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**TRADE PROSPECTS FOR DEVELOPING COUNTRIES**

**Chapter 3<sup>10</sup>**

**The Balance of Current Account Transactions and Policy Alternatives  
for a Balanced Expansion of World Trade**

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### 5.1 Service Items in the Balance-of-Payments

In the preceding discussion of the trade prospects of developing countries, all exports and imports have been expressed in f.o.b. prices. To arrive at an estimate of the current balance, we have further to take account of transportation costs, investment income, travel expenditures, and other items that are classified as services (invisibles) in the balance-of-payments. Services are of considerable importance for the developing countries: receipts from services amounted to \$6.0 billion in 1960 as against earnings on the merchandise account of \$27.1 billion, while the corresponding figures on the payments side were \$9.3 and \$28.4 billion.<sup>1</sup> Expenditures by foreign governments in less developed areas loom large among receipts (\$2.3 billion) with travel expenditures (\$1.3 billion) following. On the payments side, freight and insurance (\$2.2 billion) is, in fact, part of the cost of imports whereas the investment income of foreign companies (\$3.4 billion) is largely a deduction from export earnings.

It appears, then, that much of the current account deficit of the developing countries takes the form of a deficit in services; \$3.3 billion in 1960 as against an import surplus of \$1.3 billion. But despite the importance of invisibles in the balance-of-payments of less developed areas, the reliability of statistics is generally low. While trade is documented with customs receipts, most countries rely on sampling to

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1. The export and import data cited here include intra-area trade in each region in order to achieve comparability with the statistics on invisibles. Intra-area trade has been estimated on the basis of information derived from [ 10, 13 ]; with regard to payments and receipts on the service account, see Table A 5.1.1.

estimate travel expenditures and insurance, information on investment income is derived from the reports of private companies, and a mixture of the two procedures is used in estimating freight expenditures.

At the same time, a number of countries do not publish data on receipts and payments in the service account and statistical collections of such information are few and far between. In the present study, the balance-of-payments statistics of the International Monetary Fund have been utilized whenever available, and we have relied on national statistical sources in regard to countries not included in the IMF compilations. Finally, for countries that do not publish data on services, we have estimated freight expenditures from trade statistics, and investment income as well as spending by foreign governments on the basis of information given in the statistical publications of the developed countries.

Freight and insurance had to be estimated also in cases where imports are given in c.i.f. prices.<sup>1</sup> In such instances we have assumed that freight and insurance taken together amounted to 10 per cent of the c.i.f. value of imports<sup>2</sup> excepting the case of Mexico where the important role played by surface transportation warrants the use of a lower ratio. According to our estimates, the net payments of developing countries for freight and insurance amounted to \$1.8 billion in 1960. These countries rely to a considerable extent on shipping by foreign companies and, in view of the large capital and foreign exchange outlay involved in setting up domestic shipping fleets, this situation is not likely to change materially

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1. Apparently freight expenditures in such countries have been disregarded in a compilation of the United Nations [ 11 ], and this fact accounts for a substantial part of the difference between the relevant figures in the UN paper and those of the present study.

2. The same assumption was made in [ 3 ].

during the period under consideration. In making projections, we have assumed that expenditures on freight and insurance will increase pari passu with the rise of imports into developing areas, except for some larger countries in Latin America and Asia where increased reliance will be based on domestic shipping facilities.

The "other transportation" category includes the chartering of ships and airplanes, fees paid for the use of international waterways, and various other transactions. The largest item within this category is payments to Egypt for the use of the Suez-canal. Further increases are expected on this count while no change has been assumed elsewhere.

On the travel account, Latin America experienced a favorable balance, chiefly by reason of tourism from the United States. In other areas, however, fares paid to foreign airlines and shipping companies resulted in a deficit so that, for the developing countries as a whole, only a small surplus is shown. But given the promotional activities underway in less developed areas, the establishment of national airlines in several of these countries, and the increasing radius of tourist travel, improvements are anticipated during the period of projection. We have projected the net balance of the developing countries in tourism and travel to reach \$0.7 billion in 1970 and \$1.0 billion in 1975. The largest increase in receipts has been assumed to take place in Latin America where proximity to the United States provides an advantage.

The payments of developing countries included under the heading "investment income" have been increasing at a rapid rate and approximately doubled during the fifties. Increases have been especially pronounced in interest paid to foreign governments and international organizations given that the external public debt has nearly doubled between 1955 and 1960. Nevertheless, these payments have remained small in absolute amount and interest

paid to foreign governments and the IBRD hardly surpassed 10 per cent of total foreign investment income in 1960.

Prospective changes in the interest burden of the external public debt will depend on the size and terms of future lending. Should the inflow of public capital grow at an annual rate of around 4 per cent and should we assume some improvement in the terms at which credit is given, the interest burden may rise at an annual rate of 3 per cent. In turn, changes in the earnings of foreign companies will be affected by the rate of increase of foreign private investment, the export prospects of the industries where foreign companies are of greatest importance (oil and nonfuel minerals), and the tax-treatment of these companies. We have assumed modest increases in the inflow of private capital, and a rise in the share of the producing countries in the profits of foreign companies. Detailed estimates have been prepared for oil where a considerable amount of information is available (Table A 5.1.2).

The investment income foreign companies are expected to derive from the production and refining of oil and prospective investment earnings in Israel have been included as a debit item in the balance-of-payments of the Middle East where foreign investment income may rise from \$1.1 billion in 1960 to \$1.5 - 1.6 billion in 1970 and \$1.7 - 2.0 billion in 1975.

The expansion of oil production will account for much of the projected increase in the earnings of foreign companies in Africa. But, with the increasing mining activity and aluminum production, the profits of foreign companies engaged in mining and the processing of ores will also rise. Taken together, net payments to foreign companies and governments may reach \$1.0 billion by 1975 as compared to \$0.2 billion in 1960.

Smaller increases are foreseen in Latin America where the relatively slow expansion of oil exports and the cost cum tax squeeze on the oil companies are expected to restrain the rise of investment income, although the favorable prospects for nonferrous metals will benefit the foreign mining companies. Finally, the expected relatively moderate increase in the foreign investment income of Asia would take the form of oil profits and interest payments on government debt. All in all, the net debit balance of the developing areas under the heading investment income has been projected to rise from \$3.0 billion in 1960 to \$4.4-4.7 billion in 1970 and \$5.2-5.7 billion in 1975.

The next category in the service account includes expenditures by foreign governments, such as local purchases and wage payments by foreign military, diplomatic and economic missions and contribution to specific defense expenditures. On the basis of information provided in national statistical publications and by the OECD, these expenditures of foreign governments in developing countries have been estimated at \$2.35 billion in 1960. By comparison, expenditures by the governments of developing countries abroad -- to a large extent, contributions to international agencies -- amounted to \$640 million.

Future changes in expenditures by foreign governments are difficult to predict since much of these expenditures served military purposes in 1960 or were related to the administration of colonial territories and assistance given to the newly independent nations. It may be expected, however, that with the ending of the Algerian war and the independence of Algeria, the expenditures of the French government in Africa will decline from the high level experienced in 1960. No change has been envisaged in other areas, so that the net receipts of the developing countries on the

government account have been projected to fall from \$1.7 billion in 1960 to \$1.4 billion in 1975.

Finally, miscellaneous service transactions include post and telegraphic services, royalties and patents, management fees, as well as personal income remittances. Payments under this heading have become increasingly significant as many of the developing countries have come to hire foreign management services and use foreign patents in setting up domestic industries. These expenditures will ultimately decline, however, and no change has been assumed during the period under consideration.

Our projections indicate an increase in the net deficit of the developing countries on the service account from \$3.3 billion in 1960 to \$5.1 or 5.5 billion in 1970 and \$6.1 and 6.9 billion in 1975, depending on the income assumption chosen (Table 5.1.1). The increase in the negative balance on invisibles is explained chiefly by the projected rise in the investment income of foreigners and in transportation costs which will be hardly counterbalanced by the increase in receipts from tourism. The largest deterioration in the service accounts is foreseen in Africa where a positive balance of \$0.2 billion in 1960 has been projected to give place to a \$0.9 negative balance in 1975 due to the combined effects of the fall in the expenditures of France in Algeria and the increasing return-flow of earnings on oil.

## 5.2 The Current Account Balance of Developing Areas

Table 5.2.1 shows the current account balance of developing areas, actual and projected. The estimates provide evidence of the importance of the return flow of investment on the net export earnings of developing countries. In Africa, for example, the apparent improvement in the trade

balance has its counterpart in the increased earnings of foreign companies, while in the Middle East the rise in oil exports is accompanied by higher incomes for the oil companies.

Table 5.1.1

Developing Countries: Service Items in the Balance-of-Payments (net)  
(\$billion, current prices)

	1960					1970 I				
	LA	AF	ME	AS	LDC	LA	AF	ME	AS	LDC
Freight & insurance	-0.7	-0.4	-0.2	-0.5	-1.8	-0.9	-0.6	-0.3	-0.7	-2.5
Other transport	-0.1	0.1	0	0	.0	-0.1	0.2	0	0	0.1
Travel	0.4	-0.2	0	-0.1	0.1	0.6	-0.1	0.1	0	0.6
Investment income	-1.4	-0.2	-1.1	-0.3	-3.0	-1.8	-0.7	-1.5	-0.4	-4.4
Government	0.1	1.0	0.1	0.5	1.7	0.1	0.7	0.1	0.5	1.4
Misc. services	-0.1	-0.1	0	-0.1	-0.3	-0.1	-0.1	0	-0.1	-0.3
Services, total	-1.8	0.2	-1.2	-0.5	-3.3	-2.2	-0.6	-1.6	-0.7	-5.1

  

	1970 II					1975 I				
	LA	AF	ME	AS	LDC	LA	AF	ME	AS	LDC
Freight & insurance	-0.9	-0.6	-0.3	-0.8	-2.6	-1.1	-0.7	-0.6	-0.9	-3.1
Other transport	-0.1	0.2	0	0	0.1	-0.1	-.2	0	0	0.1
Travel	0.6	-0.1	0.1	0	0.6	0.8	0	0.1	0.1	1.0
Investment income	-1.9	-0.8	-1.6	-0.4	-4.7	-2.0	-1.0	-1.7	-0.5	-5.2
Government	0.1	0.7	0.1	0.5	1.4	0.1	0.7	0.1	0.5	1.4
Misc. services	-0.1	-0.1	0	-0.1	-0.3	-0.1	-0.1	0	-0.1	-0.3
Services, total	-2.3	-0.7	-1.7	-0.8	-5.5	-2.4	-0.9	-1.9	-0.9	-6.1

  

	1975 II				
	LA	AF	ME	AS	LDC
Freight & insurance	-1.2	-0.8	-0.4	-1.0	-3.4
Other transport	-0.1	0.2	0	0	0.1
Travel	0.8	0	0.1	0.1	1.0
Investment income	-2.1	-1.1	-2.0	-0.5	-5.7
Government	0.1	0.7	0.1	0.5	1.4
Misc. services	-0.1	-0.1	0	-0.1	-0.3
Services, total	-2.6	-1.1	-2.2	-1.0	-6.9

Source: Table A 5.1.1.

Under the most likely income assumption, the current account deficit of the developing countries, taken together, would rise from \$4.7 billion in 1960 to \$9.4 billion in 1970 and \$11.3 billion in 1975 if the medium estimate of the income elasticity of import demand applied in all regions. The deficit would be greater, however, if target rates of income growth

were realized in the world economy, partly because of the reasons explained in connection with the balance of merchandise trade and partly because higher exports from the developing countries are accompanied by larger foreign investment income and higher imports by larger freight expenditures. The relevant estimates under the high (target) income assumption are \$10.7 billion in 1970 and \$13.7 billion in 1975.

Finally, should we assume that the developing countries reached target rates of growth while the gross national product of developed economies grew at "most likely" rates, the current account deficit of the less developed areas would amount to \$12.0 billion in 1970, with a trade deficit of \$6.8 billion and a service account deficit of \$5.2 billion. The corresponding estimates for 1975 are \$10.2 billion on the trade account and \$6.4 billion on the service account, i.e., a current account deficit of \$16.6 billion.

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By comparison, the United Nations/estimated a trade gap of \$12 billion and a service account deficit of \$8 billion in 1970 [ 14, p. 6 ]. Our discussion in Chapter 4.5 indicates, however, that the UN trade-gap projection is likely to be an overestimate while the service-account forecast is affected by the apparent overestimation of the deficit on invisibles in the base year (\$4 billion in 1959).

Irrespective of the income variant chosen, a deterioration in the current account balance is indicated for all developing regions, although Africa would regain some of the loss suffered between 1960 and 1970 in the early seventies. Given the projected rise in its trade deficit, Asia is expected to show the most unfavorable picture and the current account deficit of Latin America and the Middle East will also increase.

In 1960, the deficit in the current account balance of the developing countries was financed by the inflow of foreign capital, official and private.

Table 5.2.1.

Developing Countries: Current Account Balance<sup>a</sup>  
(\$billion, current prices)

	1960			1970 I			1970 II		
	Trade	Services	Current Account	Trade	Services	Current Account	Trade	Services	Current Account
LA	+0.28	-1.78	-1.50	-0.4	-2.2	-2.6	-0.4	-2.3	-2.7
AF	-1.23	+0.21	-1.02	-1.1	-0.6	-1.7	-1.4	-0.7	-2.1
ME	+1.12	-1.21	-0.09	+1.2	-1.6	-0.4	+1.1	-1.7	-0.6
AS	-1.51	-0.53	-2.04	-4.0	-0.7	-4.7	-4.3	-0.8	-5.1
	-1.34	-3.31	-4.68	-4.3	-5.1	9.4	-5.0	-5.5	-10.7
	1975 I			1975 II					
	Trade	Services	Current Account	Trade	Services	Current Account			
LA	-0.4	-2.4	-2.8	-0.6	-2.6	-3.2			
AF	-0.6	-0.9	-1.5	-1.1	-1.1	-2.2			
ME	+1.2	-1.9	-0.7	+1.1	-2.2	-1.1			
AS	-5.4	-0.9	-6.3	-6.2	-1.0	-7.2			
	-5.2	-6.1	-11.3	-6.8	-6.9	-13.7			

Source: Tables 4.5.2 and 5.2.1.

Note: (a) The medium estimate of the income elasticity of import demand has been utilized in regard to all developing areas.

According to data published by the OECD, the net flow of public capital from the member countries of the Development Assistance Committee (OECD countries and Japan) and international agencies to the less developed areas amounted to \$4.0 billion in 1960 and net private investments to \$2.5 billion (Table 5.2.2). In the same year, disbursements of grants and loans by the countries of the Sino-Soviet area were estimated at \$186 million and contributions by Australia and New Zealand at \$72 million [4, p. 13], making up a total of \$6.7 billion.

A lower figure (approximately \$5.5-6 billion) is indicated by the United Nations chiefly because of differences in the estimates of private investment [12]. But, in any case, the recorded inflow of long-term capital appears to exceed the current account deficit of the developing countries (\$4.7 billion in 1960) by a considerable margin. Various reasons have been given to account for this discrepancy: errors and omissions in current transactions, unrecorded

repatriation of capital funds, unrecorded investment by nationals of developing countries abroad, and flight capital [12, p. 12]. Further contributing factors are private transfers, short-term capital movements, and increases in the gold and foreign exchange reserves of developing countries, which/are not <sup>items</sup> included either under current transactions or under long-term investments.

A consideration of data for individual regions can be helpful in explaining the causes of the observed discrepancies. According to the estimates shown in Table 5.2.2, there is little difference between the current account deficit and the imports of foreign capital in Latin America and Asia, while large discrepancies are shown for Africa and the Middle East. With regard to Africa, note that practically the entire \$886 million errors and omissions indicated in the balance-of-payment of France with the ~~France~~ area [2, p. 5-France] pertains to Africa. This item may be explained, in a great part, by the unrecorded repatriation of earnings by French nationals paid from French governmental funds abroad and the return flow of capital from Algeria.

The repatriation of capital from the former Belgian Congo and some British colonies have further contributed to the difference between recorded current transactions and the inflow of foreign capital in Africa. By comparison, unrecorded investments abroad by the nationals of the oil-producing countries and increases in gold and foreign exchange holdings account for much of the discrepancy in the Middle East.

The next question concerns the measures to be used to fill the prospective "current-account gap" of the less developed areas. Various alternatives will be discussed below: accelerated growth in developed economies, reduction of barriers to the exports of developing countries, increased trade with the Sino-Soviet area, regional integration in less developed areas, and capital inflow.

### 5.3. The Contribution of Accelerated Growth in the Developed Countries to the Export Earnings of Developing Economies

Whereas the value of exports of developing countries to developed economies has been estimated at \$26.9 billion in 1970 and \$33.2 billion in 1975 under the most likely income assumption, the attainment of the target rate of income growth in developed countries is expected to result in exports of \$28.6 and \$36.4 billion in the two years, respectively. Thus, the increase in the value of exports due to higher growth rates in developed areas would be \$1.7 billion in 1970 and \$3.2 billion in 1975 (Table 4.5.1).

But against these increases we should set the increment in the investment income of foreign companies in less developed countries associated with a larger amount of exports. According to information provided in Table 5.1.1, the

Table 5.2.2.  
The Balance of Current Transactions and Capital Inflow in Developing Countries, 1960

Current Account Balance	(\$ billion)						
	Overall Total	Total bilateral	Official	Private net lending	Private export credit	Multilateral flow	
Latin America	-1.50	1.49	1.48	0.32	0.91	0.25	0.01
Africa	-1.02	2.19	2.04	1.28	0.70	0.06	0.15
Middle East	-0.09	0.53	0.49	0.25	0.20 <sup>b</sup>	0.04	0.04
Asia	-2.04	2.25	2.19	1.89	0.32 <sup>b</sup>	-0.02	0.06
	-4.68	6.46	6.20	3.74	2.13	0.33	0.26

Sources: Current account balance - Table 5.2.1.

Long-term capital inflow -- OECD, The Flow of Financial Resources to Developing Countries in 1961, Paris, 1963, p. 74.

- Notes: (a) The figures do not include aid by the countries of the Sino-Soviet area but, at any rate, trade between the developing countries and the centrally planned economies was approximately in balance in 1960 (UN, Monthly Bulletin of Statistics, March, 1963).
- (b) Our estimate.

increase in investment income between the two variants would be \$0.3 billion in 1970 and \$0.5 billion in 1975, reducing the net gain developing countries obtain from an acceleration in the rate of growth of developed economies to \$1.4 billion in 1970 and \$2.7 billion in 1975. The net change in the balance-of-payments of the less developed regions will be further affected by reason of the fact that larger exports in these countries would also lead to higher imports through an increase in the rate of growth of incomes.

#### 5.4. Reduction of Barriers to the Exports of Developing Economies

Barriers to the expansion of imports from developing countries into developed economies take a variety of forms: discriminatory and nondiscriminatory tariffs, excise taxes, subsidies to domestic producers, embargoes, state trading, import licensing, and quantitative restrictions. In the simplest case, that of commodities which are not produced domestically in the developed countries (e.g., tropical beverages), estimation of the probable effects of the removal or reduction of tariffs and excise taxes on imports requires information only on the price elasticity of demand over the relevant range. In these instances, the margin of error can be said to be related to the magnitude of the fall in retail prices following a reduction in fiscal charges.

The error-possibilities of estimation multiply, however, if we inquire into the prospects of commodities that are produced also in developed economies (temperate zone and competing tropical foods), since in such instances we would have to know the responsiveness of domestic production as well as of production in other developed countries to changes in price relationships. Finally, in cases when quantitative restrictions, embargoes, state trading, and import licensing are applied, information on domestic costs is necessary to evaluate the possible effects of the removal of these restrictions on imports.

In view of the difficulties of estimation, in the present study we aim at indicating possible developments under given assumptions instead of attempting to provide numerical estimates in regard to the impact of reducing tariff barriers on imports. An exception is the case of noncompeting tropical foodstuffs where the possible effects of the removal (or reduction) of tariffs and excise taxes have been estimated.

Temperate zone foods

The evaluation of the impact of change in domestic policies in the developed countries on imports of temperate zone foods from developing economies is especially difficult. To begin with, a variety of protective measures are employed in the importing countries which take the form of quantitative restrictions, import licensing, tariffs, as well as subsidies. At the same time, developing countries account for a relatively small proportion of the quantities brought on the world market and, at least in the case of cereals, their main competitors apply policies aimed at supporting domestic incomes and prices. If we consider also the movement of temperate zone foods through noncommercial channels from the United States to some underdeveloped countries and the difficulties of estimating the supply elasticity of production in developing areas, it will be apparent that the effects of changes in production and trade policies on the pattern of trade are difficult to foresee. Still, we can indicate the possible impact of modifying various assumptions underlying the projections on the imports of temperate zone foods from less developed areas.

In estimating the future imports of meat, we have assumed that, except for purchases from Madagascar, the application of Common Market agricultural policy would lead to the disappearance of EEC beef imports ~~for~~ while the maintenance of the system of deficiency payments in Britain would be accompanied by stagnating imports of beef. The consequences of these policies are of considerable importance to suppliers in developing countries since the Common Market and the United Kingdom account for over nine-tenth of their meat exports to Western Europe, which consist almost entirely of beef. Should the regulations be amended so as to

ensure that developing economies maintain their share in the meat consumption of these countries as of 1960, the value of these exports would exceed projected magnitudes by \$88 million in 1970 and \$103 million in 1975 (Table A 5.4.1.). Much of this gain would accrue to Argentina and Uruguay although there are possibilities for expanding exportable production in East Africa, too.

Similar considerations apply to cereals given that Argentina, the largest exporter among developing countries, is a low-cost producer of wheat, maize, and barley. There is no reason to assume that Argentina and other developing countries could not maintain their present share in European consumption, provided that agricultural policies in the Common Market and in the United Kingdom permitted imports to rise in proportion to domestic consumption. Under these assumptions, EEC and UK imports of wheat and coarse grains from developing countries would exceed projected magnitudes by \$101 million in 1970 and \$117 million in 1975 (Table A 5.4.1.). At the same time, the maintenance of Japanese imports of rice at 1960 levels would increase the export earnings of her Asian suppliers by \$18 million.

With regard to oranges, the FAO estimated that imports into the European Common Market (excluding Italy), Sweden, and Norway projected for the year 1970 would increase by \$19 million if tariffs and internal duties in these countries were reduced by 50 per cent and by \$39 million if tariffs and taxes were completely eliminated [8, p. 9]. Part of this gain would accrue to developed countries (United States, Spain, South Africa), however, whereas Algeria and Morocco may lose as a result of the elimination of preferential duties.

Trade in most other fruits takes place among the developed countries

themselves, while noncompeting fruits other than bananas bear low duties in the industrial countries, and hence less developed areas could derive little gain from an elimination of tariffs. Similar considerations apply to vegetables and wine. Finally, feedingstuffs enter duty-free in the main importing countries.

### Competing Tropical Foods

The problems related to tropical oilseeds and oils, too, are rather complex. Although oilseeds of tropical origin pay no duty in Western Europe,<sup>1</sup> subsidies and compulsory mixing regulations have encouraged the expansion of rapeseed production in this area, and various measures have been taken, or are contemplated to be taken, with a view to increase the consumption of butter at the expense of margarine. Further, in the European Common Market, the domestic crushing industry is protected by tariffs on vegetable oils which hinder the shift from the importation of oilseeds to that of oils. Of greatest importance for the exporters of tropical oils and oilseeds is, however, the price-support system of the United States that has contributed to the rapid growth of U.S. soybean exports, reducing thereby the market opportunities for oilseeds of tropical origin.

Note, however, that the increasing share of soybeans in European imports has been due, in part, to the increased demand for protein-rich oil and oilcake, and the expansion of soybean production in the

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1. There is a preferential tariff of 10 per cent on the main tropical oilseeds in the United Kingdom, however, from which Commonwealth producers are exempt.

United States has also made possible its distribution under the P.L. 480 program in several developing countries that have experienced supply deficiencies. Still, a reduction of subsidies in the industrial countries could lead to an improvement in the relative position of tropical oils through increasing the total imports of oils and fats into Western Europe and Japan and altering the price ratio between soybeans and oilseeds of tropical origin.

The removal of duties on vegetable oils would further benefit the developing countries. These duties have the double effect of providing protection to domestic crushers and raising the price of tropical oil on the domestic market. While the proximity of markets for oils and oilcake provides an advantage to the European crushing and refining industry, imports of oils (and oilcake) into the Common Market would be expected to rise after a removal of the tariff averaging around 10 per cent. And although substitution possibilities are limited in many uses, the ensuing fall in prices would improve the competitive position of tropical oils as against other oils and fats.

The probable effects of changes in production and import policies are difficult to assess. There are no reliable estimates available on the possible gain derived from the exportation of oils and oilcake as compared to oilseeds and information on the expansion-possibilities in the production of the various tropical oils, too, is scarce. Nevertheless, it can be stated that inasmuch as the shift from the exportation of oilseeds to vegetable oils is restricted by the differential tariff of the Common Market, the **immediate** gain accruing to developing countries following the elimination of this duty would not exceed \$20 million -- 10 per cent of the projected value of EEC imports of oilseeds from the non-associated

countries. Developing countries would derive a gain of a similar magnitude if their exports to the Common Market countries were to grow in proportion to the EEC's consumption of oils and fats other than butter.

The protection of domestic sugar production in the industrial countries takes a variety of forms. Quotas are used in the United States, in Japan, and in some smaller European countries, while a system of subsidies is applied in the Common Market and the United Kingdom. Despite improvements in the production of beet sugar, costs are generally lower in cane-sugar producing areas and it has been suggested that, in the major industrial countries, the average unit cost of beet sugar exceeds the price that would develop in a free world market by a substantial margin. Although the marginal cost of sugar production will differ from the average cost at various levels of output, sugar production in the industrial countries would fall to a considerable extent in the absence of protection, and the slack could be taken up by extending production in the main sugar exporting countries [ 6, p. 67 ].

The possible effects of a liberalization of protective arrangements can be indicated if we consider that an increase in imports by an amount equal to one per cent of consumption in the industrial countries would amount to 285 thousand tons in 1975, i.e. \$25 million at 1960 world market prices.<sup>1</sup> Should we assume for example, that the United States were to continue to import 46.5 per cent of her sugar needs instead of 40 per cent as envisaged, her sugar imports would exceed the projected magnitudes by 750 thousand tons in 1975, valued at \$54 million.

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1. 3.14 cents per pound, Cuban raw sugar, for destinations other than the United States.

Next, we inquire into the effects of the removal of tariffs and excise taxes on sugar consumption under the assumption that domestic sugar production in the industrial countries would be maintained through a system of subsidies. According to estimates prepared by R.H. Snape under these assumptions, sugar consumption would have exceeded actual consumption by 7 per cent in North America, 9 per cent in Western Europe, and 50 per cent in Japan in 1959 [ 6, p. 65 ]<sup>1</sup>. Although our calculations suggest that the price-elasticities used by Snape are somewhat high, it would appear that, assuming the removal of these charges and the maintenance of domestic production through subsidies, sugar imports into the industrial areas would exceed the projected magnitudes by 1.8 million tons in 1970 and 2.0 million tons in 1975, corresponding to an increase in the value of imports by \$126 million and \$137 million at world market prices (Table A 5.4.1.)<sup>2</sup>

Trade in tobacco would also expand if tariffs and excise taxes were reduced in the industrial countries but part of the gain would accrue to tobacco producers in the United States, Greece, and Turkey.

#### Noncompeting tropical foods

It has often been argued that a reduction or elimination of tariffs and excise taxes on tropical beverages and bananas would increase the

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1. Snape calculates with average fiscal charges of 24 per cent in North America, 23 per cent in Western Europe, and 51 per cent in Japan, and with price elasticities of -0.28, -0.5, and -1.0 in three areas, respectively.

2. By comparison, Snape's estimate was 2.2 million tons for 1959 and an estimate of 0.8 million tons has been arrived at by Tinbergen for the same year [ 7, p. 304 ]. In the latter case an overly low figure was used in regard to fiscal charges on sugar in the United States, however, and potential increases appear to have been underestimated in the case of several other countries, too.

imports of these commodities to a considerable extent. However, calculations made by the FAO suggest that the gain to developing countries would be rather small. According to the FAO, the imports of noncompeting tropical foods into the larger countries of Western Europe estimated for 1970 would increase by \$66 million at average prices of the years 1957-1959 if duties and excise taxes were halved and by \$141 million if these charges were completely abolished. In 1960 prices, the relevant figures are \$51 and \$107 million (Table A 5.4.1.).

About three-fourths of the total gain would be obtained in coffee -- \$80 million if all tariffs and taxes were abolished -- followed by cocoa (\$20 million), bananas (\$5 million), and tea (\$2 million).<sup>1</sup> In regard to coffee, estimates have been prepared in the present study, too, indicating an increase in the value of coffee imports over projected levels for the year 1970 by \$39 or \$80 million, depending on whether tariffs and excise taxes are reduced by 50 per cent or are completely abolished. ~~The differences between the two sets of estimates are largely due to the fact that while we have calculated with a decline in price elasticities over time, the FAO has assumed constant elasticities.~~

It appears then that the increase in the imports of noncompeting tropical foods into Western Europe following the abolition of tariffs and excise taxes would hardly exceed 7-8 per cent of projected imports. The results are explained by the low price elasticity of demand for noncompeting tropical products in Western Europe. Despite the existence of restrictive regulations, per capita consumption is approaching the

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1. By comparison, Tinbergen gives estimates of \$54 million for coffee, \$8 million for bananas, and \$1.5 million for tea for the year 1959 [7, p. 300]

saturation level in the high-income countries of Europe, and by 1970 a fall in prices will not have a substantial effect on consumption.

Note further that the removal of tariffs on noncompeting tropical foodstuffs would result in a redistribution of export incomes among producing areas, since, in the absence of preferential tariffs in the European Common Market and the United Kingdom, nonparticipating countries would obtain a larger share in exports. This shift would, then, favor low-cost producers at the expense of high-cost suppliers.

#### Agricultural raw materials

Most developed countries admit agricultural raw materials duty-free and although some countries (e.g. Japan) operate licensing systems, these are rarely restrictive. A major exception is the United States, where high duties are applied to wool and the importation of cotton is restricted by quotas.

In the United States, a specific duty (25.5 cents per pound) is levied on apparel wool, equivalent to an ad valorem tariff of about 25-35 per cent, depending on quality. In turn, the proceeds of this duty are used to subsidize the domestic production of wool. A reduction in tariffs would, then, have a double effect: it would lead to higher consumption as well as to lower domestic production of apparel wool. Should we assume that a fall in prices consequent upon the reduction of tariffs would contribute to an increase in per capita wool consumption by 0.1 kg a year, wool imports projected for the year 1975 would rise by 23 thousand tons, i.e. by about \$35 million.<sup>1</sup> The same result would be attained if the share of imported wool in the consumption of apparel

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1. Unless otherwise noted, average unit values of imports derived from trade statistics are used in the calculations.

wool were to increase by about one-tenth. Much of this gain would accrue to Australia, New Zealand, and South Africa, however.

Cotton imports into the United States are regulated by quotas while cotton exporters receive a subsidy of 8.5 cents per pound. It is difficult to speculate on the probable effects of changes in the system of protection since the United States has been a residual supplier of cotton in the last decade. Thus, the U.S. supplied the difference between world import demand and the amount made available by other exporters in any crop-year. Nevertheless, with the expansion of cotton production elsewhere, the United States is likely to have to change this policy to maintain her share in the world market.<sup>1</sup> In such a situation, U.S. cotton exports encroach upon the potential market of other producers. The effects of this policy can be indicated if we consider that a one per cent reduction in the share of the United States in the imports of other developed countries would increase the exports of other producers by one and one-half per cent, i.e., by slightly less than \$15 million in 1975.

Note further that although in some developed countries tariffs apply to hides and skins, in view of the small share of producers in less developed areas in these exports, a reduction in tariffs would have little effect on the export earnings of developed countries. On the other hand, changes in Common Market policy as regards the importation of tropical timber would lead to an increase in the imports of sawn timber at the expense of roundwood.

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1. Cf. Chapter 9.4.

## Fuels

A variety of measures are used to protect the production of coal in Western Europe. However, in making projections, we have assumed a gradual liberalization of energy policies to take place with a concomitant increase in the share of oil in European energy-consumption and hence the effects of the removal of protective measures on imports are not separately considered.

The situation is different in the United States where the maintenance of the present quota-system on petroleum and petroleum products is envisaged. Given observed differences in production costs, any increase in quotas would be accompanied by a corresponding rise in imports. Should we assume, for example, that the quotas were augmented by an amount equal to one per cent of U.S. oil consumption in 1975 and that the rise in imports took the form of crude petroleum, imports of crude oil would increase by 6.9 million tons. This increment in imports <sup>if</sup> distributed among suppliers in developing areas in proportion to their projected exports to the United States, would represent a value of \$91 million.

## Nonfuel minerals and metals

Metal ores and concentrates as well as copper and tin metal are imported duty free into Western Europe and Japan. The United Kingdom applies a small duty on aluminum, zinc, and lead imported from non-Commonwealth sources, however, while the external tariff of the EEC is 6 per cent for zinc, 7 per cent for lead, and 8.5 for aluminum. At the same time, in addition to tariffs, quotas restrict the importation of lead and zinc ores, concentrates and metal in the United States.

Common Market duties on zinc, lead, and aluminum metal will hinder

the shift from the exportation of ores to that of metal for the nonassociated countries. During the period under consideration this constraint is not likely to be of importance for the developing countries in the case of aluminum, however, and, given the smallness of the tariff and the relatively small value involved, it will have little effect on the value of lead and zinc traded.

By comparison ~~the~~ U.S. import quotas on lead and zinc ores, concentrates, and metal limit the total amount of <sup>imports</sup> / as well as imports within each category. A removal of the quotas would, then, increase imports at the expense of domestic production and would raise the share of metal in these imports. Should we assume, for example, that quotas were liberalized so as to reduce projected levels of domestic production by one-fourth and that the corresponding increment in imports would take the form of metal, lead imports would rise by about 60 thousand tons (approximately \$12 million) and zinc imports by 105 thousand tons (\$45 million). Much of these imports would originate in Canada and Australia, however, and the share of the developing countries may not exceed one-third of the total.

### Manufactured Goods

Several of the manufactured exports of the developing countries come under quantitative restrictions while others bear high duties. In practically all industrial countries, formal or informal quotas are applied on cotton textiles, which accounted for one-third of the imports of manufactures from less developed areas in 1960. France, Germany, the United Kingdom, Italy and several smaller European countries use quantitative restrictions to protect their jute manufactures and, in some countries, imports of sewing machines, bicycles, and sports goods are also restricted

by quotas.

Whereas quotas limit the exports of manufactures from developing areas in absolute terms, the application of graduated tariffs discourage the exportation of commodities in processed form. Graduated tariffs -- the progression of tariff rates according to the degree of fabrication -- are applied in the major industrial countries with regard to hides and skins, rubber, timber, cotton, jute, metals, and several foodstuffs. In the European Common Market, for example, there is no duty on hides and skins, while a 10 per cent tariff is levied on leather, and 17-20 per cent on leather manufactures. Further, cocoa beans bear a 5.6 per cent duty, cocoa butter 22 per cent, cocoa paste 25 per cent, and cocoa powder 27 per cent. Similar examples can be given with regard to the United States and the United Kingdom.<sup>1</sup>

In this connection note that the disincentive effect of graduated tariffs is actually greater than the comparison of duties would suggest since the decision for exporting a commodity will not depend on differences in duties at different levels of processing but rather on the relationship between the increment in the duty to value added in the manufacturing process. The graduation of tariffs from raw materials to semi-processed and processed goods does not continue as we move to more sophisticated products, however. While tariff rates rise from iron ore to pig iron and to steel ingots and finished articles of steel, duties again become ~~level~~ lower on much of machinery and transport equipment.

Lower tariffs on highly sophisticated products as compared to the relatively simple manufactures exported by developing countries can be

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1. For a commodity-by-commodity comparison, see [ 14 , p. 79 ].

explained by reference to the process of negotiations on trade reductions in the framework of GATT where concessions are traded for concessions. A continuation of this procedure is envisaged under the U.S. Trade Expansion Act, too, although tariff-reductions would now apply to groups of commodities rather than individual products. In this connection, it should be recalled that, under the Act, Congress has empowered the President to negotiate the elimination of tariffs in regard to commodities where 80 per cent of world exports originates in the United States and the European Common Market and/<sup>a</sup>reduction by one-half for other commodities.

A further consideration is that the application of restrictive measures on goods presently exported by developing countries also affects the expansion of production in other manufacturing industries for exportation to industrial economies. Having experienced the imposition of restrictions on commodities that have come to be exported in recent years, entrepreneurs in less developed areas may feel obliged to include their in / calculations an allowance for risk due to the possibility that restrictions would be applied to other goods as these come to be exported in larger quantities.

As to the effects of a reduction of restrictions on the manufactured exports of developing areas, the possibilities of expansion can be indicated with regard to cotton textiles, for example. Even assuming the continuation of the International Cotton Textiles Agreement, the developing countries would supply only a small part of textiles consumed in developed areas, and further liberalization would bring increased imports. Also, in view of the competitiveness of Asian jute manufacturing, the removal of quantitative restrictions in Western Europe would be accompanied by a shift in importation from raw jute to jute cloth and sacking.

Changes in graduated tariffs can also lead to increasing imports in processed form. Yet, given the uncertainties associated with the measurement of substitution elasticities between the products of developed countries and developing economies, and the virtual absence of information on long-term supply elasticities in the latter, we have not attempted to estimate the probable impact of a reduction of import restrictions on the manufactures of less developed areas. An indication of the relevant magnitudes can be given, however, if we consider that an increase of imports over projected levels by one-fourth would amount to \$0.6 billion in 1975 -- less than / <sup>one-tenth of</sup> 1 per cent of the estimated increase in the gross national product of the developed countries between 1960 and 1975.<sup>1</sup>

### 5.5.3. Possibilities for Increasing Exports from Developing Countries to Soviet-type Economies

Although efforts have been made to increase the international division of labor within the Sino-Soviet area, the centrally planned economies apparently still maintain a policy of self-sufficiency vis-à-vis the rest of the world. Comparative cost considerations play little role in the international trade of this area and imports are restricted to commodities that are not available domestically, or are not available in sufficient quantities, excepting in cases when political expediency requires otherwise. At the same time, the system of priorities applied has led to

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1. Note, however, that in regard to most of these commodities, we should set the foreign exchange equivalent of the materials used in the manufacturing process against an increase in the exports of manufactures.

limitations on the importation of consumer goods that are not produced at home, such as coffee and cocoa.

Announced plans in the countries of the Sino-Soviet area indicate a continuation of the policy of self-sufficiency in the future. Self-sufficiency is a decisive factor in the planned increase in the production of synthetic materials, for example. As noted in Chapter 4.4., the Soviet Union aims at providing 97-98 per cent of domestic rubber consumption from home production, and the FAO estimated that by 1970 the degree of self-sufficiency in rubber would reach approximately 90 per cent in the Soviet Union and 65 per cent in the other countries of Eastern Europe.

By comparison, we have assumed that, in 1970, the Soviet Union would still derive 18 per cent, and the other East European countries 40 per cent, of their rubber needs from imports of natural rubber. Still, these proportions are considerably lower than those projected for the United States (26 per cent) and Western Europe (47 per cent). Should the United States follow the American example and the other countries of Eastern Europe that of Western Europe, their rubber imports would exceed the amount projected by 162 thousand tons, i.e., \$75 million at prices assumed to apply in 1970.<sup>1</sup> The corresponding figure would be nearly one-third larger in 1975.

Similar considerations apply to cotton and wool / <sup>where</sup> we have assumed that imports from developing countries would remain at 1960 levels although national plans indicate a decrease in imports into the area.

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1. The mid-point of the FAO estimates of rubber consumption have been used in the calculations: 1550 thousand tons in the Soviet Union, and 540 thousand tons for the other countries of Western Europe [1, p. 13].

Should we assume instead that imports from less developed areas would rise at the same rate as imports into the industrial countries (20 per cent in the case of cotton and 35 per cent for wool), imports would exceed projected magnitudes by \$58 million in 1975.

For further commodities such as jute and, for a large part of the area, sugar, imports are likely to have a lower real cost than domestic production, although comparisons are difficult by reason of the absence of scarcity prices in Soviet type economies. Nevertheless, available information points to inefficiencies in the agriculture of several of the centrally planned economies as compared to Western European agriculture. Thus, arguments for the opening of markets to imports of foodstuffs in Western Europe would apply a fortiori to the Soviet bloc.

The possibilities of increased imports into Eastern Europe can further be indicated in regard to noncompeting tropical products. In the absence of limitations on imports, Soviet Russia could conceivably reach levels of coffee consumption projected for Japan by 1975 (1.5 kg instead of 0.75 kg), while Czechoslovakia and Eastern Germany could attain the level assumed for Italy (4.6 instead of 4.0 kg), and the other countries of Eastern Europe that of Yugoslavia (1.9 instead of 0.75 kg). Correspondingly, an additional 196 thousand tons of coffee would be imported to Eastern Europe, valued at \$137 million in 1960 prices. Further gains could be derived if imports of cocoa, tea, bananas, and spices were liberalized.

The Soviet Union and the more developed countries of Eastern Europe could also import labor-intensive manufactures from less developed areas. A comparison with the trade of industrial countries can be of interest here. Should we equate per capita incomes in Eastern Europe in ~~1960~~

to that of Yugoslavia,<sup>1</sup> the gross national product of this area, <sup>in the year 1960</sup> would be estimated at \$195 billion if 1955 dollars ~~in that year~~ --about one-fifth of the GNP of \$964 billion in the developed countries.<sup>2</sup> But the latter countries imported manufactured goods in the value of \$1075 million from developing economies in 1960 as against Soviet bloc imports of \$48 million. Had the countries of Eastern Europe attained the ratio between imports and GNP observed in the developed countries, they would have imported manufactures from less developed areas in the value of \$215 in 1960. And if gross national product in the Soviet bloc were to double within a decade as planned, these imports would have to reach \$600 million by 1975, considerably higher than our estimate of \$136 million for that year but lower than the \$1.5-2.0 billion projected by the UN, Economic Commission for Europe in 1980/15, v, p. 18 7.

If we were to use the same analogy with regard to the total imports of the Soviet bloc from developing countries, it would appear that in 1960 the countries of Eastern Europe should have imported \$4.0 billion worth of merchandise from less developed areas as compared to their actual imports of \$1.0 billion. But one may argue that the Soviet Union is better endowed with natural resources than are Western Europe and Japan and hence we could not apply the import/GNP ratio calculated for the industrial countries, taken together, to Eastern Europe. Should we apply the ratio observed in regard to North America instead, the imports of the countries of the Soviet bloc from developing areas would have amounted to \$2.7 billion in 1960. And, again assuming projected growth rates to be reached, these imports could surpass \$7 billion in 1975 as compared to our projection of \$1.9 billion.

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1. Estimated at \$628 for 1960 in terms of 1955 prices (Table A 2.6.2.).

### 5.5 Economic Integration in Developing Regions

Much has been said about economic integration in underdeveloped areas but, so far, little has been accomplished. In Latin America, the establishment of the Free Trade Area has been followed by tariff reductions in a limited sphere but, in the absence of provisions for automatic reductions in duties, the momentum of integration appears to be slowing-down as mutual concessions are more difficult to come by. In Africa, we could observe a process of disintegration rather than integration in recent years and although several proposals for integration have been made, it is as yet uncertain which countries will eventually participate and in what kind of integration projects. Apart from the activities of the Organization of Petroleum Producing Countries, there is hardly any regional cooperation in the Middle East, and Malaysia is the only example of an economic (and political) union in Asia.

At the same time, intra-area trade in less developed areas has declined in importance over the last decade, in part because import substitution could be effected with greater ease against the less sophisticated products imported from neighbouring countries. An extreme example is that of Asia where policies aiming at national self-sufficiency in agricultural products and simple manufactures have led to an absolute reduction of intra-area trade.

National plans do not envisage a greater degree of economic intercourse for the future either. Import substitution continues to be directed to a considerable extent against commodities produced in other developing countries and the long-term plans give few indications of an increasing **intra-regional** division of labor in manufactured goods.

Correspondingly, our projections on the future imports of less developed regions reflect the assumption that national commercial policies will be continued during the period under consideration. Yet, economic integration in

developing regions would contribute to an improvement in the current account balance of these regions by reason of the large-scale economies obtainable in a wider market. On the one hand, the exploitation of economies of scale and external economies in a large market would further the expansion of manufacturing, thereby contributing to a reduction in import requirements and, possibly, to increases in the exports of manufactures; on the other, the cost of import-substitution will be reduced as the size of the area increases.

These considerations point to the possibilities of improving the trade balance of developing regions through regional integration.<sup>1</sup> However, given the uncertainties related to future developments and the structural changes accompanying economic integration in less developed areas, no attempt has been made to estimate the probable effects of integration on international trade in the present study.<sup>2</sup> Still, the relative importance of reducing imports in the framework of regional integration projects can be indicated by reference to the fact that, under the target income alternative, a reduction in the income elasticity of import demand by one-half percentage point would represent an improvement in the current balance of the developing countries by \$1.5-1.7 billion, depending on the income assumption chosen.

## 5.6 Capital Inflow

The flow of public capital to developing areas has risen to a considerable extent in recent years. According to the estimates published by the OECD,

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1. A detailed discussion on the impact of economic integration on resource allocation, trade and growth in less developed areas is given in my forthcoming book on "Economic Development and Integration", to be published by the Centro de Estudios Monetarios Latinoamericanos in Mexico City.

2. Several years ago, the UN Economic Commission for Latin America attempted to evaluate the impact of a Latin American ----- union on extra-area imports [ 16 ] but the reliability of the estimates is open to doubt.

official contributions by the countries of the Development Assistance Committee increased from an average of \$1.9 billion in 1950-1955 to \$4.3 billion in 1959, \$4.9 billion in 1960, and \$6.1 billion in 1961 [ 4, p. 15 ].<sup>1</sup>

A number of assumptions can be made concerning future changes in the flow of public funds originating in developed countries. The continuation of the rate of increase of public assistance observed in recent years may be postulated, for example. Alternatively, we may assume that the proportion of the net flow of public capital to the gross national product of the developed countries will remain unchanged or that the goal of 1 per cent of the combined national incomes of the capital-exporting countries stipulated in the U.N. General Assembly Resolution 1717 ( VI ) will be reached.

It is suggested here that the first alternative has to be discarded since internal political considerations in the developed countries would hardly permit the continuation of the rapid rate of increase in the net amount of public assistance experienced in the recent past. Should we assume that increases in the net flow of public funds will proceed pari passu with the rise of GNP in the member countries of the Development Assistance Committee, the annual rate of increase of foreign aid would be 4.0 per cent or 4.6 per cent, depending on the income assumption chosen. A higher rate of increase would be indicated if the U.N. goal of 1 per cent of national incomes were reached since, according to an estimate of the United Nations, the relevant proportion was 0.7 in 1960 [ 12, p. 14 ].

Should we calculate with a rate of growth of 4 per cent <sup>take</sup> and/ the public assistance provided in annual average of/the years 1959-61 as a basis, the net flow of public funds

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1. The figures include, in addition to bilateral assistance to countries in less developed areas (\$3.7 billion in 1960), contributions to international organizations (\$0.7 billion), grants and loans to Greece, Spain, and Turkey (\$0.4 billion), and unallocated aid (\$0.1 billion). On the composition of this assistance, see [ 4, pp. 4, 74 ].

would reach \$7.6 billion in 1970 and \$9.2 billion. These estimates may be on the low side, however, given that official contributions reached \$6.1 billion already in 1961. On the other hand, Greece, Spain, and Turkey may continue to receive some aid, and hence the above figures may <sup>be taken to</sup> appropriately represent the future flow of public capital to developing countries.

Some increases may be forthcoming in private capital flows, too, partly in the form of new investment, and partly through the reinvestment of the income of foreign companies at the place of operation. Private investment is subject to political uncertainty, however, and it is also affected by changes in tax laws and other factors which can hardly be foreseen. Thus, projections of future capital flows are subject to a large margin of error. In the present study, we have assumed an increase in net private investment (including <sup>credit</sup> guaranteed private export/for more than one year) from the 1960 level of \$2.5 billion by one-fifth to \$3.0 billion in 1970 and by one-third to \$3.3 billion in 1975. Considering the large projected increases in the investment income of foreign companies, this appears to be a conservative estimate, although in the years 1956-1961 net foreign investment has hardly risen.

Uncertainties are attached to grants and loans originating in the Sino-Soviet area, too. While commitments of bilateral loans and grants to developing countries averaged \$1.0 billion in 1955-61, actual disbursements reached only \$186 million in 1960 and \$294 million in 1961 [ 4, pp. 13-14 ]. We have assumed here that net disbursements would amount to \$1.0 billion in 1970 and \$1.2 billion in 1975, one-sixth of which would be supplied by Mainland China.<sup>1</sup>

Note, however, that the projected amount of loans and grants from the Sino-Soviet area would still be small as compared to capital flows originating

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1. On commitments for financial assistance by China, see [ 12, p. 27 ].

in developed areas. If we assumed that the countries of Eastern Europe had one-fifth of the gross national product of the developed economies, they should have provided loans and grants in the amount of \$0.9 billion in 1960 to match the public assistance supplied by the developed countries.<sup>1</sup> On the same basis, the net flow of foreign assistance from Eastern Europe would have to reach \$1.8 billion in 1970 and \$2.5 billion in 1975.<sup>2</sup>

According to the above projections, net flow of public and private capital to developing countries would reach \$11.6 billion in 1970 and \$13.7 billion in 1975. These amounts would cover the projected balance-of-payments deficit of the developing areas, taken as a whole, irrespective/whether the most likely or the high (target) income alternative / were realized in the world economy (Table 5.2.1). The flow of capital would fall short of the current account deficit of \$12.0 billion in 1970 and \$16.6 billion in 1975 estimated under the assumption that developed countries attained "most likely" growth rates and developing economies target rates, however.

## 5.7 Conclusion

We have indicated various alternative possibilities for filling the projected gap in the current account balance of the developing countries. We have seen that, with some acceleration in the flow of public capital, the current account deficit of the developing countries, taken together, could be financed even if we assumed that national income in these countries grew at target rates and

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<sup>1</sup>The relevant figure is \$1.4 billion if the net transfer of economic resources is used as a criterion, since in the latter case private investment should be included in the calculations. We have restricted our discussion to public assistance, however, by reason of the substantial return-flow on private investments in the form of repatriated earnings.

<sup>2</sup>On assumptions regarding economic growth in Eastern Europe, see Chapter 4.4.

developed economies attained "most likely" growth rates. ~~It shall be added,~~<sup>Note</sup> however, that unrecorded reverse flows may continue to augment the current account deficit of the developing countries, although these flows are likely to decline to a considerable extent from the level experienced in 1960 when the decolonization of Africa gave rise to a capital flight.

But even assuming that unrecorded reverse flows would be of negligible proportions, various considerations suggest that full reliance should not be based on foreign assistance. To begin with, an equality between the current account deficit and the inflow of foreign capital in the less developed areas, taken together, can conceal interregional and intraregional differences. Political considerations are likely to affect the distribution of public funds, and private investors will favor some areas as compared to others. The inflow of foreign capital may continue to exceed the current account deficit of the Middle East, for example, and private investment will also be directed to areas producing nonfuel minerals.

An additional consideration is that in the absence of other measures, the in-  
capital  
flow of foreign may not appropriately serve the objective of attaining high growth rates, since barriers to exports from developing countries and industrialization will  
in the framework of narrow national markets/rodeuce the effectiveness of foreign investment. Moreover, the granting of foreign aid imposes a burden on the developed countries under conditions of full employment, while they would derive a long-run gain from decreased protection by reason of the concomitant improvement in the allocation of economic resources.

The balance-of-payments effects of <sup>a</sup>reduction <sup>in</sup> restrictions on agricultural products should not be overrated, however, We have indicated above that the once-

for-all gain derived from the elimination of tariffs and excise taxes on bananas and tropical beverages in the main industrial countries would be rather small. At the same time, given the small share of developing countries in world exports of temperate zone foods and the importation of such foods through noncommercial channels into several of these countries, it is difficult to evaluate the possible impact of a reduction of price support in the United States and a lowering of trade barriers in Europe on cereals, for example. These considerations apply to some extent also to oilseeds while developing countries would decidedly benefit from a liberalization of policies concerning sugar as well as from an increase in the imports of agricultural products into the Sino-Soviet area.

Further gains could be obtained from an increase in the U.S. quota on petroleum and, to a lesser extent, lead and zinc although the benefits would accrue to countries that have good export prospects anyway. As a result, interregional and intraregional differences in export earnings would be further accentuated.

It appears, then, that countries producing minerals and metals not only have the best export prospects among developing economies but these countries also attract foreign capital and are expected to benefit from a liberalization of trade policies in the developed countries. These disparities are likely to continue beyond 1975, inasmuch as the depletion of mineral resources in industrial economies will make them increasingly dependent on foreign sources of supply, while the growth of demand for foodstuffs will fall behind the increase in incomes. If we also consider that, after the assumed adjustment in primary product prices during the sixties, exports originating in less developed areas have been projected to rise at a rate exceeding the growth of GNP in the developed countries (Table 3.1.1), it may appear that the main problem is not so much the inadequate

growth of foreign exchange earnings of the developing countries as the uneven distribution of these earnings.<sup>1</sup>

These considerations apply especially to Asia who is expected to have over one-half of the current account deficit of the developing countries. In the absence of substantial mineral resources, Asian countries / <sup>would</sup> face increasing foreign exchange problems in the future if the production and exports of manufactured goods failed to rise. India is a good example where the demand for the main agricultural export, tea, can hardly increase at a rate exceeding the growth of population in the developed countries while, in the absence of trade barriers, possibilities of expansion in the exportation of textiles exist.

In fact, the comparative advantage of countries that are not well endowed with mineral resources will increasingly lie in labor-intensive manufactures and in industrial products that utilize domestic materials. It would be necessary, therefore, to encourage the exportation of these manufactures from less developed areas. On the part of the importing countries, appropriate measures would include a liberalization of quotas and changes in the structure of tariffs.

The developing countries would derive further gains from an acceleration of economic growth in developed economies. But the application of the proposed measures in the importing countries does not guarantee that target rates of income growth would, in fact, be attained in less developed areas. Political uncertainty can give rise to a capital flight, monetary mismanagement may hinder the use of funds obtained abroad for productive purposes, inappropriate fiscal

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<sup>1</sup>It is a different question that current accounts deficit would be rising at an increasing rate if developing countries attempted to grow at a rate faster than developed economies do.

policies may lead to a misdirection of investment activity and, last but not least, the existing social structure of a number of countries can obstruct the process of economic transformation.

Expressed differently, in order to attain target growth rates in less developed areas, it is necessary that the large majority of these countries successfully follow growth-oriented domestic policies. Should this not happen-- and there are indications, especially in Latin America, that powerful obstacles stand in the way of an acceleration of economic growth--target rates will not be reached and the current account deficit of the developing countries will be correspondingly reduced. On the other hand, the current account gap would grow if cost-inflationary pressures lead to higher prices of manufactured goods in industrial economies.

Note finally that should target growth rates be reached in developing countries, increases in income per head would still be relatively small if the rapid growth of population continued. Not only does per capita foreign assistance fall as population increases but a high rate of growth of population also leads to larger imports and smaller exports by reason of the pressure exerted on the domestic resource-base. Correspondingly, a discussion of policy-alternatives for raising living standards in developing countries cannot be complete without reference given to population problems.

The present writer suggests that the successful implementation of the objective of steadily rising living standards during the UN Development Decade, and thereafter, requires the application of a triad of policies: policies for freer trade, policies for economic growth, and a population policy. Therefore, action in one field, such as trade policy that is the subject of this volume, can have only a limited effect without measures taken in other areas.

Table A 5.1.1

Developing Countries: Receipts and Payments on Account of Services, 1960<sup>a</sup>  
 (\$ billion)

	Latin America	Africa	Middle East	Asia	Developing Countries, Total
Freight and Insurance					
Receipts	0.13	0.10	0.02	0.11	0.36
Payments	0.79	0.53	0.25	0.64	2.21
Other transportation					
Receipts	0.18	0.26	0.07	0.10	0.61
Payments	0.24	0.15	0.06	0.10	0.55
Travel					
Receipts	1.05	0.13	0.07	0.06	1.31
Payments	0.65	0.36	0.09	0.12	1.22
Investment income					
Receipts	0.07	0.17	0.04	0.12	0.40
Payments	1.46	0.36	1.17	0.46	3.45
Government					
Receipts	0.24	1.19	0.27	0.65	2.35
Payments	0.17	0.18	0.12	0.17	0.64
Miscellaneous Services					
Receipts	0.48	0.21	0.07	0.22	0.98
Payments	0.62	0.27	0.06	0.30	1.25
Services, total					
Receipts	2.15	2.06	0.54	1.26	6.01
Payments	3.93	1.85	1.75	1.79	9.32

Source: IMF, Balance of Payments Yearbook, Volume 13 and 14, and national statistical publications.

Note: (a) For several smaller countries and territories, the figures include only estimated freight expenditures, spending by foreign governments, and investment income.

Table A 5.1.2

Oil-Company Profits in Developing Areas<sup>a</sup>  
(\$ million, current prices)

	1960	1970 I	1970 II	1975 I	1975 II
Latin America	410	393	441	502	567
Africa	56	335	364	541	589
Middle East	1002	1351	1463	1569	1867
Asia	<u>56</u>	<u>83</u>	<u>104</u>	<u>117</u>	<u>152</u>
Developing countries, total	1524	2162	2372	2729	3175

Notes: (a) Figures refer to company-profits on crude oil and petroleum products exported to developed countries. In the case of the Middle East, profit on oil sold elsewhere has been separately estimated: \$30 million in 1960, \$40 million in 1970, \$50 million in 1975.

Source: Quantities exported - Tables A 10.3.2 and A 10.3.3.  
Value of exports - Table A 10.

Unit costs: our estimate in part on the basis of information provided in United Nations, Economic Development in the Middle East, 1958-1961, New York, pp. 58-59.

(\$ per ton)

	Crude Oil			Petroleum Products		
	1960	1970	1975	1960	1970	1975
LA	4.00	4.30	4.30	9.50	9.90	9.90
AF	4.30	4.30	4.30	9.80	9.90	9.90
ME	1.40	1.50	1.50	5.90	6.10	6.10
AS	6.20	6.20	6.20	11.70	11.80	11.80

Share of company profits in total profits -- our estimate in part based on Symonds, E., Oil Advances in the Eastern Hemisphere, New York, First National City Bank, 1962. United Nations, Economic Development in the Middle East, 1959-1961, New York, 1962 and Petroleum Press Service, various issues.

	1960	1970	1975
LA	67	70	70
AF	57	60	62
ME	57	60	62
AS	57	60	61.

Table A 5.4.3.

The Impact of Changes in Production and Trade Policies in  
Industrial Countries on Imports from Developing Areas

TEMPERATE ZONE FOODS						
	European Common Market			United Kingdom		
<u>Beef and veal</u>	1960	1970	1975	1960	1970	1975
Consumption, million tons <sup>a</sup>	3447	4648	5200	1135	1303	1413
index	100	135	151	100	115	124
Projected imports, <sup>b</sup>						
\$ million <sup>b</sup>	47	10	10	165	165	165
Hypothetical imports,						
\$ million <sup>c</sup>	47	63	71	165	190	205
Hypothetical less projected imports, \$ million	--	53	63	--	25	40
<u>Wheat and coarse grains</u>						
Consumption, million tons <sup>d</sup>	63.2	71.8	76.5	16.9	18.3	18.9
index	100	114	121	100	108	112
Projected imports,						
\$ million <sup>b</sup>	221	155	155	40	39	40
Hypothetical imports,						
\$ million	221	252	267	40	43	45
Projected less hypothetical imports	--	97	112	--	4	5
<u>SUGAR</u>				Industrial Countries		
Projected consumption, thousand tons <sup>e</sup>	<u>1960</u>	<u>1970</u>	<u>1975</u>			
North America	9670	11482	12623			
Western Europe	10644	12598	13958			
Japan	1336	1937	2273			
Industrial countries, total	21650	26017	28354			
Estimated increase in consumption after the removal of tariffs and excise taxes, thousand tons <sup>f</sup>						
North America	348	413	454			
Western Europe	856	869	963			
Japan	445	542	568			
Industrial countries, total	1649	1824	1985			
World market price of sugar, \$ per ton	69	69	69			
Estimated increase in consumption (imports), \$ million	114	126	137			
<u>NON-COMPETITIVE TROPICAL FOODS</u>	Increase in 1970 imports of taxes and duties reduced by					
	50% at 1957-59 prices <sup>g</sup>		50% at current prices <sup>h</sup>			
EEC and EFTA, including Portugal						
Coffee	50.0	104.0	39	80		
Cocoa	13.0	30.0	9	20		
Tea	0.7	2.1	1	2		
EEC, Bananas	2.5	5.2	2	5		
	<u>66.2</u>	<u>141.3</u>	<u>51</u>	<u>107</u>		

Table A 5.4.3. (continued)

Notes:

- a) Table 6.1.1.
- b) Table A 6 and Ch. 6.1
- c) Assuming imports to rise in proportion to domestic consumption
- d) Our estimate
- e) Table 7.2.1.
- f) Assuming average fiscal charges of 24 per cent in North America, 23 per cent in Western Europe, and 51 per cent in Japan. The corresponding arc-elasticities are -0.28, -0.5, and -1.0
- g) "Tropical Fruit and Beverages: Duties and Taxes in Western Europe" Monthly Bulletin of Agricultural Economics and Statistics, December, 1962, p. 8.
- h) FAO, Trade Yearbook, various issues and Ch. 8.

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