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Review

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The international scene and Latin America's external debt

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The impact of the present crisis on Latin America and the region's external debt are the result of changes that have occurred in the international system during the last 15 years and of the transformation of the Latin American economies and societies. They are also a consequence of the domestic policies pursued by these countries, but these were in essence a reaction to the new conditions prevailing in the regional and international sphere during this period.

In the author's view, the hierarchical world that arose out of the Second World War, in which international relations revolved around the concept of security, began to crumble at the end of the 1960s owing to a tendency towards the fragmentation of world power and a vigorous process of transnationalization, which interlinked the different national societies in accordance with a wide spread of interests. Moreover, the international economic crisis, whose first symptoms go back to that same period, put an end to the record cycle of expansion that the industrialized countries had enjoyed during the last 20 years and facilitated the rise in oil prices, which generated large surpluses of liquid assets which fostered a permissive attitude in the international financial field. Some developing countries, among them the largest Latin American nations, advanced rapidly towards an intermediate stage of development and integrated themselves more closely into the international economy. Thus they could exploit opportunities and assume risks to a much greater extent than in the past, which explains the great impact of the current crisis on the Latin American countries, more severe than that of the 1930s, when these countries were much more able to detach themselves from the external cycle.

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I

The transformation of the international system

The international system, whose basic features arose out of the Second World War and lasted until the end of the 1960s, underwent from that time onwards a complete transformation. The structure of world power, which during the post-war period remained in a rigid bipolar mode powerfully influenced by the Cold War, began to change significantly with the relative decline of the power of the United States, the rise of tensions within the trilateral system and particularly in the Atlantic Alliance, the internal difficulties of the Soviet bloc and the exhaustion of the model that this represented, the growing degree of development and external projection achieved by some Third World countries, and the trend towards the fragmentation of the international system, which postulates the need to seek formulas to promote collegial action within this system.

According to the "new orthodoxy" school of thought (Hoffman, 1981; IISS) the power of the United States in the world fell sharply during the 1970s, particularly *vis-à-vis* the Soviet Union and the Middle East, which would explain the concern revealed by the fact that in 1980 "42% of United States citizens declared that foreign policy was the most important problem for their country", placing this far ahead of the economy and energy (Yankelovich and Kaagan, 1980).

Paradoxically, the decline in power of the United States coincided with the emergence of a profound malaise in the Soviet world. Despite the fact that Soviet military power had grown so fast that it had reached at least a measure of parity with that of the United States, this growth, from a structural and longer-term point of view, was a sign not of strength but of weakness. The instability of the Soviet presence in the Third World, the invasion of Afghanistan (regarded as a defensive measure by the Soviet Union to safeguard its own frontiers), and the grave challenge of Poland to the survival of the political and social system on which the entire Soviet bloc is based, constitute very serious issues which have not yet been adequately appraised (Bialer, 1981; Bialer and Afferica, 1982-1983; and Hyland, 1982-1983).

To these must be added the persistent dif-

facilities of the Soviet economy in respect of its food base, the production and distribution of consumer durables, and its urgent need to acquire western technology (Marshall and Goldman, 1982). The Soviet model as an alternative for the construction of other societies, particularly in the Third World, would seem to be in eclipse in face of the frustration of the population of the socialist countries and the growing militarization of these régimes.

The tensions that have arisen within the tri-lateral system constitute another factor of change. Their most recent indicator is found in the conflicts within the Atlantic Alliance. The unilateral replacement of *détente* by a new version of power politics on the part of the United States has estranged its European allies. It should be borne in mind that *détente* has had positive results for the Europeans, both in economic and political terms, but not for the United States. Furthermore, the globalism of American foreign policy is incompatible with the European conception, according to which *détente* is divisible, depending on the issues and regions involved. The conflict generated around the oil pipeline was an expression of these tensions (Joffe, 1981; Cohen, 1982-1983; Andelman, 1982-1983).

The arrival of the Third World on the international stage, midway through the postwar period, constitutes a new factor of instability and change. Today this group is represented by over 100 countries, half of which attained independence during this period. Many have reached stages of intermediate development and have promoted rapid industrialization processes, integrating themselves more firmly into the international system. There has been the emergence of the non-aligned movement, the Group of 77 and the Organization of Petroleum Exporting Countries (OPEC). The viewpoint of the different developing regions of the world must now be taken into account in the handling of international relations: conflicts of regional origin have come to have increasing impact on the stability of the world in general, a fact which is aggravated by the repeated efforts of the great powers to place these clashes within the framework of the East-West conflict (Bertram, 1981; *Estudios Internacionales*, 1982; Russell, 1984).

The above-mentioned factors have created a

phenomenon of diffusion of power, giving rise to a world which is more interdependent but also more fragmented. They have thus posed the need to advance towards collegial management of the international system. This new structure of world power presents the developing countries—and particularly Latin America—with a complex balance of limitations and opportunities.

As a result of these trends, a world dominated by considerations of strategic security and by the confrontation of two superpowers is evolving into another characterized by some degree of *détente* and an atmosphere more propitious for the prosecution of other interests—economic, technological, social, ecological and cultural—in the relations between nations. To the fragmentation of world economic and political power must be added the growing complexity and dispersion of the strategic conflicts. This process has also been hastened by the emergence of world problems—such as energy, the environment, 'stagflation' or the external debt—whose solution is essential for the welfare of ever-increasing sectors of the national societies.

In their turn, these societies are being transformed. The prolonged period of economic growth, social development and strengthening of democracy which the industrial societies lived through during the postwar years steadily increased well-being and promoted the strengthening and diversification of the civil society in those countries. The Nation-States committed themselves to an increasingly wide range of objectives which included (together with national security) economic development, the growth of income, the maintenance of employment, preservation of the environment and protection of cultural identity and the quality of life. These objectives came to have a decisive influence on their external relations. At the same time, as the civil society expands and is articulated into multiple interest groups, these groups aspire to take charge of a growing proportion of the affairs of the community. The transfer of responsibilities from the State to the civil society, and the ensuing proliferation of non-governmental groups in a world in which the discharge of these responsibilities depends increasingly on international factors, frequently compels these groups to seek to satisfy their interests on the external plane (OECD, 1981;

Thurow, 1980; Cardoso, 1982; Flisfisch, 1982).

These trends at world and national level reflect the transition from an international system dominated by concepts of power and security, such as that which in broad outline characterized the postwar period, to another based on interdependence and oriented towards the promotion of maximum national well-being (Cooper, 1968 and 1972; Keohane and Nye, 1972 and 1977; Rosencrance and Stein, 1976; Maghroori and Ramberg (comp.), 1982; and Roseneau, 1980).

The "realistic" view of international relations that predominated during the postwar period was based on several assumptions. The first saw international policy as being centered around the interests of the great powers, with one or other of which the smaller States must be aligned, giving rise to the formation of blocs or spheres of influence within which the leading power would settle conflicts and impose some order, and among which a state of coexistence prevailed, precarious but conforming to certain rules. The second saw the national societies as relatively simple units with regard to their external projection, and acting as a function of a limited number of objectives, generally subordinated to the maintenance of peace and security. The third assumption, deriving from the first two, reduced the international programme to a limited number of issues, in a clear order of importance, among which the issue of security enjoyed unquestionable priority. The fourth assumption was concerned with the homogeneity of the agents acting in the international sphere, represented by the Nation-States, which did not recognize the legitimacy of other agents qualified to act between or within them. It is not surprising that the fifth assumption involved an equally restricted view concerning the resources that one State could employ to influence another, which were conceived as confined to the political and military sphere, and concerning the fields in which these resources might be employed, which were regarded as few, well defined and sufficiently well known.

All these assumptions were called into ques-

tion by the trends referred to above. One might venture here the hypothesis that, in contrast to the past, international relations are today 1) influenced by an increasing number of power centres; 2) their external action seeks to satisfy a much wider variety of aims than in the past; 3) they develop around a more diversified, complex and less hierarchical programme; 4) they are managed by new and multiple State and private agents who 5) bring into play non-traditional power resources in a variety of settings much more numerous, changing and interwoven than before.

These trends give rise to a transnational system cast in a new mold, in which it is possible to refashion the structure and functioning of numerous "ambits", "plays" or "circuits" operating round the programme, agents and power resources mentioned and linking together the different national societies in various ways according to specific interests. From this angle, one could postulate the rise of transnationalized circuits in the fields of energy, food, industry, technology, finance, strategy, science, ideology, culture and religion. Each of these circuits is highly specific in scope. The conditions of access of the different countries to each of them and their relative position within the circuit do not solely depend on their status in the international hierarchy (whether within the East-West conflict or the North-South relationship) but on their relative position respecting the interests which are in play in each of these circuits. The international structure is becoming more fluid and interdependent but at the same time, paradoxically, more fragmented and indefinite. The crisis of the development style prevailing in the industrialized countries is tending to accentuate this trend. Against this background, the developing countries —especially the Latin American countries that have achieved a higher degree of integration in the international system— have seen their external vulnerability increased, although, at the same time, they have acquired more room for manoeuvre to achieve a complex equilibrium between risks and opportunities (Tomassini, 1984; Mirow and Maurer, 1981).

II

The world economic crisis

The development style prevailing in the postwar period, based on the ideology of growth and modernization and on the world projection of this model through the demonstration effect created by the transnational corporations and the entire institutional apparatus that served to sustain them, was possible thanks to the international structure in force at the time. This structure was characterized by the hegemony of the United States and the predominance of criteria centered on the maintenance of the strategic security of that nation and the other countries with which it had made defensive commitments, in a system of cold war. This made possible the diffusion of a development style which expressed and promoted United States interests and, as time went on, those of its main allies. Along with the modification of this international structure, however, came the failure of the project to consolidate and disseminate this development style, in its basic variables.

Hence since the end of the 1960s the world economy has entered into a state of profound crisis, whose structural—and not only cyclical—nature can no longer be denied. The crisis has had a severe impact on the developing world, and especially on the Latin American countries, which had achieved closer integration into the international economy. This crisis was first manifest in the ecological foundation of economic growth; then it became evident that its nucleus was in the industrial transformation of the advanced societies; and finally, in more recent years, it displayed its full virulence in the financial imbalances produced in the world order, which had their worst effects on the developing countries, especially those of Latin America.

Although it is thought that the crumbling of the postwar development style was basically due to the industrial transformation of the advanced countries, it must not be forgotten that its first symptoms appeared in the imbalances arising at its ecological base. Among these must be mentioned the growth of the world population; the diverse factors limiting greater food production; the uncertainty and the increased costs

associated with the supply of energy and other industrial raw materials; the problems posed by the excessive concentration of industrial growth in a few geographical localities; and the danger of pollution of the environment, due, in essence, to the high degree of concentration of the urban population and economic activities.

The first report on these problems published under the auspices of the Rome Club provoked multiple reactions on the theoretical plane, while the decisions adopted by the OPEC in 1973 gave the alarm signal in the world of reality (Meadows and others, 1972; Mishan, 1977; Wilson, 1977; Leontieff, 1977; Freeman and Jahoda, 1978).

Thus it came to be recognized that the tempo and degree of growth concentration in the large industrial centres had taken place at the expense of the environment, the natural resource endowment and the capacity for ecological support of productive activities. It was then that an awareness arose of the physical limits restricting economic growth.

In the final analysis this new awareness was one of the indicators that the advanced societies were reaching the limit in regard to the factors on which their postwar industrial development was based. "The world economic crisis is first and foremost an industrial crisis", is the opening statement of one of the most recent reports that seeks to forecast the future of the world economy from a European standpoint (CEPII, 1983). It is arguable whether the weakening of the industrial impulse observed in recent years in most of the developed countries is leading to a post-industrial society, or to an industrialization of the services sector in which the secondary sector will once again be converted into the engine of economic growth and will guarantee the diffusion of the technological changes on which the progress of those societies will be based. It is arguable, likewise, whether the world economy has embarked upon a stage of slow growth for a prolonged period or whether the rapid incorporation of the technological changes which are now in process will bring about a recovery of the economic dynamism of the past. Consider-

able weight can be assigned to the limitations stemming from the supply of energy and natural resources, or, alternatively, optimism can be felt as to the potential inherent in the recent technological innovations in the field of energy and the production of new materials. Whatever may be the forecasts in this field, there can be no doubt of the magnitude of the transformation occurring in world industry and the importance of the recent technological advances, coupled with the impression that mankind is on the brink of an industrial revolution unequalled since the end of the eighteenth century.

The extraordinary growth of international trade in the postwar years was mainly due to the fact that the expansion of demand for those consumer durables which form the bases for the American style of life and its diffusion throughout the world was met through greater specialization among the industrial countries in accordance with Ricardian principles. Each country thus acquired a dominant position in the market in specific industrial sectors, which favoured the continuous rise in prices. This, together with the reconstruction of Europe and the emergence of Japan as a great industrial power, stimulated competition and changes in the spectrum of specializations already acquired by the different countries. At the same time, the expansion of demand for durable goods that had constituted the basis of the development of the most dynamic industries during the postwar period began to decline at the end of the 1960s, producing a marked contraction and a change in the structure of demand following the saturation of the markets for this type of product. Another factor was the change in public preferences in a growing number of social sectors as a consequence of the radical socio-cultural reforms that are altering the modes of life in industrial societies and spreading attitudes less interested in acquiring more of the same and oriented rather towards values concerned with the quality of life.

These trends are linked with the drop in productivity in the industrial countries; with the fall in investment and the reduced profitability of enterprises; with the appearance of idle capacity in a growing variety of industrial branches; with a slower tempo of technological innovation; with higher operating costs in the productive systems and in the societies themselves through the rise in wages and public expenditure; and, in general, with reduced competitiveness in an increasing number of productive activities.

The process of transnationalization which spread the development style prevailing in the postwar period also facilitated the subsequent changes in market structure and in the pattern of technological innovation, and the reorganization of world production to meet the new requirements. Thus, a new international division of labour has begun to emerge, whose future structure is not yet clear, but which is already causing acute tensions among the developed countries and which might alter the traditional forms of linkage between the developing countries and the world economy.

To cope with this process the developing countries have had to introduce extensive adjustments. These were more painful for those countries which were more closely integrated into the world economy, which were more vulnerable to these changes and which lacked resources to mitigate the adverse effects of the world transition on their economic growth or to finance the transformations demanded. These countries tried to soften the adjustments in different ways through massive external borrowing. This was possible owing to the enormous amount of liquidity that arose in the world economy from the beginning of the 1970s, when, after almost half a century, private financial markets began to reappear as a result of, first, the weakening of the dollar, next, the reactivating policies of the industrialized countries and, last, the surpluses accumulated by OPEC.

III

The transformation of the developing countries

The notable tempo of development observed in an increasing number of developing countries in the last 25 years and their progressive integration into the international economy caused profound changes in the economic, political and social systems of these countries and in their relations with the industrialized countries.

At the beginning of the 1950s no-one placed great hopes in the possibility of promoting the development of the peripheral countries through stimuli deriving from the external markets, nor believed that this process could go hand in hand with their gradual integration into the world economy; instead, a preference was shown for policies of industrialization through import substitution and mechanisms aimed at regulating the international primary commodity markets.

During the early stages of their industrialization, many developing countries —especially in Latin America— sought to substitute imports of manufactures with domestic production. As a result of import substitution an attempt was made to increase the proportion of national consumption that would be covered by local products. Among the primary motives for adopting this strategy were the chronic balance-of-payments crises that affected the developing countries because of their structural situation of external strangulation. The strategy was also a response to the long-term political aims of the national governments. It was hoped that import substitution would reduce expenditure in foreign currency and increase the autonomy of these countries. At the same time, this strategy would open the way for the governing élites to satisfy the claims of social sectors whose bargaining power was increasing as a result of development itself, by applying a policy designed to foment development, income distribution and employment simultaneously.

To the extent that domestic demand could serve as a basis for setting up new industries which one day —and this consideration has now become very important— might be able to compete with the displaced foreign producers, it was possible to justify the protection levels agreed

upon, the same arguments being advanced as those once applied to infant industries in the past. To the extent that this last condition was not fulfilled, however, the import-substitution strategy would come up against certain limiting factors: either industry would begin to generate the foreign exchange needed for its later development, or its growth rate would be limited to that made possible by the supply of foreign exchange generated by the primary commodity sector, which in some cases these strategies had relegated to second place. In practice, generally speaking, the only import substitution made was that of consumer goods by capital goods and inputs needed for the functioning and expansion of the new industrial enterprises.

As time went on many countries recognized that the propensity to use foreign exchange without generating it is not inherent in manufacturing activity, and one after another they came to the conclusion that protection should be given less weight and that more importance should be attached to efficiency, competitiveness and export promotion.

From the mid-1970s —and even before in the cases of island States or city-States which had no other option— experiments began to be made, at different speeds and in different ways, and to an obviously exaggerated extent in some Latin American countries, with new strategies based on the liberalization of the domestic market and the opening up of these economies to the exterior.

Although this transition has frequently appeared to be a conflict between rival schools, it is now clearer to us, with the benefit of hindsight, that in practice these stages were not then proposed as alternatives but rather as complementary processes. For many countries of the Third World the import-substitution strategy was the only option feasible at that particular point in time, considering the stage of development they were living through and the existence of an adverse external situation. It frequently served as a base not only for their industrialization but also for the consolidation of their nation-

hood. Moreover, not only was there no awareness at the time of a necessary contradiction between the internal and external markets, but the former often served as a springboard to the international market. Further, although it is quite true that there were subsequent changes in the strategies of growth and in the forms of external relationship of the developing countries, it is no less certain that these did not take place overnight, as we have been wisely reminded recently in an important report (ICIDI, 1980, p. 262), which noted that these changes could not be made at a moment's notice, but from the 1960s many developing countries have progressed towards strategies aimed at promoting exports and offsetting the disadvantages arising from the isolation of their national markets, while some countries—including certain Latin American countries with a relatively long history of national independence and some island and city States whose economies were obliged from the outset to depend on external demand—have introduced export-oriented policies and were able to exploit their comparative advantages in world markets. Once industrialization had taken root, not only the labour-intensive industries, such as clothing or leather goods, but also certain moderately capital-intensive industries, such as electronics, iron and steel, and shipbuilding, became highly competitive in international markets.

As a result of these strategies—as the aforesaid report recalls in general terms—the share of manufactures in the total exports of the developing countries (excluding petroleum) rose from 10% in 1955 to 20% ten years later, and to close on 40% in 1975 (ICIDI, 1980, pp. 262 and 174).

This export boom reflects more complex changes in the economies that attained intermediate stages of development, and moreover it was concentrated in a still limited number of countries. This prompts us to refer to the growing differences observed in recent years among the peripheral countries and to the situation of those among them that have achieved intermediate development. The literature on this subject has multiplied in recent years. The first report on the evolution of the international economy prepared by the World Bank in 1978 provides a useful, though controversial, point of de-

parture in dealing with the subject (World Bank, 1978).

The growth of the developing countries has been spectacular in the last 25 years: their per capita income has increased by almost 3% per annum, while their annual growth rate has risen from around 2% in the 1950s to 3.4% in 1960. Although the experience of these countries before 1950 is little known, this rise in growth represents a considerable improvement on historical precedents. Moreover, these results are very favourable when compared with the growth rates of the developed countries during their industrialization period. But the report goes on to confirm that there were notable differences in the results obtained by the different developing countries during the period, noting that the growth rates have in general been lower in the low-income countries of Africa and Asia, where most of the poor of the world live, since they contain half the population of the developing world, and where the per capita income has risen at less than 2% per annum (World Bank, 1978).

We must bear in mind, therefore, the great diversity of the developing countries from the standpoint of the size of their economies, their levels of income, their resource endowment, their economic structure, their forms of organization, their technical capacity and their linkages with the world economy. It is reasonable to distinguish, at least, between: a) the oil-exporting countries, b) the countries at intermediate stages of development, and c) the less developed countries, or those with lower incomes, which constitute what is known as the "Fourth World". Among the low-income countries there are also great differences: the World Bank itself distinguished subsequently between those with a mining economy and the predominantly agricultural nations.

The World Bank report uses per capita income as the basic indicator for distinguishing between these last two categories of countries. Another analysis, in addition to the per capita income level, takes into account the importance of manufactures as a percentage of the total exports, the per capita value of industrial exports, and the share of "complex products" in these exports. The "simple" industrial products are usually considered to include textiles, clothing and footwear, as well as chemical products which

are basically the result of the elementary processing of primary products; the remaining industrial goods are considered "complex".

The fact is that in recent years some countries of Latin America, Asia and southern and eastern Europe have made rapid advances as producers of very competitive manufactures in the international markets. This phenomenon, viewed by some as being equivalent to "the emergence of two or three Japans" in the trade field, is acquiring ever-increasing importance. These newly-industrializing countries, as they are called, are as follows:

NEWLY-INDUSTRIALIZING COUNTRIES^a

Philippines	Argentina	Spain	Hungary
Hong Kong*	Brazil*	Greece	Poland
India	Mexico*	Israel	Rumania
Iran		Malta	
South Korea*		Portugal*	
Malaysia		Turkey*	
Pakistan		Yugoslavia*	
Singapore*			
Thailand			
Taiwan*			

^aThose marked with an asterisk are considered countries of recent industrialization by the OECD. The rest appear in a Foreign and Commonwealth Office report (1979).

The common denominator among them is a much higher growth potential than that of the less developed countries and, consequently, greater opportunities —not exclusively concentrated in the rural sector— for raising the living standard of the poor sectors. Another trait is the high rate of growth of their industrial exports in the last 15 years and their ever-increasing access to international credit in the last few years. In these circumstances, their development depends much more on international trade and the world capital markets than that of the poorer countries, and their economies are much more sensitive to the trends occurring in the industrialized countries.

It is not surprising that, to maintain economic growth or mitigate the impact of the international crisis on this process, some of these countries have had great need of external financing and have obtained record access to the international credit markets. It must be recognized, besides, that owing to defects in their accumulation processes and the inequalities inherent in their political systems, this external credit was inefficiently and inequitably used by the public and private sectors of many of these countries, thus aggravating the consequences of their external indebtedness.

IV

The external indebtedness of Latin America

The aforementioned trends of the international system combined to produce the excessive degree of external indebtedness observed in the Latin American countries (ECLA, 1983 and 1984; Iglesias, 1984). Thus, in the last ten years these countries' external debt rose more than tenfold to close on US\$ 300 billion, or almost half the external debt of all the developing countries put together. Considering these magnitudes from another angle, it may be noted that whereas in 1970 the Latin American external debt represented slightly less than 12% of the region's gross domestic product, towards the end of 1982 it equalled 30%. At the same time,

through the combined effect of a larger volume of debt and the rise in interest rates, the servicing of the debt, which in 1970 represented around 7% of the value of the region's exports, had risen to almost 40% by the end of 1982. Additionally, as most of the new credits obtained by the Latin American countries came from private sources, the maturities contracted were much shorter than those of 10 years before; thus the proportion of short-term external debt was dangerously high compared with what might have been deemed prudent for commercial credit. It must be borne in mind that, whereas at the beginning of the 1970s around 80% of Latin America's ex-

ternal credit came from public sources, at the beginning of the 1980s a similar percentage came from private sources. It must also be remembered that these debts were tied to fluctuating interest rates, which upset any forecasts that might have been made when contracting them, and abruptly raised the servicing cost of the debt.

The fact that there was a simultaneous decline in the flows of direct foreign investment into Latin America reflects the highly unpredictable nature of the world economy at that time as well as the extraordinary fluidity of the international financial markets.

The volume and characteristics of Latin America's external indebtedness are explained by a combination of international and domestic factors whose relative weight is difficult to gauge. On the one hand, the fact that the external indebtedness had the same impact on countries following very different economic policies would tend to underline the importance of external factors in accounting for this phenomenon. On the other hand, the circumstance that Latin America was more affected in its external sector than other developing countries that had achieved a considerable degree of integration in the world economy, such as those of Southeast Asia, would seem to indicate that domestic policies has an important influence on what occurred in Latin America, though it must be recognized that we are talking about countries with very different economic, social and political structures, which consequently differ greatly in their ability to adjust to the external cycle.

There are three salient factors among those that determined the abundance of external resources available during the 1970s. The first was the impact of the two sharp rises in oil prices, and the ensuing accumulation of financial surpluses in the hands of the OPEC countries, which had to be recycled by the private banking system. The second was the fall in investment and the application of anti-inflationary monetary policies in a recessive context, which caused the industrialized countries to play a less dynamic role than in the past in the absorption of these surpluses. The third was the strengthening of the function of the private banks in this process and the growing use of financial circuits such as lending by banking consortia in the Eurocurrency market (which accounts for more than 90% of

the flows from the capital markets to the developing countries in the last decade), which led to a relaxation of demands regarding creditworthiness, since these are markets that operate at world level and do not need to make a very careful analysis of isolated transactions; thus they considerably increased their operations and reduced their costs, running risks which have today become dramatically apparent. During this period the banks competed with each other in lending the surpluses entrusted to them, giving a satisfactory credit rating to clients who had not qualified before, among them some of the relatively more advanced developing countries.

At the same time, and as a result of the trends described, the demand for international credit in the Latin American countries rose sharply. Many had to mount huge transformation campaigns in order to adjust to the changing conditions of the world economy, whether to cope with the higher oil prices or to make a more efficient entry into the markets without relaxing their struggle against inflation. During this period many Latin American countries sought to transform their economies by changing the incentives offered by the tariff structures and the financial, taxation and social security systems. These processes induced business firms to resort to credit in order to remain in the market if they had suffered from the changes, or to expand if their competitiveness had increased, with the result that pressures were generated which pushed up domestic interest rates, and created a powerful incentive to borrow from abroad, where the interest rates were more favourable. The increase in public expenditure embarked on by some Latin American countries in order to finance expansion plans based on over-ambitious projects with long lead times, especially in the case of the oil-exporting countries, and in other cases the excessive expenditure of the private sector, coupled with a strong preference for consumption and a decline in investment, led to an unprecedented demand for external credit.

It seemed reasonable for the Latin American countries to base their development strategy on external indebtedness during that period, when credits were granted on very flexible terms, with negative or very low real interest rates and long maturities. Indeed, this strategy mitigated for some time the effects of the international reces-

sion on the Latin American countries, so that during most of the 1970s they were able to grow at a much faster rate than the industrialized countries.

Nevertheless, the advocates of these carefree policies of external borrowing underestimated the risk that the fluctuating interest rates and short maturities might raise the debt-servicing costs beyond the countries' short-term capacity to pay, that the permissiveness hitherto displayed by the international banks might cease, and that a period might begin of higher costs and restricted credit.

The fact that during the whole of that time the international financial markets were surprisingly unregulated contributed to the risks. As already noted, the international private banks assumed a dominant role in the recycling of the financial surpluses accumulated during those years, radically reducing the part played by the international financial institutions. Thus, for example, the credit provided by the International Monetary Fund, which in its initial stage amounted to 16% of the value of world trade, represents only 3% today. In the case of the Latin American countries, the amount of the loans authorized by the IDB—as a percentage of their deficit on current account—dropped from an average of 25% during 1965-1970 to 11% during 1975-1980, while the contribution of the World Bank went down from 21% to 12% between the two periods. The diminished role of the public agencies in Latin America's external credit had serious consequences, since the international private banks showed signs of marked instability in the face of the crisis and a lack of long-term vision, reducing their credits and taking advantage of the negotiations facing the debtor countries to shorten the maturities and increase the costs of the debt in terms of interest and commissions, precisely when these countries were in difficulties and despite the fact that these same renegotiations were reducing their own risks.

This brings us to a final reflection, directly connected with the purpose of this paper, which is to show the linkage between Latin America's external indebtedness and the general trends of international policy and economy. It concerns the responsibility that the world community should assume in the face of this problem. Hitherto, the search for formulas to deal with the

crisis has been almost entirely in the hands of the creditors, with little intervention from national monetary authorities and international financial agencies, and with the virtual exclusion of other sectors, whether economic or political. Referring to the interests at stake in the crisis, Donald Regan, Secretary of the Treasury of the United States, said that it was legitimate for American citizens to wonder why they and their Government should worry about the problem of the international debt. Why should they worry because some foreign borrowers found themselves deprived of bank loans or because private banks lost their money? No-one forced them to ask for loans and they should accept the consequences of their decisions, as in any other business. If the United States Government had no other aim than to give money to the borrowers and to their creditors, it would be difficult to justify the use of United States funds in efforts to solve the debt crisis, especially at a time of readjustments in domestic expenditure. But of course the problem and its solution had other aspects, too. First, a further sharp and large-scale contraction in the imports of the less developed countries would be very harmful to the United States economy. Second, if the situation were not handled properly the debtors' difficulties in the less developed countries would become so onerous that they would be tempted to adopt desperate measures to find a way out (statement to the Banking Committee of the United States House of Representatives on 7 April 1983).

The present situation is due not only to the policies applied by the debtor countries but also to the far from rational behaviour of the private credit sources, aggravated by the lack of regulations of the international financial market. Hence the need to recognize that dealing with the crisis is the responsibility of the entire international community.

It is essential that debt servicing in the future should be subject to the development possibilities of the debtor countries and the demands of world economic reactivation, in view of which the renegotiation of existing credits or the granting of new international loans should be subject to new conditions which comply with these objectives. Furthermore, it is necessary that there should be no sudden variations in the willingness of the private bankers to maintain a specific flow

of credit to their clients, and hence they should work in closer contact with the actual debtors, with the monetary authorities of their respective countries, and with the international financial institutions. Finally, these agencies must be given the power to contribute effectively to maintaining the necessary balance between international credit and the normal functioning of the world economy, without neglecting the part that the developing countries are called upon to play in it.

In this context, it is essential to reaffirm the link between credit and trade, which has been greatly weakened by the deterioration in the terms of trade of Latin America's export products during recent years, by the intensity of protectionism and the forms it has adopted in the developed countries, and by the general decay of the rules that governed the international commercial system. Helmut Schmidt, former Chancellor of the Federal Republic of Germany, used

to say on this subject: "Credit creates trade, trade secures credit. Major developing countries' balance-of-payments problems cannot be cured if we shut our markets to them. In many respects the developing countries are now in a position similar to that of the German Reich in the 1920s: Germany could not meet its 'reparation' payments because the allies were not prepared to tolerate German trade surpluses. So Germany could not meet its debt repayments and lost its creditworthiness." (*The Economist*, 26 February - 4 March 1983, p. 29).

It is to be hoped that the international community, in the present crisis, will be more discerning in its treatment of Latin America than it was in the case of Germany after the First World War, and that this will prevent the outbreak of violence which, in new forms, would be the inevitable result of further pressure on the debtors.

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