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Development Policy

Planning or Free Market Economy in LDCs?

by Professor Emil K  ng, St. Gall *

On the face of it it looks as if there should be no great difference between less developed countries (LDCs) and the advanced national economies as far as planning is concerned. And yet in reality such differences do exist, even if they do not necessarily stem from the inequalities in the standard of living.

One reason why there is much more planning in the poorer countries, even if they belong to the so-called Western camp, than in the more prosperous ones is, curiously enough, to be found in the fact that the LDCs are in receipt of development aid — the aid which they are given largely from the nations of the West. Now such support reaches them not only in small dribbles for some form of individual project, large or small, but also as "Programme Aid" which pre-supposes the existence of some development programme, and this in turn means nothing more or less than some sort of planned economy.

A second reason why macroeconomic planning is so frequently encountered is the political structure. As is generally known, democracy is a highly sophisticated form of government which, if it is to flourish, makes great demands on the individual citizen, requiring his intensive cooperation to make it work. This is the reason why in most LDCs democracy is again and again ousted by some kind of military regime or dictatorship. Now there exists a relationship of close interdependence between a country's political structure and its economic order. An autocracy will want to extend the political power it has attained to the economic sphere and will therefore introduce some kind of economic plan, designed to regulate the nation's economic life several years in advance. Democracy, on the other hand, is more naturally akin to a free market economy.

Dual Role of the State

But quite apart from this, it has become apparent that even in the advanced countries with their market economy some areas must be planned. The fiscal policy is for instance one of these areas. The inadequacy of annual budget estimates is becoming ever more apparent. Without longer-term planning, projects that take years to com-

plete such as a National Road Programme cannot be satisfactorily carried out. If a muddle is to be avoided, it is necessary to work out in advance, at least in outline, what shape the infrastructure is to take. Road building is but one example of the need to plan ahead for longer periods than one year; other examples are regional planning to counteract the bunching of people in certain already too densely populated areas, and the power supply. The same applies of course to LDCs. If they wish to avoid that their cities become inflated to a size altogether out of proportion to the rest of the country, they cannot but make it attractive to businessmen to establish their factories in the country, away from the big towns.

The country which goes perhaps farthest in the direction of planning is India, though it admittedly inclines that way in any case for ideological reasons. 25-year plans are being developed in the hope of being able in this manner to avoid any unexpected future consequences of measures taken now. That such delayed effects exist cannot be denied. It takes for instance many years for any expenditure on education and training to produce its full effects. Even if large-scale projects can be budgeted for now, it will be a long time before their effects on, say, the balance of payments, the national income or the energy supply will become fully apparent. Because of this, India also has short-term and more detailed plans, in addition to its 25-year plan. It is true that this procedure has also something to do with the fact that in that country government is itself among the big entrepreneurs. It is well known, however, that management, too, is also more and more inclined to favour longer-term planning.

Indicative vs. Imperative

Of course, the term "planning" by itself says nothing concrete about what is meant by it. Planning in the Russian sense is something quite

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different from what the Dutch understand by it. In the one case, a plan is mandatory, containing directives which lay down what individual plants and sectors have to produce, where what is to be produced, in what quantities, what quality and the delivery dates. The Russian type plan contains moreover precise instructions about the investments to be made and the expansions of capacity these investments must result in. Infringements of these instructions are punishable offences. By contrast, if in the Netherlands a plan is worked out, it contains no imperatives, but is indicative in form. It is drawn up with the intention of merely giving business as accurate a picture as possible of likely future trends. There is of course nothing mandatory, nothing compulsory about it.

Mixed Policy

The system used in the majority of LDCs lies somewhere between these two extremes. Encouraged or even strongly induced by international organisations, by development aid experts and foreign governments, the national authorities are expected to establish an order of priorities, to lay down what should be tackled at once and what can be left to a later date. A list of priorities of this kind makes sense, for it ensures that palaces for the Head of State are not built first, while the population continues to starve — as has happened here and there in the past. The least that can be achieved by insisting on such lists of priorities being drawn up is that the countries which provide the development aid avoid the stigma of aiding and abetting in such distortions of the true needs of the country concerned. It is of course evident that a certain infrastructure must be set up first of all. Only when this is done, is there any sense in thinking of such problems as recruitment of skilled labour for the factories, the supply of electric power, the transport of goods to and from the factories, etc. Only after the peasants have been integrated in a money economy, can they be expected to produce more and supply more for the market or to show a greater understanding for artificial fertilizer. These few indications may suffice to show that without certain basic assumptions being fulfilled a market economy cannot function. These preconditions are however not created by the market itself, but must be provided by the public authorities. It is therefore clear that in the early stages of development a considerable measure of planning is simply unavoidable.

If government planners frequently interfere also in the later stages of a country's development, they justify their action by pointing to a number of reasons which are now to be examined in some detail. One of these is the argument that the free

market provides only inadequate means of directing the economy. What does this mean? It is primarily the prices of goods which cause an economy to move in a certain direction. They reflect a temporary shortage of certain products and production factors and indicate by their level how much more—or less—of these goods should be produced. Now critics argue that these signals merely reflect the situation in the immediate present, providing no clues as to the longer term future. True—they say—a pronounced scarcity may well cause prices to soar temporarily. If manufacturers in response to these higher prices strongly expanded their output capacity, they might well by their very action bring about a future surplus.

In principle, this argument holds good in all cases where no future's markets exist on which prices for forward deliveries are quoted. What we are here concerned about, however, is the general problem of uncertainty surrounding future trends, and one can hardly expect of a single price to tell us at the same time something about the present and the future. The only fruitful question to ask, therefore, is whether the forecasts, without which no economy, industry or business can operate, are more reliable, if they are worked out by people belonging to the industry or if they have been commissioned by the authorities. In this respect there is room for considerable doubt about the reliability of the government planners, especially those in LDCs, even if they should confine themselves to predictions of a purely indicative nature, and, in any case, who is responsible for any possible incorrect forecasts?

Insufficient Flexibility

A second argument which is advanced against the market economy is that an economy in which the means of production are privately owned reacts not strongly enough to any signals. The pace and intensity of the necessary industrialisation—so the argument runs—leave much to be desired, despite the generous profit chances offered to the entrepreneurs. This argument may well have some force in individual cases where for instance the mentality of the population is more concerned with making short-term trading profits than with long-term investments and with the good management of industrial concerns. Such a state of affairs may well exist in some parts of the world, possibly in the Near East.

Apart from this, however, the problem must be formulated somewhat differently. First of all it must be established how much investment capital industry as a whole needs, and especially for the purpose of expanding its productive capacity. The next question to ask is whether these funds are likely

to be used more rationally by private enterprise or by public authorities. The answer to this vital question, if it is considered without prejudice, will more often than not be in favour of private enterprise. For in private enterprise there is a personal interest in avoiding misdirection of capital and in making maximum net profits. The owner will in general work much harder than any civil servant to ensure that the goods are produced as economically as possible and that they meet the requirements of the market. Whoever has capital to spare for investment will choose projects which promise the highest returns. By contrast, public enterprises need not necessarily be operated according to these principles. Bearing in mind that in LDCs capital is decidedly scarce, there is a clear and pressing need for it to be used profitably. If India for instance latently offends against these maxims by favouring the public sector, it has to pay for it by having to accept a slower economic growth than would otherwise be possible.

Scarcity of Entrepreneurs

A third argument advanced in favour of state planning and public ownership of the means of production is finally that there are not enough enterprising businessmen in the country ready to tackle the tasks which would be theirs to perform in a market economy. It is naturally extremely difficult to establish with any degree of certainty whether this assertion is correct in each and every case. One thing, however, is certain: if it is actually true that such people are in short supply, then they would be missing not only if private industry were given the task of solving the country's economic problems; they would be missed just as much, if not even more so, if a state economy were chosen as an alternative.

Of course, it is quite possible to entrust civil servants and government employees, engineers and technicians with the task of establishing and managing state-financed factories, but it is highly unlikely that they are at the same time the right kind of businessmen for the job. Whether on top of it they have the desired entrepreneurial qualities is even more doubtful. Whoever possesses these characteristics tends in general to have little inclination to enter into government service, least of all into a bureaucracy which distinguishes itself by its shocking unwieldiness (as is the rule rather than the exception in LDCs).

The Example of Japan

When all is said and done, economic history presents, however, one highly instructive case of a country's industry being started by the public authorities and subsequently being taken into

private ownership. This happened in the Land of the Rising Sun. When in the 19th century the country was opened up to Western ideas and influences, there existed at first no private enterprise, and the government had no real alternative but to carry out the desired industrialisation on its own account. True, there were men available from among the former warrior cast, the Samurai, who were looking for a new field of activity. It was primarily these people who later took over these industries. What is most remarkable in this case is that the state was prepared to renounce its predominant position. Looking at today's LDCs, this willingness does not appear to be present anywhere. It is consequently hard to imagine that Japan's example will find any imitators, although its brilliant success has remained unequalled.

Much more frequent is instead a state of affairs where the state places obstacles in the way of private industry. This danger is acute wherever private and public sectors exist side by side as also, for instance, in Italy. If in such circumstances foreign currencies which are necessary to pay for essential imports are allotted only in extremely limited amounts, public enterprises, by using their influence with the exchange control board, invariably manage to obtain preferential treatment. After all, do not public concerns operate in "strategically important" areas? And is it therefore not the state's primary duty to see that they prosper, even if it is at the expense of their competitors? Another form of discrimination is practised when it is a question of arranging for additional finance. Private firms have to rely to all intents and purposes on self-financing, for in a typical development country there is no properly functioning capital market to have recourse to. Public enterprises, by contrast, have the opportunity of helping themselves from the public till. Whether, in fact, they pay the state the right amount of interest on the borrowed money is another matter. What is certain is that favouritism shown to the one sector at the expense of the other — and that also in the field of taxation — is an everyday occurrence. It has for instance happened that undue expansion of the public sector has brought about a proper balance of payments crisis as a result of which the foreign exchange allocations to the private sector were limited to such an extent that investments which had already begun had to be discontinued.

Many more examples of incorrect forecasts could easily be given. In fact, macroeconomic planning in LDCs functions by its very nature under serious handicaps. First of all, there is the shortage of qualified experts from which all planning staffs are suffering. True, they are mostly helped by experts from the industrially advanced countries, but these

do not as a rule stay long enough to be able to acquaint themselves in detail with the country's special problems. Moreover, all experts, national and foreign alike, are up against notoriously inadequate statistical data so that their predictions are at best inspired guesses. It just is not good enough to have at one's disposal data about population, income and the like; much more information is wanted such as reliable figures about production and consumption for each branch separately.

Faulty Planning

Moreover, experience has shown that politicians tend to take a keen interest in planning operations with a view of influencing the decisions. For each region is naturally anxious to attract as many industries as possible with the result that in most cases an excessive number of plants are set up in

the most diverse regions. In consequence, each individual factory is too small to achieve low unit-costs. The case of India may once again be cited in evidence where there are no less than three motorcar factories, producing between them 40,000 cars per annum. That in such conditions of faulty planning of industrial locations there can be no question of making India's car industry capable of exporting its products is evident.

In the light of such and similar experiences even the economists in the developing countries are coming to the conclusion that—infrastructure apart—it is too much to expect of state authorities to bring about an evenly balanced economic growth by over-all planning. The discrepancy between the paper plans and their actual execution is so big that there seems to be little sense in wasting great numbers of highly qualified experts on drawing up such comprehensive plans.

Tourism Promotion in Developing Countries

by Dr Waldemar B. Hasselblatt, Bonn *

When announcing its ideas on development policy in the Second Development Decade which began in 1971, the Federal Government said that it "wishes to promote tourism in suitable less developed countries (LDCs) through improvement of the infrastructure, especially transport, provision of accommodation and training of the required personnel, making use of development banks in suitable cases".

The policy pursued until now has thus been reaffirmed; for the Federal Republic of Germany has been helping a number of LDCs for several years already to build up their tourist facilities. By the end of 1972 DM 332 mn of capital aid funds had been committed to this purpose, DM 39 mn had been spent on technical assistance and some DM 12 mn had been provided for ordinary and advanced training of specialists for hotels and other tourist services out of budget funds of the Federal Government and (about 10 p.c.) the Federal Lands. These German aid measures have covered a wide range.

German Aid Measures

For planning tourist projects the Federal Republic of Germany has in recent years extended help e.g. to Sri Lanka (Ceylon), Cameroun, Morocco

and Nepal. In Sri Lanka a detailed pre-investment study on the building of hotels and holiday villages was prepared in continuation of a scheme — a "Master Plan" — for the development of tourism in that country which had been commissioned by the AID. For Cameroun a target plan for the tourist industry was drawn up as a basis for decisions on individual projects by interested investors and bilateral and multilateral donors. For Morocco a general study of tourism is being undertaken; it is to yield a detailed draft programme for the current five-year plan (1973–77) and a skeleton plan for the next five-year plan (1978–82). For Nepal a Master Plan has been prepared in collaboration with Nepalese authorities; the investment volume envisaged under this plan has been allowed for in the national five-year plan.

Capital aid resources have been used for tourist roads in the wild-life reserves of Kenya and

* Federal Ministry for Economic Cooperation.