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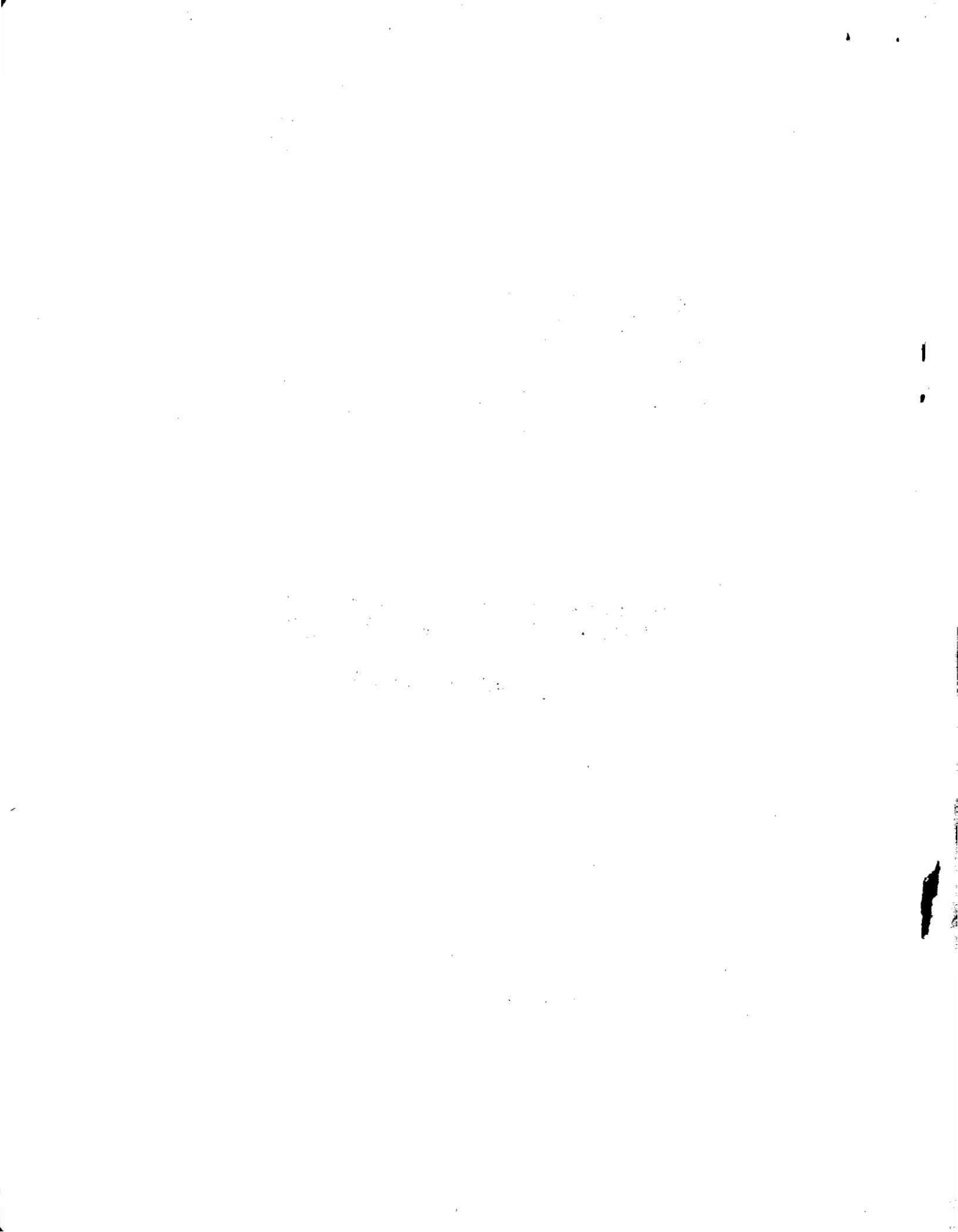
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A LEADING SECTOR STRATEGY AS A COMPLEMENT TO GOVERNMENT  
FISCAL, MONETARY AND EXCHANGE POLICIES

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When I was first asked to prepare a paper for this symposium it was suggested that I stress the use of the market mechanism. I conscientiously attempted to do so but I am afraid that, although I have a great respect for the power of economic incentives and the efficacy of decentralized decision making, I am still a planner at heart. The best I could do, therefore, was to write something on the respective roles of central planning and the market in mixed economies. "The invisible hand" became two hands, the traditional one of economic incentives and the more visible one of national policy making, working in part through the market mechanism. I distrust labels. I do not regard myself as a monetarist, nor a Keynesian nor a believer in intervention nor the market. I am rather a pragmatist who, in seeking to achieve certain goals arising from my personal values, am prepared to use any tool or approach which appears best calculated to improve the functioning of the mixed system in achieving these goals.

/A LEADING

1. The first part of the document discusses the importance of maintaining accurate records of all transactions and activities. It emphasizes that proper record-keeping is essential for ensuring transparency and accountability in financial reporting.

2. The second part of the document outlines the various methods and techniques used to collect and analyze data. It highlights the need for consistent and reliable data collection processes to ensure the validity of the results.

3. The third part of the document describes the different types of data that are collected and analyzed. It includes information on both quantitative and qualitative data, as well as the various sources from which the data is obtained.

4. The fourth part of the document discusses the various statistical methods and techniques used to analyze the data. It covers topics such as descriptive statistics, inferential statistics, and regression analysis.

5. The fifth part of the document discusses the various ways in which the results of the analysis can be presented and interpreted. It includes information on the use of charts, graphs, and tables to present the data in a clear and concise manner.

6. The sixth part of the document discusses the various ways in which the results of the analysis can be used to inform decision-making. It includes information on the use of the results to identify trends, patterns, and areas for improvement.

7. The seventh part of the document discusses the various ways in which the results of the analysis can be used to inform policy-making. It includes information on the use of the results to develop and implement effective policies and programs.

8. The eighth part of the document discusses the various ways in which the results of the analysis can be used to inform research. It includes information on the use of the results to identify new areas for research and to develop new theories and models.

9. The ninth part of the document discusses the various ways in which the results of the analysis can be used to inform practice. It includes information on the use of the results to improve the effectiveness of various programs and services.

10. The tenth part of the document discusses the various ways in which the results of the analysis can be used to inform education. It includes information on the use of the results to develop and implement effective educational programs and policies.

A LEADING SECTOR STRATEGY AS A COMPLEMENT TO  
GOVERNMENT FISCAL, MONETARY AND  
EXCHANGE POLICIES

The basic assumption underlying this paper is that it is still desirable, at least for Latin American developing countries, to set as an objective of policy the threefold goals of high and sustained growth, lessening differences in levels of consumption by a levelling up process, and conditions of relative price stability. Most of the papers in the symposium are concerned with short term government policies in the fields of monetary, fiscal and exchange policies. The task assigned me touches on such policies, but the focus lies more in what action might be taken by the government to work more indirectly through the forces of the market-place in attaining the goals just mentioned.

The Assumptions Underlying Growth

Perhaps the best way of demonstrating the probable necessity of a leading sector strategy is to examine in a little more detail the growth process, as set forth or implied in many writings on the subject. In the most elementary terms, growth results either from an increase in inputs (greater employment and more capital equipment) or a more efficient or intensive use of inputs through improvements in knowledge or from opportunities to make fuller use of specialization or the division of labor through the economies of scale and externalities.

However, we are generally more concerned with growth per capita than with growth in the gross product so that growth arising solely from the addition to the work force is placed in a somewhat different category than per capita growth. Finally, we should strictly be concerned with net rather than gross product per capita, but as it is so difficult to measure depreciation or distinguish between current production on the one hand or exhaustion of a fixed stock on the other, economists feel more comfortable in dealing with gross product, making merely a little obeisance in the direction of the net product.

/Let us

Let us assume, then, that we are relatively successful, through fiscal and other policies, in reducing the part of the working force which is openly unemployed to a few percentage points of the total and that we have achieved relative stability in prices through the exercise of monetary and exchange and other policies. Under such conditions, what can we expect in the way of growth per capita? Clearly the answer must relate to the increase, at constant prices, of the value of output per person. Putting aside, for the moment, exogenous developments in the foreign field, this depends on advances in technology, on the opportunities for greater specialization either in skills or in the additions to capital equipment, (the technology it pays to use), and--an often neglected factor--the degree of mobility of labor that permits a steady shift from lower to higher paying occupations in response to the varying income elasticities of demand and consequent rates of growth in different sectors.

For a country with a near stationary population, the growth process then depends on the replacement of less efficient by more efficient capital, the additions to capital and mobility of labor. I am neglecting, for the moment, exhaustion of national resources or the production of "bads" instead of goods. It is one of the oldest concepts of economics that division of labor, and labor embodied in capital that permits greater specialization, are keys to growth. It is also a very old concept that the division of labor is limited by the market, first set forth by Adam Smith and restated and refined in the famous article by Allyn Young in 1928. The first of the formal growth models expressed in algebraic form, that of Harrod and Domar, marked a return, after the Keynesian affirmation that any increase in spending in conditions of high unemployment would raise both monetary and real income, to the classical position that an increase in "real" capital would result in an increase in output in constant prices. This was followed by countless applications of incremental capital-output ratios in various fields.

/What was

What was rather neglected, however, were the underlying assumptions--the mobility of labor and capital, free competition, the substitutability of labor and capital, and the insatiability of wants (or effective demand for goods in general). Also neglected was the full significance of the limitation on specialization imposed by the size of the market, perhaps because of the implicit assumption that the world was the market, and the basic importance of Say's Law that the deflated value of the output of a person or group is his or its demand for the output of others--a very old concept that was largely ignored in the preoccupation with monetary or Keynesian demand and was relegated to books on the history of theory.

The importance of these assumptions and concepts can best be grasped by considering the consequences of their lack. For example, because of imperfect competition, prices may be raised to meet an increase in demand rather than additional capacity be added. Much more serious, however, may be such a lack of mobility in labor as to create a large, low income sector that has little buying power (i.e. in terms of J. B. Say) for the products of other sectors. This may severely limit the market. With the same population, the internal market in Canada is ten times that of Colombia. The external market, on the other hand, may be limited by restrictions imposed on demand by other Governments or by intense competition from abroad.

In both a Keynesian sense and in a real sense, saving may equal investment. But this does not mean that saving automatically creates investment. Low opportunities for investment and institutional obstacles to its enlargement may result in lower incomes and hence lower saving. In other words, the causal sequence may run from investment to saving rather than vice versa.

In agriculture, superabundant labor may make it uneconomic to use much capital; but the absence of such use contributes to low physical productivity in agriculture and the lack of incentive to improve productivity. The economic history of all countries abounds with illustrations of the importance of the inter-relationship between the size of the market and the extent to which it pays to specialize.

/Writers are

Writers are prone to make a wholly unwarranted identification of the insatiability of wants with the unlimited demand for capital, and an enormous amount has been written on the function of the interest rate in assuring that whatever is saved will be invested. If invested, it is assumed that a yield is obtained, which increases the national product. In other words, a freely moving interest rate has been assigned a leading role in the growth process. Hence the emphasis on "the capital market" and fluidity within that market so that savings may flow freely into the most productive uses. Just as it is the function of price to clear the market, so it is a function of the price of capital--the interest rate--to ensure that all savings are not only invested but are invested in the sectors of highest yield.

The conventional picture of the growth process is a beautiful one of an intricately functioning mechanism. It is a pity that the picture does not correspond to reality. The recognition that the interest rate is the "price" of capital, and the varying accompanying assumptions, mostly implicit, discussed above, led Nurske, in his profoundly influential six lectures on Capital Formation in Underdeveloped Countries (1953), to devote one lecture to an inconclusive discussion of the possible inadequacy of demand (the market) and five lectures to the inadequacy of savings, and this ratio, or even a less favorable one, has since prevailed <sup>1/</sup>. I think I am one of the few that have tried to emphasize the importance of the role of demand. Most of the economists who have paid any attention to my thesis have generally failed to grasp the distinction I draw between Keynesian and Sayian demand and have assumed I was discussing the former, which obviously appears quite irrelevant in a world of chronic inflation. In any case, let me try again.

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<sup>1/</sup> Nichols Kaldor is one of the few authors I know who have mentioned the interaction of supply and demand (in the sense of an offer and a demand for goods) in the dynamic process of growth. See Causes of the Slow Rate of Economic Growth of the United Kingdom, Cambridge, 1966, p. 19.



The Need for Exogenous Action on the Side of Demand

A logical place to begin is with the classical doctrine that the demand for specialized equipment, human or physical, is limited by the size of the market. For most countries, the market is mostly the internal market which, in such terms, is the gross product in real terms. Implicit in Adam Smith's dictum is the assumption that as the market grows, that is, as the gross national product in constant prices grows or more simply as economic growth proceeds, the greater is the opportunity and the incentive to use more capital equipment and specialized skills. Hence, and this is a rather crucial point for my argument, there is an intimate relationship between the overall rate of growth and the sector rates. While the overall rate is the sum of the sector rates, the sector rates are in turn determined and vary with the varying income elasticities of demand that make up and vary with the overall rate. This inter-relationship supplies the key to Leibenstein's "low level equilibrium trap" and Nurkse's "Vicious Circle of Underdevelopment" on the side of demand. If the growth in gross output per capita is 2 per cent (or in gross product 4 to 5 per cent) this very fact, in conjunction with varying income elasticities of demand that distribute this rate of growth among the various sectors of the economy, determines the growth of the market in each sector and hence the incentive to invest and specialize further.

Therefore the problem of accelerating growth can be restated in general terms as the problem of breaking out of the overall rate-sectoral rates of growth interrelationship. It is theoretically possible that this may occur through the operation of the price system in many sectors simultaneously. It is more likely, however, to arise from movements in one or more sectors independently of the overall rate. This, then, is the theoretical basis of the leading sector strategy of accelerating growth. It offers, therefore, a justification for action by the State to operate on one or more sectors where the

/conditions are

conditions are such that an initial rise in the rate of growth can be brought about independently of the overall rate and yet can subsequently influence and bring about a rise in the overall rate.

Viewed from this light, all export-led recoveries or booms (including petroleum) can be seen as examples of the working out of a leading sector model rather than as being anomalous exceptions, as they have usually been treated in the literature. Even an unbalanced budget engineered recovery shares some of the characteristics of an export boom in being an exogenous action not dependent upon automatic adjustment in a complex interrelationship of growth rates. Again, viewed from this perspective, the significant feature of an export-led recovery or growth is not the relief it affords from an exchange constraint, but rather the impetus given to the economy by the activity itself arising from exporting and the internal spending of the proceeds of exports.

#### Qualifications of a Leading Sector

To qualify as a leading sector, certain characteristics are essential. In the first place, to make a sufficient impact on the economy, activity in the sector must be potentially large enough to affect the overall rate of growth. An unmet current or potential demand must exist that can in some manner be activated. A second necessity is that a volume of activity significant in relation to the total must not quickly saturate the demand. In other words, the income elasticity of demand must be high enough to permit of a high and sustained rate of growth, once conditions are made favorable.

For a relatively small country, any action or development which permits it to meet a small additional fraction of the world demand for a commodity or number of commodities may permit a sustained rate of growth very high in relation to its overall rate of growth. The major difficulty with exports as a leading sector, however is that so frequently they are vulnerable to action beyond the control of a country, are subject to intense competition or, if an agricultural product, may encounter an inelastic price demand.

/Some countries

Some countries have found durable consumers' goods, especially automobiles, to have a high potential demand that can be tapped by the extension of consumer credit, and to have a high income elasticity of demand which can sustain a high rate of growth in the sector as the overall rate of growth grows. The difficulty is that concentration in this sector leads to such a large allocation of resources in this and related and induced expenditures (roads, parking areas, petroleum) and helps to create an undesirable urban style of living as to constitute a highly questionable national allocation of resources. However, it cannot be doubted that consumers' durables, activated by installment credit and reduced relative prices, constituted a leading sector of high growth for many years in the non-socialist developed countries and in some of the developing countries, as in Brazil. The price in urban design, inequality in styles of living and vulnerability to the effects of the exhaustion of one of the most important natural resources of the world, is now giving rise to second thoughts on the wisdom of the automobilization of modern life.

In many countries, housing and the accompanying building of shops, offices, and infrastructure, provide a possibility of high and sustained rate of growth that for many years can greatly exceed the overall rate of growth. The annual addition of units may represent a high rate of growth in an important sector but still be small in relation to the existing stock. The income elasticity of demand is also high. Up to 1973 and after 200 years, "house operation" still absorbed 25 per cent or so of consumers' disposable income in the United States and Canada. To initiate a movement may require state action to ensure the availability of funds on terms and conditions that permit rents or monthly debt servicing charges to be lower than on comparable existing homes or other buildings, or in areas or types of building that provide other advantages. The market need not be restricted to the provision of housing and related facilities to match the growth in families, but is potentially the replacement of

/much of

much of the existing stock of buildings. If there is mobility in real estate, the addition to the number of units need not be matched to the existing income structure, but be aimed at the middle and lower middle group who can afford new acceptable housing, making existing housing more available.

Before leaving the list of leading sectors where exogenous growth may be engendered, and their characteristics, it is worthwhile to point out the difference between them and a typical Keynesian engineered spurt in the GNP through an unbalanced budget, or a large and continued growth of the public sector. The first is only suitable when the basic difficulty is excessive slack in the system arising from deficiency of demand in a strictly monetary sense. If carried beyond this point to secure a growth in the national product in real terms, the effect may be only a rise in prices. How far the public sector itself can be a leading sector for this purpose raises difficult questions of measurement. In default of other means of measurement the custom in national accounts is to value all public work at cost. But obviously an indefinite addition to public payrolls in itself may not add to the sum total of goods and services except in a purely statistical sense. On the other hand, the addition could represent desirable services in meeting consumers' demands. One of the leading sectors in Brazil's period of high growth was State controlled enterprises in which exceptionally heavy investments were made, rather than in traditional public activities.

Are Leading Sectors Necessary and How Should They be Promoted?

The market oriented view is that they are not necessary. If, the argument runs, stability is maintained and interest rates are left to find their own level and funds are available to the highest bidder, the price system will ensure that capital (savings) will flow into the most profitable or productive channels to provide capacity to meet the insatiable demands of consumers. If, again, there is mobility of labor, the labor force will distribute itself through

/the mechanism

the mechanism of the price system (differing wage rates in this case). The flexibility of wage rates, competition, the profit incentive and a free capital market will ensure a proper balance in the use of labor to make consumers goods and capital goods, and in the full use of labor. Profit incentives will ensure technological advance and a positive interest rate will ensure savings and a consequent addition to the stock of capital. The combination of these factors will, therefore, ensure full employment of the work force at ever rising levels of productivity.

The bald statement of the argument should be sufficient to raise serious questions as to its validity. The conditions it requires obviously do not exist in any mixed society. Competition is imperfect, capital is not fluid, most saving is automatic or semi-automatic and much is not at all sensitive to changes in interest rates, wage rates in large sectors are flexible only upward, the wide differences in earnings indicate the low degree of mobility in labor <sup>1/</sup>, interest rates vary in flexibility, being highly inflexible in such an important part of the capital market as mortgage lending and saving. No country has been able to maintain stability in prices, but inflation is most uneven in its incidence, causing wide variations in "real" terms from the conditions required above. The demand of consumers for credit is insensitive to changes in interest rates, which in any case are generally concealed in the price of goods. The demands of the public sector are likewise insensitive and it requires a great act of faith or lack of imagination to maintain that capital is rationed in this sector to the most productive uses.

Despite titles in text books to the contrary, there is, properly speaking, no theory of distribution as such in economics. What is treated under distribution so far as earning from work and rates of

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<sup>1/</sup> A common source of confusion is that which identifies migration or movement with mobility. No matter how large migration may appear, if it does not lessen differences in wage rates we are still justified in saying that mobility is too low.

return on capital are concerned, is merely an application of price theory. Given mobility, competition and rapid growth there is a tendency for earnings in this sense to become less unequal. But there is no tendency for income (or distinct from rates of return) from property to become more equal.

All those points have been made many times and yet their relevance to the growth process and the justification for certain forms of State intervention do not appear to have been fully appreciated. To grasp their full significance, let us assume conditions in developing countries more similar to those that actually prevail. Let us assume for the moment, that prices are "relatively stable" which, in the present world would correspond with inflation of between 5 per cent and 10 per cent; that the GNP per capita in "real" terms is growing at a rate of 2 per cent per annum (or 3 per cent or 4 per cent gross) that the exports are relatively stable or growing slowly; that some 40 per cent of the work force is in agriculture; that there are relatively few large firms and hence competition is very limited in important sectors; that corporate savings run around 11 per cent of the GNP and personal savings around 3 per cent; and that interest rates in the thrift institutions catering to the mortgage field are either negative or zero.

For growth to occur under these conditions we would have to rely mainly on the replacement of existing equipment incorporating technical improvements--a slow process. The growth of most sectors would vary from zero to 7 or 8 per cent and the amount of new investment to meet this growth in physical terms would be modest. There would be no incentive to exceed this unless new equipment reduced cost so substantially as to lead to replacement of existing equipment while it still had a useful life, which in turn presupposes a substantial degree of competition. It is highly doubtful whether variations of two or three per cent in "real" interest rates (relatively large variations) would stimulate investment in most industrial and agricultural fields, if it requires additional replacement of existing equipment or addition

/to physical

to physical capacity in excess of sufficient to meet immediately foreseeable demand. Inflation of 5 per cent - 10 per cent would make the customary interest rates paid by thrift organizations (on savings deposits for example) negative or very low in positive terms, so that voluntary personal savings would be low as a percent of the gross product. On the other hand, long term borrowers would hesitate to control loans at 10 to 15 per cent for long periods, so this type of investment would likewise be low.

The case for selective credit control, generally to the agricultural but often also to the industrial field, is based on the assumption that investment can be influenced in such fields by relatively small variations in the true interest rate and can be stimulated regardless of the actual overall and sectoral growth rates, corporate or business savings and the adequacy of existing capacity. True, loans will generally be taken up if offered below the market, but whether they will actually lead to a greater investment in the particular favored sectors above what would have otherwise occurred, is another question. Loans may be contracted on favorable terms and actually used and yet the borrowers may place their own funds or earnings that they otherwise would have used in different and more profitable fields.

With low rates of growth, the absorption of a rapidly growing labor force in remunerative occupations is difficult to obtain. The increase in average productivity can be retained by the sectors with the highest growth rates (or for whose product there is the highest income elasticity of demand), forcing more people to remain in semi-subsistence agriculture. Such people cannot effectively compete with mechanized agriculture but in their efforts to do so, or in their availability at very low wages, may discourage investment in such mechanization. Since the income elasticity of demand for agricultural goods is generally very low, the possibility of securing higher growth rates in this sector (i.e. making it a leading sector) is slim except occasionally in particular exports where a larger share of world markets may be obtained.

/The case

The case for selective credit control in sectors in which investment may be characterized as derivative or responsive only to the impact of real demand from other sectors is, therefore, weak. It is especially weak if the income elasticity of demand is low in the particular field to which credit is being directed.

This line of argument, however, would not apply to the field of building if there is a large unsatisfied demand and a high elasticity of demand, and the field has been suffering, say, from a shortage of funds, as appears to be the case in many developing countries and, recently, in developed countries.

#### Real Demand vs. Monetary Demand

I should like to return to the distinction I made earlier between Keynesian and real demand, or demand in the sense of J. B. Say. Suppose that by a most appropriate contribution of monetary, fiscal, incomes price and exchange management we can achieve "full" employment under stable conditions. It is important to appreciate that even such ideal conditions may not be sufficient to assure a high growth rate. The roots of under-development go even deeper. They have to do with the rapidity of the increase in the work force, with the size of the work force in relation to resources, with the degree of mobility, competition and substitutability of capital and labor, with the conditions favoring or not favoring a rapid adoption of known technology.

The emphasis and influence of Keynes was, as was natural in his time, on spending, particularly in the form of investment, but in any case in any and every form. Since he believed that the propensity to save rose with a rise in incomes, and since, by definition, savings were always equal to investment, there was, for him, no problem of inadequate saving. Indeed his leading disciple, Alvin Hansen, became very concerned over the prospects of excess saving to maintain full employment and Keynes himself thought that with full employment the problem of poverty could be resolved in a generation or so and true interest rates could fall almost to zero.

/I say



I say all this not to criticize Keynes and Hansen, both of whom I admired, but rather to remind you that they did tend to neglect or ignore important factors. The identify of savings and investment and the stability of prices can exist in disperately poor countries and be compatible with a low level equilibrium trap. For a country as a whole, there is no good evidence that the propensity to save tends to rise. The savings of some can be offset by the dissaving of others. The Keynesian analysis never was well adapted to public accounts and the meaning of savings and investment becomes strained when applied to such accounts.

What I am suggesting is that we examine more carefully the implications of certain pre-Keynesian or more classical concepts like, for example, "real" demand in Sayian sense. The distinction is difficult to grasp as an increased demand in the latter sense is also expressed in monetary terms, since we do not actually exchange goods for goods. In one case, however, the increased money demand is a reflection of the increased output of goods at a stable price level; in the Keynesian sense, it may reflect simply increased monetary disbursements unaccompanied by any increase in real output. In dealing with a large mass of unemployed and excess capacity in the Great Depression, the distinction was not, perhaps, so important. In dealing with growth in a developing country, however, the distinction is vital. Here, mobility is a far important concept than unemployment, and the obstacles to greater mobility are formidable. Inflation or excessive monetary demand may even, paradoxically, impide desirable flows of capital and labor to increase real income. It can even act to decrease personal saving as a percent of income and decrease that type of investment traditionally dependent on such saving. Hence internal production, (which is also the demand for internal production) may continue to grow only slowly, offering inadequate incentives for the adoption or adaptation of technological advances and affording also a slow groth in the economies of scale on which the profitability of rapid specialization and heavy new investment depends.

/It is

It is to this high degree of immobility, maintained and reinforced by a high birth rate, the lack of competition, low price elasticity of demand, and institutional obstacles and barriers to fluidity in capital flows that I think we must look for an explanation of the apparent lack of elasticity of supply to a general increase in overall monetary demand resulting, say, from a government deficit. On the other hand, there can be considerable elasticity of supply resulting from more and "better" employment of people producing more real things for which there is an unsatisfied and potential demand (which includes an increase in exports). Putting the same thought in other terms, this may explain the puzzling phenomenon of the fairly rapid response of prices rather than of production to an increase in money even though there appears to be great excess capacity or underutilized factors in developing countries. Monetary demand that reflects an increase in real production is met by an increased supply of goods. But if the monetary demand comes first, and there is no change in factor proportions or capital investment, the effect will show itself immediately in a rise in prices. I was once asked "How can the system distinguish between Keynes and Say?" I confess that the question bothered me. I hope what I have just said is the answer.

The relation of monetary to real factors in Keynesian analysis has recently been re-examined by Sir John Hicks <sup>1/</sup>. He states, as is clear, that Keynes underestimated the strength and importance of barriers to expansion of output in real terms and to employment in assuming the presence of adequate inventories to meet an increased effective demand, and in neglecting the extent to which prices are fixed and can be easily raised to meet wage demands. All of these factors may cause a rise in prices rather than employment to result from an increase in investment. On the contrary Keynes laid too much stress on the existence of "surplus" labor, as was understandable in 1932-35.

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1/ "The Crisis in Keynesian Economics", Basic Books, Inc., N.Y., 1974.

While Hicks implies that actually the Keynesian multiplier analysis is misunderstood as a flow mechanism and should rather be interpreted as "an equilibrium to which the system is tending", this is, I think, being unduly kind. Despite the attempt by Keynes to convert money aggregates into constant "wage units", by definition the identify of savings and investment and the multiplier are monetary and national accounts concepts, and are true at any moment of time as well as over time in terms of monetary income. This over simplification became evident as early as 1936-37, when, with millions still unemployed, a sudden increase in the government cash deficit, following a long period of no industrial building and low inventories, touched off an unexpected and sharp rise in prices. Curiously enough, it was the very rigor of the Keynesian analysis that led both to its acceptance and to its inadequacy to deal with the complex problems of maintaining full employment with stability.

For our present purposes, the point of this excursion into Keynesian economics is to introduce the element of time into our discussion. Not only does the addition of industrial capacity take some time (which may be reduced by changing to double and triple shifts, and by imports) but also Hicks reminds us that it takes some time to build up inventories in line with production. To these elements we should, of course, in a developing country, lay much more stress on institutional obstacles and never treat labor as a homogenous aggregate, whose components have infinite substitability.

In short, in the development of leading sectors as complements to short run macroeconomic policies, the time element must be kept in mind, and the more rapidly government policy can aid in the shift of factors in avoiding bottlenecks in capacity in advance, in supplementing inadequate stocks by imports, and inadequate skills by training, the more rapidly can leading sector growth occur. By the aid of a appropriate policies, the Singapore Government was able to maintain annual rates of growth in building in real terms of 30 per cent - 35 per cent for a relatively long period, and avoid the cyclical swings or stop and go sequence that so often characterize a planless mixed society.

/Implications for

### Implications for Policy

Since the orientation of this symposium is toward policy and mostly short term policy and my paper has dealt more with underlying causes of the slow growth of developing countries, it is time to turn to the implications for governmental policy in the short as well as the long term, and to the question of operating through market forces as well as through direct governmental intervention.

While in certain activities direct governmental intervention is unavoidable, anybody who has spent much time either in or dealing with governmental agencies will probably agree that the organization of government is not well adapted to the rapid taking of a large number of decisions. The more decision making by top officials can be reduced to a relatively few crucial issues and fields, the more likely will the quality of decisions be improved, and certainly the more rapidly will the decision making process proceed. It has proved difficult in mixed economies for government officials to delegate authority without an elaborate system of checking and review which diffuses responsibility and makes for an apparently unescapable and interminable process of a paper passing. Hence, if there is a choice, it should be in the form of the government determining broad lines of policy while decentralizing individual decision making as far as possible to the private sector, or in certain cases, to government corporations organized and operating like private corporations.

Applying this general rule to the type of policy we are discussing in this Symposium, it would appear that the monetary authority should not be asked to pass on individual loan applications or to engage in selective credit control (except possibly in very broad categories) but should be concerned principally with the supply and control of money. The balance between fiscal expenditures and receipts could be the responsibility of the top economic policy making officials in the Government, while the composition of expenditures could be the responsibility (in general) of less burdened officials and the Congress.

/If the

If the argument is accepted for the adoption of a leading sector strategy to insure a higher rate of utilization of the factors of production, our general rule would suggest again that as full use as possible be made of the incentives of the private sector in the decentralization of the individual decision making process. If, for example, it is desired to accelerate growth by promoting exports, it would seem wiser for the Government to confine itself to broad policies relating to exchange rates and export financing. The effectiveness of attempting to promote individual exports or to pass on individual licences to import (other than in very broad categories) may be questioned.

Government officials in developing countries work under an almost insuperable handicap in obtaining reliable figures on current and capital costs from individual firms or industries and on foreign markets as bases for specific measures to facilitate exports of individual items. Relatively low salaries and rapid turn-over of government personnel, and lack of time of upper decision makers, make the chances of successful operation of policies relating to individual companies and items rather remote.

Again, if it is desirable to utilize building construction as a leading sector, it would appear preferable for the Government to concern itself with broad policies in establishing specialized private institutions, in ensuring that adequate incentives are provided for personal saving on the one hand, and for borrowing on the other, which incentives will be, so far as possible, made inflation proof. A government agency can concern itself with the general regulation of the savings/mortgage system, giving assurance that saving will be large but that the steady growth in building will absorb the savings, and in forecasting and breaking bottlenecks in the materials fields before they appear. In certain cases, it may prove desirable to modify the traditional pattern of urban growth from a mono-centered metropolis to a cluster of compact, high density, self-contained, "walkable" cities within and immediately adjoining a metropolitan area, and the

/Government again

Government again can establish specialized public institutions to this end, while it lays down guidelines and reviews programs and accomplishments. In this way appropriate use is made of the special characteristics of the public and private sectors.

None of these operations required "Ministry" to deal with a multitude of individual borrowers, savers, land owners of tenants or daily to take a wide range of decisions. The broad policies pursued, however, can accelerate the rate of growth under stable conditions by (a) ensuring that actual investment will occur and (b) be financed by saving, (c) that mobility is enhanced and that jobs will be available for the unemployed, partially employed or generally under-utilized workers. Since a building is largely an assembly of industrial materials, there is an immediate impetus to the derivative or following industrial sectors whose investment and production is dependant upon demand for their products coming from outside their sectors. The growth of cities can be guided into a design that avoids many of the ills of large cities today characterized by sprawl, segregation, enormous transport expenditures and transfers of buying power on balance from the less to the more well-to-do as land values rise. As real employment rises, the demand in real terms rises even if conservative monetary and fiscal policies are being followed. While most economists have probably felt that the only way to assure both stable prices and full employment is through a strictly enforced incomes-prices policy to support appropriate fiscal and monetary policies, it is not at all evident that this would be sufficient. What may be needed in addition in positive action to ensure a high level of growth in one or more sectors, financed in large part by high and rising saving. The remarkable record of Singapore where, for a number of years, rates of growth of 14 per cent and levels of savings of over 30 per cent were maintained, appears to have been due to positive action to increase the value added in exports and to house and rehouse the urban poor. A significant portion of the simultaneous growth in incomes was captured as savings to finance the building program.

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The highly ambitious French urban building program of promoting the building of satellite cities around Paris and a number of other metropolitan areas is planned and conducted by a relatively small Ministerial committee with a professional staff of some twenty people. While, to my mind, it is not as successful as that of Singapore, this is not due to the smallness of the staff but to differences in overall policy which permitted the total building effort to become very diffused in a country with a low population growth rate and which, in turn, led to too quick sales of land and buildings and hence the loss of the opportunity for cross-subsidization of rents within a new city.

In the case of Colombia, a completely new system of savings/mortgage corporations based on monetary correction was grafted onto an existing fixed interest saving system of commercial banks and a publicly owned mortgage bank financed by twenty year fixed interest bonds. Ten private corporations whose capital was subscribed by the private sector were granted charters and within a year had gathered as large a volume of savings as the mortgage bank had collected in over 40 years. The demand for construction loans steadily out-ran the rise in deposits in a ratio of 2 to 1. In two years of operation (the second under considerable difficulties) the number of individual savers grew from zero to over 200 000.

For the purposes of this discussion perhaps the aspect of chief interest is the use made in both the French and Colombian case of private initiative. The government professional staff in both cases under discussion is very small. Government action was confined to the highly difficult role of policy making and the laying down of guide-lines. In the Colombian case it was early decided not to follow the Brazilian example of a single mortgage bank largely supplied with the funds of part of the social security system, nor the Chilean case of mutual saving associations. It was felt that the system had to be established quickly; that large amounts of private capital were

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immediately necessary; that competition should be fostered. The basic decrees were very simple and underwent few modifications before the change in government. It is, I think, an instructive case of how government may make use of the advantages of decentralized decision making and the incentives of the private sector, while keeping firm control over all-over policy making and even making far reaching institutional changes.

While this could be regarded as a short term policy to accelerate growth in potentially leading sectors, or to counteract the repressive effects of a stabilization policy, it could also be a long term policy of protecting crucial sectors against the harmful effects of inflation (which, unless offset, damages exports and building particularly severely) and hence supplies some of the mobility and fluidity the existence of which economists too often take for granted.

Mention was just made of the possible use of the leading sector strategy to accompany anti-inflation policies. The familiar objection to such policies is the unemployment they may cause. But if austere monetary and fiscal policies are accompanied by, say, a building policy financed by private savings, stability may be attained without increased unemployment other than may result from exogenous mark-ups in wages and prices. The validity of this assertion depends upon adequate measure to avoid bottlenecks in building materials. High growth rates in building and exports (value added) were sustained from 1965 to 1972 in Singapore, while being accompanied by conservative fiscal and monetary policies and actual revaluations upward of the Singapore dollar, with consequent full employment and stable prices.

If, for good reasons, direct governmental action is required, the possibilities of adopting the private corporate form to public enterprises should be studied. This is not always practicable, but may be so where an activity is expected to be self-sustaining and involves a large mass of buying and selling operations and dealing with individuals. Many countries have made use of the device and, where suitable, it undoubtedly offers a way of lightening the load on

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an overburdened bureaucracy and top decision makers, while preserving the opportunity for the Government to intervene when major policy decisions involving the economy arise.

Broader Implications

It will be recalled that this paper is explicitly concerned with mixed economies. No value judgments are involved. It is simply an assumption to facilitate discussion of policy for the predominant form of economy in Latin America. On the basis of this assumption, therefore, policy can be directed both to accelerate the rate of growth through judicious intervention in the market mechanism and to make the basic underlying assumptions of the non-interventionists more realistic. Thus the use of the Leading Sector Strategy implies also action to heighten rather than reduce mobility. It favors not only direct measures to reduce the size of families but fairly drastic changes in socio-economic environmental factors to the same end as well. The quicker unskilled labor can be made scarce, the more effective will be the redistributive action of the Government. The more rapidly, in particular, that agricultural labor becomes worth more, the greater the effectiveness of the incentive to mechanize and to abandon very small and un-economic sized holdings. Whatever can be done to encourage competition, secure freely moving interest rates in the short run, maintain price stability or, in its absence, protect especially important sectors such as exports, savings, longer term borrowings, and utility rates from the distortions created by inflation, would be eminently worthwhile.

Whatever may be our feelings about the wisdom of continued growth in what, a short time ago, we referred to as affluent societies, a period of high and sustained economic growth appears desirable in developing countries if only to restrain demographic growth and to make possible a raising of standards of housing, diets, health and education of the poorer groups of the economy. Directing more of the flow of new production to this end, in mixed economies, is infinitely

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less socially and politically disrupting than trying to redistribute an existing stock. But we must keep in mind that a high and sustained rate in itself facilitates high and sustained rates. As I insisted earlier, this is an implication of the dictum that the profitability of specialization and the division of labor is limited by the size of the market. The more rapid the rate of growth, the more incentive there is to invest and the easier it is to save. The more rapidly jobs open up, the greater the incentive to acquire special skills.

The growing scarcity of certain resources may make the maintenance of high growth rates more and more difficult, but I am here thinking more of the possibility of sustaining rates of growth of 8 per cent to 10 per cent for ten years or so, rather than indefinitely, in order to achieve what Leibenstein has called the Critical Minimum Effort or the effort necessary to facilitate the attainment of various key desirabilities of what we refer to countries in the most developed category. Even this may be difficult for a few countries where population is already pressing on resources.

The argument of this paper, then, is that we should seek to make better use of the market mechanism but not to be dogmatic on the subject. We should not hesitate to intervene when it appears feasible, to modify institutions and to take steps to make the basic assumptions of the market mechanism more valid. However, it is well to recognize the limitations of that mechanism to achieve some basic objectives. For developed countries the desirability of exponential growth is already, and I think quite rightly, being questioned. This may in time call for a profound modification or sublimation of the basic incentives upon which growth rests. But this is a theme for a different symposium.

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