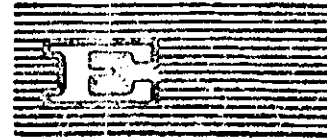


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GENERAL SITUATION AND FUTURE OUTLOOK OF THE CENTRAL  
AMERICAN INTEGRATION PROGRAMME

(Note by the secretariat)



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## I. GENERAL REVIEW OF THE PROGRAMME

### 1. Integration and the economic situation in Central America

In August 1952 the Central American Governments established the Economic Co-operation Committee, which at its first session laid down the principles governing the integration programme. The ECLA secretariat believes that the time has now come, ten years later, to review briefly the results which have been achieved slowly over the intervening period. This review is made for the purpose of providing the Committee with a basis for determining which are the major problems and for formulating the measures needed to consolidate and extend the integration achieved thus far.

The recent accession of the Republic of Costa Rica to the General Treaty and to the other instruments on economic integration means that the coverage of this Treaty is now complete. The participation of Costa Rica, in addition to fulfilling the hopes of all the Central American Governments, also satisfies one of the requirements of integration, namely, to provide an economic market basis sufficient to permit an industrial development that thus far has been lacking or has been barely perceptible in Central America. The common market has at its disposal instruments for action that are highly effective for the purpose not only of accelerating the real integration of the Central American economies, but also of offsetting some of the factors that in recent years have acted unfavourably on the economic situation.

Free trade has opened one new channel for the expansion of productive activity. In addition there is a common tariff built up on the basis of the true situation in the Central American countries, and with a view to development. There are also Central American institutions in the fields of finance, industrial technology, and even teaching and administrative training. The Economic Council, the Executive Council and the permanent secretariat of the General Treaty constitute a solid background for the efficient functioning of the common market and the progress of integration. In addition to these elements, which have grown up as a result of economic /integration and

integration and form part of that integration, there are such favourable factors as the decision of the Central American Governments to undertake the planning of development in their countries in a co-ordinated form and on a regional basis, and the prospect of the immediate initiation of a new stage of intensified public investment and the existence of sources of external financing additional to those that have been available hitherto.

All these three factors constitute effective instruments of economic action, but for an accurate appraisal of their possible effect on the Central American economies they cannot be considered separately. Economic integration, development programming and public investment and its financing, must all be viewed as part of a single mechanism designed to accelerate the region's growth. As with any development effort, this calls for the combined and simultaneous action of all components so as to reap the rewards of this effort, on the basis of common fundamental aims and co-ordinated methods of application.

Side by side with these encouraging features there exist in Central America unfavourable economic conditions that have tended to worsen during the last few years. In other words, it is clear that economic integration has reached a high point in terms of results and prospects, but that the economy as a whole is going through a period of waning activity. The product growth rate is barely enough to offset the population increase, and in some cases is at the moment lower than the population growth rate.

All the foregoing suggests the possibility of bringing into play the instruments already available to the Central American Governments for invigorating the economy by offsetting the effects of the deterioration in the external sector. This cannot be done completely, since the structural features that determine the present situation are firmly built in in the various countries, and could not be changed in the short run. The general objectives of integration can really be attained only gradually, although the rate at which the process is achieved should be modified by the use of the existing political instruments.

Recent experience shows that trade within the Central American countries is relatively independent of the factors that tend to depress

/economic activity

economic activity in general. In the last five years, when the product grew at an annual rate of only 4 per cent, exports within the region increased at an annual average rate of 20 per cent; their value rose from 8.6 million dollars in 1950 to 32.7 million in 1960, making possible a level of economic activity that could not otherwise have been attained.

## 2. The common market as a starting point

The stage of making treaties, and of designing the framework within which the integration of the Central American economies must take place, may be considered virtually completed. Full free trade has been decided on for most products, and for the remainder it has been laid down what are to be the characteristics, time-limits and rates of liberalization to be applied. Thus the common market operates in an automatic way which obviates the need for negotiations or any additional agreements of a general nature. Not only has economic integration been completed from the geographical and institutional standpoint, but it has already attained the operative stage. Yet these results constitute a new starting point rather than the completion of a task.

Since the General Treaty is only of recent application, the effects of the common market have been to enable the five national economic systems to operate more efficiently, rather than to lead to any form of consolidation of these systems. Only a limited improvement can be achieved on the basis of national economies that resort to the common market as a source of possible additional export opportunities. The improvement needed is of a general nature involving a transformation of the existing economic systems, and it cannot be fully achieved if the national forms of production become firmly ensconced. Economic integration, as conceived by the Governments, is not a means for improving five national systems at a low level of development, or a marginal opportunity to enable those systems, while preserving the same features, to mitigate some of the anti-economic features inherent in their structure. The very essence of integration is the fusion of these national economies, on a progressive basis, into what in practice would amount to an economic system of regional scope.

/The existence

The existence of wide disparities as regards basic capital resources and the fund of technical knowledge and savings available is one of the main obstacles to the gradual formation of a regional economic system. What has kept these Central American economies separate in the past is not merely a question of tariff barriers, but is also rooted in the differences between countries as regards, for example, roads and electric power plants, and the lack of links between these facilities at the regional level. Only when such differences have been abolished will the new investment deriving from the common market tend to concentrate in the places that are the most economic from the Central American standpoint. At the same time, the existence of basic facilities that are equally satisfactory throughout the region, and that are linked together, will tend to encourage investments calculated to take advantage of the external economies established within the system.

Until such time as this levelling-up of economic conditions takes place, the investment coefficient will not fully reflect the opportunities and prospects opened up by the Central American common market. Consequently deliberate action is required with a view to stimulating the development of the various activities in the light of the outlook for the region as a whole. In order to achieve this the Central American Governments have decided to undertake the development of their countries by means of co-ordinated programming of economic activity. This implies, in addition to a full programming of public investment, a less extensive planning effort that is nevertheless sufficient to encourage private investment on a regional scale.

The actual integration of economic systems poses its own problems, which do not arise at the level of an individual country. Integration aims exist side by side with national aims. In the next stage of the programme common ground will increasingly be established between these two types of aims, especially in the major economic sectors, and progressively greater effort will be made to ensure that the various national economic bodies carry out their activities in the light of the additional prospects opened up by the common market. For this purpose what is required is not a change in the actual aims of these bodies, but

/a change

a change in their scope of activity. The work of integration should cease to be a task reserved to the regional bodies, and should be shared by the institutions concerned with banking, finance, credit, and agricultural and industrial development, that are operating in each country.

The importance of this evolution, of which the first signs are already to be seen in Central America, nevertheless goes beyond its significance from the short-term economic standpoint. The operative stage that the programme has now reached is, by its very nature, the testing stage for economic integration. Regional action by the national bodies will serve to consolidate and extend the basis of common interest on which the whole integration programme rests through the benefits to be derived by the various member countries. This is hardly a mere matter of arithmetically equal benefits; in the long term the basis of common interest will depend more on how far economic integration can accelerate growth than on any other kind of adjustment. Thus reciprocity will in essence not be a matter of compensations or adjustments, but will take the more permanent form of intensified economic growth in all the member countries.

### 3. The new stage of industrial development

In conjunction with the common market there have also been established, on a permanent basis, strong stimuli to industrial investment, whose effects are already being felt. What remains to be done is to ensure the economic soundness of the new investment, and its appropriateness from the standpoint of an over-all economic unit.

For the very reason that the stimuli provided by the common market are so powerful, it is more than ever imperative to avoid duplication of investment. At the national level such duplication exists in almost all branches of manufacturing, despite the small size of the markets concerned. When these markets are expanded at the regional level, in conjunction with an external tariff that is generally based on development criteria, the opportunity of profitable operation is even greater, despite failure to use installed capacity to the full. Thus anti-economic forms of industrial  
/growth might

growth might be carried over from the national to the regional level, with harmful consequences in the way of waste of resources and virtual absence of any active competition.

The stimuli implicit in the regional scope of the market are essential because they can give rise to intensive activity by private industry leading to changes in economic structure and to specialization. But these incentives could also tend to consolidate existing conditions of inefficiency or to lead to increases in profit levels without any basic improvement in forms of production.

The spirit of enterprise, which is still inadequate but is making itself felt increasingly, may prevent this. Nevertheless, such an important matter should not be subject to any form of uncertainty as to timing or as to the form which this new outlook on the structure and functioning of industry is to take. The agencies of integration can back up the tendency that already exists in the private sector by acting as a springboard for investment on a larger scale and for the renewal and improvement of existing plant. For this purpose the programme has the Central American Research Institute for Industry (ICAITI) and the Central American Bank for Economic Integration to fall back on. Purposive action by these two agencies is only a partial solution to the problem in question, but it is a type of measure that can help to facilitate a changeover in private industrial activity to more economical forms of operation, and that can cause the common market to open the way to expanded and more efficient production.

This function of the financial and technological agencies of the programme cannot be effective if they do not act in close accord. The financial agency cannot fulfil this function if a local or national mentality has been uppermost in the formulation and technical study of the projects submitted to it, and the technological body cannot effectively promote the formulation of economic projects on a regional scale unless there is some likelihood that this type of project will have preference in Central American financing.

The approach indicated seems all the more essential because analysis of regional trade shows that in addition to the considerable stimulus

/provided by

provided by free trade, there must be encouragement of changes in the industrial structure. Thus far there has been a better use of installed capacity, and the new investment in manufacturing has been designed in part for markets wider than the national markets. But generally speaking these first results of the common market might well be reinforced so that, instead of being confined to the products already produced in the region, they would also include new production sectors, especially durable consumer goods, intermediate goods and certain capital goods. Thus the first repercussions of the common market would have a broader base, whereas in regard to the goods produced at present they will tend to lose ground as Central American trade adjusts to the new conditions.

Furthermore, the forces in a market that is suddenly enlarged, as in Central America, encourage a form of import substitution mainly directed towards the items that raise fewer technical problems, and thus promote the development of consumer goods industries and processes involving little working and manufacturing. Consequently industries producing raw materials, and intermediate and capital goods, which are the industries with a real basis for future expansion, tend to be relegated to second place in the investment field. This would restrict the field of specialization and leave out of account one of the main objectives of the programme, namely, the attainment of an industrial structure that is fully integrated and capable of providing the impetus needed for moving ahead to new stages of economic development.

#### 4. Expansion of the market

While the integration programme can of itself promote a radical change in the level of economic activity, it does not yet include elements that would be equally effective in leading to a general improvement in income levels and standards of living.

The expansion of the market already effected is almost entirely due to the total of the separate demands in the five markets. In addition integration has also resulted in an increase in the general purchasing power in all these markets. Here the question is no longer one of raising

/the productivity

the productivity of the system, which is regarded as already improved, but of ensuring that a fair share of the economic benefits obtained from integration shall be transferred to the consumer sectors. In other words, it is a matter of relative prices and incomes. The Committee believes that this effect must be an integral part of the programme's complex of repercussions, since in the absence of this broadening action the stimuli provided by the common market would gradually tend to lose their strength.

Indeed, the present distribution of income in the Central American countries constitutes what is perhaps one of the main obstacles to rapid industrialization of their economies, and to real integration. Being concentrated in certain sectors, and otherwise spread thinly as a result of the low income situation, the market available for manufactured goods is small and does not tend to grow with the same vigour as the economic system in general. The situation thus amounts to the existence of a sector with an income so high that any increases are spent on foreign goods instead of on goods manufactured in the region, while the remaining sector, consisting of the population as a whole, has so little income that its demand does not constitute an active factor, and is concentrated mainly on essential consumer goods. Thus in addition to the economic progress made possible by integration, there must be a structural change in income distribution so as to provide properly staggered points of support for economic growth.

The improvement of income distribution in a region such as Central America, which is mainly agricultural, necessarily involves basic changes in the conditions in which the agricultural sector operates. These conditions include not only those that directly affect efficiency, and thus output, but also those that determine the pattern of the distribution of agricultural income among the various factors of production, above all forms of land tenure. These forms are rooted in the Central American economic systems, and make themselves felt in all activities, from exports to production for domestic consumption. The change or progressive adjustment of these forms in relation to a more dynamic economy of wider scope, like that provided by the common market, is calculated to provide both a link between the two major sectors that are directly productive

/ - agriculture and

- agriculture and industry - and a foundation for their simultaneous development. It should be noted that a problem of interrelations arises here, since the forms of tenure constitute at the same time both the causes and the results of a given stage of development.

Fiscal policy, and public investment policy in the social field, are other factors that may eventually contribute to a more economic pattern of income distribution. The Economic Co-operation Committee has been studying this problem since 1958. At the request of the Governments a United Nations mission has carried out a preliminary study, in collaboration with the Central American universities, of forms of land tenure and their significance for the economy of the region. The results of this study are not yet complete, but they already throw light on some aspects of the problem. Similarly, a detailed study of income distribution in Central America is being undertaken, and a survey is now under way of wages, costs and labour productivity, mainly in relation to manufacturing. Since 1957 the Committee's activity in the housing field has been carried out by the sub-committee established exclusively for this purpose, and its activity has increased during the past year. The composition of the labour force and demographic phenomena have been studied by technical assistance experts. Some of the results obtained are included in Human resources of Central America, Panama and Mexico in 1950-1980, in relation to some aspects of economic development,<sup>1/</sup> of which the Committee took cognizance in 1959. In accordance with the guidelines laid down by the Committee, the ECLA secretariat proposes to intensify its studies in this field, with the collaboration of the Central American universities and of the technical assistance agencies of the United Nations.

Lastly, tax reform is another method of dealing with the immediate problems of income distribution. In the existing circumstances in Central America the tax problem includes more than the question of distribution. Nor can the achievement of tax equalization between the various countries, as an integration requirement, be regarded as the most immediate goal. In this field the Central American Governments have already established

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<sup>1/</sup> ST/TAO/K/LAT/1; E/CN.12/548. United Nations Publication, Sales No.: 60.XIII.1

full equality as regards import duties, and recently, in August 1962, they signed a Central American Agreement on Tax Incentives to Industrial Development, which eliminates the great differences that existed formerly between the five countries with respect both to the actual amount of the exemptions and to the criteria governing their application. Nevertheless there is still room for further progress towards standardization of taxes.

But the aim of tax reform, from the standpoint of the needs of economic integration, must above all be to effect structural and administrative improvements in the tax systems so as to increase their capacity to meet the new public responsibilities deriving from economic integration proper, and consequently from the policy of accelerated development of the five countries.

In 1957 the Economic Co-operation Committee adopted a resolution on this question, relating mainly to differences in taxation directly reflected as differences in the conditions of investment. On the basis of this resolution and of that adopted by the Committee at its fourth special session, what is now called for is a global approach to the problem that would include not only progressive elimination of such differences, but also actual improvement of the tax systems and their adjustment to internal and external changes in the economy, as well as the use of taxation as an instrument for a sound distribution of income.

5. Central American economic unity and its links  
with other countries

The plan for the progressive improvement of the machinery and methods of integration includes the establishment of a customs union between the five countries. Most of the components of this form of economic grouping already exist in Central America, or will exist very shortly by virtue of the General Treaty. Free trade and tariff equalization will be fully fledged within the next three years, and consequently a customs union in the case of Central America must set out to achieve more than can be achieved by the former two methods. It might even go further than the removal of customs barriers and the relevant administrative aspects. The progress made towards the common market will tend to liberate forces

/that must

that must increasingly lead, not merely to a customs union, but, in the longer run, to the economic union of the member countries. This union will have been fully achieved when, in addition to the features that already exist, there is a common basic economic structure with respect to roads, harbour facilities and energy, and when mobility of the factors to production has been achieved which - as the best channel for disseminating the benefits of integration and establishing a permanent basis of solidarity between the five countries.

The economic integration of Central America is already a recognized fact. It is often seen as a point of reference in analysing parallel regional problems, and it is an important factor in the ambition of Latin America to set up a common market. The strengthening of the Central American market as a unit will tend in future to underline economic relations with other countries and the flow of investment. The form and manner of such relations might be the subject of study by the Committee and decisions by the Central American Governments, with a view to helping to determine that form. Just as in recent years there has been established what amounts to an inter-Central American trade policy, it would be possible to work towards the adoption of a foreign trade policy and to increasingly close links with third countries or groups of countries. The Economic Co-operation Committee and the Economic Council of the General Treaty have given consideration to these possible links, and have asked for the necessary studies to be made so that decisions on the question can be taken.

The policy referred to above could be based on the fact that the joint Central American market is not large enough to support certain industrial activities, and on the additional fact that Central America, as is widely known, suffers from a lack of savings and of technical know-how. Thus in the first place the Central American market could be supplemented by that of other countries for the products of certain industrial branches, while at the same time the ground would be prepared for agreements on investment and transfer of technologies that seem appropriate for the new industrial build-up in Central America.

## II. THE INTEGRATION SECTORS

### 1. Free trade

#### (a) The evolution of trade

Integration has advanced on a number of fronts, but its most immediate results are to be found in the field of trade between the Central American countries. During the fifties this trade increased almost fourfold, rising from a total value of 8.6 million dollars in 1950 to 32.7 million in 1960. This increase continued throughout the decade, but there were two distinct periods, one from 1950 to 1955 when growth was slower, at an annual cumulative rate of 8.7 per cent, and the other from 1955 to 1960 when growth accelerated sharply and attained an average annual cumulative rate of 20 per cent.

Together with this dynamic growth rate, the outstanding feature of the practical operation of economic integration during the decade was the independence from the behaviour of the rest of the economic system, particularly the external sector, achieved by the countries of the region in respect of trade among themselves. In fact the accelerated growth rate recorded during the second half of the decade coincided with the crisis in external sector prices, and with a trend towards a standstill in economic development and in exports to the rest of the world. Thus inter-Central American trade, which in 1950 represented less than 3 per cent of all foreign trade, increased by 1960 to a proportion of over 7 per cent.<sup>2/</sup> However, this relative independence is of a somewhat temporary nature, being largely due to the still embryo stage of industrial development and multilateral free trade.

Between 1950 and 1955 one of the main aims of trade treaties between the Central American countries was to facilitate trade in surpluses of domestic products, especially for items of agricultural origin. In 1955-60 the scope of such treaties was enlarged to include a growing number of

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<sup>2/</sup> In 1960 the percentages of the total exports of each country represented by inter-Central American exports were Honduras 12.0; El Salvador 10.8; Nicaragua 6.2; Guatemala 6.1; and Costa Rica 2.3.

/manufacturing products.

manufacturing products. This led to a marked trend towards a change in the composition of regional trade in the form of an increase in the proportion of industrial goods. The mere existence of the economic integration programme, and of the first multilateral treaties, created market expectations in the industrial sector that strengthened the trend towards the export of manufactured goods.

Thus qualitative and structural changes were introduced that made an increase possible in the flow of goods between the five countries. Exports of manufactured goods increased at an annual rate of only 5.2 per cent in 1950-55, whereas in 1955-60 the rate rose to 22.5 per cent. The annual growth rate for non-manufactured goods was the same during both these periods, about 15 per cent.

However, inter-Central American trade still has little effect on industrial productions, of which it represents only 6 per cent. Moreover, of the increases in manufacturing, whose value rose to 70 million dollars for the decade, only 20 per cent represented exports to other countries in the region. Thus the main stimulus to industrial growth was the substitution of imports from the rest of the world, rather than inter-Central American trade.

The new trade openings led mainly to a better use of idle industrial production capacity, and only to a smaller extent to new investment in this sector. This partly explains how regional trade could continue to increase at a time of crisis in the external sector and a tendency towards stagnation in the economy as a whole.

Recently there have been signs of a trend towards a slower rate of expansion of inter-Central American trade. Thus in 1960 the increase recorded was somewhat lower (17 per cent) than the average annual rate for 1955-60. This trend continued in 1961, when total regional trade increased by 14 per cent, and according to the figures for the first half of 1962, appears to have continued in 1962.

This apparent reduction in the growth rate of exports was recorded before the Central American market could feel the effects of the full participation of Nicaragua, beginning in 1961, and of the more recent accession of Costa Rica to the common market. These developments will

/make for

make for a broader geographical distribution of inter-Central American trade in future (as is well known, it has been concentrated in the past in El Salvador, Honduras and Guatemala), and for a considerable increase in the volume of regional trade.

However, the stimulus that will be provided by the functioning of the General Treaty at the Central American level will be offset by a number of unfavourable factors in the demand sphere. Firstly, much of the idle industrial production capacity is already being used. Secondly, the possibilities of substituting imports of articles produced by the traditional industrial branches of the Central American economies have largely been exhausted. The proportion of imports in the total consumption of such articles is low, in general not more than 20 per cent. Even in those industries where the margin of import substitution is broader (as in the textile industry), increased trade and import substitution as the Economic Co-operation Committee has already pointed out, involves programmes of specialization in these activities, and the investment needed to modernize equipment and expand plant. The starting point for maintaining the dynamic growth of inter-Central American trade, and making use of the opportunities opened up by the establishment of the common market, must therefore be the introduction of new activities different from traditional lines, and the general strengthening of production capacity.

A change in this direction was noted during the previous decade. Exports of manufactured goods representing new industrial branches increased from 15,000 dollars in 1950 to about 2 million dollars in 1960, and the proportion of total trade they represent increased from 7 per cent to over 30 per cent.

(b) Improvement of the free-trade system

As already indicated, the measures of the type already felt to be necessary in order to facilitate a freer flow of goods are quite distinct from the formal establishment of free trade. They are a matter of taking steps to adjust certain economic activities to the new competitive conditions of the common market and to the requirements of Central American demand in relation not only to the volume of supply but also to matters

/of quality

of quality and timing of supply. The first question that arises relates to the conditions laid down in the interim régimes to enable certain products to be incorporated into the free trade régime. In the case of these products, which are expressly indicated in the General Treaty, the transition to free trade depends on the signing of multilateral agreements to regulate and co-ordinate national production and supply policies, and on the equalization of the tariffs on the items in question or on the raw materials used in their manufacture. This category includes, for example, agricultural commodities for the domestic market, and some manufactured goods, including petroleum products and textile goods.

A smaller number of items have remained subject to trade restrictions for an indefinite period, and differ from the other products covered by the interim régimes, in that it is not envisaged that they will eventually be incorporated in the free-trade régime. However, this is not a problem relating to the improvement of the common market, but merely a problem affecting the future customs union.

The second type of measure to stimulate trade is the formation of a Central American system of transport and distribution of goods that will be capable of meeting the new requirements. In general the demand for transport services has increased rapidly, whereas the supply necessarily increases at a slower rate. This raises not only the problem of the long-term expansion of basic facilities, but also the more immediate problem of the better organization of existing equipment and installations.

This is a field where the public authorities, and those private sectors that participate in trade movements, can promote or facilitate the establishment of permanent distribution machinery and at the same time tackle the problem of financing regional trade, especially in the short run.

At its fifth session the Economic Co-operation Committee considered several of the aspects referred to, and in resolution 67 (CCE) decided to request the technical assistance agencies of the programme to undertake the necessary studies so that at the appropriate time, conditions could be established in Central America that would be favourable to the development of regular transport services between the various countries. This

/question is

question is discussed in the relevant section of the present study.<sup>3/</sup> As experience in the field of exports between the Central American countries is acquired, more will be learnt about other things that need to be done in Central America to facilitate regional trade and cut down the time and formalities required for trade operations.

The existence in the various Central American countries of special rules and regulations in health and other fields, the lack of uniform and specific criteria governing the origin of goods, and the customs regulations and formalities themselves, all tend to slow down the flow of goods and occasionally result in interruptions to trade. The General Treaty provides for regulations on the origin of goods to clarify the application of article V. This and other supplementary instruments or provisions on economic integration, in such fields as health, quality standards and regional traffic, will be more urgently needed as the common market comes more fully into force, and will be essential for the future institution of a customs union among the five countries.

(c) Relation between the establishment of a customs union and the existing integration treaties

In article I of the General Treaty the Contracting States agree to create a customs union in respect of their territories. From the standpoint of the internationally recognized exceptions to the application of the most-favoured-nation clause, the customs union has been defined as an agreement between States whereby there is freedom of movement of goods originating within the territory, a common tariff applying to the rest of the world, and a unified trade policy between the countries concerned and in respect of third countries.

The features referred to are already included in the Central American common market. Consequently the establishment of the customs union provided for in the General Treaty would consist, for Central America, in the adoption of additional measures; these would comprise mainly the creation of a common customs territory and the abolition of customs frontiers between the countries, the elimination of the requirements with respect to Central American origin for goods subject to a free trade régime,

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<sup>3/</sup> See section 7 (d) below.

/and lastly,

and lastly, the establishment of a central customs administration and the redistribution of tariff revenue among the member countries.

Several of the steps referred to relate to some of the provisions included in the integration treaties already in force. Thus, under the General Treaty, free trade is restricted, during the interim period, for all the products listed in annex A to the Treaty. Once this period comes to an end the products will be automatically incorporated into the free-trade régime, except for specific goods in respect of which the Governments have agreed to restrictions for an indefinite period. For such goods the same tariff treatment will apply as that to which similar goods originating in the rest of the world are subject. The possible adoption of a customs union between the member countries would mean that the existing restrictions would have to be eliminated for as many products as possible, by means of additional agreements. With respect to those goods that for reasons of economic policy must remain subject to trade restrictions, formulas will have to be sought whose application will not involve the maintenance of frontier customs to enforce the restrictions in question. A similar situation arises as regards the products of any industries that are included in the special régime of industrial integration, since such products are subject to special forms of trade.

It should be noted, also in connexion with the relations between a possible customs union and other integration instruments, that the agreement on uniform tax incentives includes an undertaking to establish a special protocol on assembled products governing both the conditions for according exemptions and the trade régime to be applied to such products by the Central American countries. If this régime is different from the general free-trade system, this will constitute an additional question to be resolved before establishing the customs union.

This same agreement establishes national customs exemptions for imports of raw materials, semi-finished goods and capital goods for certain types of industry. The customs union will involve the application on a Central American basis of the customs exemptions granted at the national level, so that the raw materials and semi-finished goods whose imports are exempted from the payment of duty for one country can be brought in free of duty through any Central American customs frontier.

/Similarly, there

Similarly, there will have to be some study of the fiscal effects on the region as a whole, within the common system of collection of customs dues, of the granting of exemptions at the national level in sectors other than those covered by the legislation on standard tax incentives. In fact once the customs union and the common customs collection system have been established, exemptions granted by any of the States will affect not only the total of its own public revenue, but also, indirectly, the revenue of the other member countries.

The ECLA secretariat proposes to investigate further the economic significance for Latin America of the transition from a common market to a full customs union. The foregoing paragraphs give a brief account of some of the pre-requisites for a customs union in relation to the existing integration instruments. Other more general questions also require study. One essential need is to determine what should be the aims of a customs union set up with due regard to the existing conditions in Central America and to the economic policy aims pursued by Governments in relation to the integration of their countries. In this sense the establishment of a customs union will constitute not so much an agreement on trade policy, as a means of achieving a greater degree of integration of the economies, and may include new means of co-ordination in fields other than the strictly commercial sector.

## 2. Tariff equalization

In the last three years the Economic Co-operation Committee, through its Trade Sub-Committee, has built up the main part of what will be the Central American common tariff. In September 1959 the Governments signed the Agreement on the Equalization of Import Duties and Charges; in December 1960 the Managua Protocol to the Agreement on Equalization was signed, and in July 1962 a new protocol on equalization was signed at San Jose, Costa Rica. As a result common duties have been agreed on for 1,213 items, amounting to 95 per cent of the total tariff. The common duties on about half these items are already being applied in four of the countries. There remain 63 tariff items for which standard duties have not yet been agreed on.

The starting point of the equalization process consisted of five separate tariff systems, with marked differences for the same products  
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as regards the rate of duty and even the tariff structure and procedures. Broadly speaking, these tariffs were essentially of a fiscal nature. In this equalization process the Central American Governments sought to achieve, in conjunction with a uniform duties on imports from third countries, a tariff that would promote development and embody a selective policy aimed at changing the composition of imports and facilitating import substitution in the context of an expanding foreign trade.

The provisional results of the studies being undertaken by the ECLA secretariat for the full evaluation and analysis of the uniform tariff and of Central American tariff policy already make possible conclusions as to the nature of the equalized tariff. The ECLA study covered all the uniform duties for tariff items representing imports amounting to 372 million dollars in 1960. Under the equalized tariff the average rate of duty is 48 per cent, or only 6 per cent more than the average for the five national tariffs that existed before. The structure of the new tariff, on the other hand, involves important changes in relation to groups of products.

The percentage of value represented by the average duty is 82.5 per cent for the consumer goods group, 34.4 per cent for raw materials and intermediate goods, 32.2 per cent for building materials, and 13 per cent for capital goods. These first results indicate that, broadly speaking, the tariff constructed is in line with the development criteria that were laid down by the Committee, and are suitable to present conditions in Central America.

The structural change can be realized by comparison with the average incidence for the same groups of products that prevailed in Central America as a whole before equalization. However, full appreciation of the significance of this change will only be possible when the analysis of the standard tariff is applied at the level of individual products and has covered all products. Nevertheless, the average incidence in Central America before equalization was as follows: consumer goods 64 per cent, raw materials and intermediate goods 30 per cent, building materials 26 per cent and capital goods 12 per cent.

/(a) Items

(a) Items awaiting equalization

The 63 items for which uniform duties have not yet been agreed on represent 5 per cent of the total tariff items.<sup>4/</sup> Despite their small number, the items that remain to be equalized are of great significance in relation to the total value of Central American imports from the rest of the world, and as a source of revenue. External purchases of goods for which uniform duties have not yet been established represent about 30 per cent of total imports and 10 per cent of imports from within the region. Thus these are products that, because of the volume of demand and because they are not yet produced in quantity, constitute a heavy foreign trade burden. As regards their revenue significance, provisional data for 1960 indicate that the customs duties paid on imports of these items represent between 27 and 43 per cent, according to the country, of total customs revenue.<sup>5/</sup>

During the process of working out the common tariff repeated efforts have been made to agree on the equalization of the charges on most of the 63 items that are still pending. These efforts have failed for a number of reasons. The great revenue significance of some of these items is perhaps the main reason that has made it difficult to achieve the tariff equalization in question. Thus far it has not been made sufficiently clear what would be the effect of equalization on public revenue, and for products essential to economic activity it has not been determined whether, in conjunction with a protective tariff, other measures should be taken to ensure that Central America's requirements will be fully met as regards quality, quantity and price.

At the request of the Governments the ECLA secretariat has carried out detailed studies on what would be the effects of different tariff rates on consumer prices, regional supplies and public revenue from customs duties. These studies cover a relatively small number of the products that are still pending. For other products additional studies are required,

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<sup>4/</sup> Of these items, about 33 per cent are capital goods, mainly for transport activities, and 28 per cent are fuels and lubricants. The remaining 40 per cent are equally divided between the manufacturing and agricultural sectors, and include raw materials, intermediate goods, containers and finished products.

<sup>5/</sup> The percentage for each country is as follows: Guatemala 43, El Salvador 41, Honduras 38, Costa Rica 28 and Nicaragua 27. The calculation was based on theoretical revenue for Honduras, and on actual revenue for the other countries.

because of their importance and the complexity of the problems involved in tariff equalization for these items.

For the work of equalization that still has to be done, the first results of the application of the standard charges already adopted can be taken into account. This may lead to changes in some of the criteria that have been followed hitherto. For example, there has been a tendency as a general principle to free imports of capital goods from all duty, or to set a maximum rate of 15 per cent. Where a trend can be foreseen towards closer economic links with other countries, through special arrangements, it may be advisable to re-examine these and other principles with the aim of strengthening the economic unity of Central America.

If it proves necessary to introduce such a change in policy, the sector that still remains to be equalized provides an opportunity of doing so. Although as regards non-durable consumer goods, building materials, and capital goods for agriculture and industry almost all products have been equalized, much remains to be done, in terms of value, in equalizing durable consumer goods (67 per cent), fuels and lubricants (100 per cent), and raw materials and intermediate goods (26 per cent).

(b) Flexibility of the tariff

The standard tariff, conceived and formulated as an instrument of development, must respond to the changing needs characteristic of all processes involving growth, especially at a rapid rate. But at the same time there must be regard for the need for a relatively long period to enable the policy recently adopted to be applied and to produce the desired results. Thus one of the main requisites for economic integration at the present stage of the programme is the stability of the tariff.

The procedure for renegotiating the standard duties and charges has been laid down in the Central American Agreement on the Equalization of Import Duties and Charges, article XII of which stipulates that renegotiation shall be at the request of any one of the Contracting Parties, and through the Executive Council of the General Treaty. It further stipulates that the renegotiation shall affect only those goods in respect of which it is applied for, that decisions shall be adopted by the unanimous vote of the States members, and that in any event, every change shall maintain the uniformity of the tariff.

The procedures and methods laid down have been made flexible so that the common tariff will make it possible, from a technical standpoint, to meet future requirements, while at the same time the tariff's basic

/stability is

stability is maintained. The timely application of the Agreement on this subject, and the efficient functioning of the agencies of the General Treaty, would make for a satisfactory solution of the problems that arise.

In any case, any changes that are gradually introduced in the already agreed levels of uniform duties will constitute attempts to improve the structure of the common tariff so that this instrument can help to establish Central American trade with the rest of the world on the most desirable lines, and can be increasingly instrumental in ensuring the balanced development of the region's productive activity.

### 3. Central American customs code

For economic integration there is a standard tariff nomenclature for imports and exports, and a common tariff in which most of the items have already been equalized. It remains to draft and adopt standard tariff legislation that will ensure the proper application of the common tariff, and to unify the customs legislation of the five countries. Tariff legislation will have to be embodied in an agreement that, in accordance with article XX of the protocol on tariff equalization signed at San Jose, must be signed by the Governments no later than one year from the date of entry into force of the said instrument. With respect to the customs legislation, there is a draft standard code prepared by the Working Group of the Trade Sub-Committee which met in Guatemala in 1961. This was prepared in accordance with resolutions 18 (AC/17) and 22 (CCE) of the Economic Co-operation Committee. The drafting took account of the work done between 1954 and 1957 by United Nations technical assistance experts.

The draft code is of a general nature, and includes a provision that it will be supplemented by a body of regulations on specific points. The text provides for common customs arrangements, uniform organization of the national customs offices, and ways and means of co-ordinating them at the regional level.

The first point covers common definitions, terminology, time-limits and procedures in relation to the process of clearing goods through the customs, and in general to all the activity of the customs office. The second covers the concept of a Central American customs service composed of the national customs services, whose functions and form of organization are established on a uniform basis for all the countries. The third point covers procedures for co-ordination of the customs services to

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ensure the maximum of uniformity in applying the existing provisions; it is laid down that if any questions of classification and so forth arise at the national customs level that affect, or might affect, the common market, they must be dealt with on a regional basis.

The establishment of free zones and free ports is to be governed by the provisions of a special Central American agreement on this subject.

The draft customs code in some respects looks ahead towards arrangements that imply the existence of a Central American customs union. This applies, for example, to the definition of the customs frontiers and to the movement of goods from third countries within Central American territory, and also to the rules governing coastal traffic.

A transitional article establishes the national arrangements that are to apply during the interim period with respect to all these cases.

At its fourth special session, held at Tegucigalpa, Honduras, in November 1962, the Committee requested that the study of the draft code at the technical level should be completed by means of a second meeting of customs officials and experts, due to be held during the first quarter of this year. The Committee also decided at this session to consider the revised draft code at a special session in March 1963.

The main point to be decided, as basic guidance for the studies to be made at the technical level, is the scope of the code, that is, whether it is to be conceived merely as an instrument of the common market, or as an instrument that initially will serve the common market, but contains from the outset the additional provisions that will enable it to be applied when the customs union is established.

The draft prepared for the meeting of customs officials in August 1961 was submitted to the Economic Co-operation Committee at its eighth session as a background document. In its present form it can serve as an instrument for unifying the system of customs operations at the regional level, establishing a close co-ordination between the customs services, and at the same time providing a body of uniform provisions of a technical nature on the process of customs clearance.

4. Economic relations between Central America and other countries or groups of countries

Both the Economic Co-operation Committee and its ancillary technical agencies have intimated that they would welcome a series of studies to determine:

- (a) The repercussions on the economic integration of Central America that may possibly be implicit in the multilateral economic co-operation movements currently under way in other parts of the world; and
- (b) Prospects, objectives and instruments for a common Central American trade policy, and ways and means of promoting its formulation and implementation. <sup>6/</sup>

In the course of its third special session, the Economic Co-operation Committee decided to study at an early date "trade relations between Mexico and Central America and, in general, between Central America and the Latin American Free-Trade Association". Similarly, the Central American Economic Council (established under the terms of the General Treaty on Central American Economic Integration), at its first session, held at Managua (Nicaragua) in August 1962, requested that steps be taken to carry out the studies needed for the purposes of considering a Central American trade policy vis-à-vis the rest of the world.

Futhermore, the States signatories of the integration treaties have pledged themselves to support one another in the maintenance of a common position with respect to the formulation of new trade agreements. <sup>7/</sup>

Pursuant to the above-mentioned recommendations, and with the aim of furnishing the Economic Co-operation Committee with preliminary background material on the basis of which to project and systematize its work in this field, the secretariat, in the present note, attempts to give an initial idea of some of the problems associated with the determination of a common Central American economic and trade policy vis-à-vis the rest of the world.

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<sup>6/</sup> See Informe de la Duodécima Reunión del Subcomité de Comercio Centroamericano (E/CN.12/CCE/SC.1/81/Rev.1), and Informe de la Tercera Reunión Extraordinaria del Comité de Cooperación Económica (E/CN.12/CCE/258/Rev.1)

<sup>7/</sup> See Multilateral Treaty on Free Trade and Central American Economic Integration; article XXIV; General Treaty on Central American Economic Integration, articles XXV and XXVIII; and Central American Agreement on the Equalization of Import Duties and Charges, article VII.

Some of the principal foreign trade statistics for Central America are given in document CEE/VIII/DT.2, together with interesting supplementary data on trade balances, terms of trade and purchasing power of exports as from 1950.

Central America's purchases abroad doubled during the fifties. The value of imports rose from 240 million dollars in 1950 to 515 million in 1960. In 1950, 70 per cent of the area's total imports came from the United States, which is still its leading import and export market. Nevertheless, the relative importance of this market steadily declined, until in 1960 it absorbed approximately 50 per cent. Central America's import trade has shifted towards the countries which now form the European Common Market. In 1950 about 15 million dollars' worth of goods were obtained from these sources, whereas today such purchases amount to some 100 million dollars, or 20 per cent of total imports. The relative importance of purchases from Japan climbed from 1 per cent in 1950 to 6 per cent in 1960. The total value of imports from the members of the Latin American Free-Trade Association (ALALC) did not vary during the decade under consideration; these account for only 2 per cent of total imports. <sup>8/</sup>

Central American exports have followed a similar course. Between 1950 and 1960 they increased from 250 to 440 million dollars. The share of the United States dropped from 80 per cent to 48 per cent. The European Common Market countries absorbed 7 per cent of exports in 1950, and about 30 per cent from 1957 onwards. Japan's purchases in 1960 represented 6 per cent of Central America's total exports, whereas during the early years of the preceding decade the corresponding proportion had been barely 1 per cent. The relative importance of the purchases effected by the ALALC countries at no time exceeded 1 per cent. <sup>9/</sup>

Since 1955 Central America has registered persistent trade deficits, which in 1960 amounted to 70 million dollars for the five Central American countries in the aggregate. The only transactions showing favourable balances were those conducted with the European Common Market countries, Japan and Canada, although in this last case again the balance was negative in 1959 and 1960.

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<sup>8/</sup> See CCE/VIII/DT.2, table 1.

<sup>9/</sup> See again CCE/VIII/DT.2, table 2.

The decline observable in the external sector of the Central American economies simultaneously reflects the downward trend in the prices of its staple export commodities and a similarly marked reduction in the rate of expansion of its export volumes. The causes of these phenomena are such that a substantial improvement in the situation as regards exports of traditional commodities can hardly be expected in the immediate future. The terms of trade have also deteriorated. Whereas the prices of the commodities imported by Central America remained fairly stable in 1954-60, the average price of its exports fell by 31 per cent during the same period.

From the foregoing brief résumé of the facts, it can be seen that the improvement of the terms of trade and the prospects of a satisfactory rate of expansion of Central America's total exports will depend not so much upon foreseeable changes in the markets for traditional exports as upon a policy actively directed to the achievement of these ends. Among the possibilities to be studied are those relating to the opening of additional markets in which commodities produced in Central America are in short supply, and which at the same time may be in a position to supply the area with some of the goods that it will not be able to manufacture on the basis of its own market for a comparatively long time.

The need to establish a common Central American foreign trade policy is linked to the key role which the external sector of the economies of the various countries will continue to play in the future. As already pointed out, the relative independence which has recently characterized the growth of Central American trade is in the main a temporary phenomenon.

Furthermore, pursuant to provisions in the General and Multilateral Treaties, the establishment of the Central American common market involved the disappearance of several of the agreements which had previously existed and which had governed the trade relations of the different countries with the rest of the world. Hence arises the need and the occasion to formulate, at the Central American regional level, a unified policy in respect of external economic relations.

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As one of the objectives of a common policy, additional to the opening-up of new export markets, the Governments have endeavoured to facilitate the imports required for the development of the manufacturing sector. This has been reflected in some of the criteria applied in relation to tariff equalization. As this process had advanced, attention has gradually been drawn to the necessity of incorporating in the standard tariff certain elements which may later serve as the cornerstone for a regional policy designed to multiply and strengthen economic ties.

For the purposes of the possible future adoption of a common foreign trade policy, a Central American negotiation unit already exists in the shape of the standard tariff, although there are other aspects of trade policy which have not yet been co-ordinated in Central America. In this connexion, it would be worth while to consider what implications for such a policy might derive from the existence of import quotas or embargoes established at the national level, and systems of exchange controls or restrictions on the use of foreign exchange.

This further stage of co-ordination of certain trade policy instruments once left behind - should it prove needful - stronger ties than already exist should be established with specific countries or groups of countries within the framework of agreements which need not necessarily be confined to trade objectives exclusively. Closer ties presuppose the existence of economic complementarity in relation to the countries with which they are established. Potential complementarity of this kind already exists in respect of several countries which as yet carry on very little trade with Central America. The chief reason for this limited volume of trade is not to be found in the lack of trade agreements, but in more permanent factors affecting freight prospects, and in the absence of any tradition of reciprocal trade among the countries concerned. Consequently, every step in the progressive forging of increased economic links with countries of this type should be accompanied by the establishment of such additional relations in the fields of capital investment and transfer of techniques as may be needed to promote the growth of Central America's export supply.

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As regards the countries or groups of countries with which broader economic relations might be sought, there are various possibilities. One of these is represented by the Latin American Free-Trade Association, and has been suggested for study by the Economic Co-operation Committee and discussed by the Latin American countries at the ninth session of ECLA and other meetings. The secretariat of the Committee, at the request of the Governments, offers some information on this point in the present note.

In relation to a possible rapprochement between Central America and ALALC or any other group of countries, there is a problem of timing. The common market is too recently established for its effects to have been fully demonstrated as yet. It would therefore seem desirable that before the conclusion of economic agreements which would throw it open to goods produced by other countries, a sufficient interval should elapse for adequate trial of the opportunities afforded by the market to the area's own industrial development.

Again, belated entry into an economic group comprising markets which even at the national level are more thriving than that of Central America might entail unduly abrupt economic adjustments. Thus, in the specific case of ALALC, when a country joins the Free-Trade Area, it is granted all the concessions which the members have previously accorded one another, but, as a general rule, it undertakes to grant compensatory concessions in return for those it receives through negotiation and those extended to it by virtue of the most-favoured-nation clause. This suggests the need for exercising the greatest care in timing the establishment of any additional economic tie, either with ALALC or with other economic blocs.

The way to link up with ALALC is by accession to the Montevideo Treaty. The Treaty raises no barrier to the establishment of bilateral relations with one or more of the members of the Area. Under the terms of the instrument in question, accession must be unreserved and would imply acceptance of commitments deriving from the whole juridical pattern of ALALC. In the case of individual arrangements, the concessions granted by a member country to third parties would be extended, by virtue of the most-favoured-nation clause, to the other members of the Association.

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As regards the manner of accession, the only suitable procedure for Central America would be to join the Association as one economic unit, not by means of five separate acts of accession, even if the terms of these were all exactly the same. During the eighth session of ECLA, the Latin American Governments regarded the Central American countries as a single unit when discussing the establishment of a Latin American common market.

There are several points that still remain to be elucidated. Within the integration treaties, no appropriate mechanisms are established for the conduct of negotiations involving commitments for all five countries as a whole. Nor are there any clauses in the Montevideo Treaty which make provision for the accession of groups of countries.

The characteristic features of the Montevideo Treaty include a set of measures designed to encourage the economic growth of countries at a relatively less advanced stage of economic development. Under this special régime, one or several contracting parties may grant another less-developed country exclusive concessions inapplicable to the rest. Similarly, the relatively less-developed country is authorized to implement its trade liberalization programme at a slower rate.

In such circumstances, it might be possible to secure advantages in specific ALALC markets which the latter would not extend to the Area, where, in consequence, important commodities might find a sale. In addition to these benefits, the relevant chapter of the Treaty commits the contracting parties, up to a point, to facilitate financial and technical assistance to less-developed members.

With reference to the commitments that Central America would assume in acceding to ALALC, the Montevideo Treaty, since it makes no provisions for the accession of groups of countries, also fails to define whether the minimum annual tariff reduction of 8 per cent which members are obliged to grant would be calculated for each individual country or would be computed on the basis of Central America's total exports.

The foregoing considerations relate primarily to the patterns and methods of possible accession in the future. Other problems of more vital significance call for analysis. Among them should be mentioned the fact

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that the liberalization programme and any steps which the ALALC countries may progressively decide to take towards the integration of their economies may have repercussions on their economic policy, whereby, in turn, their foreign trade policy may be affected.

Another point to be considered is whether Central America's accession to ALALC would restrict its freedom to establish a trade policy in relation to other countries or groups of countries. In this connexion, the Montevideo Treaty does not prohibit its signatories from granting third countries tariff preferences or advantages, provided that such advantages are extended to the Area.

The situations outlined call for detailed studies of the impact which the expansion of Central America's relations with specific areas or countries might have upon its integration; but at the same time, the problems adversely affecting its external sector need to be tackled by means of a common trade policy. An initial step in this direction might take the form of closer contact and a better understanding between the organs of the General Treaty on Central American Economic Integration and the Montevideo Treaty, as well as the establishment of suitable procedures for the analysis of problems, especially with respect to relations with the outside world, that may concern the States members of both Associations.

## 5. Industrial integration

### (a) Evolution of the manufacturing sector

During the last two decades conditions have been relatively favourable to the development of manufacturing industry. The effect of the import restrictions imposed in 1940-45 was later reinforced by that of the bilateral free-trade treaties and, subsequently, that of the agreements of establishing the common market. Thus, the rate of growth of the manufacturing product between 1950 and 1960 was faster than that of the rest of the economy. Nevertheless, the ratio between industrial production and the total product remained virtually unchanged, amounting to 12 per cent in 1960. This state of affairs is attributable to the incipience of the industrialization process, and is the first sign that so far there has been no steady drive behind the

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process in question. Even in more recent years (1961-62), with the common market already in operation, the increase in industrial production has been relatively slight.

If the countries are taken as a whole, as early as 1950 over 90 per cent of total consumption of some staple manufactures - for example, food and beverages - was satisfied with domestic production, and there was no longer any scope for import substitution. This fact, in conjunction with the limitations of national markets during part of the period, explains why industrial development had to be based on natural growth where industries of this type were concerned, and on import substitution in respect of other lines of production for which Central American demand is still largely satisfied with imports from outside the area.

The expansion of the manufacturing sector observable during the fifties was not accompanied by any very substantial changes in the structure of production. Traditional manufactures, which in 1950 represented 80 per cent of the total product of the sector, still absorbed 77 per cent in 1960. This in turn has a bearing on the further circumstance that no significant progress was made in that period in the over-all import substitution process. The proportion of the total supply of manufactured goods represented by domestic production remained the same - about 63 per cent. Yet as regards import substitution in respect of non-traditional consumer manufacturers, Central American industry achieved considerable advances. Consequently, the stability of the over-all import coefficient is attributable rather to the dynamic rate of growth of demand for capital goods which had to be purchased abroad than to the non-existence of a substitution process. Although demand for goods of this type will have to continue to depend on imports for its satisfaction, it is in respect of some of these activities that the Central American common market offers the greatest scope for the integrated development of the industrial sector.

(b) Industrial integration activities

Under the economic integration programme, the Committee's action in the industrial field has been intensified in recent years in three main directions. In the institutional sector, the Central American Research Institute for

/Industry (ICAITI)

Industry (ICAITI) and the Central American Bank for Economic Integration were established. Furthermore, in 1956 the Committee felt it necessary to secure the more sustained participation of private enterprise in integration programmes, especially with respect to the industrial sector, and with this end in view created a Central American Industrial Initiatives Commission, composed of representatives both of the Government and of private enterprise. Subsequently, in 1959, and likewise with the aim of drawing the private sectors into the integration programme, a first meeting of Central American investors was held at San Salvador (El Salvador), on which occasion the various instruments of the programme were considered and discussed and some of the main industrial development problems were indicated. More recently, the Central American Federation of Industrial Chambers and Associations (CECAICA) was established, and in 1962 had already begun to examine some of the problems of industrial integration.

In a different direction, since 1957 the Committee has been studying, through the Technical Assistance services of the United Nations, the possibilities for specialized production of textiles. As a result, a preliminary specialization programme for the cotton textile industry is on the way to completion. This programme is on a regional scale and is being prepared in close collaboration with industrialists in this branch of activity and experts from the secretariat of the General Treaty.

Lastly, as an additional dimension of the programme in relation to the manufacturing sector, the Economic Co-operation Committee, at its fifth session in 1958, recommended to the Governments for their signature the Agreement on the Régime for Central American Integration Industries, which was duly signed. This Agreement was adopted in its entirety in Chapter VI of the General Treaty, which provides that within a specified period from the date of entry into force of the instrument in question the first protocols shall be signed by the Governments. In compliance with the Committee's recommendations, the ECLA secretariat has recently carried out further studies on additional industrial integration possibilities, covering mainly the manufacture of intermediate and production goods. These analyses include a

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preliminary evaluation of the economic viability of certain branches of industry whose installation would be a complete innovation in Central America, together with a provisional estimate of the cost of the investment required and of the repercussions of the establishment of these industries on the Central American economies.

On the basis of the aforementioned studies, and pursuant to resolution 84 (CCE) of the Economic Co-operation Committee, a meeting of an ad hoc working group on industrial development was held at Managua (Nicaragua) in December 1961, to consider projects presented by Governments as eligible for inclusion in the Régime for Integration Industries. The group examined these projects and drafted the provisional text of a protocol incorporating several of the undertakings in question. At a later date, the Central American Research Institute for Industry issued the necessary technical pronouncements, as stipulated in Article IX of the Agreement on the Régime, concerning the classification as integration industries of three projects which had been considered at the Managua meeting and afterwards formally submitted to ICAITI through the secretariat of the Treaty. These pronouncements are based upon minimum capacity requisites and others that are indispensable if a specific activity is to be classified as an integration industry, with due regard to such determinants as efficiency and costs. On the basis of the Institute's decisions and the reports submitted by the secretariat of the Treaty, the Executive Council, at its second session, formulated the draft protocol appearing as an annex to the document presented to the eighth session of the Committee, and recommended it to the Governments for signature.

As part of a co-ordinated, over-all approach to Central America's industrial development problems, the Committee deemed it necessary (resolution 50 (CCE)) to standardize existing legislation on tax exemptions for the establishment or expansion of industries, in order to eliminate discrepancies offering an inducement to invest or to select a particular site, such standardization to cover both the amount of the exemptions and the criteria applied in granting them.

At the request of the Committee, an expert from the Bureau of Technical Assistance Operations prepared a report on the subject. On the basis of this

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report and under the terms of resolution 85 (CCE) of the Committee, a working group analysed the problem, and, in the course of three sessions, <sup>10/</sup> prepared a draft Central American agreement on tax incentives to industrial development. When the Economic Co-operation Committee had taken cognizance of this draft at its third extraordinary session, held at San José (Costa Rica), and had given the text its final form, the Agreement was signed by the Governments on the same occasion.

The Agreement makes uniform provision for classification of industries, amounts of exemptions and legal administration procedures, and stipulates that the granting of tax incentives shall be established on a completely regional basis within a maximum period of seven years from the date of the Agreement's entry into force. The greatest benefits accruing from the uniform legislation are conceded to the industries producing capital goods and raw materials, considerations relating to labour inputs and the relative importance of inputs from Central American sources being also taken into account. With the application of the instrument in question, uniformity will have been achieved in this significant respect, and the system of incentives to industrial investment will be improved.

The Agreement relates only to manufacturing industry proper. With regard to assembly work, it establishes a commitment to the effect that, within a period of not more than one year, an additional protocol shall be signed, which shall institute the system of tax incentives applicable to such activities, and shall comprise, inter alia, provisions relating to the trade régime to which assembly goods will be subject in the Central American common market. It is likewise stipulated that tax incentives applicable to

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<sup>10/</sup> Held at Guatemala City (GUATEMALA), from 17 to 28 July 1961;  
Guatemala City (Guatemala), from 15 to 22 November 1961;  
Mexico City (Mexico), from 26 March to 3 April 1962.

enterprises manufacturing pharmaceutical (including medical) products shall be governed by a special protocol. In this last connexion, the Ministers of Economy, who form the Board of Directors of ICAITI, have requested the Institute to carry out the necessary technical studies. These two protocols have still to be drafted.

To ensure the satisfactory application of the Agreement, the contracting parties will adopt rules of procedures within a period not exceeding thirty days from the date of its entry into force. These rules of procedure will be drawn up by the Executive Council of the Treaty.

(c) Future requirements and measures

The foregoing measures reflect the long-term view adopted in the Committee's studies on industrial development. From this same long-term standpoint, the development of the manufacturing sector will call for a very substantial volume of new investment. With the idea of approximately estimating the amount that will be required, the ECLA secretariat has made a preliminary examination of this problem. On the assumption that during the next ten years per capita income will increase at an average annual rate of 2.5 per cent, demand for manufactured goods may be expected to rise from 1,328 million dollars in 1960 to 2,738 million in 1970. Given the prospects and projections for the capacity to import, Central America's own production would have to increase from 848 to 1,828 million dollars in order to satisfy that part of demand which could not be covered with imports.

To obtain this additional output the capacity of manufacturing industry would have to be expanded at an estimated investment cost of 950 million dollars at 1960 prices. In this calculation the conclusions previously reached in a preliminary study, prepared on the occasion of the establishment of the Central American Bank for Economic Integration, are modified by the incorporation of the figures for Costa Rica, which at that time were not included.

Investment on such a scale implies the determination of specific industrial development possibilities, better knowledge of existing natural resources, and the gradual training of skilled labour and technicians at the intermediate professional levels, as well as other elements which may directly influence the productivity of the new investment. Hitherto no attempt has

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been made to carry out a study of industrial development resources and possibilities in Central America which will pave the way for an over-all statement of the problem and, at the same time, for practical analysis of the various elements to be brought into play in order to expedite the development of the industrial sector. A project of this type would involve both broad questions of economic analysis and purely technical issues. Current and future Central American demand for industrial products might be determined by types and classes of goods, and available resources quantitatively assessed in relation to this demand, while at the same time the viability of those industries of regional scope whose economic basis of operation can apparently be found in the common market might be evaluated.

With respect to human resources, information would have to be obtained on the present composition of the labour force, its level of qualifications and skills, and the existing training institutions, all in the light of future increases in skilled labour requirements. The Economic Co-operation Committee has included in its programme for 1963 a study of the regional labour force which will be undertaken by experts from the United Nations Bureau of Technical Assistance Operations (BTAO) and from the International Labour Organization. This study might serve as a basis for more detailed research, in the course of which problems relating to the training of skilled labour would be analysed solely within the framework of industrial projections and in relation to specific branches of industry.

Not enough is known of Central America's resources at present. Information of this type would be of basic importance for the determination of many of the future industrialization possibilities. A complete study of such resources generally takes a very long time, and perhaps its findings could not be obtained soon enough for the purposes of the more immediate investment decisions. Consequently, under the auspices of the Committee and with the co-operation of ICAITI, the scope of the research might be confined at first to the mineral resources used as raw materials by those industries whose economic viability in the Central American region had been established.

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With a view to the more efficient utilization and the development of agricultural raw materials for industrial processing, activities supplementary to those already undertaken under the integration programme might also be carried out.

At present many goods manufactured from agricultural raw materials are still imported. A thorough analysis of this problem would involve detailed studies of a technical nature in so far as soil surveys and other equally specialized aspects of the subject were concerned. On the basis of these surveys, consumption and total imports of goods manufactured from agricultural raw materials could be compared with the possibilities of producing such goods in Central America. This comparison might constitute the point of departure for an analysis of the development prospects of a considerable number of manufacturing industries.

Central American industry uses a large proportion of the agricultural raw materials available in the area. Nevertheless, imports of processed foodstuffs amounted to almost 40 million dollars in 1960, and the value of textile imports in that same year was 50 million dollars. These amounts, plus the figures for other manufactures of agricultural origin, give a sum total of 149 million dollars' worth of imports in 1960.

With a better knowledge of natural and other resources, the actual formulation of specific industrial projects could be carried beyond the stage of pre-investment studies to that of complete analyses of viability. If the information in question were at the disposal of private enterprise and Central American institutions, it might be conducive to new investment. It is needed mainly in respect of industries of regional scope which constitute a support for the expansion of the whole of the manufacturing sector. The same approach might include efforts to identify possible industrial complexes formed by branches of industry whose growth prospects are overlooked when research is carried out in watertight compartments at the project level.

It would also seem needful to obtain more exact data on manufacturing production capacity and other characteristics of industry, with due regard

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not only to existing plant but to expansion plans and new projects. Such information is an indispensable requisite for the analysis of specialization or industrial complementarity possibilities.

In a more general context, it must also be borne in mind that the Central American common market alters or will tend to alter the pattern of the criteria governing the choice of sites for productive activities. The impact of the several factors on which this selection depends - such as the size of the plant, the labour supply, the dimensions of the market, and transport facilities - is not the same when the location of industries is projected at the regional level and when it is determined, as was the case until recently, by the limitations of national markets.

The findings of studies on all the foregoing topics would more fully acquaint the Economic Co-operation Committee with the problems of duplication of investment and under-utilization of existing capacity, besides affording it a first glimpse of the opportunities for complementarity between various sectors of industry and for increased specialization.

## 6. Electrification

The Central American Electrification Sub-Committee was set up under the terms of resolution 59 (CCE), adopted by the Committee in June 1958. It is composed of representatives of official agencies and private electricity companies, and its primary aims are the promotion of common and co-ordinated utilization of the hydro-electricity potential existing in the various countries; the establishment of standard bases for research on hydro resources; and other objectives relating to such matters as the study of the power market, the development of uniform statistics on the electricity industry and the formulation of technical norms for the operation of electricity companies and agencies in the Central American countries.

The Sub-Committee held its first session at San Salvador (El Salvador) in November 1959. Its programme of activities is directed primarily towards the study of specific possibilities for co-ordinated hydro-electric and interconnexion projects. A United Nations Technical Assistance expert has made a preliminary study of the probable repercussions of interconnexion

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between two of Central America's principal hydro-electric systems on the costs of investment and of the generation and distribution of power. According to the findings obtained, which must be regarded as provisional, the joint operation of the two systems would imply a reduction in investment amounting to 28 million dollars by 1970, and a substantial saving in respect of generation and distribution. The findings in question are being amplified by the mission of experts which, at the request of the Committee, began work in Central America in the course of the past year. This second phase comprises the analysis of further possibilities for the combined operation of electricity systems as between other Central American countries. The findings of this study will be presented to the Sub-Committee at its next session, which should take place in 1963.

The Sub-Committee's work programme also includes research on hydro-electric resources and inter-Central American training for research of this type, as well as the preparation of an inventory of the hydrological stations in operation in the five Central American countries and Panama. The above-mentioned mission on electric power in Central America, in consultation and co-operation with national agencies, has carried out a study on the pertinent research activities that the countries are undertaking, and has formulated a project for the establishment of a network of hydrological stations as part of a complete programme for the survey and development of hydro resources on a regional basis.

Furthermore, in 1959 it was decided to make an analytical study of the tariff rates in force in the countries of the area. The findings of the research conducted in this connexion appear in a Comparative study of electrification costs in Central America and Panama. Here the various components of the price of electric power in each individual country are established, and the reasons for the considerable disparities observable are analysed.

Pursuant to recommendations of the Sub-Committee, a project for a Central American standard accounting system for the electric power industry has been drafted.

The report of the first session of the Central American Electrification Sub-Committee (E/CN.12/CCE/207), with the appended resolutions has been submitted to the Committee.

## 7. Transport

### (a) Present status

When the integration programme was launched in 1951-52, the inter-Central American transport situation was such as to call for substantial improvement, through the establishment of a system which would efficaciously serve the region as a whole. The primary purpose of the systems then existing was to link up the areas where agricultural exports were produced, and the most important population centers in the interior of each country, with its ports and sea routes. Even so, there were investment and operational problems that were difficult to solve.

The signs of reform and of a new approach which began to be apparent during the fifties were essentially attributable to national efforts to expand internal road networks. In 1946, Central America's all-weather roads covered about 7,900 kilometres. During the next few years, road-building increased at an annual rate of 3.7 per cent, with the result that by 1952 the total extension was 9,900 kilometres. In 1961 such highways represented a total length of 20,700 kilometres, the annual rate of growth having risen during the intervening period to 8.5 per cent.

The development of motor vehicle transport has been considerable. Between 1952 and the present time the number of vehicles in circulation has doubled, and more than two-thirds of them are passenger transport and freight vehicles. It is estimated that in 1961 total freight movements amounted to almost 1,000 million ton/kilometres.

Railway, inland waterway and coastal transport have lagged behind, and the development of the corresponding networks, equipment and operations has remained stationary. The railways have not enlarged their networks, nor have they renewed their equipment for over ten years. Even so, they convey a considerable volume of freight. In some countries they carry between 60 and 80 per cent of total exports and imports transported by sea.

### (b) Central American road plan

The Economic Co-operation Committee initiated its activities in the field of transport with its resolution 4 (AC.17), adopted in 1952, sponsoring an integrated study of the transport system in Central America. Later, it established the Transport Sub-Committee to undertake this and other studies.

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Pursuant to the aforesaid resolution, a mission appointed by ECLA, Technical Assistance Administration (now BTAO) and other United Nations agencies carried out the over-all study requested and prepared a preliminary outline for a regional highway system. The study was considered and noted by the Committee in 1953. <sup>11/</sup> Subsequently, in resolution 92 (CCE), the Committee recommended the formulation of a complete programme of activities geared to the establishment of the Central American road plan.

In 1961 a Technical Assistance expert prepared a study on the progress of the Central American road network and the probable cost of its completion. <sup>12/</sup> A working group formed by the secretariat of the Treaty, the ECLA secretariat and the Central American Bank for Economic Integration was set up in 1962 to proceed with the formulation of the draft plan. The results will be submitted to the Transport Sub-Committee at its next session, which is to be held in 1963. The report of the Technical Assistance expert on the Central American road network has been presented to the Committee.

Broadly speaking, the undertakings of regional interest projected in the 1952 study comprised about 3,930 kilometres of new highway construction or road improvement, at an estimated cost of 102 million dollars. These operations would represent 95 per cent of the total included in the mission's recommendations, which amounted to 4,142 kilometres. It was also recommended that the projects concerned should be carried out within a period of seven years, concurrently with other programmes at the national level to a value of 88 million dollars. Subsequently, more routes were included and the extent of the network increased to a total of 5,164 kilometres. So far, about 47 per cent has been paved (2,443 kilometres). Second-class roads, which can also be used in all weathers, represent a total length of 2,087 kilometres. The aggregate length of first and second - class roads is thus 4,530 kilometres, i.e., 87 per cent of the total. Most of the remaining 13 per cent is

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<sup>11/</sup> See Transportation in Central America (E/CN.12/356; ST/TAA/Ser.C/8), published in Spanish only under the title El Transporte en el Istmo Centroamericano, United Nations Publications, Sales No.: 1953.VIII. 2, September 1953.

<sup>12/</sup> See Informe Preliminar sobre Red Vial Centroamericana (E/CN.12/CCE/250; TAO/LAT/38).

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constituted by dry-weather roads. It may be noted, however, that considerable stretches - estimated at 30 per cent of the all-weather roads - urgently need reconstruction or improvement. Furthermore, supplementary works are required, including permanent bridges.

The system of highways of regional importance links up the most densely-populated areas, the centres of industry, services and trade, and the principal farming areas situated along the Pacific belt, but at a much heavier investment cost than was estimated in 1952. For future undertakings a cost of about 88,000 dollars per kilometre is calculated.

In the central areas all the highways classified as of regional importance have been completed; they are all-weather roads and 90 per cent of them are paved. In contrast, nearly one-third of the roads in frontier districts cannot be used in all weathers. This prevents any expansion of the area of influence of longitudinal highways and deprives the system of its regional scope.

(c) Maritime transport and ports

In resolution 21 (AC.17) and 92 (CCE), of 1953 and 1959, the Committee decided that the problems of port and maritime transport development should be considered within the integration programme. The studies carried out indicate the need for the highest priority to be assigned to the physical reconstruction of ports, the modernization of equipment, port facilities, transport and communications, and port administration. Another recommendation is that up-to-date standard port and maritime legislation and regulations be established and the training of administrative personnel promoted.

In resolution 19 (CCE), the Committee urged that maritime legislation be brought up to date. Accordingly, the Proyecto de Código Marítimo Uniforme para los Países Centroamericanos (Draft Standard Maritime Code for the Central American Countries) <sup>13/</sup> was prepared, together with another study, properly co-ordinated with the former, entitled Disposiciones para la Legislación y Reglamentación Portuaria Uniforme en Centroamerica (Provisions for Standard Port Legislation and Regulations in Central America). <sup>14/</sup> These

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<sup>13/</sup> TAO/LAT/27; CCE/SC.3/01.1.

<sup>14/</sup> TAO/LAT/28 (limited distribution).

two projects were discussed by the competent government agencies. Generally speaking, national working groups considered that it would be premature to apply a regional maritime code, since the relevant legislation is closely linked to trade codes and these in turn seem to need overhauling. As regards port legislation, some countries have taken steps to apply a good many of the draft regulations that have been formulated, but further action in this field would appear to be required.

Progress has been made in the construction of docks and other works at the chief ports, on the basis of investment which in 1956-61 amounted to approximately 18 million dollars. These projects would have to be supplemented in the future by the establishment or expansion of such technical services and material facilities as would increase port efficiency and expedite the handling of shipping.

(d) Other matters

If by its very nature inter-Central American trade has generated increased demand for highway facilities and motor vehicle transport, the progress of the common market towards its final form and the creation of a single customs territory seems likely to call for the adequate expansion of other means of transport. The need to remedy infrastructural deficiencies at a rapid rate has precluded thorough study of the application of more modern constructional technology; nor has it been possible to prevent duplication as between two or more means of transport. But this phase may soon come to an end, and the policy to be pursued can then be systematically defined.

The development of the motor vehicle transport industry has lagged behind the road-building programme, owing, inter alia, to the lack of continuity in inter-Central American traffic and to the difficulties attending the establishment of programmes relating to the replacement of vehicles and the expansion of mobile equipment inventories.

So far, it has not been possible to create at regional level an efficient, expeditious and economically satisfactory motor transport.

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service to meet the needs of the development of regional trade. In article XXIX of the General Treaty, provision is made for the adoption of transport regulations which would eliminate some of the administrative difficulties that discourage services of this type.

Moreover, the amounts of freight carried in different directions are not evenly balanced. It has been impractical to use specialized vehicles for particular types of goods because trade in the products concerned is intermittent. These problems help to keep costs of motor transport high, so that they are almost prohibitive in the case of goods of low economic density.

The importance of modernizing telecommunications has been touched upon in relation to the establishment of various radiocommunication services in air and maritime transport, and also as a means of expediting trade movements.<sup>15/</sup> Since 1960 the Central American Governments have decided to grant priority to the establishment of satisfactory public telecommunication services, and have begun consultations with international financing institutions. In response to the interest displayed by the Governments, a mission from the International Bank for Reconstruction and Development (IBRD) visited Central America at the end of 1961, and in March 1962 the United Nations Special Fund decided to finance a study which would serve as a basis for the planning and design of the telecommunications network in each country, with due regard, in addition, to regional and international communication requirements. A fifteen-year basic plan is to be established, together with a detailed programme of targets for the first five years of the plan, and an estimate of its cost.

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15/ Informe de la Primera Reunión de Inversionistas Centroamericanos  
(E/CN.12/CCE/206), annex VI.

### 8. Co-ordination of housing programmes

The Economic Co-operation Committee has been devoting attention to housing problems since 1957. The Housing, Building and Planning Sub-Committee was established under the terms of resolution 61 (CCE), adopted by the Committee during its fifth session, in 1958. The Sub-Committee, composed of the high-ranking officials responsible for national housing institute programmes in Central America, enjoys the co-operation of the United Nations Bureau of Technical Assistance Operations (BTAO) and, more recently, the Inter-American Development Bank (IDB) and the Organization of American States (OAS).

The activities pursued to date include the determination of bases for the establishment of regional specifications in respect of building materials; a study on the natural resources of Central America that could be used in the manufacture of housing materials; an inventory of the construction materials industries already in existence in the Central American countries; a complete project for the first phase of application of a modular co-ordination system in national housing programmes; and a detailed analysis of the recent evolution and current status of these programmes. The secretariat has presented reports and documents on each of these topics.<sup>16/</sup>

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16/ See Coordinación modular en la vivienda económica (E/CN.12/CCE/SC.4/9); Informe del grupo de trabajo sobre coordinación modular en vivienda (San Salvador, El Salvador, 14 to 23 August 1962) (E/CN.12/CCE/SC.4/10); Estado actual de los recursos naturales del Istmo Centroamericano y su posible aplicación en la manufactura de materiales de construcción utilizables en la vivienda (E/CN.12/CCE/SC.4/16); Industrias o establecimientos que fabrican materiales de construcción en el Istmo Centroamericano (E/CN.12/CCE/SC.4/15); Glosario de términos empleados en arquitectura y construcción en el Istmo Centroamericano (E/CN.12/CCE/SC.4/10); Programas de construcción de viviendas en los países del Istmo Centroamericano para 1962-63 y su relación con los materiales de construcción requeridos (E/CN.12/CCE/SC.4/17); Materiales de construcción requeridos para los programas de construcción de viviendas 1962-63, en los países del Istmo Centroamericano (E/CN.12/CCE/SC.4/17/Add.1).

The final modular co-ordination project was prepared by a working group which met at San Salvador (El Salvador) in 1962. This project, together with the other studies and documents mentioned above, is to be submitted to the consideration of the Housing, Building and Planning Sub-Committee at its second session, to be held in 1963.

As regards other activities, in 1962 officials from the five Central American countries and Panama actively participated in the Latin American Seminar on Housing Statistics and Programmes which took place in Denmark. Furthermore, fellowships have been distributed among the five Central American countries and Panama to provide a year's training, in several European countries, for housing institute officials specializing in design and construction materials. These activities are being carried out with the co-operation of the United Nations and of various European institutions.

The analysis of housing problems in the countries under consideration reveals, in 1962-63, an expansion of the building activities of the various agencies operating in this sector. External financing amounting to approximately 45 million dollars is available for the construction of 20,000 housing units. Nevertheless, complete satisfaction of the requirements deriving from population growth is still a long way off, and if any attempt were made to cover part of the cumulative deficit the gap would be still wider. On the basis of a projection which estimates the increase in the population of Central America during the next two years at 700,000 inhabitants, new housing requirements will probably amount to about 140,000 units in that period.

Of the work outstanding, the following are the proposals which might be considered for immediate implementation. With respect to modular co-ordination, on the basis of a report by the United Nations Technical Assistance expert assigned to this programme, the meeting held at San Salvador (El Salvador) formulated the modules for co-ordination purposes and laid down the procedure for their first application on an experimental scale. To ensure the continuity of this effort, a pilot housing programme using the modular system should be carried out with the participation of national housing institutes and the Central American enterprises producing construction materials.

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With a view to improving the construction of housing units and ensuring the necessary flow of supplies, attention has been drawn to the need to promote the use of hand tools and low-cost construction equipment which would help to increase productivity and improve standards of quality. An attempt would be made to introduce methods of construction which, while highly efficient, permit maximum absorption of the labour force. In these activities specialized technicians would also take part, giving demonstrations on building sites. As an additional line of approach, promotion activities could be undertaken in respect of the installation and expansion of Central American production of tools and light basic equipment for such purposes.

To encourage the development of production of construction materials in Central America, thorough research on the regions natural resources should be conducted on selective lines. In some cases - for example, those of minerals and forest resources - suitable raw materials for the manufacture of building materials are known to exist in Central America, but no complete studies are available as a basis for programming the establishment of the corresponding branches of industry. However, the study already carried out by the United Nations Technical Assistance expert has made it possible to clarify and determine, inter alia, the existence of resources, such as those of volcanic origin, which could be turned to account forthwith, and which might provide some raw materials at lower costs than those currently prevailing. The aforesaid study also indicates several possibilities for trade in such raw materials among the Central American countries, which might be the subject of detailed research.

A comparison between this inventory of natural resources and the inventory also taken in Central America, of existing construction materials industries might bring to light, over the short term, additional possibilities for industrial development in this important sector of the economy.

In addition to the foregoing activities of the Sub-Committee, mention should be made of the increasing emphasis placed in the Central American countries on public investment in housing, as well as of the fact that ampler external financing facilities than formerly existed have recently been made available. Clearly, if these three elements were brought into play in Central America on the basis of a co-ordinated approach at the regional level, the objectives pursued by the Governments in this field could be sooner and more efficaciously attained.

