LONG RUN TRENDS IN THE GROWTH OF DEVELOPING COUNTRIES
(Closing the Gap Between Developing and Industrial Countries)

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During their peak development periods in the 19th and early 20th centuries, the industrial countries grew for the most part at only 1 to 2 percent per year. Their growth was barely positive in the 1910s, and it was negative in the 1930s. Growth rates for the rest of the world were even lower during this time. The high rates of growth achieved worldwide during the last 30 years (Table 1) have thus been as unprecedented as they were unexpected.[1] From a long run perspective, growth has even been high since 1974, particularly for developing countries.

Developing and industrial countries represent a broad income spectrum ranging from the lowest income countries of Africa, South of the Sahara to the high income countries of Northern America, Western Europe and the Middle East. Indeed, the classification of countries into industrial and developing groups or according to any other criteria is necessarily arbitrary. "Levels of development" range

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1. Economists substantially underestimated the growth potential of developing countries during the 1950s. See D. Morawetz, *Twenty-Five Years of Economic Development, 1950-75,* The World Bank, Washington, D.C., 1977. The 1970's petroleum price increases were accompanied by another spate of unreliable forecasts that predicted that it would be impossible to transform the savings of the petroleum countries into productive investment elsewhere, and slow growth by petroleum importing countries.

from very poor, undeveloped countries such as Bhutan or Chad to very highly developed industrial countries.

Income and development levels do not always coincide. The petroleum exporting countries of the Middle East have high per capita incomes, but in terms of development capacity they are still developing countries. Some very poor countries, notably India, have large and sophisticated industrial sectors so that they are in some sense "newly industrializing" or "semi-industrial" countries. Regional differences within countries cut across income and development lines. The Sao Paulo region of Brazil is more developed than Southern Italy. In the spectrum of development generally, growing numbers of the semi-industrial, higher income countries such as Argentina and Singapore, which are still developing countries, have more in common with industrial than with very low income countries.

For analytical purposes, it is, nevertheless, worth grouping countries by categories such as levels of development, income, endowment of natural resources, geographical region, or some combination of these. This paper postulates that developing countries as a group have been catching up with the industrial countries during the last 30 years, and that the "closing of the gap" between poor and rich countries has been accelerating. A new gap, between the slowly and rapidly growing developing countries, may be identified, but although the slowly growing countries are largely very poor countries, this is not altogether so. Some very poor countries have grown rapidly, and some relatively high income countries have lagged behind. The essential factors in growth and catching up have been countries' domestic policies and the liberalization of the international economy. These are discussed in Sections I and II respectively. The paper concludes with a brief review of long run production trends.

1. Long Run Growth Trends

Many factors have been identified at one time or another as principal causes of rapid growth for the last 30 years. These include the vast improvements in technology, the development of "human capital" through mass education, the acceleration in investment and capital accumulation, the structural shifts which took a significant proportion of the work force out of low productivity agriculture

[illegible] productivity manufacturing and service activities, the movement of women from household to remunerated work, and also the [illegible] flows of temporary and permanent immigrants. The remarkable freeing of trade and capital flows and to some extent of migrant [illegible] (discussed in Section 2) has clearly been critical. But the major [illegible] underlying these trends was the focus on social progress. The [illegible] economic crisis had prompted changing social perceptions, [illegible] these led to changed approaches to policy-making. These were strengthened by World War II. The unemployment and social waste [illegible] had prevailed for centuries became unacceptable. Wartime economies had demonstrated that national economic management [illegible] be used in essentially market-oriented systems, and greatly improved policy formulation and administrative capacities were developed in the transition to peace time economies.

During the 1950s and 1960s, most industrial countries were [illegible] up" with levels of productivity and living standards that [illegible] United States had achieved by the late 1940s. Their progress until [illegible] end of the 1960s is well known. Although the United States has [illegible] grown very rapidly by historical standards, some European countries overtook it during the burst of economic activity that [illegible] in the boom of 1972-73. Japan, itself only recently a developing country, became a leading industrial power and continued [illegible] grow relatively rapidly. For other industrial countries, including [illegible] United States, the period of easy growth was over by the late [illegible], so that new goals and policies were needed. Declining rates of productivity growth, rising rates of inflation and unemployment [illegible] the transition, and the lack of appropriate policy responses [illegible] "stagflation". When governments tried to tackle the 1971 [illegible] by traditional, mainly employment-oriented policies, [illegible] industrial economies on both sides of the Atlantic overheated. [illegible] petroleum price increases of 1973-74 greatly exacerbated the [illegible] countries' difficulties in the subsequent cyclical downturn, [illegible] the halcyon years to an end. For the rest of the 1970s, the [illegible] countries nevertheless grew at some 3 percent or faster [illegible] any time before the 1950s.[2]

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[2] The growth rates of industrial countries in the 1970s appear, moreover, [illegible] understated in relation to the 1960s by the emergence of the "black" [illegible]. The increasing emphasis on environmental improvements such as [illegible] controls similarly leads to understatement. Once any initial expenditure

The socialist countries of Eastern Europe found it relatively easy to plan postwar reconstruction and to rebuild their economies on the basis of heavy industry after World War II. In the 1950s, they may have grown even faster than the industrial market economies. By the 1960s, however, it became clear that central planning could not deliver living standards as high as those of market economies, and in the 1970s, the centrally planned economies' growth began to falter so that the official growth rates (Table 1) seem suspect. The failure to use prices that would realistically reflect scarcities, the absence of markets to establish such prices, the failure of most public enterprises to organize production efficiently and economically, and the sheer difficulties of detailed central planning resulted in most of the East European countries lagging severely behind the industrial countries in productivity and living standards, and even falling behind the more rapidly growing developing countries.

Table 1 – Growth Trends in GNP and GNP Per Capita (Average Annual Percentage Growth Rates in 1980 US$ at Official Exchange Rate)

	GNP			GNP Per Capita		
	1950-60	1960-70	1970-80	1950-60	1960-70	[illegible]
Industrial market economies	4.2	5.2	3.2	3.0	4.1	[illegible]
Developing market economies[a]	5.0	6.1	5.1	2.7	3.5	[illegible]
European centrally planned economies	n.a.	n.a.	5.5	n.a.	n.a.	[illegible]
Central surplus petroleum exporters	n.a.	n.a.	8.3	n.a.	n.a.	[illegible]

[a]Excluding capital surplus petroleum exporters, South Africa and China.
Source: World Bank data.

The developing countries' internal pressures for "catching up" with the industrial countries were, in contrast, stronger than ideology, and they were endorsed internationally by the spread of social welfare ideals. Once poverty became unacceptable in a nation

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is completed, the improvements yield a continuing service without increasing recorded output in the GNP sense.

context, inequality among nations also became a national concern, leading to substantial international support for developing countries' growth. But the developing countries represent 75 percent of the world's population and some 150 of its 180 or so countries and territories. Although they performed remarkably well overall and are beginning to close the gap between themselves and the industrial countries, their experience was very diverse.

Regional per capita income differences indicate the wide variations among individual countries' growth trends.[3] Differences existed at the end of World War II. They increased considerably over the past thirty years because most of the low income countries grew only very slowly, while the higher income developing countries were, like some more developed countries, taking part in the "catching up" process. The process continued in the late 1970s. Growth was not, however, merely a function of the level of development. Some very poor countries grew so rapidly that they overtook higher income countries. Korea and the Ivory Coast are notable examples. Differ-

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3. The use of official rather than purchasing power exchange rates, of Laspeyres indices not corrected for quality and preference changes to measure prices, and of indirectly derived Paasche indices to measure output, not only distorts comparisons between levels of income among countries at a given time, but also understates true growth rates, particularly of such countries as the Federal Republic of Germany and Japan which caught up rapidly in the 1950s and 1960s, and of the rapidly growing developing countries. See Irving B. Kravis, Zoltan Kenessey, Alan Heston and Robert Summers, *A System of International Comparisons of Gross Product and Purchasing Power,* The World Bank, The Johns Hopkins University Press (Baltimore and London), 1975 and Irving B. Kravis, Alan Heston and Robert Summers, *International Comparisons of Real Product and Purchasing Power,* The World Bank, The Johns Hopkins University Press (Baltimore and London), 1978, for an indication of the distortions introduced by the use of official exchange rates in international comparisons. Such distortions are not removed by the use of domestic currency growth rates to estimate past growth (see Irving B. Kravis, Alan W. Heston and Robert Summers, "Real GDP Per Capita for More than One Hundred Countries," *The Economic Journal,* No. 88, June 1978, pp. 215-242) for these also underestimate the growth of countries moving from simple, non-monetized to industrial economies. Ongoing work by Kravis, Heston and Summers is seeking to identify the character and magnitude of such underestimation of growth. The catching up process which is underestimated by growth rate measurements, whether in local or international currencies, is fully captured only when countries revalue their currencies against those countries with which they are catching up.

ential income levels and growth rates emerge when countri
grouped by regions (Tables 2 and 3).

Table 2 – Developing Countries' Population and Per Capita Income by Region, 1980

	Population		GNP	
	Million	Percent	Billion $	Percent
Petroleum Importers[a]	1871	55.7	1474.8	59.8
Southern Europe	152	4.5	466.6	18.9
Latin America and the Caribbean	249	7.4	453.2	18.4
East Asia and Oceania	183	5.5	227.3	9.2
Middle East and North Africa	34	1.0	28.9	1.2
South Asia	991	29.5	208.1	8.4
Sub-Saharan Africa[a]	262	7.8	90.7	3.7
Capital Deficit Petroleum Exporters	482	14.4	520.9	20.7
Capital Surplus Petroleum Exporters	27	0.8	199.5	8.1
People's Republic of China	977	29.1	280.6	11.4
Total	3357	100.0	2465.8	100.0

[a]Excludes South Africa.
Source: World Bank data.

Capital Surplus Petroleum Exporters

This group of countries, all small in population terms, co
very high per capita incomes with only modest levels of
ment. Some of these countries only achieved economic indep
in the 1950s, and all grew rapidly in the 1960s when their ex
petroleum were expanding fast. During the 1970s, as their in
rose, they sought to come to grips with their unique develop
problems. They had not yet acquired the administrative capaci
easily manage the high growth strategies which would be nece
they were to enjoy continued high incomes when their petro
and gas resources would be exhausted. They boosted their dom
absorptive capacity by massive immigration from Turkey, Egypt

Table 3 – Developing Countries' GNP and Per Capita Growth by Region (Average Annual Percentage Growth Rates in 1980 US$ at Official Exchange Rate)

	GNP		GNP Per Capita	
	1960-70	1970-80	1960-70	1970-80
...m Importers[a]	5.8	5.0	3.4	2.7
...n Europe	7.2	4.5	5.7	2.9
... America & Caribbean	5.3	5.9	2.7	3.4
... Asia & Oceania	7.8	8.3	4.9	5.7
... East & North Africa	5.0	5.6	2.4	2.7
... Asia	4.2	3.3	1.8	1.1
...Saharan Africa[a]	4.2	2.9	1.7	0.0
...Deficit Petroleum ...	6.5	5.4	3.8	2.7
...Surplus Petroleum ...	n.a.	8.3	n.a.	4.2

... South Africa and China
... World Bank data.

... Middle Eastern countries such as the Yemen Republic, ... and Syria, and Pakistan, India and Bangladesh. They ...theless had to invest heavily abroad in order to absorb their ... productively. However, restrictions on such investment in ...trial countries limited their opportunities for productive invest... while inflation eroded the value of their capital and income. ...rvationist" petroleum production and export policies to ... consumers' energy conservation followed. Kuwait, for ex...ple, can meet its current economic and social obligations from its ...ment income without exporting any petroleum at all. Some of ... countries, led by Saudi Arabia, have nevertheless maintained ... petroleum flows, notably during the Iran-Iraq war, and thus ...ated OPEC price increases. Countries with ample petroleum ...rces, and low domestic absorptive capacities, naturally are ...ted in maximizing long run gains from petroleum by keeping ... so low that substitutes are not developed prematurely though ... so low that substitutes would not be developed at all. As a ...quence of the latter energy shortages, economic and political ... might develop. Some of the capital surplus petroleum ...ers were also interested in protecting their foreign investments

against economic and political crises, but unfortunately this was not feasible.

Southern Europe

Some of the countries in this grouping – notably Greece, Spain and Portugal – have at one time been relatively wealthy. However, industrialization passed them by, so that by the 1950s, they had become relatively low income countries, illustrating what happens to countries that do not adjust to the growth around them. In the 1960s, with improving economic policies, they started to catch up with developing countries, with per capita income coming close to those of lagging industrial countries such as Ireland, and even above them as in the case of Spain. In the 1970s, their catching up impetus floundered for several reasons. Their economies have traditionally been closely linked with those slowly growing countries of Western Europe. Greece has now joined the European Economic Communities and some others are expected to do so.

The Southern European economies were similar to those of European industrial countries in economic and social organization, so that they too found it difficult to adjust to changing world economic conditions. Yugoslavia's particular policy problems arising from federalism and socialist management policies grew as living standards rose. The severe economic management problems which came to a head in Turkey were, however, akin to those of other middle income developing countries, with heavily protected inward oriented production, poor fiscal discipline, an inefficient public sector, and repressed financial sectors.

Southern Europe is the only developing country region that has to date discovered very little petroleum or gas and has poor coal reserves. Petroleum imports had to be high, but exports were not competitive enough to respond adequately to the severe balance of payments pressure created by the rising petroluem prices. Moreover, previously high immigration to Western Europe was declining sharply, so that workers' remittances diminished as petroleum prices rose. Even in Southern Europe, however, a country that had appropriate policies could continue to grow rapidly. Malta, which managed to limit price rises in spite of its dependence on petroleum imports so that tourism and merchandise exports flourished, had an average annual GDP growth rate of some 10 percent during the 1970s.

Latin America and the Caribbean

Latin America has had a longer history of political independence than most developing countries. Argentina and Chile were, together with Australia and New Zealand, among the highest income countries in the world in 1900, and they had taken their first steps toward industrialization by the 1930s. Latin America is richly endowed with natural resources, including petroleum. In addition to the principal petroleum exporters (Venezuela, Mexico, Ecuador, and Peru), Argentina and Bolivia are substantially self sufficient in petroleum, Chile and Colombia have some petroleum resources, and even Brazil has petroleum and coal. The islands of the Caribbean are well developed in terms of human resources, have had relatively high income levels, and are well located to exploit North American product and service markets and tourist potential. But despite a heavy emphasis on industrialization after World War II, overall economic growth in Latin America and the Caribbean has been relatively slow.

The region was heavily influenced by inward-looking economic policies. It was generally believed that developing countries were unable to compete internationally because "the rules of the game" in the international economy were skewed against developing countries; that public enterprises were socially more desirable than private ones; and that industrial development was superior to agricultural growth. In spite of a great deal of commitment to socialism, there was little practical attention to poverty alleviation. The policies that reflected these views led to capital-intensive and high-cost industrialization at the expense of agricultural development, low employment growth and chronic balance of payments difficulties. There was little public finance discipline, with consequent monetary and exchange policy difficulties as inflation took the place of taxation. Large inflows of capital into economies with highly protected manufacturing, and restricted financial sectors accentuated difficulties with resource mobilization and allocations.[4] In the Caribbean, social policies have moved ahead of productivity gains so that high wages make many of the islands uncompetitive. It was difficult for most countries in this

4. For a detailed examination of this and related issues, see W. M. Corden, Chapter 2 and Ronald I. McKinnon, Chapter 3 in J. Cody, H. Hughes and D. Wall eds., *Policies for Industrial Progress in Developing Countries,* World Bank, Oxford University Press, 1981.

region to take advantage of the liberal international economic trends. Those that attempted to do so did it rather inefficiently by offsetting domestic protection by high export incentives. The petroleum rich countries, like the region's other mineral rich countries before them, experienced a bonanza in the 1970s, but found it difficult to take advantage of their high incomes because of the inefficient structure of their economies, particularly as living expectations rose ahead of petroleum receipts. Paradoxically, many of the petroleum importing countries restructured their economies to varying degrees as a result of the shock of the petroleum price increases. Combined with growing internal industrial competitiveness in the larger economies, Latin American countries emerged from the 1970s with less bias against agriculture and greater international competitiveness. Overall then, the Latin American and Caribbean countries, petroleum importers as well as exporters, grew faster in the 1970s than in the 1960s.

East and Southeast Asia

The East Asian market economies have been the outstanding development performers: Korea, Taiwan and Hong Kong which, with Singapore, form the remarkable "gang of four" that have been the fastest growing developing economies in the world. Hong Kong and Singapore are city states with little alternative to export-oriented manufacturing development, but Taiwan and Korea have demonstrated the value of paying attention to all sectors and seeking a balance between domestic and externally oriented policies. Growth has led to declining fertility and this has translated high income growth into rapidly rising standards of living.

The growth of the Southeast Asian countries has also been relatively rapid. They all have rich and varied resource bases so that petroleum exports are not dominant even in petroleum-exporting Indonesia and Malaysia. The Philippines is known to have petroleum and Thailand has gas. The Southeast Asian countries have also pursued relatively balanced economic policies, developing agriculture as well as industry, and exports as well as domestic production, and they now have well developed infrastructure, agriculture, manufacturing and modern service sectors. The East and Southeast Asian countries thus not only grew faster than almost all other economies in the 1950s, but they maintained their lead by increasing their growth rates in the 1970s.

Middle East and North Africa

Petroleum and phosphates have made contributions to growth in North Africa. The resource poor countries (and also Egypt) have benefited from migration opportunities within the region. But performance has otherwise been disappointing. Industrial growth has been slow, very capital intensive and by and large not competitive with either the old industrial countries or the newly industrializing countries of Latin America and East and Southeast Asia. Public ownership of manufacturing enterprises has been largely unsuccessful in dealing with the risks, uncertainties and changes inherent in manufacturing production. Despite some privileged access to European markets under special bilateral country arrangements, agricultural exports have been constrained by the European Community's Common Agricultural Policy, and such constraints seem likely to worsen with the Community's enlargement. Egypt's situation has improved markedly in recent years with the re-opening of the Suez Canal and the export of petroleum. With the exception of Israel, however, the countries of the region have not done justice to their natural endowment and potential.

China

China, the largest of the developing economies, is still an enigma, not only to foreign observers, but to its own analysts. Chinese data now available are so dubious that generalizations are almost impossible. It appears that China, like the European centrally planned economies, found the first stage of putting a war torn country on its feet relatively easy, but it has now begun to face the more difficult problems. Its technology is very outdated, its infrastructure, particularly transport, is very poor and it has practically no distribution or monetary system. Its physical planning and enterprise management are not suitable to its modernization objectives. It will have to become a major exporter in order to purchase modern technology, but its current raw material exports, including petroleum and coal, will be needed for rapid domestic industrial growth. The export emphasis will therefore have to be on the production of labor intensive manufactures. Hong Kong and Macao are already serving as bases, but a substantial expansion is likely to take a decade or so. China is not likely to emerge fully into the international economy until the 1990s.

South Asia

The large poor countries of South Asia came to independence with some relatively well developed human resources, infrastructure and production facilities, but with very low overall productivity levels. Some regions, notably Bengal, are probably the poorest in the world. India's large size and heterogeneity made it difficult to create a meaningful political consensus for rapid growth. Bangladesh, like Pakistan, has had acute political problems from its inception. Development has therefore been very slow and very painful, though not without major progress in some sectors. The 1970s were a turning point in agriculture. Inadequate monsoons in the early 1970s led to very poor harvests and low growth rates, but the effects of changes in agricultural policy in India during the late 1960s were being felt. In the mid 1970s, India achieved self-sufficiency in food and from 1974 to 1980, its growth averaged 5.6 percent despite fluctuating climatic conditions. Infrastructure development, particularly in transport and energy, however, has been slow. The manufacturing sector is large and well develeloped but production has grown at only 4.5 percent a year. High protection and intensive regulation of industry, combined with a great deal of public ownership, has resulted in inefficiency despite the opportunities for competition in the large domestic market. Although India also has a restricted financial sector, in contrast to Latin America, it has followed conservative fiscal and monetary policies, so that it has not been plagued by inflation. Pakistan's agricultural development has also been considerable, and even Bangladesh may now be approaching self-sufficiency. The smaller countries of South Asia also have difficulties, even if these are sometimes of their own making. In contrast to the countries that are catching up, Sri Lanka, for example, is falling behind. During the last 30 years, its per capita income has fallen from about 60 percent to 16 percent of Malaysia's.

Sub-Saharan Africa

The sub-Saharan countries are the poorest, least developed and most prone to political problems. These underlie many of their economic failures. They lack human resources, physical and social infrastructure, and productive capacity. Productivity is almost universally low. The region is well endowed with agricultural resources and with petroleum and other minerals, but the develop-

ment of these has presented problems which inexperienced governments have found very difficult to handle. Where agricultural growth takes the form of enlarging cattle herds, it often leads to desertification. The countries tied to the French franc are quite severely handicapped by the overvaluation of their currencies in export markets. Their incomes are, of course, overstated. The Lome Agreement by no means fully offsets the protectionist effects of the European Community's Common Agricultural Policy. The beneficial effects of the General Scheme of Preference and the Lome Agreement are frequently severely limited, particularly by "rules of origin" and similar regulations. As in Latin America the resource rich countries have been among the most troubled. Some, such as Zaire and Zambia, have experienced problems in absorbing their resource rents. The region's export performance has accordingly been dismal and balance of payments problems are endemic. Petroleum imports are not large, but represent a high proportion of total imports, and of export income because the latter is negligible. A handful of countries – the Ivory Coast, Malawi, Kenya, and recently Botswana, Lesotho and Mauritius – have nevertheless been able to achieve high rates of growth. Their experience is worth studying. This is undoubtedly the region with the most difficult development problems.

An Overview

The developing countries' growth processes are as varied as their cultural, political and economic evolution. While some have found it relatively easy to achieve the political cohesion, human and physical resource accumulation necessary to "take-off" on the development path, others are still far away from rapid progress.

All developing countries faced the same international economic stimuli in the 1950s and 1960s, and constraints in the 1970s, but those with well managed economies were able to take advantage of international trade, capital, and labor movement opportunities, whereas those that had inappropriate domestic policies could not. In the 1970s, for various reasons, the developing countries as a group grew more rapidly than the industrial countries. They have a strong growth motivation to improve living standards. They are better endowed with petroleum resources than industrial countries, even when the capital surplus petroleum exporters are excluded from consideration. Those petroleum importing countries which were

growing strongly were competitive enough to be able to take advantage of the petroleum exporters' rapidly expanding markets which became a source of further growth. They were able to increase their previously low penetration of industrial country markets. The newly industrializing developing countries provided growing markets for other developing countries, particularly for primary products. With strong export performance, many developing countries were thus able to take advantage of high international liquidity to supplement their savings. The labor market opportunities that opened up in the petroleum exporting countries helped several low income countries to break balance of payments bottlenecks.

The economic growth process has been accompanied by greatly improved living standards. The population explosion of the 1950s and 1960s followed a rise in nutrition and health standards with consequent declines in mortality rates. Where economic growth has been rapid, fertility rate declines appropriate to a "demographic transition" have followed. Total developing country population growth is now declining, although total population will continue to grow, adding some 2 billion people to the developing countries' population during the next 20 years. Life expectation has risen and infant and child mortality have declined. Primary education participation and literacy have become widespread in all but the poorest and most isolated countries or regions. Access to higher education has also grown, sometimes ahead of the demand for it. Other social indicators – calorie intake, quality of housing, access to potable water, sanitary facilities and so on – vary considerably from country to country that it is not possible to make any meaningful international generalizations. It is clear that millions of people – perhaps half of the population – are still living in extreme poverty in the low income countries of sub-Saharan Africa and South Asia, and that there are also pockets of very great poverty in some of the higher income countries. Northeast Brazil, the Altiplano areas of other Southern Latin American countries, and Central America are examples. However, wherever there has been rapid and sustained growth, poverty has generally diminished sharply.[5]

5. Data on income distribution (usually household survey based) are as poor as those on physical indicators of standards of living and of little use for temporal international comparisons. A combination of physical und income da-

Examination of the experience of a variety of countries shows that some apparent advantages have not led to radical improvements. Conversely, some characteristics thought to handicap the growth process are shown to be of lesser importance. Being small, "land-locked" or "sealocked", or lacking natural resources all limit development options, but are not serious barriers to growth. Indeed, having rich natural resources can present problems, particularly if complementary human resources are inadequate. Unrealistic expectations generated by the existence of mineral wealth, for instance, may encourage fiscal policies which ultimately inhibit growth. Many richly endowed countries have not grown consistently or rapidly. Large land areas can be handicaps in spite of the gains from economies of scale that major domestic markets provide. India, Pakistan, Bangladesh, Indonesia and Nigeria have had problems because of their large and heterogeneous political bases. In contrast, in the liberal trading environment of the last 30 years, a small domestic market does not necessarily preclude rapid growth. A good location can help, but whereas some small Mediterranean countries have taken advantage of their proximity to Europe, most of those in Central America and the Caribbean have failed to take advantage of the United States' market. Some island economies such as Malta and Mauritius are growing strongly, others are not. Being landlocked is a handicap if surrounding countries are poor. However, the world's highest per capita income country, Switzerland, is landlocked. Malawi and Paraguay have done relatively well in comparison to other countries in their regions despite being landlocked.

Large injections of aid in per capita terms, e.g., in Taiwan and Korea, and access to international capital markets, particularly in combination, have helped many countries grow rapidly, but others have failed to achieve sustained growth despite large aid and commercial capital inflows. Breaking through balance of payments constraints is critical, but the claims made for "outward oriented" industrialization strategies and export growth have sometimes exaggerated the importance of exports in development. Some countries have broken the balance of payments constraint mainly as a result of

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distribution data suggests that poverty has been reduced in terms of absolute and relative numbers in most developing countries, the main exception being in countries which have experienced war, and that standards of living have grown most in countries that have grown rapidly. It is impossible to make adjustments about the impact of growth on income distribution over time or among countries.

emigration leading to significant receipts of remittances. The rapidly growing countries have indeed focused on exports, but they have also introduced social infrastructure policies to overcome human resource constraints, invested in appropriate physical infrastructures, broken rural production bottlenecks, and followed industrialization paths that lead to internationally competitive costs of production. Their common characteristic is a policy balance.[6]

The specific components of such a policy balance vary according to the circumstances of the country, but the objective is simultaneous development of agriculture and industry, of production for export and for the domestic market, and of social and physical infrastructures. An important element of the policy balance has been the maintenance of open economies, especially for the smaller countries. International competition has helped develop competitive export lines but it has also ensured that production for the domestic market is efficient and competitive. Countries which develop industrial production predominantly for a protected domestic market, have let vested interests grow up, which seek to perpetuate their positions, resist competition, change and adjustment. In a liberalized trading environment, competitive pressures force continuous adjustment and lead to the development of a flexible and dynamic economy, a major benefit which has generally been found to exceed the costs arising from fluctuations in the international economy.

Monetary, fiscal manpower and other macro-economic policies are also important components of policy, determining price stability and hence the climate for saving and investment, the utilization of factors of production, and the extent to which special sectoral policies are needed to stimulate growth. Generally, the more balanced and successful the macro-economic policies are, the less need there is to intervene sectorally by production licensing, subsidies and similar policies. That is, bureaucratic interventions can be limited to important issues and they can thus be more appropriately targeted and executed.

The development of social and physical infrastructure in the framework of an open economy contributes to development of

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6. For a more detailed account of the developing countries' experience in the 1970s. see Francis X. Colaco, "The International Economic Environment and the Developing Countries, 1960-90," World Bank, EPDIT Division Working Paper, 1980/14.

competitive production and of human resources, and in itself is a stimulus growth. Reasonably equitable social policies not only lead to the accumulation of human capital but also hasten the transition from the short life expectancy/high fertility pattern to the slower population increase which improves the growth of per capita income.

A few countries, including Singapore and Malaysia, have been successful in accelerating "trickle down" distribution effects by careful attention to access to public goods. The majority, however, paid little attention to welfare. Some, like Sri Lanka, have traded off growth against equity. Some countries achieved neither growth nor equity. In all the rapidly growing countries, governments played an important role in investment in the social and physical infrastructure, and in following policies that made it possible for markets to function. Hong Kong and Singapore, for example, often regarded as laissez faire economies, had very considerable public works, education, health and housing programmes which, together with fiscal, monetary and labour policies, stimulated private sector growth. Indicative planning has played an important role in the development of Korea, Singapore and Taiwan.

Growth-oriented policies are hard to implement successfully without both a degree of political cohesion and some administrative capacity. The latter in turn requires the development of skills and human capital. Political cohesion demands consensus on the objectives of economic development and the means of achieving them. The rapidly growing countries have in fact avoided the shibboleths of the right as well as of the left. A narrow dedication to ideology has had a poor growth record. This does not mean, however, that the objective of efficiency in production is incompatible with equity in distribution, unless of course production decisions are overriden by distributional considerations. There is, evidently, no one path to rapid economic growth. Countries must be selective and choose the one that suits their particular economic, social and political conditions and levels of development. If they do so, they can supplement their domestic resources by taking advantage of the liberal international economy that has come into existence in the last [illegible] years to accelerate their growth. If they do not, even minor international economic fluctuations could exacerbate their domestic problems.

2. International Linkages

The liberalization of the flows of trade and capital after World War II, and a return to the high volumes of migration reminiscent of the nineteenth century, contributed to a rapid spread of technology and gave countries an opportunity to exploit economies of scale and specialization beyond their own borders, thus enabling the developing economies to avoid balance of payments constraints and augment their savings through trade and borrowing. In trade, the principal liberalization impetus came through the General Agreement on Tariffs and Trade (GATT) and the series of multilateral tariff and other protection reductions negotiated under its auspices. The post World War II reductions in capital movement controls culminating in the end of fixed exchange rates played a parallel role in capital markets.

The Movement of Labor

The industrial countries of "new settlement" were traditionally countries of immigration, and still have relatively low density of settlement. The United States and Canada remain the most popular countries of immigration, attracting migrants from the developing countries, particularly from Central and Latin America. The end of the colonial era and associated political settlements also led to some migration to other industrial countries, principally France and the United Kingdom. With full employment in industrial countries in the 1960s, a new type of short-term immigration began to flow to the rapidly growing countries of northwestern continental Europe. Germany and Switzerland were the principal host countries for these "guest workers". Flows of workers among developing economies were also increasing, mainly from slowly to rapidly growing countries. Migration was growing in Africa and Latin America in the 1960s, and the rapid economic growth of the low population petroleum exporting countries of the Middle East led to a new wave of migration from neighboring states and from South Asia. The United States legally admits some 400,000 people annually but estimates of illegal immigrants, mainly from Latin America, who now reside in the United States, range from 2 to 6 and more million people. There were about 6 million temporary migrants in Europe in the mid 1960s, with as many dependents. Estimates suggest that about 2 million people have migrated in Africa (including to South

Africa) and 3 million in Latin America. Immigration into the Middle East involves some 2 to 4 million.

To the individuals concerned, the benefits of such migration evidently exceeded the costs. There have always been more applicants than places for short- and long-term migration, and the pressure for illegal migration has been very strong. In the case of the United States, it has been successful. Although migrants have, for the most parts, come into the work force at the lowest prevailing wages and for the least attractive jobs, both wages and jobs were more attractive than those in their home country. The European host countries also pay substantial social security benefits to the migrants, either together with their wages or as a lump sum on their return home. While living conditions for temporary workers are usually inferior to those enjoyed by the local population, they are rarely as bad as, and are often much better than those in the home country. The workers accumulate considerable savings and they usually return to their home ountry with new skills and sufficient capital to improve their living standards markedly. For permanent migrants, the industrial economies offer an unequalled opportunity to catch up with the industrialized countries' living standards, usually within a generation.

Workers' remittances have been important in breaking the balance of payments constraints in the developing countries bordering the Mediterranean, some Caribbean and Latin American countries, and Middle Eastern and South Asian countries. In 1977, workers' remittances and net private transfers contributed some $20 billion to the foreign earnings of the developing country. Rapid growth in remittances to the countries bordering the Mediterranean took place during the 1960s. More recently, there has been spectacular growth in remittances to the non-oil developing countries of the Middle East. For Yemen People's Democratic Republic, Yemen Arab Republic and Jordan, remittances in 1979 were by far the largest source of foreign exchange earnings. Table 4 shows other countries where remittances were a major source of foreign exchange (i.e., between 10 percent and 100 percent of merchandise export earnings). They assume particular importance in countries such as India, Bangladesh and Egypt which have not been able to formulate and implement appropriate policies to stimulate exports.[7]

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7. Gurushri Swamy, "International Migrant Workers' Remittances," World Bank Staff Working Paper, No. 481, August 1981.

Table 4 – Magnitude of Remittance Inflows into Major Labor-Exporting Countries, 1978-79

		Remittance Inflow $ million	Remittance in[illegible] as % of merch[illegible] exports
Europe and North Africa	Yugoslavia	2938	43
	Greece	989	30
	Turkey	1012	77
	Spain	1752	13
	Cyprus	69	18
	Portugal	1689	69
	Morocco	763	51
	Tunisia	220	25
Middle East	Egypt	1762	89
	Sudan	69	12
Asia	India	1022	15
	Pakistan	1303	77
	Bangladesh	115	21
Africa	Upper Volta	66	60
	Mali	31	33
	Benin (1977)	24	17

Source: Gurushi Swamy, "International Migrant Workers' Remittances: Issues and Prospects," World Bank Staff Working Paper No. 481, August 1981.

All the effects of migration are not positive. It is argued th[illegible] emigration draws away the relatively skilled and enterpris[illegible] workers, relatively few of whom return to inject skills, enterprise [illegible] capital back into the economy. In the country of destinati[illegible] immigration delays technological change, investment, and increas[illegible] in productivity. If true, migration thus contributed to the [illegible]petitiveness of developing country exports in the 1960s and 19[illegible] by avoiding the substitution of capital for labor through [illegible] technology. There are, moreover, social, and political costs [illegible] countries of emigration and immigration, and these, particularly [illegible] countries of immigration, tend to become paramount. Immigrati[illegible] into Europe was slowed down in the early 1970s by the h[illegible] countries for social reasons and similar trends may now be observ[illegible] in the Middle East. Thus, although there seems little doubt th[illegible] migration is a very efficient – perhaps the most efficient – means [illegible] raising living standards for poor people, it is likely to continue to [illegible]

[illegible]ed, and probably will grow relatively slowly in the future. Trade, [illegible] and associated technology flows will have to continue to be [illegible] core of international economic relations.

[illegible]ds in Trade

[illegible]he industrial market economies still accounted for almost [illegible] thirds of world trade throughout the 1960s and 1970s, and the [illegible]th of trade among them was the dominant component in the [illegible]ally rapid trade growth of the period. The developing eco-[illegible] took up nearly a third, leaving a very small share for the [illegible]ally planned economies.[8] (See Table 5).

[illegible]ble 5 – Country Composition of World Exports[a] 1960, 1970 and 1978 (Percent)

	1960	1970	1978
[illegible]trial market economies	62	69	65
[illegible]ean centrally planned economies	8	8	8
[illegible]loping market economies	30	22	27
[illegible]f which capital surplus [illegible]troleum exporting countries)	(4)	(2)	(5)
[illegible]le's Republic of China	b	1	1
[illegible]	100	100	100
[illegible] billion	150	94	1,594

[a] [illegible]rchandise trade and non-factor services. Non-factor service data for the centrally [illegible] economies had to be estimated from very partial information.
[b] [illegible] than 1 percent.
[illegible] World Bank data.

[illegible]he commodity composition of trade has changed sharply. Table [illegible] on merchandise exports indicates that an increase in the share of [illegible]ufactures in the 1960s was followed in the 1970s by an increase [illegible] the share of fuels.

[illegible]he growth rate of global exports peaked in the late 1960s and [illegible]ly 1970s with growth rates of 7.5 percent for 1960-70 and about

[8] For further detail, see A. Schwartz, E. Lutz, I. Jacobsen, and A. Lee, [illegible]ld Trade Flows by Origin and Destination, 1970-90: A Functional Analy-[illegible]," World Bank, EPDIT Division Working Paper No. 1980/8

6.5 percent in the 1970-79. The capital surplus petroleum exporting developing economies' exports increased rapidly in the 1960s when the volume of petroleum consumed and traded internationally increased sharply. Thus, they maintained their share in petroleum price increases in the 1970s. The other developing economies' share of total trade, however, declined, largely reflecting the decline in their share of primary product exports. Supply constraints rather than fluctuating or low commodity prices were thus commonly export problems for many developing countries. Countries like Colombia, Ivory Coast and Malawi did well in spite of fluctuating prices and were able to expand output of primary products, or move into processing activities.

Table 6 – Composition and Growth of World Merchandise Exports by Commodity Groups, 1965, 1970 and 1978 (Percent)

	1965	1970	1978	Real Average Annual growth rate 1965-78
Agricultural products	27	20	17	4.5
Metals and minerals	7	7	4	7.4
Fuels	10	9	20	4.0
Manufactures[a]	57	63	59	8.9
Total	100	100	100	6.9
US$ billion	190	310	1,120	

[a]Standard Industrial Trade Classification 5 to 9 minus 68. Note that this understates the growth in trade in manufactures because processed raw materials which are increasingly traded are included in SITC categories 0-5.
Source: World Bank data.

Latin American countries in particular lost a substantial share of their agricultural temperate climate exports to the industrial market economies in the 1950s and 1960s. This was largely due to the excessive protection of manufactures. The introduction of the European Common Agricultural Policy and agricultural protectionism in the other industrial market economies, however, was also

factor in restricting the markets for a number of products, notably sugar and beef. Latin America also lost some of its share of mineral exports to other developing countries. Exports of petroleum and manufactures did not grow rapidly enough to make up for the export losses in agricultural products and minerals. Thus Latin America's share of world merchandise exports fell from 12 percent in 1950 to 8 percent in 1960 and to about 5.5 percent in the 1970s. The neglect of trade during the 1950s and the 1960s was part of the policy mix that resulted in most Latin American countries' growth lagging substantially behind that of other countries at similar and lower levels of development. Except for petroleum, Middle Eastern and African countries also had relatively poor export performance during the 1950s and 1960s. The South Asian countries' shares of world exports also fell during the period. The East and Southeast Asian countries, in contrast, increased their share of trade rapidly from decade to decade.

Although the most rapid expansion of trade from the 1950s to the 1970s was among industrial countries, trade between developing and industrial countries also grew rapidly. At the end of the 1970s, the industrial countries accounted for some 75 percent of developing country markets, and the developing countries represented about 25 percent of industrial country markets. Intradeveloping country trade, which had lagged in the 1950s and 1960s behind north-south trade growth, began to grow more rapidly in the 1970s with the growing demand in petroleum exporting countries and the relatively strong performance of the more rapidly growing developing countries. The newly industrializing developing countries provided a market for raw materials, and about a third of their exports of manufactures went to other developing countries.[9] (See Table 7).

The developing market economies' share of world exports of manufactures rose from about 10 percent to 20 percent between 1960 and 1977, growing at about 15 percent a year between 1960 and 1973, and at more than 12 percent per year even in the second half of the 1970s. Exports of manufactures began on a small scale in the 1950s when Israel and Hong Kong were the only significant exporters. Taiwan followed in the early 1960s and then Korea,

9. O. Havrylyshyn and M. Wolf, "Trade Among Developing Countries: Theory, Policy Issues, and Principal Trends," World Bank Staff Working Paper No. 479, August 1981.

Table 7 – Regional Structure of Merchandise Trade Flows, 1970 and 1979

	Industrial Market Economies	Developing Market Economies	Centrally Planned Economies
Industrial Market Economies			
1970	72	24	4
1979	68	27	5
Developing Market Economies[a]			
1970	67	25	6
1979	68	27	4
Centrally Planned Economies[b]			
1970	24	9	65
1979	23	13	63
World			
1970	70	24	5
1979	67	27	6

[a]Includes capital surplus petroleum exporting countries.
[b]Includes People's Republic of China.
Source: United Nations trade data.

Singapore and the Southern European countries in the mid
Colombia was the first of the Latin American countries to
facilitate non-traditional exports by a change in exch
policies combined with high export incentives. Brazil follow
the early 1970s, enthusiasm for exports of manufactures had
the new conventional wisdom. Although Hong Kong, Taiwan,
and Singapore continued to dominate the developing
exports of manufactures and even increased their share in the
more than 30 developing countries were exporting over $100
of manufactures annually by the late 1970s. While some
advanced industrial countries such as India continue to lag in
of manufactures, many newcomers are emerging.

Products exported have also widely diversified.
products such as processed food, textiles, footwear and toys
dominate, but there is considerable expansion in primary

processing, basic materials such as chemicals and steel, mechanical components and machinery of various types, and in consumer goods such as china, pottery and glassware.

Industrial countries found it more difficult to adjust to imports from developing countries than to increased mutual trade with them. The developing countries faced protectionist measures against their exports almost from the start despite the industrial countries' trade liberalization movement of the 1950s and 1960s. In fact, there is a continuous history of protectionism against developing countries since the time the first "developing" country, Japan, came on the market with a large volume of low cost products in the 1920s. It is salutary to recall that the trade diversion policies pursued by the United Kingdom, France and the United States in their home and colonial markets in the 1920s were precursors to the protectionism of the 1930s, and contributed to Japan's involvement in World War II. Protectionist measures against Japan were continued as soon as it came back into world markets in the 1950s, and were extended to include the rapidly expanding East Asian exporters by the 1960s.

Industrial countries' difficulties in adjusting to developing country exports of manufactures reflect, in part, the particular characteristics of those exports. Developing countries tend to come in at the bottom end of the market with very low cost products, reflecting their per capita income and correspondingly low wage rates. Once production and marketing problems are overcome by the developing country or transnational corporation entrepreneurs, exports can be increased rapidly because of ample labor supply. For the same reason, it takes time for costs of production to rise, although the growth process eventually does increase per capita incomes and force countries to move into other, less labor intensive products. But this may take a long time, particularly in relatively large countries where pockets of poverty may remain for long periods. In any case, other developing countries whose incomes are still low can come into the export market, again with low costs and wages. Also, in contrast to trade among the industrial countries, the direct impact of developing country exports tends to be on entire industries such as clothing, textiles and footwear, rather than on individual firms which might anyway diversify successfully. Further, these industries tend to employ the least skilled workers, often women who are denied entry into skilled trades and, as secondary income earners, have low geographic mobility. Whereas adjustment is

relatively easy within industry groups such as metal wo glassware, or pottery, which produce a range of product difficult when a whole, large industry employing marginal wor affected. Adjustment is also easier within a transnational co tion's organization. Japan has been particularly successful in ut its large corporations for the purpose of adjustment. The co tions can bear the costs covering as they do a range of activiti when a relatively large industry is being phased out, th efficient and financially weak firms employing the least skill enterprising workers are usually the last ones left produc traditional product. If such firms are geographically concen adjustment becomes particularly difficult because whole begin to decline.

In the 1950s and 1960s, when the industrial countries' was rapid, the adjustment process worked quite well, clothing, textiles and footwear where the labor force charact that make adjustment difficult were concentrated. The dev countries' expansion went almost unnoticed in some industri the industrial economies' production in those industries bein phased out. Some articles of sports equipment in the USA example. The difficulties of adjustment, however, became gr growth in the industrial countries slowed.

Developing country exports of manufactures still have a ly low share in industrial country markets (Table 8) averag than 3.5 percent of apparent consumption of manufactur The share of industrial production is about the same (3.3 Market penetration grew by about 8 percent annually from 1979 (7 percent from 1976 to 1979). The displacement im this growth, together with the impact of developing countr to third markets, were much smaller than those resulti increasing trade among the industrial countries, or from ch technology, consumer tastes, petroleum price increases recession.[10] But trade with developing countries is political

10. For further detail, see the summary of a study of developin penetration of industrial country markets in Helen Hughes and Jean W "Trade and Protection in the 1970s: Can the Growth of Developin Exports Continue into the 1980s?," *The World Economy*, Vol. 4, N 1981.

	Share in Apparent Consumption of:				Growth of Import Shares	
	1970		1979		1970-79	
	All Imports	Developing Country Imports	All Imports	Developing Country Imports	All Imports	Developing Country Imports
Australia	20.8	2.1	24.3	5.3	2.8	12.0
Canada	26.1	1.2	36.3	2.3	3.0	6.6
EEC	18.9	2.7	29.6	4.7	5.3	6.4
Belgium	61.7	5.6	70.7	4.6	1.2	−0.5
France	12.1	2.1	16.0	2.9	3.3	5.0
Germany	19.3	2.3	30.3	4.5	5.2	8.4
Italy	15.1	2.1	29.3	4.8	7.3	9.3
Netherlands	41.2	4.9	53.6	9.0	3.0	7.2
United Kingdom	16.3	3.3	27.2	5.5	6.3	4.1
Japan	4.5	1.3	5.7	2.3	1.8	5.5
Sweden	31.0	2.8	38.7	4.1	2.3	3.5
United tates	5.4	1.2	9.6	3.0	6.6	11.3
Total	10.6	1.7	16.8	3.4	5.1	8.1

Source: Helen Hughes and Jean Waelbroeck, "Trade and Protection in the 1970's: Can the Growth of Developing Country Exports Continue in the 1980's?" The *World Economy*, June 1981.

isolate and so it has often had to bear the brunt of the
countries' willingness to adjust. Such unwillingness is
shortsighted. The long run experiences of countries such as
Spain, Portugal and Argentina, as well as the more recent
of countries such as the United Kingdom, indicate that the
adjustment is put off, the costlier it becomes.

Trade in non-factor services (tourism, contracting,
insurance, etc.) is becoming an increasingly important
world trade accounting for more than 20 percent of world
(Table 9). Developing countries have been successful in
exports, notably in tourism and contracting services.[11]

Table 9 – Non-Factor Services: Shares in Total Exports, 1970,
(Percent)

	1970
Industrial Market Economies	21
Developing Countries[a]	25
World	20

[a]Includes capital surplus petroleum exporting countries but excludes China.
Source: World Bank data.

Debt as an Engine of Growth

At the end of World War II, the former colonial and
powers and other industrial countries acknowledged some
bility for helping the developing countries extricate themselves
extreme poverty, whether for reasons of conscience,
political interest. They began to asist the newly emerging
through grants, loans on concessional terms and technical
Aid flows grew rapidly in the 1950s (in part as colonial grants
transformed into aid) reaching some $10 billion or 0.4 percent
industrial countries' GNP in the early 1960s. Thereafter,

11. A Sapir and E. Lutz, "Trade in Non-Factor Services: Past
Current Issues," World Bank Staff Working Paper No. 410, August
and A. Sapir and E. Lutz, "Trade in Services: Economic
Development Related Issues," World Bank Staff Working Paper No. 480,
1981.

slowly, about 4 percent a year, and while they reached about 1 percent of GNP in Sweden and the Netherlands, for industrial countries as a whole, flows dropped to about 0.35 percent of GNP. The centrally planned economies' contribution to aid has been negligible, but the capital-surplus OPEC countries began to make contributions in the early 1970s, and these became substantial after 1973, reaching more than 3.5 percent of their GNP. The aid impetus slowed in the 1970s, but there were some improvements in its quality. Less aid was given in kind (food aid, etc.). There was a move from loans to grants, particularly for low income countries, and to "forgiveness" of interest and amortization on old loans. The developing countries' successful development effort as well as humanistic concerns led to a somewhat greater concentration of aid on the lower income countries. The tying of aid, which reduced its value to the recipients, however, was continued by most donor countries.

Private capital flows to developing countries were very low, consisting largely of short term trade credits. It was widely thought that developing countries were not creditworthy for longer term capital, but as capital flows were freed from controls in the industrial countries, private long term capital began to flow quite early to the higher income and rapidly growing developing countries.

Private direct investment, that is, in equity form, was the first major form of the flow. Many transnational corporations had links with the former colonial countries, mainly in the exploitation of natural resources, transport, power and other public utilities. But some of these corporations had been closely associated politically with the foreign rulers, and almost all had appropriated high rents from their exploitation of mineral and other natural resources, and monopoly gains from public utilities. The developing economies wanted to appropriate these rents and other gains for themselves, and the transnationals' investment moved to manufacturing and related banking, insurance and advertizing activities that were beginning to flourish with high protection and other incentives. Some countries such as Korea, followed Japan in industrializing almost entirely without foreign investment. In others, principally those in Latin America, Southeast Asia and Africa, foreign investment became an important component of industrialization although generally it accounted for only a small proportion, usually less than 25 percent, of total investment in manufacturing, in all except sub-

Saharan African countries. Thus, despite disinvestment in [illegible] net direct investment flows continued to grow at some [illegible] percent, accounting for the bulk of private flows and about a [illegible] total flows to developing countries in the 1960s (Table 10).

Table 10 – Composition of Net Capital Flows to Developing Countries, 1960-62 and 1976-78 (Percent)

	1960-1962	1976-[illegible]
Official development assistance	59	[illegible]
Other non-concessional, mainly official	7	[illegible]
Private non-concessional	34	[illegible]
Direct investment	(20)	[illegible]
Export credits	(7)	[illegible]
Financial flows	(7)	[illegible]
Total	100	[illegible]
US$ billion	9	[illegible]
US$ billion in 1978$	25	[illegible]

Note: The figures for 1976-78 cover flows from OPEC and the centrally planned [illegible] as well as from the DAC and India, Ireland, Israel, Luxembourg, Spain, [illegible] lavia. For OPEC, the 3-year totals were an estimated $13.6 billion in net [illegible] multilateral aid and an estimated $4.4 billion in net non-concessional flows, [illegible] representing about 9 percent of the entire net flow. For the centrally [illegible] nomies, the figures were $2.5 billion and $3.2 billion, respectively, or about [illegible] of the total. Comparable information on OPEC and CPE flows is not available [illegible] 1960-62.

Source: OECD, *Development Cooperation,* (Paris) passim.

In the 1960s, export credits also began to be available [illegible] more rapidly growing countries. Some were part of aid flows, [illegible] others were from private sources, though sometimes granted [illegible] conjunction with aid funds for such projects as hydro-[illegible] installations. Some were associated with direct investment, and [illegible] were obtained independently. Export credits gave develop[illegible] countries access to additional funds, but often at a cost. In [illegible] such credits were tied to given suppliers whose technology, [illegible] efficient for capital rich economies, was often costly for [illegible] intensive ones. Government interest subsidies, used as [illegible] incentives by the industrial countries, were often only available [illegible]

such products. Developing countries having become exporters of capital goods themselves have had to match such subsidies. Moreover, by the mid 1960s, export credits were being pushed out to the developing countries in such volume that they led to severe repayment problems and "debt crises" in a number of countries. Toward the end of the 1960s, when both the exporting and receiving governments became more experienced in the use of export credits, these problems were slowly overcome. Their use has been revived as the industrial countries began to experience relatively low growth. However, export credits still involve hidden costs for developing countries. Those using them to import face the additional costs of being tied to the suppliers offering the credit, and those who must compete by giving credit as exporters are forced, in effect, to provide subsidies to their clients.

In the late 1960s, the faster growing developing countries began to have access to the then rapidly expanding international capital markets. The loosening of capital flows among industrial countries, the excess of savings over investment in some of these countries, and the particular circumstances that led to the creation of the Eurocurrency markets, came just as the growing developing countries were ready and able to borrow directly from financial institutions. Long established commercial banks and other financial institutions in the industrial countries provided the bulk of the intermediation services required, but developing country financial centres also began to spring up in places such as Singapore. There were considerable shifts from direct investment, to avoid difficulties over equity shares, and export credits, to avoid tying, to purely financial flows. Then in the 1970s, the increase in petroleum prices led to accelerated growth of the international capital market. Many developing countries and the European centrally planned economies took advantage of greatly increased international liquidity to cushion their adjustment to the petroleum price increases. The international capital market was thus able, again quite unexpectedly, to "recycle" the high savings of petroleum exporters and other countries by moving them to countries that, being in the early stages of the catching up process, had low capital stocks and high marginal productivity of capital. The rate of growth of total net private flows to developing countries was, however, about the same: 7 percent a year in the 1970s as it had been in the 1960s. With the move toward positive, and even high interest rates at the end of the 1970s as inflation expectations caught

up with reality, new trends are emerging with a move back into export credits and direct investment.

It is ironical that the complaints of the developing economies' lack of access to capital markets, prevalent in the 1950s and 1960s should by the mid 1970s have turned into a fear that they had accumulated too much debt! Since 1975, it has been argued that the developing countries have borrowed so much that they, or a large number of them, will go bankrupt, one setting off others in domino fashion. It is further claimed that this will shake the world economy and bring on another financial collapse like that of 1929, a view particularly favored at the end of 1979. The banks that have lent to the developing countries are said to be "overexposed" in developing countries so that they too will go bankrupt, in domino fashion, contributing to the collapse of the entire international financial structure. It is argued that even if an international crisis of this dimension does not occur, disaster is nevertheless around the corner because the "developing economies" and "the banks" are now so vulnerable that the international capital markets will stop functioning or, put more crudely, "will stop recycling the petrodollars" and industrial country savings.

It is by definition true that, having acquired access to capital markets, the developing countries have acquired debt liabilities. The question that should be asked is whether these debts are excessive in relation to the productivity in social as well as financial terms of the projects they have financed, and the national income growth of the countries concerned. This is the "solvency" equivalent of a private enterprise's borrowing. It has, of course, been greatly eased by inflation which transferred income from lenders such as the petroleum rich countries to borrowers.

A second legitimate question relates to the management of the debt and its servicing, and related balance of payments issues. This is a "liquidity" issue. The developing countries again had these problems eased because the initial reaction to accelerated inflation was to allow interest rates and other costs of borrowing to lag behind inflation. The gradual shift to positive interest rates at the end of the 1970s led to a build up of interest rate obligations for the early 1980s, but these will stabilize, or decline if inflation drops. The liquidity of the private market has made for smooth refinancing facilities in contrast to the difficulties of rescheduling debt from official sources, so that, for strong borrowers with well established

relationships with lending institutions, the maturity terms of debts have not been of very great concern. The growth of workers' remittances and the continuing growth of exports has meant that debt service obligations could be met.

Thus, although the developing countries' debt has been increasing – they owed nearly $400 billion at the end of 1979 – for developing countries as a group, there is no "debt problem". The ratios of debt to exports and to GNP increased in the 1970s, but they are still relatively low. Debt to reserve ratios have been falling as heavy borrowers have increased their reserve levels for debt management purposes. Debt service ratios have risen, but this in part reflects the shift from direct to indirect financing. Capital service ratios that include direct investment service have hardly risen at all. Banks are interested not in getting their money back, but in earning interest on it, and refinancing opportunities therefore continue to be favorable. It is the interest service ratio that is most relevant to the developing countries' situation, and this is still very low (Table 11).

Borrowing is highly concentrated in a relatively small number of middle income countries, with 31 countries accounting for 80 percent of total debt and 90 percent of the debt service. Among these, Brazil ($52 billion), Mexico ($34 billion), Spain ($20 billion) and Korea ($15 billion) are the largest borrowers, accounting for almost a third of all debt. With the exception of Korea, they are also among the largest recipients of private investment. Other countries with debt of more than $10 billion include Algeria, Egypt, Indonesia and Venezuela. These are all petroleum exporters. India, with a debt of $16 billion, almost all on concessional terms, is the only large low income borrower.

Countries such as Zaire, Jamaica and Turkey, which have run into severe debt servicing problems, are not large borrowers. Their debt problems are really signs of general economic management problems which lead to low returns on investment and balance of payments difficulties. Most of the large borrowers have gained access to international capital markets because of their domestic growth and their export performance, and their management of reserves and other aspects of the balance of payments. In favorable circumstances, even relatively high debt service ratios of 30 percent or more are manageable. It should be noted that countries such as Canada and Australia sustained higher rates of borrowing in the late 19th and early 20th centuries. Debt, indeed, has also stimulated growth

Table 11 – Developing Country[a] Debt and Debt Service Indicators,[b] 1970-1979 (Percent)

Indicators	1970	1974	1977	1978	[illegible]
Debt/GNP	15	16	21	23	[illegible]
Debt/Exports	98	77	100	108	[illegible]
Debt/Reserves	321	186	270	271	[illegible]
Debt Service Ratio[c]	12	12	14	18	[illegible]
Interest Service Ratio	4	4	5	6	[illegible]
Capital Service Ratio[d]	18	16	18	21	[illegible]
Memo Item					
Total Debt (U.S. billion)	61	110	250	314	[illegible]

[a]Includes all developing countries except (i) the capital surplus petroleum exporters, and [illegible] countries for which reliable time series data are not available (Afghanistan, Bahrain, [illegible]wana, Burundi, Comoros, Guinea, Iran, Iraq, Lebanon, Lesotho, Liberia, Maldives, [illegible] Papua New Guinea and South Africa).

[b]Total developing country debt to total GNP, exports and reserves of all developing countries.

[c]Redemption and interest payments as percentages of merchandise exports, non-factor service receipts and factor services (including emigrant remittances and other private [illegible]fers) earnings.

[d]The debt service ratio plus profits and dividends (including profits on direct investment) [illegible] the numerator.

Source: World Bank data.

indirectly. Countries that have large debt must continue to grow and to export. They have to avoid the costs of highly protectionist policies.[12]

The banks operating in the international sphere have also been sound on the whole. Most refinancing arrangements have been made on mutually beneficial terms, and losses have been negligible. The developing countries accounted for about half of all international borrowing in the late 1970s, but their borrowing represented only a small proportion, certainly less than 10 percent of total global capital flows, if the internal industrial market economies' capital flows are

12. N. Hope, "Developments in and Prospects for the External Debt of Developing Countries," World Bank Staff Working Paper No. 483, September 1981.

included. Excessive government guaranteeing has led to some marginal lending, for example, in sub-Saharan Africa. Some uneconomic lending has also been evident where the existence of strong political forces increased the likelihood of support for countries in trouble. But such borrowing has been marginal to the system as a whole. Particular countries and banks may be expected to run into trouble in the future, as they have in the past. Capital market forms will undoubtedly continue to evolve. Nevertheless, the overall situation is healthy and favorable to developing country growth.

3. The Long Term Outlook

Economists are congenitally myopic, always fighting yesterday's battles. This is the reason why the notion persists that the gap between industrial and developing countries continues to widen, primarily because of the international environment's hostility to developing countries. The use of official rather than purchasing parity exchange rates also helps to perpetuate the myth. Translating the 1960 to 1980 growth trends from official exchange rate into purchasing power parity, and extending the trend toward the year 2000, indicates in fact that the "gap" has stopped growing. For some developing countries, narrowing of the gap started in the 1950s and 1960s. The 1970s' continuing acceleration of many developing countries' growth was the turning point for many others. This does not, of course, mean that income disparities between rich and poor countries are diminishing rapidly enough, or that serious development problems do not remain for developing countries. The case for direct assistance to very poor countries on a liberal and significant scale remains as strong as ever. Given the role of the international markets in facilitating the growth of countries wanting to take advantage of international trade, labor and capital flows, the case for maintaining and further liberalizing the international economy remains even stronger. Overall, the outlook for developing countries seems more optimistic than it was 30, 20 and even 10 years ago (Table 12).

Although the developing countries' per capita incomes would still be substantially below those of the industrial countries even in the 1990s, a considerable number of developing countries would be "catching up", and some would be overtaking the slowly growing industrial countries. In a reversal of the situation existing as recently

as 1960, more than half of the world's output is likely [illegible] produced in developing countries by the year 2000.

Table 12 – Shares of World Population and GNP (Percent)

	Market industrial economies	Centrally planned industrial economies	Capital surplus petroleum exporting economies	Devel[illegible]
		Population		
1960	19	11	1	[illegible]
1978	16	9	2	[illegible]
2000	12	8	2	[illegible]
		GNP at official exchange rates		
1960	68	13	1	[illegible]
1978	60	16	3	[illegible]
2000	50	16	4	[illegible]
		GNP at purchasing power parity exchange rates		
1960	54	15	1	[illegible]
1978	47	16	2	[illegible]
2000	33	11	3	[illegible]

Source: Based on the World Bank data for the 1950s, 1960s and 1970s and data [illegible] from Irving B. Cravis, Alan W. Heston and Robert Summers' project on [illegible] ing power parity (see "Real GDP for More Than One Hundred Countri[illegible] *Economic Journal,* June 1978) and Robin Marris' project on "Catch[illegible] Down or Convergence? Statistical Observations on 25 Years of World [illegible] Growth in the Light of Kravis Numbers". The 1978-2000 figures are [illegible] tions of 1960-1978 trends. Note that the centrally planned economies' [illegible] are derived from official data which may be subject to revision.

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