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**LATIN AMERICAN
TRADE POLICIES IN THE 1970's
A PROSPECTIVE APPRAISAL**

by

Daniel M. Schydrowsky

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Latin American Trade Policies in the 1970's
A Prospective Appraisal

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I. Postwar Development of Latin America: A Synopsis

Latin American economic growth in the post war period has been overshadowed by an almost continuous sequence of balance of payments crises. In part this situation has been the consequence of real factors and in part it has been merely the result of a mistaken perception. In either case the effect on the economic destiny of Latin America has been well nigh determining.

The balance of payments crises have had their origin in a number of circumstances. The first and perhaps most important of these is an inconsistency in the development policies Latin American countries have pursued. Almost all of them have had the major goal of an increase in the rate of growth of income. A higher rate of growth naturally required a higher level of imports of capital goods, raw materials and semi-manufactures. At the same time, however, Latin American countries did not adopt export promotion policies designed to make available the foreign exchange required by the imports implicit in the growth target. Thus, one of the major reasons for the recurrent balance of payments crises has been the inconsistency between the targets of income and export growth. In consequence, either the growth target had to be abandoned in toto, or growth took place in spurts and starts whenever the

The author wishes to acknowledge his intellectual debt to Ing. Marcelo Diamand of Buenos Aires with whom fruitful interchange of ideas over the years has done much to shape the views here presented. For an exposition of Mr. Diamand's analysis, the reader is referred to "Bases Para Una Política Industrial Argentina", Cuadernos del Centro de Estudios Industriales, Año 1, No. 2, Buenos Aires 1969. Appreciative thanks are also due to Prof. G. Harberler, Dr. S.E. Guisinger and Mr. D. Dapice for valuable comments and to the latter for assistance in preparing the statistical material. The data shown in Tables 5a, 6, 7, are from the country studies included in the IBRD Project on Protection in Developing Countries directed by Bela Balassa and to be published under the title The Structure of Protection in Developing Countries by The John Hopkins University Press.

balance of payments would allow it to do so. This often took the form of a few years of rapid growth, a run down of reserves, an acute balance of payments crisis, then devaluation and recession followed by a period of recuperation of reserves and finally the resumption of the cycle.

Table 1 shows the figures for Gross Domestic Product and Manufacturing Domestic Product for Argentina, Brazil, Chile, Mexico and Uruguay. Figure 1 graphs these data on a semi-logarithmic scale. It will be noticed that the cycle is clearly distinguishable in Argentina and Uruguay from 1950-1967; in Chile it has apparently receded after 1960 and in Brazil it has taken hold after 1964. Furthermore, the cycle is more pronounced in manufacturing than in total GNP.

A second element leading to balance of payments crisis has been the cycle of export revenue that affected some of the Latin American countries. This cycle in itself would not have been harmful had it been recognized as such, however, there has been a tendency to assume that every upturn of export revenue would be permanent. As a result, higher level of export earnings led quickly to greater imports and expansion of domestic activity which then proved unsustainable as the export cycle turned down. The ensuing downward adjustment has always been quite painful.

A third contributing element has come from the fluctuations in the capital account. Consistent with the upturns and downturns of the general economic situation and with the total economic and political climate in each nation rather sizeable capital flows on private as well as official account have taken place. These flows have been prone to rapid turnarounds, often in anticipation of acute balance of payments crises, with the ensuing outflows leaving even less foreign exchange available for import. Once again, as in the case of export cycles, had increases in capital inflows been regarded as cyclical rather than secular, the adjustment process to reverse flows would have been substantially less painful.

Table 1

GROSS DOMESTIC PRODUCT OF SELECTED LATIN AMERICAN**COUNTRIES 1950-67**

(Units of Local Currency at Constant Prices)

	1950	1951	1952	1953	1954	1955	1956	1957	1958	1959	1960	1961	1962	1963	1964	1965	1966	1967
Argentina																		
Total GDP	710	739	692	741	769	822	835	881	945	890	961	1028	1009	974	1052	1142	1136	1158
Total Manuf.	192	196	191	191	204	227	238	257	282	260	284	312	298	284	327	369	364	
Brazil																		
Total GDP	376	395	417	431	464	496	505	540	575	618	659	707	745	757	780	810	846	882
Total Manuf. ^{1/}	42.1	44.8	47.0	51.1	55.4	61.3	65.5	69.2	80.5	90.9	100.	110.8	119.3	120.2	126.2	120.2	134.4	
Chile^{2/}																		
Total GDP	9983	10415	11009	11584	11632	11616	11682	12908	13261	13189	14059	14929	15672	16412	17099	17956	19137	19800
Total Manuf.	2240	2353	2339	2654	2750	2910	2849	3239	3288	3109	3207	3484	3885	4049	4293	4567	4911	
Colombia																		
Total GDP	1469	1515	1610	1708	1826	1898	1975	2019	2068	2213	2304	2418	2540	2624	2781	2870	2999	3120
Total Manuf.	191	197	211	223	251	267	287	300	313	338	359	378	406	425	450	471	503	
Mexico																		
Total GDP	41.1	44.2	45.9	46.0	50.9	55.3	59.0	63.4	66.9	68.9	74.3	76.9	80.7	85.9	94.6	99.6	107.0	114.0
Total Manuf.	8.4	9.3	9.7	9.6	10.6	11.6	12.9	13.8	14.5	15.8	17.1	17.7	18.9	20.6	23.5	25.2	27.8	30.2
Uruguay																		
Total GDP	12208	13214	13161	14011	14813	15045	15306	15454	14909	14491	15005	15460	15124	14969	15566	15711	11113	
Total Manuf.	2355	2638	2654	3092	3289	3303	3481	3545	3502	3360	3464	3378	3383	3348	3598	3620	3649	

^{1/}Volume index. ^{2/} Data before 1960 not comparable with data after 1960.

SOURCE: OECD, National Accounts of the less Developed Countries

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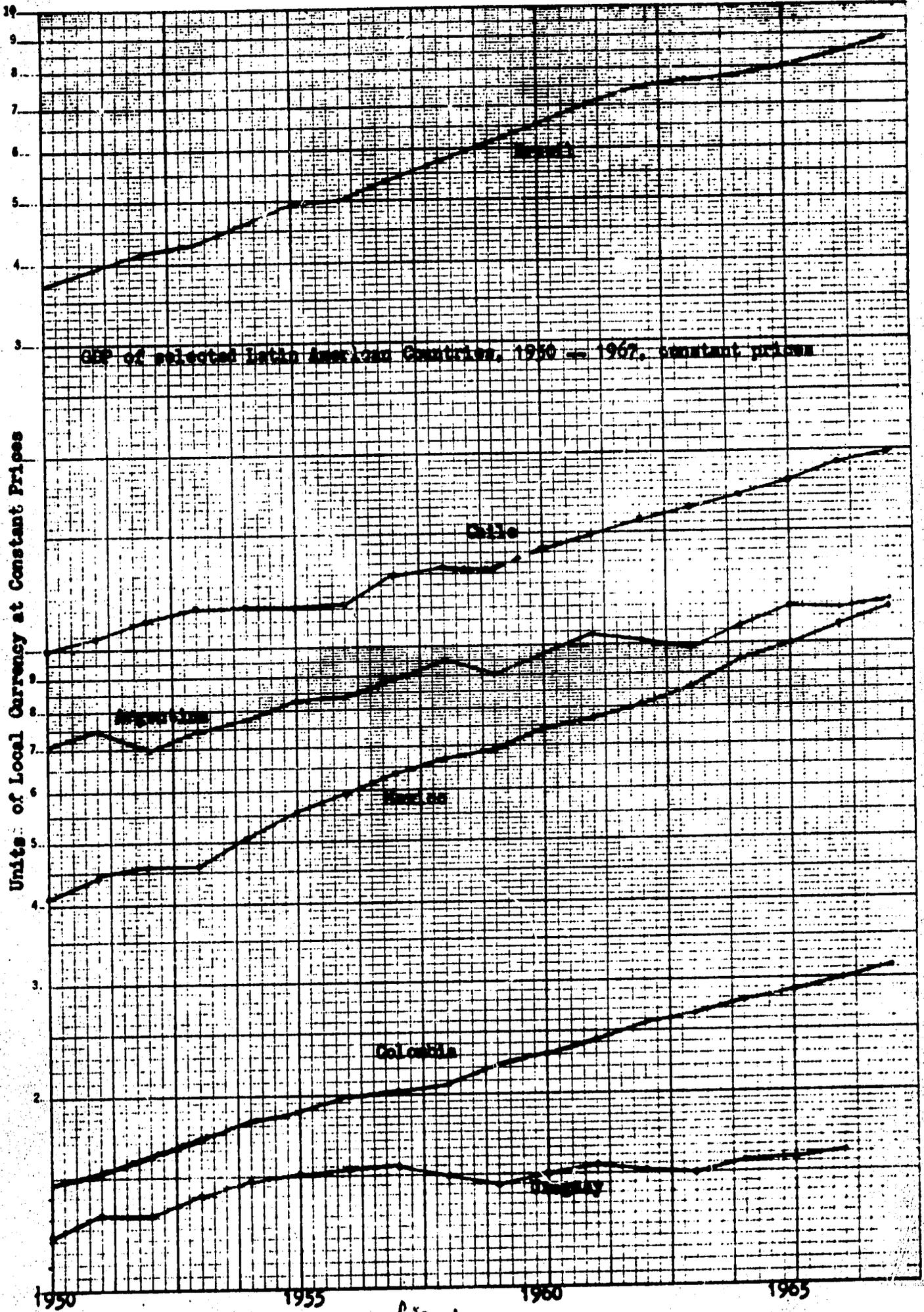


fig. 1 a

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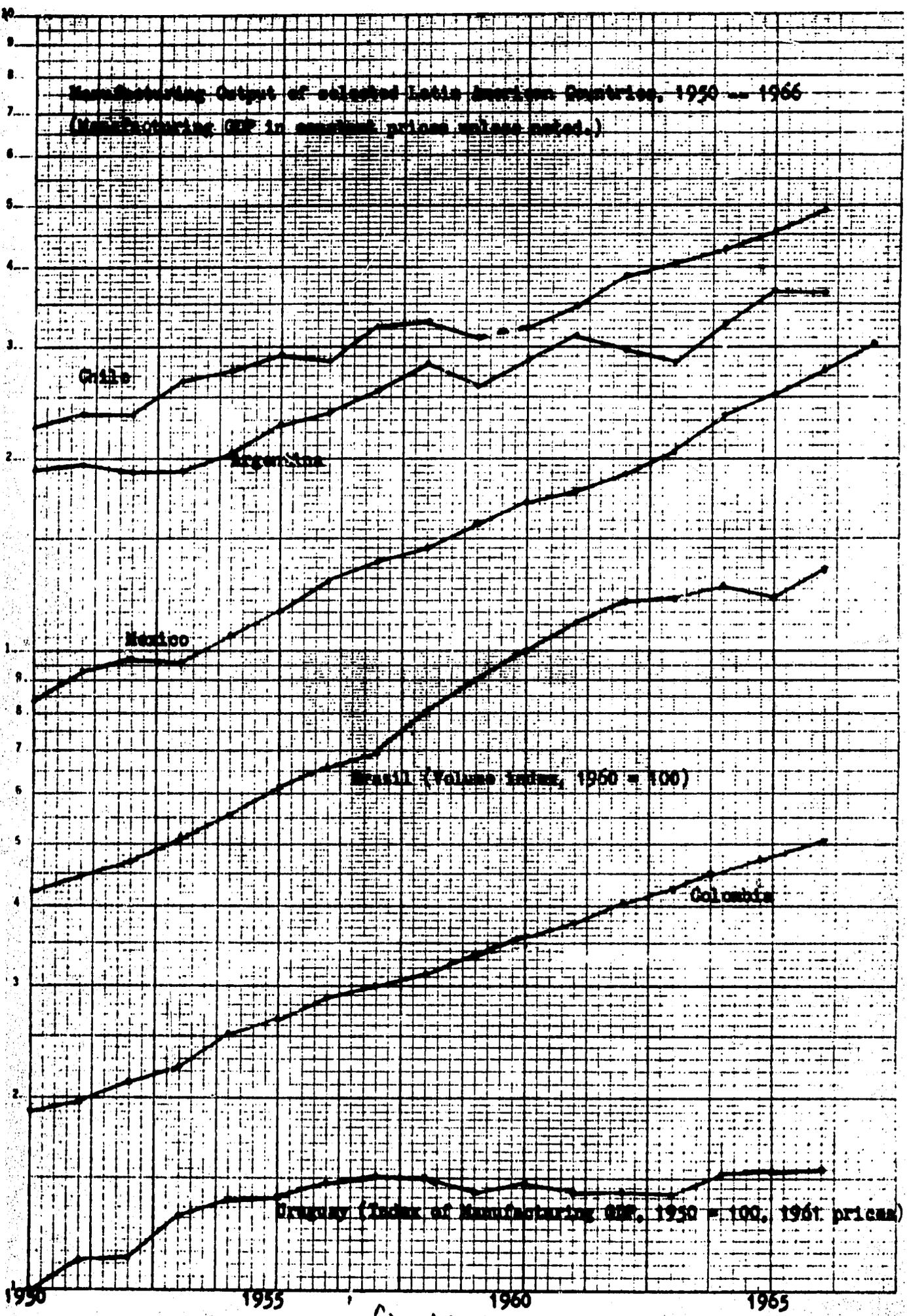


fig. 16

Capital Flows for Selected Latin American Countries, 1950 -- 1967

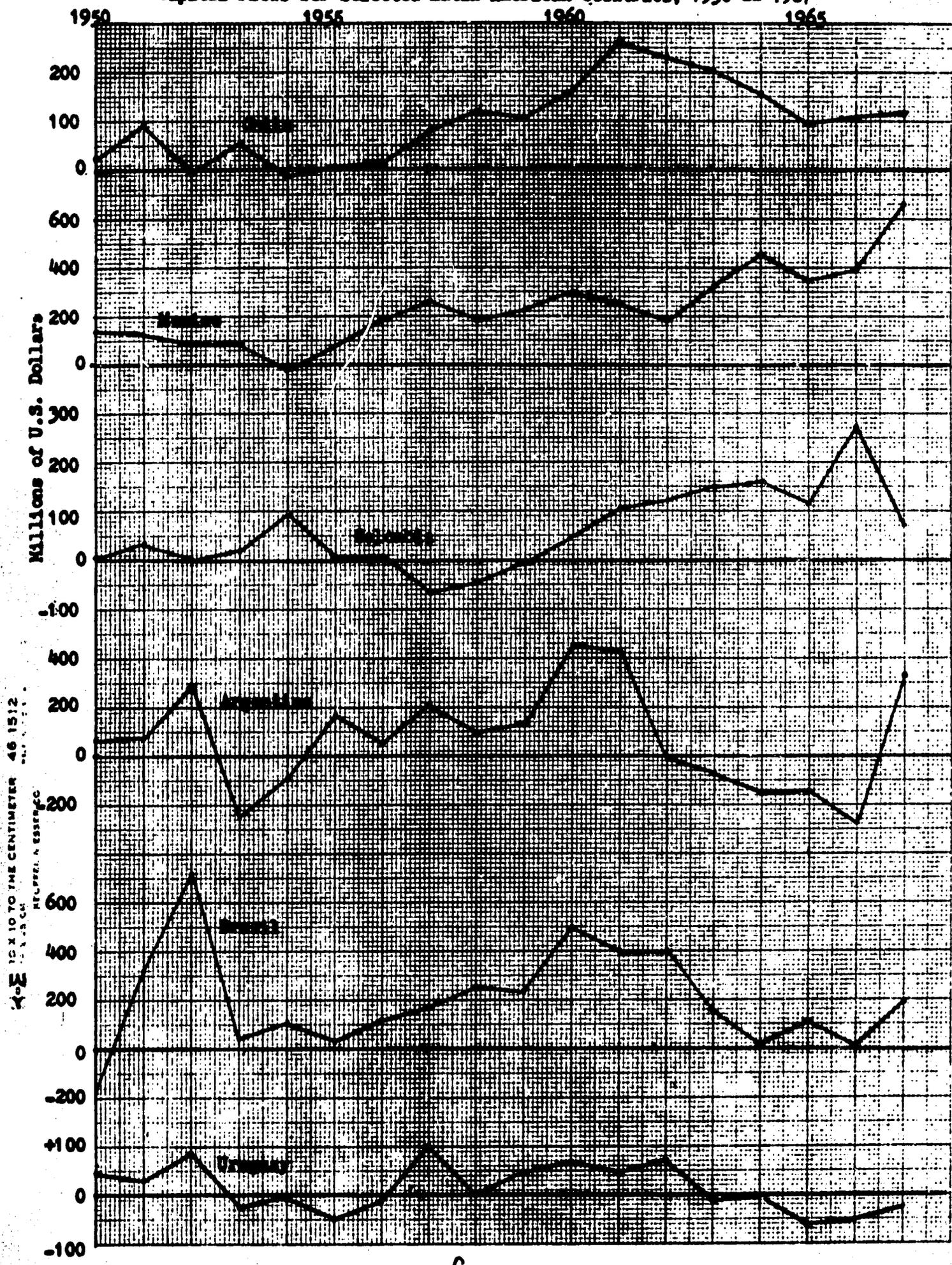


fig 26

Table 2 summarizes the export performance and capital flow data for Argentina, Brazil, Chile, Colombia, Mexico and Uruguay whereas Figure 2 presents them in graphical form. It is readily appreciated that the fluctuations have been rather considerable.

The main policy adopted to deal with the balance of payments problems can best be described as import substitution. This policy has been very attractive in part because it seems to be an obvious answer to a balance of payments problem. If the amount of imports necessary to maintain output at any given level can be reduced, then a reduction in the availability of foreign exchange will cause a smaller decrease in the level of activity. At the same time, import substitution contributes to the fostering of industry, and industrial growth has been regarded in Latin America as one of the intrinsic components of economic growth. Furthermore, once under way, the policy tended to create its own constituency among the new industrialists and industrial laborers who were its beneficiaries.

Import substitution was implemented throughout Latin America by the use of high and increasing import duties combined at times with quantitative restrictions, pre-import deposits, multiple exchange rates and other devices. Import duties of 100% or more, or equivalent quantitative restrictions or multiple exchange rates, became the rule rather than the exception and were justified very often on traditional infant industry grounds but just as commonly as generalized protection of the balance of payments.

By superficial measures of success, the policy of import substitution for some time brought satisfactory results. The ratio of imports to income

Table 2

EXPORTS AND CAPITAL FLOWS^{1/} FOR SELECTED LATIN AMERICAN COUNTRIES 1950-67

(millions of U.S. \$)

	<u>1950</u>	<u>1951</u>	<u>1952</u>	<u>1953</u>	<u>1954</u>	<u>1955</u>	<u>1956</u>	<u>1957</u>	<u>1958</u>	<u>1959</u>	<u>1960</u>	<u>1961</u>	<u>1962</u>	<u>1963</u>	<u>1964</u>	<u>1965</u>	<u>1966</u>	<u>1967</u>
Argentina																		
Exports	1188	1399	866	1240	1161	1068	1099	1114	1093	1148	1238	1195	1379	1502	1565	1662	1795	1707
Cap. Flow	64	76	292	-247	-93	172	54	204	99	133	447	434	-2	-76	-153	-141	-276	327
Brazil																		
Exports	1401	1833	1485	1654	1662	1537	1635	1590	1409	1435	1459	1540	1328	1528	1558	1747	1875	1840
Cap. Flow	-163	320	720	46	108	35	113	169	256	238	500	401	400	153	24	112	16	191
Chile																		
Exports	331	419	512	382	446	536	526	442	414	488	551	521	567	564	682	788	982	997
Cap. Flow	24	92	-1	54	-13	6	18	80	119	107	160	265	231	206	157	96	108	117
Colombia																		
Exports	432	506	523	666	716	642	733	680	614	610	589	578	571	590	749	709	662	715
Cap. Flow	3	33	2	20	96	7	8	-64	-44	-5	48	105	121	148	160	16	271	71
Mexico																		
Exports	803	981	974	938	1055	1332	1392	1335	1343	1438	1354	1436	1564	1699	1824	1972	2132	2145
Cap. Flow	139	124	89	91	-18	78	185	260	184	225	299	253	182	321	451	341	389	663
Uruguay																		
Exports	293	276	239	297	279	197	227	155	168	139	171	221	197	207	231	253	248	230
Cap. Flow	47	32	87	-23	-2	-47	-11	102	3	47	70	48	71	-10	-1	-61	-52	-27

^{1/} Calculated as imports minus exports plus (minus) the increase (decrease) in official reserves.
 SOURCE: IMF, Balance of Payments Yearbook; International Financial Statistics, various years.

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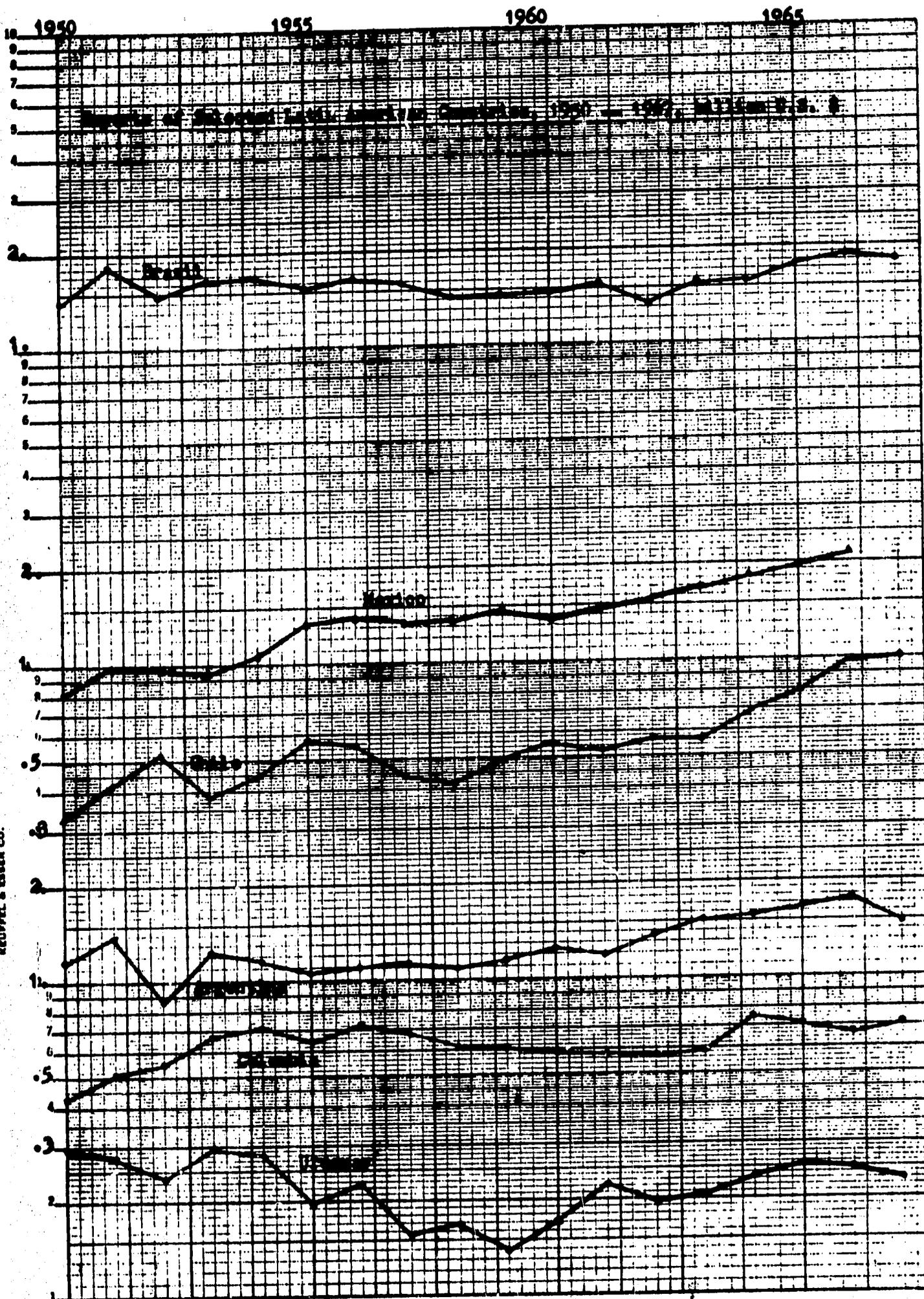


fig 2a

fell considerably in the early stages of import substitution in those countries that assiduously practiced the policy and although after a time the ratio ceased falling, it stabilized on a level substantially below its initial one. The portion of this development occurring from 1950 to 1967 can be followed in Table 3 which tabulates the ratio of total imports to GDP for Argentina, Brazil, Chile, Colombia, Mexico and Uruguay. In terms of the growth of industry, the policy can also chalk up rather substantial successes. As can be seen from Table 4, in almost all the Latin American nations, the rate of growth of industry substantially exceeded the rate of growth of total GNP. Thus the countries which applied an import substitution strategy should on the whole be expected to be very satisfied with the outcome of their policy. Such, however, is not the case.

The first major difficulty arising out of the import substitution strategy appeared in connection with the external dependency of Latin American nations. It had been expected that import substitution would isolate the Latin American economies from the fluctuations of their external account. In the event, however, they have become, if anything, more dependent. Rather than being importers of a wide variety of consumer and producer commodities, some of which could be temporarily restricted with little pain in the event of a balance of payments crisis, Latin American countries after import substitution found themselves importing only essential raw materials and capital goods. This implied that if a reduction of imports became necessary, it would perforce take place in the form of lower imports of raw materials or capital goods, thus directly affecting the growth rate and/or the level of industrial employment in the economy. Thus, prior to import substitution a decline in imports implied mainly a tighter belt for consumers; after import substitution a reduction of imports meant unemployment and a lower rate of growth. A dramatic

TABLE 3

1/
THE EVOLUTION OF IMPORT COEFFICIENTS IN SELECTED
LATIN AMERICAN COUNTRIES

1950 - 1967

	<u>1950</u>	<u>1951</u>	<u>1952</u>	<u>1953</u>	<u>1954</u>	<u>1955</u>	<u>1956</u>	<u>1957</u>	<u>1958</u>	<u>1959</u>	<u>1960</u>	<u>1961</u>	<u>1962</u>	<u>1963</u>	<u>1964</u>	<u>1965</u>	<u>1966</u>	<u>1967</u>
Argentina	.126	.181	.151	.099	.116	.132	.122	.133	.119	.106	.127	.142	.136	.108	.120	.104	.112	.109
Brazil	.065	.111	.100	.071	.078	.060	.061	.066	.056	.054	.057	.049	.046	.043	.037	.036	.045	.047
Chile	.12	.15	.15	.13	.13	.15	.16	.15	.13	.14 ^{2/}	.172	.186	.172	.160	.165	.155	.189	
Colombia	.215	.240	.216	.268	.292	.285	.266	.212	.190	.175	.206	.210	.208	.198	.226	.177	.224	
Mexico	.162	.216	.203	.200	.183	.185	.211	.212	.194	.180	.195	.187	.185	.191	.204	.206	.200	
Uruguay	.222	.293	.229	.178	.232	.182	.168	.199	.133	.141	.180	.174	.196	.156	.167	.178	.135	

1/
Ratio of imports to GDP. "Imports" are debit item on Goods and Services Account in IMF Balance of Payments Yearbooks, in dollars. GDP is in constant prices, local currency. Imports are converted to local currency either (a) at the official rate of the year of constant prices or (b) at the implicit rate, being a ratio of CIF merchandise imports in local currency to CIF merchandise imports in dollars of the base year.

2/
GDP data before 1960 not comparable with that afterwards. Escudo rate of 3.4 per \$ used throughout.

Table 4

**The Growth of Domestic Product and of
Manufacturing in Selected Latin
American Countries
1950-52 to 1964-66**

<u>Country</u>	<u>GDP</u>	<u>Manufacturing GDP</u>
Argentina	3.2%	4.4%
Brazil	5.3	7.8
Chile	4.0	5.0
Colombia	4.6	6.4
Dominican Republic	5.1	5.9
Guatemala	4.8	6.3
Honduras	3.6	6.8
Jamaica	7.4	8.1
Mexico	6.1	7.6
Nicaragua	5.8	7.5
Panama	6.4	9.8
Paraguay	3.1	2.6
Uruguay	1.5	2.5
Venezuela	6.4	9.3

SOURCE: OECD, National Accounts of Less Developed Countries

example of the evolution of the role of imports is offered by the Brazilian data tabulated in Table 5.

The second unexpected and undesirable consequence of this policy of import substitution followed directly from the first. As a result of the greater dependency on imported raw materials resulting from the first round of input substitution, a renewed effort was made to cut down the dependency on imported inputs by means of further substitution. This, however, required diverting scarce foreign exchange from "maintenance imports" (i.e., raw materials and intermediate goods for existing industries) to the import of capital goods for the installation of additional capacity. A restriction on the availability of maintenance imports, however, lead to increasing excess capacity in established industrial plants. Thus, Latin America found itself suddenly with industrial plants being operated at a fraction of rated capacity. The increase in industrial costs that ensued was validated with further protection. With the industrial sector often contributing upwards of 20% of GNP, the magnitude of the social waste implied by excess capacity is rather substantial. An estimate of its size can be derived from Argentinian data where capacity utilization has fluctuated between 55% and 67% from 1961 to 1965.^{1/} Taking an average of 60% utilization and considering a target of 90%, Argentina could have had a 50% higher industrial output. Since industry contributes 30% to 35% of GNP, this implies that total (and per capita) national income could have been some 15% higher each year. Thus, even excluding investment effects out of the higher income, excess capacity meant that Argentina lost one year's worth of GNP every six years.

^{1/} Conade, Results of the Survey on Production and Investment Expectation of Industrial Enterprise, Buenos Aires, March 1965, Table 3.

Table 5

THE ROLE OF IMPORTS IN BRAZIL

1949-1964

(a) Imports as Percentage of Total Supply of Manufactured Products by Use

<u>Year</u>	<u>Consumer Goods</u>		<u>Producer Goods</u>		<u>All Manufactures</u>
	<u>Durable</u>	<u>Non-Durable</u>	<u>Intermediate</u>	<u>Capital</u>	
1949	60.1	3.7	25.9	59.0	19.0
1955	10.0	2.2	17.9	43.2	11.1
1959	6.3	1.1	11.7	34.5	9.7
1964	1.6	1.2	6.6	9.8	4.2

(b) Percentage Composition of Imports by Use

	<u>Consumption Goods</u>	<u>Intermediate and Raw Material</u>	<u>Investment Goods</u>	<u>Total (in U.S. millions of \$)</u>
1949	18%	45%	37%	1,112.
1955	9%	59%	32%	1,300.
1959	6%	52%	42%	1,371.
1964	8%	62%	30%	1,258.

SOURCE:

- (a) Joel Bergsman and Pedro S. Malan, "The Structure of Protection in Brazil", IBRD mimeo., Table 6.2.
- (b) ECLA, Statistical Bulletin for Latin America, selected issues.

II. The Legacy for the 1970's

Latin America enters the 1970's with a set of unusually diversified economies. Far from having specialized according to their comparative advantage, these economies have spread their productive effort over most economic sectors and are operating them at widely differing levels of productivity. An indication of the extent to which Latin American economies have departed from the principle of comparative advantage in choosing the sectors to operate can be derived by calculating the real productivity of each of their existing economic sectors in terms of the amount of foreign exchange produced by a unit of domestic currency worth of domestic factors of production (labor, capital, etc.). The reasoning behind this calculation is as follows: in the Latin American economies most of the goods which make up gross national product are either export commodities or import competing commodities. It is therefore possible to scale them in terms of their international price, be it the export price (FOB) or the import (CIF). Thus it is possible to speak of a dollar's worth of radios, a dollar's worth of sewing machines or a dollar's worth of wheat. Similarly, the material inputs required to produce radios, sewing machines, etc. can also be valued at their international price. Subtracting the international value of the inputs from the international value of the output, we obtain a net amount of foreign exchange which corresponds to the net dollar worth of the economic activity performed, (i.e. value added at international prices). On the other hand, we can value domestic factors of production at their social cost and determine the peso worth of domestic factors used. If we now relate the net dollar worth of output on the one hand to the peso worth of factors used on the other, we can calculate for each economic activity the number of dollars produced per peso of factors. Or conversely we can define how many pesos worth of factors are necessary in each activity to produce a dollar's worth of output. The latter quotient is generally called the domestic resource cost of foreign exchange. It is worth mentioning here that it is possible to calculate this indicator

for each transforming activity in the economy, i.e., weaving, spinning, etc.; it is also possible to calculate it for each commodity in the economy. These two calculations will provide different indices of productivity, since each product results from the accumulation of different economic activities. Thus, textile cloth is a result of the activities of growing cotton, ginning cotton, spinning, weaving, and finishing. For our purposes it is more appropriate to look at each activity rather than each commodity, since the opportunity is open to the Latin American economies to import and export raw materials and intermediate goods as well as final consumption and investment goods.^{1/}

The domestic resource cost of foreign exchange for each processing activity is tabulated in Table 6 for the economies of Chile, Brazil and Mexico. In these tables domestic factors have been valued at their market prices since data on the breakdown of value added and on the relevant social prices is not available. Furthermore, in order to simplify comparison the domestic resource cost is standardized in terms of the financial exchange rate, i.e., a domestic resource cost of 2100 escudos per dollar is shown as 2, since the financial exchange rate in Chile for the relevant year (1961) is 1050 escudos per dollar.

The diversification of Latin American economies described above has been produced by a very particular form of exchange rate system. In usual parlance the exchange rate refers to the number of units of local currency that is obtained for one unit of foreign exchange, usually one dollar, in the financial market. For economic analysis purposes, however, the "commodity" exchange rates are equally relevant and important. Each commodity exchange rate is defined as the number of units of domestic currency for which a dollar's worth (at international prices) of that particular commodity sells on the internal market. In general there will be as many commodity exchange rates as the

^{1/} For an extensive discussion of the measurement of comparative advantage Cf. Balassa, Bela and D.M. Schydrowsky, "Effective Tariffs, the Domestic Cost of Foreign Exchange and the Equilibrium Exchange Rate", Journal of Political Economy, May/June 1968.

Table 6

THE PRODUCTIVITY PROFILE^{1/} OF SELECTED LATIN AMERICAN COUNTRIES

<u>Industry</u>	<u>Brazil</u>	<u>Chile</u>	<u>Mexico</u>
	<u>1967</u>	<u>1961</u>	<u>1960</u>
Non-Metallic Mineral Products	1.47	3.48	1.97
Metallurgy	1.44	3.62	1.73
Machinery	1.38	1.89	1.08
Electrical Equipment	2.72	2.17	1.13
Transport Equipment	2.15	2.07	1.3-1.5
Wood Products	1.27	1.22	1.30
Furniture	3.08	3.24	-----
Paper and Products	1.78	1.46	1.82
Rubber Products	2.42	2.22	1.34
Leather Products	2.13	11.94	2.45
Chemicals	1.48	2.11	1.24-1.35
Pharmaceuticals	1.48	-----	1.09
Perfumes and Soaps	-3.15	-----	1.52-1.95
Plastics	1.99	1.48	-----
Textiles	5.12	9.64	1.22*
Clothing	2.93	5.18	336.6
Food Products	1.55	54.5	1.23
Beverages	7.02	9.27	3.92
Tobacco	2.47	2.46	2.24
Printing and Publishing	1.93	1.93	1.55
Metal Products	-----	1.46	1.62
Fertilizers and Insecticides	-----	-----	1.06

* Cotton Textiles

^{1/} Cost of producing a dollars worth of value added in each activity as a multiple of the official exchange rate.

SOURCES:

Bergsman, J. and Pedro S. Malan, "The Structure of Protection in Brazil", Table 6.6.

Jeanneret, T., "The Structure of Protection in Chile", Table 7.8.

Bueno, G., "The Structure of Protection in Mexico", Table 8.7.

IBRD Project on the Study of Protection in L.D.C.'s, B. Balassa, Director.

economy has commodities tradable internationally and often a single commodity may have more than one rate. All the commodity exchange rates together with the financial rate form the exchange rate system. In Latin America, most countries operate with a set of import restrictions which raise the commodity exchange rates for imports substantially above the financial exchange rate. On the export side, some countries have operated at times with an export tax on traditional export commodities which has reduced the commodity exchange rate for traditional exports below the financial exchange rate. The net result is analogous to a multiple exchange rate system. Thus, for example, Argentina was operating in 1966 approximately with the following exchange rate system:^{1/}

<u>RATE</u>	<u>Composition</u>	<u>Pesos per \$</u>
Agricultural Export	= Financial less 10% tax	= 200
Financial	= Financial	= 220
Non-traditional Export	= Financial + 18% tax rebate	= 260
Raw Material Import	= Financial + 50% duties	= 330
Semi-manufactures Import	= Financial + 120% duty	= 460
Components Import	= Financial + 175% duty	= 600
Finished Products Import	= Financial + 220% duty	= 700

It is worth noting that with this kind of an exchange rate structure it is almost impossible for industrial exports to take place. This is simply the consequence of the interaction of the exchange rates applying to import commodities and to non-traditional export commodities. Consider the normal industrial manufacturer in the Argentina example given above. He will purchase his inputs on the basis of an exchange rate ranging from 330 pesos to 600 per dollar,

^{1/} Taken from "Proyecto de Modificación de la Estructura Arancelario-Cambiaría", Cámara Argentina de Radio, Televisión, Telecomunicaciones y Afines (CARTTA), September, 1966.

^{2/} If the inputs are imported, this is obvious. It also holds broadly for domestic inputs, however, since the domestic producer is unlikely to sell at much below the price of similar imports.

the wage rate he pays will be based on the average industrial exchange rate of about 600 pesos per dollar. Thus his costs are based on exchange rate of 450 to 500 pesos per dollar. At the same time he is requested to export at 260 pesos per dollar. It is hard to see how the Argentinian industrialist could be expected to operate in the export market in face of such an exchange rate structure. Unfortunately, this type of situation is rather widespread in Latin America as can be seen from the data for Brazil, Chile and Mexico shown in Table 7. The ratio presented relates for each industry factor remunerations payable on the basis of export business to factor remunerations currently being paid (on the basis of sales in the domestic market). Thus a ratio of .5 means that export sales would only allow payment of half the current wages, salaries, interest, profit, etc. At the same time, a ratio of .5 can signify that export sales can only go forward if the industry concerned has costs or can cut costs to one-half of current factor payments. It is clear from Table 7 that Latin America takes as heritage into the 1970's an exchange rate system with a structure substantially biased against non traditional exports.

An additional and very important effect of the exchange rate structure is what may be called the inefficiency illusion of Latin American industry. It is generally "known" that Latin American industry is inefficient and uncompetitive. This "fact" is easily demonstrated by translating its costs into dollars: they turn out to be substantially above the price of comparative imports. This operation naturally uses the financial exchange rate. Since we know that domestic costs are based on the commodity exchange rates and these are usually considerably above the financial exchange rate, it should not surprise us very much to find that domestic costs will be higher than international prices when converted at an exchange rate lower than the one on which they are based. This expected phenomenon, in the absence of the obvious explanation has produced the

Table 7

**THE ANTI-EXPORT BIAS OF THE EXCHANGE RATE
SYSTEM IN SELECTED LATIN AMERICAN COUNTRIES**

Percentage of actual factor remuneration
payable on the basis of export sales

<u>Industry</u>	<u>Brazil</u>	<u>Chile</u>	<u>Mexico</u>
Non-Metallic Mineral Products	.64	NVA	1.06
Metallurgy	.68	NVA	.49
Machinery	.71	.03	.57
Electrical Equipment	.36	.11	.71
Transport Equipment	.46	.15	.57**
Wood Products	.78	.30	.75
Furniture	.32	NVA	-----
Paper and Products	.54	.21	.38
Rubber Products	.41	NVA	.53
Leather Products	.43	NVA	.61
Chemicals	.66	NVA	.5
Pharmaceuticals	.66	-----	.65
Perfumes and Soaps	NVA	-----	56-.77
Plastics	.49	.34	-----
Textiles	.68	NVA	.79*
Clothing	.34	NVA	.83
Food Products	.66	NVA	.59
Beverages	.14	NVA	.55
Tobacco	.40	.04	.53
Printing and Publishing	.52	.31	.77
Metal Products	-----	.28	.48
Fertilizers and insecticides	-----	-----	.77

NVA = negative value added, i.e.: no payments to factors feasible

* Cotton textiles

** Railroad equipment only; motor vehicles have NVA

SOURCES:

Bergeman, J. and Pedro S. Malan, "The Structure of Protection in Brazil", Table 6.6.

Jeanneret, T., "The Structure of Protection in Chile", Table 7.8.

Bueno, G., "The Structure of Protection in Mexico", Table 8.7.

IBRD Project on the Study of Protection in L.D.C.'s, B. Balassa, Director

inefficiency illusion effect and given Latin American governments and public the impression that they have an industrial structure totally out of kilter and hopelessly inefficient. The fact of the matter is, however, that much of the inefficiency is merely the result of an improper comparison by the use of an exchange rate that is not applicable to the respective costs. When domestic costs are deflated by an appropriate exchange rate, i.e., one that is related to the commodity exchange rates, it turns out that Latin American industry is substantially more efficient than generally believed. An indication of the size of this effect can be derived from the data for Brazil shown in Table 8.

The pattern of nonspecialization of the Latin American economies and the large differences in the real productivity between the primary producers and the newer industrial sectors also explain the difficulties that the balance of payments adjustment mechanism has faced in Latin America. Under conditions of specialization approximating those called for by comparative advantage and where differences in real efficiency between sectors are rather small, the burden of adjustment to a shortage of foreign exchange or a desire for additional imports falls upon two variables: the level of real income of the country and the relative prices of traded and domestic goods. A balance of payment deficit is absorbed by exporting more, importing less, and having a lower level of real income. The concomitant is usually that new commodities become exportable as well as that traditional exports expand in volume. In Latin America, it has been very difficult to incorporate new commodities into the export trade because the size of devaluation necessary to overcome their cost disadvantage has been of such a magnitude as to call forth reactions of income receivers that nullify the devaluation. Thus all the adjustment has had to be borne by the income variable and this has been one of the major reasons why balance of payments adjustment processes in Latin America have often

Table 8

THE "INDUSTRIAL INEFFICIENCY ILLUSION" IN BRAZIL

Excess of domestic price (=cost) over international price

<u>Sector</u>	<u>At Financial Exchange Rate</u>	<u>At Industrial Cost Exchange Rate</u> ^{1/} _{2/}
Non-Metallic Minerals	40%	- 5%
Metallurgy	34	-10
Machinery	34	-10
Electrical Equipment	57	6
Transport Equipment	57	6
Wood Products	23	-17
Furniture	68	13
Paper and Products	48	0
Rubber Products	78	20
Leather Products	66	12
Chemicals	34	-10
Pharmaceuticals	37	- 7
Perfumes and Soaps	94	31
Plastics	48	0
Textiles	81	22
Clothing	103	37
Food Products	27	-14
Beverages	83	24
Tobacco	78	20
Printing and Publishing	59	7

^{1/} Derived as follows - rate for intermediate products 1.49
rate for wages 1.48
1.48

^{2/} A negative sign indicates domestic price is below international price.

SOURCE: Joel Bergsman and Pedro Malan, op. cit., Table 6.6 and 6.8

taken the form of a reduction in industrial activity and unemployment, i.e., a recession if not a depression.

III. Action in the 1970's: Industrial Exports to the More Developed Countries

Industrial exports to the more developed countries are a fundamental policy goal for the 1970's from several points of view. In the first place it is difficult to imagine a manner in which the excess capacity existing in the industrial sectors of the Latin American countries can be put to use without requiring the generation of industrial exports. It is probable that by expanding domestic aggregate demand in the Latin American economies, a market for most of the industrial produce potentially available could be created. At the same time, however, such action would also generate a need for additional imports which would be impossible to satisfy with the existing level of export and other foreign exchange revenues. In consequence, it becomes indispensable to export part of the industrial produce generated by putting the excess capacity to use in order to pay for the imports needed to maintain the higher level of operation of the economy. In the second place, in many Latin American countries the potential for import substitution has been exhausted to a large extent. As a result, industrial growth would have to slow down to the rate of expansion of the domestic market thus ceasing to be an engine of growth, or industry must break into the export market. Thirdly, the present bleakness of the unemployment situation and its prospective deterioration make the creation of more jobs exceedingly urgent.^{1/} As a consequence of these employment effects, the utilization of excess industrial capacity and the maintenance of a high rate of industrial growth acquire a human and political dimension which heightens the essentiality of generating industrial exports.

^{1/} Urban unemployment has been determined by surveys for various Latin American cities to be between 5% and 16%; ILPES has estimated the overall unemployment rate to be about 11% which rises to 25% if the underemployed are included. At historical growth rates of output overt unemployment is estimated at 18% for 1980. For a detailed survey of this situation Cf. "The Unemployment Problem in Latin America", Organization of American States, Third Interamerican Conference of Ministers of Labor on the Alliance for Progress, Document 10. 18 September, 1969.

Finally, the existence of large and growing industrial exports from the less developed countries would produce a substantial change in the process of balance of payment adjustment. In the absence of industrial exports, as has already been mentioned, the adjustment has to be borne almost totally by the income effect with the consequent unemployment and other utilization of capacity problems. In the presence of industrial exports with their narrower productivity differentials, the adjustment process of Latin American countries would become much more similar to that of developed countries. As a result, devaluations would become a more effective policy tool and it is quite likely that inflation-devaluation cycles would become much less common to the Latin American countries than they have been in the past.

In order to generate these exports of industrial commodities to the developed countries a number of conditions have to hold. Among these, the following can be enumerated; a) Price competitiveness in the buying markets is required; b) Competitiveness in quality is required; c) Commercial channels must be activated; d) Information must be available in the less developed countries on the markets and demand in the developed countries; e) A decrease in the perceived risk of exporting must take place in the less developed countries.

Among these various conditions the one most amenable to policy action on the part of governments is price competitiveness. In order to assess the magnitudes involved, it is useful to analyze first the process of price formation in the multicountry multiproduct world and then to explore some actions that developed as well as less developed countries can take to narrow the gap between the price in the developed countries and the cost in the less developed countries.

Consider first the situation in which there is one developed country and numerous less developed countries, with the former exporting industrial products to the latter where in turn a certain amount of industrial produc-

tion goes on behind tariff walls. In such a situation the prices of import competing goods in the less developed countries would be expected to be approximately equal to the prices of similar commodities in the developed country but for the tariff imposed on the imports of these commodities and the transportation costs incurred in bringing them from the developed country to the less developed ones. Thus, if there are no significant monopolies in the production of goods in the less developed countries, we would expect the difference of the cost of production in these less developed countries and the prices in the markets of the developed country to be approximated by the tariffs against imports in each of the less developed countries and the respective transportation costs. To the extent that there are import competing monopolies in the LDC's one would expect the difference between the cost in these countries and the price in the developed country to be less than the import restricting tariffs in the less developed countries plus the transportation costs. The situation can be easily visualized in Figure 3. In diagram (a) we have the standard competitive situation of an import-competing industry. DD is the domestic demand curve; $S_o S_d$ is the domestic supply curve, $P_m S_m$ is the supply curve of imports, assumed to be infinitely elastic. Since a tariff is imposed, the relevant import supply curve is $P'_m S_m(1+t)$. The total supply curve therefore is $S_o CBS_m(1+t)$. Market equilibrium is reached at B and the domestic price settles at $P'_m = P_m(1+t)$. Since P_m equals the export price of the developed country plus freight, we have $P'_m = P_m(1+t) = P_x(1+f)(1+t)$ where f is the percentage freight rate. In diagram (b) of Figure 3 we have a monopolist competing with imports. Under these circumstances the demand curve facing the monopolist is kinked, i.e., $P'_m BD$. The marginal revenue curve is therefore discontinuous. Equating marginal cost to marginal revenue produces equilibrium at A with costs at C. In this case, we have $Cost < P_x(1+f)(1+t)$.

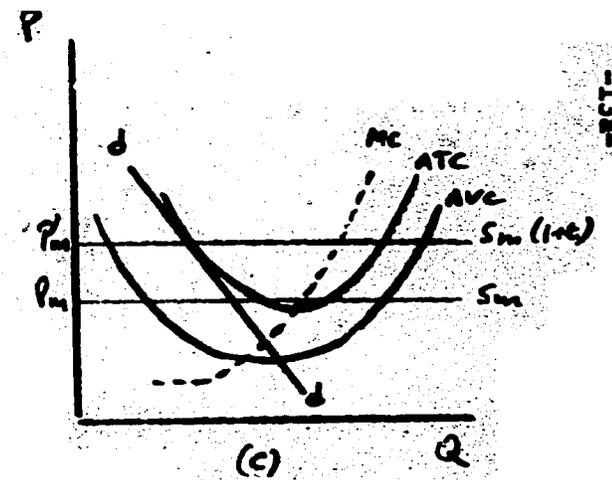
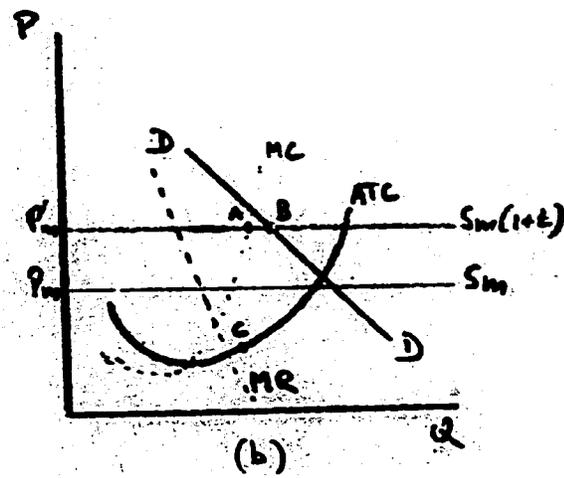
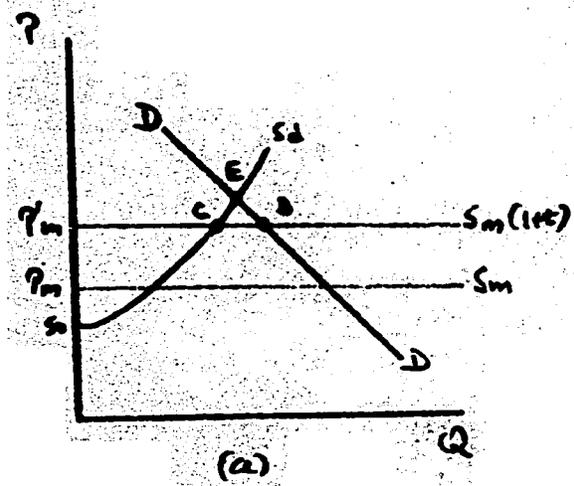


Fig. 3

In diagram (c) of Figure 3 we have the situation of one of many competitive firms in an industry operating with excess capacity. In this type of situation firms are assumed to behave in the short run like monopolistic competitors and develop an implicit market-sharing behaviour. The resulting short run equilibrium is thus the Chamberlinian tangency solution with marginal cost below price. Thus in this case marginal but not average cost will be less than $P_x(1+f)(1+t)$.

If there were two or more developed countries rather than one the same analysis would hold, with the export price of the lowest cost developed country becoming the determining factor.

If the less developed countries wish to export to the markets of the developed countries they must be able to produce at a price equal to that paid in the market of the importing country minus whatever import duties are levied upon entry minus the cost of transportation between the less developed countries and the market in the developed country. From what we have previously established about the formation of prices in less developed countries we can conclude that in the absence of monopolies and price differentiation, this required price will be below the cost of production in the less developed country concerned by an amount approximately equal to twice the freight rate, plus the rates of import duty imposed in both the importing developed country and the exporting less developed one. Should the export price of the developed country concerned be lower than the price at which the same product sells in the domestic market, this differential offsets the cost disadvantage noted before. Furthermore, if the importing developed country is not the lowest cost producer, the freight cost from the lowest cost producer to the importer's market will provide an offset to the cost/price differential. Finally, if import competing producers in less developed countries are monopolists or competitive monopolists, the cost disadvantage is further reduced and may in-

deed vanish altogether.

Table 9 tabulates an estimate of the difference between costs of production in Brazil, Chile and Mexico and prices in developed countries on the assumption of fully competitive markets all around and sales to the market of the lowest cost producer. Since developed country exporters often price at marginal cost for export, Latin American industry is often oligopolistic in structure, and sales may take place in markets of other than the lowest cost countries, these estimates are likely to overstate the true cost/price gap.

The rather large gap existing between the costs of developing countries and the price in the developed country markets can be narrowed in part by the extension of import duty preferences on the part of developed countries. It will be recalled that one of the elements listed above as contributing to the cost/price differential is the import duty imposed by the developed countries. If these are waived, it is made correspondingly easier for the industrial exports of developing countries to be price competitive in developed country markets. A rough impression of the quantitative importance of developed country tariffs in the total price/cost gap can be derived from Table 9.

Less developed countries for their part can undertake to narrow the cost/price differential by two main techniques: the first of these constitutes the payment of an export subsidy and the second of these is the undertaking of a compensated devaluation. Both these techniques are essentially directed at making the export exchange rate for nontraditional commodities similar to the commodity exchange rates of inputs in these industries.

Export subsidies can be used as a direct means to bridge the gap between cost of production and sales price by making a cash payment through the Treasury. It is important to point out, however, that this outpayment through the Treasury need not burden fiscal finances if the respective country has excess

TABLE 9

THE EXCESS OF COST OVER EXPORT PRICE FOR SELECTED
LATIN AMERICAN COUNTRIES

Sector	<u>Brazil</u>				<u>Chile</u>				<u>Mexico</u>			
	Own Tariff	Industrial Country Tariff	Freight	Total ^{1/}	Own Tariff	Industrial Country Tariff	Freight	Total	Own Tariff	Industrial Country Tariff	Freight	Total
	(%)	(%)	(%)	(%)	(%)	(%)	(%)	(%)	(%)	(%)	(%)	(%)
Non-Met. Minerals	40	5	5	62	139	5	5	177	-4	5	5	11
Metallurgy	34	5	15	86	66	5	15	131	29	5	15	78
Machinery	34	22	8	90	84	22	8	103	30	22	8	84
Electrical												
Equipment	57	22	8	122	105	22	8	191	25	22	8	77
Transportation												
Equipment	57	22	8	122	84	22	8	161	26*	22	8	78
Wood Products	23	5	30	119	35	5	30	140	14	5	30	103
Furniture	68	16	8	117	129	16	8	210	—	16	8	—
Paper & Products	48	5	8	81	55	5	8	89	35	5	8	65
Rubber Products	78	8	8	124	102	8	8	154	33	8	8	67
Leather Products	66	16	8	114	161	16	8	252	20	16	8	62
Chemicals	34	8	8	69	94	8	8	54	24	8	8	56
Pharmaceuticals	37	8	8	73	—	8	8	—	12	8	8	41
Perfumes & Soaps	94	16	8	162	—	16	8	—	10**	16	8	48
Plastics	48	8	8	87	30	8	8	64	—	8	8	—
Textiles	81	8	8	128	82	8	8	255	12***	8	8	41
Clothing	103	16	8	174	255	16	8	380	10	16	8	48
Metal Products	—	8	8	—	60	8	8	100	31	8	8	65
Fertilizers & Insecticides	—	8	8	—	—	8	8	—	9	8	8	38

$$\frac{1/}{\text{Total}} = \left(1 + \frac{\text{own tariff}}{100}\right) \left(1 + \frac{\text{Industrial tariff}}{100}\right) \left(1 + \frac{\text{freight}}{100}\right)^2 - 1$$

SOURCES: Own tariffs: Bergsman & Malan, Jeanneret, Bueno, op. cit. Industrial Country Tariffs, Balassa, B., "The Structure of Protection in Industrial Countries and Its Effect on the Exports of Processed Goods from Developing Countries." Paper submitted to UNCTAD II, Table 1. Freight: Balassa, B., footnote in above source taken from "Trade Prospects in Developing Nations."

capacity in its industrial plant. As a result of the new subsidized exports a higher level of domestic activity and of imports will ensue. Both these increases augment the tax base, thus yielding higher levels of tax collections at the same tax rates. Since in the presence of excess capacity there will be an income multiplier effect, the taxes collected may well be sufficiently large to pay for the subsidy necessary to generate the exports in the first place. Indeed, in some cases, a net surplus may result. Calculations performed for the case of Argentina suggest that if indirect tax effects are taken into account export subsidies up to the 130% of the FOB value of the new exports will not worsen the fiscal situation. For the case of Peru a comparable figure is of the order of 70%.^{1/}

A compensated devaluation consists of a simultaneous and off-setting adjustment of the financial exchange rate and the trade restrictions such that all the commodity exchange rates for imports and traditional exports stay unchanged. The only net change takes place in the financial rate and in the non-traditional export rate. As a result the latter obtain the equivalent of a subsidy.^{2/} An example might be taken from the Argentinian exchange system as follows:^{3/}

^{1/} For a detailed presentation and discussion of the model used to derive these results on an aggregate and sectoral basis, Cf. D.M. Schydlosky "Short Run Policy in Semi-Industrial Economies", Economic Development and Cultural Change (forthcoming).

^{2/} For a detailed presentation and discussion Cf. D.M. Schydlosky "From Import Substitution to Export Promotion for Semi-Grown-Up Industries: A Policy Proposal", Journal of Development Studies, July 1967.

^{3/} Taken from "Proyecto de Modificación de la Estructura Arancelario-Cambiaria", Cámara Argentina de Radio, Television, Telecomunicaciones y Afines (CARTTA), September, 1966.

<u>Pre-Compensated Devaluation</u>				<u>Post-Compensated Devaluation</u>		
<u>Total</u>	<u>Tax/Subsidy</u>	<u>Basic</u>	<u>Rate</u>	<u>Basic</u>	<u>Tax/Subsidy</u>	<u>Total</u>
200	- 10%	220	Agricultural Exports	330	- 40%	200
220	0	220	Financial	330	0	330
260	+ 18%	220	Non-traditional Exports	330	+ 18%	390
330	+ 50%	220	Raw Material Imports	330	0	330
460	+120%	220	Semi-Manufactured Imports	330	+ 47%	460
600	+175%	220	Component Imports	330	+ 80%	600
700	+220%	220	Finished Product Imports	330	+115%	700

It is important to note that under a situation of excess capacity and unemployment of labor, the use of domestic resources entails little or no cost to society, that is, the use of additional labor and some of the installed idle capacity to produce for export does not require the society to sacrifice much, if any, other output. As a result, under such circumstances it is appropriate to activate all existing industry, whether or not it corresponds to the long term comparative advantage of the country. When full capacity utilization in all sectors of industry is reached, further export (and other economic) expansion, now entailing capacity expansion as well, should be directed to those sectors in which the economy has a comparative advantage and away from the indiscriminate diversification that has been followed in the past. Thus, whereas for the short run, while excess capacity persists, all industrial output can be promoted, in the longer run considerable selectivity must be exercised (this may merely consist of setting an upper bound on the export subsidy).

It should also be mentioned that neither of the two policies suggested is an answer to the problem of chronic inflation that plagues some Latin American countries. This problem should be dealt with by a separate although concomitant set of policies. It is likely, however, that under a higher level of activity and with larger industrial exports the greater flexibility introduced into the adjustment process will produce an easing of the policy conundrum facing stabilization efforts in the past.

IV. Action in the 1970's: Economic Integration

The benefits expected from economic integration in Latin America have been often cited. Among them are: greater competitiveness of industry, more scope for utilization of economies of scale, gains from greater specialization, continental import substitution, and greater bargaining strength in negotiations with the developed countries. It is our purpose here to take up two problems that arise in the context of economic integration and that have received relatively scant attention.

The first of these problems is related to the pattern of specialization which will emerge between the Latin American nations. It has already been pointed out that each Latin American country operates with an exchange rate system which has substantially biased their development away from the comparative advantage outcome. Each particular exchange rate system has its own anti-export bias arising from the particular combination of financial exchange rate, export taxes, and import duties of which it is composed. Under these conditions, the formation of a customs union that removes intra-union import duties but leaves untouched the remainder to the exchange rate system, offers no guarantee whatsoever of generating an expansion of trade and a specialization in production corresponding in any sense to an optimal spatial distribution across the continent. In fact, there is every reason to believe that quite the opposite will occur. The biases in the existing exchange rate

systems are likely to overpower whatever comparative advantage exists.

An obvious example of this situation arises in the context of trade between Colombia and Venezuela in an expanded Andean Group. Colombia's exchange rate system includes an implicit export tax on coffee and a set of preferential non-traditional export rates in addition to the usual multiple import commodity rates. Venezuela, on the other hand has equated its financial rate to that of oil exports and non traditional export commodities receive no preferential treatment. Thus, with the removal of tariffs one would expect Colombia to be able to sell its industrial products in Venezuela but not vice versa. The cause, of course, lies largely in the way Colombia's export exchange rates compensate for the real productivity differentials between coffee production and industrial production, whereas Venezuela's does not compensate for their similar differential between oil and industry. That this type of situation is general across the Latin American economic landscape can be seen from Table 7 by comparing the anti-export biases for the same industry across the three countries shown.

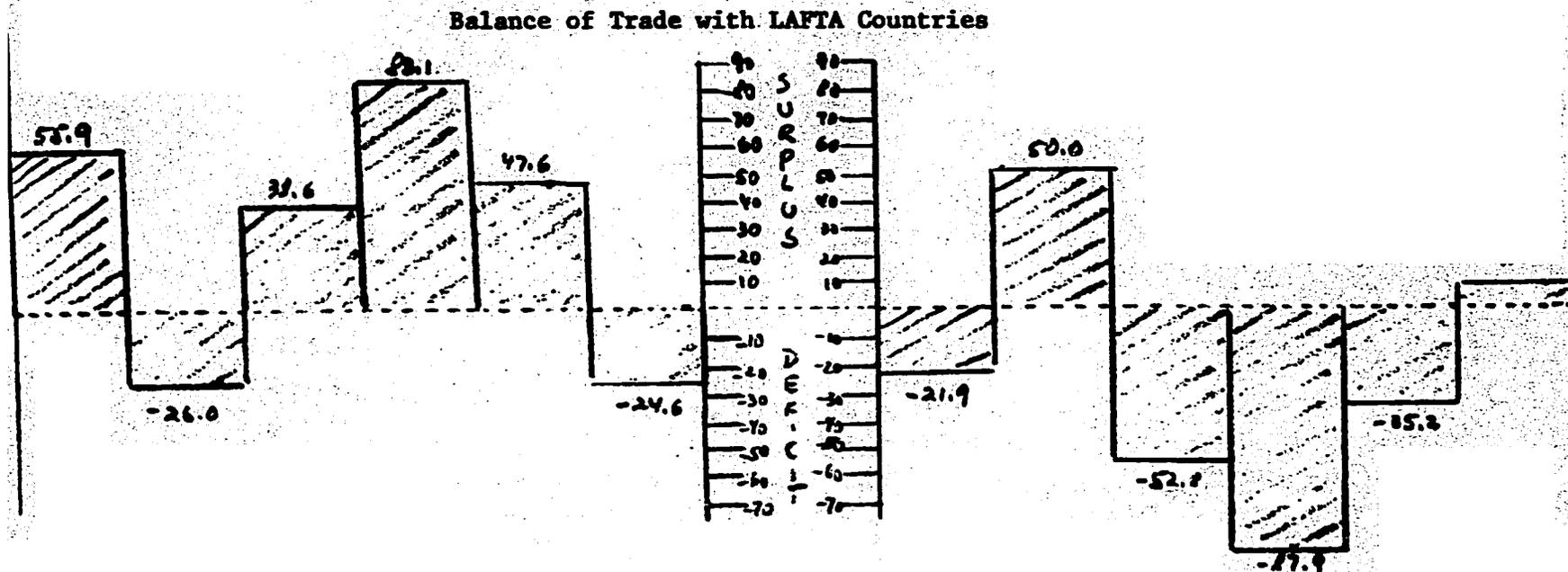
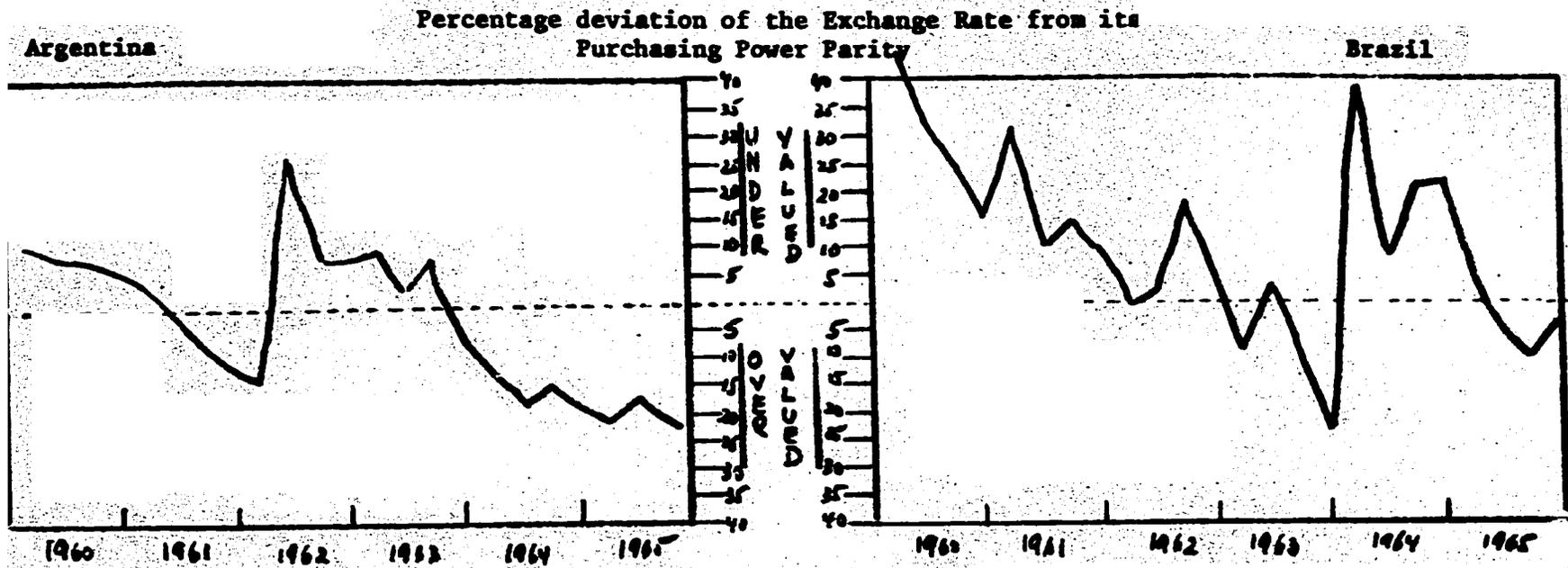
The second major problem arises in connection with the stability of the direction of intra-regional trade. Some Latin American countries are more notorious than others for their high rates of inflation. Nevertheless, many Latin American nations devalue regularly and the majority of them do so in a step-wise fashion. This implies that their exchange rates are sequentially over-and under-valued at different points in time as the domestic price rise leads or lags behind the adjustment in the exchange rate. For any one country this cycle causes considerable swings in its balance of trade. If several Latin American trading partners have such cycles and they are not synchronous, an amplified effect results with what may well be substantial swings in the volume and direction of trade. For example, if Argentina has just devalued and Brazil is in its overvaluation phase of the cycle, Argentine

prices will look very attractive to Brazilian buyers, thus leading to large exports from Argentina to Brazil. At the same time Brazilian products are priced out of the Argentinian market. Further along the cycle, Brazil devalues and Argentina's exchange rate becomes overvalued. The competitive situation is then reversed: Brazilian exports to Argentina will soar whereas Argentina will be priced out of the Brazilian market. Such trade reversals and the concomitant boom and bust cycles are clearly undesirable on economic welfare grounds. In addition, however, they will produce considerable resistance to tariff cutting initiatives on the part of industrialists as none of them will view the prospect of seeing his market swamped by imports with equanimity even if he gets the occasion to reciprocate the courtesy some time later. A further and equally serious consequence is the resulting uncertainty about the appropriate location of investment as between the various producing and consuming areas in the continent. With relative prices and the direction of trade fluctuating widely, location decisions cease to have a firm grounding in the underlying economic realities and become unduly influenced by the cyclical overlay. In consequence, existing distortions of the location and structure of production are unlikely to improve significantly with the integration process.

A preliminary assessment of the relationship of the valuation cycle and the direction of trade can be made on the basis of Figure 4 which compares the deviation of the exchange rate from its purchasing power parity to the balance of trade with the Latin American Free Trade Area for Argentina and Brazil in the period 1960 to 1965. It is striking to observe in how destabilizing a manner their cycles have interacted.

Policy in the 1970's will have to address itself to the solution of these problems if economic integration in Latin America is to become a successful rather than an ailing reality. The ingredients for such a policy are

Fig. 4



SOURCE: LAFTA Secretariat, "Influencia de los Tipos de Cambio Sobre las Corrientes de Comercio Exterior Entre los Países de la ALALC." November 1966

compensated devaluation or export subsidies on the one hand and price stabilization or a crawling peg on the other. Compensated devaluation or export subsidies would aim at equalizing the anti-export biases in the exchange rate systems, thus leading towards trading and investment according to comparative advantage. Price stabilization or the crawling peg would deal with the valuation cycles in order to eliminate the policy induced swings in trade with their negative effects. An interesting combination of these measures would be the formation of a payments union going considerably beyond the pattern of the clearing agreements currently in force, by including flexible exchange rates between each member's currency and the clearing currency unit plus full free trade within the union. The flexible exchange rates could then iron out the biases in the exchange rate systems while at the time compensating continuously for the various degrees of domestic inflation.^{1/}

The package which appears preferable depends to a large extent on the context in which economic integration would take place in Latin America. In the context of a world wide export promotion campaign, the export subsidies or compensated devaluation established would presumably leave only minor distortions between the exchange rate systems of the various Latin American countries which could be easily taken up by additional and minor policy action in the nature of special subsidies or other remedies. On the other hand, if economic integration of Latin America is thought of as a substitute to world wide export promotion, then it is probable that the payments union is the preferable solution although compensated devaluation or export subsidies and a crawling peg would accomplish the same purpose in a slightly more cumbersome manner.

^{1/} For a specific formulation of a payments union of this kind, Cf. D.M. Schydrowsky, "A Payments Union for Underdeveloped Countries", Document TD/B/AC.3/R.29*, 10 June 1966, UNCTAD.

V. Summary and Conclusions

In the foregoing we have argued that in the post-war period Latin American economic development and even more Latin American economic policy has been decisively influenced by the balance of payments situation. The typical response has been to import substitute industrial goods. Contrary to expectations, this had led to greater foreign dependency and in addition has produced considerable excess capacity in the industrial plant.

As a result of this process, Latin America enters the 1970's with economies which are widely diversified and operate their productive sectors at many different levels of real efficiency. This considerable departure from specialization along comparative advantage lines is the consequence of an exchange rate system which is implicitly of the multiple rate type and consists of numerous differing commodity exchange rates in addition to the financial rate. The particular structure of the exchange rate system has a strong bias in favor of import substitution and against industrial exports. In addition it creates the illusion that Latin American industry is hopelessly inefficient. Finally the large difference in real productivity it has validated explain in large measure the observed fact that the balance of payments adjustment mechanism in Latin America operates primarily through the income effect and only to a minor extent through adjustments in relative prices.

Policy action in the 1970's must be directed strongly to the generation of industrial exports. This is indispensable if installed excess capacity is to be put to use and also if industry is to perform a role as engine of growth and provider of employment. In addition, such exports will help improve the balance of payments adjustment mechanism and lead to greater economic stability. Success on this front will require the cooperation of developed and less developed countries to devise means to narrow the cost/price differential between producers in the former and markets in the latter as well as to increase pro-

ductive capacity and ease the adjustment of Latin American economies towards producing more in accordance with their comparative advantage. In this context, tariff preferences, export subsidies and compensated devaluations have been proposed and examined as tools to narrow the cost/price differentials. Aid could well bolster this process in a variety of ways, while private capital inflow could help the economies grow in the direction of further industrial exports. Economic Integration has also been examined in this connection and it has been found that the existing exchange rate systems are likely to produce distorted patterns of specialization; stepwise devaluation accentuates these distortions by creating recurrent cycles in the direction of trade. An improved outlook for integration would require the uniformization of the exchange rate structures of the participating countries and the smoothing of the over-and under-valuation cycle.

In sum, a healthy economic development of Latin America in the 1970's calls for some novel departures in the restructuring of the exchange rate systems of the Continent.