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Article — Digitized Version

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Intereconomics

Suggested Citation: Westphalen, Jürgen (1976) : Economic growth or redistribution?, Intereconomics, ISSN 0020-5346, Verlag Weltarchiv, Hamburg, Vol. 11, Iss. 6, pp. 168-171, <https://doi.org/10.1007/BF02928961>

This Version is available at:

<https://hdl.handle.net/10419/139380>

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Economic Growth or Redistribution?

by Dr Jürgen Westphalen, Hamburg *

Economic and development policies in Latin America, as in all other developing countries, are supposed to tackle the problem how to increase total income and, at the same time, how to reduce the present inequalities in the distribution of income. The opinions on the question, which of these tasks deserves priority, differ widely.

On the one hand, it is assumed that a noticeable decrease in income differentials in developing countries (LDCs) would enable large groups of the population to develop additional demand for consumer goods which, in turn, would create powerful new impulses to goods production and, thereby, to the development of the whole economy. In other words: a sharp redistribution at the expense of the rich would, automatically, cause growth of the whole economy.

On the other hand the argument is held that economic and development policies should give priority to forceful economic growth, because overall expansion of the economy is said to be, on the whole, nothing but rising goods production, and this in its turn means nothing else but a rising number of jobs, that is, growing income for wage and salary earners. Reduced to a brief formula, this opinion signifies: Economic growth will lead automatically to a more balanced distribution of incomes. Some even say that redistribution policy is not only superfluous but harmful because it prevents the well-to-do groups of the population from saving enough and thereby from laying the foundations for productive investments.

An objective rating of these general points of view with regard to the actual situation in Latin America needs, on the one hand, knowledge of the present position of Latin America in the worldwide dif-

ferentials of income and, on the other hand, certain insights into the actual distribution of incomes within Latin America¹.

Development Differentials against the Outer World . . .

Those Latin American countries with the highest per capita incomes were in 1972 Argentina and Venezuela (in both of them about US \$ 1,300), those with the lowest ones Bolivia with US \$ 200 and Haiti with US \$ 130². In the same year, per capita income in the US was 4.3 times higher than in Argentina and 43 times higher than in Haiti. In comparison with the Federal Republic of Germany the corresponding proportions were 2.6:1 and 26:1.

Irrespective of all the reservations advisable when using per capita incomes for measuring the development level of a given country, these figures make it clear how wide the gap is which still has to be filled even by the relatively advanced Latin American countries in order to reach the present-day level of the industrialized countries of North America and Western Europe — not to speak of the relatively underdeveloped countries like Bolivia and Haiti.

However, from the Latin American point of view there exist no less marked differentials regarding the opposite direction, that is compared with the even poorer LDCs in Africa. In order to make a comparison, we choose two Latin American countries which, within this group, lie approximately in the middle, namely Costa Rica with US \$ 630 and Brazil with US \$ 530 annual per capita income. Both countries still enjoy an average income which is about seven to eleven

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¹ A third, extremist point of view, which however, is not to be discussed here, asserts that there is no solution at all possible, within the present economic system, for the problem of unequal distribution of incomes. An indispensable condition for overcoming this problem would in this view, be the destruction of the present and the creation of a new social system.

² World Bank Atlas. Population, Per Capita Product and Growth Rates. Published by the World Bank, 1974.

times higher than those of Upper Volta and Burundi (both US \$ 70) and Rwanda (US \$ 60).

The gap between one of the development levels and the higher one used for measuring is of about the same magnitude in both cases: The per capita incomes in Upper Volta and Burundi equal slightly over 11 p.c. of the income in Costa Rica and that of the latter lies somewhat above 11 p.c. of that of the United States.

The Latin American position in the scheduled ranking table of per capita incomes has become more and more marked during the sixties. In other words: on both sides, the differentials have not shrunk — on the contrary, they have expanded noticeably. Only in very recent years, there were some indications that the trend of growing income differentials between Latin America and the highly industrialized countries has begun to decline. For, whilst in the industrialized countries the further growth is apparently hindered by facts resulting partly from technological, partly from economic reasons, the countries of Latin America can still expect almost unlimited development possibilities in both their economies and their technology.

... and within Latin America

Even steeper than the differential between Latin America and the United States, to the one side, and between the former and the poorest LDCs in Africa, to the other, is the differential measured by per capita incomes within Latin America. For 1973, the Inter-American Development Bank reported the average per capita income in Latin America to have been US \$ 616³. From this average level, there are remarkable deviations upwards and downwards: In 1973, Venezuela heads the list with a per capita income that is almost double of the average income of all Latin Americans, and Haiti continues to form the end of the line with only barely 20 p.c. of the Latin American average. This comparison shows conspicuously how deceptive it may be to speak of Latin America as of a unified economic region and of problems which affect this region in the same way everywhere, for example in Venezuela and Haiti.

Marked differentials between wealth and development levels exist in Latin America, however, not only between different countries but also within individual countries between different settlement areas. Thus, for example, in the mid sixties, per capita income in the Venezuelan capital Caracas stood at 164 p.c. of the average per capita value

for the whole country, and in Mexico, per capita income in the capital city was even over 220 p.c., i.e., more than twice the average for the whole country. And lastly, the distribution of incomes in Latin America within the different rural and/or urban areas is, in general, also anything else than well-balanced.

Unequal Income Distribution

In contrast to the statistical data about per capita incomes of the different Latin American countries, information available as to the distribution of incomes is relatively limited; besides, the data published in the individual Latin American states show marked differences with regard to their comprehensiveness and reliability. Therefore, it seems preferable to build one's conclusions mainly on the material on income distribution which has been published by the UN Economic Commission for Latin America (CEPAL) ⁴.

CEPAL, in its reporting, differentiates between the following five groups of income earners:

□ The first Group consists of those 20 p.c. of all income earners who have the lowest incomes ("más pobre").

□ The second and third Groups represent 60 p.c. of all income earners, 30 p.c. each representing those with higher middle incomes („superior a la mediana“).

□ Lastly, there follow the Groups earning higher incomes („inferior al 5 p.c. más alto“) and highest incomes („más alto“), of which the former represents 15 and the latter 5 p.c. of all earners of income.

Income Distribution in Latin America in the Early Sixties

Income Groups (in p.c. of all income earners)	Share in Total Income (in p.c.)	Average Income per Inhabitant in 1965 (in US \$)
20 p.c.: Lowest Incomes	3.1	60
30 p.c.: Lower Middle Incomes	10.3	130
30 p.c.: Higher Middle Incomes	24.6	310
15 p.c.: Higher Incomes	29.2	750
5 p.c.: Highest Incomes	33.4	2,600

Comparing the distribution of income in Latin America with that in a number of industrialized countries brings out the fact that the portion of total income falling to the share of the lowest group is relatively low in all countries. However, the share of this group in the US in total income is still about one-half higher than in Latin America, and in addition, it must not be forgotten that there

³ Progreso económico y social en América Latina. Informe Anual 1974. Published by Banco Interamericano de Desarrollo. Washington, D.C., without year of publication, p. 492.

⁴ La Distribución del Ingreso en América Latina. Published by Comisión Económica para América Latina, New York 1970.

is a considerable absolute differential between incomes in the US and in Latin America. To be poor in a highly industrialized country — as hard and as bitter as this may ever be in the individual case — in general does by no means come up to the same want of providing for vital needs as in an LDC.

Income Distribution in Latin America and in the US in the Early Sixties

Income Groups (in p.c. of all income earners)	Percentage Share of Total Income	
	Latin America	US
20 p.c.: Lowest Incomes	3.1	4.6
30 p.c.: Lower Middle Incomes	10.3	18.8
30 p.c.: Higher Middle Incomes	24.1	31.1
15 p.c.: Higher Incomes	29.2	25.5
5 p.c.: Highest Incomes	33.4	20.0

On the other hand, when assessing this international comparison, it must not be forgotten that the members of the poorest groups of the population in the cities and towns in the northern United States and in Northern and Central Europe could not survive at all with an annual per capita income of US \$ 60, which is that of the lowest group in Latin America, because of the climatic conditions and because of the high degree of division of labour in the economy, which virtually excludes the possibility of self-support from own agricultural production. The subsistence minimum in urban settlements is higher than in the countryside, and it is also higher in industrialized countries than in LDCs.

Moreover, it has to be noted regarding this lowest income group that a large part of it consists of so-called „special cases“ in the industrialized countries: these are the aged, temporarily unemployed and sick people and very young unskilled workers. For many people, belonging to this group is not meant to be a permanent state in an industrialized country, and for the majority of the rest it is at least possible to mitigate their misery noticeably through measures of social policy.

Poverty as a Permanent State of Affairs

In contrast to this, in Latin America, on the one hand, all those belong to this group who are, for long periods or permanently, without employment or not engaged in some productive work. The very high number of such people cannot even approximately be estimated with any degree of certainty. The employment problem in Latin America has been justly compared with an iceberg⁵, the visible part of which is open unemployment, while its much bigger part consists

of statistically not recorded and largely unrecordable forms of hidden unemployment and of unproductive, frequently only temporary and extremely lowly paid employment of people, mainly in farming and in urban service occupations. On the other hand, among the recipients of the lowest incomes there are also numerous people in permanent employment, most of them in rural parts, but rising numbers also on the outskirts of the big cities. The extremely low incomes in this group reflect a situation befalling those concerned and often even their children for a long time. This situation can hardly be changed through individual initiatives or through the instruments of an official social policy. Poverty in Latin America — as on the whole in all LDCs — more frequently than in industrialized countries is a permanent state.

Marked Concentration of the Highest Incomes

The second and third groups of income recipients — which are the two groups with middle incomes — claim in Latin America only 34 p.c., but in the US and in the UK almost 50 p.c. and in Norway even 55 p.c. of total income in the respective country. Taking the first (lowest) and the second groups together, the lower half of all income earners receive in Latin America only 14.4 p.c., but in the US 23.4 p.c. of the total. This shows most markedly the relatively high degree of inequality in income distribution in Latin America.

Inequality is even more evident in the case of the two groups with the highest incomes which, in Latin America, absorb almost two-thirds of total income, but in the US not even one-half. This difference is caused mainly by the small group of earners of the highest incomes: they receive one-third of the total in Latin America but only one-fifth of total income both in the US and the UK whilst the share of the next-lower group of earners of higher incomes, in Latin America, is only about 15 p.c. higher than in the United States. However, there are striking differences in the

Income Distribution in the Early Sixties

(p.c. of the respective total incomes)

Countries	p.c. of all earners of income	20 p.c.: lowest incomes	30 p.c.: lower middle incomes	30 p.c.: higher middle incomes	15 p.c.: higher incomes	5 p.c.: highest incomes
El Salvador		5.5	10.5	22.6	28.4	32.9
Costa Rica		5.5	12.5	22.0	25.0	35.0
Mexico		3.6	11.8	26.1	29.5	29.0
Venezuela		3.0	11.3	27.7	31.5	26.5
Argentina		5.2	15.3	25.4	22.9	31.2
Latin America		3.1	10.3	24.1	29.2	33.4
USA		4.6	18.8	31.1	25.5	20.0

⁵ Notas sobre la Economía y el Desarrollo de América Latina. Published by CEPAL, Santiago de Chile, No. 154 (1 May 1974).

parts which this latter group plays in individual Latin American states for example, in Argentina, the apportioned share of total income was recorded as 22.9 p.c., in El Salvador as 28.4 p.c., and in Venezuela as 31.5 p.c.

The quoted CEPAL study justifiably underlines as the decisive factor in the gross maldistribution of incomes in Latin America the high share in total income claimed by the recipients of the highest incomes, which means the marked concentration of incomes in the hands of a small group.

Limited Chances for Redistribution

From this fact, people frequently draw the conclusion that, in Latin America, the redistribution of incomes should have absolute priority over any efforts towards further economic growth. This conclusion, however, cannot be accepted without considerable qualifications.

Quite specifically, it should never be overlooked that even the average incomes of Latin American recipients of the highest incomes are still remarkably low, and that therefore any redistribution of part of the income of this group achieves only a very limited improvement in the financial situation of the poor groups of the population. M. Gester⁶, in this context, in a comment on the discussion of the Brazilian income distribution in 1970 states that "there are (in Brazil) hardly any 'rich people' by European standards. Only a mere 1.2 p.c. of all employed people were earning in 1970 more than DM 1,800 (per month). Therefore, it is not true that, at the top of the income pyramid, hundreds of thousands of big-income earners live as spongers at the expense of the rest, but almost everywhere the coat is not cut according to the cloth."

In spite of this limit to any useful redistribution, which not only in Brazil, but also in all Latin American countries is more or less marked, income policy should at least aim at the rise of low nominal income to such an extent that the poor population does not suffer from losses in real income caused by inflation.

If and when income should be redistributed, the respective measures ought also to be formulated and used in such a way that they do not cut down the savings activities of the better earners but restrain their consumption. With full justice, H.-P. Nissen⁷ emphasizes that "the obstacles which

arise in the path of such a policy... (are) by far more difficult than those which must be overcome by a pure growth strategy."

Growth and Redistribution — No Alternatives

Apart from making use of all the possibilities in Latin America for useful redistribution of incomes, the efforts to accelerate economic growth must be continued and reinforced. Among their main aims must be changes in the structure of production, which means a promotion of the secondary sector, and, within this sector, above all the manufacturing industry. Above and beyond that, diversification of the export structure is essential, which means a determined dismantling of the raw material monocultures, which are a heavy burden on the economic development of many Latin American countries.

One of the causes not only of the low per capita incomes but also of the unbalanced distribution of incomes in Latin American countries is the inherited structure of their production. CEPAL distinguishes, between narrow sectors of production where modern technologies have spread, and "primitive" sectors where outdated techniques are still in use but where by far the overwhelming majority of the working population is employed. In the limited modern sector, only slightly more than 12 p.c. of all workers of Latin America produced almost half of the total GNP in the early sixties; on the other hand, the "primitive sector" with about 40 p.c. of all workers produced less than 10 p.c. of the Latin American GNP. Considering further that, in the "primitive sector", there is usually an oversupply of workers, whereas the modern sector suffers from a shortage of them, the connection between the heterogeneous production structure and the unequal distribution of incomes is clearly visible. It must therefore be the aim of development policy in Latin America to give priority to fostering economic growth in the modern sector and to dismantle the "primitive sector", which has lost almost all significance in the industrialized countries, step by step. In this process, it will be necessary to develop and apply technologies in the modern sector (which inclines to high capital intensity) that permit a sufficient employment of labour. At the same time, the available workers must be prepared for taking over their highly-demanding tasks in the modern sector.

In conclusion, it can be summed up that, also in Latin America, growth policies and redistribution policies must not be considered to be alternatives. On the contrary, economic and development politicians ought to strive towards the two discussed objectives, but the redistribution of incomes should have its limit where it threatens to become an obstacle to further economic growth.

⁶ M. Gester, Das brasilianische Modell ist besser als sein Ruf (The Brazilian Model is better than its reputation), in: Frankfurter Allgemeine Zeitung, 27 August 1973.

⁷ H.-P. Nissen, Einkommensverteilung in Entwicklungsländern (Income Distribution in LDCs), in: Entwicklung und Zusammenarbeit. Beiträge zur Entwicklungspolitik. Published by Deutsche Stiftung für Internationale Entwicklung (German Foundation for International Development), No. 8/1975, pp. 6 ff.