the equipment which had been installed at the beginning of the decade, but which had remained virtually idle owing to the circumstances described above. The plant was therefore able to process the stickwater which still contains high proportions of solid matter and fats. Because of this, the yield in fish meal and oil per ton of input improved by approximately 5 per cent. Thus the production of fish meal in 1974 was 850,000 tons, and that of fish oil, also an export product, 300,000 tons.

As regards the rest of the sector, the increase in the catch from ocean fishing is estimated at 5 per cent. However, the major increase occurred in the interior of the country. The supply of lake and river fish supplemented by the fish farms, which are beginning to produce in the Sierra, is rapidly increasing and acquiring importance in the regional diet.

(c) *Mining*

The domestic product of the mining sector increased by 2.5 per cent in 1974 as a result both of the continuous expansion in the production of the main mining centres, and of the temporary working of small mines, the production of which is normally marginal. These mines or some shafts in them were opened when the prices of metals in the international market rose towards the end of 1973, and they were closed in the second half of 1974 when these prices tended to fall.

Production data for major items are still subject to confirmation. Export data, estimated to December 1974, give an indication of expansion in value at current prices, and in physical quantities.

Demand also increased for some products in the domestic market. In the case of zinc, for use in the

[59] See ECLA, *Economic Survey of Latin America, 1973.*

iron and steel industry, consumption increased from 6,000 tons in 1972 to 27,000 in 1973, and possibly to between 34,000 and 40,000 tons in 1974, this last figure represents almost 10 per cent of production.

Attempts to raise funds for investment in the mining sector, and new investments were stepped up. The plan for the construction of a zinc refinery north of Lima is completed, and construction should begin in 1975. Progress continues to be made in several relatively minor deposits, and a contract has been signed with Japanese investors for the development of Michiquillay. As regards the Cuajone copper project, it is in the construction stage and approximately 60 per cent of the physical structure has been completed. In the field of hydrocarbons, the outlook was highly promising in 1974. The production of crude increased by 6 per cent, the Talara Refinery was expanded by the addition of a catalytic cracking plant, and a contract was entered into with the Brazilian State petroleum organization for exporting 5,000 barrels per day by the Amazon river.

In October Petroperu stated that no new concessions would be granted to foreign private enterprises. The probable production of the Amazon Basin, the major concession area, is sufficient to make the construction of a pipeline from the Basin to a Pacific port feasible. A pipeline would carry 250,000 barrels per day, 100,000 of which would be reserved for exports. The agreement on its route was reached early in 1974, and at the end of the year the tubes and related equipment for its installation began to arrive.

(d) *Manufacturing*

Available estimates on the growth of the manufacturing sector in 1974 put its growth rate at 8 per cent, which, although comparatively high, probably completely omits or provides only partial information on new high growth production units. It is possible, therefore, that the growth of the manufacturing sector is underestimated.

SIDERPERU, which had almost doubled its production of liquid steel[60] in 1973, increased its production this year by approximately 35 per cent. Although the greater part of the production of this State enterprise is reserved for import substitution, its price margins and delivery dates, among other factors, have stimulated an increase in the supply of steel products.

Furthermore, the shipyards of the Pacific coast made fuller use of their capacity to meet foreign orders. Ninety-three fishing vessels are under construction for export. The Servicio Industrial de la Marina (SIMA), which builds large ships, launched one ship of 25,000 tons, and took steps to increase its capacity to build ships with a displacement tonnage of up to 300,000 tons. The shipyards in Amazonia began production in 1974, building barges and tug boats and, in general, lighters for transporting petroleum and for exporting crude to Brazil. With the increase in the purchases of the mining companies in Peru, and the construction boom, the number of medium-sized enterprises and their production of varied manufactured products have expanded.

Some of the long-established manufacturing branches recorded considerable increases. The manufacture of fish meal and oil which has depressed industrial production indexes since 1972 recorded an increase of approximately 50 per cent. Although not as high, there were also relatively high rates of growth in other branches of the subsector producing food-stuffs, in the assembly of motor vehicles, and in the construction materials industry. On the other hand, there were moderate rates of growth in the canning industry, excluding fish canning, textiles, footwear and clothing, non-ferrous metal products, and other traditional manufactures.

(e) *Construction*

The construction sector recovered the high growth rate characteristic of it prior to 1973. In that year its domestic product increased by 8.2 per cent, and in 1974 by 17 per cent.

The higher growth rate was due to the construction of public works and the new arrangements adopted for financing low-cost housing. As regards the former, it should be noted that central government gross fixed investment increased by 42 per cent. That of the municipal governments continued to rise during 1974, the communications systems for which they were responsible, public buildings and urban works being improved and expanded. For their part, public enterprises made a substantial contribution to this activity with investments directed towards expanding their productive capacity.

To a certain extent this sector had lost a great deal of its dynamism with the drop in the number of families eligible for housing loans. This situation remains unchanged since, by September 1974, the main mortgage institution had attracted 2,300 million soles, but the amount of its loans for housing were 1,200 million. Although to a lesser extent, the same imbalance is found in other private institutions which finance housing.

[60] SIDERPERU calculates its production on the basis of liquid steel, that is to say, measuring it at converter level. Expressed in bars (crude steel), the resulting tonnage diminishes by no more than 4 per cent.

(f) *Electricity*

The product of the electricity generating sector increased by a little more than 13 per cent in 1974. This rate is higher than that recorded in previous years and is the result of both the increase in installed capacity and the expansion of distribution networks.

1974 was the first year in which the Mantaro power station was in operation, since it started to operate at the end of 1973. In addition to this power station, other smaller stations came into operation in various parts of the country, and several of the existing ones increased their installed capacity.

Another factor which played its part in this result was the expansion of the distribution networks and the interconnexion of some of them. The production of the power station on the Mantaro river, whose waters flow to the Atlantic, serves an extensive region, including important areas in the south-central sector of the Pacific coast. The interconnexion of networks has enabled more efficient use to be made of electricity produced by the power stations in the north.

4. EXTERNAL SECTOR

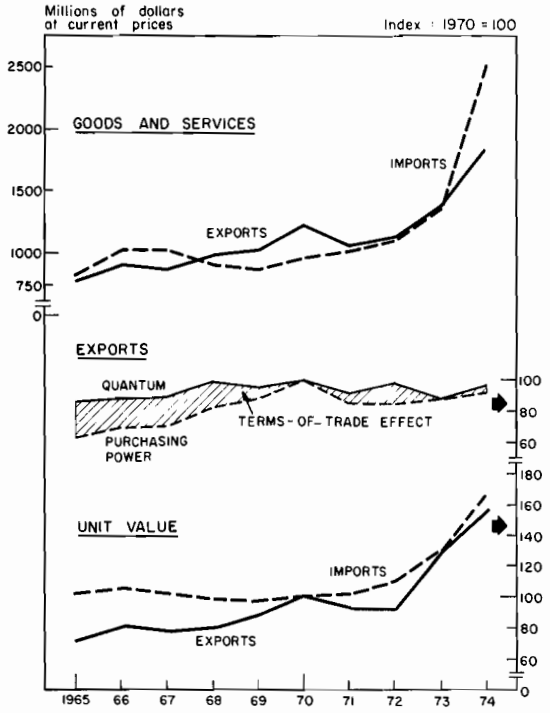
World inflation and economic policy gave an extraordinary impulse to the external sector of Peru during 1974. Exports of goods increased by 13.8 per cent in volume and by 21 per cent in unit value compared with 1973, but even so, the increases in the import of goods were more rapid and sustained (see figure XLV), as a result of which the trade surplus of 113 million dollars in 1973 was converted into a deficit of 426 million in 1974. In respect of services, the balance on current account closed with an extraordinarily high deficit of 850 million dollars. For the previous year, the deficit was 165 million.

(a) *Exports*

The current value of exports of goods increased from 1,142 million dollars in 1973 to 1,573 million in 1974. This change was the result of a general expansion in the volume of the major products exported, and also of the rise in prices in the international market. On the basis of provisional estimates, the indexes of physical volume and unit value increased by 14 per cent and 21 per cent respectively in 1974.

Exports of fish meal were of considerable importance. In 1973 they amounted to 388,000 metric tons, and in 1974 to 809,000. However, their unit value fell sharply, so that their contribution to the current value of exports amounted to only 195 million dollars. Other fishing products provided 77 million more.

Figure XLV. Peru: trend of external variables
Natural scale



The major agricultural products on the whole also showed a favourable growth rate. Their export value increased from 218 million dollars to 351 million. Except for the stagnation observed in zinc production, the volume of exports of the major metals increased substantially. In all cases, prices were higher than in 1973 (see table 253).

Although exports from the new oilfields in the eastern area have not made any substantial difference so far, exports of petroleum and petroleum products increased from 2.6 million barrels to 3 million barrels between 1973 and 1974. As a result of the increase in prices their

Table 253. Peru: principal exports in 1974
(*Percentage variation*)

	Volume	*Price*
Cotton	6.5	39.2
Coffee	−40.2	13.0
Wool	10.1	−2.0
Sugar	2.0	58.2
Copper	12.8	4.9
Lead	4.0	21.7
Zinc	–	43.4
Silver	5.3	55.2

SOURCE: ECLA, on the basis of official data.

value in terms of current prices was 15 and 36.4 million dollars respectively. At the end of the year PETROPERU and PETROBRAS signed a contract for the delivery, by inland waterway, of 5,000 barrels per day at a unit price of more than 12 dollars a barrel.

Non-traditional exports also showed a high rate of increase, approximately 50 per cent in current values, as a result of both the increase in world prices and the introduction of new products in this category.

(b) *Imports of goods*

The current FOB value of total imports increased from 1,029 million dollars in 1973 to 1,999 million in 1974, that is to say, by 94.3 per cent.

Imports of consumer goods amounted to 210 million dollars in 1974. Although the volume of some common staple food products increased, this expansion was due mainly to the general rise in international prices. The same could be said of imports of raw materials, intermediate goods and fuels, the total value of which was 909 million dollars. This increase of 170 per cent on the figure for the previous year was caused partly by the increase in effective demand in the manufacturing and mining sectors, and the increase in stockpiling by enterprises. However, the higher price of fuels was the most important factor, since some 30,000 barrels of crude were imported per day at a price somewhat higher than 12 dollars per barrel. It is common knowledge that this price was approximately 3.5 times higher than in 1973.

The value of imports of capital goods, 612 million dollars, was almost double the 1973 figure. Such goods include construction materials, the value of which probably dropped compared with 1973, owing to the 37 per cent expansion in the production of the iron and steel industry. A new group of items which began to acquire importance at the end of the year when they started to arrive at Peruvian ports comprised materials and equipment for transporting liquids, destined for the oilfields which are starting to produce in the eastern and north-eastern areas, and for the pipeline which is to link them. The expansion of the manufacturing sector and agricultural mechanization also accounted for a higher share of these imports than in 1973.

(c) *Balance of payments*

In 1973 there had been a trade surplus of 113 million dollars. On the other hand, in 1974 there was a negative balance of 426 million dollars. Services taken together also showed a negative balance, in the current account, of 424 million dollars, 53 per cent higher than in the previous year. The items which made the greatest contribution to this deficit were freight, insurance and other transport, which increased from –97 million dollars in 1973 to –205 million in 1974, and returns on investments and interest payments, which rose from – 135 million to – 199 million.

As a result, the balance on current account closed in 1974 with a considerable deficit of 850 million dollars, the equivalent of SDR 707 million, whereas that recorded in 1973 was SDR 137 million (see table 254).

The deficit on current account, however, was smaller than the total inflow of capital, which amounted to SDR 934 million, and determined a substantial increase of SDR 227 million in net international reserves. One of the certain causes of such an increase was the action taken by the public sector in raising external funds for investment, and improving the terms of the external debt.

Private capital provided SDR 78 million, 76 million of which went into direct investment. Central Bank instructions on the raising of foreign loans by the private sector this year meant an inflow of SDR 2 million, compared with an outflow of 11 million in 1973.

Gross financing obtained by the public sector amounted to SDR 848 million, 83 million of which was only a book entry since it corresponded to refinancing. To improve the terms of the guaranteed external public debt, SDR 96 million was raised, which replaced loans previously obtained at less favourable rates of interest and for shorter periods.

The loans obtained for investment, that is, tied to development projects, amounted to a total of SDR 520 million. The loans for other purposes amounted to SDR 149 million. The greater part consists of short-term debts, which in 1973 added 108 million to the positive flows in the capital account.

Short-term loans, which are included in the statistical figures under errors and omissions, recorded a substantial increase for the second year running. From 275 million dollars in 1973, a figure which almost doubled that of 1972, they increased to 358 million in 1974.

5. Structural reform: the agro-industrial sugar complexes

The 1969 *Survey* reviewed legislation on agrarian reform enacted during the year, and the systems which had been established for its rapid implementation. As regards its objectives it was pointed out that it would have the effect of

Table 254. Peru: balance of payments
(Millions of SDR units)

	1970	1971	1972	1973	1974[a]
Current account					
Exports of goods and services	1,224.0	1,067.0	1,063.0	1,136.0	1,535.1
Goods FOB	1,034.0	889.0	871.0	947.0	1,308.0
Services	190.0	178.0	192.0	189.0	227.1
Transport	69.0	59.0	55.0	63.0	91.5
Travel	52.0	50.0	55.0	57.0	64.9
Imports of goods and services	971.0	1,038.0	1,060.0	1,132.0	2,082.0
Goods FOB	699.0	764.0	774.0	853.0	1,662.1
Services	272.0	274.0	286.0	279.0	419.9
Transport	131.0	144.0	146.0	154.0	261.9
Travel	60.0	38.0	41.0	45.0	49.9
Net external investment income	−133.0	−107.0	−114.0	−145.0	−165.5
Profits	−73.0	−42.0	−48.0	−72.0	−77.3
Interest	−60.0	−65.0	−66.0	−73.0	−88.2
Net private transfer payments	26.0	4.0	7.0	4.0	5.8
Balance on current account	146.0	−74.0	−104.0	−137.0	−706.6
Capital account					
Net external financing (*a* + *b* + *c* + *d* + *e*)	−146.0	74.0	104.0	137.0	706.6
(*a*) Net external non-compensatory capital	−69.0	51.0	139.0	224.0	933.6
Direct investment	−70.0	21.0	44.0	54.0	
Long- and medium-term loans	219.0	222.0	294.0	410.0	
Amortization payments	−194.0	−199.0	−187.0	−238.0	
Short-term liabilities	−80.0	−28.0	−42.0	−25.0	
Official transfer payments	56.0	35.0	30.0	23.0	
(*b*) Domestic non-compensatory capital or assets	230.0	10.0	−12.0	−50.0	
(*c*) Errors and omissions	−24.0	−45.0	−25.0	−25.0	
(*d*) Allocation of SDRs	14.0	13.0	13.0	–	–
(*e*) Net compensatory financing (increase −)	−297.0	45.0	−11.0	−12.0	−227.0
Balance-of-payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	21.0	16.0	30.0	5.0	...
Amortization payments	−27.0	−23.0	−3.0	−27.0	...
Movements of foreign exchange reserves (increase −)	−253.0	66.0	−26.0	24.0	...
Movements of gold reserves (increase −)	−24.0	–	1.0	−18.0	...
SDRs (increase −)	−14.0	−14.0	−13.0	4.0	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26.

[a] Estimates based on official statistics.

"forming small-scale and medium-scale farm enterprises to replace the existing latifundia and minifundia",[61] except in the case of the agro-industrial sugar-producing complexes which would remain intact. The main reason for this exception was to maintain the producing capacity of the complexes which could have diminished considerably if broken up.

Since then Peruvian agrarian reform has shown rather the opposite tendency. The latifundia which were expropriated maintained their administrative unity, and in almost all cases have been incorporated into larger units, the Sociedades Agrícolas de Interés Social (SAIS), in which they are associated on a co-operative basis with other forms of Peruvian enterprises, that is, rural communities, and, to a lesser extent, minifundia co-operatives of community groups organized for this purpose.[62]

As a result of these events the average size of units in Peruvian agriculture increased steadily in 1974. This trend still continues, although in recent months the legal recognition of the immunity from expropriation of small unincorporated enterprises, not larger than 12 hectares, has been speeded up. It is probable that these small enterprises number more than 55,000 units, and that there are also an unknown number of minifundia, and a further indeterminate number of rural communities which altogether employ two thirds of the rural workers which have not been affected by agrarian reform.

At present, the sector affected by the reform is made up of 800 large units. Of these, 630 are

[61] United Nations, *Economic Survey of Latin America, 1969.*

[62] United Nations, *Economic Survey of Latin America, 1973.*

co-operatives with an average of 3,700 hectares each, 130 communities with 3,600 hectares on average, and 46 SAIS of 48,000 hectares each. In comparison, all the unincorporated enterprises of the reformed sector work a total of 127,000 hectares.

There are a number of reasons for this aspect of the policy of agrarian reform followed in Peru. One, which is not always clearly understood, is that the supply of agricultural land in the inhabited zones of the country is extremely small. With less than half a hectare per rural inhabitant, an equal distribution of land would have provided highly negative results by creating an agriculture made up exclusively of smallholdings. Another reason also difficult to understand is the traditional community ownership of rural land, as a result of which the rural worker readily accepts co-operative systems.

Thirdly, the agricultural enterprises also have external economies which tend to increase as the techniques they use improve. Some technologies can be broken down to a level suitable for use in the smallest enterprise, for example, the use of improved seeds. This is not true of other technologies, the use of which requires equipment which needs a minimum of inputs, and whose depreciation requires a fairly large gross profit.[63] This is one of the factors which account for the historical increase in the average size of rural property in the industrialized market economies.

In addition to the three factors mentioned above, there is also the fact that the first latifundia expropriated, namely, the agro-industrial sugar complexes, were not divided up. Formed into co-operatives their operations not only continued along usual lines in spite of the administrative change, but basically increased. Given the important role they had played in moulding indirectly the agrarian reform policy, special attention should be given to them.

(a) *Organization of the sugar co-operatives*

The agro-industrial complexes were expropriated in 1969, a little after the law on agrarian reform was enacted. There were 12 units in all, which form four geographical groups. Eight are in the north (two of which are in the far north), one is in the centre and three in the south. All are located on the Pacific coast which stretches for more than 1,500 kilometres from north to south. The differences in latitude give rise to ecological variations and, therefore, to variations in natural productive capacity and production techniques.

[63] Thus, for example, a tractor with complete accessories is uneconomic for areas below 10 hectares.

The 12 complexes were owned by 10 private enterprises up to 1968, which also owned extensive latifundia deep in the interior. In 1969 these were expropriated by the agrarian reform agency, which only replaced the directors of each complex. This agency replaced them with government staff who were not only responsible for running the new enterprises, but also for organizing the present co-operatives in collaboration with the permanent workers.

As was to occur again in other reformed areas when the SAIS were organized, technicians continued in their functions since their individual status had not been changed except that they were offered the possibility of becoming members of the co-operatives. Although there were some resignations, the figure was similar to that of staff turnover or, at most, it opened the way for promoting suitably trained national staff. No appreciable changes took place among the skilled workers.

The period between expropriation and the change in the administration, as such, varied in each case. Although the pattern of organization was the same, there were, of course, a series of factors which either accelerated or delayed the formation of the co-operatives and the corresponding take-over. However, in practice this period generally covered a maximum of three years.

While this process continued, the organization of the co-operatives took a further step towards horizontal integration. The Central de Cooperativas Azucareras del Perú (CECOOAP) was established. Each one of the co-operatives maintains its identity as an enterprise, its directors being responsible for deciding on their respective operational plans and appointing their representatives in CECOOAP.

Although it plays an important part, this organization is not however, a simple spokesman for the industry. It provides services to the co-operatives which include the dissemination of specialized economic information, participation in operative plans and advisory assistance in the use of the external and internal financial resources of member enterprises. The institutional fluidity characteristic of Peruvian agrarian policy makes it impossible to give a suitable assessment of the evolution of CECOOAP. Certain transfers of surplus funds for investment for the benefit of the group of co-operatives, the part they played in studies on sugar potential, and the setting up of a joint co-operative in the Amazon area are the first indications that it is playing a more important role than in the past.

Allowing for exceptions arising from the general trend of Peruvian economic policy, it could be said that there is likely to be an effective

or potential merger of the co-operatives into a bigger entity which, should this occur in the private sector, would be equivalent to the formation of an entrepreneurial matrix. The diversification taking place in manufacturing and that planned would give such a matrix considerable importance on the Peruvian economic scene. However, since there has been no experience with such a complex co-operative system, it is difficult to give even an approximate evaluation of its future development.

(b) *The co-operatives and production*

The recent shortage of potatoes and some staple foods observed in 1974 do not constitute grounds for supposing that the agrarian reform launched in 1968 may have had negative consequences on agricultural production or its marketing. On the contrary, if the performance of the co-operatives grouped in CECOOAP is examined, it will be seen there were improvements in production and in yield per hectare, and that they have an expansion programme which includes not only extending the areas under cultivation but also diversifying production along vertical lines. A detailed description of these efforts is beyond the scope of this note and, therefore, a summary of the most important aspects is given below.

(c) *Importance of the co-operatives*

If the figures for the agricultural area subject to agrarian reform are examined, the importance of the sugar co-operatives will be seen to be small. Up to December 1974 the area under irrigation expropriated amounted to 493,000 hectares, approximately a quarter of the total of this type of land in the country. The 12 co-operatives grouped in CECOOAP hold approximately 95,000 irrigated hectares.

In terms of the population employed in agriculture, the proportions are even smaller. The co-operatives employ, with the annual variations stemming from various causes, between 23,000 and 26,000 workers, which represent a small portion of the agricultural labour force of the country or of the coastal area itself.

However, the co-operatives are of considerable economic importance. When they ceased to be private enterprises, they also ceased to be enclaves linked by their supply needs to the exterior or to national industries which provided their shops with consumer goods. To the extent that domestic supply is able to do so, they have made some import substitution possible, and although the co-operatives have their own shops, their employees are showing a growing tendency to use the goods and services which neighbouring cities of some importance, Chiclayo and Trujillo, have to offer.

The production of the co-operatives is of major significance in the domestic supply of goods. They provide all the sugar for direct or indirect consumption at low prices, compared with international ones, which have not changed over a long period. They also supply the domestic market with alcohol for consumption and for industrial use, syrups and molasses and other by-products from the refining of sugar-cane. They also supply certain meats, fats and hides.

Export of raw sugar in 1973, before the sharp increases in prices in the international market, amounted to 407,000 metric tons, or 78 million dollars. In that year total exports amounted to 1,142 million dollars, and, therefore, the co-operatives contributed under this item only 6.8 per cent of that total. Owing to the considerable diversification of Peruvian exports this is a high percentage, for raw sugar was fifth in line among the important exports in 1973.

As opposed to the pattern established in other sugar-producing countries, the contribution of the industry to the economy is not seasonal. In Peru the planting, harvesting and refining of cane is continuous and does not experience any interruptions other than those required periodically, for short periods, for cleaning distilling equipment. The labour force employed, to which reference was made above, is permanent and an additional 6,000 workers approximately are taken on under short-term contracts. The material and financial flows originating in the co-operatives do not, therefore, follow seasonal cycles of plenty followed by lean periods, for they continue throughout the year.

(d) *The technical performance of the co-operatives*

In the most recent *Statistical Yearbook* published by FAO, data is provided on the sugar-cane yield per hectare in all producing countries. The yield of sugar-cane per hectare was 144.8 metric tons in 1961-1965, the highest in the world. In 1970, the year in which there was a relative shortage of water, it fell to 141.6 tons. In 1971 it increased to 155.7 tons, a figure which was maintained in 1972. In 1973 it rose to 171.4 tons, a level which was maintained in 1974. It is not likely that the sugar yields per ton of crushed cane would have varied greatly, which means that figures for previous yields are valid for the final product of the co-operatives.

The increase recorded in production per hectare in Peruvian harvests has not been repeated to the same extent in other countries. For example, in the United States a clear decline has been observed. In 1971-1972 the index in Peru was 107 (1961-1965 = 100) whereas in the United States it was 71.

The larger yields obtained by the co-operatives have come up against the conditions in international markets in which they sell raw sugar. Although consumption has sustained increased production, the same cannot be said of external supply. For this reason the increased yields have made it possible to release approximately 10,000 hectares, of a total of 83,000, for other crops.

The co-operatives did not confine themselves to improving the production of sugar-cane. They also became involved in other lines of production which are of benefit to them and to the economy of the country in general.

By acting jointly they have been able to make full use of equipment which formerly remained idle, in seasons when the demand of the unincorporated units fell. Of course this refers to mobile equipment capable of being transferred from one co-operative to another, e.g., loading cranes, special trucks for transporting them, and machines for farm work. Although there are limits to this type of seasonal transfer, the fact that it takes place implies an improvement in the productivity of capital invested.

In addition to the foregoing, the co-operatives have revised the criteria for declaring equipment obsolescent, which were followed when the private enterprises were acting independently. The replacement of such equipment acquires a new dimension for, since they are complex machines, all their parts do not suffer the same amount of wear. Those which are in a good state of repair may, depending on the case in point, be transferred from one co-operative to another. In some cases equipment has been rebuilt using used parts which were previously regarded as scrap.

The co-operatives are also trying to diversify their activities. One of these efforts is the setting up of a pilot plant for the manufacture of proteins from micro-algae, and results have so far been satisfactory. This project in which UNDP is participating will help to produce low-cost proteins for use in the staple diet.

Their operational plans include both the expansion of sugar production in the Selva zone and the industrialization of the bagasse produced. As regards the former, a study is being completed on the most suitable locations for its cultivation, taking account also of the economic aspects. In respect of the industrialization of bagasse, CECOOAP will invest 6,000 million soles (approximately 130 million dollars) in various plants for pulp bleaching, and the manufacture of particle board, newsprint and furfural.

DOMINICAN REPUBLIC

1. Recent economic trends

In 1974 there was a break in the growth trend of around 11 per cent per year which had been displayed by the economy of the Dominican Republic since the end of the 1960s, although the gross domestic product still grew by the substantial amount of 8.9 per cent (see figure XLVI).

This loss of dynamism was observed to different extents in most sectors of production of goods and basic services, even though there was substantial additional income during the year (the value of exports rose by 45 per cent) due to the high prices of sugar and other export products, as well as to a bigger inflow of non-compensatory capital, all this being reflected in a considerable expansion of imports of goods and services.

Among the various sectors of production, the slackening in the growth rate was particularly notable in agriculture, where the rate was halved (from 6.6 to 3.2 per cent); in mining, where there was a much bigger drop from 47.4 to 10.1 per cent as a result of the settling-down process after the initial impulse given by the opening of the ferro-nickel plant; and in electricity, gas and water supply, where the growth rate dropped from 17 to 6.5 per cent between 1973 and 1974 (see table 255).

The growth rates of manufacturing and construction were only slightly less than the year before, thus retaining their traditionally dynamic image, while services, except for basic services, increased their added value by a larger amount than in 1973 because of the recovery shown by government activity and bigger real income from ownership of dwellings.

During 1974, domestic production was supplemented by a considerable increase in imports of goods and services, which rose by 17 per cent in real terms as a result of the favourable situation created by an increase in the country's external payments capacity. As is shown by the relatively high import coefficient, which fluctuated between 23.9 per cent in 1970 and 22.6 per cent in 1974, the high proportion of imports in the total supply is a characteristic of the Dominican economy. In

Table 255. Dominican Republic: gross domestic product at factor cost, by sector of economic activity

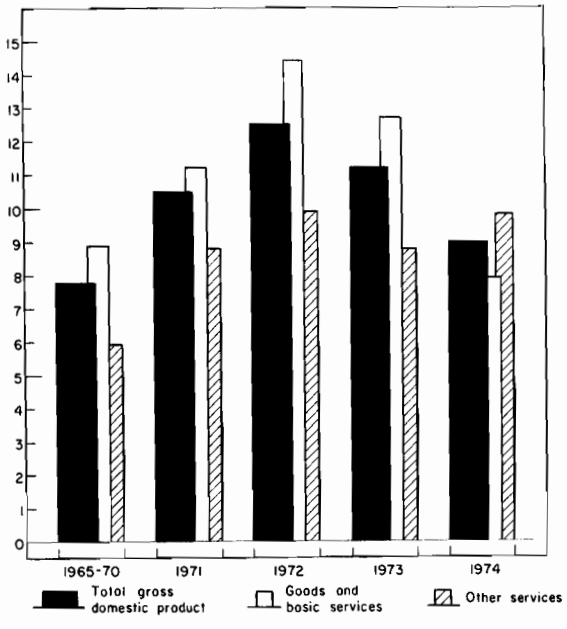
	Millions of pesos at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970-1972*	*1973*	*1974*[a]
Agriculture	331.2	385.6	398.1	25.2	20.2	4.5	6.6	3.2
Mining	22.7	110.1	121.2	1.7	6.1	80.0	47.4	10.1
Manufacturing	219.0	309.2	343.9	16.7	17.4	30.0	13.0	11.2
Construction	72.7	136.2	153.4	5.6	7.8	28.0	13.9	12.6
Subtotal goods	*645.6*	*941.1*	*1,016.6*	*49.2*	*51.5*	*13.4*	*13.4*	*8.0*
Electricity, gas and water	17.5	26.1	27.8	1.3	1.4	12.7	17.0	6.5
Transport and communications	113.2	146.5	157.1	8.6	8.0	9.8	7.4	7.2
Subtotal basic services	*130.7*	*172.6*	*184.9*	*10.0*	*9.4*	*10.2*	*8.8*	*7.1*
Commerce and finance	168.6	241.3	264.2	12.9	13.4	14.0	10.1	9.5
Government	152.1	156.7	163.0	11.6	8.3	1.5	–	4.0
Ownership of dwellings	100.2	128.8	144.8	7.6	7.3	8.2	9.7	12.4
Miscellaneous services	114.8	170.4	193.4	8.7	9.8	13.3	15.6	13.5
Subtotal other services	*535.7*	*697.2*	*765.4*	*40.8*	*38.7*	*9.4*	*8.8*	*9.8*
Total	*1,312.0*	*1,814.7*	*1,975.5*	*100.0*	*100.0*	*11.5*	*11.2*	*8.9*

SOURCES: 1970-1973: ECLA calculations based on figures supplied by the Central Bank of the Dominican Republic; 1973: ECLA estimates based on data from the same source.

Note: As the individual activities and the totals were calculated independently, the sum of the former does not correspond exactly with the latter.

[a] Preliminary figures.

Figure XLVI. Dominican Republic: growth of gross domestic product
(Annual growth rates)
Natural scale



addition, the internal availability of goods and services expanded faster in the last two years (13 per cent in 1972 and 12 per cent in 1974) as a result of the virtual stagnation of exports in real terms. This increased availability was reflected in a rapid and persistent increase in capital formation and private consumption (see table 256).

Gross fixed investment, which had risen in the first two years of the present decade at the rate of 20.7 per cent as a result of investments in the ferronickel plant and the oil refinery, maintained high growth rates of 18.5 and 15 per cent in 1973 and 1974 respectively, thus bringing about a rapid increase in the investment coefficient, which rose from 16.7 per cent in 1970 to 22 per cent in 1974. The coefficient of public investment increased even more between those years, rising from 5.2 per cent to around 8.8 per cent as a result of an ambitious programme of building up the economic and social infrastructure.

During 1974 there was some slackening in inflationary pressures, which had intensified in 1973. The Dominican economy had shown full price stability up to the beginning of the 1970s, but then prices gradually began to rise, the increase amounting to 7.8 per cent in 1972 and 15.1 per cent in 1973 (comparison of annual averages). In 1974, according to partial information, the increase was 13.8 per cent for the general price index and a little over 16 per cent for the food-stuffs component of this (as against 18.4 per cent for the same component in 1973).

Domestic price rises slackened in 1974 even though the prices of the imports which had such a strong incidence on domestic costs and were the main channel for the transmission of imported inflation increased by around 30 per cent. Fortu-

Table 256. Dominican Republic: total supply and demand

	Millions of pesos at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970–1972*	*1973*	*1974*[a]
Total supply	*1,824.2*	*2,464.9*	*2,718.3*	*123.9*	*122.6*	*10.3*	*11.1*	*10.3*
Imports[b]	352.0	428.7	501.6	23.9	22.6	5.1	10.3	17.0
Gross domestic product	1,472.2	2,036.2	2,216.7	100.0	100.0	11.5	11.2	8.9
Total demand	*1,824.2*	*2,464.9*	*2,718.3*	*123.9*	*122.6*	*10.3*	*11.1*	*10.3*
Exports[b]	255.9	355.4	351.1	17.4	15.8	17.4	0.7	−1.2
Domestic demand	1,568.3	2,109.5	2,367.2	106.5	106.8	9.1	13.0	12.2
Gross fixed investment	245.9	424.5	488.5	16.7	22.0	20.7	18.5	15.0
Public	76.1	163.4	196.1	5.2	8.8	34.6	18.5	20.0
Private	169.8	261.1	292.4	11.5	13.2	13.9	18.5	12.0
Construction	147.0	283.6	...	10.0	...	25.8	21.8	...
Machinery and equipment	98.9	140.9	...	6.7	...	12.6	12.4	...
Total consumption[c]	1,322.4	1,685.0	1,878.7	89.8	84.8	6.8	11.7	11.5
General government	172.0	158.9	165.3	11.7	7.5	−4.9	2.1	4.0
Private[c]	1,150.4	1,526.1	1,713.4	78.1	77.3	8.4	12.8	12.3

SOURCES: 1970–1973: ECLA calculations based on figures supplied by the Central Bank of Ecuador; 1974: ECLA estimates based on data from the same source.

Note: The figures for exports and imports of goods and services were taken from balance-of-payments data expressed in dollars at current prices, which were converted to constant 1970 values by deflation, using price indexes calculated by ECLA for the purpose.

[a] Preliminary figures.

[b] Goods and services, excluding factor payments.

[c] Including increase in stocks.

nately, there were other factors operating in the opposite direction. Thus, the means of payment, which expanded by 20 per cent in 1973, were scarcely any higher at the end of October 1974 than in the previous December.

The country's international reserves, which had grown continually since 1971, dropped somewhat in 1974 because part of them was used to help to finance the considerable deficit of 183 million SDR units on the balance-of-payments current account. This reduction of reserves had the effect of a contraction in the means of payment.

Furthermore, the expansion of 34 per cent shown by domestic credit as at October 1974 (22 per cent in 1973) was partially compensated by the increase of 52 per cent recorded over the same period by savings and time deposits, which thus constitutes another form of contraction of monetary liquidity. It may be noted that in 1974 credit to the private sector (70 per cent of domestic credit) rose by October by 39 per cent, while credit to the Government rose by 21 per cent.

In addition, the better supply of imported consumer goods and food-stuffs during the year helped to compensate the rigidity in the domestic supply of some products and the effect that this would have had on prices.

2. AGRICULTURAL PRODUCTION IN 1974

Agricultural production increased by only a little over 3 per cent in 1974. This is only half the figure for the year before, and it is also lower than the average increase for the period 1970–1972.

This result is explained by the drop in the output of four important products: rice, which dropped by around 15 per cent; maize, which dropped by a third; peanuts, 7 per cent down, and tobacco, which fell by 10 per cent. In addition, there were only slight increases in the output of the remaining agricultural and livestock products.

The drop in the output of two such basic elements of domestic consumption as rice and maize, which was due to unfavourable weather conditions, made it necessary to import 63,000 tons of rice and around 70,000 tons of maize, as well as other products which are normally imported such as wheat (around 120,000 tons) and edible oils.

The 1974 production of sugar-cane, which is estimated at around 10,500,000 tons, was slightly higher than the harvest of the year before. A contributory factor in this was probably the larger area cultivated under the expansion plan, but even so the increase in production was less than

expected because of the drought which affected the eastern part of the country.

The 1973-1974 coffee harvest was a good one, amounting to about 7 per cent more than the season before. The production of cocoa, which rose by 14 per cent, was also good, although it was far from matching the 1971-1972 harvest of 41,500 tons.

As regards livestock production, there was an increase in the commercial production of beef, although beef sales abroad fell by around 10 per cent, thus resulting in a significant increase in domestic consumption. Poultry production also increased, in this case by 9 per cent, as a result of the high prices prevailing.

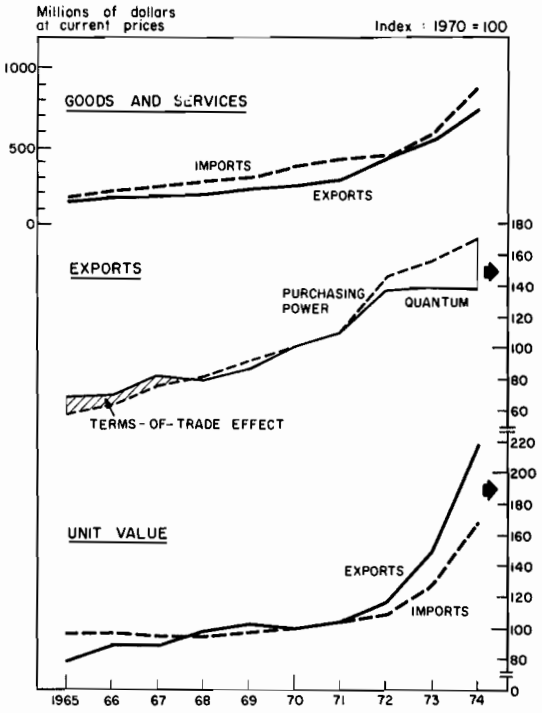
3. THE EXTERNAL SECTOR

In 1974 exports of goods increased by 45.8 per cent, largely as a result of the high prices attained by sugar. Coming as it did on top of the increases recorded in the two previous years, this meant that total exports rose from 243 million dollars in 1971 to 650 million in 1974, this increase being explained by a 110 per cent rise in prices and a 27 per cent increase in volume (see figure XLVII).

In 1974 the increase in exports was attributable solely to higher prices, since the volume actually showed a slight drop. Most of the increase (about 72 per cent) was due to sugar, sales of which increased in value by around 70 per cent as a result of higher world prices: the actual volume exported is believed to have remained close to a little over 1 million tons.

As regards the other products, the value of exports of cocoa increased by 125 per cent, while that of tobacco exports rose by 28 per cent. Sales of minerals (ferronickel and bauxite) are believed to have increased by approximately 10 per cent,

Figure XLVII. Dominican Republic: trend of external variables
Natural scale



but coffee exports, like those of meat, are believed to have gone down (see table 257). Meat exports dropped by approximately 10 per cent to about 9,000 tons in 1974, and they will continue to go down in 1975, since the United States has allotted the Dominican Republic a quota equivalent to 5,670 tons of deboned meat under its import restrictions programme.

There was a bigger increase in imports of goods in 1974 than in the last year or two, since they

Table 257. Dominican Republic: structure of exports
(Millions of dollars)

	1971	*1972*	*1973*	*1974*[a]
Sugar and sugar products	139.2	175.6	205.2	347.9
Ferronickel	0.5	47.0	83.5	92.0
Bauxite	16.0	14.9	14.8	20.4
Coffee	23.8	29.7	46.4	44.8
Tobacco	20.7	28.5	29.5	37.9
Cocoa	12.9	15.9	19.5	44.0
Meat	3.0	6.7	10.1	9.2
Other agricultural products	...	...	9.2	11.8
Other industrial products	...	...	30.0	42.0
Total exports	*243.0*	*347.4*	*448.2*	*650.0*

SOURCE: *Boletín de comercio exterior* and data from the Dominican Foreign Trade Centre and the Central Bank.
[a] Preliminary figures.

rose by 56.7 per cent. In 1972 and 1973 they had increased less than exports, so that the trade surplus of 20 million dollars recorded in 1973 turned into a deficit of a similar amount by the end of 1974.

Unlike exports, the volume of imports increased by about 20 per cent, while the unit value rose by 30 per cent.

An important factor in the increase in imports, apart from their higher prices, was the high degree of dependence of Dominican economic activity on imports of raw materials, capital goods, fuel and food-stuffs, which is reflected in a high coefficient of elasticity of imports with respect to the product. It is estimated that imports of food-stuffs in 1974 came to some 130 million dollars: food imports by the Instituto de Estabilización de Precios (INESPRE) alone came to 100 million dollars, which was double the figure for 1973.

The 1974 increase in imports was facilitated by the greater availability of foreign exchange coming from exports. Thus, the purchasing power of exports rose by 8.3 per cent as a result of the favourable terms of trade, and a further contribution was made by the increased flow of foreign loans and investments.

The deficit on the trade in goods was aggravated by that on services, which was 66 per cent greater than the year before, and by bigger payments of profits and interest abroad, the total result being a balance-of-payments current account deficit of 183 million SDR units—2.2 times higher than in 1973 (see table 258).

During 1974, there was an unusually large flow of non-compensatory capital which left a net balance of 171 million SDR units—70 per cent more than in 1973, and sufficient to finance imports for more than three months. Even so, this

Table 258. Dominican Republic: balance of payments
(Millions of SDR units)

	1970	*1971*	*1972*	*1973*	*1974*[a]
Current account					
Exports of goods and services	255.9	292.2	378.2	431.2	610.1
Goods FOB	213.2	243.0	320.0	371.6	540.5
Services	42.7	49.2	58.2	59.6	69.6
Transport	9.3	10.5	11.3	11.3	13.7
Travel	16.4	21.4	30.3	31.9	36.1
Imports of goods and services	364.5	406.9	404.1	474.5	725.2
Goods FOB	278.0	311.1	311.0	354.6	557.1
Services	86.5	95.8	93.1	119.9	168.1
Transport	40.7	47.5	47.2	59.5	89.8
Travel	37.0	36.5	34.5	43.4	58.2
Net external investment income	−25.9	−28.8	−43.2	−64.6	−89.7
Profits	−18.4	−19.5	−32.6	−50.4	−73.6
Interest	−7.5	−9.3	−10.6	−14.2	−16.1
Net private transfer payments	8.5	21.1	26.7	24.2	22.0
Balance on current account	−126.0	−122.4	−42.4	−83.7	−182.8
Capital account					
Net external financing ($a + b + c + d + e$)	126.0	122.4	42.4	83.7	182.8
(*a*) Net external non-compensatory capital	97.6	118.4	88.3	66.2	
Direct investment	58.4	50.0	41.2	28.6	
Long- and medium-term loans	55.0	54.4	71.1	41.1	
Amortization payments	−23.1	−16.6	−17.2	−14.1	
Short-term liabilities	6.5	29.3	−8.3	9.2	171.4
Official transfer payments	0.8	1.3	1.5	1.4	
(*b*) Domestic non-compensatory capital or assets	20.3	20.0	19.5	10.0	
(*c*) Errors and omissions	0.9	−6.6	−43.7	23.1	
(*d*) Allocation of SDRs	5.4	4.6	4.6	–	–
(*e*) Net compensatory financing (increase –)	1.8	−14.0	−26.3	−15.6	11.4
Balance-of-payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	22.7	39.3	31.5	29.0	...
Amortization payments	−23.5	−33.8	−55.1	−21.8	...
Movements of foreign exchange reserves (increase –)	5.4	−19.5	4.2	−12.1	...
Movements of gold reserves (increase –)	−2.8	–	–	−10.7	...
SDRs (increase –)	–	–	−6.9	–	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26. [a] Estimates based on official statistics.

net inflow of capital was less than the current account deficit, and it was therefore necessary to make use of external compensatory financing and draw on international reserves to the extent of 11.4 million SDR units—something which it had not been necessary to do since 1970.

TRINIDAD AND TOBAGO

1. RECENT ECONOMIC TRENDS

The basic event which gave impetus to the country's economic activity in 1974, in particular in connexion with external trade, was the exceptional increase of 208 per cent in the value of exports (which increased from 714 to 2,200 million dollars), and the increase of 139 per cent in imports mainly as a result of the high international prices of petroleum and other export products (see figure XLVIII).

The increase in the gross domestic product was tentatively estimated at around 50 per cent for 1974, expressed in current prices, and would appear to be greater than that of the previous year (19 per cent) since it does not take into account the price increase which took place in the meantime (see table 259). This increase in the product, however, reflects to a large extent the effect of the higher prices used to evaluate production, since although the volume of petroleum produced increased by 12 per cent, in refining there was a drop in the quantity processed; agriculture also recorded unsatisfactory results in terms of volume of output (where data are available), while industry did no better. This situation is in line with the information that employment levels showed no change in the course of the year while the unemployment rate, estimated at 17 per cent of the labour force, continues to be a major problem.

Figure XLVIII. Trinidad and Tobago: trend of external variables
Natural scale

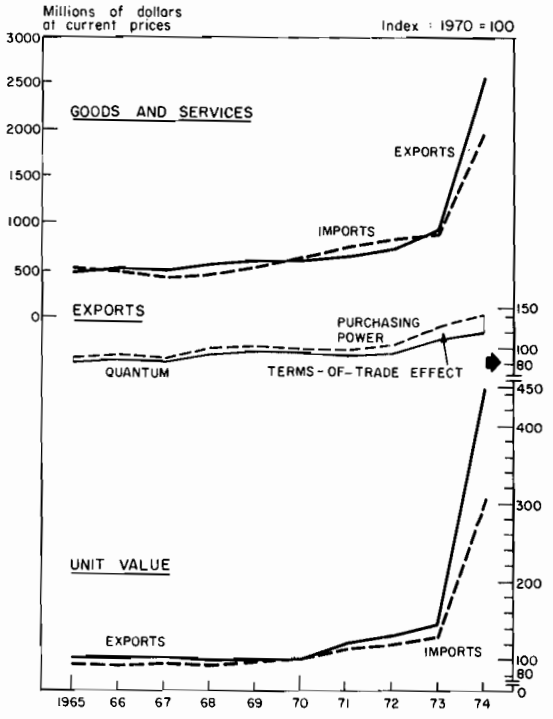


Table 259. Trinidad and Tobago: gross domestic product at factor cost

	Millions of TT dollars (at current prices)			*Annual growth rate*		
	1971	*1973*	*1974*[a]	*1972*	*1973*	*1974*
Agriculture, forestry, fishing and quarrying	130.0	118.5	179.0	3.4	−11.9	51.1
Mining and refining of petroleum, asphalt and gas	349.0	530.0	1,198.0	10.6	37.3	126.0
Manufacturing	333.0	419.0	487.0	10.8	13.6	16.2
Construction	89.0	124.5	166.0	19.1	17.5	33.3
Transport and commerce	321.0	408.0	539.0	8.1	17.6	32.1
Government	218.0	294.0	400.0	15.5	16.8	36.1
Public utilities	93.5	115.0		9.6	12.2	
Ownership of dwellings	64.5		543.0	11.6		17.0
Banking and finance	67.0	349.0		22.4	22.9	
Other services	111.5			16.6		
Total	*1,776.5*	*2,358.0*	*3,512.0*	*11.5*	*19.0*	*49.0*

SOURCE: Government of Trinidad and Tobago, *Draft Third Five-Year Plan*, 1969-1973; and ECLA estimates.

[a] Provisional ECLA estimates.

Another feature of the evolution of the economy in 1974 was the speed of growth of domestic prices, as a result of the high prices paid for imported goods–which are of considerable importance in expenditure on consumption and investment–and the decrease apparently recorded in the production of some standard consumer goods. As from 1972 the rate of growth of consumer prices may be observed to have increased (9.3 per cent in 1972, 14.8 per cent in 1973 and 32 per cent in 1974), mainly in food items.

In the face of the rise in domestic prices, public sector remunerations were readjusted by between 25 and 35 per cent, and those of some groups of private sector wage earners by even larger percentages. The minimum labourer's wage, however, was only increased by 10 per cent in May 1974.

2. MAJOR SECTORS OF ACTIVITY

Petroleum production, including refining, increased its relative share of the total product at current prices from 23 per cent in 1973 to 34 per cent. Production of crude increased by around 12 per cent (to 68 million barrels); this increase came exclusively from marine deposits which at present account for 72 per cent of the total, and whose share is increasing. In addition, in 1974 the output of natural gas continued to increase.

Despite the increased output of crude, petroleum brought in for refining decreased by 8 per cent, reflecting the drop of 7.2 per cent in imports of petroleum for refining in Trinidad and Tobago.

Agricultural output, which accounts for slightly over 5 per cent of the total product and which has rapidly been losing importance, had relatively unfavourable results in the course of the year (according to partial data available), and continued to be affected by the serious drought of 1973 and the crop destruction caused by the storms at the end of 1974. In addition, the sugar industry had labour problems at the beginning of the year. In the circumstances, with the exception of output of cocoa and citrus fruit to a major extent (fruit and juices), which recovered from a sharp drop in 1973, other products, generally speaking, recorded decreases or little change. Up to September, sugarcane had decreased slightly, coffee production (January-June) had decreased by 30 per cent. There were also decreases in meat (beef and pork), eggs, milk, fish, etc. Poultry breeding was one of the few activities in which there was a comeback in 1974.

Partial indicators available for volumes of output of some important manufactures generally speaking showed decreases which in some cases were fairly noteworthy. Up to August, motor-vehicle assembly industries recorded a drop of 42 per cent in output; the production of gas cookers dropped by 30 per cent while the production of the industries assembling radio and television sets decreased by 16 per cent. During the same period, however, the assembly of refrigerators increased by 8 per cent. On the other hand, fertilizer output dropped by 11 per cent up to August and no increases were recorded in the production of textiles or clothing.

Construction activity also declined in 1974, affected by the high cost of construction due to increases in the prices of materials (around 30 per cent) and the costs of labour in that sector. In addition, there were restrictions on the granting of mortgage loans and the rate of interest increased considerably.

Other indicators of the downturn in this activity may be found in the reduction of the area approved for the construction of buildings (during the period January-September) and in the decrease in production and sales of cement (10 per cent in the case of production and 6 per cent in the case of sales), bricks and other materials.

The total expenditure of the government sector increased considerably in 1974 (91 per cent). The majority of these resources were directed towards construction projects in progress. although current expenditure also increased, owing to the increase in remunerations paid by the sector.

3. THE EXTERNAL SECTOR

The partial data available on external trade operations give an idea of the growth explosion in this sector. Between 1973 and 1974 it is estimated that the value of exports of goods increased from 714 to 2,200 million dollars (United States) while the value of imports increased from 712 to 1,700 million dollars.

In 1973, imports of crude for refining in Trinidad and Tobago and related products accounted for 51 per cent of total imports, while in the case of exports their share was 82 per cent. With the considerable increase in international prices of these products which took place in the meanwhile, the share of imports increased to 71.5 per cent of total imports in the first nine months of 1974, although the volume of imported crude decreased, while exports of these commodities increased their value to 90 per cent of the total value of exports during the same period.

The decisive importance of petroleum in both the flows of external transactions and the rapid increase in its price–in addition to that of other goods–go almost all the way to explaining the

considerable increase in the value of exports (208 per cent) and of imports (134 per cent) in 1974. There was practically no change in the volume in the case of exports while the increase in that of imports was only 1.9 per cent.

Petroleum and its associated products dominated the changes which took place in the structure of external trade in 1974. Other goods, mainly food-stuffs, chemicals and manufactures, among imports, and food and chemical products among exports, also recorded important increases in value, although in terms of volume they apparently showed little variation.

The appreciable difference between increases in exports and imports, which showed up during 1974 resulted in a large positive trade balance (of 415 million SDR units); this was much higher than in previous years and despite higher expenditure on freight and insurance and remittances of profits and interests, for the first time in the present decade it allowed the current account of the balance of payments to close with a surplus of 291 million SDR units, which in view of a rather smaller outflow of non-compensatory capital, resulted in a substantial increase of 283 million SDR units in net international reserves (see table 260).

Table 260. Trinidad and Tobago: balance of payments
(Millions of SDR units)

	1970	*1971*	*1972*	*1973*	*1974*[a]
Current account					
Exports of goods and services	591.3	652.7	668.2	783.3	2,146.8
Goods FOB	502.0	529.7	548.3	592.1	1,829.2
Services	89.3	123.0	119.9	191.2	317.6
Transport	57.7	79.1	67.6	82.1	182.9
Travel	21.6	32.9	38.6	48.7	59.9
Imports of goods and services	606.9	726.6	751.9	726.0	1,642.1
Goods FOB	486.9	589.0	636.2	590.5	1,413.5
Services	120.0	137.0	115.7	135.5	228.6
Transport	74.0	88.8	86.4	81.7	162.1
Travel	22.9	24.0	25.0	19.5	24.9
Net external investment income	−75.5	−61.1	−61.5	−71.6	−212.0
Profits	−76.7	−62.5	−61.8	−70.5	−225.3
Interest	1.2	1.4	0.3	−1.1	13.3
Net private transfer payments	2.3	2.1	2.1	−1.8	−1.7
Balance on current account	−88.8	−132.9	−143.1	−16.1	291.0
Capital account					
Net external financing ($a + b + c + d + e$)	88.8	132.9	143.1	16.1	−291.0
(a) Net external non-compensatory capital	60.2	90.5	95.3	53.8	
Direct investment	75.0	80.1	81.0	26.2	
Long- and medium-term loans	3.8	19.6	22.4	27.7	
Amortization payments	−9.8	−5.6	−3.5	−4.0	
Short-term liabilities	−4.6	2.8	0.9	9.7	−7.6
Official transfer payments	−4.2	−6.4	−5.5	−5.8	
(b) Domestic non-compensatory capital or assets	−2.3	5.1	6.8	2.9	
(c) Errors and omissions	12.2	52.4	22.3	−54.1	
(d) Allocation of SDRs	7.4	6.7	6.7	–	–
(e) Net compensatory financing (increase −)	11.3	−21.8	12.0	13.5	−283.4
Balance of payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	–	–	–	–	...
Amortization payments	–	–	–	–	...
Movements of foreign exchange reserves (increase −)	15.6	−15.1	12.1	6.7	...
Movements of gold reserves (increase −)	−3.8	–	–	6.6	...
SDRs (increase −)	−0.5	−6.7	−0.1	0.2	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26. [a] Estimates based on official statistics.

URUGUAY[64]

1. GENERAL FEATURES OF RECENT ECONOMIC TRENDS

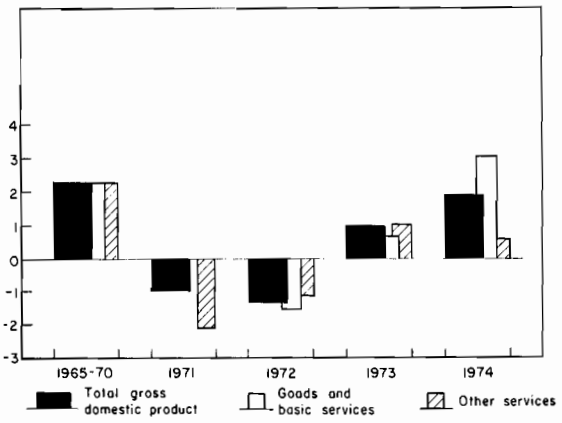
Following a period of virtual stagnation economic activity recovered slightly during 1974. The gross domestic product increased by 1.9 per cent, a rate which although small exceeded the growth rate of the population (estimated at 1.2 per cent), signifying an upturn compared with the 1.2 per cent per year drop in the growth rate which occurred in the period 1970-1972, and the 1 per cent increase in 1973 (see table 261 and figure XLIX).

The recovery in manufacturing, construction and in transport services underlie the performance of the global product; on the other hand agricultural production increased by just about 0.8 per cent, the production of beef having remained at the same level as in the previous year.

The over-all supply of goods and services increased at a rate higher than that of the GDP, because the volume of imports of goods and services increased by 8.2 per cent. On the global demand side there were increases in the volume of exports of goods and services and in consumption. On the other hand, a further drop in capital formation—added to those observed in 1972 and 1973—resulted in an investment coefficient, with reference to the GDP, of 10.4 per cent, a figure which is considerably lower than that usually found in a developing country with a *per capita* income similar to that of Uruguay (see table 262).

In the external sector the situation worsened compared with that of 1973, mainly as a result of the sharp increase in the unit value of imports of goods (57 per cent) which was much higher than

Figure XLIX. Uruguay: growth of gross domestic product
(Annual growth rates)
Natural scale



[64] See, in Part One of this *Survey*, the section dealing with Uruguay in the chapter on inflation.

Table 261. Uruguay: gross domestic product at factor cost, by sector of economic activity

	Millions of pesos at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970-1972*	*1973*	*1974*[a]
Agriculture	67,164	66,072	66,600	12.6	12.5	-2.3	3.1	0.8
Mining	b	b	b	b	b	b	b	b
Manufacturing[b]	128,760	125,477	129,995	24.2	24.4	-1.1	-0.4	3.6
Construction	20,182	22,075	24,084	3.8	4.5	5.7	-2.0	9.1
Subtotal goods	216,106	213,624	220,679	40.6	41.5	-0.8	0.5	3.3
Electricity, gas and water	7,919	9,123	8,749	1.5	1.6	4.6	5.0	-4.1
Transport and communications	45,496	44,193	45,917	8.6	8.6	-1.8	0.6	3.9
Subtotal basic services	*53,415*	*53,316*	*54,666*	*10.1*	*10.2*	*-0.8*	*1.4*	*2.5*
Commerce and finance	91,603	84,952	87,201	17.2	16.3	-4.2	1.2	2.6
Government	76,734			14.4		-1.1		
Ownership of dwellings	27,436	170,982	170,263	5.2	32.0	1.5	0.7	-0.4
Miscellaneous services	66,336			12.5		0.1		
Subtotal other services	*262,109*	*255,934*	*257,464*	*49.3*	*48.3*	*-1.6*	*0.9*	*0.6*
Total	*531,630*	*524,593*	*534,560*	*100.0*	*100.0*	*-1.2*	*1.0*	*1.9*

SOURCES: 1970-1973: ECLA calculations based on figures supplied by the Central Bank of Uruguay; 1974: ECLA estimates based on official data.

Note: As the individual activities and the totals were calculated independently, the sum of the former does not correspond exactly with the latter.

[a] Preliminary figures.

[b] Mining included in manufacturing.

Table 262. Uruguay: total supply and demand

	Millions of pesos at 1970 prices			Structure (percentages)		Annual growth rate (percentages)		
	1970	1973	1974[a]	1970	1973	1970-1972	1973	1974[a]
Total supply	*688,716*	*670,090*	*686,958*	*112.5*	*110.9*	*-2.2*	*1.8*	*2.5*
Imports	76,562	65,974	71,364	12.5	10.9	-11.2	9.4	8.2
Gross domestic product	612,154	604,116	615,594	100.0	100.0	-1.2	1.0	1.9
Total demand	*688,716*	*670,090*	*686,958*	*112.5*	*110.9*	*-2.2*	*1.8*	*2.5*
Exports	71,636	59,285	64,547	11.7	9.8	-4.1[b]	-9.9	8.9
Domestic demand	617,080	610,805	622,411	100.8	101.1	-2.0	3.1	1.9
Gross domestic investment	70,030	64,363	64,041	11.4	10.7	-2.7	-3.0	-0.5
Gross fixed investment	68,478	55,001	...	11.2	9.1	-8.2	-4.6	...
Public	...	...	...	...	...	...	...	...
Private	...	...	...	...	...	...	...	...
Construction	40,416	44,738	...	6.6	7.4	6.7	-2.7	...
Machinery and equipment	28,062	10,263	...	4.6	1.7	-35.4	-12.3	...
Total consumption	547,050	546,442	558,370	89.4	90.4	-1.9	3.8	2.2
General government	92,117	83,461	83,211	15.0	13.8	-6.4	3.4	-0.3
Private	454,933	462,981	475,159	74.4	76.6	-1.0	3.9	2.6

SOURCES: 1970-1973: ECLA calculations based on figures supplied by the Central Bank of Uruguay; 1974: ECLA estimates based on data from the same source.

Note: The figures for exports and imports of goods and services were taken from balance-of-payments data expressed in dollars at current prices, which were converted to constant 1970 values by deflation, using price indexes calculated by ECLA for the purpose.

[a] Preliminary figures.

[b] The figure for 1972 does not include a special sale of non-monetary gold.

the increase in the unit value of exports (7 per cent). There was, therefore, a relatively high deficit in the current account, which had to be financed by foreign loans and international reserves.

The inflationary process stepped up its pace, for the consumer price index recorded an increase of 107.3 per cent between December 1973 and December 1974 compared with an increase of 77.5 per cent for the previous 12 months. However, the indicator of real wages showed a slight reduction of about 1 per cent.

2. MAJOR SECTORS OF ACTIVITY

The agricultural sector grew by a little less than 1 per cent as a result of an increase of 3 per cent in crop farming and stagnation in stock raising. Among the agricultural products the best results were shown by wheat, rice, barley and sugar beet, whereas there were reductions in sunflower, flax, and sorghum cultivation; among animal products there were moderate increases in the production of wool and milk, which were offset by a drop in poultry, eggs, and lamb and mutton production, whereas beef production remained unchanged.

Manufacturing activity increased by 3.5 per cent after three consecutive years in which production had declined. Products which recorded substantial increases were food-stuffs, rubber, chemicals, petroleum, coal, and non-metallic mineral products. On the other hand, the relative changes in the production of other goods were small, except for metal manufactures where production fell by 10 per cent (see table 263).

The increase in construction activity, a little higher than 9 per cent, was brought about by the strong recovery of this activity in the public sector.

Table 263. Uruguay: changes in manufacturing production in 1974

ISIC	Industry	Percentage variation
20.	Food	7.4
21.	Beverages	0.5
22.	Tobacco	-0.6
23.	Textiles	1.9
24.	Clothing and footwear	2.3
27/28.	Paper, printing, publishing and related industries	-5.6
30.	Rubber	24.7
31.	Chemicals and chemical products	4.4
32.	Petroleum and coal products	4.7
33.	Non-metallic mineral products	7.7
35.	Metal manufactures	-10.5
37.	Manufacture and repair of electrical machinery	-2.3
	Total	*3.5*

SOURCE: Central Bank of Uruguay.

In turn, the improvement recorded in transport and communications was linked to the performance of the goods-producing sector which was relatively better than in 1973.

3. THE EXTERNAL SECTOR

Exports of goods and services increased by 13 per cent, expressed in SDR units, mainly as a result of the increase of 5 per cent in the volume of exports of goods, and an increase of 7 per cent in their unit value (see figure L). The international price of wool fell, and problems were also encountered in finding markets for exportable surpluses. However, the international price of beef rose slightly, but sales to the European Common Market were blocked after the month of July. A considerable part of the surpluses resulting from this was sold to Brazil. Non-traditional exports continued to grow rapidly.

Imports of goods and services increased by 55 per cent and those of goods, taken separately, by 69 per cent. This increase was the result of increases of almost 8 per cent in the volume imported and of 57 per cent in the unit value of imports. The strong upswing in average prices which had to be paid by the country for its imports reflects the effects of the rise in the international prices of oil and oil products, and the impact of world inflation on raw materials in general, intermediate products and final products imported into the country.

The shift described in trade, and the trends shown by other items in the current account, resulted in a change in this account from a surplus of SDR 15 million in 1973 to a deficit of 119 million in 1974. This deficit was financed through

Table 264. Uruguay: balance of payments
(Millions of SDR units)

	1970	*1971*	*1972*	*1973*	*1974*[a]
Current account					
Exports of goods and services	290.0	252.7	286.4	339.8	385.1
Goods FOB	224.1	196.8	222.9	271.6	307.7
Services	65.9	55.9	63.5	68.2	77.4
Transport	8.0	5.1	8.2	9.9	11.8
Travel	42.6	39.9	41.3	36.0	43.2
Imports of goods and services	319.6	302.9	257.5	303.8	470.9
Goods FOB	203.1	203.0	164.6	206.1	348.9
Services	116.5	99.9	92.9	97.7	122.0
Transport	50.2	46.6	38.5	39.1	61.3
Travel	45.0	34.8	37.2	36.6	33.3
Net external investment income	−24.8	−21.6	−21.7	−20.8	−32.8
Profits	−1.7	–	–	–	–
Interest	−23.1	−21.6	−21.7	−20.8	−32.8
Net private transfer payments	−0.9	−0.6	−0.2	−0.1	–
Balance on current account	−55.3	−72.4	7.0	15.1	−118.6
Capital account					
Net external financing (*a* + *b* + *c* + *d* + *e*)	55.3	72.4	−7.0	−15.1	118.6
(*a*) Net external non-compensatory capital	23.7	83.1	62.6	39.3	
Direct investment	–	–	–	–	
Long- and medium-term loans	26.0	57.0	53.8	26.2	
Amortization payments	−17.1	−19.3	−22.5	−39.2	71.0
Short-term liabilities	4.6	36.5	20.7	36.5	
Official transfer payments	10.2	8.9	10.6	15.8	
(*b*) Domestic non-compensatory capital or assets	17.9	−2.6	0.5	−21.3	
(*c*) Errors and omissions	−27.5	−44.8	−51.0	−68.4	
(*d*) Allocation of SDRs	9.2	7.4	7.3	–	–
(*e*) Net compensatory financing (increase −)	32.0	29.3	−26.4	35.3	47.6
Balance-of-payments loans, trade arrears, IMF loans and other liabilities of the monetary authorities	62.0	36.7	56.0	41.0	...
Amortization payments	−42.9	−15.0	−5.6	−70.5	...
Movements of foreign exchange reserves (increase −)	13.1	−6.1	−92.5	54.5	...
Movements of gold reserves (increase −)	−0.1	13.6	23.4	12.3	...
SDRs (increase −)	−0.1	0.1	−7.7	−2.0	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26.

[a] Estimates based on official statistics.

Figure L. Uruguay: trend of external variables
Natural scale

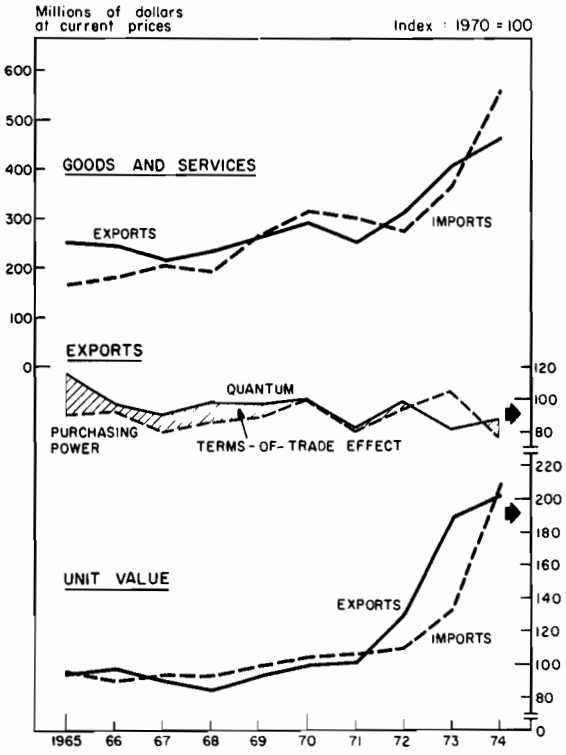
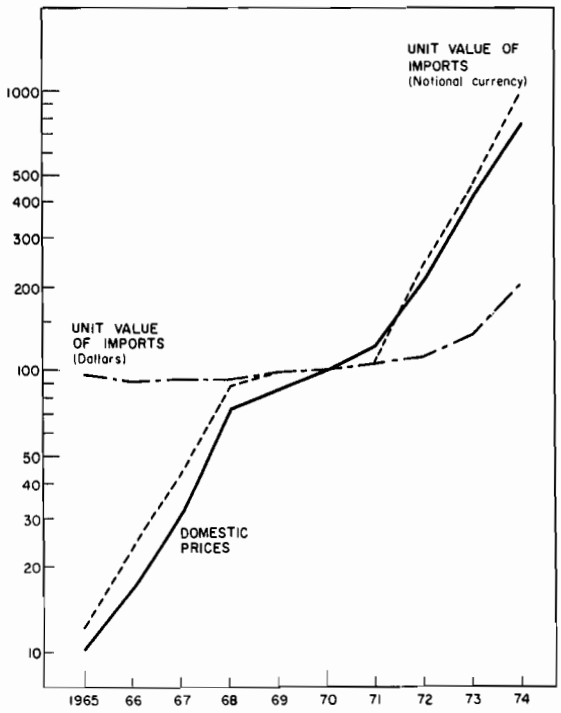


Figure LI. Uruguay: indexes of unit value of imports and of domestic prices
(Index: 1970 = 100)
Semi-logarithmic scale



a net entry of non-compensatory capital of SDR 71 million, and a net use of compensatory reserves—including those obtained from the IMF Oil Facility and the use of international reserves—in the amount of 48 million (see table 264).

4. Trends in prices and other variables linked with the inflationary process[65]

The acceleration in the rate of price increases, particularly during the second half of the year[66] was influenced by the import of world inflation, the impact of which was transmitted, in the main, through the increase in the unit value of imports (see trends shown in figure LI). The import of inflation was made easier by the economic policy of gradually bringing the domestic prices of goods into line with those prevailing for similar goods in international markets, which has been followed since 1972. Government finances also contributed to the acceleration of inflation since the central government's over-all deficit increased by approximately 250 per cent as a result of a more rapid growth in total expenditure, compared with current income. To cover this deficit, the Treasury had to borrow from the monetary authorities the amount of approximately 100,000 million pesos during the year.

In turn, domestic credit in the monetary system expanded by 440,000 million pesos (86 per cent higher than the figure at the end of 1973). This factor exercised a decisive influence on the increase of 62 per cent in the quantity of money, although the net loss of international reserves which occurred during the year acted as a restrictive factor (see table 265).

There were also other important factors which had an effect on price trends.

First, a new rent law was introduced in August, establishing a system for the adjustment of rent contracts which had lapsed, on the basis of the value of readjustable mortgage units.

Secondly, during the year, the exchange policy of mini-devaluations of the national currency, which began in 1972, continued to be applied. Between December 1973 and December 1974 the value of the dollar in pesos applicable to commer-

[65] In Part One of this *Economic Survey* a special section deals with the review of Uruguayan inflation.

[66] As was pointed out, consumer prices increased by 107.3 per cent between December 1973 and December 1974, and by 77.5 per cent during the previous 12 months; nevertheless, rises between annual averages show a variation of 77.2 per cent in 1974 and 97 per cent in 1973.

Table 265. Uruguay: price trends, and fiscal and monetary variables
(*Percentages*)

	1973		1974[a]	
	December to December	*Between annual averages*	*December to December*	*Between annual averages*
1. *Consumer price index*	77.5	97.0	107.3	77.2
2. *Central government finances*				
(*a*) Current income	–	120.9	–	63.7
(*b*) Total expenditure	–	103.8	–	80.8
(*c*) Total deficit	–	13.8	–	255.2
3. *Monetary trends*				
(*a*) Money	74.5	–	62.2	–
(*b*) Domestic credit	51.3	–	86.0	–

SOURCE: ECLA, on the basis of official statistics.
[a] Estimates.

cial transactions[67] increased by 70 per cent, but the rate of devaluation during the second half of the year was twice as fast as during the first half.

Thirdly, the compensatory adjustments in wages made during the year acted as another means of propagating the upward pressure on prices. Nominal adjustments were 74.6 per cent for the general wage index, which corresponded to 72.6 per cent in the public sector and 76.4 per cent in the private sector. In real terms, this meant—compared with the previous year—reductions of 0.9 per cent in the general index and 2.6 per cent in the public sector, and an increase of 0.6 per cent in the private sector.

[67] Side by side with the so-called commercial market, the financial market continued to operate. In September the latter was expanded and restrictions removed, leaving the prices of foreign currency to be fixed by the free play of supply and demand.

VENEZUELA

1. GENERAL TRENDS

Venezuela is one of the major oil-exporting countries in the world and, as a result, since 1973 its economy has been subject to special conditions which differentiate it from the remainder of Latin America. In 1974 its gross domestic product increased by 5.1 per cent, the decision to extend the life of its petroleum reserves by reducing present production exercised a strong influence on this growth rate. For the remainder of the economy rates somewhat better than or similar to those of 1973 prevailed, except in the construction sector, where the growth rate fell considerably.

Needless to say, the external sector performed favourably in 1974. However, it is possible to point out that it increased domestic savings substantially, that there were no geographical restrictions on spending, and that it raised the potential and size of savings to a level which outstripped that of investment possibilities. This imbalance between savings and investment, which also occurs in the other OPEC countries, provides ample scope for an intensive and wide-ranging development policy, as well as one for projecting financial operations beyond its frontiers. These are the general aspects and characteristics of the policy adopted in 1974.

These conditions do not make the Venezuelan economy immune from the impact of world inflation which affects all of Latin America. Domestic prices were also subject to upward pressures due, initially, to the higher unit cost of imported goods and, subsequently, of goods and services produced in the country. The creation of job opportunities is not rapid enough to offset the depressive effect of higher prices on domestic demand, and the reduction of employment in the construction sector. Venezuelan economic policy seeks to correct these imbalances through certain price subsidies and higher investment in low-cost housing (see table 266).

Table 266. Venezuela: total supply and demand

	Millions of bolívares at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1973*	*1970–1972*	*1973*	*1974*[a]
Total supply	*62,372*	*71,072*	*77,369*	*119.9*	*120.9*	*4.1*	*5.1*	*8.9*
Imports	10,364	12,271	15,569	19.9	20.9	8.2	1.2	26.9
Gross domestic product	52,008	58,801	61,800	100.0	100.0	3.3	5.9	5.1
Total demand	*62,372*	*71,072*	*77,369*	*119.9*	*120.9*	*4.1*	*5.1*	*8.9*
Exports	13,115	12,556	11,119	25.2	21.4	–5.1	6.4	–11.4
Domestic demand	49,257	58,516	66,250	94.7	99.5	6.5	4.8	13.2
Gross domestic investment	14,415	19,209	...	27.7	32.7	9.4	11.3	...
Gross fixed investment	11,325	17,014	...	21.8	28.9	14.0	15.5	...
Public	3,013	5,870	...	5.8	10.0	29.3	16.5	...
Private	8,312	11,140	...	16.0	18.9	8.0	15.0	...
Total consumption	34,842	39,307	...	67.0	66.8	5.2	1.9	...
General government	6,889	7,477	...	13.2	12.7	5.2	–2.0	...
Private	27,953	31,830	...	53.8	54.1	5.2	2.9	...

SOURCES: 1970–1973: ECLA calculations based on figures supplied by the Central Bank of Venezuela; 1974: ECLA estimates based on data from CORDIPLAN.

[a] Preliminary figures.

2. GENERAL GUIDELINES OF ECONOMIC POLICY IN 1974

The most outstanding aspects of economic policy adopted in 1974 are related to agricultural development, manufacturing, the nationalization of basic export commodities, and the internal and external financial reorganization of the economy. The latter, of course, includes the modifications that are being introduced in government income and expenditure.

(a) *Agricultural development*

During 1974 a series of measures was adopted which sought to provide incentives for agricultural development. Efforts were made to correct the imbalances caused in the sector by the previous price policy and, at the same time, to exercise a favourable influence on the levels of sectoral employment, the income of farmers and, lastly, national supplies.

The process of rationalizing agricultural prices began, in keeping with a strategy which takes account of the level of wages and employment; tax exemptions were also established for farmers, and a law for the reconversion, consolidation, and remission of their debts was enacted. An important feature of financial policy was the establishment of a fund of 2,000 million bolívares for agricultural development.

(b) *Industrial development*

In the industrial field the following strategic objectives were set: (*a*) the optimum use of basic natural resources; (*b*) the specialized integration of the industrial system as a whole; (*c*) the improved geographical spread of the sector; and (*d*) the creation of exporting capacity in manufactured products.

In connexion with the first aspect, emphasis has been placed on the development of basic metal industries and petrochemicals, for which Venezuela has a favourable combination of resources. In the third quarter of 1974 the sheet-rolling mill of the company Siderurgia del Orinoco (SIDOR), which has an annual capacity of 1.5 million metric tons, began production. In 1974 SIDOR also accepted the offer to set up two pelletization units with a joint annual capacity of 6 million tons, at an investment cost of 630 million bolívares; and two direct reduction plants, with a joint capacity of 718,000 tons which are being installed at an investment cost of 260 million bolívares. The two reduction plants will probably begin operations towards the end of 1976.

Other projects are also under study, among them the installation in the State of Zulia of an iron and steel plant with a capacity of 5 million tons, to take advantage of the coal in that region; another for special steels, and several others, all of which will be incorporated in the National Iron and Steel Plan which envisages a production of 10 million tons in 1980.

As regards the basic metals industries, the production of aluminium is of some importance. In 1974 the expanded ALCASA plant, with a capacity of 50,000 tons per year, began operations and work has started on increasing its capacity to

120,000 tons. The Industria Venezolana de Aluminio C.A. (VENALUM) was also set up, in which 80 per cent of the capital is held by nationals, and the remainder by Japanese investors. Production capacity will be 280,000 tons and is intended mainly for international markets. Investment cost will amount to some 2,000 million bolívares.

As regards petrochemicals, an attempt is being made to overcome the technical problems which have cropped up in some sections of the El Tablazo Complex. A national petrochemical plan has also been prepared, which provides for the construction of five major industrial complexes located in different areas of the country.

In order to improve the integration of industry as a whole, the second stage of the plan for the development of the automobile industry has been prepared. This is to be launched at the beginning of 1976. The aim is for 70 per cent of the value to be made up of national parts by 1980, the present use of simple parts, which in 1974 already account for a third of the value, being extended to include mechanical units and complex parts. To achieve this it will be necessary to limit the number of models and types, and set up a centralized smelting works and workshops. Estimates for the implementation of such an ambitious programme put investment costs at approximately 2,500 million bolívares and it will create 30,000 new jobs. The policy for the integration of industry as a whole includes the manufacture of capital goods, such as transport equipment, and equipment for construction, agriculture, mining, and industry.

As far as industrial location is concerned, co-ordinating machinery has been set up for locating new industry in accordance with a decentralization guideline. The installation of new large industries in the metropolitan area has been prohibited; the infrastructure of several centres in the interior of the country has been strengthened and tax holidays have been offered to enterprises which set themselves up in these centres.

(c) *Nationalization of primary products*

The policy for recovering and conserving basic non-renewable resources has high priority. Hydrocarbons, iron ore, coal, forestry and water resources are included.

The Reversion Committee[68] is studying the implications of the expected reversion to the State of petroleum concessions, the majority of which expire between 1981 and 1985. This Committee drafted a bill for the nationalization of the petroleum industry, which is being revised prior to submission to the national congress, probably during the first half of 1975. Under this bill, the State is expected to take over the assets of the petroleum companies for the equivalent book value, as in the case of the nationalization of the iron-producing enterprises.

At the end of the year Decree No. 580 was enacted, which on 31 December 1974 cancelled all concessions for the exploitation of iron ore, and the State, through the Corporación Venezolana de Guayana (CVG) took over the assets of two United States enterprises which were operating in the sector for the equivalent book value, to be paid in quarterly instalments over a period of 10 years subject to an annual interest ceiling of 7 per cent.[69]

The CVG, under its mandate, entered into operation and technical assistance contracts, as well as contracts to supply iron ore, with the United States enterprises.[70]

Separately, the CVG acquired 51 per cent of the registered capital of the reduction plant and the briquette-producing plant of the Orinoco Mining Company, which began operations in 1973 but was unable to use all its installed capacity of 1 million tons per year, owing to technical problems. The nationalization of iron ore and the simultaneous development of the iron and steel industry will enable Venezuela to substitute exports of steel and steel products for its exports of ore. Conditions prevailing in the international market favour this objective.

(d) *Financial reorganization*

During 1974 financial policy covered aspects as varied as the need to rationalize the use of the abundant resources accruing from the petroleum surpluses, the transformation of the entire financial system, the reform of the Venezeulan Central Bank, the financing of economic development, government financing, and the granting of external financial aid, particularly to the countries of the region.

The financial strategy is based on the rational use of the funds available for accelerating the

[68] Established by Decree No. 10, of 22 March 1974.

[69] The net book value as at 30 June 1974 was 409.8 million bolívares (97.6 million dollars) in the case of the Orinoco Mining Company, a subsidiary of the United States Steel Company, and 68.7 million bolívares in the case of the Iron Mines Company of Venezuela, a subsidiary of Bethlehem Steel Corporation.

[70] The operation and technical assistance contracts shall remain in force until 31 December 1975, and those for the supply of ore until 1979 in the case of Bethlehem Steel, and for a period of 7 years in the case of United Steel.

economic and social development of the country; for ensuring the recovery of basic resources; for stimulating Latin American integration; and for the external recycling of the monetary income which is not being put to immediate use.

(i) *The Venezuela Investment Fund.* The purpose of the Investment Fund is to complement the financing of the expansion and diversification of the economic structure of the country, taking up profitable investments abroad, in assets which are likely to maintain their value, and the development of international financial co-operation programmes.[71]

The fund will operate so that it will be able to maintain the purchasing power of its resources while earning a given rate of profit and will gradually inject these resources into the domestic economy, in keeping with its capacity to absorb them productively.

To this end, a budget allocation of 13,000 million bolívares was earmarked for the Fund, an amount which is equal to 50 per cent of special fiscal revenue from the petroleum sector. In subsequent years, a similar contribution will be made from government funds.

(ii) *Development financing.* Parallel with the Investment Fund, the Agricultural Credit Fund, Industrial Credit Fund and Urban Development Fund were created, each with a capital of 2,000 million bolívares, to stimulate the corresponding sectors. For industrial financing the Development Corporation for Small and Medium-scale Industry was also set up, with an initial capital of 400 million bolívares. Measures have also been taken to make financial action more flexible, and to promote the Venezuelan Development Corporation, and additional funds have been granted to Regional Development Corporations.

Attempts have been made to promote non-traditional exports through the enactment of laws which provide export incentives, and the law which set up the Export Finance Fund. Fifty million bolívares were set aside for the latter, and the former received government credit in the amount of 45 million bolívares.

Another noteworthy measure is the co-ordination of the funds set aside under the special budgetary provision, which will make it possible to use public investment funds to greater advantage.

The foregoing measures are expected to have a strong impact on production and investment. Of course, this implies the increased mobility of financial resources which could eventually change the present system of sectoral financing.

[71] Decree No. 151 of 11 June 1974, Article 2.

(iii) *International financial co-operation.* Recently Venezuela formulated a policy of financial aid to help the countries of the region to develop their natural resources. This policy is aimed mainly at favouring the relatively less developed countries.

In the short term, Venezuelan financial aid attempts to relieve the pressures on the balance of payments which the oil-importing countries suffer, and to recycle the monetary income which is not being put to immediate use in order to reduce the pressures on the economy. In keeping with this policy bonds worth 500 million dollars were purchased from the World Bank, and a contribution of 540 million dollars was made to the Oil Facility of the International Monetary Fund. In addition a grant of 40 million dollars was made to the United Nations Emergency Fund.

In the long term, the intention is to promote Latin American integration and recover for the countries of the continent control of their natural resources. In line with this policy trust funds were set up in integrating financial institutions and in the Inter-American Development Bank.[72] These funds have been granted to strengthen integration projects and institutions, which offer better conditions to the relatively developed countries and channel credits towards the development of natural resources. They offer the possibility of promoting Latin American multinational enterprises which will serve both to recover the wealth of the region and to ensure the economic integration of the Latin American countries.

Venezuela has also undertaken to provide financial assistance to the Central American countries through bilateral agreements entered into with each one of them. The Central Bank in turn approved a loan of 30 million dollars to the Dominican Republic. Venezuela plans to take up a minority holding in the capital of various multinational enterprises operating in different countries of the region.

3. Economic results in 1974

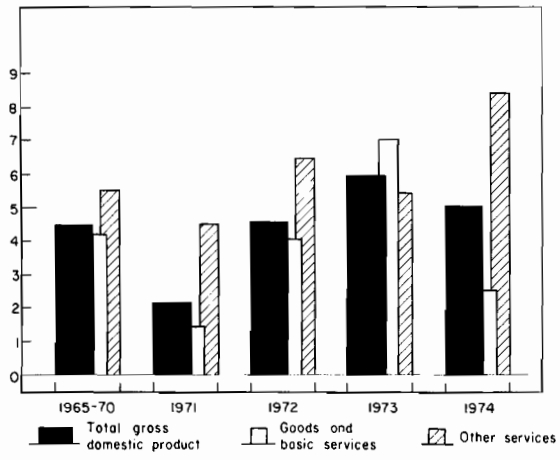
(a) *General considerations*

In order to assess economic trends in Venezuela it is necessary to differentiate between the export performance of the mining sector—hydrocarbons and iron—which decreased by 8.2

[72] The following trust funds are planned: IDB, 600 million dollars in annual contributions of 100 million; CAF (Andean Development Corporation) 60 million dollars; the Caribbean Banks, 25 million dollars; and the Central American Bank for Economic Integration, 40 million dollars.

per cent, and that of the other sectors of the domestic economy, which increased by 8.3 per cent compared with the previous year, in which a strong expansion had already been recorded. The gross domestic product grew on the whole by 5.1 per cent, a rate lower than that recorded in the previous year, but slightly higher than that of the previous 5 years (see table 267 and figure LII).

Figure LII. Venezuela: growth of gross domestic product
(Annual growth rates)
Natural scale



(b) *The mining sector*

The gross domestic product of the mining sector fell by 8.2 per cent compared with the previous year. The product of the petroleum sector–the extraction of crude, and refining–was reduced by 10 per cent in line with the conservationist policy applied by the Government; mining activity experienced a strong expansion of 19 per cent as a result of a significant increase in the production of iron ore and, to a lesser extent, of diamonds and coal.

(i) *Hydrocarbons.* A drop in the demand for petroleum in the industrialized countries, and the substantial increase in the prices of this product constituted the background to the introduction, by several of the producer countries, of varied policies for conserving their basic resources, either by reducing the rate of growth of production, or cutting back on present levels of production. In 1974, Venezuela cut back its production of crude petroleum by 11.6 per cent compared with that of the previous year. Average daily production fell from 3,260,510 barrels to 2,976,251 barrels, a trend which continued into 1975. The average is expected to fluctuate around 2,800,000 barrels and if necessary to fall to 2,600,000 barrels.[73]

[73] Statements made by the Minister of Mines and Hydrocarbons, *El Universal*, 16 January 1975.

Table 267. Venezuela: gross domestic product at factor cost, by sector of economic activity

	Millions of bolívares at 1970 prices			*Structure (percentages)*		*Annual growth rate (percentages)*		
	1970	*1973*	*1974*[a]	*1970*	*1974*[a]	*1970-1972*	*1973*	*1974*[a]
Agriculture	3,738	3,997	4,265	7.6	7.2	0.5	5.8	6.7
Mining (including petroleum)	11,475	10,751	9,869	23.4	16.7	–6.3	6.7	–8.2
Mining (excluding petroleum)	644	681	810	1.4	1.4	–7.6	24.0	19.0
Petroleum[b]	10,831	10,069	9,058	22.0	15.3	–6.2	5.8	–10.0
Manufacturing	5,653	7,104	7,800	11.5	13.2	8.0	7.7	9.8
Construction	1,985	3,219	3,309	4.0	5.6	21.0	10.8	2.8
Subtotal goods	*22,851*	*25,071*	*25,243*	*46.5*	*42.7*	*1.1*	*7.4*	*0.7*
Electricity, gas and water	829	1,084	1,192	1.7	2.0	8.6	10.9	10.0
Transport and communications	5,144	6,374	6,922	10.5	11.7	8.5	5.2	8.6
Subtotal basic services	*5,973*	*7,458*	*8,114*	*12.2*	*13.7*	*8.5*	*6.0*	*8.8*
Commerce and finance	6,663	7,651	8,324	13.6	14.1	4.6	5.0	8.8
Government	5,769	6,766		11.7		6.1	4.2	
Ownership of dwellings	5,181	6,095	17,500	10.5	29.7	5.7	5.4	8.2
Miscellaneous services	2,723	3,313		5.5		5.9	8.6	
Subtotal other services	*20,336*	*23,825*	*25,824*	*41.4*	*43.6*	*5.5*	*5.4*	*8.4*
Total	*49,160*	*55,581*	*58,416*	*100.0*	*100.0*	*3.3*	*5.9*	*5.1*

SOURCES: 1970–1973: ECLA calculations based on figures supplied by the Central Bank of Venezuela; 1974: ECLA estimates based on data from CORDIPLAN.

Note: As the individual activities and the totals were calculated independently, the sum of the former does not correspond exactly with the latter.

[a] Preliminary figures.

[b] Including all petroleum activities.

The production of petroleum products and natural gas also experienced a drop of 7.1 and 5.5 per cent respectively.

Another important aspect of the petroleum industry is the policy aimed at modifying the refining patterns which have so far been designed mainly to produce heavy products that were used to complement United States production, which is geared mainly to the production of light fuels. In 1974 the proportion of such fuels from refineries in Venezuela amounted to 15.6 per cent.

On the other hand, during 1974 better use was made of natural gas, the volume flared off being reduced from 14,619 million cubic metres in 1973 to 9,974 million cubic metres in 1974, 21.4 per cent of total production. The Ministry of Mines and Hydrocarbons has decided to make full use in the years ahead of up to 98 per cent of economically recoverable gas, thereby reaffirming the policy of conserving this natural non-renewable resource and using it for industrial purposes, particularly for the production of petrochemical products.

Government income from royalties increased from 3,653 million bolívares to 9,787 million (167.9 per cent), and taxes on petroleum companies' earnings increased from 9,341 million bolívares to 28,730 million (207.6 per cent) (see table 268).

In 1974, net earnings of petroleum companies amounted to 2,269 million bolívares, a figure 15 per cent lower than that of 1973. This was the result of the effects of Decree No. 440 of 1 October 1974, which increased the rate of taxation on earnings to 63.5 per cent.

Lastly, expenditure on salaries and wages increased by 6.1 per cent, and other operational costs by 15.2 per cent.

On 31 December 1974 proven recoverable petroleum reserves in concession areas amounted to 18,568 million barrels, which means an increase of 34.43 per cent compared with the previous year. This is due to the valorization of certain reserves which, owing to the increase in prices, are now considered recoverable.

(ii) *Iron.* In 1974 the production of iron ore reached its highest level ever of 27.7 million metric tons, which represented an increase of 20.4 per cent compared with the previous year (see table 269).

The volume of exports of iron ore increased by 19.4 per cent. Their value increased from 167 million dollars to 259 million, that is, by 55.1 per cent. During 1974 increases in the prices of the

Table 268. Venezuela: financial results of the operations of the petroleum industry
(Millions of bolívares)

	1971	*1972*	*1973*	*1974*[a]
Income	*13,720*	*13,566*	*19,855*	*45,354*
Exports[b]	12,815	12,573	18,784	44,527
Petroleum	8,403	8,132	11,586	27,899
Refined products	4,272	4,219	6,746	15,485
Liquefied gas	140	222	452	1,143
Sales within the country	905	993	1,071	827
Petroleum	4	9	35	–
Refined products	756	826	852	636
Gas	145	158	184	191
Costs and expenditure	*6,820*	*6,742*	*7,849*	*14,355*
Wages and salaries	1,100	1,153	1,296	1,379
Depreciation, amortization, and depletion	1,160	1,104	1,075	1,027
Losses resulting from writing off assets[c]	51	36	4	–
Other operational expenditure	1,644	1,668	1,792	2,065
Royalties	2,828	2,752	3,653	9,787
Various taxes[d]	37	29	29	41
Pre-tax profit[e]	*6,900*	*6,824*	*12,006*	*30,999*
Income tax[f]	4,653	5,558	9,341	28,730
Net profit	2,247	1,266	2,665	2,269

SOURCE: Ministry of Mines and Hydrocarbons.
[a] Preliminary figures.
[b] Income based on actual prices.
[c] Covers losses incurred in writing off assets (obsolescence, poor condition, etc.).
[d] Including municipal and national taxes, except income tax.
[e] Income tax.
[f] From 1971 onwards, at export values.

Table 269. Venezuela: indicators of iron ore production
(Millions of metric tons)

Year	*Production*	*Exports*	*Reserves*
1970	22.1	21.1	1.923
1971	20.2	19.1	1.901
1972	18.5	16.5	1.882
1973	23.0	21.5	1.859
1974[a]	27.7	25.5	1.831

SOURCE: Ministry of Mines and Hydrocarbons, Office of Mining Economics.
[a] Provisional figures.

mineral were in the region of 25 per cent.[74] Under a joint resolution adopted by the Ministries of Finance and of Mines and Hydrocarbons, minimum export prices for iron ore are to be fixed towards the end of the year, and will remain in force during 1975. These prices represent increases of approximately 45 per cent for "fine" quality ores and by 35 per cent for "lump" ores, compared with 1974 prices.

(c) *The domestic economy*

In 1974 the sectors which direct their supply preferably towards the domestic market recorded, on the whole, a highly satisfactory rate of growth of 8.3 per cent. However, the results of the different sectors varied somewhat (see table 267).

(i) *Agricultural sector.* During 1974 the agricultural sector experienced a higher rate of growth than in the previous year, thereby strengthening the tendency towards recovery, for its performance in recent years has been irregular.

The items which showed the highest increase in the year were mainly sugar-cane, maize, sorghum, cotton, potatoes, milk, pork, poultry, shellfish and timber. On the other hand there was a drop in the production of coffee, sesame and eggs.

In spite of the high levels of production achieved in 1974 the external dependence on several food products continued, such as cereals, oilseeds, and others. The years ahead hold a number of opportunities for the substitution of the majority of these imports.

(ii) *Manufacturing industry*. In 1974 the manufacturing industry grew by 9.8 per cent, a rate higher than that recorded in previous years of the present decade, with the exception of 1970, when it increased by 10 per cent.

[74] In January the price per metric ton increased from 42.15 bolívares to 42.20 bolívares, and at the end of the same month rose to 42.46 bolívares under the Joint Resolution adopted by the Ministries of Finance, and of Mines and Hydrocarbons. On 9 March it rose to 43.03 bolívares, and on 2 April to 44.89 bolívares.

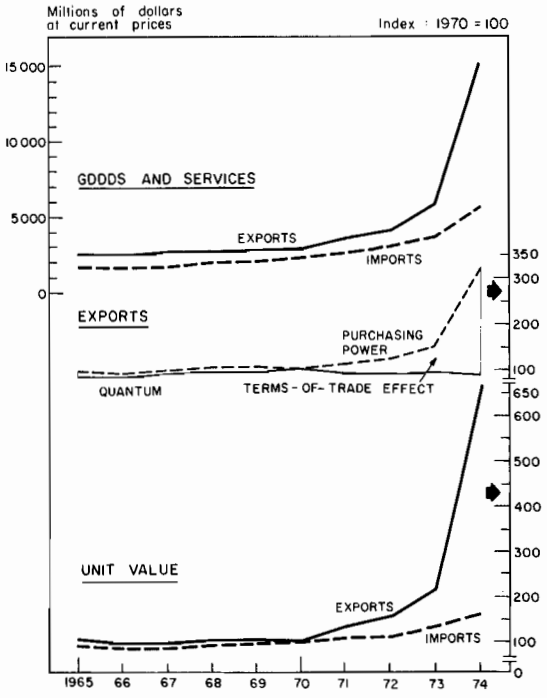
The engineering sectors showed the highest rate of growth, an over-all increase of 15.2 per cent. For their part, traditional industries showed a growth rate of 8.7 per cent, and intermediate industries one of 8.6 per cent. The graphic arts and other industries suffered a slight drop in their growth rate.

The increase in the growth of engineering industries was due to a strong expansion in the electrical machinery and electrical equipment sector (28.8 per cent), and in the transport equipment sector (21.4 per cent). The production of motor vehicles was in the region of 120,000 units.

In the traditional industries the sectors of food-stuffs, tobacco, textiles, and skins and hides recorded the highest increases in response to an increase in demand during 1974 brought about by adjustments in wages and salaries.

In the intermediate industries, the greatest growth was experienced by the rubber and rubber products sector (45.2 per cent), owing to an increase in the manufacture of motor vehicles, and basic metals (12.7 per cent). In the third quarter the SIDOR steel-rolling plant came into operation. This and the expansion of the ALCASA aluminium plant which increased its production from 27,690 metric tons in 1973 to 45,595 tons in 1974 were responsible for the increases experienced in these sectors.

Figure LIII. Venezuela: trend of external variables
Natural scale



(iii) *Construction.* After having experienced rates as high as 10.8 per cent in 1973 and even higher ones in the two previous years, construction activity experienced a marked drop in its growth rate in 1974, which fell to 2.8 per cent. Various factors were responsible for this.

There was a contraction in public sector construction as a result of the application of new work guidelines which gave priority to the construction of physical infrastructure for agricultural activities, and the construction of medium-cost or low-cost housing units in an attempt to prevent construction in the metropolitan area, where it had been concentrated in recent years, from being stepped up.

Trends in private construction were irregular throughout the year as a result of the new government construction policy, changes in financing arrangements, and increases in prices of some of the major inputs of domestic origin. However, in the closing months of the year the situation evolved favourably as a result of the greater availability of financial resources, and tax incentives for construction.

(iv) *Basic services.* Electricity, gas, and water services recorded an increase of 10 per cent, maintaining the dynamic trend of previous years, mainly as a result of the increase in the generation of electricity which accompanied the expansion in manufacturing production. As for transport and communication services, they increased their activities by 8.6 per cent.

(v) *Other services.* The over-all product of the different service sectors increased by 8.4 per cent. The financial sector recorded the highest increase as a result of the impulse given to domestic economic activity by a large portion of the financial resources stemming from petroleum,

Table 270. Venezuela: balance of payments
(Millions of SDR units)

	1970	*1971*	*1972*	*1973*	*1974*[a]
Current account					
Exports of goods and services	2,943.0	3,572.0	3,703.0	4,867.0	12,680.0
Goods FOB	2,756.0	3,372.0	3,498.0	4,620.0	12,405.6
Services	187.0	200.0	205.0	247.0	274.4
Transport	59.0	55.0	52.0	61.0	74.0
Travel	50.0	61.0	67.0	99.0	108.9
Imports of goods and services	2,318.0	2,588.0	2,770.0	3,001.0	4,690.4
Goods FOB	1,793.0	1,994.0	2,158.0	2,354.0	3,765.8
Services	525.0	594.0	612.0	647.0	924.6
Transport	238.0	283.0	292.0	343.0	548.8
Travel	140.0	138.0	164.0	161.0	213.7
Net external investment income	−669.0	−874.0	−960.0	−1,401.0	−3,550.5
Profits	−657.0	−858.0	−943.0	−1,402.0	−3,683.5
Interest	−12.0	−16.0	−17.0	1.0	133.0
Net private transfer payments	−86.0	−79.0	−82.0	−87.0	−91.5
Balance on current account	−130.0	31.0	−109.0	378.0	4,347.6
Capital account					
Net external financing (*a* + *b* + *c* + *d* + *e*)	130.0	−31.0	109.0	−378.0	−4,347.6
(*a*) Net external non-compensatory capital	153.0	425.0	216.0	264.0	
Direct investment	−25.0	215.0	53.0	69.0	
Long- and medium-term loans	168.0	260.0	168.0	214.0	
Amortization payments	−34.0	−82.0	−98.0	−114.0	
Short-term liabilities	50.0	36.0	98.0	100.0	−1,020.6
Official transfer payments	−6.0	−4.0	−5.0	−5.0	
(*b*) Domestic non-compensatory capital or assets	−69.0	71.0	−109.0	49.0	
(*c*) Errors and omissions	94.0	−117.0	210.0	−252.0	
(*d*) Allocation of SDRs	42.0	35.0	35.0	–	–
(*e*) Net compensatory financing (increase −)	−90.0	−445.0	−243.0	−439.0	−3,327.0
Balance-of-payments loans, trade errors, IMF loans and other liabilities of the monetary authorities	2.0	7.0	10.0		...
Amortization payments	−5.0	–	–	−2.0	...
Movements of foreign exchange reserves (increase −)	−30.0	−416.0	−218.0	−410.0	...
Movements of gold reserves (increase −)	−9.0	−1.0	–	−38.0	...
SDRs (increase −)	−48.0	−35.0	−35.0	11.0	...

SOURCE: IMF, *Balance of Payments Yearbook*, vol. 26.

[a] Estimates based on official statistics.

and the expansion of credit operations as a result of the sharp rise in imports and the increase in investments in mortgage bonds, among others.

The service sectors were the ones which in the first instance benefited from the favourable impact of the surplus petroleum funds. In productive activities the positive effects of these surplus funds will only be able to be judged from 1975 onwards, for such activities require a longer lead time.

(d) *Balance of payments*

In 1974, the major expansion of exports, 169 per cent measured in SDR terms and, to a rather lesser extent that of imports (60 per cent) resulted in a trade balance 3.8 times higher than that of 1973, which had already shown a marked increase over previous years (see figure LIII). From SDR 1,340 million in 1972 it increased to SDR 2,260 million in 1973 and to SDR 8,640 million in 1974.

Services which had a negative balance also showed a moderate increase, although lower than that of goods, with the result that the current account of the balance of payments closed at the end of 1974 with a surplus of SDR 4,350 million, a figure that bore no relation whatever to that recorded in previous years, and one which in the final analysis meant an increase of SDR 3,327 million in net international reserves, bringing them up to SDR 5,330 million, the highest figure in the history of the country (see table 270).

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