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Preface: Changing Perspectives on Latin-American Trade

Werner Baer and *Malcolm Gillis**

This volume contains papers and comments presented at the conference "Trade Prospects Among the Americas: Latin-American Export Diversification and the New Protectionism," which was held in São Paulo, Brazil, 23–26 March 1980. The conference was cosponsored by the Fundação Instituto de Pesquisas Economicas (FIPE) of the University of São Paulo, the National Bureau of Economic Research (NBER) of Cambridge, Massachusetts, and the Bureau of Economic and Business Research of the University of Illinois at Urbana-Champaign, with financial support from IBM World Trade Americas/Far East Corporation and the Central Bank of Brazil. This was one in a series of conferences on Latin-American economic issues that the NBER, with IBM support, has helped organize. The conference was organized by Malcolm Gillis, Institute Fellow at the Harvard Institute for International Development and representative for NBER, and Carlos Longo, and the proceedings were edited by Werner Baer and Malcolm Gillis.

The principal focus of the conference was upon trade relations between Latin America and the advanced industrial countries, particularly the United States. But in addition, opportunities for and constraints upon intra-Latin-American trade were examined. The time horizon of the discussion extended beyond current questions to problems likely to be of significant concern for the rest of the decade of the 1980s. Some of the papers in this volume are primarily empirical in character, others focus upon theoretical considerations.

The editors expect that the papers included in this volume will be of substantial interest to a variety of constituencies, ranging from trade and Latin-American area specialists in academia, to public officials in both North and South America, and to that part of the business community concerned with hemispheric trade and development issues.

AN OVERVIEW

In the past decade, there has been a palpable shift in trade policies within most Latin-American countries toward greater reliance on export-led growth. For a long period, Latin-American countries pursued import-substitution industrialization policies, in many cases closely geared to autarkic goals. Beginning in the 1960s, policymakers in most of the nations in the region, particularly the larger ones, began to view such inward-looking strategies with growing reservations, as the contradictions inherent in this approach became steadily more evident. One of the major contradictions was, of course, that policies of vigorous import substitution often led ultimately to more, not less, national vulnerability to shocks and cycles generated in the world economy. Further, inward-looking strategies involving heavy use of capital (the relatively scarce factor of production) did not, by and large, yield the gains in employment and distributional equity foreseen by early proponents (both within and outside Latin America) of import substitution. In addition, the vestiges of inward-looking approaches led to persistent deficits financed by external borrowing and, occasionally, to the threat of default. Often the process culminated in loss of considerable degrees of freedom in the conduct of national economic and social policy.

However, the legacy of the import-substitution era was not by any means wholly unfavorable. In particular, the learning process inherent in the import substitution experience proved useful, as several countries gained valuable production experience essential for competing in world markets. This consideration, together with the growth limitations imposed by the size of internal markets, suggests that further shifts toward a more trade-oriented development strategy may be both feasible and desirable, as some countries in the region have already begun to demonstrate. One other consideration strongly indicates that such a shift will be indispensable: the very rapid recent growth of external debt among countries in the region. The servicing and amortization of very large debt obligations will eventually require sustained growth in export earnings if income growth is to proceed without severe dislocations, and at a pace required to meet basic social goals of Latin-American societies. In recent years, rates of income growth in Latin America have slackened considerably from those recorded from 1966–75. During this decade of peak growth performances for the region, total GNP increased at an average annual rate of 6.4 percent, as reported by the World Bank. But regional income growth declined to 4.7 percent in 1977 and to only 3.9 percent in 1978 [1]. Although rates of growth as high as those experienced from 1966–75 will not guarantee that many Latin-American countries will be successful in dealing with major social problems of income distribution, employment, and disease, growth at rates as low as those observed since 1975 offers even more limited opportunities for resolving such problems. Provision of conditions necessary for expanded and diversified export

earnings is, therefore, in the mutual interest of both Latin-American and capital-exporting nations.

The external debt issue is a matter of both immediate and longer-term concern to both constituencies. Recent developments in Latin-American borrowing, coupled with palpable resurgence of protectionist sentiment in the countries of the industrial North and the large jump in world energy prices in 1979 provide ample basis for the pessimistic forecasts of growth in the region. That the debt of Latin-American countries (exclusive of softer-term official transfers) has been increasingly rapid in recent years is well known. The approximate dimensions of this growth are less widely perceived. During 1974, total new external debt obligations of Latin-American countries contracted in international private capital markets was recorded by the World Bank at $4.4 billion [2]. For the year 1977, such market-term obligations (including foreign and international bonds as well as publicized Eurocurrency credits) increased by $11.7 billion, a figure which probably significantly understates actual growth, since many large Eurocurrency credits are not publicized. Of the latter amount, Mexico and Brazil together accounted for nearly two-thirds. If growth in external debt of Latin-American countries proceeded throughout 1978 at the same pace as in the third quarter of that year, total new obligations on market-term debt contracted in 1978 would have grown by nearly $18.0 billion, which is more than four times 1974 borrowings. These numbers imply compound annual growth of more than 40 percent per annum, a rate far in excess of the growth in gross export earning, not to mention growth of current account surpluses, in the region. The heavy Latin-American borrowings in the past four years, coupled with debt outstanding prior to 1974, had by early 1979 resulted in a stock of private external debt of a size few would have predicted in the early 1970s. By mid-1978, Brazil alone owed no less than $25 billion in private loans (out of a total of $37 billion in total external obligations). By the end of 1979, the Brazilian finance minister was reported to have placed that country's total external debt as close to $50 billion, at a time when Brazil was still trying to digest a more than 100 percent increase in prices of imported oil.[1] Finally, such poorer countries as Peru and Bolivia were faced with severe problems in coping with external debt obligations in excess of $5 billion, in the former case, and perhaps half that in much smaller Bolivia.

Clearly expansion and diversification of exports from Latin-American countries will be essential if large de facto defaults of the types experienced in 1979 by Turkey and Zaire are to be avoided in the 1980s. The question is whether world markets will permit sufficient scope for the requisite expansion and diversification, and whether Latin-American economies can be reoriented rapidly enough to make this possible, export markets permitting.

It is possible that the experiences of a small group of Asian nations from 1960–78 may be of some relevance for many Latin-American nations that have

already begun to reorient trade strategies. The economic performances of Korea, Taiwan, Hong Kong, and Singapore had been widely extolled by Western observers even well prior to 1977, before Jagdish Bhagwati first applied to them the sobriquet "Gang of Four." Clearly, all of these nations belong in any list of "superexporters" of the 20th century.

That the export experience of these countries has been little short of phenomenal is not in question. Indeed, in 1976, *each one* of the Asian superexporters had manufactured exports that exceeded the sum total of manufactured exports of all Latin-American countries together [4]. However, the relevance for other nations of the experience of the "Gang of Four" for other countries is often debated. For example, it is typically argued that Singapore and Hong Kong represent the most unusual of special cases, given the "untypically small" populations of both city-states. Further, it is often claimed that the experiences of both Korea and Taiwan furnish little basis for useful generalizations, because in both cases perceived dangers from potential aggression have allowed tight military control of otherwise fractious societies, so that development could proceed in an atmosphere of political stability. There may be something to be said for these views.

In addition, there appear to have been siguificant differences in the earlier strategies of Import Substitution Industrialization (ISI) followed by the superexporters on the one hand and the larger Latin-American countries on the other. Latin American-ISI investments in manufacturing were aimed at the large, protected internal markets, especially in Brazil, Mexico, and Argentina. Whether with early emphasis on exports multinationals would have initially entered manufacturing sectors in the region in the same massive way is unknowable. But when countries in the region did begin to shift toward export diversification, the multinationals already had substantial excess capacity from large investments made during the ISI stage; it became feasible for policymakers to reorient foreigu and domestic firms toward the external market.

There are, therefore, a number of reasons why the experiences of the Asian superexporters may be of rather limited relevance to Latin America. Nevertheless, it may be no less appropriate to seek useful generalizations on development and trade from the experiences of relatively small Singapore and Hong Kong more than from such untypically large nations as India or Indonesia, both of which have furnished ample grist for the economist's mill. In any case, Hong Kong and Singapore are not that small, in terms of population. Of the 92 LDCs listed in the World Bank's 1979 *World Development Report*, 25 are smaller than Hong Kong (with 4.5 million) and 11 are smaller than Singapore; and surely military-dominated governments in much larger Korea and Taiwan have a large number of counterparts in the world, including Latin America.

Finally, the nature of ISI in both Korea and Taiwan may not have been that different from that of the larger Latin-American countries. To be sure,

the relative importance of foreign direct investment in manufacturing was much smaller in Taiwan and Korea, particularly the latter. But in both Asian countries development efforts prior to the mid-1960s were strongly geared to import substitution, and the initial spurt in the rapid transformation to export-led development in both countries in the late 1960s was made possible by substantial excess capacity in industries originally established for import substitution purposes.

One major generalization that does seem of some relevance to would-be superexporters in Latin America is that robust expansion of manufactured exports from LDCs depends upon more than "getting the prices right." While the influence of incentives flowing from reforms involving major adjustments in basic macro prices (exchange rates, interest rates, energy prices, and so on) is generally adjudged to have been a necessary condition for the successful export drives of each of the Asia superexporters, nonprice factors may have been no less important. Such "nonprice" factors as appeared to have been operative in the Asian countries include extensive market research, readiness to accept and implement marketing innovations developed elsewhere when advisable (and to foster indigenous innovations when necessary), heavy emphasis on quality control, timely delivery, augmentation and modernization of port facilities, removal of impediments (such as lengthy customs procedures) of access to imported raw materials incorporated into export, and superior deployment of organizational skills.

David Morawetz [3], among others, views failure to confront these nonprice factors as an important part of the explanation for the low share of Latin-American countries in world markets for manufactured exports. Problems in marketing, quality control, punctuality of delivery, port procedures, and low worker productivity have not been widely perceived, much less adequately resolved. Until such barriers are sufficiently eroded, prospects for rapid export growth are not bright, particularly since nonprice factors tend to become steadily more important as Latin-American countries begin to move away from the export of standardized products such as yarn and semiprocessed foodstuffs and into more sophisticated, nonstandardized lines such as garments geared to fashion, specialized capital goods, and more fully processed foodstuffs.

Expansion of Latin-American exports may encounter other difficulties as well. Part of any growth of Latin-American exports would have to come at the expense of the Asian "superexporters," not noted for passivity in the face of threats to their export markets. In addition, there is now the prospect of reentry of two poorer but populous Asian countries, China and Indonesia, into a variety of markets for processed natural resources and manufactured exports. Although part of the needed growth may be absorbed through intra-Latin-American trade, a still larger part will challenge European capacities to transform, and the remainder will pose additional adjustment problems for the US economy.

The conference approached the range of associated issues sketched herein from several perspectives. The comprehensive paper by Donald B. Keesing provides a critical appraisal of past Latin-American development policies with regard to their impact on the region's position in the international economy; he also provides alternative international scenarios within which Latin-America's export growth may take place. Keesing feels that Latin-America's export performance was weak because policies were biased against them, especially nontraditional exports. The principal remedy offered is strong emphasis on policies which could set the prices right, that is, making the export sector more competitive.

A number of contributions deal with the region's primary exports. F. G. Adams, J. R. Behrman, and M. Lasaga, examine UNCTAD-types of price stabilization programs for nonfuel primary products. They conclude that these are not likely to solve Latin-America's trade problems. Comparing the gains with the costs, the net positive impact is found to be very slight. Of more general interest, they present an integrated econometric model designed to explore the impact of the commodity problem on goal attainment in one particular country, using copper in Chile as a case study. Raymond Vernon considers the role of Latin-American state enterprises as exporters, especially of such primary materials as oil and iron ore. He reviews their advantages over the domestic private sector in gaining access to markets and in international bargaining, and also considers their drawbacks in establishing production facilities abroad. He also distinguishes between prospects for two types of state-enterprise-manufactured exports: standardized and unstandardized products. Among his conclusions are that the former type of export, particularly processed raw materials, faces a volatile and uncertain market, and that efforts to expand the second type of export may succeed if state enterprises are given enough freedom to develop arrangements that allow them to be more firmly linked to markets in importing countries.

One paper deals with agricultural exports. Adolfo Figueroa presents an analysis linking increased income concentration and "derived rural income." He finds that the latter tends to decline as income becomes more concentrated. The situation of the rural sector is worsened even more, he maintains, by the decline of Latin-America's share of world trade in agricultural products and by the growth of food imports for the urban sector. Thus the countries have lost ground where they supposedly should have a comparative advantage — food products. As a consequence the agricultural sector's role in Latin America seems to be changing. Instead of providing both foreign exchange and cheap food, the emphasis is increasingly on the former. The role of traditional agriculture has, therefore, been largely reduced to the maintenance of a cheap rural labor force, some of which eventually migrates to the cities.

A paper by Abel Beltran del Rio focuses on a country "blessed" with oil — Mexico. He begins by contrasting the recent Mexican experience in coping

with a surge in oil export revenues with that of several countries in the Persian gulf. Beltran del Rio identifies both the benefits and costs that may be derived from oil windfalls. The nature of the former is fairly obvious; the latter includes structural imbalances resulting from too rapid growth by too many sectors simultaneously. In particular, inflationary pressures prove difficult to contain. Finally, he examines likely oil policies in Mexico through 1990 and traces their effects on major macro magnitudes.

Two authors consider policy reactions to external shocks. Bela Balassa deals with the reaction of three Latin-American countries to the shocks of the mid-1970s. He finds that Brazil maintained a rapid growth rate in the face of an adverse balance of payments and still promoted further import substitution; this resulted in accelerated inflation and increased foreign indebtedness. In Mexico the internal shock of an overambitious public expenditure program dominated the external shock, resulting in unsustainable balance of payments deficits and considerable socioeconomic unrest. Uruguay, Balassa maintains, used the impact of the external shock to reform the country's incentive system, leading to rapid export growth and expansion.

A paper by Eliana A. Cardoso examines external disequilibrium in Brazil over the 30-year period 1950–79. She contrasts the Brazilian experience with many devaluations over most of that period with the results of the "maxi-devaluation" of late 1979. Her analysis of the burden of exchange rate adjustments throws doubts on the effectiveness of the latter in dealing with the balance of payments deficit due to strong internal cost responses. She argues that devaluation can improve the trade balance in the short run at the cost of a reduction in the real wage of unskilled labor, as long as unskilled can substitute for skilled labor. She demonstrates this through the use of a model where an imported intermediate good is used for production of a good that is consumed at home and abroad.

A contribution by Miguel Urrutia deals with Colombia's participation in the Andean Group since the inception of that organization in the late 1960s. Colombia is widely perceived, both within and outside the Andean Group, as both a prime beneficiary of expanded intra-Andean trade and a principal supporter of the group's economic objectives. Urrutia argues that neither perception is valid: Colombia has derived only marginal trade benefits from the Andean Pact, and has remained as a member primarily for political rather than economic reasons. He also furnishes an insider's view of how internal decision processes in Colombia have governed the nature of the country's involvement in the Andean Group over the decade of the 1970s.

Gustav Ranis's paper compares the development and trade strategies of East Asian superexporters and Latin-American countries. As in other previous articles by Ranis, emphasis is placed on the important distinction between "export promotion" programs characteristic of much of Latin America, and "export substitution" as typified by policies followed by Korea, Taiwan, Singa-

pore, and Hong Kong since the mid-1970s. Export promotion involves the selective encouragement of particular industries, featuring ad hoc measures undertaken in the absence of general changes in the structure of policies affecting trade. Export promotion is, therefore, best viewed as an effort involving grafting of still more controls onto an elaborate latticework of policies required to effectuate import substitution. By contrast, *export substitution* requires fundamental policy changes, not least of which is the dismantling of most of the policy superstructure built up under the drive for import substitution, and employs a strategy of general, as opposed to selective, reorientation of production. Few Latin-American countries opted for this path in the 1970s.

Two papers discuss the reaction of developed countries to Latin-America's export drive. Rachel McCulloch focuses on the implementation of the General System of Preferences (GSP), the Tokyo Round of Multilateral Trade Negotiations, and the growth of protectionist pressures in industrial countries. She shows that neither preferential access under GSP nor lower tariff barriers has been a major force in explaining the growth of the region's exports. Rather, the most important determinant is the business cycle of industrial countries. Her analysis also leads to the conclusion that Latin America would benefit more from MFN (most favored nation) trade concessions than from preferential trade agreements. Finally, Latin-American countries (and those of the LDC world in general), which have in the past been passive beneficiaries of trade concessions, would benefit from more aggressive collective trade negotiations in which they would offer their own reciprocal concessions.

J. N. Finger analyzes recent US responses to dumping by foreign private firms and to subsidies to exports by foreign governments. Both are examples of less than fair value (LFV) mechanisms. Among various findings, Finger notes that LFV complaints were filed against a significantly lower proportion of US imports from Latin America than from developed countries. He also provides insights into the types of strategies that developing countries in general, and Latin-American countries in particular, might employ in order to exercise more influence on the outcome of LFV complaints.

The final paper by Millard Long focuses on the rapid buildup of external indebtedness of Latin-American countries in the period 1972–80. He first traces both the reasons for growth in the debt, and difficulties in devising appropriate ways for measuring it. He then utilizes a simple model to explore future debt growth under various scenarios. In addition, Long raises a number of methodological issues and argues that tools used by economists for analyzing the external debt have lagged well behind developments in the increasingly important market for debt.

NOTES

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1. These figures refer to 1976. See [3].

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2. ———, *Borrowing in International Capital Markets: Foreign and International Bond Issues, Publicized Eurocurrency Credits*, Document EC 181/783 (Washington, December 1978).

3. David Morawetz, "Why the Emperor's New Clothes Are Not Made in Colombia" (Washington: IBRD, 1979), Table 4.1, p. 82.

4. *World Business Weekly*, "Latin Debt Makes Bankers Uneasy," 17 December 1979, p. 51.