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Chapter 1

Trends and Phases in the Colombian Economy and Its Foreign Trade and Payments, 1950–72

In this chapter, major trends in Colombian foreign trade and payments occurring mainly between 1950 and 1972 will be reviewed, with sporadic discussion of events occurring before and after that period. Contemporary developments in the rest of the economy will also be discussed, but more selectively. Breaking a sector away and analyzing it apart from its proper general-equilibrium setting is no less arbitrary than cutting off the historical flow with starting and finishing dates for the study. But both prunings will, it is hoped, help yield richer fruit.

Possible subdivisions of the 1950–72 years will also be examined here. In the Colombian setting, one scheme of division readily suggests itself, based on the behavior of the dollar coffee price which, simplifying somewhat, may be taken as exogenously given to the country. The discussion of trade and payments policies can also be organized around four-year presidential terms, which since 1958 have followed the constitutional pattern foreseen in the National Front political agreement between the Conservative and Liberal parties. Finally, changes in foreign economic policy can be traced with the help of the phases devised by Jagdish N. Bhagwati and Anne O. Krueger and described in Appendix A. Each of these schemes will be used here, and their interconnections will be explored.

AN OVER-ALL VIEW: GROSS DOMESTIC PRODUCT AND ITS DISTRIBUTION

The postwar growth of the Colombian economy, while not spectacular, has been respectable. Table 1-1 shows one measure of long-term growth, yielding

TABLE 1-1

Average Annual Growth Rates and Standard Errors of Key Colombian Domestic Variables, Selected Periods,[a] 1950–72

(per cent; figures in parentheses are standard errors)

	1950–72	1950–56	1956–67	1967–72
Real gross domestic product at	4.75	5.23	4.57	6.08
market prices	(0.07)	(0.22)	(0.09)	(0.06)
Primary production	3.36	2.86	3.06	3.84
	(0.05)	(0.21)	(0.12)	(0.29)
Manufacturing	6.11	7.25	5.68	7.62
	(0.08)	(0.33)	(0.10)	(0.24)
Construction (value added)	5.72	12.85	3.21	6.29
	(0.41)	(1.88)	(0.75)	(0.68)
Services, Type I	5.48	7.43	5.64	7.58
	(0.16)	(0.68)	(0.33)	(0.16)
Services, Type II	5.00	4.26	5.22	5.98
	(0.07)	(0.14)	(0.10)	(0.15)
Real gross domestic fixed capital	3.61	11.41	2.64	7.52
formation	(0.47)	(1.97)	(0.90)	(0.85)
Volume of capital goods	0.76	13.32	0.60	8.01
imports (BdlR)	(0.81)	(2.89)	(1.93)	(2.03)
Production of manufactured	14.25	17.25	12.88	19.55
capital goods	(0.49)	(1.31)	(0.98)	(2.39)
Construction and building	4.87	9.44	2.99	5.37
(investment)	(0.32)	(1.89)	(0.57)	(0.66)
All investment in machinery	2.36	13.10	2.40	10.41
and equipment	(0.74)	(2.67)	(1.72)	(1.66)

SOURCE: Data obtained from BdlR-CN (see Appendix C for explanation of abbreviations used in this book). "Primary production" includes agriculture, livestock, fishing and hunting, forestry, and mining. Services, Type I includes commerce, transport, communications, electricity, gas and water, and banking and insurance. Services, Type II includes housing, government, and personal services.

METHOD: Growth rates were estimated by fitting a regression of the form $\log Xt = a + bt$ to the basic data, where Xt refers to the relevant variable, and t to a time trend. The coefficient b yields the growth rate; its standard error provides a measure of instability for different variables covering the same period of time. Note that the subperiods overlap one year, e.g., 1956 and 1967 observations appear twice in the subperiod regressions, but only once in the regression for the whole period 1950–72. This and other reasons, related to sharp breaks in trends, imply that growth rates for the whole period need not fall within the range of growth rates obtained for the subperiods, although that is usually the case.

Measures of instability, other than the standard error of the trend coefficient, are of course possible and can yield different instability rankings. For example, the standard deviation of year-to-year growth rates will be larger, and in different proportions for different variables, than the measure shown in this table.

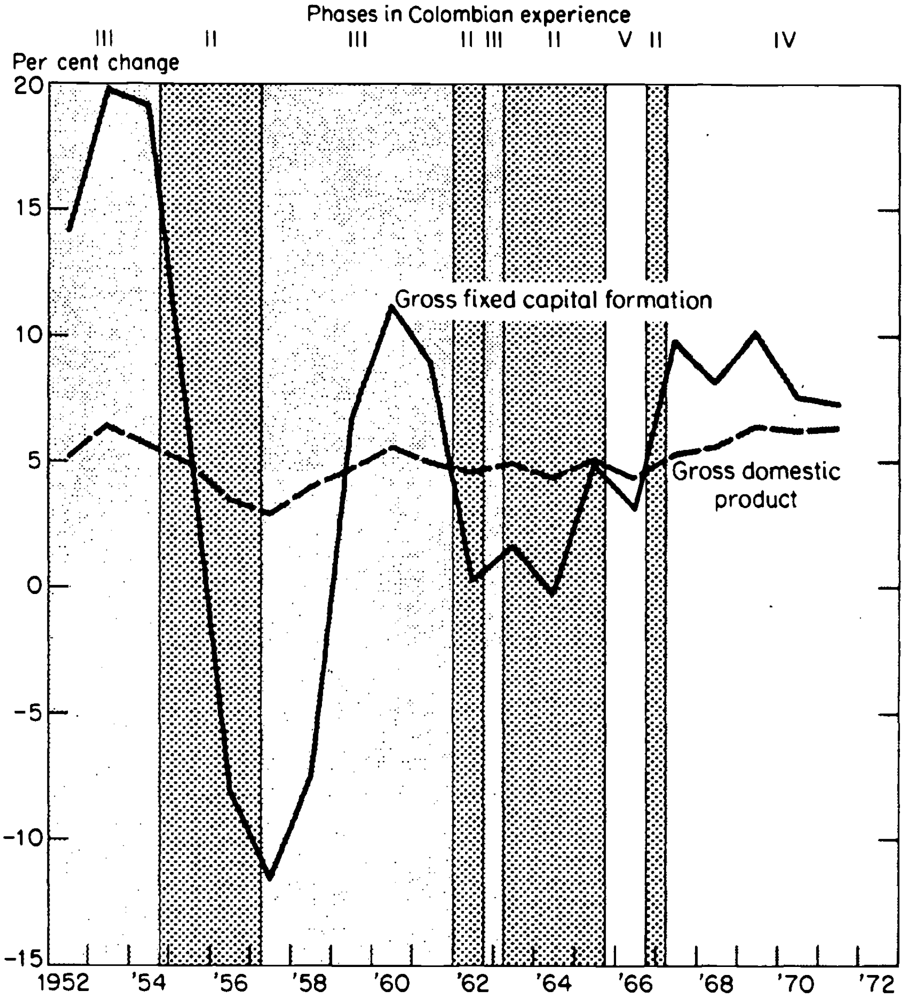
a. Unless otherwise indicated, all dates in this volume are inclusive.

an expansion of real GDP of 4.8 per cent per year for 1950–72 (all dates are inclusive unless otherwise indicated). Such expansion was far from smooth, as can be seen in charts 1-1 and 1-2; consequently, different estimates for the growth of GDP and of other macroeconomic variables shown in Table 1-1 are

CHART 1-1

Rates of Growth of Colombian Gross Domestic Product and Gross Fixed Capital Formation, 1952–71

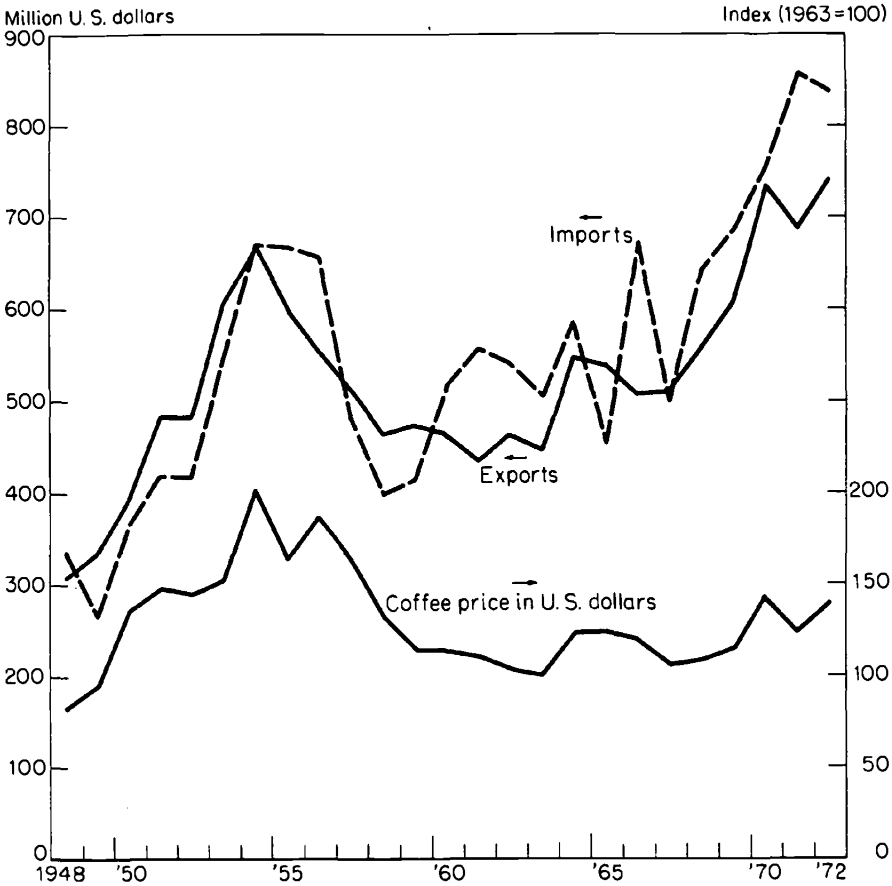
(centered three-year moving averages)



SOURCE: Basic data obtained from the sources listed in Table 1-1.

CHART 1-2

Merchandise Imports, Exports, and Coffee Prices, 1948–72



SOURCE: Basic data obtained from the sources listed in Table 1-2.

possible, depending on the method of calculation and the years used. For example, for just 1972 compared with 1950, the annual GDP growth is 5.0 per cent. Between those years, population grew at about 3.0 per cent per year.[1] Per capita GDP toward the end of the period under study is estimated to be U.S. $380 in 1970 prices, somewhat below the average for Latin America and the Caribbean.

Primary production, including rural activities, fishing, and mining, accounted for 28 per cent of GDP at current market prices in 1971–72; the corresponding amount was 39 per cent in 1950–51. The real output of this sector as a whole grew at a rate not much above that of population. In spite of massive rural-urban migrations, by 1970 about 59 per cent of the total population still lived outside the thirty principal urban conglomerations defined as having at least 50,000 inhabitants. These thirty urban centers grew during the period under study at the remarkable annual rate of 6.5 per cent. Of the economically active population, it has been estimated that 43 per cent could be regarded as engaged in rural activities.

Value added by the rural coffee sector alone amounted to 8 per cent of GDP in 1950–51 at current prices; by 1971–72 that percentage had declined to an estimated 4 per cent. Were Colombian output to be measured at "world prices," those percentages would undoubtedly be higher, inter alia because coffee output is valued at (after-tax) prices received by producers. Coffee output has expanded at an annual rate of 1.7 per cent, not far ahead of the growth of the volume of coffee exported (1.0 per cent per annum). In other words, the performance of the primary sector excluding coffee is significantly superior to that suggested by Table 1-1.

Measured at current prices, the manufacturing share of GDP in 1971–72 was 20 per cent, compared with 17 per cent in 1950–51; a moderate decline in the relative implicit prices for manufacturing was registered between these two periods. Measured in real terms, manufacturing annual growth was 1.3 times that of GDP as shown in Table 1-1. Manufacturing employment, however, appears to have expanded at a rate similar to that of over-all population, and thus lower than the growth of city dwellers.

The GDP share of construction and those services more closely linked to commodity production and distribution (Type I in Table 1-1) expanded from 26 per cent in 1950–51 to 33 per cent in 1971–72. This upward trend has been stimulated by the urbanization and modernization that have been taking place in Colombia between those years, and probably absorbed a large share of the increments to the urban labor force. But these services grew less than did manufacturing. The GDP share of Type II services, closer to pure "home goods" or nontradables, remained at about 19 per cent between 1950–51 and 1971–72, growing only slightly faster than GDP.

Evidence on the distribution as compared with the sectoral composition of output is scarcer. The most thorough study on Colombian income distribution concludes that over-all distribution has probably not improved over the last thirty or forty years. It is likely that the so-called middle class, which can be placed in the eighth and ninth deciles of the income distribution, has benefited most from the growth of those years. As of 1964, the Gini coefficient for the distribution of personal income was 0.57, ranking Colombia, among the countries for which such estimates are available, as one of those with a most unequal distribution. Between the 1930s and mid-1950s, income distribution worsened in both urban and rural areas. Between the mid-1950s and mid-1960s the evidence indicates an improvement in urban distribution, a continued worsening of that in agriculture, and a moderate global improvement.[2]

AN OVER-ALL VIEW: FOREIGN TRADE

Even measured at current-dollar values, total merchandise imports and exports as well as international reserves show trend growth rates for 1948–72 below those of real GDP, manufacturing, and even primary production and population, as may be seen in Table 1-2. No long-term leading sector can be detected here. Indeed, many authors have identified the sluggish expansion of Colombia's postwar capacity to import as the major brake on growth.[3]

During 1948, 1949, and 1950, coffee accounted for 75 per cent of all registered merchandise exports; petroleum accounted for an additional 16 per cent. For both commodities, export dollar values had little to do with domestic policy and much to do with luck in world markets or in exploration. Colombian policy has had *some* influence on the behavior of the world coffee market and on the extent of oil exploration, but room for maneuvering has been small. Thus, from the viewpoint of Colombian policymakers, the meager 1948–72 growth rates shown in Table 1-2 for coffee and petroleum can be taken, in a first approximation, as exogenous parameters. Perhaps little more need be said to define Colombia's postwar foreign trade plight than to indicate that the two commodities accounting for 91 per cent of the export bill during 1948, 1949, and 1950 showed no sustained significant long-term upward trend in their dollar earnings.

Colombian coffee policy has sought higher and more stable dollar prices, if necessary by restricting sales and output in cooperation with other coffee-exporting countries. Internal coffee price policy has aimed at keeping real returns to growers at a stable level, too, but below that justified by dollar prices. The Colombian share in world coffee exports measured in physical units rose from 13.9 per cent in 1934–38 to 16.8 per cent during 1950–54, declining steadily since then to 11.6 per cent in 1971–72. The Colombian share in the value of world exports is higher (13.8 per cent in 1971–72) because of the quality of Colombian coffee, but has declined during recent years at a steeper rate than her share in physical units. Colombian policymakers regard these trends as an inevitable consequence of the rise of new producers, particularly in Africa, and changes in consumer tastes.

During the 1960s declining international oil prices coupled with relatively high Colombian costs for extraction and exploration led to the observed shrinkage in oil exports. An increasing share of oil output was used domestically. Domestic oil policy, which involved cumbersome regulations, special exchange rates, and specific price controls, seems to have had no major

TABLE 1-2

Average Annual Growth Rates and Standard Errors of Key Colombian Foreign Trade Variables, Selected Periods, 1948–72

(per cent; figures in parentheses are standard errors)

	1948–72	1948–56	1956–67	1967–72
Merchandise exports, current	1.85	8.94	0.30	7.69
dollars	(0.48)	(1.69)	(0.71)	(1.48)
Coffee exports, current dollars	0.57	10.01	−1.51	6.14
	(0.57)	(2.12)	(0.73)	(2.34)
Dollar price of coffee per pound	−0.40	9.58	−3.33	6.11
	(0.60)	(1.82)	(1.24)	(1.88)
Volume of coffee exports	1.04	1.21	1.34	0.98
	(0.24)	(1.57)	(0.71)	(0.63)
Registered "minor" exports,	8.89	7.37	9.02	14.15
current dollars	(0.77)	(3.34)	(1.95)	(1.95)
Registered crude petroleum	−1.13	3.90	0.05	−6.77
exports, current dollars	(0.65)	(1.81)	(0.95)	(6.82)
Merchandise imports, c.i.f.,	2.85	11.58	0.85	10.18
current dollars	(0.57)	(1.64)	(1.40)	(1.79)
Volume of merchandise imports	1.92[a]	10.49	0.69	13.72[b]
	(0.70)	(1.54)	(1.70)	(2.10)
Gross international reserves,	0.88	5.96	−7.14	20.67
current dollars	(1.08)	(3.52)	(1.88)	(6.18)

SOURCE: Data obtained from IMF-IFS: growth rates estimated as in Table 1-1.
a. Refers to 1948–70 only.
b. Refers to 1967–70 only.

discouraging effect on oil output during those years. More recently, however, Colombian oil policy has not reflected changes in the international oil market: prices for local consumers and producers are substantially below world prices, discouraging exploration and intensive exploitation of old fields and encouraging consumption of oil products. The state oil enterprise, ECOPETROL, has devoted its efforts toward refining and petrochemicals, neglecting exploration. Noticing the ample oil deposits found in neighboring Venezuela, Perú, and Ecuador, some Colombians may fret and wonder why only relatively poor deposits have been discovered thus far in their own country.

Hope for a vigorous and diversified export sector had to focus on exports of goods other than coffee and oil, still referred to in Colombia as "minor" or nontraditional exports. It will be seen in Chapter 2 that domestic policy can be said to have much to do with their behavior, but only fairly recently has pessimism regarding the competitive strength and growth of these exports been decisively routed in Colombia. In Table 1-2 an impressive long-term growth rate is shown for these exports; their starting base, however, was so small that until recently the impact of their expansion on the over-all export growth rate was modest. Nevertheless, these exports, which represented only 9 per cent of export earnings in 1948–50, were responsible for 56 per cent of the net increase in export earnings between those years and 1970–72.

High targets for GNP growth, sluggish expansion in traditional exports, and nontraditional exports still in their infancy provided the setting for policies encouraging import substitution, particularly in the industrial sector. As in other countries, both short-run balance-of-payments difficulties and a long-run desire for industrialization buttressed by export pessimism provided the rationale for protectionist policies to be discussed in chapters 3–6.

The fluctuations in Colombian postwar foreign trade have been particularly severe, and if just the years 1970–72 are compared with 1948–50, export growth rates are obtained that differ substantially from the trend estimates of Table 1-2, in which every year is taken into account. There is, of course, no "right" or "wrong" way to handle these ambiguities. For 1970–72 compared with 1948–50, the annual growth rate for minor exports is 9.8 per cent, and for coffee plus petroleum it is 1.9 per cent. It is an encouraging reflection on the progress already achieved by Colombia that if identical growth rates for traditional and nontraditional exports are projected for twenty-two years into the future, the over-all export growth rate turns out to be a healthy 6.7 per cent per year, almost double that achieved between 1948–50 and 1970–72 (3.4 per cent). Minor exports had reached 34 per cent of total export revenues by 1970–72, and would reach 63 per cent at the end of the following twenty-two years if the indicated past growth rates hold.

EXTERNAL AND INTERNAL INSTABILITY

Colombia has been one of the classic examples of an export economy that relies on a major staple whose price is subject to considerable fluctuation in world markets. But even during the early 1950s, exports of goods and services did not exceed 16 per cent of GDP at current prices. The corresponding figure for 1972 was 14 per cent. (It will be seen later that sharp fluctuations took place during the period under study in the price of tradable goods relative to those of nontradables.)

The data in the first column of Table 1-2 show that two pieces of conventional wisdom regarding the typical Latin American export economy hold up reasonably well for the Colombia of 1948–72. The terms of trade of its major staple declined, with dollar coffee prices showing no trend while dollar import prices crept steadily upward (compare lines 7 and 8 and disregard quality complications). The dollar coffee price registered substantial instability, as measured by the standard error of the estimated annual rate of change; contrary to what has been argued for other countries,[4] the expansion of the volume of coffee exports shows a much smaller standard error. The fluctuations registered in the growth of dollar earnings of coffee exports can then be properly blamed mostly on price fluctuations. Indeed, for 1948–72, the correlation between (the logarithm of) the dollar value of coffee exports and (the logarithm of) the dollar price index of coffee yields a coefficient of determination R^2 of 0.74; a similar correlation between the value and volume of coffee exports yields an R^2 of 0.11. Instability in coffee export earnings was reduced in some years because of the inverse relation between price and quantity, but for the whole period the price-quantity correlation was weak, as reflected by a negative R of only 0.18 between the logarithms of price and quantity.

It is less well recognized that import instability during 1948–72 was as high or higher than export instability,[5] whether measured in dollars or in physical units. Clearly, such instability cannot be blamed solely on external circumstances: domestic policies play a prominent part in the explanation of this peculiar fact. More on this in later chapters.

Given the stress in the literature on the dependence of the Colombian domestic economy on foreign trade, and the confirmation of the instability of imports and exports, it is surprising to find that the standard error of real GDP growth is only 0.07 (first column of Table 1-1). Had I used a macroeconomic measure embodying term-of-trade effects (which the GDP does not), the instability would of course be higher, but it is nevertheless notable that small echoes of fluctuations in exports and imports may be found in short-run GDP expansion. Even more striking, in view of all the literature stressing rigid links, is the steadiness found in manufacturing growth for the whole period. Which is the most unstable component of GDP? It is construction, which presumably is one of the least import- (or export-) intensive sectors of the economy![6]

Fluctuations in trade, especially imports, are so much larger than those of GDP that it could be argued, in a reversal of the chain of causation, that we are looking at an economy where slight adjustments in GDP expansion, perhaps brought about by monetary and fiscal policies, are highly successful in correcting payments imbalances. Additional knowledge permits us to discard this argument, applicable to economies with relatively unrestricted trade and payments systems, in the Colombian case. But it serves to emphasize the apparently marginal influence of Colombian foreign trade on GDP growth in the short run.

Another remarkable (negative) result involves the lack of correlation between real GDP growth for a given year t and the growth in exports, deflated by import price indices (or an approximation to the growth of "capacity to import"), during t, $t - 1$, $t - 2$, and $t - 3$. Even when a trend term was added to the regression, the results were insignificant, showing no link, both for the period 1950–68, and for 1929–68.[7]

For *any given year* it appears that above a certain minimum, which was in fact available to Colombia during almost all the years under study, few *imports* are indeed absolutely essential for the maintenance of economic activity. Imports of capital goods for expansion of capacity, as well as those of durable and nondurable consumer goods, can of course be postponed without much loss of that year's GDP. It is more difficult to cope with fluctuations in the supply of intermediate and raw material inputs, spare parts, etc. However, in an ongoing economic system, especially one in which people are accustomed to import controls, fluctuations in import availability can be partly absorbed in the short run through changes in inventories as well as use of more imaginative expedients, thus decreasing (but not eliminating) the negative impact of the fluctuations on GDP.

It should also be recalled that primary production still represents a substantial share of Colombian GDP. Much of it has only tenuous links with foreign trade and with economic activity in the rest of the country. By combining many services and even segments of manufacturing, especially crafts, a robust nontradables sector can be put together, the hard core of it located among the small cities and towns scattered amidst the abrupt Colombian mountains (see Figure 1-1). In this sense, the Colombian economy can be said to retain widespread "duality," or structural heterogeneity.

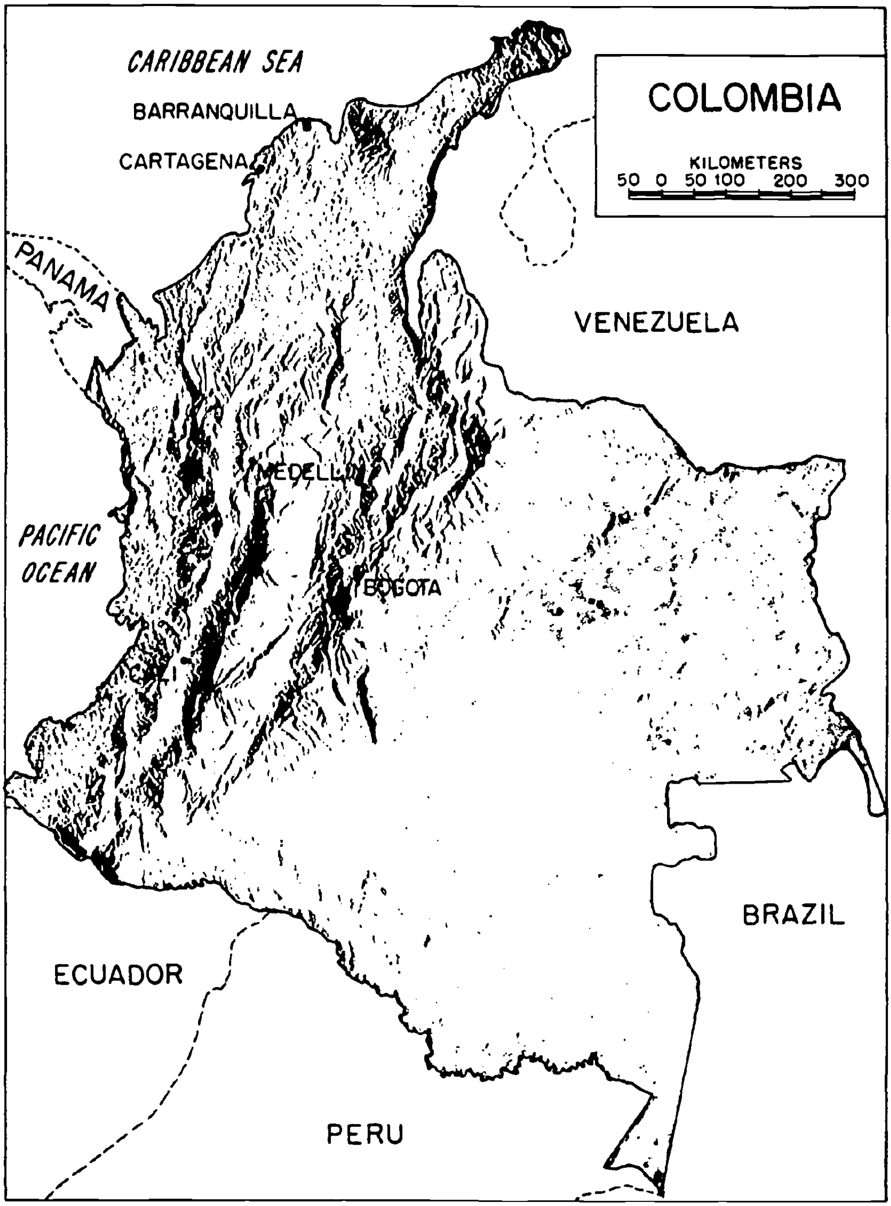
The above considerations help to explain why on the basis of year-to-year changes the link between foreign trade and GDP growth in Colombia has been relatively weak. But the foregoing factors are less informative regarding longer-term links.

CAPITAL FORMATION AND FOREIGN TRADE

Trend growth of real fixed capital formation during 1950–72 was lower than that of GDP. Domestic production of machinery and equipment, like minor exports, expanded at a rapid clip, but from a low base. Construction experienced a trend growth similar to GDP. The growth of total capital formation was dragged down by the sluggish expansion of capital goods imports, as may be seen in Table 1-1. As imports accounted for 93 per cent of capital formation in the form of machinery and equipment in 1950, and for 67 per cent as late as 1972 (magnitudes measured in 1958 prices), the failure of import capacity to

FIGURE 1-1

Topographical Map of Colombia



rise over the long run seriously limited investment and probably important aspects of technical change. Note that in Table 1-1 capital formation in all machinery and equipment shows a trend growth rate inferior to that of population.

The standard errors for the growth rates in all investment components are high, as old-fashioned business cycle theory would predict. But those for machinery and equipment and for capital goods imports are the highest. Here is where trade instability and stagnation take their sharpest bite. As will be seen in Chapter 3, there is in fact a very close correlation in Colombia between capital formation, especially in machinery and equipment and imports. This is surprising only insofar as it includes construction, given the weakness of the Colombian machinery and equipment industry. Under these circumstances, the export sector is the major (indirect) supplier of machinery and equipment.[8]

The relative prices of capital goods in Colombia, especially machinery and equipment, have on the whole followed the acute gyrations of the prices for tradable goods relative to nontradables. So while the share of all gross investment in GNP measured at current prices was 17 per cent in 1950 and 21 per cent in 1972, the corresponding figures in constant 1958 prices are 22 per cent and 20 per cent.

While the link between Colombian foreign trade and capital formation has been strong, variations in the marginal capital-output ratio, even for a medium run of several years, considerably loosen the connection between capital goods imports and growth. In the last chapter, I will discuss possible explanations for the variations in the marginal capital-output ratio, which include direct and indirect effects of Colombian foreign trade policies.

COFFEE AND PHASES

The years 1948 through 1972 cover a variety of trade and domestic experiences that clearly deserve separate treatment. The fundamental nature of the Colombian economic system remained unchanged, but dollar coffee prices as well as domestic policies differed substantially from phase to phase.

A first subdivision, based mainly on the world coffee market, is easy to make: before 1956, from 1956 through 1967, and since 1967. Coffee prices showed an impressive upward trend from 1948 through 1956, pulling up export and import dollar values, the physical volume of imports, and fixed capital formation. GDP rose from 1950 through 1956 at a faster than average (for 1950–72) rate, but the gap between the booming trade and investment variables and the unspectacular GDP performance looks puzzling. At least part of the answer to this contrast can be found in the divergence in sectoral growth rates. On the whole, urban (and especially big-city) activities such as manufacturing and construction boomed, while the important rural sector made slow progress. During 1948–56, a good part of rural Colombia was in the midst of social turmoil or bloody civil war. Another name for growth and development, or for favorable terms of trade, is not always peace, as this experience shows. A good share of investment during those years went into social overhead facilities, as well as spectacular projects with debatable social returns.

The trend of coffee prices from 1956 through 1967 was downward; attempts of the Colombia government to cope with that situation make up much of the substance of later chapters. While the annual growth in the volume of merchandise imports dropped dramatically, from 10.5 per cent to 0.7 per cent (Table 1-2), GDP growth sagged by less than a percentage point, from 5.2 to 4.6 per cent, as shown in tables 1-1 and 1-2. The slowdown in manufacturing expansion was larger, from 7.3 to 5.7 per cent per year, although far less spectacular than the drop in the growth rate of construction (value added), in spite of the latter's relative independence from imported inputs. Capital formation, especially in machinery and equipment, behaved more like the trade variables than like GDP, manufacturing, or primary production (the latter growing quite steadily in spite of unsteady weather). The slowdown in the expansion of domestic production of capital goods is notable, suggesting that while this activity is aimed at import substitution, it maintains complementary links with imported inputs. It may be added that the Colombian social and political picture was quieter and more peaceful during 1956–67 than it was before.

Dollar coffee prices did not change abruptly after 1967, as they had done after 1956. As will be seen below, the claim that 1967 was a turning point in Colombian economic history rests primarily on domestic policy accomplishments. Nevertheless, after a dip in 1967, dollar coffee prices tended to rise; their average for 1971–72 was still below that for 1955–56, but by 1973 that postwar high had been surpassed. As shown in Table 1-2, from 1967 through 1972 coffee earnings grew at 6 per cent per year, a healthy rate, but outpaced by the 10 per cent rate registered from 1948 through 1956. The most significant feature of the post-1967 years was the remarkable 14 per cent annual growth in minor exports, which was double the rate for 1948–56, in spite of its having started from a larger base. Supported by an expanded capacity to import, which even discounting inflation in dollar prices rose remarkably after 1967, the GDP grew faster and in a more balanced fashion than during 1950–56. In Chapter 8, I will examine in detail several characteristics of the post-1967 growth path. Here it is sufficient to note that by 1973 such growth had left the Colombian economy in a much better position to withstand external shocks than it was in 1956.

POLICY AND SUBPHASES

Before the Fall.

While trends in dollar coffee prices provide the critical 1956 watershed in Colombian postwar economic history, and 1967 provides, ex post, another clear turning point, policy hesitations and coffee price instability hinder neat and simple further subdivisions of the period under study. Appendix B contains a detailed list of principal postwar economic events related mainly to Colombian foreign trade and payments. A close look at policy shifts reflected there will show that they were influenced by at least the following major factors: cyclical fluctuations in the ex ante demand for imports and foreign exchange; dissatisfaction with the mechanisms used to repress such demand; the search for ways to stimulate minor exports; general political events, which since 1958 have followed a four-year presidential cycle; pressures from international and bilateral creditors, mainly the IMF, the IBRD, and the United States government; and, of course, the short-run gyrations of coffee prices.

Subdivision into phases is naturally somewhat arbitrary, but it is hoped that those suggested in Table 1-3 will on balance add more clarity than confusion. The last four follow, as well as calendar years and data allow, the post-1958 terms of the National Front presidents. They are preceded by two biennial transitional subphases (1957–58 and 1955–56), and by 1950–54. The following brief sketch of the characteristics of each of these subphases and their relation to the Bhagwati-Krueger phases (see Appendix A) is intended to place later discussion in perspective.

As in many Latin American countries, the great depression of the 1930s put an end to an era of relative economic liberalism in Colombia; in terms of the Bhagwati-Krueger scheme, Colombia went from Phase V to Phase I. Key import duties were raised, and widespread exchange and import controls were introduced in 1931; they have not been fully abandoned since. It should be noted, however, that quantitative restrictions were not the only response to the crisis; the Colombian exchange rate went from 1.03 pesos per U.S. dollar in 1929 to 1.78 pesos in 1935. An index (1963 = 100) of the purchasing-power-parity exchange rate, adjusted for price-level changes both in Colombia and the United States, rose from 56 in 1929 to 101 in 1935 when GDP deflators are used as proxies for "the price level," and from 70 in 1929 to 103 in 1935 when cost-of-living indices are used.[9] Such real devaluation foreshadowed the one following the post-1956 drop in the price of coffee. Indeed, the index for the real exchange rate for imports was not to reach the 1935 level again until 1958. As in the cases of Argentina and Brazil, the real devaluation helped Colombia weather the Great Depression surprisingly well, and stimulated industrialization.

Coffee recovery and the threat of war, then the Second World War, and later the circumstances of postwar European reconstruction appear to have induced the authorities to leave exchange rates alone. At any rate, between 1935 and 1948 the nominal exchange rate hardly moved, and Phase I controls became an established feature of the trade and payments system. The index for the purchasing-power-parity import exchange rate, which stood at 101 in 1935, dropped to 80 in 1939, to 63 in 1945, and to 59 in 1948 (similar results are obtained using cost-of-living deflators). In spite of some adjustment in the nominal rate, the index fell further, to 54 in 1950, roughly the 1929 level. As was the case in some other Latin American countries, the 1950s opened with exchange rates which had gradually, almost imperceptibly, become overvalued during the 1940s as nominal rates remained frozen while domestic inflation advanced faster (but not that much faster in any given year) than in the United States, the major participant in the world market.

The adjective "overvalued" is one to be used with care at all times, but particularly so in Colombia. There is probably no exchange rate observed in Colombia during 1925–72 which could not have been turned into an "equilibrium" one at some dollar coffee price, even if the possible choices were limited to the range of prices actually observed during the same period. The instability and unpredictability of world coffee prices thus has discouraged exchange authorities from seeking such an "equilibrium" rate, and has provided a major rationalization for import and exchange control.[10] For the 1930–68 period, there has been in fact a significant negative correlation between the purchasing-power-parity import exchange rate and the terms of trade as well as a significant upward trend in the real import exchange rate. The same results are obtained if just the 1950–68 years are analyzed. While on the subject of (very) long-term trends, it may be noted that although the Colombian coffee terms of trade (international) declined when the years 1948–72 are considered as a whole, they show a significant *positive* trend, or at worst no trend, when all of the years since 1925 are taken into account.[11]

The early postwar years, through 1954, are generally regarded as prosperous ones. While comprehensive national accounts are available starting only in 1950, earlier estimates of UNECLA put the annual growth of real GDP during 1945–50 at 5.2 per cent. The corresponding figure for 1925–45 is 4.1 per cent, at a time when population was expanding at an annual rate of about 2.1 per cent. As current-dollar coffee prices tripled between 1945 and 1950, the expansion of consumption plus investment (absorption) must have been higher than real GDP growth. By the late 1940s and during 1950 dissatisfaction with import and exchange controls rose, in spite of tinkering with the system.

TABLE 1-3

Major Colombian Economic Indicators, 1950–72
(annual averages)

	1950–54	1955 and 1956	1957 and 1958	1959–62	1963–66	1967–70	1971 and 1972
Foreign trade indices (averages for 1950–54 = 100)							
Merchandise exports, current dollars	100	109	92	87	97	114	136
Coffee plus oil exports, current dollars	100	105	90	83	86	87	93
Other (*minor*) exports, current dollars	100	156	121	146	244	483	698
Dollar price of coffee per pound	100	112	94	71	74	75	85
Volume of coffee exports	100	103	97	115	112	120	122
Merchandise imports, current dollars	100	137	91	105	115	133	175
Volume of merchandise imports	100	132	85	92	96	101	n.a.
GDP and its components (average annual percentage growth rates)							
GDP	5.6	4.0	2.3	5.5	4.6	5.9	6.1
Primary production	2.9	3.2	4.5	3.1	2.7	4.8	3.2
Manufacturing	7.1	7.0	4.5	6.8	5.5	6.4	8.8
Construction	13.6	5.5	−4.2	6.2	2.3	11.1	4.5
Services, Type I	9.1	2.4	−2.3	8.2	5.9	6.4	7.5
Services, Type II	4.1	5.0	3.8	5.2	5.7	5.6	6.1

Fixed capital formation as per cent of GNP (1958 prices)	21.2	25.1	17.1	18.1	16.4	17.7	18.3
In building and construction	9.3	10.9	10.0	9.8	8.6	10.3	10.1
In machinery and equipment	12.0	14.2	7.1	8.3	7.8	7.3	8.3
Over-all marginal fixed capital-output ratio, with capital formation leading by one year	3.9	9.2	3.4	4.3	3.4	3.0	2.7[a]
Purchasing-power-parity exchange rates, 1963 prices (pesos per dollar)							
Effective coffee rate	4.83	5.15	6.10	5.99	5.45	5.78	6.13
Average nominal import rate	6.08	5.58	9.19	9.11	8.44	10.34	11.45
Effective minor-export rate	7.96	9.78	9.76	11.19	11.39	12.35	13.58
Annual percentage rate of change in price indices							
Wholesale prices	6.6	4.7	20.8	5.8	17.4	6.8	14.9
Consumer prices	10.6	−1.2	14.9	5.6	18.3	7.7	11.7

n.a. = not available.

SOURCE: Basic trade and national accounts data obtained as in tables 1-1 and 1-2. GDP and GNP estimates, and those for their components, are at 1958 market prices. Foreign trade data refer to registered transactions. Effective coffee rate calculated by comparing peso prices in Colombia with dollar prices in New York, taking into account estimated transport costs and quality differences. Price data obtained from IMF-IFS. Import and minor-export exchange rates are taken from chapters 2 and 4.

a. Includes an estimated GNP growth rate of 7 per cent for 1973.

During those years Colombia could be said to be in Phase II of the Bhagwati-Krueger scheme.

The export-led or coffee-fueled prosperity, aided by the quietest and least expected postwar devaluation, in March 1951 (which led to a 28 per cent increase in the nominal peso price of the U.S. dollar), was accompanied by a relaxation of exchange and import controls inherited from the war and the Great Depression. Consequently, in the first half of 1954, in spite of an import exchange rate which in purchasing-power-parity terms was still substantially cheaper than the rates of the 1930s, the prohibited import list was eliminated and the most liberal import regime witnessed in Colombia since 1929 was instituted. It appears, however, that import controls and regulations were used even during those years for specific, ad hoc protective purposes. Nevertheless, 1951–52 can be considered to mark the first Phase III liberalization episode in Colombian postwar history, with movement toward Phase IV taking place during 1953 and early 1954.

Coffee prices dropped sharply in mid-1954 from the astronomical levels reached earlier that year, but remained at historically high levels through 1956. A booming demand for imports and exchange (merchandise imports during 1954 reached $672 million, a level not surpassed until 1966) led to growing payments arrears, which piled up during 1955 and 1956 as pending requests to the Exchange Control Office. Import and payments liberalization began to be reversed late in 1954, and controls once again tightened, with the authorities reluctant to devalue across the board.

During early 1955 stamp taxes were imposed on imports, graduated according to the degree of their "essentiality." In May, a free market was introduced, where exchange for the less essential imports and most invisibles was to be purchased. Most minor exports also benefited from the new free-market rate. A large gap appeared between the free and official rates, and the free rate fluctuated considerably. Throughout 1955 and 1956 the control regime grew in complexity and, it is said, in arbitrariness of administration. Colombia was back to Phase II.

It may be seen in Table 1-3 that although exports and imports remained at high levels during 1955–56, GDP growth slowed down. The 1955–56 rate of capital formation, buttressed by massive imports, reached 25 per cent of GNP (at 1958 prices), the highest average for the period under study, and the growth rate of manufacturing held up. The investment rate in machinery and equipment is particularly noteworthy. It can also be seen in the table that in spite of the creation of a free market for some imports, the purchasing-power-parity import rate declined during 1955–56 relative to 1950–54. The effective purchasing-power-parity rate applicable to minor exports, however, improved. Finally, the table shows that large imports did a fine job in keeping down price rises.

The 1957–58 Crisis.

Economic conditions during early 1957 were of a sort to inspire journalists and unsympathetic critics of those then in power to use lively, descriptive words such as "chaos" and "bankruptcy." The bad news included growing payments arrears, capital flight, tightening import restrictions, increasing use of bank credit to finance public deficits, as well as a generally expansive credit policy, growing inflationary pressures, a rising black-market peso rate, stagnant real output, and, last but not least, a falling dollar coffee price. In May 1957 a provisional military government took power from General Rojas Pinilla, and the next month a stabilization program was undertaken. A new Phase III had begun.

The June 1957 program simplified the multiple exchange-rate structure which had developed during previous years, replacing it with two fluctuating peso rates. The new certificate market,[12] however, was to cover most merchandise transactions, including minor exports, and some invisibles; the free market was limited to unregistered capital and most invisibles. Various export taxes were also introduced. This was the second time during the 1950s that simplification of the multiple rate system led to a lower nominal rate for (most) minor exports. Before the March 1951 exchange reform and devaluation, minor exports (excluding hides, gold, and bananas) received the fluctuating nominal exchange certificate rate, which at the end of 1950 stood at 3.2 pesos. After the March 1951 measures, the nominal rate applicable to minor exports was reduced to 2.5 pesos, until export vouchers were introduced, in August 1952. In a similar fashion, before the June 1957 reforms most minor exports received the free rate, whose nominal value reached 7.0 pesos in April 1957. By July 1957 the rate applicable to minor exports was the certificate rate, which stood at 4.8 pesos. The effective change against minor exports was even higher, not only because of the acceleration of Colombian inflation but also because of the imposition of emergency export taxes to finance the servicing of the foreign debt that had piled up during 1955 and 1956.

It appears from these and later events that the quest for simplicity and stability in the Colombian exchange-rate structure was often carried out at the expense of incentives for minor exports. A somewhat rigid interpretation of the letter of the Bretton Woods agreements was frequently invoked during the 1950s and early 1960s both to close the gap between favorable rates applied to minor exports and the coffee-influenced major rates, as well as to eliminate free fluctuations in the rate applicable to minor exports. In practice, both of these policies led to less favorable rates for minor exports, as politically it was much easier to lower those rates than to raise the ones corresponding to imports and coffee. The Colombian and international civil servants who maintained such legally admirable but economically faulty adherence to Bretton Woods also expressed concern from time to time that excessive rates for minor exports would breed inefficiency, even as protection against imports was kept at high levels and the foreign-exchange shortage persisted.

The stabilization efforts that began in June 1957 also highlighted a policy problem which persisted, although in a reduced way, until 1973. It was urgent for the authorities to get control of and slow down the expansion in domestic credit. This was done only with difficulty, as at that time the government did not even fully control the bank of issue, the Banco de la República. Powerful private banking groups, as well as the Coffee Growers' Federation, were able, at least within certain limits, to circumvent the government's desire to tighten up credit. Under these circumstances, after June 1957 increasing use was made of import prior-deposit requirements not only as a way of reducing import demand, but also of controlling the growth in the money supply. As those deposits grew, the authorities found themselves increasingly locked into a rigid and cumbersome situation.

Pressure from the politically powerful coffee growers resulted in an increase in the purchasing-power-parity de facto coffee exchange rate of about 18 per cent between 1955–56 and 1957–58 despite gloomy prospects in the world coffee market. This experience illustrates the political difficulties which traditionally have limited the freedom of the Colombian policymaker to raise exchange rates applicable to imports and minor exports while trying not to touch, or to lower, the de facto coffee rate. Coupled with the relatively easy access coffee growers have had to central-bank credit to finance their price-supported crop, this limitation on policy flexibility has accounted for a good share of the headaches of those in charge of coordinating Colombian short-run policies during the years under study. It may be seen in Table 1-3 that only after 1959–62 has there been a sustained increase in the gap between the effective exchange rate applied to minor exports and that applied to coffee. The relationship between these two rates fluctuated around 1.7 throughout 1950–62, rising to about 2.0 since then.

In spite of the difficulties and ambiguities, and in spite of dollar coffee prices which during 1957–58 were 16 per cent below those for 1955–56, the stabilization plan was successful in clearing up many of the short-term economic problems in time for the inauguration of a new constitutional President in August 1958. This, incidentally, contrasts with the luck of the next two Colombian presidents, who during their early months in office faced serious short-term crises. Only President Pastrana Borrero, inaugurated in August 1970, was to inherit, as President Lleras Camargo did in 1958, a smoothly going concern.

The stabilization plan could not stave off an average annual rate of inflation of around 15 to 21 per cent during 1957–58. Given the magnitude of the gross devaluation of the average import rate, as well as the clumsiness of the monetary policy tools and the degree of adjustment sought in the economy, these rates do not appear unreasonable and were clearly on the decline when the new President was inaugurated. The average purchasing-power-parity import rate rose by an impressive 65 per cent between 1955–56 and 1957–58, as shown in Table 1-3, and import and exchange controls were rationalized, but remained very tight. The austerity policy on imports drove their average dollar value during 1957–58 to one-third below their level of 1955–56; restrictions on capital goods imports appear to have been unusually severe, and the rate of capital formation in machinery and equipment, measured as a percentage of GNP at 1958 prices, was *halved* between 1955–56 and 1957–58.

Given these circumstances, it is not surprising to find GDP growth falling below that of population during 1957–58. Indeed, the surprise is that it did not fall more.[13] Construction and some services performed more poorly than import-intensive manufacturing. Luckily, the crops appear to have been good during the period of the stabilization plan.

The commercial arrears accumulated during 1955–56, the immediate cause of the payments crisis, had been either paid off or refinanced by the time of the inauguration of the new President. In spite of lower coffee earnings during 1957–58, a current account surplus was generated which, together with official short-term borrowing, went to pay for the arrears as well as to finance private capital outflows. This can be seen in Table 1-4, which summarizes the Colombian balance of payments since 1957 (earlier years are not available in this format). Such a dramatic belt tightening earned Colombia the respect of international creditors, and prepared the scenario for making Colombia a "showcase of the Alliance of Progress."

Four Presidencies.

Dramatic developments in Colombian foreign trade and payments, comparable to those just discussed, came again in 1962 and reached their peak of excitement during 1965–66. These episodes deserve a special chapter, as they illustrate the difficulties of a transition from Phase III to Phase IV; so in this section I will limit myself to discussing a few key trends and themes of policy during the four presidencies of the National Front, touching upon those dramatic events only lightly.

Especially until March 1967, most policymakers involved with Colombian international trade and payments appeared to have had the following major objectives, often difficult to reconcile:

a. Import liberalization, in the sense of meeting all "reasonable" requests for imported capital, intermediate goods, and raw materials. The notion of

TABLE 1-4

Colombian Balance of Payments, 1957–71
(annual averages in millions of current U.S. dollars)

	1957 and 1958	1959–62	1963–66	1967–70	1971 and 1972
Coffee exports	378	317	366	380	416
Exports of petroleum products	69	70	79	53	39
Nonmonetary and monetized gold	—	—	11	7	7
Other merchandise exports including nonregistered	124	107	106	217	356
Merchandise exports, f.o.b.	570	494	562	657	818
Merchandise imports, f.o.b.	−418	−492	−537	−632	−825
Trade balance	153	2	25	25	−7
Transport receipts	n.a.	n.a.	58	82	102
Travel receipts	n.a.	n.a.	26	48	67
Other receipts from services and transfers	n.a.	n.a.	41	79	82
Transportation payments	n.a.	n.a.	−85	−120	−188
Travel payments	n.a.	n.a.	−46	−61	−73
Other payments for services and transfers excluding investment income	n.a.	n.a.	−85	−111	−133
Net services excluding investment income	−38	−41	−91	−83	−143
Net payments for investment income	−44	−47	−80	−144	−189
Balance on current and transfer account	71	−85	−146	−202	−339
Net long-term private capital	−13	29	107	98	106
Net short-term private capital	−8	5	12	−2	23
Private commercial arrears and net credit from commercial banks	−104	4	19	36	40
Net grants and official capital	—	25	44	113	137
Errors and omissions	−34	16	−42	0	84
Net "autonomous" capital	−159	79	140	245	390
Net loans and credits received by BdlR	97	−18	8	−21	19
Net IMF account and net SDRs	3	8	3	5	−19
BdlR gold and foreign exchange net of payment agreements liability	−12	17	−4	−28	−52
Net "compensatory" capital	88	7	7	−44	−52

Notes to Table 1-4

n.a. = data not available in directly comparable form.

SDRs = special drawing rights.

SOURCE: Adapted from IMF-BOPY, various issues, analytic presentation. Negative signs denote debits; all other figures are credits. Therefore, for BdlR gold and foreign exchange, a negative sign indicates a buildup of reserves. Note that net long-term private capital includes loans received by the Colombian private sector from institutions such as IBRD, IABD, and USAID. Merchandise trade includes adjustments for coverage and timing; so the figures differ from those in trade returns.

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allowing imports of goods that competed with local production, or imports of "luxury" goods, even with stiff tariffs but without prior import permits, was seldom popular and even more rarely became a policy objective.

b. Stable, "noninflationary," "nonspeculative" exchange rates.
c. Sharply growing minor exports.
d. Substantial inflows of concessional long-term capital, particularly from the IBRD, the IADB, and the U.S. government, as well as ready access to short-term international credit, especially from the IMF, U.S. commercial banks, and suppliers of imports.
e. Keeping down the de facto coffee exchange rate, to reduce excessive domestic coffee stocks and promote agricultural diversification, while increasing public revenues and dampening inflationary credit requests from the Coffee Growers' Federation.
f. Maintenance of exchange controls, particularly over capital outflows and service payments, and over inflows of direct foreign investments.

The coordination of just the various policy instruments relevant to the balance of payments was a difficult task during most of the years under study, since frequently each policy instrument was jealously guarded by a separate bureaucratic unit. Unless the President himself kept a firm grip on the policy package, the likely result was contradictory and unstable policies.

The coordination between foreign trade and payments policies, on the one hand, and more general growth and development policies, on the other, was of course even trickier. The first Colombian development plan was completed during the last year of the Lleras Camargo administration (1961–62). It was analyzed and reported on by the Committee of Nine of the Alliance for Progress in July 1962.[14] It was quietly ignored by the Valencia administration which took power a month later. Serious, comprehensive, long-term planning was not again undertaken until 1966.

Although the country has been governed by constitutional civilian regimes since 1958, and although before 1953 the country had a long tradition of civilian, constitutional governments, its political system has been aptly described as "elitist rule" by Albert Berry,[15] even though the "elitism" gradually declined throughout the 1960s and early 1970s. As noted earlier, income distribution is sharply skewed. Furthermore, in 1962 only 34 per cent of children aged 5 to 19 were in primary and secondary schools (though that was some improvement over the corresponding figure of 24 per cent in 1950). Other social indicators confirm the picture of inequality, severe poverty, and nonparticipation in public affairs of families at the bottom 50 per cent of the income scale.

It appears that the poorest half of the population has shared to some extent in the increases registered in Colombian per capita income over the last two or three decades. So they cannot be said to be totally indifferent to what goes on in the economy as a whole. But it should be borne in mind that, especially in the short and medium run, many of the policies discussed in these and later chapters touch only marginally upon the welfare of large parts of the Colombian masses. And it is not always clear whether policies desirable on grounds of growth and efficiency positively or negatively affect the welfare of those people in the short and medium run. At any rate, their opinions in these matters are unlikely to carry much weight among the politicians, the national and international civil servants, and the private pressure groups, including local and foreign businessmen, some trade union leaders, and the Coffee Growers' Federation, who have the most to say on these issues and have the most to gain or lose from the way they are settled.

THE LLERAS CAMARGO PRESIDENCY.

This presidency opened not only with considerable national and international goodwill, but also with short-run trade and payments well under control, thanks to the austerity program of 1957–58. There was an understandable eagerness to return to higher growth rates and to more relaxed import and credit controls. Circumstances appeared propitious for a smooth transition to Phase IV. As shown in Table 1-3, higher GDP growth rates were indeed achieved, and merchandise imports, although still below the 1955–56 levels, rose sharply above the depressed 1957–58 figures and were comparable to those registered during 1950–54. Coffee prices, however, continued their decline; their average for 1959–62 was 37 per cent below their 1955–56 levels. Some contribution toward equilibrium in the balance of payments was made by the start of Alliance for Progress disbursements during 1961 and 1962, recorded in Table 1-4 both under net grants and official capital and under net long-term private capital.

The more generous granting of import licenses, started in 1959, was accompanied by a stickiness in the nominal import exchange rate, which was to prove fatal to the hope of a smooth transition into Phase IV. Earlier plans gradually to adjust that rate, aimed at an eventual unification of the free market with the certificate market, in which exchange for imports was obtained, were quietly dropped under circumstances to be explored in Chapter 7. An opportunity to adopt the crawling peg, which proved successful after 1967, was missed. The purchasing-power-parity average import rate in 1963 prices dropped from 11.2 pesos in 1958, to 9.9 pesos in 1959, to 9.2 pesos in 1960, and to 8.7 pesos in 1961. The 1958 rate was not to be reached again until the last quarter of 1970. Fears of reviving inflationary pressures blocked a more vigorous adjustment of the import rate. Inflation was in fact kept to an annual rate of less than 6 per cent from 1959 through 1962.

The effective exchange rate applicable to minor exports, however, remained at levels above those of 1950–58, reaching quite a high level late in 1962. Systematic use began to be made during this period of powerful tax incentives to exporting firms, while crop-specific promotion programs originally undertaken to replace imports, and which featured credit and tax concessions, began to pay off also in terms of new exports, as in the case of cotton. Exports of sugar and tobacco also received a boost, accepted but not celebrated by sensitive Colombians, from the blockade imposed on Cuban exports by most countries of the Western Hemisphere. A more positive source of improved Colombian export prospects was the creation of the Latin American Free Trade Association in 1960.

The more favorable exchange rate applied to minor exports came about from its identification with the free-market rate, beginning in January 1959, after the former had been associated with the pegged certificate rate during most of 1958. The free market, however, remained thin and fluctuated a fair amount; the average quarter-to-quarter (absolute) change in the nominal free-market rate during the sixteen quarters of 1959–62 was about 6 per cent. Neither the extent nor the contribution toward stability, if any, of sporadic central-bank intervention in the free market during this period is clear.

By early 1962 the pressures on the balance of payments were becoming quite severe, a fact not unrelated to the rapid Colombian presentation of its first development plan to Alliance for Progress experts. But the expansion of aid and of minor exports was insufficient to meet growing import demands, and the dreary process of denials, heroics, and increased Bogotá-Washington shuttles clearly pointed to an impending devaluation of the major import rate. The trend toward some liberalization of import licensing observed from 1959 through 1961 was reversed early in 1962, and the restrictions gathered force throughout the year. Matters were complicated by the inauguration in August 1962 of a new administration, headed by President Guillermo León Valencia, a remarkable man of talent and courage, but not particularly interested in economics, just at a time when the inherited situation called for a chief executive with an appetite for financial matters.

THE VALENCIA PRESIDENCY.

On November 7, 1962, all imports were placed on the prohibited list, and licensing was suspended for about a month. On November 20, the exchange rate applicable to most imports was allowed to move from 6.7 to 9.0 pesos per U.S. dollar. Memories of this devaluation, undertaken in the midst of financial disorder and without a comprehensive political-economic program, were to play an important role during the following years, hindering liberalization efforts. Reasons for the failure of this devaluation will be discussed in Chapter 7. It is enough to point out here that a sharp domestic inflation during the early part of 1963 wiped out practically all the incentive effects of the devaluation; as a result, the purchasing-power-parity average import exchange rate for 1963 was only 4 per cent higher than that for 1962 and was, of course, below the 1958–60 levels. The gloomiest predictions of devaluation opponents had come to pass. Furthermore, in January 1963, in a misguided search for stability, the central bank began to peg the free rate, applicable to minor exports, at 10 pesos, or below the December 1962 level, which had averaged 11.1 pesos during the last two weeks of that year. As a result, the effective exchange rate applicable to minor exports during 1963 was 13 per cent below what it had been during 1962.

Under these circumstances, expected postdevaluation import liberalization moves remained feeble, and it was not long before rumors of a new devaluation began to circulate. Colombia was once again in Phase II. In October 1964, almost two years after devaluation, the central bank, short of reserves, ceased pegging the free-market rate. Import licensing became progressively tighter; and on December 1, 1964, the import free list was suspended for ninety days (except for imports from LAFTA). The President, however, burned by the devaluation of November 1962 and in a difficult political position, would not hear about any new major devaluation of the basic import rate. The Colombian image as the "showcase of the Alliance for Progress" became tarnished, and aid disbursements for 1964 and 1965 fell below the 1963 level.

Throughout the first half of 1965 import restrictions continued to tighten. New lists of prohibited imports were issued, and on May 5 even imports from LAFTA countries were included in the prior license list. The free-market rate climbed steadily from 10 pesos in October 1964 to nearly 19 pesos in June 1965. Once again the authorities deemed this to be an excessive reward for minor exports, whose rate was pegged on June 30 at 13.5 pesos.

Once established, the figure of 13.5 took on some magic. It is said that the President was persuaded that a gradual transfer of imports from the ("preferential") rate of 9 pesos to the new ("intermediate") rate of 13.5 pesos could be interpreted as a *revaluation* relative to the free rate, which went beyond 19 pesos during July and August of 1965, as devaluation rumors became widespread.

Be that as it may, in September 1965, that plan was announced, and the rate of 13.5 pesos began to be applied not only to minor exports, but to a growing list of imports, which at the same time were freed from license requirements. This was indeed the beginning of the most ambitious liberalization attempt of Colombia's postwar economic history, a leap toward Phase V which ended in a dramatic confrontation between a new Colombian government and foreign creditors in November 1966. The import liberalization program advanced boldly, with the result that by September 1966 practically all imports had been transferred to the 13.5-peso rate and had been freed from licensing requirements. Many tariff rates were adjusted, mainly upward, to take into account the new situation, almost unique in Colombia's post-1929 economic history and comparable only to the early 1954 liberalization. The Valencia administration, which opened with a devaluation bang, and went through a variety of moods in trade policy, ended up with an import boom.

During the years 1963–66 taken as a whole, GDP growth slowed down, as shown in Table 1-3, with the rates of expansion of manufacturing, construction, and type I services showing the most significant declines, even though both the value of exports and of imports recovered somewhat from the depressed levels of 1959–62. In spite of the hesitations over incentives, minor exports continued to grow. The rate of capital formation declined, but more in construction than in machinery and equipment. The average rate of inflation for the whole period was about three times that registered during the previous four years, mainly reflecting the 1963 experience. Although hiding many gyrations, the exchange rates for coffee, imports, and minor exports during 1963–66 were fairly close to those of 1959–62.

THE LLERAS RESTREPO PRESIDENCY.

The administration of President Carlos Lleras Restrepo, inaugurated in August 1966, at first continued the inherited import liberalization program. Indeed, during the first half of 1966 the Colombian balance of payments, bolstered by new aid commitments from foreign creditors delighted with the liberalization program, appeared to be in reasonable shape. The free-market rate declined from 19.2 pesos in August 1965 to 16.0 pesos in July 1966. But toward the end of the third quarter of 1966 a new fall in dollar coffee prices, growing nervousness about the high import levels and a decline in the growth rate of minor exports, coupled with preoccupation with the thinness of foreign-exchange reserves, led to a questioning of the viability of the existing pattern of exchange rates and import freedom. Some influential foreign creditors argued that a new devaluation was required. They claimed that at the start of the liberalization program in 1965 the Colombian government had committed itself to further devaluations if certain targets, mainly related to the level of exchange reserves, were not met and that such a failure had been registered in September 1966. At any rate, they first hinted and later made clear that aid would be held up unless a further devaluation was forthcoming.

The new Colombian government pleaded for time so as first to get a firm grip on monetary and fiscal policy, pointing out the circumstantial nature of the fall in export earnings, while forecasting that import demand was likely to decline after its postliberalization boom. Aid, it added, was supposed to help out precisely in times such as those, and no simple quantitative trigger should provoke a major devaluation. The memory of the 1962 devaluation, of its loose or nonexistent coordination with fiscal, monetary, and wage policy, and of its politically disastrous effects was of course very much in the mind of the new government. More will be said on these matters in Chapter 7. Here it will be sufficient to note that in an extraordinary television appearance on November 29, 1966, President Lleras Restrepo announced to the nation a rejection of the demands of the by then united foreign creditors and termination of the import liberalization program and of operations in the free exchange market. Rigorous exchange and price controls were also announced. The speech came almost exactly four years after the traumatic November 1962 devaluation.

The President and his economic team, a sophisticated and capable group indeed, immediately turned their full attention to the preparation of what was to become Law 444 of March 22, 1967. The President took a direct role in the economic discussions; ministers not involved with the economy could hardly see him between November 1966 and March 1967. Law 444 restructured the whole Colombian trade and payments system, and has remained the key piece of legislation in that field to this day, giving the country its longest postwar period of policy stability. A vital element in the package was the establishment of small, frequent devaluations, or a controlled "crawling peg," for the major certificate market, avoiding the twin dangers of stickiness in the major rates and volatility in the free-market rate. Past stickiness in the major rates had eventually led to balance-of-payments crises and to large, traumatic devaluations; the volatility of the free-market rate had led to real or imagined instability and distortions. The free market was substituted for a pegged capital market rate, set at 16.3 pesos. When the upward-crawling certificate rate reached that level, in June 1968, the two markets were unified, i.e., the capital market was abolished. Special exchange regulations for the petroleum and mining industries as well as for some other minor items were maintained by Law 444, which, however, introduced a subtle but important change in the treatment of coffee exports. Earnings from coffee were to receive the same major fluctuating certificate rate paid by importers and received by minor exporters, *minus* an ad valorem tax, first set at 23 per cent and later lowered to 20 per cent. Previously, coffee exports received a special fixed exchange rate. In other words, after March 1967 coffee exporters acquired a vested interest in the continuation of the upward crawl of the certificate rate, while before they had been primarily interested in just a favorable coffee rate.

Law 444 replaced previous fiscal incentives for minor exports, under which proceeds from these exports could be used to reduce the income tax liability (Law 81 of 1960), with the simpler and more general tax credit certificate (*certificado de abono tributario*, CAT). The CAT given to minor exporters was set at 15 per cent of the export value, and could be used in payment of taxes one year after its date of issue. Those certificates were to be freely negotiable, and were exempt from all taxes. More will be said about them and their changing features in the next chapter. The new law also created the Export Promotion Fund (PROEXPO), with wide powers and functions.

In the field of exchange and import controls Law 444 reorganized previous regulations, maintaining and often strengthening restrictive mechanisms. Stringent rules for the negotiation and holding of foreign currencies and gold were set up; controls over direct foreign investors and over royalties and payments for patents foreshadowed, and in some respects inspired, the tough rules adopted by the Andean Common Market since 1970.

Simultaneously with the preparation of Law 444, the Lleras Restrepo administration struggled to get a firm and integrated grasp on fiscal, monetary, and wage policy, and on the whole succeeded. So March 1967 opened a new chapter in Colombian economic history and, paradoxically, the stormy and interventionist events of November 1966–March 1967 set the stage for a gradual liberalization trend which continued at least until mid-1974.

The new Phase IV, starting from a quite restrictive situation, has not been free of hesitations, especially regarding the proper pace for the "crawl" in the exchange rate. The year 1967 was a difficult one for the Colombian economy, and import restrictions were applied rigorously. Only in May 1968 did the free import list regain some significance, when some essential products, corresponding to 150 tariff positions, were exempted from import licensing. Throughout 1968 previous import deposit rates were lowered, but licensing remained tight. A sharp upswing in coffee prices, starting late in 1969, gave further impetus to liberalization which had also been encouraged by the resumption of large aid commitments in 1967, once foreign creditors became adjusted to the new Colombian administration. By the end of that administration, in August 1970, the import system remained more restrictive than it had been at the time of its inauguration in August 1966, but expectations of sudden and disruptive changes in policies had declined considerably. How the restrictive system looked in 1970 and 1971 will be discussed in later chapters.

During 1967–70 the GDP growth rate, as shown in Table 1-3, exceeded even the 1950–54 levels, and the growth profile by sectors appeared more balanced than in earlier years. The 1967–70 aggregate marginal capital-output ratio was the lowest recorded up to that time.

Dollar coffee prices in 1967–70 were on average not much higher than during 1963–66. The dollar value of minor exports, however, about *doubled* between these two periods. Helped by minor exports and capital inflow, merchandise imports approached the average dollar values reached during 1955–56. As shown in Table 1-4, expansion this time was accompanied by a sizable growth in central-bank gross gold and foreign-exchange reserves, as well as net repayments of credits received by the central bank during earlier years. Gross gold and exchange reserves, which were only $77 million at the end of 1966, reached $221 million at the end of 1969, dipping to $206 million at the end of 1970. The sum of errors and omissions, net short-term private capital, private and commercial arrears and net credit from commercial banks (Table 1-4), rose from a net debit of $11 million a year during 1963–66 to a net yearly credit of $34 million in 1967–70.

The 1967–70 averages for exchange rates for both imports and minor exports surpassed those of earlier subphases (Table 1-3). Furthermore, their rise was gradual, some calculations[16] to the contrary notwithstanding. The Colombian inflation during those years dropped to about the normal levels of 1950–54 and 1959–62 and was not much ahead of the inflation registered in industrial centers during the same years.

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This administration, inaugurated in August 1970, maintained the gradual import liberalization trend and the promotion of minor exports, which also benefited from the 1973–74 boom in world commodity markets. By the end of this administration's term, however, a transition into Phase V had not occurred, and only about half of imports were on the free list.

Available data show that from 1970 to 1974 Colombia enjoyed the highest GDP growth rates of any comparable four-year postwar period. Both minor and coffee exports boomed and, as will be discussed in Chapter 8, foreign-exchange limitations to growth appeared to be a thing of the past. Other economic problems, however, became more severe. Partly because of influences emanating from world markets, and partly because of an overheated domestic economy, inflation accelerated, particularly during 1973 and 1974. During those years the government launched a development plan heavily stressing urban construction. Since the plan was put into effect on top of an already prosperous domestic economy, it led to excess demand pressures.

A weakening of the financial position of the public sector, in spite of the prosperity, plus favorable world prices for exportable goods stimulated proposals to reduce export subsidies, which experienced several adjustments during 1970–74. On the other hand, the inflationary pressures encouraged further import liberalization. If world market conditions and coffee prices do not experience a severe deterioration, it is conceivable that the López Michelsen administration, inaugurated in August 1974, will further liberalize the trade and payments system and take the country into a Colombian-style Phase V, while adopting anti-inflationary measures, thus culminating the trends started in March 1967.

All this looks like a happy ending to our postwar summary narrative. In the last chapter of this book I will discuss in detail the achievements and limitations of the post-1967 growth path, as well as what can be expected from further liberalization. But before we get there many details need to be filled in.

NOTES

1. Alvaro López Toro, in his brilliant analysis of the internal consistency of the population censuses of 1938, 1951, and 1964, concluded that the most acceptable estimates for Colombian population growth were 2.4 per cent per year for 1938–51, and 2.9–3.0 per cent for 1951–64. See his *Análisis Demográfico de los Censos Colombianos: 1951 y 1964* (Bogotá: Ediciones Universidad de los Andes for CEDE, 1968), pp. 85–86.

2. This paragraph is based on the concluding chapter in R. Albert Berry and Miguel Urrutia, "Income Distribution in Colombia," mimeographed (New Haven: Yale Economic Growth Center, 1974).

3. See in particular R. R. Nelson, T. P. Schultz, and R. L. Slighton, *Structural Change in a Developing Economy; Colombia's Problems and Prospects* (Princeton, N.J.: Princeton University Press, 1971); and Jaroslav Vanek, *Estimating Foreign Resource Needs for Economic Development: Theory, Method and a Case Study of Colombia* (New York: McGraw-Hill, 1967).

4. See Alasdair I. MacBean, *Export Instability and Economic Development* (Cambridge: Harvard University Press, 1966). Colombia has traditionally held large coffee stocks, thus isolating the quantity of her exports from the effects of crop fluctuations. The International Coffee Agreement was also a stabilizing influence during the 1960s and early 1970s.

5. This is also true for several other Latin American countries. See Carlos F. Díaz-Alejandro, "Planning the Foreign Sector in Latin America," *American Economic Review*, May 1970, especially pp. 170–174.

6. See Lauchlin Currie, "The Exchange Constraint on Development—A Partial Solution to the Problem," *Economic Journal*, December 1971, pp. 886–904. A glance at year-to-year growth rates indicates that if alternative measures of instability were used, construction would still rank as less stable than manufacturing.

7. Three import price indices were tried: those of UNECLA (SB and DANE) for the whole period; those in IMF-IFS for the postwar period; and, linked to those of IMF-IFS, those in UA, pp. 212–213 (estimates of William Paul McGreevey). Current export values are found in the same sources. The highest t statistic (1.72) was for the coefficient of the percentage changes in the real value of exports concurrent with the change in GDP, in the regression covering 1929–68, but the absolute value of even that coefficient is very small.

8. For an elaboration of this point see Carlos F. Díaz-Alejandro, *Essays on the Economic History of the Argentine Republic* (New Haven: Yale University Press, 1970), especially pp. 79–85.

9. Basic data obtained from UA, pp. 82 and 158; UNECLA-DANE, pp. 135 and 149; and Council of Economic Advisers, *Economic Report of the President* (Washington, D.C.: U.S. Government Printing Office, 1970), Statistical Tables. The Colombian price indices are rough.

10. Cf. Henry C. Wallich, *Monetary Problems of an Export Economy* (Cambridge: Harvard University Press, 1950), especially Chap. XIV, "A Case for Exchange Control?"

11. The coffee terms of trade calculated by UNECLA (SB and DANE) show a positive coefficient of 0.4 per cent per year for the time trend, but with a *t* statistic of only 1.65. The terms of trade found in UA, pp. 212–213, linked with those of IMF-IFS show an annual rate of improvement of 2.1 per cent per year and a *t* statistic of 5.5. Both estimates were obtained by fitting semilogarithmic equations to all observations for 1925–68.

12. See Appendix B, entries for November–December 1956 and June 1957, for explanation of the certificate market.

13. Compare Colombian GDP behavior with that of Argentina, where real GDP *fell* in 6 of the 23 years between 1945 and 1967, mainly as a result of foreign-exchange crises. In 1959, for example, the absolute value of real Argentine GDP fell by nearly 6 per cent.

14. The Committee of Nine report, "Evaluación del Programa General de Desarrollo Económico y Social de Colombia" (mimeographed), was distributed by the Pan American Union. The ad hoc committee was formed by Felipe Pazos, Harvey Perloff, Raúl Sáez, Eduardo Figueroa, Jorge Méndez, and Pierre Uri. A preliminary note to the report lists Carlos F. Díaz-Alejandro as director of the technical staff of the committee; he was also the only member of that staff during most of the preparation of the report.

15. See R. Albert Berry, "Some Implications of Elitist Rule for Economic Development in Colombia," in Gustav Ranis, ed., *Government and Economic Development* (New Haven: Yale University Press, 1971), pp. 3–29.

16. Calculations are often seen in which the exchange rate "crawl" is compared only to the rise in Colombian prices, neglecting inflation in the rest of the world. This is sometimes defended on the ground that since the Colombian exchange rate is overvalued anyway, any argument for accelerating its upward "crawl" is to be welcomed and used, presumably on unsophisticated policymakers. It is doubtful whether many policymakers would swallow such a gross calculation, particularly after the world inflation of 1973–74. At any rate, that kind of tactic will not serve an educational purpose, and in the long run it could very well backfire, once it is seen that technicians have failed, after all, to be objective and neutral outliners of options open to the politician.