TOWARDS A NEW TRADE POLICY FOR DEVELOPMENT

Report by the Secretary-General

of the

United Nations Conference

on

Trade and Development

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PREFACE

The United Nations Conference on Trade and Development meets at a time of growing world-wide recognition that there is no acceptable alternative to international co-operation if mankind is to survive. Only through co-operation between all countries, irrespective of their political or social system, can the peace of the world be ensured. And only through co-operation can sufficient impetus be given to the struggle of mankind for a better and fuller life.

In December 1961, the United Nations General Assembly created new goals for international co-operation by setting a target to be achieved by all developing countries by 1970. The target of the Development Decade is a minimum annual rate of growth of 5 per cent. In adopting this target, the United Nations explicitly recognized that its achievement is a matter of international as well as national concern. And the countries participating in this effort implicitly accepted an obligation to contribute in every way they could to the attainment of the common goal.

During the past year a further vital step has been taken. The idea has gained universal acceptance that the development goals of the United Nations have direct implications for international trade and aid. A continuation of existing trends in world trade, adverse to the developing countries, would greatly intensify the difficulty of reaching adequate growth objectives. It is vital for the world community to create an international trade environment that would facilitate the growth of developing countries, and not thwart it.

That is the basic aim of the United Nations Conference on Trade and Development, and it is also the aim that inspires this report. All the experience of the United Nations has been mobilized in preparing this report and the success of the Conference will depend on the willingness of Governments to face all the implications of that experience and take action accordingly. I commend this report to Governments, to the Conference, and to the public generally, in the hope and conviction that it will contribute to a better understanding of the need for a new international trade policy for the Development Decade.

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Secretary-General of the United Nations

INTRODUCTION

This report constitutes an attempt to present the principal issues with which the United Nations Conference on Trade and Development is confronted and to suggest an integrated programme of measures to assist Governments in considering ways of dealing with these issues.

It draws heavily on ideas expressed and recommendations made in the various United Nations organs and in the numerous studies and reports of the United Nations Secretariat. Its preparation would not, however, have been possible without the extensive and creative labours of the Preparatory Committee of the Conference. The discussions of the Preparatory Committee, in particular at its second session, furnished a comprehensive account of the issues facing the Conference and of possible solutions to the crucial problems of trade and development. It is the work of the Preparatory Committee that has enabled the secretariat of the Conference to prepare this report which, together with all the other detailed studies and reports, will, it is hoped, constitute a working basis for the Conference.

If the report goes beyond the findings of the Preparatory Committee, this is to no small extent due to the extensive consultations which took place with officials of many Governments in all parts of the world and at various sessions of the regional economic commissions. These consultations enabled the Secretary-General of the Conference to reach a better understanding of the problems and issues involved. He is grateful to all government officials and representatives of the various international organizations who so generously gave of their time.

In preparing the report, the Secretary-General of the Conference was also fortunate in being able to consult the Executive Secretaries of the four regional economic commissions who spared no effort in providing him with suggestions for which he is most grateful.

The report is founded on the conviction that practical action in the field of trade and development is second to no other responsibility which the United Nations, established to maintain peace, must face in the 1960's. It is on the basis of this conviction that the Organization has convened a Conference whose primary objective it is to point the way *towards a new trade policy for development.*

Raúl PREBISCH
Secretary-General of the United Nations Conference on Trade and Development

Part One

THE PROBLEM OF INTERNATIONAL TRADE AND DEVELOPMENT

Chapter I

THE INTERNATIONAL ECONOMY: THE PAST AND THE PRESENT

1. The United Nations Development Decade and the potential trade gap

This second world trade Conference, convened by the United Nations, is meeting under a star very different from that under which the first one met at Havana sixteen years ago.

The first conference was clearly influenced by experience of the events that preceded the great depression of the 1930's, experience of a system reaching back to the nineteenth century. At that time, the remarkable expansion of world trade, with multilateralism in full swing, acted as a powerful catalyst of spontaneous development in the peripheral countries, which provided the industrial centres with food and raw materials.

The great depression precipitated the break-down of this old order, already undermined by the political impact of the First World War. In view of all this and of the consequences of the Second World War, it is out of the question to think of restoring the old order now. In the not too distant days of Havana it might have been possible to harbour illusions of doing this, but the subsequent course of events has finally dispelled these illusions once and for all.

It is imperative to build a new order with a view to solving the serious problems of trade and development that beset the world, especially the problems that affect the developing countries.

From the standpoint of the developing countries, the Conference will be particularly concerned with a phenomenon that was a subject of controversy until recently, but which is today a matter of understandable general concern: the persistent tendency towards external imbalance associated with the development process. The phenomenon is already well known. While primary commodity exports are, with a few exceptions, expanding relatively slowly, demand for imports of manufactured goods is tending to grow rapidly, at a pace that increases with the rate of development. The resulting imbalance creates a serious external bottleneck which makes development difficult. The imbalance must be rectified if development is to be accelerated in conditions of dynamic equilibrium.

One of the main objectives of the United Nations Development Decade is the attainment of a minimum annual growth rate of 5 per cent in the income of the developing countries by 1970. This is certainly a rather modest target and not much higher than the average rate of 4.4

per cent registered in the 1950's. Nevertheless, it will be extremely difficult—if not impossible—for many of the developing countries to achieve and maintain this rate of growth unless the present Conference brings about a policy of international co-operation that would make it possible to eliminate the imbalance in trade.

What are the implications of the 5 per cent minimum growth target for international trade? First and foremost, it should not be expected that, if the income of all developing countries is to rise at the minimum by 5 per cent every year, their imports can increase at a rate much less than 6 per cent. One of the main reasons for this is that any acceleration in the rate of growth requires additional investment; and the import content of this investment is normally much higher than that of income as a whole. Consequently, it is not going too far to conclude that imports would have to rise at a rate somewhat higher than that of total income. This view is supported by estimates based on the experience of developing countries.

The second implication of the 5 per cent growth target is that exports of the developing countries would also have to rise at the rate of 6 per cent *per annum*, in order to maintain balance-of-payments equilibrium. More precisely, a volume of exports should rise at a rate which, after allowing for changes in the terms of trade, would pay for a volume of imports increasing each year at a rate of 6 per cent.

As we all know, experience during the 1950's was highly unsatisfactory in this respect. The annual rate of growth in export volume of the developing countries during that decade was only 4 per cent *per annum*, and, if the petroleum-exporting countries are excluded, the average is significantly lower. At the same time, the terms of trade deteriorated, so that the purchasing power of exports over imports rose more slowly still, by under 2 per cent *per annum*.

Thus, even at existing rates of growth there is a widening gap in the balance of payments of the developing countries; at higher rates of growth consistent with the objectives of the Development Decade, the gap would be even greater if the trends of the 1950's continued.

This, then, has to be the starting-point of the Conference. One cannot posit a 5 per cent rate of development without accepting also all the consequences that this implies for the rates of growth of imports and exports.

There are many ways, of course, in which the external resources of the developing countries could be increased: through additional exports of primary products, through more exports of manufactures, or through greater external aid. To some extent, each of these possible solutions is a substitute for the others. To the extent that one fails in solving the problem under one heading, one increases the burden to be borne under other headings. For example, in so far as one fails to secure any significant improvement in the rate of growth of exports of developing countries, recourse must be had to a greater inflow of international finance. And within any given target rate of increase in exports as a whole, the less that is done to widen market opportunities for foodstuffs and raw materials, the greater need will there be to open up new markets for manufactures. A combination of interdependent elements is involved; and it is an essential condition for success that the various measures adopted should be integrated within an over-all policy for achieving the desired result.

Unless these measures are adopted, the trade gap of the developing countries will be immense; available estimates show that, if the factors responsible for the present trend in world trade continue, the trade gap may reach an order of magnitude of about $20 billion[1] by 1970 if the growth rate of 5 per cent is to be achieved. This gap is potential and not real: if the means of bridging the gap are not found, the developing countries will be forced to reduce their rates of growth unless they are prepared to achieve higher rates at an excessive economic and social cost involving serious political consequences.

The rate of growth of 5 per cent *per annum*, set as an objective of the Development Decade, can in no sense be considered fully satisfactory. It would mean an annual rate of increase of only 2.6 per cent in the average per capita income of the peripheral countries in view of the rapid rate of population growth, which is higher than in any previous era and makes it all the more difficult to expedite development.

Nearly half of the capital invested in the developing countries is needed to provide for the increase in population, thereby limiting the resources available for substantially and steadily raising the over-all level of living. Unless the present tempo of population growth slows down,[2] it would take eighty years at an annual rate of growth of 5 per cent for the developing countries to reach the current average per capita income level of western Europe, and approximately forty years more for them to reach that of the United States. For the least advanced countries, accounting for one half of the population of developing areas, the period required to reach the present western European level would be of the order of two hundred years.

A 5 per cent annual rate of growth could therefore be considered acceptable only for a short transitional period in which to create the internal and international conditions required for accelerated development.

On the other hand, even if a fall in the rate of population growth were to help in alleviating certain problems and tensions, it would in no sense be an excuse for slackening rather than intensifying the domestic development effort or for narrowing the scope of international co-operation; rather should it provide an opportunity for accelerating development so that its basic objectives may be attained in a shorter period of time, a period that is politically and socially acceptable.

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[1] This figure has been calculated on the basis of a 5 per cent *average* rate of income growth. If a *minimum* growth rate of 5 per cent is used, the figure for the potential trade gap will be higher.

[2] During the 1950's, the annual growth rate of the population of the developing countries as a whole was 2.2 per cent. It is estimated that it will rise to 2.4 per cent between 1960 and 1980.

The potential of modern technology is so enormous that the developing countries should not have to wait as long as the present industrially advanced countries had to wait to develop their technologies step by step and use them for the eradication of poverty and its inherent evils. Indeed, they cannot wait as long, because the acceleration of their development is an absolute necessity that brooks no delay. The pressure exerted by the masses for real improvements in their levels of living has never been as strong as it is now, and in the years to come it will become a growing source of internal and world-wide tension if it is not met by a vigorous policy of economic and social development in which international co-operation must play a decisive role.

The obstacles which the economic and social structures of the peripheral countries place in the way of development policy are well known. It is quite clear that important decisions must be taken to bring about structural changes, as has been indicated in previous reports of the United Nations and its specialized agencies. Suffice it to state here that, without such structural changes, and without a determined political effort to promote development and remove the internal obstacles from its path, measures of international co-operation, however good in themselves, will be very limited in their effect.

2. The old order

The imposing code of rules and principles, drawn up at Havana and partially embodied in the General Agreement on Tariffs and Trade (GATT), does not reflect a positive conception of economic policy in the sense of a rational and deliberate design for influencing economic forces so as to change their spontaneous course of evolution and attain clear objectives. On the contrary, it seems to be inspired by a conception of policy which implies that the expansion of trade to the mutual advantage of all merely requires the removal of the obstacles which impede the free play of these forces in the world economy. These rules and principles are also based on an abstract notion of economic homogeneity which conceals the great structural differences between industrial centres and peripheral countries with all their important implications. Hence, GATT has not served the developing countries as it has the developed ones. In short, GATT has not helped to create the new order which must meet the needs of development, nor has it been able to fulfill the impossible task of restoring the old order.

In the context of the nineteenth century and the initial decades of the twentieth, as we see it, there was no place for this idea of rationally influencing and so modifying the course of events. The course of events had merely to be followed and anything that obstructed it eliminated. Development in the periphery was a spontaneous phenomenon of limited scope and social depth; it came about under the dynamic influence of a unique combination of external factors which have since ceased to exist.

The situation can be presented simply in the following terms. During the last quarter of the nineteenth century, the United Kingdom, as the world's leading dynamic centre, accounted for 36 per cent of world exports of manufactures and 27 per cent of the imports of primary commodities. Since the historical accident of the industrial revolution happened in the United Kingdom before it did in other parts of the world, that country, with its limited resources and given its level of technology at the time, had to grow outwards and there emerged the classic pattern of exchanging manufactured goods for primary commodities. Imports of primary goods and other commodities by the United Kingdom grew apace, as did their share in the national income: the over-all import coefficient rose from approximately 18 per cent in 1850 to the very high figure of almost 36 per cent in 1880-84, as a result of free trade. This phenomenon influenced the rest of Europe, although not to the same extent, and its effects on the development of countries on the periphery of the world economy were striking.

Actually the process was the opposite of that which has gradually come into existence since the end of the First World War and especially since the great depression: the substitution of imports of food and raw materials for domestic production and not *vice versa*.

There was another factor which encouraged the growth of consumption and primary commodity imports: these imports were not yet subject to the adverse effects of technological progress as they would be in later years. Per capita income was still able to sustain an active demand for foodstuffs, synthetic production of raw materials had not yet begun on a larger scale, and European farmers still clung to their traditional methods.

3. The great depression and world trade

It is sufficient to mention these facts to emphasize the radical change which was ushered in during the First World War as a result of political and economic factors and which grew in scope and intensity as a result of the world depression of the 1930's.

The United States displaced the United Kingdom as the leading dynamic centre. This was more than a mere change of hegemony; it had a far-reaching influence on the rest of the world. The enormous natural resources of the vast territory of the United States and the resolutely protectionist policy it pursued from the start of its development were apparent in the steady decline of its import coefficient. In 1929, on the eve of the world depression, this coefficient was barely 5 per cent of total income and the restrictive measures resulting from the depression reduced it still further. In 1939, at the beginning of the Second World War, it had fallen to 3.2 per cent.

The effects of these developments on the rest of the world were of enormous importance. With the advent of the great depression, the order that dated back to the nineteenth century, and which the First World War had seriously shaken, now disintegrated. The trends towards agricultural self-sufficiency were encouraged to an extraordinary degree in the industrial countries, which were striving to cut their imports in order to cope with the violent contraction in their exports. Bilateralism and discrimination emerged as means of mitigating the intensity of this phenomenon. This movement spread throughout the world and forced many developing countries to adopt even more drastic restrictive measures, since the value of primary exports was declining more sharply than that of industrial goods.

The precipitous fall in the import coefficient of the United States, the leading dynamic centre, and the slow recovery in the level of its activity, compelled the other countries of the world to lower their import coefficients too by all kinds of restrictive expedients. Under the most-favoured-nation clause, the restrictions ought to have been applied to all countries alike, but the discrimination fostered by bilateralism allowed them to be directed mainly against the United States, as a means of remedying the acute dollar shortage.

This problem recurred after the Second World War. As in the 1930's, recourse was then had to bilateralism but this phase was very short-lived. Western Europe decided to attack its difficulties boldly, not just by adopting negative and defensive attitudes but by positive action of enormous scope: the modernization of its economy, which boosted its export capacity, and the policy of integration, which promoted its reciprocal trade to the particular detriment of imports paid for in dollars. While this attitude contributed to over-all equilibrium, it had a serious effect on some developing countries. So it was that the European Economic Community (EEC) and the European Free Trade Association (EFTA) came into existence.

Thus ended the long period of structural imbalance vis-à-vis the United States, which not only unreservedly welcomed the formation of the Community but also offered it its firm support.

In their turn, eight socialist countries[3] formed their own grouping, the Council for Mutual Economic Assistance (CMEA), in order to integrate certain important activities, plan them jointly, and import greater fluidity to the reciprocal trade of the participating countries.

A new order is thus emerging among the more advanced industrialized States and the next few years will reveal its ultimate significance more clearly: it remains to be seen whether this new order will be one in which vast regions withdraw into their shells and isolate themselves with a minimum of trade between them, or whether it will be one in which they take advantage of a closer economic link involving new forms of the international division of labour.

Hence the vital significance of the massive cut in tariffs proposed by the late President Kennedy for the next round of GATT negotiations. The

[3] For the sake of brevity, the term "socialist countries" in this report refers to the countries designated as "countries with centrally planned economies" in United Nations publications.

success of these negotiations among the advanced countries which conduct their trade relations mainly by means of tariffs will thus have a considerable influence on the future development of the world economy.

The EEC authorities have repeatedly affirmed the outward-looking character of their economic policy, a position which coincides with that of the United States. There has been a gradual relaxation of that country's traditional protectionism and it is to be hoped that this new policy can now enter upon a very broad phase.

The socialist States of CMEA have also repeatedly expressed their support of the principle of the international division of labour. The success of the Kennedy round and the improvement in the international political atmosphere could considerably facilitate the adoption of formulae which would enable the socialist countries to play an active part in world trade by removing the obstacles which obstruct their participation. This refers not only to relations between them and other industrially advanced countries, irrespective of the differences in their economic and social systems, but also to relations with the developing countries, in view of the interdependence of world trade.

4. The disintegration of the old pattern and the developing countries

All this is highly important for the developing countries, but it is far from enough, as will be seen later. What was happening in those countries after the great depression, while such significant changes were taking place in the industrial countries?

The break-down of the old pattern of trade created new problems for the developing countries. The persistent trend towards external imbalance began, first, as a result of the contraction of their exports during the great depression and, later as a result of their slow rate of growth. From the outset, a number of countries tried to counteract this imbalance by means of import substitution, i.e., by inward-looking industrialization, without foreign markets, and later, after the Second World War, by continuing this policy without interruption and by drawing on the international financial resources made available to them.

The external imbalance was thus covered, but in a precarious manner in the countries which at that time were pushing ahead with their industrialization. As time went on, the consequences of this system became increasingly apparent. Industrialization encounters growing difficulties in the countries where it is pursued furthest. These difficulties arise from the smallness of national markets and also from the following peculiar fact. The further substitution proceeds in respect of some imports, the more other imports grow because of the heavier demand for capital goods and, subsequently, because of the effects of higher income. In addition to this pressure, the adverse effects of the decline in the terms of trade in recent years have weakened the effectiveness of financial contributions from international sources.

Furthermore, these contributions entail a heavy burden of servicing which is mounting rapidly, mainly owing to the amount of amortization in respect of relatively short-term credits. Thus servicing competes with an active demand for imports for the relatively scanty supply of foreign exchange earned by exports.

This phenomenon has no historical parallel. The old pattern of international trade, as it existed in the nineteenth century, was characterized, as has already been pointed out, by a strong and steady growth in exports, which provided the means for servicing debts. Any difficulties which arose were due not to structural defects, as now, but rather to financial misbehaviour or short-term cyclical contractions. In addition to all this, there is the mounting burden of external payments for maritime freight and insurance. The developing countries own only 6 per cent of the world maritime tonnage and this creates a series of problems. Moreover, while the system of shipping conferences may be explained by the very nature of sea transport, it involves combines that restrict competition and affects the developing countries as regards both the cost of services and the impact of this cost on various products depending on their degree of processing. The desire to extend import substitution policy to these services is therefore very understandable, but the information so far available in support of this policy is very meagre. All this necessitates further inquiry, and it is to be hoped that the information needed for the purpose will be forthcoming.

This is a characteristic picture of many of the developing countries, especially those where industrialization has made most headway. None of the others, however, is, over the short or long term, immune to the persistent tendency towards imbalance, except in certain exceptional cases; and what is now happening in the more industrialized developing countries foreshadows what will happen in the others unless a conscious and deliberate effort is made to influence the course of economic events and to apply the enlightened policy which those events have made imperative.

Chapter II

PRIMARY COMMODITY EXPORTS AND THE DETERIORATION IN THE TERMS OF TRADE

1. THE SLOW GROWTH OF EXPORTS

As has been pointed out, the trend towards external imbalance in the developing countries is mainly a manifestation of the disparity between the rate of growth of their primary exports and that of their imports of industrial goods. While primary exports, with certain exceptions, develop fairly slowly, demand for industrial imports tends to accelerate. This is a spontaneous feature of economic development.

The slow growth of primary exports is an inevitable results of technological progress in the industrial centres. On the one hand, there are direct consequences, since technological progress leads to the increasing substitution of synthetics for natural products; and it is also reflected in one way or another in the smaller raw material content of finished goods. On the other hand, there are indirect consequences, since only a small part of the increased per capita income generated by technological progress goes into the demand for foodstuffs and other staple consumer goods, as compared to the demand for industrial goods and services which tends to rise rapidly. It is significant, for example, that, in absolute terms, total consumption of wheat in the United States has remained almost constant since the beginning of the century, in spite of the rise in both population and per capita income.

To all these developments must be added the remarkable effects of the propagation of modern agricultural techniques in the advanced countries.

One of the characteristics of technological progress is that it has not permeated all productive activities or all countries evenly, a fact which largely explains the structural differences and consequent contrasts and disparities in the development process. Until fairly recent times, technological progress was confined to industrial production and had not spread to agriculture to any great extent, except for mechanization. Finally, however, the technological revolution reached this lagging sector, first in the United States and then in Europe. Modern farming techniques made rapid headway and in fact agriculture is becoming industrialized; thus, new dynamic elements are being introduced into the economic complex, at both the internal and the international levels. The old pattern of trade, under which less developed countries were the suppliers of agricultural exports, is undergoing a chance which may become permanent and thus help to develop new forms of the international division of labour.

It so happens, however, that the enormous increase in output that has ensued in some major industrial countries, has further weakened the export trade in a number of agricultural products from the temperate zones and also in some tropical or semi-tropical products. And here a very significant fact emerges which is not the inevitable result of technological progress but of political attitudes towards this progress, attitudes that are certainly capable of being changed. In spite of the huge increases in productivity, domestic prices in the industrial countries concerned usually stay higher—and often much higher—than those on the international market. In this way, or through the payment of subsidies to farmers, the adverse effects of technological progress on prices are countered. But this policy also provides an additional incentive to expand production, and the expansion is often carried out on marginal holdings and at excessive costs. In order to guarantee a domestic consumer market for the increased output, imports from other producing countries are restricted or eliminated by various devices that are not always compatible with the provisions of GATT. If this encouragement results in exportable surpluses, such surpluses are exported by means of subsidies or other incentives which tend to depress world prices, while other producing countries are unable to follow suit because of the very weakness of their economies.

Hence, the tendency of the terms of trade to deteriorate occurs in the case of the highly industrialized countries too, largely as a result of technological progress and in spite of their economic strength. This tendency is the outcome of the well-known readjustment difficulties experienced by primary production which are aggravated by technological progress, as will be explained in the relevant part of this report.

The measures adopted in those countries and the social motives underlying them are understandable: they do not wish the benefits of greater productivity to be transferred to other sectors to the detriment of producers. It is not this policy we have to discuss but rather the fact that the harmful effects of such measures on the primary exporting countries do not appear to have been taken sufficiently into account. It is possible to conceive of a price or income policy which does not encourage marginal production in the industrialized countries and which guarantees the developing countries a reasonable share in consumption. In other words, we should visualize a policy which does not seek to solve the domestic problems of the industrial countries by aggravating the problems of the developing countries.

The restrictive measures applied to imports by the industrial countries cover the whole vast range of primary items except for those which, by their nature, cannot be produced domestically in these countries.

In western Europe, cereals and meats, milk products, vegetable fats and oils, sugar and other foodstuffs are thus well-protected by fixed or flexible tariffs and import quotas. Thanks to this protection, it is possible to pay domestic producers, as stated above, prices much higher than those prevailing on the international market, or to grant them substantial subsidies. While the effects on consumption vary, depending on the nature of the measures adopted, all these measures serve to stimulate increased domestic production at the expense of imports, which have thus dropped to a level where they are merely residual.

In the United States, too, the impact of protectionism is significant and is intensified, in the case of some agricultural products, by the sale of surpluses abroad, which, despite efforts to prevent them from invading traditional markets, have a harmful effect on other producing countries.

It is often asserted that the weight of the restrictive measures applied to agricultural products from the temperate zones falls mainly on the primary exports of industrial countries and that they consequently have little effect on developing countries. But there are two reasons why this is not so. The first is that certain Latin American and Mediterranean developing countries which export such temperate-zone products are seriously affected by these restrictions. The other is that the sale of surpluses in world markets often displaces tropical or semi-tropical products. One example is rice in the consumption of countries of the Far East and Canada. Furthermore, oils and fats from the industrial countries are tending to oust imports from developing countries; temperate-zone fruits are tending to take the place of tropical varieties; and the competition between beet sugar and cane sugar is seriously harming the developing countries, as are highly subsidized exports of cotton, maize and tobacco from industrial countries.

In addition to the foregoing, the following consideration must also be borne in mind. International trade cannot be arbitrarily fragmented, and the unfavourable effect that sales of surpluses have on exports from other developed countries also impairs their capacity to import from the developing countries.

Thus, for example, the difficulties experienced by such countries as Australia, Canada, the United States and New Zealand are bound to affect the ability and willingness of these countries to open up their internal markets to larger shipments from developing countries.

Tropical products are not subject to import restrictions in the markets of the industrial countries, but their consumption is discouraged in some of them by internal taxes which are usually more than the value of the items imported. Furthermore, the preferences granted to certain countries which export these tropical products are detrimental to the interests of other developing countries.

Imports of many mineral products tend to rise as industrial development progresses. This is happening in the countries of western Europe, which continue to depend on imports for most of their requirements in minerals and non-ferrous metals, while the United States has become a net importer rather than a net exporter of this group of products. Nevertheless, the United States continues to restrict imports in the interest of domestic production of lead, zinc and petroleum. Similarly, certain coal-producing western European countries levy duties and taxes on petroleum products that compete most directly with coal.

The foregoing remarks relate to the advanced private-enterprise countries. The socialist countries too have obviously made great efforts to stimulate their primary production, and the technological revolution in agriculture is proceeding there also. In recent years, as will be seen elsewhere, their imports of primary commodities from the developing countries have increased rapidly, although not yet commensurately with their economic potential. Consequently, the aforesaid objectives as regards a reasonable share in consumption hold good in the case of the socialist countries as well.

2. Why the prices of primary commodities tend to deteriorate in relative terms

The easing or elimination of protectionism in the industrial centres could have a far-reaching effect on the prices of the goods benefiting thereby. But it would be idle to believe that this can have any decisive effect on the downward trend of the terms of trade for primary commodities in relation to industrial products, which has again prevailed in the past decade. The factors operating in this direction have deeper roots in the peripheral countries than in the industrial centres. The former suffer from a congenital weakness that makes it extremely difficult, if not impossible, for the deterioration to be checked by a decision on their part and on their part alone.

Owing to the slowness of the growth of demand for primary commodities, only a dwindling proportion of the increment in the economically active population in the developing countries can be absorbed in their production, and the more productivity in primary activities rises as a result of the assimilation of advanced techniques, the smaller will that proportion be. The economically active population therefore has to be shifted to industry and other activities.

This shift is a lengthy process, even in the industrial countries where the proportion of the economically active population employed in primary production is already relatively small. Hence the phenomena discussed above. If the switch-over were effected rapidly and primary production were quick to adjust itself to the slow growth of demand, one of the requisites for obviating the deterioration of the terms of trade would be fulfilled.

For this to happen, industry and other sectors would have to develop very rapidly in the peripheral countries and achieve a rate of growth much higher than that heretofore attained in those countries, particularly if efforts to introduce advanced techniques into primary production and other low-productivity activities were intensified.

The magnitude of this process is indeed enormous. It should be remembered that, although there are differences from country to country, about 60 per cent, on the average, of the economically active population of the developing countries is still engaged in agriculture and other branches of primary production, working generally at a low rate of productivity, and that to this figure must be added that part of the economically active population engaged in artisan activities and personal services at very low scales of remuneration. All these sectors of the population exert constant pressure on the real level of wages in the developing countries and make it extremely difficult for this level to rise in direct proportion to productivity as the latter improves with technological progress. The increase in income generated by higher productivity in the agricultural sector thus tends to shift to other parts of the domestic market or abroad, as the case may be, provided that the shortage of available land does not absorb the increase in income by raising the rent for the benefit of landowners and provided that the play of market forces is left undisturbed.

In the industrial countries, on the other hand, the relative shortage of labour and strong trade-union organization allow wages not only to rise as productivity increases but even, as often happens, to outstrip the increase.

Thus there is a fundamental disparity in these trends. It is a consequence of the structural differences between industrial centres and peripheral countries and it explains the tendency of the terms of trade to worsen. The protection enjoyed by the primary commodities of the industrial centres obviously encourages this tendency because it accentuates the disparity between demand for primary commodities in the centres and demand for imports of manufactures in the periphery.

This should not be regarded as an immutable law. It is a trend which can be slowed down or halted when the demand for primary commodities in the major centres expands very rapidly either because of the speed with which income rises or because of extraordinary requirements, and it cannot be immediately followed by a corresponding expansion in primary production. The terms of trade will then become favourable; and if, as is usually the case, both land and manpower are available, production will expand to the point where it exceeds demand and the tendency of the terms of trade to deteriorate will reappear, particularly if techniques which increase productivity are applied and the demand of the industrial countries is restricted at the same time.

With an effort of the imagination it is possible to visualize a situation of dynamic equilibrium in the distant future in which the trend in question disappears as a result of the world-wide process of industrialization. If the advanced centres themselves have not yet succeeded in reaching that stage, the countries on the periphery of the world economy can hardly be expected to do so within a short space of time. The readjustment will come about in the end when the structural change is completed, but the period of transition will be very long. In the meantime, it is precisely through this period of transition that the present and successive generations are destined to live, and it is those generations which will have to bring about the change. The change will also require capital formation on a vast scale, to say nothing of time. In the developed economies, capital formation, intrinsically very strong, is facilitated by the very increase in productivity which accompanies technological progress, whereas in the developing countries, owing to the transfer abroad of income caused by the deterioration in the terms of trade, the capacity for capital formation, intrinsically very feeble, will be further diminished.

It is obvious that, if technological progress in primary production is intensified and if technology in the developing countries also undergoes a revolution, without which they cannot grow faster, the tendency of the terms of trade to deteriorate may be even stronger than in the recent past. This is not a prediction. But, what factors can we descry on the economic horizon that are capable of countering this tendency?

There are those who are inclined to set great store by the recent firmness of primary commodity prices and indeed, the United Nations index of world commodity export prices, having declined by the beginning of 1961 to a level of 8 per cent below that of 1953, remained stable during 1961 and 1962 and has since recovered more than half of the loss since 1953. But can it be argued that the general trend has finally reversed itself and that there is no longer any need to worry about the possibility of further deterioration? Or ought we, on the contrary, to face up to this phenomenon with a great sense of foresight?

There are various ways in which this can be done: by means of commodity agreements, which not only improve prices but also facilitate access to the markets of the industrial countries, or by compensatory financing. These are in fact convergent measures, the nature of which will be analysed in the appropriate part of this report. Suffice it to say here that there are difficulties but that they can be solved. However, for the technical discussion to be profitable, it must be preceded by a political decision of the first importance, namely, a decision to transfer, in one way or another, to the countries exporting primary commodities the extra income accruing to the industrial countries as a result of the deterioration in the terms of trade.

From a pragmatic point of view this means recognizing that countries experiencing a deterioration in the terms of trade have a *prima facie* claim upon additional international resources—resources over and above those which they would have received in the normal course of events.

Some aspects of this matter are rather delicate and might lead the discussion on to barren ground unless we keep these pragmatic considerations uppermost in our minds. Practically speaking, the position is this. The foreign earnings of the developing countries have suffered severely from the deterioration in the terms of trade. Unless these countries succeed in obtaining additional resources, they will be unable to achieve the reasonable rate of growth set as a target in their plans. The situation will be worse still if the terms of trade deteriorate further in the future.

Additional resources, then, are indispensable, and it is the purpose of compensatory financing to provide them through such a transfer, in so far as the purpose is not achieved through higher prices. This would give economic development plans a large measure of stability which can certainly not be achieved by expedients designed simply to cushion the impact of fluctuations in exports, although such expedients are an important step in the right direction. These plans will have to be reviewed whenever necessary in order to deal with the consequences of deterioration. In other words, compensatory operations must be an integral part of a more rational policy for financing development.

3. The influence of these factors on the development of peripheral exports

All the factors mentioned above can be summed up in some very eloquent figures. These figures reflect the fundamental changes that have been taking place in the international economy and having such a great effect on the peripheral countries. They reveal first and foremost the contrast between the periods before and after the great world depression.

Before the depression, trade in manufactures and trade in primary commodities grew steadily and at much the same rate. Between 1876 and 1929, the cumulative annual rate of growth of both was approximately 2.5 per cent.

With the great depression, a truly striking disparity began to appear, for the first time since the industrial revolution. Trade in manufactures expanded faster than during the earlier period, while primary commodity trade slumped. Thus the first group of products registered an annual rate of growth of 3.1 per cent,[1] while the latter trade grew at an annual rate of only 1 per cent[2] (see the following table):

World production and exports of primary commodities and manufactures, 1960

	Volume index (1928=100)	*Average annual percentage increase (1928 to 1960)*
Production		
Total	236	2.7
Manufacturing	293	3.4
Primary	170	1.7
Primary, excluding petroleum	159	1.4
Exports		
Total	190	2.0
Manufactures	260	3.1
Primary commodities	158	1.4
Primary commodities, excluding petroleum	137	1.0

Source: Bureau of General Economic Research and Policies of the United Nations Secretariat.

[1] Throughout the chapter, data relate to non-socialist countries unless otherwise specified.

[2] Excluding petroleum.

This sharp decline in primary exports was due to a combination of two types of factors, as explained above. First, there were spontaneous economic factors which led to a slackening in relative demand for primary commodities, and, secondly, there were factors deriving from the protectionist policy of the industrial centres.

The first type is reflected in the difference in the growth rate of output for the two groups of products. During the same period of 1928-1960, when the annual rate of growth of output of manufactures for the world as a whole was 3.4 per cent, the corresponding percentage for primary commodities was only 1.4.[3] The second type is reflected in the difference between the latter growth rate of 1.4 per cent and the growth rate of 1 per cent for primary exports.[3] Primary exports increased at a slower rate than the aforesaid 1.4 per cent because production for the home market developed more rapidly than exports, mainly owing to the barriers placed in the way of exports.

Now we come to another very interesting aspect. These figures for the period following the great world depression do not reflect the full complexity of the situation. The first part of the period was influenced by the adverse effects of the depression and the Second World War. But thereafter primary exports made a strong recovery which carried them to levels even higher than those reached during the pre-depression period. Thus, between 1950 and 1961, world exports of these products grew at an annual rate of 4.6 per cent. Nevertheless, there were no grounds for satisfaction for most of the developing countries, since this trend did not help them. First, the large industrial countries—usually on the basis of subsidies—and the few petroleum-exporting countries accounted for the marked increase in primary exports. Secondly, there were the adverse effects of the deterioration in the terms of trade.

The significance of these facts is such that they deserve further elaboration. The industrial countries greatly enlarged their share of world exports of primary commodities from 47 per cent in 1950 to 55 per cent in 1961, whereas over the same period the share of the developing countries fell from 41 per cent to 29 per cent.[3]

Thus, while world exports of primary commodities grew at the rate of 4.6 per cent, the exports of the developing countries expanded at the rate of 1.9 per cent.[4]

We may now turn to the adverse effects of the deterioration in the terms of trade. Between 1950 and 1961, the terms of trade of primary commodities fell by 26 per cent[4] in relation to those of manufactures, mainly owing to the rise in the price of the latter.

It should be noted, however, that the magnitude of the deterioration was less for some develo ng countries than this figure indicates, because

[3] Excluding petroleum.
[4] Excluding petroleum. Based on data provided by the Statistical Office of the United Nations.

those countries also import primary commodities and export manufactures, even if on a small scale in the latter case. From the over-all standpoint, even if these circumstances are taken into account, the deterioration in the terms of trade between developing and developed countries over the period in question was 17 per cent.[5]

In order to bring out the significance of this fact, we may compare the effects of the movement in the terms of trade with the net allocation of international finance to the developing countries. The net inflow of all types of finance (loans, investments and grants-in-aid) from 1950 to 1961 amounted to $47.4 billion.[6] This figure drops to $26.5 billion, if remittances of interest and profits for the same period are deducted. The fall in the purchasing power of total exports[7] from the developing countries due to the deterioration in the terms of trade has been estimated at almost $13.1 billion, which means that, after the cost of servicing is deducted, approximately half of the benefit of this inflow was nullified by the adverse effects of the deterioration in the terms of trade. This phenomenon occurred in different degrees of intensity in the several developing regions and was particularly severe in Latin America, where the effects of the deterioration for the same period were calculated at approximately $10.1 billion. It should be emphasized, in addition, that during the same period net inflows of foreign capital of all types[6] to this region reached the figure of $9.6 billion, whereas Latin American remittances abroad amounted to $13.4 billion.

Let us now examine the impact on growth rates. As mentioned above, from 1950 to 1961 the volume of the developing countries' exports of primary commodities, excluding petroleum, rose by 1.9 per cent a year. The figure rises to 3.6 per cent if their exports of manufactures and petroleum[8] are included. If there had been no deterioration in the terms of trade, the import capacity generated by exports together with the inflow of international resources—again minus the cost of servicing—would have increased by 4.5 per cent a year. Because of the deterioration, however, this did not happen, so that the developing countries' capacity to import expanded by only 3.5 per cent a year.

This expansion in the capacity to import was very far from satisfying the demand for imports generated by economic development. The rate of growth of the aggregate income of the peripheral countries during the period was approximately 4.4 per cent. The demand for imports, for the reasons already indicated elsewhere, must have been considerably greater than this average rate. Through import substitution it was possible to reduce the effective growth of imports to 4.6 per cent, which is still higher than the rate of 3.5 per cent at which the capacity to import was growing. The developing countries were able to do this only by making inroads in their currency reserves and increasing their external short-term liabilities.

[5] Excluding petroleum. Based on data provided by the Statistical Office of the United Nations.
[6] Including private reinvestment.
[7] Including socialist countries and petroleum.
[8] Including socialist countries.

Chapter III

INDUSTRIALIZATION AND THE NEED TO EXPORT MANUFACTURES

1. INWARD-LOOKING INDUSTRIALIZATION

If the peripheral countries manage to secure a larger share for their primary exports in the consumption of the industrial countries, this, together with the transfer of income from the latter countries to the former to offset the effects of the deterioration in the terms of trade, will help to narrow the trade gap but will not in itself be enough to close it. These measures will be palliatives, and the relief they afford, though considerable in some cases, will be of limited scope owing to the size of the gap. Hence, the absolute necessity of building up trade in industrial exports. Exports of manufactures ought to have been the natural complement of the industrialization of the peripheral economies. But it would not have been easy to develop such exports in the very midst of the world slump of the 1930's, when industrialization was beginning to gain momentum in a number of peripheral countries. At that time, the industrial countries, as has already been stated, were obliged to adopt measures severely restricting their imports. Would they, in those circumstances, have permitted the entry of industrial exports from developing countries when they were placing such serious barriers in the way of the latter's primary exports?

Some developing countries, too, had to protect themselves in those days by applying similar measures in order to offset the shrinkage of their export trade and, later, the patent and persistent tendency of that trade to expand slowly.

Thus protected, industrialization began to gain momentum, rather as a defensive reaction aimed at overcoming adverse circumstances and external imbalance than as a clearly conceived and rational design.

A process thus took shape that was very different from the one that had characterized the emergence of new industrialized countries from the latter half of the nineteenth century onwards following the example originally set by the United Kingdom. The United Kingdom at that time applied no protectionist tariffs; they were, generally speaking, relatively low in the European countries; and in the peripheral countries they either did not exist or usually served fiscal purposes. In this propitious international setting, industrialization was able to turn outwards, in addition to satisfying internal requirements. And in this way the countries in process of industrialization reaped the benefits of specialization and of an adequate scale of production. Industrialization thus proceeded in an environment of expanding international trade.

The contrast with what happened after the great depression is striking. Circumstances compelled industrialization to turn inwards like a simple import substitution process–simple but generally costly. Could there have been any alternative? Could the industrialized countries, in their efforts to fight the depression with tariffs and other restrictions, conceivably have encouraged imports of industrial goods from the peripheral regions? Of course not. Nor is it at all likely, given the ease with which domestic production could be geared to import substitution under strong protection and with a relatively guaranteed and expanding internal market, that the countries just embarking on industrialization would have set a different course and directed their efforts towards hostile and risky external markets.

Thus, in the developing countries which undertook to industrialize at that time, industrialization proceeded piecemeal in a large number of watertight compartments with little inter-communication, to the serious detriment of productivity.

The Second World War gave this form of inward-looking industrialization still further impetus, and nothing happened thereafter to alter this characteristic trend. Industrialization based on import substitution has certainly been of great assistance in raising income in those developing countries, but it has done so to a much lesser extent than would have been the case had there been a rational policy judiciously combining import substitution with industrial exports.

The experience of the countries–especially the Latin American countries–which were thus becoming industrialized in watertight compartments is of particular interest in this connexion, because it illustrates the problems that the other developing countries may have to face if, for lack of external markets, they too are forced to look inwards in their industrial development. The former countries are now confronted with the following consequences of their industrial development:

(*a*) The simple and relatively easy phase of import substitution has reached, or is reaching, its limit in the countries where industrialization has made most progress. As this happens, the need arises for technically complex and difficult substitution activities, which usually require great capital intensity and very large markets if a reasonable degree of economic viability is to be attained. Thus there are limits to import substitution in the developing countries which cannot be exceeded without a frequent and considerable waste of capital.

Moreover, the extension of import substitution to a wider range of goods generates or increases demand for other imports, whether of raw materials and intermediate goods to manufacture products in respect of which such substitution is taking place, or of new lines of capital goods or consumer goods that technology is constantly creating.

(*b*) The relative smallness of national markets, in addition to other adverse factors, has often made the cost of industries excessive and necessitated recourse to very high protective tariffs; the latter in turn has had unfavourable effects on the industrial structure because it has encouraged the establishment of small uneconomical plants, weakened the incentive to introduce modern techniques, and slowed down the rise in productivity. Thus a real vicious circle has been created as regards exports of manufactured goods. These exports encounter great difficulties because internal costs are high, and internal costs are high because, among other reasons, the exports which would enlarge the markets are lacking. Had it been possible to develop industrial exports, the process of industrialization would have been more economical, for it would have made possible the international division of labour in manufacturing.

(*c*) Usually industrialization has not been the result of a programme but has been dictated by adverse external circumstances which made it necessary to restrict or ban imports; these measures have been applied especially to non-essential imports that can be dispensed with or postponed. Thus home production of these goods has been encouraged, absorbing scarce production resources, often regardless of cost. A more rational policy would have given priority to import substitution in respect of goods which could be produced under more favourable conditions than others, not only consumer goods, as has generally been the case, but also raw materials and intermediate and capital goods.

(*d*) This substitution in respect of non-essential or not urgently needed goods has led those developing countries which are most advanced in the process of industrialization to concentrate, so far as their imports are concerned, on essential goods, particularly those required by productive activities. Hence, any sizable drop in the earnings of primary exports cannot be offset as easily as in former times by compressing imports, because nowadays the margin of such imports that can be eliminated without slowing the pace of internal economic activity and employment is much narrower.

(*e*) Finally, excessive protectionism has generally insulated national markets from external competition, weakening and even destroying the incentive necessary for improving the quality of output and lowering costs under the private-enterprise system. It has thus tended to stifle the initiative of enterprises as regards both the internal market and exports.

The development of industrial exports, in addition to counteracting the potential trade gap, will make it possible gradually to increase the advantages of industrialization by correcting its defects. This applies not only to the developing countries which have already started this process and are making headway, but also to the others, especially those which have emerged with the collapse of the colonial system. A process of fragmentation even greater than that which previously existed in the international economy is now taking place. Nearly one hundred of the developing countries have each less than 15 million inhabitants and in two thirds of them the population is less than 5 million; their national markets are handicapped not only by the smallness of their populations but also, in many cases, by their extremely low incomes per capita.

These countries must become industrialized, come what may, for, generally speaking, they do not have sufficient agriculture to provide adequate employment for the increment in the economically active population, particularly when new techniques are introduced which increase productivity and reduce the relative demand for labour.

On the other hand, the circumstances in which the great industrial countries now find themselves are very different from those of the 1930's and the post-war period, yet the atmosphere prevailing in those countries has often not encouraged industrial exports from the developing countries. Moreover, the latter, in their turn, usually lack a clear-cut policy for promoting their manufactured goods.

2. Barriers in the industrial centres to exports of manufactures from the periphery

The barriers which the industrial countries have placed in the way of exports of manufactures from the developing countries are of long standing and have recently become greater in some cases.

Among the foremost of such barriers special mention should be made of differential tariffs. These tariffs seriously hamper the processing of raw materials in the developing countries, because as a rule they rise in proportion to the degree of processing.[1]

No special attention has been devoted to these differential tariffs in the GATT customs negotiations, although their importance has been recognized in that organization's reports. It is understandable that the tariff cuts granted to each other by the industrial countries which are Contracting Parties of GATT, although extended to the less advanced countries under the most-favoured-nation clause, had no significant effect on them, since the goods to which they applied were usually those of interest to the former countries and not to the latter.

Furthermore, in cases where some developing countries have surmounted the obstacles and, as a result of preferences or relatively low tariffs, have succeeded in securing a foothold for their industrial exports in certain major centres, the latter have imposed restrictions on imports from such countries to prevent a disruption of the market.

This has happened even in cases where there were no balance-of-payments or unemployment problems, two of the reasons usually cited to justify import restrictions. The countries of western Europe, in spite of their large trade surplus and manpower shortage, have not been noted for a liberal import policy towards manufactures from developing countries. Thus, in 1962, so far as total manufactures[2] imported by the EEC coun-

[1] These differential tariffs also exist in the developing countries and obstruct their reciprocal trade.

[2] Excluding non-ferrous metals and slightly processed materials.

tries are concerned, the proportion imported from all developing countries fluctuated between only 1 and 4 per cent, whereas, the corresponding proportions were 11 per cent for the United States and 12 per cent for the United Kingdom. The United Kingdom imports more manufactures from the developing countries than does the entire European Economic Community, and between 40 and 50 per cent of the cotton textiles it consumes comes from them and Japan.

Unfortunately, both the United States and the United Kingdom have made their policy considerably less liberal by concluding agreements with the developing countries which severely limit the latter's exports of manufactures. For example, under existing arrangements, if exports to the United States and the United Kingdom remain unchanged, it seems unlikely that exports of cotton textiles, which expanded at the rate of 14 per cent from 1955 to 1961, will be able to increase by more than 3 per cent in the next few years.

Apart from cotton textiles, there are also restrictions on jute and tobacco products, preserved fish, coconut fibre articles, sewing-machines and bicycles.

It should be noted that, in addition to import restrictions, limitations are frequently imposed through administrative procedures. Sometimes private enterprises also introduce their own restrictions, either by preventing imports of products manufactured by their subsidiaries or affiliates in the developing countries or in other ways.[3]

The problems created by some industrial imports from developing countries cannot be disregarded, but neither should they be exaggerated. Unfortunately these imports have covered a small range of products and countries,[4] and if the range of both were substantially wider, this diversification would by itself considerably reduce the risk of disrupting the markets of the developing countries.

Moreover, the volume of industrial goods which the developing countries need to export to reach their growth targets is by no means unmanageable. As will be seen below, if half the potential gap were to be covered by such exports by 1970, this would represent only between 4 and 5 per cent of the increment in the advanced private-enterprise countries' consumption of manufactures. These proportions would, of course, be lower still if the more industrially advanced socialist countries are included in the calculations.

Can so tiny a figure possibly be a cause of anxiety? Reference is often made to the sacrifice that exports from the peripheral countries would

[3] A well-known example of this type of action is the so-called Noordwijk Club, formed by producers of cotton textiles in Austria, Switzerland and the EEC countries for the purpose of preventing the re-export to countries members of the Club and to the associated African States of cotton textiles imported from the developing countries. The Noordwijk agreement is implemented by the Governments of the club members.

[4] India, Honk Kong, Israel and Mexico account for more than half of the industrial exports from developing countries.

entail for the industrial countries. But neither the above figure nor the nature of the process involved can really be described as a sacrifice. For these additional exports from the developing countries would very soon be reflected in further imports from the major centres, particularly of capital and intermediate goods. These are precisely the goods in which the productivity of the industrial centres is very high and which earn very substantial sums. To export such goods in increasing quantities against imports of articles which they manufacture with relatively less efficiency, far from being a sacrifice, would be a positive advantage.

3. A NEW SUBSTITUTION POLICY WITHIN THE REGIONAL GROUPINGS

The stress just laid on industrial exports does not mean that import substitution policy should be abandoned. On the contrary, it should be maintained. In calculating the potential trade gap, it was assumed that the tempo of the substitution process will remain the same as in the past. There is still a margin for import substitution, although it has shrunk considerably in those peripheral countries which have made more headway with industrialization. The margin could be appreciably widened if substitution were to be carried out, not within each individual country's domestic market, but within groupings of countries so as to reap more easily the benefits of competition, specialization and economies of scale.

This more rational form of substitution policy could be applied to imports not only of goods but also of services, such as freight and insurance, which form an important component of the potential gap. Furthermore, in some cases the export of these services might be increased if a collective approach were to be adopted through such groupings. But the difficulties in the way are by no means negligible.

It is sometimes assumed that the formation of such groupings is a valid alternative to the expansion of industrial exports to the developed countries. Import substitution policy, if applied by a large grouping of developing countries, could certainly carry the process further and ensure greater economic viability than at present. But the effectiveness of such a policy has its limitations.

First and foremost, beyond a certain point import substitution becomes increasingly difficult and costly. Several factors account for this: the lack of natural resources; the technical complexity of certain industries; and the inadequate scale of production even in a grouping of developing countries. If even large economic areas, endowed with a wide variety of abundant natural resources and a high level of technical skill, are interested in promoting the international division of labour, they do so because they find the interchange advantageous. Can countries in a less satisfactory economic and technological position possibly deny themselves such advantage even if they group together? In any event, it takes time for these groupings to develop, and, even if they made considerable and effective headway with their substitution policy, they would still have to pass through a period during which it would be extremely convenient for them to export increasing quantities of manufactures in order to supply themselves especially with the capital goods they require to complete and consolidate this development.

Again, the steady advance of technology in the manufacture both of new and more efficient capital goods and of consumer goods adds further advantages to those of trade visualized in purely static terms. Not all the industrial countries keep step so far as modern techniques are concerned and these innovations are not evenly distributed over the vast range of goods. A mounting flow of trade has the merit of quickly disseminating the goods that incorporate these new techniques. If the developing countries were to closet themselves within their own groupings, they would be lagging behind continually in the march of technological progress, since their primary exports would not earn them nearly enough to purchase such goods. It is inconceivable that, in the foreseeable future, they will have access to the innovations in question or be able to incorporate them in their own production if they are compelled to restrict their imports of capital goods in this way.

Lastly, within a regional grouping, particularly if it is very limited in scope, there is a risk that its smaller members may become too dependent on their larger associates; perhaps the best way to prevent this is through the diversification of their export trade in respect of both products and countries of destination. And this can only be achieved at the world trade level.

All these points explain why the developing countries have displayed great interest in expanding their trade with the more advanced countries. Actually the problem of narrowing and closing the potential gap must be attacked simultaneously on both fronts. Their interdependence is obvious. The expansion of industrial exports to the rest of the world will undoubtedly have beneficial effects on trade between countries of the same region. In turn, if regional exports of manufacture are thus increased, the industries concerned will be in a better position to compete with the rest of the world.

Chapter IV

GATT AND THE DEVELOPING COUNTRIES

1. The achievements of GATT

GATT has important achievements to its credit. Following the inter-war period of chaos, it introduced a new concept of a rule of law in world trade. One may criticize the particular character of some of the law that has been applied. But this should not be allowed to obscure the fact that the decision of Governments that world trade should be subject to this law was in itself of vital importance in this field.

In the past, increases in trade restrictions by particular countries have frequently led to a spiral of retaliation in which all have lost and none have gained. The application of a rule of law in world trade has already helped to limit excesses of this type and could do much more if the law itself were made more responsive to contemporary needs.

A second virtue of GATT is its machinery for complaint and consultation. Each member country has an opportunity to bring forward instances in which it feels that it has suffered injury at the hands of another member, and can claim the redress authorized or adequate compensation, although it must be admitted that this procedure has often not been effective in practice.

GATT also provides a forum in which countries can discuss the impact of one another's trade policies, with a view to reaching a satisfactory accommodation.

Within this framework of rules and consultative machinery, GATT has brought about considerable reductions in the tariffs and other restrictions on world trade that were established during the difficult period following the great depression.

It is true, however, that these reductions have been of benefit mainly to the industrial countries and that the developing countries generally have obtained very little direct benefit from this process. But in so far as the reduction of tariffs and restrictions may have created a more favourable basis for growth in the industrial countries, some indirect benefit will have accrued to the developing countries in the form of a higher demand for their exports than would otherwise have occurred.

Finally, since the publication of the report, *Trends in International Trade,* in October 1958, GATT has been making a serious effort to conduct its activities in a way that would take more adequate account of the unsatisfactory position of developing countries in world trade. Still, it must be admitted that the positive results of these efforts, after more than five years, have been somewhat disappointing. But the problem itself has been recognized, and this recognition led to the consideration of a Programme of Action by a GATT Meeting of Ministers in May 1963, and subsequently to efforts to implement that Programme. The matter now rests with Governments: if this Programme of Action could be fully carried out by all countries concerned, a very important step forward would have been taken. The resolutions relating to the Kennedy round were also adopted at this Meeting of Ministers. The principle of not demanding full reciprocity from the developing countries was accepted, among others, during these negotiations on tariffs and other barriers to trade. In addition, the achievement of satisfactory conditions of access to world markets for agricultural products was set as an objective.

The GATT Tariff Conference of 1960/61 resulted in very limited benefits for the less developed countries; it is to be hoped that the Kennedy round will produce a more favourable balance in view of its significance as crucial evidence of the practical benefits which GATT can offer to the developing countries.

Furthermore, it is acknowledged that GATT has a very efficient secretariat, a fact that is borne out by its studies and the careful preparation of its negotiations; and it has also shown its ability to adapt itself to the changing realities of the times.

The above comments on GATT should be approached within a broad perspective. We can now see clearly things which were still confused and vague in the Havana days. The absolute necessity of industrialization for the peripheral countries had not been recognized or realized nor had the need to intensify this process as advanced techniques permeated into agriculture. Another thing which was not properly understood was the persistent trend towards external imbalance, which was attributed more to the inflationary policy of Governments than to the nature of the growth phenomenon. In addition, the developing countries were still very far from stating their position and defining their aspirations and attitudes. The end of the colonial era was only just in sight. And social tensions in the developing countries were not then so conspicuous or so pressing as they now are. We can now see all this clearly and there is an increasingly strong feeling that a very great effort will have to be made to alleviate and eliminate those tensions, which have such a great impact on world peace.

This effort could no longer take the form of a few rules and principles specifying what must be avoided; it is essential also to determine what must be done and to formulate a policy which meets this need for positive action.

Why has GATT not been as efficacious for the developing countries as for the industrial countries? There are two main reasons. First, the Havana Charter, as has already been said, is based on the classic concept that the free play of international economic forces by itself leads to the optimum expansion of trade and the most efficient utilization of the world's productive resources; rules and principles are therefore established to guarantee this free play. Secondly, the rules and principles in question have not always been strictly complied with and, even though they seem to have been observed in the letter in certain instances, the spirit underlying them has not been respected.

2. The structural differences and their consequences

The free play concept is admissible in relations between countries that are structurally similar, but not between those whose structures are altogether different as are those of the industrially advanced and the developing countries. These structural differences show themselves in various ways which were outlined in the preceding section.

The structural origin of the deterioration in the terms of trade has already been indicated and there is no need to revert to the subject here. It will be recalled that the Havana Charter mentions this phenomenon at one point. Elsewhere, however, in the articles relating to commodity agreements, the predominant idea that ultimately emerges is that basic market trends should not be impeded.

We have also commented on the disparities in international demand, which also derive from structural differences. This is a fundamental point which does not seem to have been given the importance it deserves in the Havana Charter. Thus, in seeking to lower or eliminate tariffs and restrictions with a view to promoting trade, neither the Charter nor the Agreement draws any distinction between developed and developing countries. And since there is an initial assumption of homogeneity, such reductions have to be equivalent everywhere. This is the principle of conventional reciprocity that prevailed until recently. The fact that these disparities place primary and industrial exporting countries in diametrically opposite positions has not been taken into consideration. Hence the importance of the fact that the need to depart from the idea of conventional reciprocity was recognized in the Kennedy round.

The former group of countries, given the relatively slow growth of their primary exports, cannot cope with the intensive demand for industrial imports unless they alter the composition of the imports in question, replacing some of them by domestic production so as to be able to increase others. In the absence of an export trade in manufactured goods, the only alternative left open to the developing countries is to grow at the slow tempo set by their primary exports, or to encourage these substitution activities by means of protectionism so as to develop more rapidly and prevent or correct the external imbalance as they develop.

If protectionism is kept within certain bounds, i.e., if it is applied only to the extent necessary to counteract the disparity in demand, there is no reason why it should have a depressive effect on the dynamics of world trade; on the contrary, it should have a purely balancing influence. Within these limits, not only is industrialization compatible with the development of primary production and exports, but an optimum relation between the two, conducive to intensive economic development, is conceivable. Of course, if a developing country weakens its primary export position by measures which act as disincentives and its place is not filled by other exporting countries, these depressive effects on international trade will be inevitable. But such effects, however we may look at them, are not inherent in the industrialization of the peripheral countries.

On the other hand, protectionism in respect of primary production in the countries exporting manufactured goods does exert a depressive influence, since the disparity in demand, instead of being levelled out, is accentuated, to the obvious detriment of world trade and the growth of the developing countries. In this form, protectionism helps in these centres to slow down still further the growth of the developing countries' primary exports, and hence the expansion of imports of the manufactures needed for their development. In other words, protectionism in respect of primary production in the industrial countries has definitely unfavourable repercussions on international trade and compels the peripheral countries to adopt further import substitution measures so they can continue their development; thus it makes this development even more difficult by curtailing their opportunities for an advantageous international division of labour. The Havana Charter fails to recognize this lack of symmetry and its practical implications for trade policy.

Given the prevailing conception, the objective pursued when that Charter was drawn up could be summed up in the following simple terms. The restrictions and tariffs which had been doing so much to distintegrate the world economy had to be gradually removed and the free play of international economic forces thus restore. The reduction and elimination of restrictions and tariffs would also cover the primary commodities imported by the industrial countries, and, in return, the countries exporting these primary commodities would have to lower their import tariffs on manufactured goods.

Herein lies the concept of the symmetry of a situation that was far from symmetrical: if the peripheral countries wished to reap the benefits of a liberal tariff policy for primary imports in the industrial centres, they likewise had to make equivalent concessions in their own tariffs. This is the serious drawback of such a conception of trade policy: the failure to take into account the fact that those equivalent concessions would intensify the trend towards trade imbalance inherent in the disparity of international demand, instead of helping to correct it.

Great strides have been made of late towards recognizing that these rules of reciprocity in trade negotiations must be changed because of the economic inequality between countries. A clear distinction must be made, however, between this conventional reciprocity and real reciprocity.

This is a very important point which must be borne in mind. The request for reciprocity in negotiations between countries which have not structural disparity in their demand is logical. Indeed, it is essential for the stability of the world economy that any expansion of exports which a given country achieves on the basis of concessions from the others should be accompanied by concessions granted to the latter, so that its imports from them can increase.

In the case of trade between the developing and the industrial countries, the situation is different. Since the former tend to import more than they export—owing to the international disparity in demand—concessions granted by the industrial countries tend to rectify this disparity and are soon reflected in an expansion of their exports to the developing countries. In other words, the developing economies, given their great potential demand for imports, can import more than they would otherwise have been able to do had those concessions not been granted. Thus there is a real or implicit reciprocity, independent of the play of conventional concessions. And this is what must be recognized in international trade policy.

This distinction is inherent at the transitional stage through which the developing countries are passing. The disparity in world demand does not have to be a permanent phenomenon. As the structure of production gradually changes with industrialization and industrial exports, this disparity will tend to disappear. Indeed, as such exports, both to advanced and to other developing countries, make headway, the disparity can be levelled out gradually. When this happens—and only then—will the bases have been laid for conventional reciprocity between the industrialized countries and countries that are pressing on along the road of industrialization. But this is a long process for most of the developing countries.

3. Compliance with rules and principles

It was stated at the beginning of this section that GATT had not been effective from the standpoint of developing countries for two main reasons. The first, inherent in the concept of the free play of international economic forces, has just been described. Let us now consider the second: the failure to comply with rules and principles. We shall not undertake an inquiry from the point of view of the relevant texts; we shall rather examine the spirit in which they seem to have been drafted.

The first question to be asked is whether, in the industrial countries, excessive agricultural protectionism aiming at self-sufficiency is consistent with this spirit of GATT, with this objective of expanding trade and not restricting it. This is especially relevant to the restrictions on agricultural imports in western European countries which were intensified at a time when the restrictions on industrial imports, imposed during the post-war period, were being liberalized. It has already been seen that such protectionism—and protectionism in respect of primary commodities in general—accentuates the disparities of demand and compels the peripheral countries to reduce their imports still further to the detriment of trade and the tempo of development in the periphery.

In practice, whenever the industrial countries have needed to safeguard their domestic production, whether in agriculture or in mining, from foreign competition, they have found direct and indirect ways of doing so.

This is what finally happened with respect to the developing countries. It was not so in the early days, when GATT tried to lower the tariffs of the developing countries and to keep protectionism in check. Later, however, it showed greater understanding of their difficulties. A point has thus been reached where such countries can in fact apply, in one form or another, such measures to restrict imports as the persistent trend towards external imbalance would seem to make advisable.

Hence it is not surprising that protectionism has been carried too far by many developing countries. Are the tariffs and restrictions in which this protectionism is reflected sacrosanct? The need for protectionism in the developing countries is now recognized and no longer a subject of controversy. But in several of these countries the tariffs are much higher than is needed to compensate for differences in cost. Their readjustment is thereby fully warranted and this should be an important item in the policy to be formulated at the Conference. The readjustment is justified, however, not by considerations of conventional reciprocity so long as the disparities of demand remain uncorrected, but by the desirability of progressively encouraging competition and vitalizing the industry of the developing countries, thus helping to accelerate their rate of growth. Nevertheless, no such readjustment would be possible unless exports expand and the external bottle-neck hampering development was reduced until it ceased to exist, for if foreign competition is to have this effect, it is essential for a country to have sufficient external resources to cope with the possible impact of tariff reduction on its imports and to avoid new elements of imbalance in trade.

The correction of excessive protectionism could be undertaken only in connexion with the over-all policy considered in this report. It could not be an isolated or immediate process; it would have to take place as the targets for increasing exports were reached. In this way it will be possible to continue lowering the excessive tariffs and other unnecessary barriers by applying a rational concept of protectionism.

4. Preferences and trade among industrial countries

We shall now pass to another important aspect of the GATT system, namely, the matter of preferences. What do they imply with respect to the primary objective of expanding trade? No valid generalizations can be formulated on this subject, for a distinction must be drawn between the different types of preferences before their significance can be perceived. The following types may be distinguished: preferences between industrialized countries, preferences between industrial and developing countries, and preferences between developing countries. This distinction already indicates the role played by differences of economic structure, but there are other factors too that must be considered in this examination.

The first type of preference finds its fullest expression in the EEC, whose population and economic magnitude are similar to those of the United States. The preferences that the member countries grant each other are intended to convert their reciprocal trade into internal trade.[1] This preferential system is giving a powerful impetus to trade among the member countries. Is this irreconcilable with the expansion of trade with other industrial countries and with the developing countries in general?

These two objectives are not at all incompatible. The integration to which the Community aspires, through the lowering of tariffs until they are completely eliminated, will tend to increase trade among its members more quickly than their aggregate income: in other words, it will tend to raise the coefficient of internal trade within the Community itself. Now this expansion of reciprocal trade could also be effected at the expense of trade with the rest of the world, with a consequent decline in the corresponding import coefficient. But not necessarily; everything will depend upon the final level of the Community's common tariff and on the degree of restrictiveness of its agricultural policy.

If the common tariffs are substantially reduced and the restrictions removed, trade with the rest of the world, too, may grow more intensely than the aggregate income of the Community. And if this income rises faster than before, the effects will be even more beneficial. These are, in the last analysis, the factors which will determine whether the development of the Community is inward-looking or outward-looking. Events up to the present do not yet allow a final evaluation.

All this is important for the developing countries from various points of view. First of all, there is a manifest intention to extend to them the tariff reductions granted to each other by the advanced countries without demanding reciprocity from them, and this intention involves recognition of a principle that is very meaningful for the developing countries, as was explained above. However, the positive effects of these reductions are doubtful for the developing countries, because those advanced countries will be in a better position than the less developed ones to take advantage of them. But there is another way in which this might benefit the developing countries: if, as a result of such reductions, the advanced countries increase their trade in industrial goods of a high degree of technical complexity or in the new goods that technology is constantly creating or changing, there will be room for the developing countries to expand their own exports of those manufactures which the industrial countries are relatively less efficient at producing as compared with the former goods. But this would not come about spontaneously; rather it should be the result of deliberate action, as will be seen later.

Moreover, the developing countries in the temperate zones might also benefit if the Kennedy round of negotiations succeeded in liberalizing western Europe's extremely restrictive policy towards agricultural imports, giving those countries a reasonable share in consumption.

[1] Neither the juridical aspect of these preferences nor the preferences of EFTA and the Latin American Free Trade Association (LAFTA) are discussed here. What we are discussing is their economic effect, as will be seen in the text. In the case of EEC, once the tariffs between member countries are completely eliminated, the influence of EEC on international trade will largely depend on its common tariff vis-à-vis the rest of the world, as in the case, for example, of United States tariffs.

Nevertheless, however much progress is thus registered in trade relations between industrial private-enterprise countries, and between them and the socialist countries, it will be far from constituting a basic solution so far as the developing countries and the policy they require are concerned. Conditions conducive to a policy that favours them will be created, but these conditions cannot be a substitute for that policy. For however much trade may grow between these advanced countries, it will not provide the dynamism required by the export trade of the peripheral countries gradually to bridge the potential trade gap so that they can enjoy the benefits of international trade to an increasing degree.

As has been seen, a similar impulse was given in the nineteenth century by a unique combination of favourable factors which have not recurred since then and are not likely to recur in a spontaneous way. So the impetus now required must be the outcome of a policy, the result of a deliberate effort to alter the course that events would probably follow if there were no such effort.

5. General preferences in favour of the developing countries

This policy would require the industrial countries to grant preferences to the developing countries in order to create markets for their exports of manufactures and, at the same time, to bring about the gradual elimination of the difficulties that now hinder the entry of these exports to the industrial countries. This brings us to the second type of preferences mentioned, namely, those that the industrial countries could grant to the developing countries. In principle, GATT does not allow these preferences except in so far as they existed when the Agreement was signed. But, in view of the need to revise some of the principles of the Agreement, this problem could be approached from a substantive rather than a formal point of view to see whether the preferences that the industrial countries may grant to the developing countries would or would not promote GATT's basic objective: the expansion of international trade. A study of this matter was begun at the last GATT Meeting of Ministers.

We have already shown that, unless the developing countries manage to expand their exports by stepping up their characteristically slow rate of growth, they will have to continue import substitution in spite of the obstacles in the way. If they were able to export more industrial goods under a preferential system, they could also import more, and this would enable them to relax the substitution policy and make it more rational.

Now would this really constitute a net increment in world trade or simply a diversion of trade? Various situations may be envisaged. In the case of certain articles, preferences would make it possible for imports from the developing countries to compete with the domestic industrial production of the countries granting them; in other cases, such imports would be effected at the expense of other countries that customarily supplied the articles in question. In the first case, there would be a net expansion of world trade, while in the second there would be a simple diversion of the flows of trade, without any real increase in its volume.

It would be a mistake, however, to situate the problem within a narrow frame of reference, since the lowering of tariffs and restrictions of the industrial countries, mentioned earlier, could more than offset the absolute or relative decline that some of their exports might suffer owing to the competition of the developing countries. In other words, expanding trade among industrial countries, if concentrated in highly specialized and complex goods and in the new products constantly being created by technology as it advances, would leave ample room for exports of manufactures from the periphery.

It follows that, from the standpoint of the growth of world trade, the ultimate effect of a preferential policy towards the developing countries would largely depend upon the success of the Kennedy round and of the consequent expansion of trade among the industrial countries. Similarly, as we have seen, whether or not the preferential system of the European groupings will help to promote an increase in world trade will depend on the outcome of these negotiations. Still, it was possible for the groupings to come into existence long before those negotiations.

This is further evidence of the fact that world trade problems cannot be examined piecemeal; they must be considered as a whole if their interdependence is to be properly grasped.

Be that as it may, the effects of a preferential policy in favour of the developing countries could not be considered only from the standpoint of world trade. Actually, trade is only a means of promoting growth, and, if the preferential policy helps to accelerate it in the developing countries, it will have fully accomplished its purposes.

Let us now pass to another aspect of the same subject. Should the developing countries give concessions to the industrial countries in return for the preferences granted by the latter? Such concessions would not be justified in the light of what has already been said concerning implicit reciprocity. The developing countries need to export more in order to be able to import more and thus help to prevent or rectify the structural imbalance of their trade. This is really the ultimate goal of the preferences. As that goal is approached, the preferences will gradually have to disappear. The time will then have come for the gradual restoration of the system of conventional reciprocity. For once the direction of the present imbalance is corrected, care will have to be taken to prevent the scales from tipping in the other direction.

6. Partial preferences for the developing countries

As has just been stated, preferences granted generally to the developing countries, besides quickening the tempo of their growth, could constitute an effective instrument for expanding world trade.

The same cannot be said of the present partial preferences favouring some developing countries at the expense of others. They generally divert but do not add to world trade flows.

This system of partial preferences was started immediately after the great depression of the 1930's. The United Kingdom applied it with the countries of the British Commonwealth and France with its colonies. These and other lesser preferences were recognized when GATT was formed, a situation very different from the later one in which the preferences that France previously had with its colonies, now countries associated with EEC, were extended to all countries of the Community.

Although such preferences are a serious problem for some developing countries, their simple elimination could not be contemplated except within the context of a development policy. Many of the countries favoured by these preferences, particularly as regards tropical products, have only recently become independent and are in the first stage of their economic development. Obviously they will have to industrialize, and the policy of general preferences advocated in this report will enable them to carry out that process avoiding the distortions that were created by inward-looking industrialization in other parts of the world. But this will necessarily take time and consequently could not be reasonable compensation for the adverse effects of the sudden removal of existing preferences. Their elimination could be effected only in an equitable way, as part of a gradual plan accompanied by agreements which improve the prices of primary exports, and by firm pledges of extensive financial co-operation, both for infrastructural investments and for the promotion of other exports, including industrial items.

As regards the partial preferences granted for industrial products from developing countries, few have benefited from them so far, and the drawbacks to which the removal of these preferences might give rise would be more than offset by the advantages which such countries would certainly derive from the introduction of a general preference system in the industrial countries.

These partial preferences, as is well known, have not generally been one-sided; they are also accompanied by the granting of preferences in developing countries for imports from the industrial countries in return for those granted by the latter.

Obviously, in this case it is not possible, as it is in the former, to invoke the need to encourage countries whose production is in its infancy. These preferences spring from a very understandable attitude whereby certain industrial countries take advantage of their buying power in order to obtain trade advantages in other countries that depend primarily on the markets of the former for selling their exports.

The removal of this latter type of preference, apart from its intrinsic significance as a factor in favour of multilaterialism, would have the merit of enabling the developing countries to form regional groupings, according each other reciprocal benefits without having to extend them to the industrial countries to which they now grant preferences.

7. Preferences among the developing countries

This leads us to a very important aspect of the subject under consideration: the preferences that developing countries might grant one another in order to promote reciprocal trade and thus help to expedite their growth. GATT has established too rigid a framework for these preferences, requiring the formation of a customs union or of a free-trade area. The Havana Charter was more flexible in this respect, but the relevant provisions (article 15) were unfortunately omitted from the text of the Agreement. In addition to this, in certain circles there have been attitudes opposed to the conclusion of payments arrangements between the developing countries designed to promote their reciprocal trade. All this would now have to be revised.

Trade between the developing countries represents a relatively small percentage of their total trade. In 1962, only 22 per cent of the exports from these countries flowed from one to the other. In fact, goods from the developing countries are still exported within the traditional pattern of trade; a large part converges on the major industrial centres, and the peripheral countries engage in reciprocal trade only to the extent required by the differences in their primary production. Moreover, there has been a vicious circle there too, for the low level of trade is one of the factors determining the high cost of transport, and this high cost in turn discourages reciprocal trade. It is often more expensive to ship merchandise from one developing country to another than to industrial countries which are much further away but on the traditional sea routes.

The relative volume of this trade within the total trade is small and has been declining over time–from approximately 26 per cent in 1950 to about 22 per cent in 1962. This can probably be partly explained by the severity of the restrictions on imports which the developing countries were obliged to impose in order to counteract the persistent trend towards external imbalance. The lack of a preferential and payments system was one of the reasons why other developing countries could not be exempted from these restrictions.

The significance of import substitution has already been explained. Each country has engaged in this substitution process in isolation. If, in order to lighten the difficulties they encounter in this process, they carry out substitution jointly in a grouping of developing countries, their imports from the rest of the world will not decrease in volume on that account; they will merely undergo a change in composition. Their volume depends, in the last analysis, upon the attitude of the industrial countries, not on unilateral decisions on the part of the developing countries: this is a consequence of the lack of symmetry of international trade which was already explained. If the industrial countries buy more from the developing countries, their sales to them will grow correspondingly, but, if the latter buy more from the former, their sales of primary commodities will not thereby increase. The trend towards external imbalance will simply be intensified.

Thus it will be the decision taken by the industrial countries, especially those of key importance in trade, that will determine whether the groupings formed by the developing countries will be inward-looking or outward-looking.

In any event, trade among the member countries will have to grow more rapidly than their aggregate income if the grouping is to be successful. So far as trade with the rest of the world is concerned, whether it grows or does not grow faster than this income will mainly depend, as has just been said, upon the policy adopted by the industrial centres. It will be possible to consider that these groupings of developing countries are deliberately pursuing an inward-looking expansion policy only if, even though they have corrected the disparity of demand by enlarging their export trade, they intensify their protectionist policy.

In the case of groupings of industrial countries, on the other hand, the rate of growth of their trade with the developing countries depends basically on their policy towards the latter.

Be this as it may, groupings of developing countries are imperative on a number of counts: to make industrialization policy more rational and economical through specialization and the division of labour; to avoid or remedy, as the case may be, the former distortions deriving from the policy of industrialization in watertight compartments; to promote industrial competition among member countries; and to counteract the trend towards excessive agricultural protectionism in some of the developing countries.

As we have said, the existing provisions of GATT prescribe, as a condition for the establishment of a preferential system, the elimination of duties and other restrictive regulations of commerce with respect to substantially all the trade among the countries concerned through a customs union or free-trade area. It is all or nothing, as regards the preferences that the member countries may grant one another; these are the rules.

Understandably enough, by these rules it was hoped to avoid a patchwork of preferences for different products and countries, with its pernicious consequences. The most-favoured-nation clause is actually the foundation stone of GATT. But what harm would be done to international trade if developing countries formed a grouping to establish a system for eliminating duties with respect to a sizable proportion, even if it were not substantially all, of their trade? By this means, although they would not secure the benefits of full liberalization, they could introduce an element of rationality into the new import substitution activities and correct at least some of the previous distortions to which we have referred.

From another standpoint, it must be recognized that, while the legal framework of GATT is rigid in this regard, there has been a certain flexibility in its application. Such was the experience of the Latin American Free Trade Association which might possibly not have been established had it not been for this flexibility. This flexibility also existed in the case of other groupings. But it must also be recognized, in the light of experience, that it is not enough to reach an agreement and provide the machinery required to promote reciprocal trade, but that a firm political decision to use this machinery, overriding all the opposition that naturally arises, is also indispensable. This decisive step must now be taken in LAFTA.

8. Comments on GATT

What has been set forth in the foregoing pages shows that the comments on GATT that are frequently made with respect to the developing countries are far from unfounded.

But it is important to stress that the purpose of such comments is not to harp back on the past in order to pass judgement, but rather to point out the course that should be followed so that GATT may become as effective an instrument for the developing as for the advanced countries. Can the measures hindering primary imports in the industrial centres at least be alleviated? Will it be able to work out a satisfactory procedure for gradually removing the preferences that favour some countries at the expense of the others? Can a preferential policy emerge which favours the developing countries' exports of manufactures? And if this can be done, will it be possible to formulate measures which will lessen the excessive protectionism of some developing countries? Will action be taken which will enable the regional groupings of peripheral countries to pursue a rational industrialization policy and promote their industrial exports? In a nutshell, can a policy basically designed to eliminate the persistent trend in the developing countries towards a trade gap possibly be put into effect?

It must not be forgotten, however, that GATT is not an abstract entity with an independent life of its own. It is what Governments wanted it to be. Whether events take a new course that furthers development will depend upon their attitudes, upon their policy decisions. This does not concern only the advanced countries. For although there is resistance in those countries to new forms of trade, there is also resistance, and in no lesser degree, in the developing countries. Many of them are accustomed, after thirty years, to a precarious inward-looking growth and there are powerful forces standing in the way of new flows of reciprocal trade and of the structural changes which this requires. To what extent will it be possible to persuade the industrial centres to leave some opening in their markets for the manufactures of the developing countries if the latter do not themselves make a serious effort to pull down the barriers and restrictions that constitute such formidable obstacles to their reciprocal trade?

Part Two

POSSIBLE SOLUTIONS AND INSTITUTIONAL ASPECTS

Chapter I

PRIMARY COMMODITY EXPORTS

A. *The question of prices*

1. The redistribution of income in international trade

There are at present three major problems relating to international trade in primary commodities: the question of prices; access to the markets of the industrial countries; and agricultural surpluses and their utilization in development policy.

The phenomenon of the deterioration in the terms of trade affecting primary commodity exports is understood better today than it was a few years ago. The difficulties of other countries are usually better appreciated when they arise in one's own country.

As explained in part One, primary production tends to increase beyond the limits of what is required by the relatively slow increase in demand. As a result, there is a tendency towards deterioration in the terms of trade; this tendency is aggravated by the effects of technological progress on the volume of production.

The industrial countries have been able to observe that, if market forces were allowed free play, shifts in the terms of trade between agriculture and industry would have distinctly regressive effects on the internal distribution of income. The primary producers would be deprived of part of their real income because of the drop in relative prices and this loss of income would, in general, be all the greater as productivity increased as a result of technological progress. In order to avoid that situation, steps have been taken to support prices of, or income from, agricultural products. Such measures of support are also necessary at the international level with respect to primary commodity exports.

This better understanding out of the problem is no doubt one reason for the recent more favourable attitude of great industrial nations towards commodity agreements. The conclusion of the International Coffee Agreement is an example of this, even though it is still early to pass judgement on its implementation. Similarly, whatever may be thought of particular features of the French plan for the organization of markets,[1] the plan seems to be based on the conviction that it is necessary to intervene at the international level in order to avoid, or at least attenuate, the consequences of the regressive redistribution of income which has been taking place between developed and developing countries. These new

[1] See document E/CONF.46/P/5.

attitudes are not, however, established as yet on a completely firm basis. To create such a basis is one of the primary objectives of the Conference.

The achievement of this objective requires that the industrial countries which import primary commodities should be prepared to consider an extremely important policy decision, namely, to take such measures as would prevent this regressive redistribution of income in the international field. It is to a consideration of the factors on which such measures must be based that we now turn.

2. Prices, market forces and demand

It is necessary, in the first place, to face up squarely to the fact that the international prices of primary commodities would, in general, have to be supported at levels higher than those which would prevail in the absence of international regulation.

The price mechanism cannot fulfil its traditional functions when most transactions in particular commodities are subject to government regulation at the national level, so that world prices are determined in a very narrow residual market that cannot be regarded as representative of the real market forces. Speaking generally, the smaller the share of the total supply of a particular commodity that is exported, the larger the spread that is apt to develop between prices in the various national markets subject to regulation and the greater the difference that arises between national prices and world market price. The small proportion traded is not, of course, in itself a cause of these disparities: rather it reflects the protection and mutual isolation of national markets which make it impossible for international trade and competition to perform their normal equilibrating functions.

Thus the prices realized on the world market reflect the existence of temporary imbalances between supply and demand outside the main regulated markets: such prices cannot therefore offer a sound basis for determining the level of commodity prices to be included in inter-governmental agreements.

This situation prevails particularly in the case of temperate-zone agricultural products grown by the industrial countries largely for their own consumption and insulated from the world market by various types of price-support measures: In 1959-61, less than 20 per cent of world production of these goods was traded internationally. This proportion stands in contrast with ratios characteristic of tropical products, where the proportion of production traded internationally is high.

Although world market prices are more meaningful for the tropical and mineral exports of developing countries than temperate products, they none the less do not provide valid guidance for decisions by producers or by the Governments concerned, though for a different reason from that mentioned in connexion with temperate-zone products. For, in situations in which resources devoted to agriculture or mining have little or no alternative employment and in which the response of producers to a decline in prices may, in some circumstances, be an expansion rather than a contraction of output, the price mechanism is as incapable of operating in the normal manner as it is in the case of the residual markets discussed above.

It is for these reasons that it is no longer possible to take the view that commodity agreements should not interfere with the long-term operation of underlying market forces through the price mechanism. Where prices are determined in the context of abnormal restrictions on trade, in fact they no longer reflect the operation of market forces. Under such conditions, it becomes necessary to bring about, on a permanent basis, a confrontation of the production policy and the trade policies of the various countries in order to arrive at solutions satisfactory to all.

It is recognized, of course, that prices cannot be set at any level in a completely arbitrary manner. A number of considerations have to be taken into account, notably the effect on consumption. What domestic prices in the importing countries are higher than world market prices, it would be possible to raise the latter through international agreements without affecting the prices paid by the consumer. It is clear that, where import taxes or internal levies exist with respect to imported primary products, the reduction or elimination of such charges would be necessary if prices to the consumer were not to be raised.

In the case of some tropical products, prices to consumers could be increased reasonably, without appreciable reductions in the quantities consumed. Moreover, in most cases in which such products are subject to heavy domestic taxes, world prices could be raised without any increase in the price to the consumer, provided that the internal taxes were reduced accordingly. Indeed, in some cases, these internal taxes are so high that, if they were eliminated, it would be possible not only to raise export prices but also to effect a significant reduction in prices paid by consumers, which would naturally have a very beneficial effect on consumption.

In particular, where commodities exported by developing countries compete with output of the same commodities in developed countries, or with similar natural, synthetic or substitute products, it will be evident that the ability to raise or maintain prices depends on the co-operation of the developed countries. Even where developing countries are sole producers of a given commodity, lack of agreement among these countries themselves, or differences of interest between members of various preferential systems—as well as between them and non-members—may make concerted action to raise or maintain prices difficult to achieve.

Particularly difficult problems arise in relation to synthetics. It has been estimated that more than one third of the increase in the consumption of industrial raw materials in the developed countries between 1953 and 1961 consisted of synthetics and aluminium,[2] and the relative displacement

[2] Based on data communicated by Mr. A. Maizels, National Institute of Economic and Social Research, London.

of exports of developing countries was almost certainly even greater than this would imply.

How is that competition to be faced? In no circumstances could we seriously entertain the thought of restraining technological advances. That does not mean, however, that it is advisable to encourage certain types of research which should not, for the time being, enjoy any priority whatsoever, as, for instance, research into substitutes for coffee. Moreover, in some cases, the transition might be made easier for the producing countries if minimum proportions were established in the use of the natural product, just as minimums are fixed in some cases in the use of certain national primary products in relation to imported commodities.

On the other hand, it is argued that the competition of synthetics or substitutes should be countered by technological improvement in the production of the natural product. For example, there appear to be encouraging prospects for developing certain properties of wool which, in addition to the natural qualities of the product, might enable it to compete favourably with artificial fibres. It is also pointed out that there are possibilities of increasing productivity and reducing prices in order to come out ahead in competition, and natural rubber is mentioned as one of the products in which that objective could be attained. It is evident that we should then be confronted by a case in which the benefits of technological progress would be transferred abroad in the form of lower prices corresponding to lower costs, which would only be acceptable if it was accompanied by a substantial increase in export volume.

Problems also arise when natural products exported from developing countries compete with identical or similar commodities produced in the industrial countries. Efforts to raise the prices of cane sugar and of tropical oils and fats, for example, would be faced with the difficulty that these products compete with beet sugar and oils and fats produced by industrial countries.

Each particular case will need special consideration. Here we may note, however, that wherever it is found impossible or inadvisable to raise or maintain prices to the extent required to avoid deterioration in the terms of trade, as in the case just mentioned of competition between certain natural products and synthetics, it will be necessary to resort to compensatory financing, as will be explained in the relevant chapter below. In other words, it will be necessary to achieve indirectly whatever cannot be secured through direct action on prices.

The means employed for maintaining or raising prices will generally have to include the regulation of supply, involving export quotas and possibly import quotas as well.

This would appear to be inevitable, if the measures for raising prices restricted consumption to any appreciable extent. This could happen if the countries importing a primary commodity imposed import duties in order to transfer the corresponding income to the producing countries, so as to compensate them for losses resulting from the deterioration in the terms of trade. If consumption were to fall because of the rise in internal prices and exports were not regulated, international prices would decline; and thus the exporting countries themselves, instead of benefiting, would pay the duty in whole or in part. The same would happen if, instead of import duties, export taxes were levied in the producer countries.

Lastly, it should be recognized that an international commodity agreement that sets reasonable prices for primary exporters should also contain provisions involving appropriate action to be taken when and as shortages occur by setting ceiling prices in the latter eventuality. This would not only provide protection to consumers but would also be of long-run benefit to producers since unreasonably high prices would stimulate excessive production which, in turn, could lead to low prices for producers.

3. THE EFFECT OF HIGHER PRICES ON PRODUCTION

One of the most cogent arguments against raising the prices of primary commodities is that such increases would stimulate production. If a deterioration in the terms of trade results from the difficulty of adjusting the volume of production to the slow expansion in demand, the difficulty would be even greater if the rise in prices provided additional incentives for increasing production.

Developing countries have acquired sufficient experience in fixing prices to producers at levels different from those prevailing on the world market. Where government trading agencies have been employed, prices received by producers have generally been different from those in force in the international market. In addition, wide-spread use has been made of export taxes and multiple exchange-rate systems. The motives for such policies have been various and have included such goals as the stabilization of producer prices; the protection of consumers from sharp changes in the cost of living; the expansion of government revenue; and the containment of inflationary forces.

If, therefore, it were decided in a particular case that the international price of some commodity might be raised above the current level through intergovernmental agreement, and that the additional proceeds should not accrue to individual agricultural producers, there is abundant experience for implementing such a decision.

The idea of not allowing price incentives to encourage over-production ought also to be applied to importing countries. As explained elsewhere, the policy of agricultural protectionism in many western European countries has resulted in very high prices, making it profitable to farm high-cost marginal land, to the detriment of imports. There is a danger that this process may be intensified during the negotiations pending within EEC. It has been estimated[3] that, on alternative income assumptions, EEC

[3] *Agricultural Commodities and the European Economic Community*, prepared by the FAO secretariat (E/CONF.46/45, pp. 6-7).

grain imports would average between 8.4 million and 10 million tons by the end of the present decade, at unchanged producer prices. If, however, French grain prices rose by 20 per cent in the movement towards a common price level, EEC imports would fall, on the same income assumptions, to between 2.9 million and 4.5 million tons by that time.

Every country is entitled to redistribute its income internally as it deems most fitting from the economic and social point of view. That cannot be a subject of international discussion. But it is possible to discuss the means employed to that end. There are some methods which have purely internal effects and are unobjectionable, but there are others which resolve domestic difficulties by aggravating the problems of other countries. If instead of resorting to high prices, additional revenue were to be paid to the producer without being linked to the volume of his output, it might be possible to attain the social objective sought, namely, to effect a redistribution of income without stimulating production. EEC has itself been considering the idea of utilizing subsidies instead of high prices in supporting the agricultural economy.[4]

Domestic price policy, as pointed out above, is closely related to the demand for imports. Any commodity agreement or other international measure agreed upon in connexion with trade in primary products would have to prescribe minimum import quotas or commitments by the industrial countries. There would be no point in agreeing on higher prices for internationally traded primary commodities only to find that the volume of commodities demanded was declining and perhaps tending to disappear altogether owing to the growth of domestic production in the industrial countries.

This problem is reflected in the French plan for the organization of markets in the recognition that the development of agricultural production in EEC might tend to generate agricultural surpluses; and the plan recommends the sale of such surpluses on concessional terms as a form of aid to developing countries. A number of problems would arise as regards the financing of such sales. But, in any event, it should be understood that there would be a need for firm commitments guaranteeing access to imports from the developing countries, even if such imports had the effect of increasing the volume of surplus supplies to be disposed of on concessional terms. The whole matter should, moreover, be dealt with through concerted action at the international level.

B. *Access to markets*

1. The restriction of imports

As stated earlier, the establishment of prices higher than world market prices, as well as measures for compensatory financing, must be linked with access to markets. The reason for this is not merely that imports might fall when prices rise, but the fact that this rise in prices

[4] See European Economic Community, Commission, document VI/COM(60)105 (provisional edition), part II, para. 11.

would be borne mainly by countries that pursue a liberal import policy and which would therefore have to shoulder a heavier financial burden than countries applying a restrictive import policy.

The problem of access to markets must be viewed broadly; it is not merely a matter of the policies being pursued by members of EEC or of EFTA but of long-term trends which may be traced back to the inter-war period. Likewise, it is not merely a matter of the tendency of supported agriculture in western Europe to become more and more self-sufficient, but also of the tendency of supported agriculture in the United States to develop larger and larger excess supplies.

If we go back to the period preceding the great world depression, it will be seen that the subsequent increase in the imports of primary products by western Europe has been extraordinarily small. Between 1927-29 and 1958-61 imports (excluding petroleum) of the most important commodities increased by barely 13 per cent during the entire period, whereas consumption[5] rose much more sharply: per capita imports of these products actually dropped by 2 per cent.

These developments can be explained mainly by the import trend in cereals, meat, fibres and sugar. Imports of cereals in 1958-61 amounted to 21 per cent less, and imports of meat to 24 per cent less, than in the years preceding the great depression. The falling-off in imports of those two groups of commodities is attributable to a combination of protectionism and the technological revolution. Imports of fibres dropped by 12 per cent as a result of competition from synthetics. Imports of sugar were 30 per cent higher, but consumption rose by 87 per cent in the western European countries taken as a whole.

The contrast between agricultural products, on the one hand, and minerals which western Europe does not produce for itself, on the other, is very striking and indicates the possibilities for increases in imports where protectionism is less significant. Western European imports of metals and ores rose by over 160 per cent from 1927-29 to 1958-61 and imports of petroleum have risen twenty-two-fold, as shown in the table on page 51.

The same table shows the figures for the United States. Gross imports there increased much more than in western Europe, and also more rapidly than consumption. The table does not, however, provide a valid basis for over-all comparison with western Europe because the United States is a major exporter of primary products and its exports have increased as well as its imports, and also because of differences in population growth.

2. Possibilities for effective action

Consideration should now be given to the action that might be taken regarding the facts outlined above. In view of the legitimate interests of

[5] Full data on meat consumption do not exist for the early years. Excluding meat and petroleum, consumption of the other primary commodities rose by 52 per cent and imports by 16 per cent during the period mentioned.

both industrial and developing countries, the first minimum policy objective regarding grains might be a standstill agreement: importing countries might, under a contract similar to the International Wheat Agreement, undertake to maintain existing access to markets, and exporting countries might undertake not to increase pressure on world markets through surplus disposals and to reduce export subsidies.

In the case of western Europe, total grain production now represents about 90 per cent of consumption; it would therefore be desirable to ensure at least that the proportion of 10 per cent currently imported is maintained for cereals as a whole. This could not apply to wheat alone since, as income increases, per capita consumption of wheat tends to decrease. In the case of forage cereals used for feeding livestock, however, there could be a large increase in consumption, since meat consumption rises considerably as per capita income advances. It is clear the attainment of this objective of maintaining the ratio of imports to consumption depends, as we said earlier, on domestic policy regarding prices and surpluses.

For other products, the objective should be greater access to markets wherever possible. There are cases in which agricultural production in both western Europe and North America is high-cost and ought to be readjusted gradually so as to provide greater opportunities for exports from developing countries. Prominent among such commodities is sugar but there are many others, including fats and oils. New taxes or duties affecting imports of primary products from developing countries, such as that now put forward in EEC with respect to margarine, should certainly be avoided. At the same time, improved access should be provided for tropical products in western Europe and for minerals in the United States, involving the gradual removal of existing restrictions, including import or domestic levies of one kind or another.

It would scarcely be possible for the Conference to consider individual commodities in detail. It might, however, consider the advisability of:

(*a*) Taking action to provide greater access to markets in industrialized countries, partly by means of import targets that increase as consumption rises, and partly by the removal of various barriers to trade in primary commodities, including consumption taxes, tariffs and import quotas;

(*b*) Setting certain quantitative import targets in the form of commitments to purchase entered into by importing countries and specifying quantities or prices. This provision could be tied to a guarantee given by exporting countries to provide the importing countries with adequate quantities, thus ensuring supplies of essential foodstuffs and raw materials for the latter countries in times of shortage.

All this would constitute one of the most important and urgent functions to be discharged within the new organizational scheme which is suggested later in this report. Once this policy of setting targets was ap-

United States and western Europe: relative growth of consumption and imports

[*Indices, 1927-29=100*]

Commodity or commodity groupings[a]	*United States*				*Western Europe*			
	Total consumption		*Gross imports*		*Total consumption*		*Gross imports*	
	1955-57	*1958-61*	*1955-57*	*1958-61*	*1955-57*	*1958-61*	*1955-57*	*1958-61*
I								
Cereals	90	96	120	89	138	151	74	79
Meats	215	217	136	1,077	—	—	78	76
Fibres	133	131	171	173	103	99	91	88
Copra and coconut oil	91	98	91	97	122	96	122	99
II								
Tobacco	181	204	166	216	131	162	99	108
Coffee, cocoa and tea	163	176	170	179	125	153	142	143
Sugar	133	149	100	113	159	187	194	130
Bananas	114	140	114	141	194	266	208	236
Metals and ores	222	220	172	156	214	260	343	263
Rubber, natural	139	114	126	106	356	255	1,500	264
Petroleum, crude	863	872	526	576	1,600	2,402		2,277
III								
Average (including petroleum)[b]	167	172	167	176	167[c]	179[c]	126	141
Average (excluding petroleum[b]	131	136	145	151	149[c]	152[c]	108	113

SOURCE: United Nations, *World Economic Survey, 1958*, updated.

[a] The commodity groupings contain the following commodities: *cereals* (wheat, rice, barley and maize); *meats* (beef and veal, mutton and lamb); *fibres* (cotton, wool and jute); *metals and ores* (aluminium, copper, lead, tin and zinc).

[b] Weighted throughout by 1962 average export unit values.

[c] Excluding meats.

proved in principle, it would be necessary to make specific proposals concerning these targets and the ways in which they could be put into effect.

The adequancy of such targets in relation to the export needs of developing countries depends, of course, on the willingness of the industrial countries to make significant modifications in their domestic policies. The case of Sweden provides a striking illustration of a country that has been able to raise the productivity and incomes of its agricultural population without being forced into a policy of self-sufficiency thereby. The Government has adopted as a deliberate objective of its policy the reduction of agricultural output to a level corresponding to 90 per cent of domestic consumption requirements. Swedish agricultural prices, though above world market levels, reflect changes in the pattern of world prices, and are set on the basis of the calculated revenues of well-managed farms. Small farmers receive additional cash payments, but the payments are limited to the current farmers' period of occupancy and do not devolve upon their successors.

A variety of other measures could be introduced to facilitate a scaling down of inefficient agricultural operations in the industrial countries, ranging from the withdrawal of high-cost marginal land from cultivation, to the retraining of agricultural manpower for new occupations. These matters have been the subject of recommendations by FAO and the Organization for European Economic Co-operation (OEEC).[6]

C. *Agricultural surpluses*

1. Surpluses and world consumption

We shall now consider the third point which was mentioned at the beginning and to which reference has been made several times in this chapter: agricultural surpluses. It is impossible to say to what extent the technological revolution and high prices have each contributed to the accumulation of agricultural surpluses. There is no doubt, however, that the application of modern techniques to agriculture, including the use of fertilizer and improved seed, has been stimulated by high prices. Be that as it may, there is every indication that agricultural productivity will continue to increase rapidly. It is estimated that agricultural productivity will go on rising in the United States at an annual rate of over 6 per cent, or more rapidly than industrial productivity. A similar pace of development is to be expected in western Europe, where, apart from the use of better techniques, the consolidation of marginal holdings into large areas employing advanced agricultural methods could lead to major increases in productivity.

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[6] *See*, for example, *An Inquiry into the Problems of Agricultural Price Stabilization and Support Policies* (Rome, 1960), and "Agricultural Policies in Europe in the 1960's", *Monthly Bulletin of Agricultural Economics and Statistics* (Rome, January and February 1963); and OEEC, *Trends in Agricultural Policies since 1955*, Report by the Ministerial Committee for Agriculture and Food (Paris, 1961), chapter V.

It is obvious that, if increased productivity were accompanied by an even greater shift of manpower from agricultural production, the problem of maintaining imports would not be insuperable. Such an arithmetical exercise is, however, very unrealistic, for, as we know, there are great obstacles in the way of such shifts. It is true that, in the United States, the proportion of agricultural workers in the whole of the economically active population dropped from 22 per cent in 1930 to 8 per cent in 1960 and that, in the principal western European countries, the corresponding proportions over the same period dropped by between 33 and 50 per cent. But these shifts have not been sufficient to prevent production from rising faster than consumption in both areas.

Thus surpluses are a fact that will have to be reckoned with for quite a long time. In a world in which large variations in agricultural output from year to year are still commonplace, a substantial food reserve may be of great importance in preventing famine or shortage, especially in densely populated areas. But the role that surpluses might play in the development of the peripheral countries is also very important.

We must beware of exaggeration in this matter. Surpluses represent, and will continue to represent, a comparatively small proportion of the world's needs in foodstuffs. In 1957-59, for example, world consumption of cereals totalled 555 million metric tons[7] and surpluses sold on non-commercial terms amounted to scarcely 8 million metric tons,[8] or less than 2 per cent.

Moreover, in view of world population growth and the need to improve nutrition, it is estimated that by 1980 the world will require a one-third increase in supplies of cereals. There is therefore an important difference between the immediate situation and the long-term outlook. The surpluses of today may very well give way to deficits in the future unless the technological revolution in agriculture spreads to developing countries. Generally speaking, yields in those countries have increased much less than in the developed countries, as may be seen from the following table:

Percentage increase in yields per hectare of twelve major crops[a] from 1934-38 to 1958-60

North America[b]	78
Oceania	52
Western Europe	29
Africa	28
Eastern Europe and USSR	16
Latin America	14
Far East[c]	6
Near East	2

[a] Price-weighted totals of wheat, rye, barley, oats, maize, rice, potatoes, soy beans, ground-nuts, tobacco, cotton and jute.

[b] The North American yield improvement reflects not only technical progress but the drought years during the base period.

[c] Excluding mainland China.

[7] Excluding the socialist countries.

[8] Sales under United States Public Law 480 (title I).

It is not surprising, therefore, that per capita food production in the developing world in general has remained practically stationary in relation to the pre-war period. Thus the essential task is to increase production in the developing countries, and it must be tackled with great vigour and foresight, as has been pointed out in FAO publications.

2. Surpluses and economic development

This does not imply that surpluses do not have a role of considerable importance to play, though not so much from the standpoint of their contribution to the increased consumption as in relation to the trade gap—the fundamental problem with which we are concerned in this report.

The fact is that imports of foodstuffs frequently constitute a significant item in the growth of imports in developing countries, and surplus disposals on concessional terms may be of great importance in meeting this need. Even where such imports represent a comparatively small percentage of consumption, they may weigh heavily in the balance of payments. If such concessional imports were not available, the developing countries concerned might have to sacrifice other imports such as capital goods in order to purchase foodstuffs, to the detriment of their economic development.

It cannot, of course, be assumed that concessional sales of surpluses always enlarge the capacity to import of developing countries considered as a whole. For while it is true that some of the latter benefit thereby, it is equally true that the incomes of exporters of the products concerned may be directly and adversely affected. In any event, it would be necessary to take measures, in line with FAO recommendations, to ensure that surplus disposal does not take place at the expense of export opportunities of the developing countries, whether to one another or to the developed countries.

Nor can it be taken for granted that additional investment is always undertaken in the importing countries in an amount corresponding to the value of the imported surpluses. Food aid provides an opportunity for stepping up investment, but it does not lead automatically to such investment.

Countries also need to guard against the danger that the receipt of food aid will diminish the vigour of their own drive for agricultural development and lead to the postponement of vital decisions on reforms that have to be undertaken.

It has been suggested that food aid should be given in cash rather than in kind, so that the supplies could be obtained from the lowest-cost exporters. However, it should be asked to what extent a country faced with a surplus problem would be prepared to risk the possibility that a substantial share of any food aid it might give would be spent elsewhere. On the other hand, it should be noted that some of the contributions under the World Food Programme are made in cash, even though the amounts are not very large.

Looking further ahead, it is conceivable that the developing countries may in future be able to pay with goods for the imports of foodstuffs that they now receive in the form of surplus disposals. This is an important role that their industrial exports must fulfil within the new pattern of the international division of labour to which reference has been made elsewhere.

In addition to the question of agricultural surpluses, other important problems arise in connexion with the disposal of stocks of minerals, notably from large strategic stockpiles in the hands of developed countries. As in the case of surplus foodstuffs, it is essential to ensure that such disposals do not disrupt world markets, or exert a downward pressure on the volume of prices of exports from developing countries. Such disposals should therefore be subject to international discussion and agreement.

D. *International commodity agreements*

1. Recent experience

So far as commodity agreements are concerned, experience since the end of the Second World War reveals many positive elements and a progressive evolution towards a more favourable framework for international commodity trade. But even more vigorous action is required.

It is not so much a question of creating new machinery, as of adapting the existing machinery to the needs of a policy in which the objectives pursued are more clearly and more fully defined.

The Havana Charter recognizes that international commodity trade is subject to difficulties resulting from persistent disequilibrium between production and consumption. The Charter also refers to measures designed gradually to reduce any unwarranted disparity between world prices of primary commodities and those of manufactured products.

Nevertheless, the Charter gives a rather narrow definition of the circumstances in which commodity agreements may be applied. But nowadays these problems exist on a greater scale and, generally speaking, the view is held that commodity agreements should include suitable measures relating to the various aspects of international trade, especially the fixing of minimum prices, access to markets, and surplus disposal. Notwithstanding this progress, it has so far proved possible to establish international commodity agreements for only five products: wheat, tin, sugar, coffee and olive oil.

Among the difficulties facing countries seeking to formulate these agreements has been the fact that, when export prices are high, many of the exporting countries are less interested in reaching agreement and importers consider that their bargaining position would be better at another time. And, when prices are low, the opposite applies.

From another standpoint, the Havana Charter provides for equal representation of importing and exporting countries. This does not take into account the fact that, under normal conditions, exporting countries have a much larger stake than importing countries in the operation of an agreement because their total export incomes are usually largely dependent on trade in the commodity concerned.

The effort to conclude commodity agreements can hardly succeed so long as such agreements are regarded simply as a compromise between the interests of exporting and importing countries and if they are based mainly on the idea of dealing with market fluctuations. Apart from the understandable interest in having lower prices for the commodities they import, there are at least two aspects to be taken into account by the importing countries. The first involves recognition of the fact that, as the export incomes of the developing countries fall because of the drop in prices, their demand for exports from the industrial countries also declines. The second aspect to be taken into account is the unfavourable impact of low commodity prices upon the growth of the developing countries and hence upon the general outlook for political and economic well-being throughout the world.

Part of the difficulty surrounding the negotiation of commodity agreements lies in the fact that these aspects of the problem are not always given the consideration they deserve. More of these agreements—and more comprehensive ones—could possibly be concluded if these aspects carried greater weight during the negotiations. But this obviously requires a clear statement of the policy to be followed in respect of primary commodities.

The sort of problem that is apt to arise may be illustrated from experience with attempts to negotiate commodity agreements for coffee and cocoa. It appears that for several years it was impossible to negotiate a commodity agreement for coffee because the point of view of the importing countries was largely influenced by commercial interests. However, as a result of the sharp declines in coffee prices during the latter part of the 1950's and the serious impact of these declines upon a large number of Latin American countries, the importing countries began to take a broader view of the problems relating to the regulation of world trade in coffee. This recognition of the issues made it possible for an agreement to be reached embodying the concept of supporting the price of coffee at the 1962 level.

The precedent set in the coffee negotiations aroused expectations that a similar outcome might be reached for cocoa. However, this favourable attitude towards commodity agreements does not appear to have extended to the case of cocoa. Fewer countries were seriously affected by the outlook for this product, and the cocoa problem therefore did not have the same impact in the higher governmental echelons of the importing countries as had the coffee problem. The result was that considerable difficulty was experienced in reaching a meeting of minds on prices. Under these conditions it was, perhaps, inevitable that the negotiations should fail. This breakdown is a great disappointment, and it is to be hoped that the outlook will improve in the future.

2. The broadening of commodity agreements

What is required is that Governments should formulate their policies in this matter and thus provide a frame of reference within which negotiations can be carried out; in other words, there must be a political will to reach these agreements and a desire to carry them out. There can be no doubt that the obstacle here is primarily political rather than technical.

In the first place, a major effort should be made to increase considerably the number of commodities regulated by inter-governmental agreements.

It is important, moreover, that the preparatory work for the formulation of new commodity agreements and the negotiation of such agreements should be vigorously pursued irrespective of current market conditions. In the case of a number of commodities, steps are already under way. The United Nations Cocoa Conference will, it is hoped, be reconvened as soon as there is an indication of better prospects for agreement. Draft agreements on cotton and rubber were discussed some time ago. The International Lead and Zinc Study Group is also considering the drafting of an agreement. A study group on copper has been suggested and tungsten problems are now receiving inter-governmental consideration in a United Nations committee. Certain agricultural commodities are being considered by FAO groups.

From the technical point of view, considerable importance attaches to the study of the problem of standardization and the development of a mechanism for setting up price differentials between various commodity grades, as has been done successfully in the case of wheat.

As was stated earlier, commodity agreements should also be more comprehensive and cover the various aspects of international trade in the commodities concerned. There is already a trend towards this broader approach. For example, the International Coffee Agreement contains an article concerning the removal of obstacles to trade; the International Tin Council has been undertaking negotiations regarding the disposal of non-commercial stockpiles; and the International Wheat Agreement provides for an annual review of international trade in wheat which could influence the determination and implementation of domestic production and price policies.

The latter development is particularly important since one of the main shortcomings of commodity agreements so far is that they have only dealt with international trade in the commodity concerned and, in some cases, with only part of this trade; thus other very important aspects, e.g. the policy of support prices, have been neglected and the consequences have not always been compatible with the interests of other exporting countries.

Under the Havana Charter, no agreement is to remain in force for longer than five years, and the principal objective has been to deal with short-term difficulties or special temporary problems rather than to create conditions for the long-term expansion of commodity trade at stable prices.

In short, there needs to be greater recognition of the role of commodity agreements in the production and trade policies of both exporting and importing countries; the possibility of increasing consumption of primary products and of thus improving long-term prospects should also be further explored. A movement in this direction has already begun with the setting up of a publicity fund under the Olive Oil Agreement, and with the various provisions for promoting consumption contained in the International Coffee Agreement. Reference was made earlier to the possibilities that research may open up new uses for wool; and similar research might well be undertaken for other commodities. This is a field in which international resources might well play an important role.

Some thought might also be given to those commodities for which no agreements are at present envisaged, particularly in cases where they are subject to regulatory measures at the national level. Inter-governmental consultations should be held on these measures, with a view to arriving at solutions in the common interest.

Much of the machinery necessary for a broader and more vigorous commodity policy already exists in embryo, in the form of study groups and similar bodies and commodity commissions of the United Nations and FAO; what is needed is a clearer sense of the objectives to be achieved and of the policy to be followed, and a simplification and unification of structure.

All this would have to be the subject of further study in the event that the Conference agreed in principle on the need for such a policy.

Chapter II

INDUSTRIAL EXPORTS FROM THE DEVELOPING COUNTRIES AND PREFERENCES

A. *Exports of manufactures from the developing countries*

1. Technological development and industrial exports

It would be a mistake to suppose that, in the new international division of labour recommended in this report, the developing countries would merely export simple manufactures and the products of an incipient technology. This would only serve to perpetuate existing forms of production, whereas exports, besides their primary aim, must be an effective instrument for promoting technological progress, i.e., a means of changing these forms of production.

There are forms of advanced technology which are, for the moment, beyond the reach or not easily within the reach of the developing countries, while there are others which are within their reach or could be so in a short space of time. Apart from the supply of capital, the main limiting factor is each country's technological density in the sense of available techniques and skills.

The main industrial centres of the world have attained considerable technological density in the course of time; they are not limited to just this or that speciality but have at their disposal a whole complex of specialities and techniques which tends to extend over a growing proportion of the economically active population and which is reflected in a vast range of skills, from the manual worker right up to the senior technician and the alert and capable executive.

This technology generally requires a high input of capital per person employed. Capital goods can be imported into the developing countries, but not technological density which has to evolve gradually. Only isolated special skills or techniques can be imported. A clear distinction must, therefore, be drawn between capital goods and technological density. There are industries which employ advanced and complex capital goods but which do not require great technological density to develop; if there are a few special skills, or if they can be imported, this is enough to ensure their smooth operation.

These industries may constitute an important factor in the developing countries' policy for exporting manufactures. If such industries absorb large amounts of manpower, they will obviously be more attractive under that policy. It is common knowledge that the problem of absorbing manpower is of vital importance for the developing countries. But they also have another problem to solve with reference to the matter under consideration: the potential trade gap.

Consequently, even though the industries to be developed for exports do not have this capacity to absorb human resources in sufficient measure, this is no reason for disregarding them. On the contrary, they could play a very important role in attaining the second objective.

The same might be said of the industries which are based on a country's natural resources. It is, of course, highly desirable that such resources should be utilized, but the degree to which and the form in which this is done will be subject to those technological possibilities as well as to the availability of capital.

From all these considerations it is clear that the promotion of industrial exports from the developing countries is not just a matter of steering existing industries outwards. Undoubtedly, those industries which in the course of time, could become competitive on the international market should be assisted. However, at the same time, it is advisable to concentrate on the new industries or the new lines of production in existing industries which, with some support in the local market, or preferably in the wider market constituted by a grouping of developing countries, could be launched in the search for external markets.

Furthermore, this situation could not remain static. For, as the technological density of each developing country increases and as its ability to compete abroad improves, new export lines of manufactures will come to the fore encouraged by the dynamism of demand for a series of products. It must not be forgotten that the objective is to lessen the technological disparity between the developing countries and the industrial centres, even though this cannot be done rapidly given the latter's pace of advance.

These considerations give us a clearer picture of the problem of the international division of labour as regards manufactured goods. Naturally, the more advanced countries tend to concentrate on lines which enable them to put their high capacity for capital formation and their great technological density to the best use and thus to raise the income level of their populations as high as possible. Naturally, too, when these structural changes take place, industries that, for one reason or another, are unable to take the same advantage of these favourable conditions gradually give ground to those which can. But it is essential that restrictive measures applied to imports should not impede this trend.

But it is not just a matter of filling the void left by declining industries. This would greatly narrow the horizon. Increasing advantage should also be taken of the opportunities offered by a large number of industries in the developed countries which are growing rapidly in response to the dynamic demand just mentioned. In addition to the finished goods produced by these industries, there is a large variety of intermediate goods which they need and which could be supplied by new industries in the developing countries. The latter countries could then take advantage of the opportunity to share in a very rapidly growing demand, supplying not only goods that are competitive but also goods that complement those produced by industries in the advanced countries.

From another point of view, such sharing by the developing countries in a fast growing demand would not create the same problems for industries in the importing countries as would imports in the case of industries in which the demand is sluggish. These problems we will now examine.

2. Significance of the developing countries' exports

However, before we go any further, a certain confusion should be dispelled. The significance of industrial imports from the developing countries must be clearly explained. The idea has been spread that the low wages prevailing in the developing countries will enable them to flood the markets of the industrial countries and seriously threaten their level of living. The fact is that wages are low in the developing countries but productivity is also low; and even in cases where wages are lower than productivity, the total cost per unit of output is usually high, either because of the shortage of capital or because of the lack of external economies which are such important factors in the cost of industrial products.

On the other hand, even though the cost of some of the developing countries' exports is relatively low, it should be borne in mind that they give rise to remunerative trade. If such countries propose to increase these industrial exports, they do so because they need to import more capital goods and other manufactures from the advanced countries. And if the latter limit their imports from the developing countries, they will lower the level of activity of their more efficient industries in which technological density and capital intensity generate higher incomes, i.e., the more productive industries.

It would clearly pay the industrial countries to shift productive factors from those industries where they can buy more cheaply abroad to those in which their high level of technology really counts. Undue concentration upon the short-term difficulties that may be involved for particular domestic industries in the industrially developed countries may obscure the elementary fact that, in the longer run, it pays a country to buy as cheaply as possible. In this sense the availability of certain low-cost goods from developing countries offers opportunities for new types of mutually advantageous specialization and exchange.

In point of fact, in the advanced countries wages are commonly higher in the main export industries, because it is there that the highest productivity increments are usually registered. Thus, for example, in the United States the average wage paid in ten leading export industries in

1958 was $2.43 per hour, while in the ten industries where the volume of imports was greatest, it was $1.87 per hour.[1] It would therefore be advantageous for the industrial countries to shift labour over a period of time from those industries in which imports from developing countries have been playing an increasing role in recent years and move resources to the export industries where productivity and earnings are higher.

The magnitude of this problem is often exaggerated. Actually, exports of manufactures from the developing countries amounted to somewhat in excess of $2 billion in 1961 and, even assuming an increase of $10 billion by 1970, i.e., by more than half the trade gap, this would represent only some 4-5 per cent of the total increment in the consumption of manufactures calculated for the developed countries from 1961 to 1970.

The effect of imports of manufactures from developing countries on employment has, of course, been very small.

This may be seen from the calculations in the following table of the displacement of labour through rising imports from developing countries between 1953 and 1961. It should be emphasized that the table deals only with the gross displacement of labour by imports: no allowance has been made for the labour absorbed by the additional exports to the developing countries which could not have occurred without such imports from them. Obviously the *net* displacement of labour would have been much smaller. The figures for the gross displacement are relatively small by comparison with the manpower displaced from agriculture or with the increment in the active labour force. The table is intended to illustrate this point.

Displacement of labour by increased imports of manufactures[a] from developing countries, 1953 to 1961

				Numbers displaced as proportion of	
Country	*Numbers displaced*[b]	*Decrease in agricultural labour force*	*Net increase in active labour force*	*Decrease in agricultural labour force*	*Net increase in active labour force*
United Kingdom	30,398	130,000	1,255,500	23.4	2.4
United States[c]	23,303	953,000	7,606,000	2.5	0.3
Germany (Federal Republic)	14,513	1,132,500	2,592,500	1.3	0.6
Belgium-Luxembourg.	5,981	82,000	– 4,400[d]	7.3	
Italy	4,793	916,000	2,136,700	0.5	0.2
Netherlands	2,727	85,500	371,500	3.2	0.7
France[c]	2,690	1,304,000	124,000	0.2	2.2
Canada[c]	1,910	220,000	1,295,000	0.9	0.2

SOURCE: United Nations, Bureau of General Economic Research and Policies.

[a] Excluding metals.

[b] Estimated as the increase in imports of manufactures from developing countries from 1953 to 1961 in 1958 prices divided by twice the value added per person employed in manufacturing in 1958.

[c] Data relate to period 1953 to 1962.

[d] Minus sign indicates decrease in active labour force.

[1] D. D. Humphrey, *The United States and the Common Market,* New York, 1962, p. 127.

The table shows, for example, that in the United States, the gross displacement of labour by imports of manufactures from developing countries was equivalent to only 2.5 per cent of the numbers displaced from agriculture, and to 0.3 per cent of the increment in the economically active population. In France, the proportion was even lower with respect to the decrease in the agricultural labour force, even though it was higher in relation to the growth in the economically active population. The United Kingdom is an interesting case because the number of workers employed in agriculture had already fallen to nearly 5 per cent of the labour force by 1953, so that new displacements from agriculture were very limited. Consequently, the manpower displaced by imports from the developing countries was equivalent to a relatively large proportion of the decrease in the agricultural labour force, namely, 23.4 per cent; but it was only a small proportion (2.4 per cent) of the increment in the active labour force.

It may be calculated from the figures in the table that the increment in the economically active population was equivalent to between 40 and 500 times the gross displacement of labour through additional imports of manufactures from developing countries. Thus, even if the rate of expansion of imports of manufactures from developing countries was stepped up during the years ahead, the consequential problem of adjustment would remain small in relation to the problems that have to be tackled by dynamic industrial economies in any case.

3. Effects on industrial countries

Nevertheless, the difficulties that would arise in certain cases, especially when the importing country is suffering from a serious unemployment problem, whether wide-spread or confined to certain areas cannot be disregarded.

Situations of this kind may hinder the structural changes mentioned earlier. The point of these changes, as far as employment is concerned, is that the labour displaced from certain less productive industries will be absorbed by the expansion of other more productive industries as a result of the expansion of exports. This displacement takes time, however, and meanwhile it will be necessary to prevent serious unemployment, especially when there already is some, as has already been said.

This could occur if imports increased very rapidly and at prices that were exceptionally low in relation to normal market prices and caused a sudden fall in the production of the lines affected.

There is absolutely no reason, however, to attach general significance to these exceptional cases. Industrial exports, as has been stated elsewhere, have been confined so far to a very small number of goods and have gone to a very small number of countries. By contrast, the policy advocated in this report is based on the opportunities offered by a wide range of articles for which demand is growing rapidly. Exports could thus be diversified and the number of cases in which home production would be severely affected would not be very great.

It seems inevitable that there would be cases of this kind. They occur continually in industrial development. What is more, they are an inherent feature of such development, particularly when there is a great dynamic impetus in industry. That is why leading countries have taken positive steps to deal with problems of this kind.

Such steps are designed to facilitate the displacement of workers from industries that are declining because of technological changes to those that are rapidly expanding, and at the same time to provide incentives for attracting capital to the areas affected by industrial unemployment.

Similar steps could be applied also to some industries that may suffer as a result of imports of manufactures from the developing countries. What we are concerned with is a particular case in the general phenomenon of structural change in industry caused by technological progress.[2]

It is clear that steps of this kind take time to produce results and that there will be cases in which it will be necessary to adopt temporary measures to prevent the harm that may be caused to some industries by imports. GATT has appropriate machinery for doing this through the imposition of restrictions on imports; article XIX provides that, if as a result of unforeseen developments, any product is being imported into the territory of a Contracting Party in such increased quantities and under such conditions as to cause or threaten serious injury to domestic producers, remedial action, subject to appropriate safeguards, shall be permitted. Such emergency measures, however, should be of a non-discriminatory character, but in the case of cotton textiles special action was taken outside the framework of the General Agreement, and discrimination against the developing countries was authorized. The fact of such discrimination, and the lack of the normal safeguards which GATT provides in such matters, is clearly cause for serious concern in the countries affected.

4. The GATT Programme of Action

No less serious are various other obstacles to the export trade of developing countries in semi-manufactures and finished manufactures, often discriminating against developing countries, with which the GATT Programme of Action is intended to deal.

It would be very important for the Conference to give its firm support to this Programme. In the first place, the general standstill provision that "no new tariff or non-tariff barriers should be erected by industrial countries against the export trade of any less developed country" is clearly just as applicable to manufactures as to primary commodities and not only to the products now exported but also to the developing countries' new export items.

[2] We may refer here to the legislation enacted for this purpose in the United States (Area Redevelopment and Trade Expansion Act) and the United Kingdom (Distribution of Industry Act) and to various industrial readjustment programmes of the European Coal and Steel Community and of the European Economic Community.

The Programme of Action recommends further that industrialized countries should urgently prepare a schedule for lowering and eliminating tariff barriers to exports of semi-processed and processed products from less developed countries, providing for a reduction of at least 50 per cent of the present duties over the next three yaars. The importance of this recommendation will be apparent from our earlier discussion of the impact of the differential tariffs applied by the industrial countries.

Finally, the Programme of Action requires that restrictions on imports from the developing countries which are inconsistent with the provisions of GATT should be eliminated within a period of one year; or, in special cases of difficulty, not later than 31 December 1965. These restrictions, which are a survival of the period of heavy balance of payments pressure in western Europe, have been considerably reduced in recent years. Those of them that still remain were authorized as transitional measures by GATT in 1955 to ease the process of adjustment. The restrictions are frequently applied on a basis that discriminates against the developing countries, and there is less and less justification for their continuation as western Europe grows economically stronger and the problem of the developing countries' trade gap becomes steadily more acute.

In general, it is essential to remove all existing discrimination against exports of manufactures from developing countries and to ensure that they gain access to world markets on terms and conditions not less favourable than those which apply generally. This is the objective of the GATT Programme of Action, and it is an objective that should receive strong endorsement from the Conference.

B. *The question of preferences*

1. Meaning of the problem

In order to stimulate exports of industrial products from developing countries, two types of measures are required. In the first place, channels to the markets of the great industrial centres should be opened through the elimination of obstacles to the flow of exports. Secondly, the active promotion of exports should be undertaken both in the developing countries themselves and on the international plane.

The existing obstacles to exports have just been examined. But it is necessary to go further and introduce a system of preferences.

The case for preferential treatment for exports of developing countries is that it would help the industries of developing countries to overcome the difficulties that they encounter in export markets because of their high initial costs. It is a temporary measure which, by opening up larger markets to the industries of developing countries, would enable them to lower their costs and thus compete on world markets without the need for continuing preference.

The case is thus a logical extension of the infant industry argument.

It is not a matter of controversy among economists that national protection of infant industries is justifiable wherever such industries have a long-run prospect of reaching a high level of efficiency.

In order to be efficient, those industries must have access to wider markets; otherwise they may not be able to break out of the vicious circle of low output and high costs. Such markets must be sought in the developed countries as well as in other developing countries. But if infant industries need protection in the domestic market because of high costs, they obviously need even more protection in foreign markets, whether developed or developing, in the form of preferential treatment. It is for this reason that the following two suggestions have been made: (*a*) developing countries should give preference to imports from other developing countries in their own markets; (*b*) developed countries should give preference to imports from developing countries in their own markets.

The two suggestions raise somewhat different issues. The main features of the first have already been outlined, and the following discussion will concentrate on the second.

As was said earlier in this report, GATT sanctioned the continuation of preferential arrangements in force at the time the Agreement was signed, but prohibited new arrangements of this sort except where they represen‑ ' a stage in the setting up of customs unions or free-trade areas.

The reason for the prohibition was, and still is, the belief that countries ought to treat one another equally in their foreign trade and not grant advantages to some countries that they are not prepared to extend to others. But however valid the most-favoured-nation principle may be in regulating trade relations among equals, it is not a suitable concept for trade involving countries of vastly unequal economic strength. The acceptance by the Meeting of Ministers of GATT in May 1963 of non-reciprocal tariff concessions to developing countries was a valuable first step in recognizing the need for special encouragement to the trade of these countries. Adoption of the principle of preferential treatment for the trade of developing countries is the logical next step.

It should be emphasized that the granting of preferences to developing countries would not conflict with the objective of the Kennedy round of tariff negotiations or indeed with any other effort to bring down or remove the barriers to trade. Even if the Kennedy round were completely successful, it would mean the reduction but not the elimination of tariffs by the negotiating countries. The issue that arises, therefore, is whether the industrial countries would be ready to grant free entry at least to the developing countries if not to one another. The idea is not to create permanent margins of preference that could be maintained only through retention of existing tariffs by the developed countries. The suggestion is, rather, that pending the elimination of obstacles to trade by the developed countries, free access should be granted to the developing countries.

The introduction of a new system of preferences would involve the mutual adjustment of various conflicting interests among the developing countries on the one hand, and between the developing and the industrial countries, on the other. There may be a temptation to try and take account of any difficulties that arise in reaching such adjustment by introducing complicating devices and refinements into the scheme so as to cater to particular preoccupations. Certain of these devices and refinements could indeed prove to be indispensable, but the general proposition should be borne in mind that the greater the complication of the scheme, the less chance it has of being accepted or found workable.

The first question for consideration is: which countries should grant preferences? The hope and expectation, as already noted, is that all developed countries would agree to grant preferences to all developing countries. While it may be doubted whether the scheme could be effectively implemented unless all major developed countries agreed to participate, unanimity would not be essential. The scheme might enter into force when an important group of countries indicated their willingness to participate.

So far as the participation of the socialist countries in the concession of preferences is concerned, as indicated elsewhere, tariffs do not have the same meaning in these countries as in private-enterprise economies. Nevertheless, whenever tariffs are imposed, free entry should be assured to imports from developing countries. At the same time, the socialist countries should favour imports from developing countries in their foreign trade plans, and their State trading agencies should give effect to such preferences in their purchasing arrangements.

The implementation of all such measures could be evaluated in the light of actual performance, and would be one of the subjects for annual review within the new organizational scheme of trade and development that might be suggested by the Conference.

The selection of countries to benefit from preferences is somewhat more difficult. No single criterion has been found satisfactory in identifying those countries which should be regarded as qualifying for preferential treatment. Such factors as per capita income, the size of the country, the share of agriculture and industry in total employment and output, and the impact of the primary export sector on the growth of the economy should be considered. If these factors are taken into account, it is relatively easy to decide which are and which have ceased to be developing countries in most cases. There is, nevertheless, a small group of borderline cases at the top of the per capita income range and it is not an easy matter to establish the cut-off point among them.

The problem is, perhaps, not too important from the standpoint of the industrial countries, because imports of manufactures from the developing countries are not likely to be a matter of overwhelming consequence for them in any case, as we have seen. But they are for some developing countries which may fear that they will not be able to benefit from preferences if they have to compete with other more advanced members of the developing group. The problem of which developing countries should be included in the scheme is thus closely linked to the problem of gradation or differentiation of preferences which will be examined below.

2. Selection of general preferences and their duration

Most of the discussion of preferences thus far has proceeded on the assumption that they should be granted on a selective basis for particular products. The main consideration underlying this approach appears to be the desire to exclude products which would raise domestic problems for the developed countries, notably those produced in relatively weak or stagnant sectors of the economy of these countries. There may also be a desire to direct the efforts of developing countries towards industries offering substantial growth potential and the prospect of viability within a reasonable number of years, making it possible to discontinue the preferences.

These two considerations appear reasonable enough, but if they are examined more closely, serious disadvantages may be observed.

First and foremost, the experience of GATT and of other bodies has shown that a system of selective negotiations, product by product, raises great difficulties. Naturally enough, each industry which considers itself threatened by foreign competition is liable to adopt a severely defensive attitude and seek to maintain the *status quo*. This very understandable attitude does not find its logical counterbalance in the industries which may increase their exports to the developing countries as the foreign-exchange earnings of the latter advance, since these advantages are still problematical and therefore do not provide a tangible incentive for the adoption of preferences. Nor is it to be expected that an industry that felt itself affected by imports would examine this matter from the viewpoint of the economy as a whole and not for its own particular situation.

If, moreover, the preferences to be granted by all developed countries are to be standard in terms of commodity coverage, the ultimate list of products qualifying for preference is likely to be the lowest common denominator of all national lists; since any industry regarded as vulnerable in any one country is likely to have its way with the general list of all countries.

From the standpoint of the developing countries, moreover, it is difficult to imagine how a suitable selection of industries for preferential treatment could be made. It would surely be better to leave scope for the initiative of enterprises to seek out the best opportunities, subject, of course, to measures of guidance and assistance, in which Governments should have a very important role, as will be seen later. One wonders what degree of success might have attended efforts, in any of the countries that are now industrialized, to draw up a precise pattern of possible industrial exports in advance when they were at the earliest stage of development. It is hardly likely that an effective selection could now be made, from the whole range of industry, of all those particular branches which might prove to be successful in particular developing countries in the long run.

Thus the danger is that a selective list of products qualifying for preference may turn out to be unduly restricted and drawn up much more with an eye to static considerations than to the dynamic possibilities of a new international division of labour. For this reason, a better and simpler approach would be for preferential treatment to be granted in principle to all imports from the developing countries, subject only to certain specified exclusions, as well as certain safeguards, as indicated below.

Much of the discussion that has taken place so far has been related to preferential treatment for semi-finished and finished manufactures only. Acceptance of this limitation would raise a number of difficulties in defining the scope of these products, calling for expert study and recommendation. Expert study would also be required of the problem of defining the origin of products manufactured or semi-manufactured from imported materials or components. Neither these nor any other difficulties seem to be of major consequence, and they should not prevent the Conference from adopting a decision in principle in favour of preferences. Indeed, this decision in principle is necessary in order to provide, through common agreement of Governments, a framework within which the technicians will be required to work out practical details.

A small margin of preference is not likely to provide adequate incentives for establishing new export industries in developing countries. If a new system of preferences is worth introducing at all, the margins of preference should provide incentives that are clearly adequate in relation to the magnitude of the problem.

Since many or most of the tariffs applied to manufactures by the industrial countries are relatively low, and are expected to fall even further as a result of the Kennedy round, the optimum solution would be to grant free entry to imports from developing countries. For the members of EEC and EFTA this would simply mean granting to the developing countries treatment not less favourable than they are prepared to give one another.

Since the new preferential system is intended as an encouragement to infant industries, it will be evident that some provision must be made for the elimination of preferences once the industries are firmly established. In general, preferences should be introduced for a period of no less than ten years with respect to any given industry in any developing country. At the end of the ten-year period, preferences would be withdrawn unless it could be shown, to the satisfaction of an appropriate international authority, that special circumstances warranted their continuation. The ten-year period would be reckoned from the time of the initial granting of preferences to exports of a particular industry in a given country even though this would mean that plants established subsequently in the same country would not benefit from the full period of preference.

The fact that preferential treatment for any one industry in a developing country would normally come to an end after ten years would have two advantages. For one thing, it would compel the entrepreneurs concerned to concentrate on making the industry fully competitive by the time the shelter of preferences was withdrawn. A second advantage would result from the fact that infant industries, established shortly after the inception of the scheme in countries that are still at an early stage of development, would count their ten-year period of preference from the time such preference was first applied to any industry subject to this régime. This means that such industries would enjoy preferential treatment not merely in relation to the industries of developed countries but also in relation to those of the more advanced developing countries, once the respective industries of the latter countries were no longer entitled to preferences.

The duration of preferences should probably not be fixed at less than ten years. Sufficient time must be allowed for their incentives to take effect and for significant results to be achieved in export markets. In the conditions obtaining in developing countries, a short-term scheme of preferences would scarcely be better than no scheme at all.

Thus the duration of preferences raises an issue similar to that involved in the margin of preference, namely, that there is a minimum scale and duration below which the incentive provided would be inadequate. It would not be worth facing all the political and other difficulties entailed in a new departure from the most-favoured-nation principle simply for the sake of token margins of preference on a few selected products for a very limited period, amounting to little more *in toto* than a gesture in the face of the immense problems of the trade gap.

3. Safeguards for developed countries

It would not be difficult to understand an initial hesitation on the part of the industrial countries in accepting a scheme that appears to promote competition from developing countries with the output of certain of their own industries. In time, they would undoubtedly see the advantages of the scheme, since it would provide a means of increasing their sales to developing countries by the amount of the additional purchasing power accruing to the latter countries from the expansion of their own exports with the aid of preference. Thus, the industrial countries may see advantages in expanding rather than in contracting the volume of their preferential imports. Nevertheless, particularly at the outset of a programme of preferences, the developed countries would no doubt wish to have assurance as regards both the total volume of preferential imports and the volume of imports in any one category.

As we have seen, an expansion of exports of manufactures that would be very large in relation to the existing shipments by developing countries would still be extremely small in relation to the actual and potential consumption of manufactures by the developed countries. If, therefore, the developed countries wished to set an over-all limit to the volume of goods imported preferentially, that limit could be fixed at a level very high in relation to existing exports of developing countries, but still very small in relation to the size of their own domestic markets.

The question now arises as to how the aggregate quota of manufactures from the developing countries would be divided between the various industrial countries. One way of doing this would be to divide the total quota in proportion to the consumption of manufactures by each importing country. But this approach would make no allowance for the fact that large countries with highly diversified resources and productive facilities naturally tend to import less in relation to consumption than small countries whose economies are more highly specialized.

An alternative method would be to divide the import quota in proportion to each developed country's imports of manufactures. In this way imports from developing countries would increase, from year to year, in line with total world imports of manufactures. However, the disadvantage of this method is that the developed countries whose import coefficient is very low would have a relatively small quota of preferential imports. It may be possible to combine these two methods in order to find a formula acceptable to all developed countries.

As regards the impact of preferential imports on particular industries, it is necessary to keep in mind the fact that preferences are designed to help in offsetting the high costs of infant industries in developing countries. If, however, as a result of the preference, a country exerts undue pressure on the prices prevailing in the industrial countries, it thereby demonstrates either that it does not need the preference or that the preference is excessive.

Developed countries could hardly be expected to offer encouragement through preferences to those industries in developing countries that are already able to stand on their own feet in world markets and still less to those industries whose costs are much lower than those of similar industries in developed countries.

In view of this, it may be considered desirable that, at the time the new preferential system is introduced, each developed country should be able to reserve its right to withhold preferential treatment from products accounting *in toto* for a reasonable percentage of its aggregate imports or consumption of manufactures. This percentage could include some articles, which it might be considered advisable to exclude from the preferences so as not to affect certain imports from other supplying countries, and certain articles that would be specially reserved for the less advanced developing countries, as will be seen below.

Once the system is in effect, developed countries might add new exceptions to the preferential régime, in accordance with clearly established criteria.

Another possible safeguard might be to provide that imports of particular products could cease to qualify for preferential treatment when they exceed a certain percentage, to be fixed in advance, of the domestic consumption of a particular importing country.

It should be emphasized that the withholding of preference from particular products, under provisions such as those discussed above, would simply imply that normal most-favoured-nation treatment would be applied. The withholding of preference could not in any case justify action to restrict normal imports of the products in question outside the provisions of GATT.

4. Differences between developing countries in relation to preferences

It is now necessary to examine the possibility that some of the more advanced of the developing countries might quickly pre-empt so large a proportion of the total preferential quota allocated by the industrial countries as to leave insufficient scope for countries at a much earlier stage of development. In general, the extent of any danger that the total quota might be used up would obviously depend on the size of the latter. As already noted, in the course of time, developed countries may see enough advantages in the preferential scheme to be prepared to enlarge the total quota.

If the quota were large in relation to existing exports from developing countries, there would be adequate room for all, and it would probably not be necessary to take any steps in the immediate future. Action would be required only if it became apparent, in the course of such an annual review, that there was an obvious danger that some countries might be excluded from the quota and that no possibility existed of enlarging it.

If, however, the total quota is established at a relatively low level, the case for exporting country quotas becomes stronger. The difficulty here is that such an approach is so complicated as to be, in all probability, unworkable. It is not simply that a dozen or so industrial countries would have to establish a quota for each of one hundred or more developing countries—or well over a thousand quotas in all. Difficult as such a sharing out of a small total quota might be, it would be simplicity itself compared with the problem of policing such quotas for each and every item on the import list.

Instead of establishing individual exporting country quotas, it might be better to set some limit to the share which any one country might take of the available total quota. Countries would be permitted to exceed this limit only where it could be shown that the unutilized portion of the total quota was so large in relation to the exports of other developing countries as to leave ample margin for the latter. At the same time, special measures should be adopted to encourage exports from the least developed countries, along the lines discussed below.

Among the most difficult of all problems connected with the introduction of a new system of preferences is whether to give different degrees or kinds of preference to countries according to their per capita income or stage of development.

The rationale for such a gradation of preferences is quite a simple one. The productivity differential between the least and most advanced of the developing countries is far greater than the corresponding differential between the latter and the industrially developed countries. Consequently, the very same considerations that would justify the granting of preferences to developing countries in general would call for substantially larger preferences to the least developed than to the most developed among them.

Differentiation of this sort among developing countries has already found a place in the Treaty of Montevideo establishing the LAFTA. Under the Treaty, the relatively less developed of the Latin American members of LAFTA receive particularly favourable treatment as regards the mutual reduction of tariffs and in other respects.

There is no doubt that not all developing countries would be equally able to benefit from a preferential scheme drawn on a uniform basis. As already noted, the group of developing countries currently exporting manufactures on a significant scale to the industrial countries is relatively small, and the short-term gains from preferences would be limited to this small group. On the other hand, the objective of the preferences would be to provide incentives leading to a broader distribution of manufactured exports in terms of supplier countries as well as of types of products. The danger is that, if these incentives were uniform, the increment in exports might tend to be concentrated in those countries that have already taken the lead in this field.

Unfortunately, the scope for a gradation of preferences may not be very great, especially if the Kennedy round of tariff negotiations achieves significant successes.

When tariffs are relatively low, for example, of the order of 10 to 15 per cent, the gradation of preferences could be detrimental to the incentive to export in the most advanced developing countries without the less advanced having a meaningful advantage; indeed, this advantage could be smaller than would be necessary to overcome cost differences with the most advanced developing countries.

At the same time, it has to be stressed once again that, however well founded may be the reasons for introducing refinements into the scheme, the greater the administrative complications, the smaller the chances that anyone at all will benefit, since the scheme may prove unworkable.

It should also be noted that it is in the nature of the case that not all countries will benefit equally from any one proposal before the Conference, taken by itself. Thus the only countries in a position to benefit from the elimination of domestic charges on tropical commodities in certain industrial countries are those that can or do produce those commodities; and no gains from long-term compensatory financing will accrue to those whose terms of trade do not decline.

At the same time it should be recognized that the problem of the least developed countries as regards preferential arrangements is a very real one and that the issue must be faced squarely. These countries may not now be in a position in which they are likely to benefit to any great extent from preferences on industrial products, and may not be ready to do so spontaneously for some years. Immediate steps must be taken for the ultimate attainment of this objective.

It has already been suggested, as a partial response to the problems of these countries, that preferences should be terminated for any given industry in any given country at the end of ten years, so while the benefits accruing to the least developed countries will begin later, they will also end later. In this way they will enjoy preferences which no longer apply to other developing countries.

Furthermore, the possibility of granting preferences on a series of articles to the less advanced developing countries without extending them to the more advanced can well be envisaged. For this purpose use could be made of the list of products with regard to which the industrial countries had reserved the right not to grant general preferences.

But this is not sufficient. It will be necessary to set special targets for national and international policy in relation to the least developed countries as well as the adoption of special measures to achieve these targets. Such measures should include exceptional efforts to analyse export market opportunities for such countries, to promote their exports accordingly, and to provide aid at a higher per capita level commensurate with the gap to be bridged between them and the most advanced developing countries. In other words, it may be that the provision of a larger volume of per capita aid and of higher promotional effort is a better way of handling the problems of countries at the earliest stage of economic development.

This is not, however, a matter on which a dogmatic position can be taken; it is *par excellence*, one of the most important questions calling for further analysis and discussion.

5. The alternatives of subsidies or devaluation

As was said before, preferences are justified as a means of protecting infant industries in their attempt to gain export markets. The question may be raised whether this could not be achieved by readjustment of the exchange rate rather than by a preferential system.

It is a well-known fact that, generally speaking, the exchange rate appropriate for the traditional trade of developing countries tends to discourage the development of new types of exports. While, in the case of an industrially developed country, a single rate of exchange is sufficient to secure equilibrium between domestic costs of production and the prices in foreign markets, in the case of a developing country there may be no single rate of exchange capable of securing this result. It has to be borne in mind that the exchange rate of a developing country reflects the level of money costs of production in the primary sectors of the economy and not in the manufacturing sector. On the other hand, the less developed a country is, the higher are its manufacturing costs, in general, relative to money costs in the primary sectors of the economy. Thus the exchange rate equating domestic costs and prices in the primary sector with those of the world market will cause manufacturing costs to be excessively high in terms of foreign currencies. It is therefore an overvalued exchange rate from the standpoint of exports of manufactures. On the other hand, the particular rate of exchange which would make it possible for a developing country to gain export markets for its manufacturing industries would mean a considerable undervaluation of the currency in terms of the primary commodities which form the great bulk of its exports.

Devaluation would be a possible solution in such cases, provided that it did not lead to further increases in costs. This might be difficult to ensure in countries where a rise in the price of imports has a direct and marked impact on the cost of living, thereby generating demands for higher wages. Moreover, devaluation would probably lead either to a fall in the external prices of traditional exports or to excess profits for primary producers.

It has been suggested that, in order to avoid these drawbacks, devaluation should be accompanied by two other measures: first, a tax on traditional exports equivalent to the amount of the devaluation; and, secondly, a cut in tariffs, also in proportion to the devaluation. Exports of new products would not, therefore, be subject to the export tax, but would benefit from the incentive provided by the lower exchange rate, while the rise in the cost of foreign exchange for imports would be offset in its effects on internal consumption by the cut in tariffs.

If, for political or other reasons, it proved impracticable to devalue, some method of subsidizing industrial exports could be studied. In this case it would be necessary to secure the agreement of the developed countries not to apply countervailing duties. Such agreement would no doubt be conditional on the construction of an acceptable framework providing for safeguards against abuse.

It goes without saying that, in so far as the above solutions require that the cost of promoting exports of manufactures would have to be borne by the developing countries themselves, neither of the solutions would be as satisfactory for these countries as preferential treatment for their exports.

C. *The promotion of exports of manufactures*

It is clear that the development of an export trade in manufactures from developing countries depends primarily upon the efforts of these countries themselves. No guarantee of access to world markets nor even the granting of preferential treatment could replace measures taken in the developing countries to stimulate industries capable of production for export. There are many obstacles to the expansion of manufactures in the developing countries.

First and foremost, it is necessary to induce export-mindedness. For reasons that have already been explained, their industrialization has been based almost exclusively on import substitution. There is no conflict between import substitution and export promotion. Industries that begin by catering to the domestic market may, as they gain experience and efficiency, branch out into export markets. On the whole, however, import substitution has gone furthest in the light industries, and this is precisely the area where demand is least buoyant in the developed countries, and where the sensitivity to low-cost imports is therefore greatest. Without in any way giving up the hope that the developed countries will be prepared to progressively increase access to their markets for the products of light industries, the developing countries should also seek out the many opportunities that exist in areas of more dynamic demand.

Recent experience strongly suggests that the comparative advantage of developing countries does not lie solely in the textile and other similar industries. There is significant evidence that the developing countries may also have an advantage in, for example, certain of the metal-transforming industries.

There is also a case for exploring, much more systematically than hitherto, the possibilities of manufacturing certain types of intermediate goods and components in the developing countries for use in the industries of developed countries. It is already the practice of large-scale industry in the advanced countries to subcontract certain of their operations to specialized firms, and it is possible that subcontracting of this type may prove feasible on an international as well as a national scale. The advantage of such manufacturing operations for the developing countries is that export sales would be closely linked with the production process of industries in the developed countries, and no elaborate efforts of marketing or merchandising would therefore be required. Such subcontracting would, moreover, emphasize a complementary relationship between industries of developed and developing countries rather than competition. There should be further study of possibilities along these lines, including an examination of methods of avoiding excessive dependence on external factors or an unduly specialized industrial structure such as might result from industrial development of this type.

Much could be done, moreover, to overcome the difficulties that result from the lack of familiarity of industrialists in developing countries with the needs and quality standards of developed countries. At the national level, Governments may undertake their own investigations of foreign market possibilities, introduce inspection and quality-control programmes to export industries, and foster better design through institutes and research centres.

Governments may also be in a position to share certain of the risks involved in breaking into new markets abroad. For example, Governments might well underwrite production and export feasibility studies.

Even in the advanced countries, Governments have assumed a major responsibility in the provision of information to the business community based on their contacts overseas. Governments should also consider offering various types of risk insurance and even undertake to indemnify exporters for losses incurred during an initial period of market exploration or penetration. Provision is also required, particularly for durable goods industries, for export credit facilities that would enable producers in developing countries to compete with the credit terms available to exporters in the developed countries.

A variety of fiscal and other incentives could also be provided. The granting of tax advantages, special treatment in the allocation of import licences or export bonuses, favourable transport rates and many other incentives could help to promote the achievement of adequate export goals. Experience along these lines in the industrially developed countries should be studied with a view to drawing the necessary lessons for developing countries. In addition to these incentives, the developing countries should eliminate certain obstacles which result from their own policies. We have referred elsewhere to monetary overvaluation of a structural nature. But there is another kind of overvaluation which is the result of a process of suppressed inflation: internal costs rise while the exchange rate is artificially maintained. In some developing countries, this has seriously discouraged exports and at the same time stimulated imports, thus aggravating the tendency towards a trade deficit. There is often also a series of administrative obstacles hindering exports. All this should therefore be revised.

All the measures discussed so far involve action primarily at the national level. The effectiveness of such action would, however, be greatly reinforced if supplemented by international financial and technical assistance. For example, studies of market opportunities suitable to the industrial potential of developing countries could be undertaken on a larger scale and more thoroughly if international resources and expertise were made available. Similarly, much more credit and insurance facilities could be made available to exporters if international sources of finance could be brought into play. In this connexion, the pilot programme of the Inter-American Development Bank in providing export credit facilities to Latin American industries constitutes a significant beginning.

Careful study is also needed of the proposal made by the delegation of Brazil to GATT for the establishment of an international trade centre to supply information on market potentialities in the developed countries for goods produced in the developing countries.[3]

There is also scope for private foreign capital to play an invaluable role in promoting exports of manufactures from developing countries. Private foreign investment in the manufacturing sector in developing countries generally brings with it the most up-to-date technical develop-

[3] GATT, Committee III, "International Trade Information Centre" (document COM.III/93, 26 October 1962).

ments as well as a sound knowledge of the markets to be served. Experience in recent years suggests that, for a variety of reasons, foreign capital is likely to be most effective as well as most acceptable in developing countries if it is combined with local capital and initiative. It would also be important for the developing countries to require, in suitable cases, that adequate export goals be achieved by industries established with foreign capital resources. Where international companies establish subsidiaries in developing countries, they frequently concentrate on import substitution in local markets, avoiding exports which would compete with the output of their home-based plants. Governments of developing countries should study the possibility of making the co-operation of private foreign capital conditional upon adequate export performance, and certainly any special incentives provided to private foreign capital should be linked to such performance.

In general, there is still much to be learnt and studied in the field of export promotion, and the time available for preparing the present Conference has not been sufficient for this purpose. The co-operation of the United Nations Centre for Industrial Development should be sought in pressing forward the necessary investigations in this field.

Chapter III

THE PROVISION OF INTERNATIONAL RESOURCES FOR THE DEVELOPING COUNTRIES

A. *Compensatory financing to counter the effects of deterioration in the terms of trade*

1. THE POLICY OF FINANCIAL CO-OPERATION

The great defects discernible in present financial co-operation policy towards the developing countries must not blind us to the substantial progress that has been made both in the scale and the results of financial co-operation since its beginning soon after the Second World War.

The funds supplied by the private enterprise economies in various forms (loans, private investment and assistance proper), which amounted to $1.8 billion in 1950, reached a total of $6.6 billion in 1962. Although the average rate of increase has been around 11 per cent *per annum,* a great deal remains to be done. In 1962, the funds supplied amounted to only 0.7 per cent of the combined income of these developed countries. On the other hand, although this is a great deal less than the 1 per cent approved by the United Nations General Assembly, it compares favourably with the figure of scarcely 0.3 per cent recorded in 1950.

There have been very positive advances in the conception of financial co-operation. While the importance of external private investment in the developing countries is recognized, the need for the provision of considerable amounts of public resources is no longer questioned. The liberalization of the terms on which these are made available, with respect to maturity, interest charges, and type of projects, is in itself a considerable advance. Regional institutions have been set up which usefully supplement the world finance agency, while the recent evolution in the policy of the latter has given a strong impetus to a process that had been developing over the years as a result of experience. Quantitative targets for the provision of international resources were established in the Punta del Este Charter and the amounts and allocation of those resources were linked not only to the viability of specific projects but also to development plans in which modifications in the economic and social structure are recognized as an indispensable requirement for development.

However, this progress in financial co-operation policy is not without its negative aspects. There are two which are of major concern to us here. First, the deterioration in the terms of trade has seriously impaired the developing countries' capacity to import capital goods, thereby offsetting the positive effects of the international resources made available. Secondly, the relatively early maturity dates for repayment of a considerable proportion of these resources, together with the kind of servicing some of the loans require, are a heavy burden on many developing countries and will become so for others if things continue as at present. These are matters which are obviously important and we shall proceed to examine them in view of their close connexion with the purposes of the Conference.

2. THE NEED FOR COMPENSATORY FINANCING

If the developing countries are to reach and surpass the goals of the Development Decade, they must be able to plan the necessary mobilization of internal and external resources to this end. Any acceleration in the rate of growth implies a stepping up of the rate of investment; and in so far as this in turn involves imported equipment, it can be programmed only on the assumption that the required volume of disposable foreign exchange will be available.

Most of the developing countries have little or nothing in the way of a safety margin for absorbing declines in foreign exchange availabilities. Their external reserves are low, and in many cases their imports of non-essential goods have already been cut to the minimum. Thus, any deterioration in the terms of trade seriously impairs their capacity to import the capital equipment required for growth. Such a deterioration thereby undermines the achievement of the very objectives for which international resources are supplied to them. Economic development is or should be a coherent process in which particular elements and projects mutually support and reinforce one another. The effectiveness of any project financed under a programme of co-operation is therefore bound to be diminished if other foreign exchange resources, which were counted upon for complementary investments, cease to be available because of an unforeseen decline in commodity export prices. In seeking reasons for the shortcomings in existing programmes of financial co-operation one cannot afford to overlook the damage caused by the deterioration in terms of trade.

The solution to this problem should be approached from two sides. We have already examined the case for commodity agreements. But such agreements cannot offer a complete solution for all commodities or for all situations. It is therefore important to provide supplementary resources to compensate developing countries for losses from declining terms of trade.

The fundamental aim of a compensatory scheme should be to maintain the total purchasing power of the external resources accruing to developing countries through their exports.

Much thought has been given to the short-term aspects of this problem. Proposals have been made for a development insurance fund designed to give full or partial compensation for a shortfall in export proceeds compared with some base period. While action on these proposals has been deferred, the International Monetary Fund has begun to apply a new scheme of lesser scope which provides certain accommodations to tide countries over a period of temporary balance-of-payments disequilibrium resulting from export shortfalls.

Useful as holding operations of this kind may be, they do not go to the heart of the longer-term problems associated with a downward trend in the terms of trade. As in the case of commodity agreements, a basic policy decision is required—a decision in principle that developing countries experiencing a deterioration in their terms of trade should have easy access to additional international resources in order to achieve the objective of maintaining their purchasing power. As will be explained, the satisfaction of such requirements must depend on certain conditions. Subject, however, to the fulfilment of acceptable criteria, the international community should recognize that it has a clear responsibility towards developing countries that have suffered a deterioration in their terms of trade in the same way as Governments recognize a similar responsibility towards their domestic primary producers.

However, the additional resources that would thus be provided are different from the usual resources made available in the form of loans. Loans represent resources which the countries making them take from the income they themselves generate, whereas the operations under discussion constitute transfers of resources derived from the income which accrues from countries exporting primary commodities as a result of the deterioration in the terms of trade in respect of those products.

What, then, should be the point of departure for measures of compensation? In relation to what point in time should losses be calculated? Would it suffice to assure the developing countries that they will not be subject to new losses in relation to present prices? Or should losses be calculated in relation to some past year, when the terms of trade were less unfavourable to developing countries than they have recently been? To compensate for new losses is important but it is not enough; something needs to be done to restore the purchasing power of the developing countries, and not simply prevent it from weakening further.

So far as the first aspect is concerned, the point of departure presents no major difficulty, since it would be possible to take the terms of trade prevailing in the last year and, in the light of any new decline that may have occurred, to calculate the resources to be transferred.

The second aspect, however, raises the problem of deciding from what year or years the deterioration ought to be calculated, since the results will obviously be very different depending upon the year chosen and there is no objective or automatic way of solving this problem. It will therefore be necessary to adopt a pragmatic approach to a solution.

Such an approach would have to be based on a study of the potential investment resources lost by each country as a result of actual past deterioration in the terms of trade, the impact of this deterioration on the balance of payments, the effects of both these phenomena on the rate of growth, and any other factors that it might be advisable to consider in each particular case. This study would be necessary in order to determine what additional international resources would have to be provided in order to compensate developing countries for the adverse effects of the terms of trade.

It is not for this report—and much less for the Conference—to deal with such questions of methodology nor with the statistical procedures that might be developed to determine what further deterioration there may be in the terms of trade or, as has just been explained, to compute the amount of additional resources that would have to be furnished in order to deal with the consequences of past deterioration. All this should be studied by experts, whose recommendations will have to be submitted to the Governments for consideration. However, in order to prevent the experts from proceeding along the wrong track, there must be a prior political decision regarding the transfer of resources and the two aspects that the transfer will involve. In other words, a clear distinction must be made between a political decision adopted in principle and the most appropriate technical methods of implementing it.

3. Compensatory financing and development plans

The pragmatic approach to which reference has just been made would be easier if the countries concerned had a development plan. A development plan is generally based on the assumption that the export and import prices currently prevailing will be maintained during the period of the plan. It is on this assumption that the possibilities of mobilizing domestic capital are quantified. If, however, the terms of trade subsequently worsen, not only will it be impossible to finance imports on the scale envisaged in the plan, but domestic resources may also fall short of the target because of the adverse effect on real income.

Nor is it usually possible, in such a situation, to have recourse to external borrowing to replace the lost resources, since the institutions providing long-term credit are apt to regard the deterioration in terms of trade as a factor which, because of the impairment of ability to repay, reduces a country's credit-worthiness. This reduction in borrowing capacity aggravates still further the consequences of the deterioration in terms of trade.

The need for compensatory financing to maintain the integrity of development programmes will therefore be apparent. Nevertheless, such financing cannot be purely mechanical. The mere transfer of compensatory funds will not suffice to restore the plan to its original course. It will be necessary—as was said before—to examine the new situation that has been created and to determine the impact of the deterioration in the terms of trade, the adjustments that should be made in the plan, and the manner in which the funds given in compensation should be applied. The important point is that the country should know in advance that, subject to the fulfilment of certain conditions, it can count on the necessary funds to offset the consequences of the deterioration.

It should also know in advance that, if the plan has been based on a serious effort to mobilize domestic capital, a country will not be required to intensify that effort at a time when its ability to do so is clearly reduced. Any such additional effort would in any event reinforce, but not be a substitute for, compensatory financing, assuming there was sufficient margin for that purpose. Finally, the availability of compensatory funds would afford the international credit agencies the assurance they would need that the country's ability to pay would not suffer from the effect of the adverse terms of trade.

Any significant review of the development plan will obviously take time, and if a country had to wait until such a review was carried out, the deterioration of the situation might make the plan, as originally conceived, unworkable. It is in such conditions that the experiment in short-term compensation initiated by the International Monetary Fund might come into play: such compensation would provide a means of tiding a country over the period during which the necessary adjustments in the plan could be made, and a claim established for long-term compensatory financing.

In the light of this explanation of the close link between compensatory financing and development plans, it will be understood that the resources in question should not normally be allocated directly to individual producers. If that were done, not only would the basic objectives of the development programme be adversely affected, but the problem of deterioration in the terms of trade might be aggravated in the future as a result of the incentive which the higher return would offer to producers.

The relationship between compensatory financing and developing programming is linked to still another consideration. To ensure that such financing achieves its purpose, the additional resources mobilized should not be obtained at the expense of financial resources already being supplied to the developing countries. The percentage of national income which such resources now represent should not decrease but should go on increasing towards the accepted target of 1 per cent. Compensatory funds should constitute a net addition to that target, the amount of the addition depending, of course, on the terms of trade. Moreover, in view of the outright loss that a deterioration in terms of trade represents, the compensatory resources should not take the form of loans subject to amortization and interest payments.

4. Receipt and disbursement of resources

While the obvious differences between compensatory and other forms of financing would necessitate separate treatment of the former, including perhaps the creation of a separate fund, it does not follow that a new institution would be required. A fund of this type could be administered through existing international credit institutions, including regional credit institutions.

In order to fill this new role, these institutions could review claims for compensatory financing submitted to them under general rules approved by Governments. An alternative might be the creation of a body of independent experts of the highest standing which would be responsible for the review.

In this connexion, it may be noted that experience with development plans has shown the need to specify the investments required for the attainment of the plan's objectives, the internal resources to be mobilized for that purpose, and the international financial resources required for the same end. Much remains to be done in working out appropriate methods and procedures along these lines: particularly difficult for recipient countries is the practice of financing individual projects without committing the total external funds required for the duration of the plan. It is to be hoped that procedures for allocating resources furnished as compensatory financing will help to give developing countries every reasonable assurance that they can rely on the global funds needed for the carrying out of their development plans.

Finally, as to the form in which the necessary resources should be raised, naturally it would be for each country to determine the form which suits it best. However, if use is made of a levy on imports of primary committing the total external funds required for the duration of the plan. care would have to be taken to ensure that it does not have a very marked effect on consumption, and that the effective incidence of the levy is on importing and not on exporting countries, as we have already explained in our comments on such arrangements elsewhere in this report.

It would also be necessary to bear in mind what was said in these comments about the need for a link between such measures and access to markets, not only because of its importance as such but also for reasons of equity since, without it, the more primary commodities a country imported, the greater the effect would be on the receipt of resources.

B. *The burden of servicing and other aspects of external financing*

1. CRITICAL SITUATIONS IN THE MATTER OF SERVICING

The problem of the burden of servicing is closely linked to the slow growth of exports and the deterioration in the terms of trade. It is also clear evidence of the need for a consistent policy of international economic co-operation. While on the one hand the flow of international financial resources to the developing countries has increased—and this is very laudable—on the other hand, the access of exports from these countries to markets of industrial countries has not been facilitated, nor been provided reasonable stability in the purchasing power of those exports.

In what way, other than by such exports, could the increasing financial burden of servicing be borne? Reducing imports for that purpose has its limits, and the greater the need for essential imports, the narrower those limits will be.

The results of this contradiction are apparent in a number of countries and have assumed critical proportions in some of them, as we have said before. This is due not only to the accumulation of external debts but also to the relative shortness of their repayment periods, the relatively high rates of interest on some obligations, and the high earnings of some investments. According to preliminary findings contained in a report that the International Bank is preparing for the Conference, the public and publicly guaranteed debt[1] on the developing world rose from approximately $8-10 billion at the end of 1955 to some $24 billion at the end of 1962: i.e., increasing at an annual average rate of around 15 per cent. The increases, of course, varied markedly from country to country, as shown in the following table:

External public debt of nine major debtor countries
($ million)

Country	*End 1955*	*End 1962*	*Average annual percentage increase*
Argentina	(600)*	2,067.1	19
India	309.8	2,925.9	38
Pakistan	147.4	829.2	28
Turkey	(600)*	931.5	7
Mexico	478.9	1,359.9	16
Yugoslavia	331.5	778.1	13
Colombia	276.2	638.8	12
Chile	350.7	741.9	11
Brazil	1,380.3	2,349.0	8
ABOVE TOTAL	(4,475)	12,621.4	16

SOURCE: IBRD, Economic Department.
* Estimates.

For all developing countries, servicing charges arising from interest and amortization[2] on the public and publicly guaranteed debt rose from $900 million in 1956 to $3.1 billion during 1963: the growth rate for such service payments, therefore, averaged somewhat in excess of 19 per cent during this interval. Of course, the amount of these annual servicing payments depends not only upon the level of a country's existing debt, but also upon the repayment terms under which international public loans are extended. As can be seen below, a considerable number of developing countries currently face an important problem because of the relatively short period within which repayment of their public debt is due.

[1] Excluding socialist countries. The public debt data exclude net obligations arising from transactions with the IMF, and outstanding short-term commercial arrears. If the latter were included, the 1962 figure has been estimated at approximately $28 billion.

[2] Excluding socialist countries. In both periods, amortization represented over two thirds of the total.

Percentage of public and publicly guaranteed debt[a] repayable over the next five years

50% or more	*40-49%*	*30-39%*	*20-29%*
Argentina	Burma	Ecuador	Bolivia
Brazil	Ceylon	Ethiopia	Dominican Republic
Guatemala	Chile	Iran	India
Israel	Colombia	Nicaragua	Pakistan
Mexico	Costa Rica	Nigeria	Paraguay
Philippines	El Salvador	Peru	Sudan
Turkey	Spain	Thailand	Uruguay
Venezuela			
Yugoslavia			

SOURCE: IBRD, Economic Department.
[a] Excluding short-term commercial arrears.

Loans and investments for the developing countries have not always been made in reference to their need for resources and in the light of their ability to pay but have often been motivated chiefly by the immediate convenience of the countries exporting capital goods. This has frequently resulted in the establishment of repayment periods which, while possibly justified in individual transactions, were not compatible with a cautious estimate of the country's ability to pay.

Actually, the care with which some institutions have adjusted the repayment periods of loans to the special situation of each country was of little value in cases where similar transactions were taking place through other channels.

In any case, those are the facts and they have to be confronted without delay. The way in which that should be done is being studied by competent bodies and we will therefore limit ourselves here to some general comments, comments which we consider relevant to this Conference.

For the purposes of the Conference, there are two aspects to be examined: first, the critical problems confronting a number of countries; and, secondly, the need to prevent their repetition by measures affecting both the countries which provide international financial resources and those which receive them.

2. Consolidation of debts and extension of repayment periods

So far as the first of the above aspects is concerned, the consolidation of a number of short-term or medium-term debts and the average extension of the repayment period for the external debt as a whole, would appear to be unavoidable for some countries. Experience, both national and international, has shown, more than once, that some very critical situations of indebtedness have been successfully dealt with, and serious dangers avoided in this manner. However, meeting pressing obligations by assuming others which soon will become equally pressing simply postpones the hour of reckoning but is not a solution.

Obviously it is not merely a matter of calculating by mathematics how servicing could be reduced by stretching out the repayment periods. This is a problem which cannot be divorced from a country's economic development policy. It must therefore be part and parcel of a development programme which makes provision for using, together with other internal and external resources available for covering the investment programme, the resources released by the lightening of the servicing burden as a result of debt adjustments.

There is no doubt that compensatory financing is an important factor in this adjustment of the external debt. Compensating a country for the loss it suffers because of worsening terms of trade will provide a much sounder basis than at present for these adjustments of the external debt and for further operations in the future. What is more, such compensatory financing resources might be used by Governments for servicing the new debts deriving from the adjustment. There is no doubt that this additional safety factor would help considerably to make the operation more feasible, particularly the reduction in the interest burden.

The other problem—that of preventing a repetition of the events that led to the critical situations which cause so much concern—must also be related to the need for gearing international loan and investment operations to the requirements of each economic plan. The composition of a developing country's debt, so far as its type, repayment period and other characteristics are concerned, cannot be arbitrary; it must respond to the conditions and needs of each country.

3. Problems that will be solved more easily with development plans

There has been considerable progress in thinking in this field in recent years but not enough. Where a plan is considered sound by those who have to decide on the provision of supplementary international resources, it would be highly desirable for such resources to be committed in principle for the duration of the plan and for their disbursement to be subject to fulfilment of the basic conditions of the plan and to the submission of specific projects. This over-all approach to the plan and its financial requirements would give the Governments and institutions providing the resources an opportunity to co-ordinate the various operations so as to make them compatible with the plan and the capacity to pay all servicing charges, in the light of probable export growth, import requirements and other external payments.

Naturally, in the complex of reciprocal commitments involved in an operation of this kind, countries receiving resources will have to assume, *inter alia,* the obligation of prior consultation concerning any marginal operation not included in the over-all financing of the development plan with those who have undertaken to provide the international resources. Otherwise they would run the risk of once again finding themselves in a critical situation.

Again, a plan is the only way of solving a problem which is closely linked to foreign trade in the developing countries. A start has been made in the right direction but the complete solution of this problem will depend on a plan's over-all perspective. We are referring to the external financing of a part of internal investment.

There has been considerable reluctance to do so because it has been felt that external resources should be used exclusively for imports of capital goods. The result has been that a developing country which found it convenient to produce some capital goods domestically could not do so with international resources: it was compelled to use its own limited resources, not only for that purpose but also for the local expenditure related to investments effected with imported goods.

The fact is that external resources are needed to make up for the shortage of internal resources in programmes of investment and if they are effectively used for any of those investments and are not spent on consumption, it makes no difference, economically speaking, whether they are used to pay for imported capital goods or for internal investment.

That reluctance may be due mainly to a desire to promote the export of capital equipment in the major centres, but, while such desire is understandable, it may not necessarily coincide with the requirements of good development policy, since there is no reason for stimulating imports of certain types of capital goods when they can be economically produced in the developing countries. Moreover, if external resources are used internally, either in the production of such capital goods or for local costs of investment, that does not mean that they will be lost from the point of view of foreign trade. Actually, they will be used for other imports, since there is no perceptible tendency in the developing countries to accumulate unduly large monetary reserves.

It would therefore be advisable to avoid this water-tight separation of resources not only as regards the aspect just indicated but also as regards another important respect. In this report, emphasis has been laid on the advisability of forming groupings of developing countries in order to promote their reciprocal trade and thereby to reduce their potential trade deficit. Now, it is the desire of industrial countries to promote their own exports of capital goods which generally prevents financial resources obtained in such countries by a developing country from being used in other developing countries for procuring the same goods under competitive conditions. This is part of a general problem of multilateralism in the employment of international financial resources. However, pending a solution of that problem, it would be advisable to introduce this additional element of flexibility as an integral part of the policy of international co-operation for economic development.

If this were to happen, considerable impetus would be given to exports of capital goods from some developing countries to others, as well as to industrial countries, in the course of time.

Under present circumstances, the developing countries are at a disadvantage because they cannot compete with the more advanced countries with respect to the granting of export credits. In order to remedy this inequality, the Inter-American Development Bank has initiated a system of export credits for the Latin American countries and it is to be hoped that the necessary resources will be forthcoming to give these operations the impetus they require. Likewise it would be desirable for a similar system to be extended to the other developing countries, and for the possibility to be studied of setting up an insurance scheme for such credits.

This close link between the external resources granted to a developing country and specific projects geared to imports of capital goods is also based on the need for a thorough study of the projects. However, in the absence of a development plan in whose context such a study could be made, there is nothing to prevent internal resources from being used on low priority projects or on projects which are meaningless from the economic or social point of view.

All these considerations make the need for planning more imperative, a point that is duly stressed in this report. What is more, planning is the best way of making the policy of financial co-operation most effective.

In this connexion, it must be borne in mind that the extent to which international resources allocated to developing countries in recent years have been effectively utilized is being widely questioned in the developed countries.

Comparisons are being made with the European Recovery Programme—a programme of aid which was associated with the rapid post-war revival in western Europe in the space of a few years, and which it was possible to discontinue as country after country regained its economic strength.

There is no doubt that much remains to be done by the developing countries in taking the internal measures which would enable them to make more effective use of the external assistance available to them. We shall refer to some of these measures later.

But one cannot in any case make a valid comparison between the aid that was supplied to western Europe after the war and the resources now being placed at the disposal of the developing countries. For one thing, the average annual amount of economic aid given to western Europe from 1948 to 1951 was of the order of $12 per capita, while the corresponding assistance now being supplied to developing countries works out at about $4.

Above all, it is in the very nature of the problems of developing countries that they do not yield to rapid or sudden solutions. The task of making up for the economic lag of centuries cannot be compared with the problem of European economic recovery even after a destructive war.

Chapter IV

TRADE BETWEEN THE SOCIALIST COUNTRIES AND THE REST OF THE WORLD, PARTICULARLY THE DEVELOPING COUNTRIES

1. TRADE POTENTIAL OF THE SOCIALIST COUNTRIES

The importance of the socialist countries in the world economy is reflected in the fact that their share in world industrial production is estimated to be of the order of one third. Their share in world trade, however, is not of the same relative importance.

This fact, combined with the plans of these countries for a continuing process of rapid economic expansion indicates the possibility of a much higher volume of trade with the rest of the world than exists at the present time. The form and manner in which that trade potential could be realized, and could help other members of the world community progressively to obtain the benefits of economic development, constitutes one of the most important questions before the Conference.

The present relatively low level of trade of socialist countries with the rest of the world has to be considered in a broad perspective. Before the revolutions that took place in those countries, their external trade pattern (with the exception of Eastern Germany and Czechoslovakia) resembled that of developing countries: they supplied a number of primary products to the industrial countries in exchange for manufactures, trading very little with one another or with the rest of the developing regions. Before the Second World War, the smaller countries in this group did not maintain extensive trade relations with the USSR, which had already built its industrial economy. After the war however, these trade relations expanded considerably, while their trade with the rest of the world was much lower than before the war.

This shift in the direction of their foreign trade should not be attributed to purely economic reasons, although undoubtedly they found advantages in their reciprocal trade. But even more significant may have been international political developments whose examination is outside the scope of this report. If, however, the favourable change currently under way in the international political sphere continues—as is to be hoped—new and important possibilities for closer trade relations between socialist and private-enterprise economies may emerge, to the benefit of both.

Exports of CMEA countries to the rest of the world have been growing rapidly for a number of years. As can be seen in the following table, they rose from approximately $1.9 billion to $4.7 billion between 1955 and 1962, and during this same period exports to developing countries increased from approximately $0.4 billion to $1.9 billion.

Exports of CMEA countries[a]
($ million)

	1955	*1962*	*Annual growth rate (%)*
To CMEA countries	4,750	10,150	11.5
To the rest of the world	1,900	4,760	14.0
To industrialized private enterprise countries	1,480	2,750	9.3
To developing countries	420	1,910	24.0
TOTAL EXPORTS	7,950	15,770	10.4

[a] Based on data provided by the Statistical Office of the United Nations. The 1955 and 1962 components in both tables do not add up to the totals, due to unallocated residuals.

Although exports of developing countries to the socialist world are still equivalent to less than 5 per cent of their total exports, the increment in these exports in recent years has accounted for an important proportion of the total expansion in the value of exports of these countries, as shown by the following figures:

Exports of developing countries[a]
($ million)

	1955	*1962*	*Annual growth rate (%)*
To industrialized private enterprise countries	17,120	21,030	2.9
To developing countries	5,840	6,550	1.6
To CMEA countries	445	1,420	18.0
TOTAL EXPORTS	23,957	29,630	3.1

[a] Based on data provided by the Statistical Office of the United Nations. The 1955 and 1962 components in both tables do not add up to the totals, due to unallocated residuals.

The socialist countries members of the Council for Mutual Economic Assistance (CMEA) plan for a considerable growth in their foreign trade. According to estimates of the secretariat of the Economic Commission for Europe, if current plans of these countries for a growth of national income are realized, total imports may rise from $15.2 billion in 1962 to nearly $30 billion in 1970 and over $50 billion in 1980.

If one could assume that the share of the developing countries will be maintained at around 10 per cent of the total, as at present, this would imply a potential expansion in their export markets in the CMEA countries from $1.4 billion in 1962 to $3 billion in 1970 and more than $5 billion by 1980.

On the other hand, certain CMEA countries foresee increases in the share of trade with developing countries in their total turnover, and if this became true of the other countries in the group as well, the potential for expansion could be greater than indicated above.

But might not CMEA policy develop in such a way as to reduce the relative importance of trade with the developing countries and with the rest of the world in general?

In this respect, the socialist countries are in a very different position. On the one hand, the Soviet Union, with vast natural resources, might be in a position to maintain its own rate of economic development with very little need to trade abroad more extensively even if international relations improved. The same is not true of the other socialist countries, which, by the very nature of their economies, need to increase their trade with the rest of the world. That is why it is clearly in their interest to work out a more dynamic approach to foreign trade.

But the Soviet Union also, despite the above-mentioned considerations, has expressed its interest in active participation in a new international division of labour with the rest of the world, both industrial and developing, in order to achieve the most effective utilization of its productive resources through international trade.

There is nothing in the constitution or machinery of the CMEA which would stand in the way of an intensive development of trade with the private enterprise world. Experience to date, moreover, shows that such development has in fact already begun, even though it remains within the modest limits of an initial effort undertaken in generally unfavourable circumstances. Thus between 1955 and 1962, according to the first table, trade among CMEA countries increased at an average annual rate of 11.5 per cent, while trade with the industrial countries advanced at a rate of 9.3 per cent *per annum*, and with developing countries at a rate of 24.0 per cent *per annum*.[1]

2. Trade between socialist and private-enterprise economies

The establishment of more favourable conditions for trade between socialist and developing countries should be considered in the light of the relations between the socialist countries and the private-enterprise countries in general. World trade is an intimately interrelated network, and the repercussions of obstacles in any one part are felt inevitably in all others.

The low levels of trade between socialist economies and developed private-enterprise countries are attributed to different causes. On the one hand, it is contended that many of the private-enterprise economies discriminate against trade with the socialist countries by a variety of means which include the application of controls on certain categories of exports and a refusal to give most-favoured-nation treatment in respect of imports. On the other hand, it is asserted that the trading system of the socialist countries does not permit verification of the application of most-favoured-nation undertakings, that the specification of countries of origin in import plans as well as the quantitative regulation of imports in general may

[1] Excluding Cuba, the rate would be somewhat less than 20 per cent.

involve discrimination, and that in any case the level of trade depends on the socialist countries' plans and their ability to meet the specific needs of both the advanced and developing private-enterprise countries, rather than on any obstacles that may be encountered in the latter countries.

No useful purpose would be served by entering into the substance of these differences in the present report. Fortunately, there is evidence of some progress as regards the possibility of finding a *modus vivendi* in this matter. Both sides are beginning to recognize that they must respect each other's systems and try to adjust their policies so as to secure a mutually satisfactory solution. It was in this spirit that experts, from seven countries of different economic and social systems, met in Geneva under the auspices of the Economic Commission for Europe during September, 1963, and were able to agree that trade relations could be developed on the basis of effective reciprocity and mutual advantage, as reflected in "the increase in the volume and composition of trade between countries with different systems which would satisfy the trading partners and would serve as a basis for its further development on a long-term and balanced basis".[2] There was also a general consensus that a realistic and practical approach of this sort would be more profitable than detailed discussion on the theoretical aspects.

The experts recognized further that while the developed private-enterprise economies use tariffs to regulate their foreign trade, tariffs do not serve the same functions in the socialist countries. For the imports of socialist countries are determined through their national economic plans and the state monopoly of foreign trade: tariffs have a complementary function, namely, to discourage imports from countries not granting reciprocal most-favoured-nation treatment. When market economies negotiate with one another for mutual reductions in tariffs, the comparable role of tariffs in each of the various negotiating countries makes it possible for them to reach an equivalence of concessions. Where there are basic differences in trading systems however, reciprocity can be obtained primarily through reciprocal commitments of the trading partners to increase the volume and broaden the range of their imports from one another.

It has been suggested that, in view of the different role of tariffs in the two economic and social systems, consideration should be given to the possibility of reducing internal prices in socialist countries as a counterpart to the lowering of tariffs by private-enterprise countries. This, however, would not bring about the desired result. A lowering of prices in socialist countries would not by itself promote higher imports, as a reduction of tariffs does in private-enterprise countries. The level of imports in socialist countries depends upon the provisions made in the economic plans, which

[2] Economic Commission for Europe, "Preliminary Report of the *Ad Hoc* Group to the 12th Session of the Committee on the Development of Trade" originally released as document TRADE/140 2 October, 1963 issued as Trade Conference document E/CONF.46/PC/47, para. 24 (*b*) Annex A. The group consisted of governmental experts from Czechoslovakia, France, Hungary, Sweden, the Union of Soviet Socialist Republics, the United Kingdom and the United States.

are in turn based upon expected exports. Thus, an increase in exports would be required to permit an expansion of imports, and only then would a lowering of prices have meaning in stimulating the consumption of larger quantities of imported goods. In turn the level of exports depends on the one hand, on the ability of socialist countries to satisfy the requirements of developed countries and, on the other hand, on the willingness of the latter to import from them.

The main objective of socialist countries for many years was to have high rates of growth to a significant extent based on a rapid expansion of heavy industry which would enable them to attain the living standards of the western countries. In so doing, they gave a higher priority to imports of machinery and equipment in general, mainly from the developed countries, than to imports of consumer goods or products such as tropical beverages which they regard as being in the category of luxuries or which did not form part of their normal pattern of consumption.

More recently, imports of foodstuffs, raw materials and finished goods for personal consumption have been rising significantly. But the amount of foreign exchange available for such imports is still necessarily limited by the total volume of resources that can be obtained from the marketing of their exports abroad. If they were able to export more, whether to developed or to developing countries, it would be easier for them to import larger quantities of the primary commodities and finished manufactures which at present have a relatively low priority in their import programmes.

3. Prospects of increasing trade with developing countries

What are the concrete prospects for a substantial expansion of the trade of developing countries with socialist countries?

The future trade of the socialist countries cannot be regarded merely as a projection of the past. While the current plans of these countries are based on economic and political assumptions related to the experience of past years, a change in these assumptions might mean an improvement in the prospects for trade of the developing countries with the socialist world, to an extent greater than present plans might indicate. For example, one of the most important questions for the socialist countries in planning ahead is whether they will always have access to external supplies of commodities for their economies and whether it will be possible to market their exports in the expected quantities without risks other than the usual commercial ones.

For the time being, estimates of the possibilities for trade can only be based on such plans as exist at present. The prospects for trade, as set out in the plans of the socialist countries, vary greatly according to the products. In the case of agricultural products of the temperate zones, for instance, there would appear to be a definite effort on the part of the socialist countries to increase production to the maximum in order to meet the demands of population growth and of rising levels of living. In view of these intentions, long-term prospects for the import of temperate products may become unfavourable with the passage of time, although they may improve sporadically. Nevertheless the possibility should not be overlooked that in the socialist countries, just as in the private-enterprise economies, some proportion of the increment in domestic demand could be supplied from imports. Even if that proportion was very small, it could represent quantities of appreciable magnitudes for the primary exporting countries. The opportunities for opening up markets for exports of primary commodities along these lines would therefore be worth exploring, especially if the drive to increase production in the socialist countries stops short of utilizing high-cost marginal land.

The same thing could be said as regards raw materials for industry, the market for which may be of importance to developing countries in the years to come if measures are taken by the socialist countries to assure an adequate participation of imports in total consumption within the framework of reciprocal trade and if, furthermore, they could have reasonable assurance of regular access to the sources of supply.

The growing consumption potential of the socialist countries offers a favourable market outlook for tropical foodstuffs and beverages. Should the per capita consumption of these products reach, by 1980, the levels prevailing in the richer private-enterprise economies today, imports might amount to very sizable figures. On certain assumptions along these lines it has been estimated that imports of these commodities by CMEA countries, which were valued at scarcely $130 million in 1961, might reach some $3 billion by 1980.

Similarly, the possibilities for imports of manufactures from developing countries might be very great, since higher incomes are reflected in an ever greater demand for industrial consumer goods; if this demand is to be translated into higher imports, it would be essential for the socialist countries to introduce a suitable division of labour in this field. Such a trend has already begun to manifest itself in the case of industrial imports, thus far originating principally in India and the United Arab Republic, among the developing countries.

It would be highly desirable if socialist countries could indicate their long-term import targets of primary products, as well as of industrial goods, coming from developing countries. This could play an important role in the export plans of developing countries as well as in their plans to reduce their trade gap.

If all these possibilities are to be realized, the developing countries will have to provide for corresponding increases in their imports from the socialist countries. The socialist countries have expressed their willingness to supply an increasing amount of the capital goods needed for development, although there are differences between them in the extent to which they have experience and knowledge of markets in developing countries. Some socialist countries have already gained such experience, which has enabled them to promote an active export trade in machinery and equipment; for other countries, on the other hand, this is a relatively new problem calling for considerable efforts in the way of organization and of adaptation to the conditions and requirements of the developing countries.

The fear is sometimes voiced that if the possibilities of trade between the socialist countries and the developing countries were to be realized, the economy of some of the smaller countries might become unduly dependent on the purchasing power of bigger countries: a danger which may be all the greater if that purchasing power is exercised through decisions of State organs or of large commercial firms. The fact is that exclusive or preponderant dependence on a single purchasing market in any part of the world has serious drawbacks, of a magnitude in inverse ratio to the size of the exporting country. That is one of the chief reasons for diversifying not only the products exported but the destination of those exports. It is to be hoped that such situations will be avoided by a well-balanced development of trade among all countries.

4. Bilateral agreements and their significance

Any assessment of the possibilities for rapid development of trade between the socialist countries and the developing countries must take into account the disadvantages arising from bilateralism in trade. They are well recognized. However, while conditions are not yet fully favourable to the universal application of the multilateral trade system, as would be highly desirable, bilateral agreements are useful in so far as they serve as an instrument for promoting additional exports and correlatively additional imports.[3]

It would be a serious step away from the universal application of the multilateral system if bilateral trade were to spread to areas in which trade now takes place on a multilateral basis. But the present case is quite different, since the idea is to open up new channels of trade through bilateral agreements rather than to move backwards from a multilateral to a bilateral system.

Bilateral agreements may be entered into for long as well as for short periods of time. Long-term agreements may provide for a steady growth of trade over a number of years by setting targets for mutual trade expansion, both over-all and for particular products. Such agreements may thus provide a basis for the planning of expanded production for export.

It is important to distinguish bilateralism in these conditions from that which was characteristic of the great world depression of the 1930's. At that time there was recourse to such trading arrangements in order to

[3] In their approach to bilateral trade the socialist countries usually offer bilateral payments arrangements in terms of the currencies of the respective developing countries. Any deficits or surpluses arising from the agreements in any period are settled through commodity deliveries in the required amounts during a subsequent period. Trade in both directions is carried out generally at world market prices.

protect exports against the disastrous restrictions which threatened them in the circumstances then prevailing. Faced with the imperative necessity of restricting imports, countries engaging in bilateral trading arrangements sought to shift their imports towards countries that were buying their exports in equivalent amounts even if prices were higher than in other sources of supply.

Bilateral agreements were then an instrument of trade diversion rather than trade expansion. The current question of bilateral agreements with the socialist countries is different, since they can be used for the fundamental purpose of generating additional flows of trade through bilateral channels which would otherwise not take place at all. Thus bilateral agreements can be used as instruments for trade expansion, provided that instead of diverting trade they stimulate additional trade and that the transactions follow international prices.

It should therefore be possible for the developing countries to maintain and increase their traditional trade to the extent permitted by the access granted them by the private-enterprise countries while, at the same time, expanding their trade with the socialist countries.

The ultimate goal should be the extension of multilateralism to the whole of world trade. On that basis a form of bilateral agreement consistent with multilateralism can be envisaged. It would be possible, for example, to conclude agreements specifying the commodities which the countries in question seek to import and export without trying to establish any rigid balance of trade by pairs of countries.

The socialist countries, as has already been stated, employ long-term contracts in their import and export trade. In some of the private-enterprise countries the advantages that may be secured by this means have recently won recognition. For example, one of the main conclusions and recommendations of the trade mission from the Birmingham and London Chambers of Commerce that visited the Soviet Union in May 1963 was that:

> "The fact that the Soviet Ministry of Foreign Trade is prepared to talk about five-year contracts both for buying and selling is a very important and significant step. British industry should be ready to take full advantage of it. It could now be possible for particular branches of industry to plan production ahead and even to expand facilities to accommodate Soviet orders."[4]

In other words, long-term contracts[5] arranged under bilateral agreements may provide a firm basis for industrial planning in private-enterprise and socialist countries alike.

Short-term bilateral agreements are employed by socialist countries

[4] *Trade Prospects in the USSR: a survey for businessmen,* report of the Birmingham and London Chambers of Commerce, May 1963, page 18.

[5] Moreover, it should be recalled that France and the United Kingdom have been operating this system for some time with countries with which they have special links.

as well as by some developing countries. Where a country experiences difficulty in selling abroad, whether because of market weakness in particular products, over-valued exchange rates, discrimination by other countries, or other factors, bilateral agreements may offer a means of assuring export sales. What happens, in effect, is that the country concerned uses its import buying power as a means of selling its exports through bilateral channels. Although most of the trade of the socialist countries, both with one another and with the rest of the world, is based upon a system of bilateral agreements, a bilaterally balanced basis of trade is also sought by some private-enterprise economies as well, in their exchanges with socialist countries. In this connexion reference has been made to the case of developed countries which insist on a bilateral balance in their transactions with socialist countries so as to obtain additional outlets for export products encountering difficulties in other markets.

5. Possibilities of multilateral trade

There can be no question that multilateral trade has notable advantages over bilateral trade and that everything possible should be done to expand its scope until bilateral trade has been eliminated. This, however, is not a matter of simply applying a formula but primarily of creating conditions favourable to the development of multilateral transactions.

It would be appropriate in this connexion to recall that the socialist countries have stated repeatedly that the bilateral trade in which they were engaging had been the outcome of circumstances and that progress could be made in the direction of multilateral trade if these circumstances became favourable. There is in fact no reason why planning should be incompatible with multilateralism. Under suitable conditions, it should be just as possible to plan for multilaterally balanced trade as for bilateral balance.

A movement in this direction has already begun in the CMEA countries with the recent establishment of a multilateral payments system among them. It is to be hoped that this system may be gradually extended to the rest of the world,thus giving a considerable impetus to international trade.

The factors which tend to encourage bilateralism in trade rather than multilateralism may be much more a matter of the volume and composition of trade than of the particular economic system under which it is conducted. A low level of trade is certainly not conducive to multilateralism. In general, the larger the volume of trade, the number of participating countries, and the variety of products, the greater would be the possibilities for multilateral compensation. For this reason and because of the considerations referred to above, it appears that a necessary condition for the attainment of the multilateral goal by the socialist countries would be a widening of the orbit of their trade with the rest of the world, both developed and developing. Multilateral trade, in its turn, will reinforce this trade expansion.

Chapter V

THE INSTITUTIONAL MACHINERY OF WORLD TRADE AND DEVELOPMENT

1. Defects in the existing machinery and the need to correct them

After this discussion of a series of possible international trade and financial measures aimed at eliminating the potential trade gap, it is necessary to ask whether or not the existing institutional machinery is adequate for the systematic implementation of these measures, for modifying them or adopting other new ones, in accordance with changing practical requirements, and finally for implementing the policy within which all these measures should be incorporated.

The arguments generally advanced concerning the existing machinery are the following:

First, GATT is far from being universal, because it has sixty-one full members and thirteen associate members,[1] whereas the number of States Members of the United Nations and members of the specialized agencies which have been invited to participate in this Conference is 122.

Secondly, the problems of international trade are dealt with in a fragmentary fashion and not as part of a general problem of development which must be tackled on various fronts and with clearly defined objectives.

Thirdly, although GATT has clearly shown itself to be a suitable instrument for dealing with trade problems among the industrial countries, it has not proved equally effective in coping with trade between the developing countries and the industrial countries nor has it promoted trade relations among the developing countries themselves. This explains why many of the developing countries have been reluctant to join GATT.

Fourthly, GATT was conceived as an instrument for expanding international trade by means of the tariff system; trade between Governments was regarded as an exception. The result has been that the Soviet Union and several other socialist countries that regulate their trade mainly through bilateral import and export agreements have remained outside the scope of this institution. It should be noted in this connexion that since the end of the Second World War, trade through official agencies has reached considerable proportions in a number of non-socialist countries as well.

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[1] Including countries which are provisional members and others participating in various ways in its activities and operations.

Fifthly, the agreements and other activities relating to primary commodities are negotiated largely outside GATT and are not subject to co-ordinated action.

This situation has led to the suggestion that a new international trade organization free of such shortcomings should be established as the body responsible for carrying out the policy emerging from this Conference and from similar successive periodic conferences.

This last point is basic, because it is only by deciding to agree on this new policy that such an institutional reorganization would make sense. It is equally true, however, that the reorganization itself, if properly carried out, could facilitate the formulation of this policy, since it will not be a single brief operation but rather a long-term association with the serious problems facing the world in these matters. Furthermore, an intellectually independent secretariat with the authority and ability to submit proposals to Governments within the framework of the United Nations could help in formulating this policy and seeing that it is carried out correctly.

The conviction has grown that some kind of new trade organization is needed in one form or another. If it gains further ground at this Conference we should take important decisions here and decide whether this objective is to be achieved by immediately establishing a new organization with all the necessary powers or by proceeding gradually and by stages, making use of the experience acquired in the process.

2. Utilization of existing facilities

As far as the latter course is concerned, there already exists a valuable group of facilities which could be utilized in a regular and systematic manner by making whatever additions or modifications are necessary and giving unity and coherence to what is now fragmentary and scattered. Various ideas could then be combined in this connexion. They will now be considered.

How could the existing facilities be used to remedy the defects mentioned in the institutional machinery in such a way as to lead eventually to a new trade organization?

3. The periodic conferences

It may not be fully realized that an effort to remedy the first two defects was begun by the United Nations some time ago. This effort, although still insufficient, could now be stepped up and carried out organically and in ways that would correspond more closely to the aims in view.

The United Nations, because of the wide range of its membership, has in fact provided Member States, and especially the developing countries, with a broader institutional framework than GATT has so far offered.

While it is true that GATT, because of its very nature, has discussed trade problems as such, it is also true that, in the United Nations, consideration of such problems has always been an integral part of the periodic discussions on economic development. Such has been the case in the regional economic commissions, the Economic and Social Council and its subsidiary organs, the General Assembly and in the Secretariat's reports to these bodies.

It may be said without exaggeration that it was at these periodic meetings that many of the highly important matters which this Conference is to consider were initially broached. It was there that emphasis was first laid on the tendency towards persistent external imbalance and its structural significance. The same could be said with regard to the terms of trade and compensatory financing. It was also in the United Nations that there originally emerged the concept of structural inequality between countries and the need for a policy to remedy the serious consequences of the disparities in international demand and that opposition to the conventional idea of reciprocity was originally expressed. It was in the United Nations organs that the need for a policy for the industrialization of the periphery of the world economy was first unequivocally recognized. The movement towards the establishment of regional groupings of developing countries was likewise given a strong impetus in the world Organization. Finally, the need to plan development and the role of trade in development was strongly emphasized in the United Nations.

Furthermore, the Secretariat has concerned itself with all these topics on a continuing basis. Indeed, without such concern, it would have been unable to submit to the Preparatory Committee or this Conference all the reports requested of it at such short notice.

Undoubtedly, therefore, the United Nations is capable of assuming much greater responsibilities in these fields.

Continuing even further along this path, an organizational scheme could be outlined, based on the holding of periodic conferences similar to the present one, where the problems of international trade would be discussed as an integral part of the general problem of development. At the same time, international payments and development financing would have to be approached, not as isolated matters, for there are agencies concerned specifically with them, but as part of a closely integrated whole. The approach must be both global and, at the same time, universal, for these matters cannot be broken down by geographical areas or by groups of countries belonging to different economic and social systems.

Such a review would lead to the formulation of an over-all policy that would have to be continually revised in the light of experience. For this purpose, it is considered desirable to organize, in addition to the periodic conferences, a standing committee which would fulfil this continuing function of examination and revision, with a view to submitting suggestions or recommendations to the conferences or to Governments, depending on the nature or urgency of the matters involved. It would act as a preparatory committee for the said conferences and might have a similar, although not identical, geographical composition, so as to enable States which are members of the specialized agencies but not of the United

Nations to participate. Some of these countries play a very important role in world trade.

4. Principal tasks of the standing committee

In that task of examination the standing committee would have to consider a number of important aspects:

(*a*) The potential trade gap and the way in which the import targets are being met, as also financial and other measures which may have been taken to cover it;

(*b*) The steps taken to facilitate the access of primary commodities to the industrial countries;

(*c*) The development of preferential policy in those countries with respect to imports of manufactured goods from the developing countries;

(*d*) The preparation, concerting and implementation of commodity agreements;

(*e*) The functioning of the compensatory financing system;

(*f*) Trade between socialist countries and other countries as an integral part of world trade; and the attainment of targets set for imports from the developing countries;

(*g*) The formation and functioning of preferential groupings of developing countries and the progress of import-substitution policy in such groupings.

In this review on the implementation of such a policy, with a view to preparing recommendations for the periodic conferences or submitting them to Governments through the appropriate channels, the standing committee and, of course, the conferences should count on the co-operation of GATT and United Nations specialized agencies.

GATT, without prejudice to its independence, could give very valuable help, particularly with respect to all matters concerning tariff policy and the application of the preferential system.

The United Nations Commission on International Commodity Trade (CICT) and the Interim Co-ordinating Committee for International Commodity Arrangements (ICCICA), as also FAO, and other bodies currently functioning in this field, could make available the full benefit of their experience in this matter. As has been stated elsewhere, if further progress has not been made along these lines, the fault lies not so much in a lack of institutional machinery but in the lack of a clear and energetic policy. If such a policy is formulated, the standing committee and the conferences should provide the necessary impetus so that this machinery may be set in motion in an efficient and co-ordinated manner.

The Committee for Industrial Development, with the help of the Centre for industrial Development, will have a very important role to play, particularly with respect to all matters concerning industrial exports.

International financial institutions could co-operate in the matter of compensatory financing and other financial measures designed to correct external imbalance.

As far as trade between the socialist countries and the rest of the world is concerned, the Committee on the Development of Trade of the Economic Commission for Europe has already made a significant contribution to the examination of relations between the socialist countries and the private-enterprise industrial countries and ways of improving them. It should be remembered that non-European countries may attend its meetings as observers.

If the idea of the conferences and the standing committee is accepted, practical arrangements should be made to avoid, as far as possible, any unnecessary overlapping of functions, so that the discussions in these bodies would not be unnecessarily repeated in other United Nations bodies or in GATT. Apart from its intrinsic disadvantages, this overlapping would unnecessarily take up the time of governmental representatives and might thus lead to a situation in which participants in the conferences and in the standing committee might not always be of the appropriate level.

Again, once the policy emerging from this Conference is formulated, it would be possible to study the readjustments to be made in existing machinery so as to give them a structural cohesion that would make them respond efficiently to that policy. That would also be the time to decide whether or not interim or permanent auxiliary bodies will be needed for the analysis of special matters and for the implementation of the measures specifically embodying that policy.

5. The regional economic commissions as basic organs of the conferences

The co-operation of the United Nations regional economic commissions should be enlisted as a means of facilitating the work of the conferences and the standing committee. The part played by these commissions and their trade committees and by the studies of their secretariats in considering the problems of trade and development is fully recognized. It would therefore be advisable to establish a clear organic link between the conferences and the regional economic commissions. The commissions, with the co-operation of their secretariats, could be given the responsibility of examining and discussing the problems of their member countries, current trends in the potential gap, the obstacles impeding the implementation of the policy agreed to, and the relationship between this policy and internal development policy. The regional commissions would thus carry out the primary function of the conferences. Their periodic reports would contain an analysis of the chief problems of each region in connexion with the matters of interest to the conferences and whatever relevant recommendations the Governments might see fit to make. The performance of this primary function would not only be valuable in itself but would also make it easier for the conferences to avoid spending time on details and to concentrate on those problems that call for more general solutions.

Part Three

REALISM AND RENOVATION

A. EXTERNAL BOTTLENECKS OBSTRUCTING DEVELOPMENT

There is one dominant note in this report. On the international economic scene we are faced with new problems, new in kind, in some cases, and new because of the magnitude they have acquired, in others. We therefore need different attitudes from those prevailing in the past, and these attitudes should converge towards a new trade policy for economic development.

The problems that beset the developing countries are very grave indeed. They have to assimilate modern techniques swiftly in order to raise their levels of living. But new techniques, while they bring enormous advantages with them, are fraught with dangerous consequences, because we have not yet learnt fully to control the forces of development in a rational way.

The direct and indirect effects of technological progress are responsible for the fact that world demand for primary commodities is growing so slowly, to the detriment of the developing countries. The effects of the protectionism prevailing in the industrial countries are an added factor. Even though access to the markets of the latter countries is facilitated, the primary production of the developing countries should adjust to this slow tempo of demand, but structural difficulties prevent it from doing so to the extent necessary to prevent primary commodity prices from deteriorating in relation to those of manufactures. The further modern techniques permeate primary production, the stronger may be the tendency towards such a deterioration. Action by Governments is therefore imperative to deal with this paradox of development.

Such action is also essential for rapid industrialization to become the dynamic factor in the development of the world periphery, just as primary exports were the dynamic factor in the development of the world periphery in former times. But in those days development had no social depth. Today it must. This makes the problem of development more complex and pressing.

The circumstances in which industrialization must proceed are, moreover, very adverse. The developing countries are still suffering the consequences of the disintegration of the world economy that followed upon the great calamity of the 1930's. They do not export industrial goods, except in very small quantities. Since their primary commodity exports are growing so slowly and their terms of trade tend to deteriorate, they lack the resources necessary to import, on an adequate scale, the goods required for a satisfactory rate of development.

These imports are mostly industrial goods, and only part of them have been or could be produced domestically on an economic basis owing to the smallness of national markets. They must export in order to enlarge these markets. But it is usually difficult to increase exports because costs are high, and costs are high because of the difficulty of realizing economies of scale in the absence of exports. Here too a policy is needed, action by Governments to break this vicious circle by providing reasonable access to the markets of the industrial countries for manufactures from the developing countries, and a decided effort to promote the exports of such manufactures.

The developing countries should also form their own groupings in order to plan and develop their industries in wider markets. In some cases they have only just embarked on this policy and they should be given firm international support in the technical and financial fields, within a more favourable institutional framework than now exists. Such co-operation is needed to help import substitution within the groupings with respect not only to goods but also to services, since maritime transport and insurance, for example, represent very substantial external payments.

Among the growing imports necessary for development, capital goods stand out prominently. Such imports have been financed in part by international financial resources. But, in addition to being inadequate, these resources present a further problem. The burden of servicing them grows heavier and heavier, and in some cases the situation is becoming very critical, again because the exports which must provide the necessary funds for servicing are expanding very slowly and losing their purchasing power, while the demand for imports continues to grow.

All these factors that are so unfavourable to the developing countries converge in the persistent trend towards external imbalance that stifles economic development. As was seen at the beginning of this report, it has been estimated that the potential trade gap in goods and services will amount to some $20 billion by the last year of this decade if the present course of events continues unchecked. This is a staggering figure from the standpoint of the developing countries, but not from that of the industrial countries, since the amount by which the former would have to increase their exports of primary commodities and manufactures in order to bridge this gap, to the extent that it is not covered by international financial resources, represents only an insignificant fraction of the latter's consumption.

The problem must therefore be cut down to its proper size. The remarkable development of the industrial countries has given them a high foreign trade potential. Everything depends on ensuring that part of this potential is translated into practical measures that would bring about a significant increase in imports from the developing countries.

B. THE POTENTIAL OF THE MAJOR INDUSTRIAL COUNTRIES IN RELATION TO DEVELOPMENT REQUIREMENTS

The immediate aim of a new trade policy is to bridge the potential trade gap. Calculations of this gap may serve as a guide for setting targets in the industrial countries for imports of primary commodities and manufactures from the developing countries. But such calculations are only an approximation of the order of magnitude of the phenomenon and therefore give only a general indication of the extent of the changes that may be needed. They cannot be taken as precise, since they are inevitably based on assumptions about the future that the facts may belie. For example, it has been assumed that the rate of income growth in the industrial private-enterprise countries will be 4.2 per cent *per annum*. This rate may, however, turn out to be higher. If this happens, the demand for imports from the developing countries may be correspondingly greater and thus reduce the magnitude of the potential gap. Would targets that had been set on the assumption of a larger gap then be meaningless? Would they then have to be readjusted?

1. RATES OF GROWTH IN DEVELOPED AND DEVELOPING COUNTRIES

This is not, of course, a question of mere statistical readjustment. It is a matter of much more importance. If the industrial countries succeed in stepping up their rates of growth, this will create favourable conditions for a corresponding acceleration in the developing countries. The potential gap is the external limiting factor and, if it is reduced, it will be less difficult for the developing countries to reach and exceed the rate of growth postulated for the Development Decade. But, at the same time, the inflow of international resources should be increased and this would be more feasible if the industrial countries grew more quickly.

It is therefore a mistake to think that faster growth in the developed countries would necessarily add further to the disparity between their incomes and those of the developing countries. On the contrary, it would create conditions in which the latter would find it easier to overtake the developed countries in their rate of per capita growth, thus gradually lessening the disparity which causes so much anxiety.

Countries that assimilate an existing, although constantly changing, technology can and must attain rates of growth much higher than those recorded by the industrial countries in the past, when this productive technology was taking shape. This helps to explain the high rates of growth of the socialist countries and of Japan and the impressive transformation which those countries have undergone. It also explains the extraordinary growth rates of the countries of western Europe in recent times when they were engaged in modernizing their industrial and agricultural technology, making up for the lag previously created by adverse circumstances. Thanks to the progress thus achieved, all of the countries mentioned have an import potential which could be utilized on a much greater scale than it is now, for their own benefit as well as that of the developing countries.

2. International monetary reserves

This potential is also considerable and could be much greater still in some other important countries that are now experiencing balance-of-payments difficulties which tend to slow down their economic expansion. We cannot ignore the significance of this phenomenon in this report because, as we have already said, the consequences of faster growth in the industrial countries would be of the highest importance for the developing countries.

This balance-of-payments problem actually consists of three distinct, although closely interconnected, problems: the problem of monetary reserves, or strictly speaking, liquidity; the problem of trade policy; and the problem of the world production of gold.

The problem of reserves can be summed up as follows. Whereas from 1950-1962 the value of world imports more than doubled, monetary reserves increased by only 33 per cent. Moreover, the distribution of reserves was very uneven. The shortage, which had hitherto been a feature of the countries of continental western Europe, was remedied at the expense of the reserves of the United States which, for its part, had previously accumulated an excessive share of the world's gold.

The gold reserves of the United States fell from $26 billion at the beginning of 1950 to $17 billion at the end of 1962. In evaluating these totals, account should be taken of the net position of foreign short-term claims upon the United States, which rose from $5.5 billion at the beginning of 1950 to $16.9 billion by the end of 1962.

These developments were the results of an external deficit which, during this thirteen-year period, reached a total of $25.9 billion. The deficit occurred in spite of a large surplus in exports of goods and services. But it so happens that United States loans, investment and grants-in-aid in the rest of the world exceed this export surplus.

The existence in the United States of such a vast quantity of assets belonging to foreign monetary authorities seems to be one of the factors that restrict that country's freedom of action, as regards the measures it can adopt to correct the external imbalance.

Hence emphasis has been laid on restoring liquidity, and solutions are being sought with that purpose in mind. In short, the aim is to add, in one form or another, new resources to those now available in the International Monetary Fund. In certain cases, the thinking goes even further: it is suggested that these operations may be organized in a regular and systematic manner as part of an international mechanism and in a way that relieves the major industrial countries of the burden of holding other countries' monetary reserves and thereby impairing their freedom of action, as mentioned above.

3. The trade and financial policy of the key countries

These solutions are very important from the point of view of international liquidity, but they are not basic solutions to the problem of imbalance, nor do they claim to be. This brings us to the second problem: trade policy. Until recently major countries of western Europe were accumulating large monetary reserves since their loans, investments and grants-in-aid to the rest of the world were less than their trade surpluses. The automatic mechanism has not functioned well or has functioned too slowly.

The basic solution to the problem must be sought both in credit and investment policy and in trade policy. If, in addition to lending and investing more abroad, these countries open their doors wider to imports of primary commodities and industrial products from the developing countries, this would have favourable effects not only for the latter but for the world as a whole in view of the interdependence of world trade. The manpower shortage, which has been a feature of these European countries, could greatly facilitate the implementation of a more liberal trade policy.

It is remarkable that, given such favourable conditions for external payments, one of the most persistent remnants of bilateralism has still not been abandoned: the requirement that resources allocated to the developing countries must be used in the lending country.

4. The dynamic role of gold

Let us now briefly consider the third problem. During the period 1950-1962, visible stocks of gold increased by only 17 per cent while, as has already been said, world trade doubled. Much of the gold produced has gone into private hoards. We are not, of course, saying that there has to be a close link between world trade and monetary reserves, especially if better use could be made of the reserves in solving the problem of liquidity, but there can be no doubt that, if there had been abundant output and less hoarding of gold, the reserves position would be much easier.

Still, this is not the only important aspect of gold; there is another, perhaps even more important from the dynamic point of view. In other days, new production of gold was a significant factor in increasing the demand for exports of goods and services; and this factor has now become weaker. Thus, gold, apart from being the basic element of monetary reserves, has this dynamic role to play. Sometimes it is suggested that gold should be revalued in order to stimulate production and, at the same time, enlarge existing reserves. But the disadvantages of this suggestion are considered to outweigh the advantages. Hence, other solutions must be sought. The possibility is mentioned of creating new international resources on the basis of part of existing reserves, in the same way as central banks create internal resources. These resources would be put at the disposal of existing international credit institutions so they can make loans to the developing countries, in accordance with rules and principles approved by Governments. Similarly, it has also been suggested that other forms of reserves should be used in addition to gold.

The time may have come to examine these aspects in the relevant circles. A wise and constructive solution would be very effective in helping to speed up development, not only because of the direct impact that these additional resources would have on the capacity to import of developing countries, but also because of the impetus that these larger imports would give to the economies of the industrial countries and their rates of growth.

5. Resources from disarmament

When one reflects on the need for additional resources for investment, one's mind naturally goes back to the enormous possibilities for releasing resources that would be opened up by world-wide disarmament. The Declaration, which the United Nations adopted in 1953 and in which the Governments of Member States expressed their intention to devote a portion of those resources to economic development "when sufficient progress has been made in internationally supervised world-wide disarmament", is still in effect.

It has been estimated that annual expenditure on armaments amounts to some $120 billion. In the industrial countries,[1] this represents about 8 to 9 per cent of national income. If 1 per cent of such income became available as a result of disarmament, the allocation of international resources to the developing countries could rise from the present figure of 0.5 per cent of the aggregate income of these industrial countries to 1.5 per cent. This would enable the developing countries, provided an appropriate policy were followed, to raise their annual rate of over-all growth to 7 per cent, instead of the 5 per cent established for the Development Decade. If this were to happen, the average per capita income of western Europe could be matched not in eighty years but in almost half that time.

Furthermore, if part of the resources released by disarmament were used to increase the productive investment of the industrial countries, this would give a greater impetus to their own growth and to the demand for imports from the developing countries and help to accelerate the flow of these imports.

C. THE RESPONSIBILITY OF THE DEVELOPING COUNTRIES

While technological progress in the industrial centres and its gradual spread to the rest of the world creates new problems at the international level, as was stated at the beginning of this part of the report, it also

[1] Including socialist countries.

creates problems in the developing countries and requires new attitudes and gigantic efforts by the latter countries to solve such problems.

The obstacles in the way of this effort are formidable. In many developing countries, however, attention is often centred on the external obstacles; the problems seem more urgent there, perhaps because they are more conspicuous. But it would be dangerous self-deception to imagine that, once these external obstacles are overcome, the way will be wide open for spontaneous economic development.

On the contrary, the determination to overcome these obstacles and exert a conscious and deliberate influence on the forces of economic and social development is also essential. The policy of international co-operation is only complementary; it cannot be a substitute for internal development policy. Nor can the internal policy fulfil its aims without effective and timely international co-operation.

This report would therefore be incomplete if we failed to remember the nature of the main obstacles to be overcome internally. In every country there is a different complex of problems, and the attitudes towards them are also different; the risks implicit in these generalizations should therefore be borne in mind.

1. The internal changes required by development

Generally speaking, there are three main obstacles in the way of propagating technological advances and which therefore obstruct the growth of productivity and per capita income in the developing countries: land tenure; limited social mobility and the ignorance of the masses; and the concentration of income in the hands of relatively small population groups.

The forms of land tenure generally to be found in the developing countries are plainly incompatible with technological progress. This is particularly so, when a large part of the productive land is concentrated in the hands of a few, while a very large number of small and medium-sized holdings generally make up a tiny proportion of the cultivable land. All this conspires to frustrate development; in some cases, because the high rent already received by the landowner makes him reluctant to take the trouble of introducing modern techniques, and, in others, because the very size of the holdings and the shortage of resources for investment are often such that contemporary techniques cannot be fully and properly used.

The ignorance of the masses and limited social mobility are two aspects of the same problem. If up-to-date techniques are to penetrate, there must be opportunities for learning and training and easy access to such opportunities. Conditions must also be favourable for the most able and dynamic people at all social levels to come forward and get ahead. Generally speaking, this happens to a very limited extent only, which means that a vast human potential is wasted, just as the outdated forms of land tenure impede exploitation of the enormous productive potential of the land.

The concentration of income is, of course, linked to these other two features and, in many cases, is aggravated by the serious effects of inflation, a phenomenon usually also influenced by structural factors. It might be thought that this concentration would actively contribute to capital formation, but this is so only in exceptional cases. More commonly, high incomes mean superfluous and excessive consumption by the groups that have them, to the detriment of the investment that technological progress requires on an ever-growing scale.

It would be a serious mistake, however, to imagine that the problem of capital formation could be fundamentally solved in most developing countries, if this savings potential of the high-income groups could be used for investment rather than consumption, and if, at the same time, the flight of capital, which reaches rather significant figures in several developing countries, could be avoided. There is no doubt that all this must be done and that the tax instrument should be used together with other measures for the purpose. But in many countries the problem of capital formation has also to be tackled resolutely with international financial resources, which, by stimulating the rapid growth of income, help to create opportunities for domestic capital formation that are now extremely slight.

The weakness of the development impetus in many of the peripheral countries is a result of all these internal factors that combine in a particular social structure, in addition to the external factors that hamper growth. Development calls for changes in the forms of production and in the economic structure which cannot come about unless a change in the social structure leaves the way open to the forces of technological progress.

Without such changes industrialization cannot run its full course. Generally speaking, industrialization has simply superimposed itself on the existing state of affairs without basically altering it. Furthermore, the excessive protectionism frequently sheltering industries adds a further privilege to those already existing in the distribution of income.

Again, industrial development is constricted not only by the lack of exports but also by the smallness of the internal market. Rural masses working generally in a very unproductive way, urban masses who, to a large extent, take refuge in very low-paid artisan occupations and personal services, or who waste their efforts in antiquated forms of trading —these do not provide a large and lively market for the products of industrial development. And industry itself does not generate, to the extent desired, the income that could create its own strong market; for excessive protectionism and restrictions on imports usually shield it from healthy competition and weaken the incentive to raise productivity and the incomes of the people who work in it through the efficient use of men and machines.

2. Industrialization and Demographic Growth

But the problem is not a simple one. The development of the domestic market through technological improvements in agriculture, better marketing organization, the gradual elimination of artisan occupations, and a gradual decrease in the number of people precariously employed in personal services, will release an enormous potential of workers who will swell the ranks of those who, owing to the high rate of population growth, have to be incorporated in the economy each year. It is the extremely important dynamic function of industry and other activities which thrive with it to absorb this human potential at a satisfactory level of productivity. If they are to fulfil this absorptive function effectively, all these activities must forge ahead all the faster as modern techniques penetrate to those strata of the population which are technologically so conspicuously backward.

The nature of this question should be stressed here, for it is still asserted sometimes that the solution of the development problem is to be sought in the domestic market and not in the expansion of exports.

The fact is that the development of the domestic market and the promotion of exports are not two alternative or mutually exclusive propositions. The two processes must take place simultaneously and in a co-ordinated manner. The penetration of modern techniques to the submerged strata of the population is an inevitable prerequisite for accelerating growth. If this acceleration is to be achieved, the persistent trend towards external imbalance must be overcome through the expansion of exports and other measures of international economic co-operation.

This dynamic role of industry and other activities in the absorption of the human potential is a key element in the process of development. In most cases, this role is not being played well. For example, in Latin America the minimum rate of per capita income growth of 2.5 per cent a year, laid down as a target in the Punta del Este Charter, would not be sufficient to bring about this absorption under the present conditions in which modern techniques are penetrating rather slowly. If the penetration could be speeded up, it would become even more imperative to expedite growth and industrialization.

Naturally, when the subject of accelerating development is broached, the question is often asked whether the developing countries could not themselves attain this objective by lowering their rates of demographic growth.

There would seem, however, to be very little prospect of achieving such a reduction in the next decade. Historically, the decline in the birth rate has been a consequence of industrialization and of improvement in the level of living, and this process has been very gradual. On the other hand, it is difficult to envisage the possibility of bringing about a sharp reduction in the birth rate quickly by a conscious and deliberate policy. It has been pointed out more than once that, even where religious considerations do not affect the implementation of such a policy, it would encounter formidable social, educational and economic difficulties. The success that might be achieved is therefore very uncertain. Actually, with the leeway which the developing countries still have to make up in order to reduce their death rates, and with persons of marriageable age forming an increasing proportion of their populations, the rate of demographic growth appears more likely to rise than to fall in the immediate future.

Be that as it may, reducing the rate of population growth cannot in any sense be an alternative to the vigorous development policy advocated in this report. It could not be a method of evading or slackening the effort which this policy necessarily entails; on the contrary, it would be a means of deriving more far-reaching and effective results from such a policy.

3. Development planning and international co-operation

All these considerations give us some idea of the nature and complexity of the changes which development demands. Furthermore, these changes call for a great effort to mobilize resources which, like the changes themselves, need to be given a definite direction and clear economic and social objectives. Hence the need for development planning.

Planning is something more than a new technique superimposed on the framework of public administration, which is usually so defective in the developing countries. Here again, basic changes are required both in thinking and in action, and such changes are far from easy to make.

Among the major obstacles in the way of planning mention must be made of those of an external nature. Persistent fluctuations and the trend of the terms of trade to worsen, added to the slow growth of exports, have been very adverse factors hindering regular economic development and hence the task of planning. It is very difficult to plan, set targets and quantify resources when the effectiveness of such action largely depends on external factors beyond a country's control.

If the whole situation could be corrected in a reasonable manner by means of an enlightened policy of international co-operation, the peripheral countries would be better able to fulfil their responsibility in the dynamics of development. This responsibility, far from decreasing, would then be greater than ever, for, if external conditions took a favourable turn, there would be no justification for any slackening or hesitation in the internal effort to expedite development.

All this calls for major political decisions, but these decisions cannot come from outside. Nor can agrarian and educational reform, tax reform, and, in short, the various measures aimed at effecting structural changes, be a matter for international negotiation as a counterpart of financial co-operation. They must spring from each country's deepest conviction and from its genuine determination to bring about such changes. What is needed from the outside world, however, is a large measure of understanding and support.

That is certainly not the meaning of those not infrequent admonitions to put one's house in order so that development can come about spontaneously. Maybe they are a remembrance of bygone days. In those days putting one's house in order was enough, given the resultant influx of foreign private capital and the expansion of exports, to enable the peripheral countries effectively to fulfil their function as producers of foodstuffs and raw materials for the industrial centres.

Today the phenomenon of development is very different and its requirements are usually not compatible with that order of things. It is true that one's house must be put in order, but in a different order from that sometimes visualized in these admonitory attitudes. These attitudes cannot be allowed to guide the policy of international co-operation. This policy must be imbued with the same deep sense of renovation as the internal policy of economic and social development, since it is its indispensable complement.

In all of this there is a clear convergence of responsibilities, internally as well as internationally. The controversy about whether internal ills are caused by external factors or whether the source of these ills should be sought exclusively in the behaviour of the country concerned has been rendered obsolete by events and is meaningless now. There are both internal and external factors to be attacked simultaneously. To emphasize the former and exclude the latter, or *vice versa,* would be an aimless exercise and only divert our attention from the real solutions.

D. THE CONCERTING OF TRADE MEASURES

These solutions cannot be adopted in isolation, since they form an integral part of a more comprehensive policy of international co-operation for economic development. Solutions of this kind have been outlined in part Two of this report, as a basis for discussion rather than as final proposals. It may be helpful for us to recapitulate them briefly here.

1. Import targets

With regard to primary commodities and industrial goods produced by the developing countries, it is advocated that *quantitative targets* should be set for their entry into the industrial countries' markets, to be reached within a certain number of years.

The import targets for *primary commodities* could be, depending on the individual case, quantities of specific commodities or groups of commodities, or desired proportions of the consumption, or of the increase in consumption, of each importing country.

The targets for *industrial goods* could be expressed for each importing country in terms of a *global value* covering the quota of imports of manufactures enjoying preferences and the minimum target of imports not subject to preferences that should be attained in order to help eliminate the trade gap.

Cases of *injury to domestic producers* resulting from exceptional increases in imports from developing countries should be dealt with under the normal procedures laid down by GATT.

2. INDUSTRIAL PREFERENCES

Within the aforesaid global value, the industrial countries could establish a quota for admitting manufactured goods from the developing countries *free of duty*, but they could *exclude from these preferences* a schedule of items constituting a reasonable percentage of the total goods they import. This exclusion could take effect from the outset or during the operation of the system, in accordance with criteria to be laid down.

Manufactures from developing countries thus excluded from the scope of preferences would be admitted by the industrial countries on the usual most-favoured-nation basis.

All the develoipng countries, irrespective of their level of development, would be eligible to avail themselves of the *preferential system* up to the amount of the relevant quota. But there would have to be a periodic review of the flow of exports; and if exports from one or more countries increased so much that they did not leave sufficient room for those from the others, equitable solutions should be sought.

Special preferences could be granted to the less advanced developing countries. For this purpose, the list of items excluded by the industrial countries from the preferential system applied to all developing countries should be used.

The preference would *remain in force for ten years* from the time when each industry in a given country started to export. But this period could be extended in accordance with internationally agreed procedures, if an *exception to the rule* was fully justified.

3. EXISTING PREFERENCES

The ultimate objective should be to adapt existing preferential arrangements to the new system of preferences in such a way that there is *no discrimination among developing countries*, and so that developing countries presently obtaining such preferences should continue receiving *benefits* under the new system at least *equivalent* to those they now enjoy. The precise way in which this ultimate objective might be secured is a matter for further discussion but it should include, in particular, international technical and financial assistance to countries at the earliest stage of economic development.

In any case, preferences granted by developing to industrial countries should cease.

4. Nature of the targets

The targets are an expression of the *objectives to be reached;* thus they are of an indicative character and, generally speaking, do not constitute commitments to import. But the targets for primary commodities, in addition to representing quotas of goods to be imported without restrictions, might constitute *commitments to purchase* over a number of years.

When the targets are set, Governments would pledge to take all necessary action to reach them, including *promotional measures in the technical, trade and financial fields.*

In the socialist countries, the targets would also be of an *indicative character,* but they should be translated into long-term commitments to import under the system of bilateral agreements.

5. Commodity agreements

Two converging kinds of measures are envisaged to *guarantee the purchasing power of exports* of primary commodities: commodity agreements and compensatory financing.

Commodity agreements can be used to establish minimum prices or improve prices, as the case may be, by maintaining their parity with those of manufactures, when the price improvement does not *substantially affect* consumption by reducing it or by giving synthetics and substitutes a competitive advantage.

Commodity agreements should establish whatever system of *export quotas* may be necessary to support the price policy.

When internal prices are higher in the industrial countries than on the international market, the adverse effects on consumption could be avoided if the raising of prices was accompanied by an *equivalent lowering of tariffs or internal taxes* where such exist.

In the case of *tropical commodities,* the internal taxes should be lowered still more until they are completely eliminated, so as to encourage consumption.

As regards competition from *synthetics and substitutes,* there might be cases in which it is advisable to *increase productivity and lower the costs and prices* of some natural commodities, provided that the loss of income thus suffered by the exporting countries is offset through compensatory financing.

Whenever the temporary shortage of a primary commodity leads to price rises that adversely affect producers and consumers, *ceiling prices* should set set. The agreements should also lay down rules for the disposal of surpluses and non-commercial stocks.

The scope of commodity agreements, or of corresponding intergovernmental action, should be considerably extended and conditions should be laid down for access to the markets of the industrial countries through *import quotas* and *import commitments*, where feasible; in addition, provision should be made for the gradual lowering of *support prices* and arrangements made for co-ordinating the internal and external production policy of the importing and exporting countries. The purpose of all these steps is to ensure that the latter obtain a reasonable share in the growth of consumption of the former.

6. Compensatory financing

Compensatory financing is imperative to the extent that it may not be possible, through commodity agreements, to prevent the exporting countries from suffering losses owing to deterioration in the terms of trade.

Two kinds of losses would have to be compensated *henceforth:* those due to *the previous deterioration in the terms of trade* and those resulting from *future deteriorations*.

The *amount of compensation* to be received by each exporting country would be determined after consideration of the effect that the deterioration has had on its investment resources and balance of payments, so that the country can receive whatever additional resources it needs to continue *its economic development plan* without disturbances.

These *additional resources* should not be transferred directly to producers, except where this is essential to ensure the normal development of production.

Each country should take whatever internal action it sees fit to obtain resources for *compensatory financing*. But it should not do so through taxes which, by raising prices for the consumer, *discourage consumption or encourage the replacement* of natural commodity by substitutes or synthetics.

The compensatory resources might form part of a fund administered by *international credit institutions*, at either the international or the regional level, in accordance with rules approved by Governments.

The required resources might also be made available to developing countries by national and international agencies acting through consortia or by other suitable co-operative arrangements.

In either case, the relevant decisions might be based on an independent finding by an *international team of independent experts* of the highest standing that a particular country's economic development was being prejudiced by terms-of-trade losses.

7. Readjustment of the external debt

Consideration should be given to the *readjustment of repayment periods* and terms of the *external debt* of some countries. External financing could facilitate this operation. Steps should also be taken to avoid the subsequent recurrence of critical situations resulting from excessive increases in the burden of servicing.

8. Maritime transport and insurance

The possibility should be examined of developing merchant marines and insurance operations within regional groupings of developing countries or of promoting among them specialization in the miscellaneous activities that constitute these services.

The system of shipping conferences and the impact of their agreements on the developing countries should also be examined.

9. Groupings of developing countries

The developing countries should pursue their industrialization policies and especially their *import substitution* policies and should endeavour to pool their efforts rationally by means of preferential groupings on as large a scale as possible.

These preferential groupings should be supplemented by *payments agreements* between their constituent members.

10. The GATT rules

The GATT rules now in force should be amended to take into account the consequences of the structural inequalities between industrial and developing countries. These amendments should relate in particular to reciprocity with a view to establishing the concept of *implicit reciprocity;* to the *preferences* granted by the industrial countries to the *developing countries;* and to the *preferences granted by developing countries to each other* through groupings of countries.

11. Reduction of excessive tariffs

Without being committed to reciprocity, developing countries with excessive protectionism should undertake *to lower their high tariffs* as they gradually counter the trend towards external imbalance by expanding their exports of primary and industrial products and by import substitution.

12. Differences between the developing countries

In the application of these concerted measures, it is essential to recognize the different situations of the developing countries, depending on the degree of their development, and to adapt and co-ordinate the measures adopted so that the advantages deriving therefrom accrue in particular to the *less advanced of the developing countries* in order to give strong impetus to their growth. In this connexion, not only might the less advanced countries to be given general preferences, shared with the other developing countries irrespective of their degree of development, and special preferences, but they should also receive particular attention so far as the measures for promoting their exports are concerned. They should also be given special attention as regards the allocation of international financial resources; the per capita volume of the resources that these countries obtain should generally be greater than that granted to the more advanced of the developing countries and especially to those of them which may already have improved their ability to generate their own investment resources.

E. NATURE AND ADAPTABILITY OF THE POLICY OF INTERNATIONAL CO-OPERATION

Now that the principal measures proposed in this report have been thus summarized, two important observations should be made.

The first concerns the very nature of the policy which embraces all these measures. It is not simply a matter of lowering or removing barriers which stand in the way of the developing countries' trade and of laying down more appropriate rules than those now in force. What is required is positive action.

This is the significance of the import targets. They are the tangible and practical expression of the responsibility which Governments–both of the industrial and of the developing countries–may decide to assume in order to achieve certain basic foreign trade objectives. And this responsibility would necessarily involve the adoption of whatever measures may be called for, both internal and international.

Thus, should the import targets set be insufficiently high, or prove to be so in practice, the inflow of international finance would have to be increased to cover the trade gap.

This does not mean that import targets and external financial aid are interchangeable concepts. Actually, the quantity of external finance should rather be a supplement to internal investment resources, to compensate for their present scarcity. Under normal circumstances, their direct role should not be to bridge the gap. This has to be done through the expansion of exports. Hence there is no conflict between trade and aid. Each of these has its specific role to play.

Consequently, the extent to which exports and international financial resources have to be co-ordinated is not arbitrary. The proportion of these resources in each country's investment programme must become smaller in the course of time as domestic savings capacity draws strength from the economic development process itself. Exports, on the other hand, must expand continuously in order to cover mounting import requirements and pay for servicing the external debt.

All this points to desirability of periodically examining the way in which those objectives are being achieved, not as ends in themselves but as means which, in combination with others, would make it possible to reach a bigger target, the growth target set for the United Nations Development Decade and the more satisfactory targets which may be established later.

The second observation concerns the flexibility with which this policy must be carried out. The developing countries have certain very important common denominators, but there are also great disparities between them, deriving from their different degrees of development and from the particular problems that affect them. Owing to these disparities, the measures advocated here would also have very different effects from country to country. Thus, while access to the manufactured goods markets of the industrial countries is important for all, some developing countries would be able to enjoy the advantages of these measures much earlier than others, unless those opportunities are accompanied by very energetic promotional measures in the countries which would otherwise lag behind. Commodity agreements or compensatory financing would also have a very diverse impact. All of the foregoing emphasizes the need to bear in mind these disparities in degrees of development and in individual situations. The decisive element here could be international technical and financial aid. The intensity of this aid would have to be geared to those disparities so that all the countries could expedite their pace of growth, or maintain it in the few cases where an acceptable tempo has been attained.

This very heterogeneity opens up interesting vistas so far as the dynamics of development is concerned. At one extreme are the countries which are close to a level of income that will enable them, in a relatively short time, to grow at a satisfactory pace with their own resources, but which have to correct the persistent trend towards external imbalance so they can convert part of these resources into imports of capital and other goods needed for their economic development. At the other extreme are the countries which are only beginning to develop, and there the top priority is to obtain international finance, most especially for building up their generally weak economic infrastructure and for basically important social investments. The countries which are at an incipient stage of development may possibly not have to contend with an acute persistent imbalance as do the former, since this imbalance is a consequence of development; but it would be advisable to act now to prevent this from occurring in the future by guiding their development, and particularly their industrialization policy, along rational lines, both by import substitution within groupings of countries and by the promotion of exports of manufactures.

In the course of time, the more advanced of the developing countries should be able to provide a market for exports of manufactures from countries which are embarking on the first stages of industrialization by according them preferential treatment.

In all of this there is no master plan, drawn up once and for all, that is equally applicable to all countries. That is why this policy is necessarily a complex one. Furthermore, it must respond and adapt itself continually to endless changes.

F. NEW PROBLEMS AND NEW ATTITUDES

Such are the issues for which this Conference must seek international solutions in support of internal endeavour. They are solutions which must be embodied in a new policy, not necessarily in response to new ideas—for the ideas presented here are not fundamentally new—but because they demand new attitudes. Will it be possible to bring about these new attitudes? Will the proposals formulated here be realistic? If realism means proposing what is feasible at a given moment, then perhaps not all that is suggested in these pages is realistic; it might be considered an illusion. But what is realistic today was not always so yesterday, and today's illusion may be tomorrow's realism.

Nothing is more significant in this connexion than the way in which ideas have evolved in the short time that has elapsed since the proposal to hold this Coneference was adopted by the United Nations.

Again, reality is made up not just of the tangible facts which we have before us now, but also of the facts still to unfold. Realism is, moreover, the ability to discern what could happen when we do not know how, or do not wish, to take deliberate and timely action to shape the course of events.

The prospects facing the developing countries are grave indeed. Development is turning inwards in the countries that have made more headway in the industrialization process; it is closeting itself more and more in watertight compartments; and the same thing will happen in the others, the less advanced, if they too have to become industrialized within the narrow confines of their national markets. What is more, those countries in general, and the less advanced of them in particular, are not obtaining sufficient financial resources from abroad. These resources are indispensable for breaking that other vicious circle in which incomes are low because investments are inadequate and investments are inadequate because incomes are precarious.

The developing countries must not be forced to cut down the inherently very low consumption of the masses in order to increase capital formation, particularly in view of the impressive magnitude of their aspirations for social betterment. It is no good to preach the need for them to develop by their own efforts and at the same time to limit their possibilities of giving practical expression to that effort in the international field through the expansion of their exports. They must not be forced into a kind of closed development. Hence a broad policy of international co-operation in trade, in financial resources and in the propagation of technology is unavoidable. Without it the economic and social cost of development will be enormous. Closed development leads to compulsion, and usually compulsion involves a political cost fraught with very serious consequences. Realism is also foresight, and an elementary sense of foresight should induce us to read the sign of the times in the developing world.

These pages are therefore an act of faith: an act of faith in the possibility of persuading, of making these ideas sink in where they should sink in, and in the possibility of provoking constructive reactions. The facts are there and cannot be denied. And if the ways of dealing with them proposed here are not acceptable, others will have to be sought which are. For the problem is inescapable. Never before has the world been faced with it in this form and on this scale, nor has it ever had the enormous possibilities that it now has of solving it, or the conviction—which is steadily growing—that it is also feasible consciously and deliberately to influence technical and economic forces in the prosecution of grand designs.

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